



Bright horizons

Faroe Petroleum plc
Annual Report
and Accounts 2017

Faroe Petroleum is
an independent oil and
gas company focusing
principally on exploration,
appraisal and production
opportunities in Norway
and the UK



More information is
available online at:
www.faroe-petroleum.com

Introduction

I am pleased to announce our full year results for 2017 which was another significant period for the Company and one in which Faroe continued its evolution into a full-cycle E&P business.



Year on year reserves growth of 20%, reflecting continued success with the drill bit. Financially, the year was also strong for Faroe, generating EBITDAX of £82.2 million from ongoing operations and completing our debut bond issue in November 2017 to raise \$100 million on good terms.

Graham Stewart
Chief Executive

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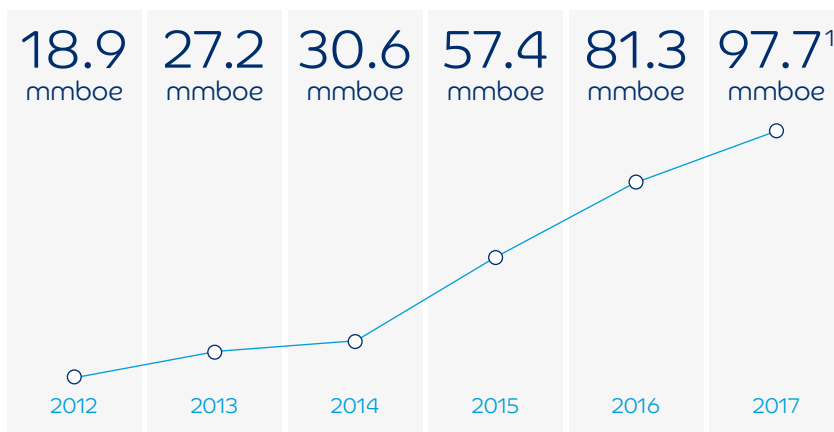
At a glance

Sustained delivery through the drillbit

Faroe is on track to deliver our organic production growth target of over 35,000 boepd in the medium term from existing projects, representing growth of around 2.5 times 2017 production.

2P Reserves growth

Year-on-year reserves grew by 20% and in the last five years reserves have grown by more than 400% – mainly as a result of maturing our discoveries into attractive development projects. This strategy continues in 2018. With an average finding cost in Norway of approximately \$1.20/boe, Faroe has developed a compelling route to sustainable value creation for the Company.



¹ After adjusting for the Fenja disposal of 17.5%.

Financial highlights

£149.1m

gross cash at 31 December 2017

£75.0m

net cash at 31 December 2017

£152.9m

Revenue in 2017

£82.2m

EBITDAX in 2017

\$54.5m

Post-tax consideration for Fenja divestment in 2018

Operations highlights

14,349 boepd

Total average economic production for 2017 at 14,349 boepd (2016: 17,395 boepd)

Successful Brasse

appraisal well and flow test with 2P Reserves of 30.7 mmboe (net)

Oda and Njord & Bauge

PDOs approved in 2017 and developments progressing on plan and budget

Tambar

Two new infill wells on stream and installation of gas lift continues

Fenja

PDO submitted in December 2017 (Faroe 7.5%)²

² Faroe interest post completion after divestment of 17.5% interest.

Strategically well positioned



97.7³
mmboe
2P Reserves



78.6
mmboe
2C Resources

³ Adjusted for Fenja partial divestment.

- With an average finding cost in Norway of approximately \$1.20/boe, Faroe has developed a compelling route to sustainable value creation for the Company.
- Recognised technical and operational organisation with over 40 oil & gas assets, and over 80 employees.
- Production guidance for 2018 is 12,000 – 15,000 boepd split approximately 67% liquids and 33% gas.
- Opex in 2018 is expected to be in range \$23-27 per boe.



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Financially flexible



\$250m
unused RBL
facility



\$100m
unsecured
bonds

- Debut bond issue of a \$100 million senior unsecured bond in November 2017 with a fixed coupon of 8%, complementing existing credit facilities and providing financial flexibility and optionality.
- \$250 million reserve based lending ("RBL") facility, undrawn at 31 December 2017.
- NOK 1 billion exploration finance facility ("EFF") in place.



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Growth focused

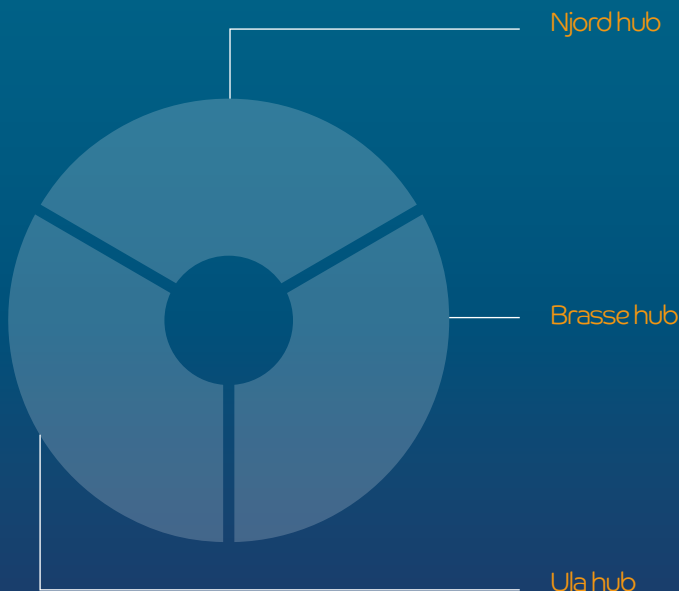


35,000
boepd in the
medium term

- Excellent progress across portfolio of high-quality development projects.
- Further 14% of Blane oil field acquired from JX Nippon for consideration of \$5.25 million (Faroe now 44.5%).
- On track to deliver our organic production growth target of over 35,000 boepd in the medium term from existing projects.
- Opportunities to accelerate further growth through potential value-accretive acquisitions and disposals continue to be a major focus for the Company going forward.



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The hubs

Faroe has a portfolio of significant production and development, pre-development, appraisal and exploration projects, centred around our core Norway hubs of Njord, Brasse and Ula.

The Company has developed a strategy and organisation which are centred on these hubs to which over 90% of Faroe's 2P Reserves at 1 January 2018 are connected.

Our business model

Faroe Petroleum has developed a geographically focused strategy with a diversified full-cycle portfolio which provides a strong growth trajectory for the future.

Strong growth trajectory

Faroe has an asset base with a clear line of sight to deliver material growth in high value production to over 35,000 boepd.

We expect to add further new organic projects to this growth plan through maturing a number of discoveries and infill wells as well as potential new discoveries generated from our ongoing exploration programme.



12,000-
15,000
boepd
2018 production
guidance



\$23-27
opex/boe¹
2018 guidance

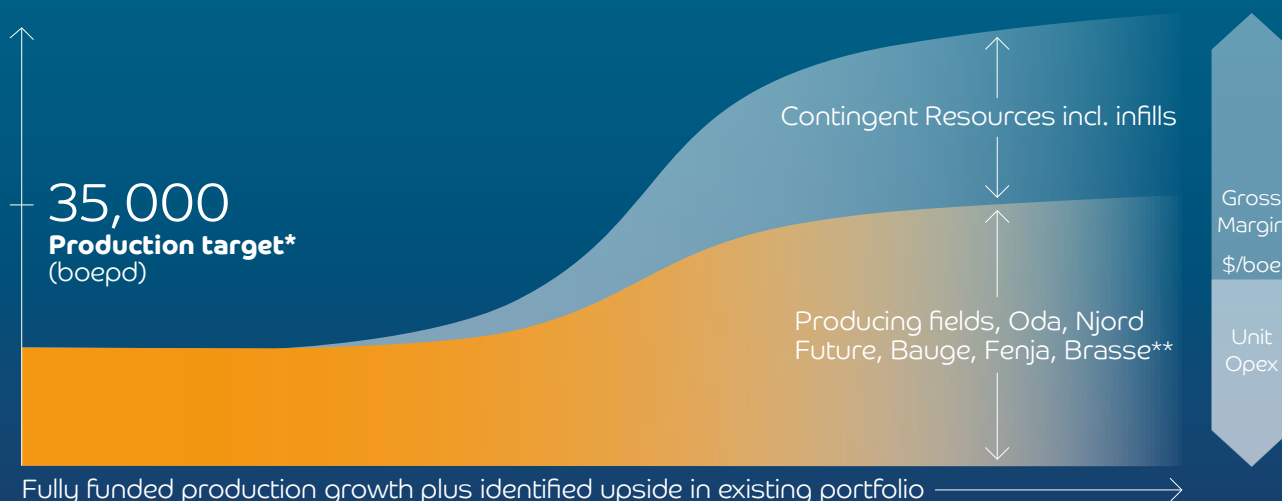
¹ Producing assets and excluding future upgrade costs.



67% liquids
33% gas
2018

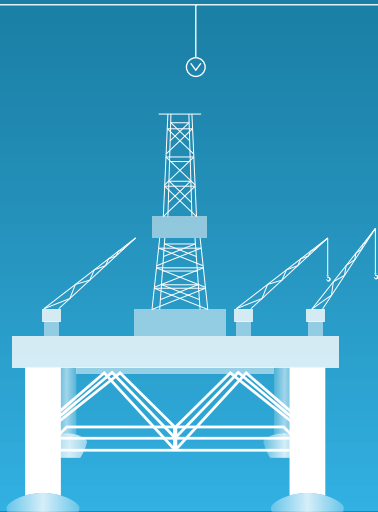
85%
of gas and 60% of
oil hedged in 2018

Material organic production growth potential



*This chart is illustrative and is not forward guidance

**Pending development commitment

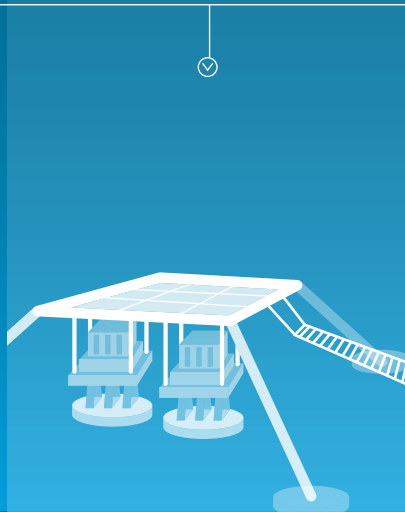


Exploration

For several years, the Company has been among the most successful independents in winning prime quality exploration acreage in Norwegian waters. In January 2018, Faroe was awarded eight new prospective exploration licences including four operatorships under the 2017 Norwegian APA Licence Round on the Norwegian Continental Shelf.



Read more
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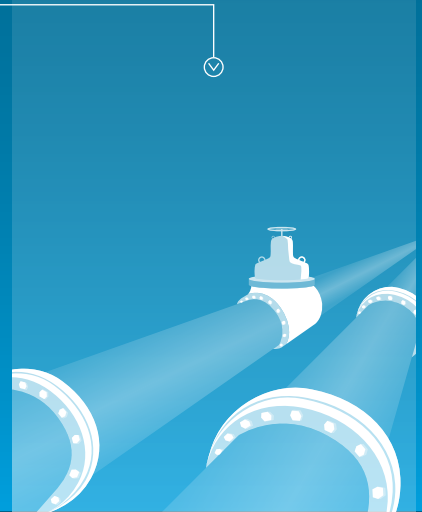
Development

Following a series of successful exploration wells over recent years, Faroe now has four important projects in Norway progressing towards development:

- the Njord Future project, including the Bauge development. PDO approved by MPE in 2017.
- the Oda development. PDO approved by MPE in 2017.
- the Fenja development. PDO submitted in 2017.
- the Brasse pre-development. PDO submission expected in 2019.



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Production

Faroe's production portfolio performed very well in 2017, delivering net average production of 14,349 boepd with an average opex per boe of \$26.5 for producing fields. Faroe's production is spread across a balanced and high quality portfolio of assets with an approximate geographic volume split 80%/20% Norway/UK and an oil/gas split of 55%/45% respectively in 2017 and generated EBITDAX of £82.2 million in 2017.



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Exploration

Future potential

With an average finding cost in Norway of approximately \$1.20/boe, Faroe has developed a compelling route to sustainable value creation for the Company.



6
E&A wells
committed to
date in 2018
and 2019



78%
of Norway E&A
spend eligible for
a tax refund from
the Norwegian
State

Highlights

2017

Successful Brasse appraisal

Boné and Goanna wells dry, Iris & Hades well spudded.

2018

Drilling schedule

Fogelberg appraised well commenced drilling in February.

At least a further 3 exploration wells to be drilled this year.

2019

Future exploration

Many further targets being matured to drilling decisions to continue to deliver sustainable long-term drilling programme.



Prospect	Operator	Working interest	Expected timings						Status
			Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	
Iris & Hades	OMV	20%	○						Drilling
Fogelberg Appraisal	Spirit Energy	15%	○						Drilling
Rungne	Faroe	40%	○						Committed
Cassidy	Spirit Energy	15%	○						Committed
Pabow	Statoil	20%	○						Committed
Brasse Extension	Faroe	50%	○						Pending commitment
Yoshi	Wintershall	30%	○						Committed

Development

Brasse Case Study

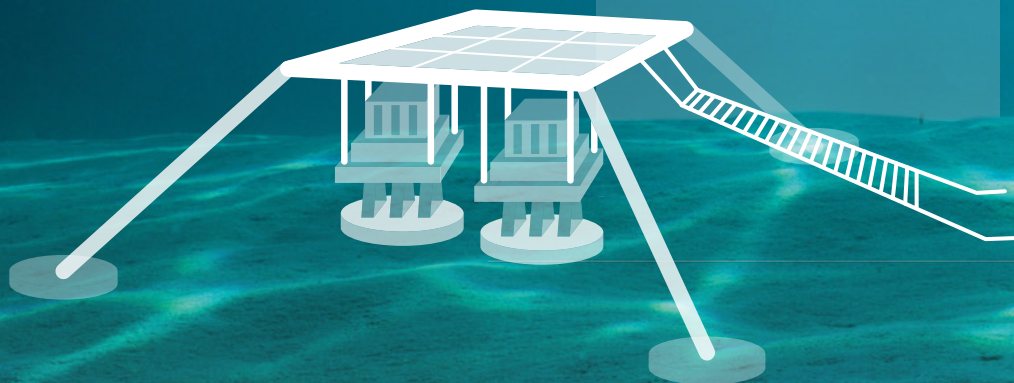
Organic value growth

Faroe on track to deliver production growth target of over 35,000 boepd in the medium term from existing projects.

**Brasse 2P Reserves
(net to Faroe):**

 **25**
mmbbl
recoverable oil

 **34 bcf**
recoverable gas

**Brasse timeline****2015****Award**

50% equity awarded to Faroe in the APA 2014 round as operator.

2016**Exploration well**

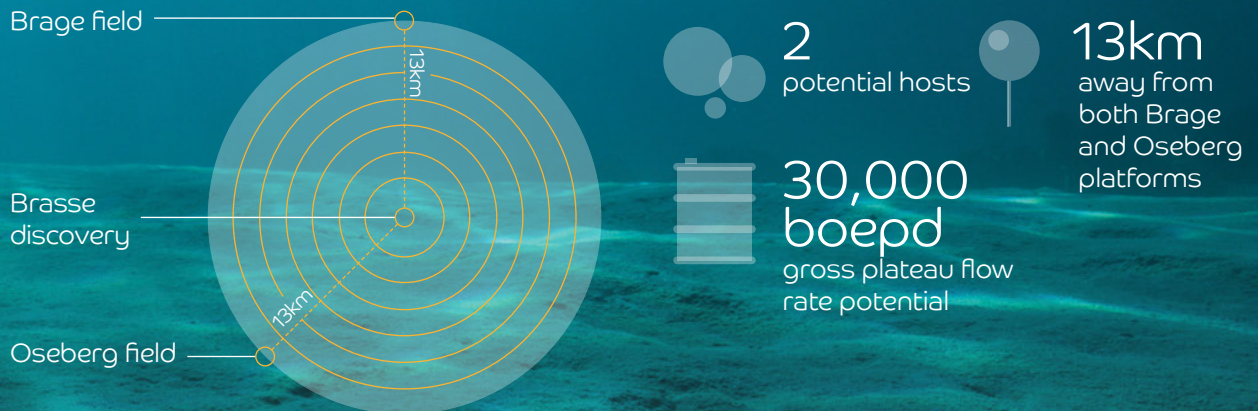
Exploration well and side-track drilled, discovering material oil and gas volumes in a high quality reservoir.

2017**Appraisal**

Appraisal drilling, including a drill stem test, undertaken, proving up an increase in recoverable hydrocarbons of approximately 20%. By the end of 2017, development project feasibility was confirmed and Faroe booked net 2P reserves of 30.7 mmboe.

Dynamic operator

The Brasse success underpins Faroe's strategic focus on near-field exploration and appraisal opportunities as we continue to pursue our consistent exploration-led business model. The Brasse project also establishes Faroe as a dynamic operator on the Norwegian Continental Shelf with less than three years passing from licence award to the booking of 2P reserves on the field.



2018

Further drilling

Possible drilling to be carried out in 2018 and 2019 to test further upside potential on the Brasse Extension.

2019

PDO submission

PDO submission expected in 2019.

2020-2021

First oil anticipated

Preliminary estimates assume subsea tie-back development.

Production

Tambar case study

Maximising upside potential

Faroe is active in maximising near-term upside potential around the Ula hub, including Oda development, Tambar redevelopment, maturing infill targets on Ula and Blane and potentially redeveloping the Oselvar field.



32
mmboe

2P Reserves
connected to Ula
(net to Faroe)

Tambar timeline

July 2016

DONG deal

Faroe agrees to buy four producing fields from DONG, including Tambar.

October 2016

Preliminary discussions

Discussions begin with new operator Aker BP on Tambar redevelopment.

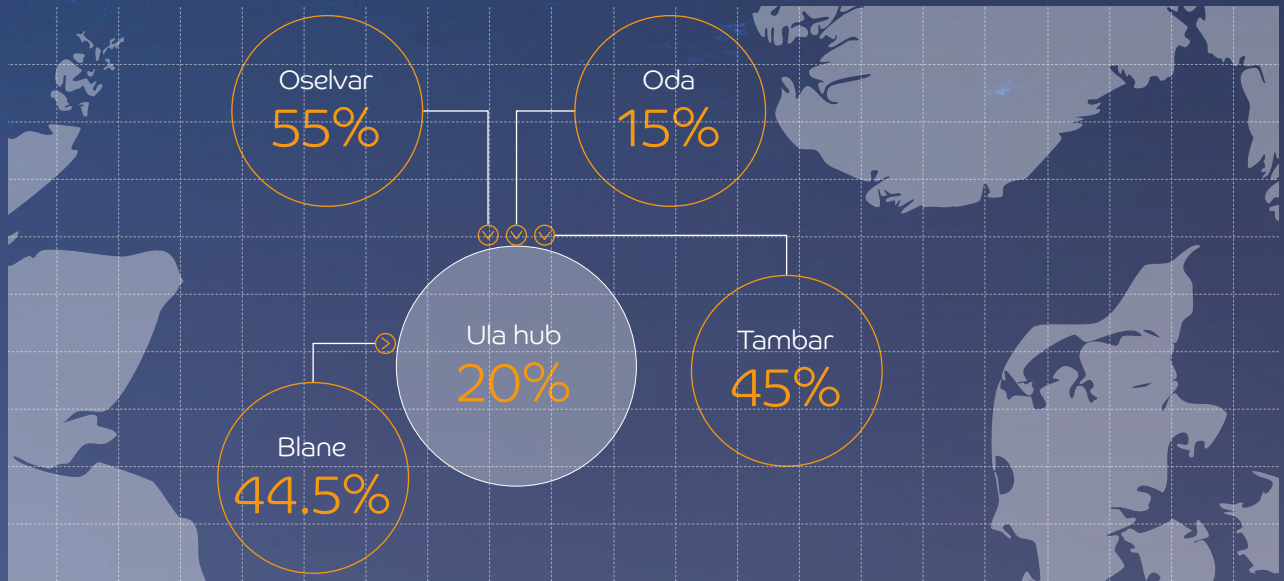
March 2017

Project sanction

Decision to drill two infill wells and gas lift project sanctioned by partners.

Tambar redevelopment

Following the acquisition of Tambar from DONG, the new partnership was able to target upside potential through a joint evaluation approach and nimble decision-making. Tambar redevelopment is expected to extend the life of the field by 10 years.



October 2017

Rig mobilisation

Maersk Interceptor commences drilling of infill wells.

March 2018

Infill wells online

By end of March 2018 both infill wells were completed and online, with initial rates exceeding pre-drill expectations.

Chairman's and Chief Executive's statement

Faroe's consistent strategy of creating value through the drillbit has delivered another year of strong progress and reserves growth.



John Bentley
Chairman

Graham Stewart
Chief Executive

Year-on-year reserves grew by 20% and in the last five years reserves have grown by more than 400% – mainly as a result of maturing our discoveries into attractive development projects. This strategy continues in 2018.

With an average finding cost in Norway of approximately \$1.20/boe, Faroe has developed a compelling route to sustainable value creation for the Company. We look forward in 2018 to drilling up to six exploration and appraisal wells and progressing our material programme of several high-quality developments in order to deliver a significant ramp-up in production in the coming years.

"As we embark on another very busy year for the business, Faroe is again well positioned to capture the growth opportunities which we continue to generate from our balanced portfolio of development."



20%
increase of
2P Reserves



£75m
year-end
net cash

Faroe's exploration is backed by a solid and diverse production base with healthy cash flow – in 2017 Group production of 14,349 boepd generated EBITDAX of £82.2 million. Following the debut issue of a \$100 million senior unsecured bond in November 2017, the part-divestment to Suncor in February 2018 of 17.5% of Fenja for a cash consideration of \$54.5 million, and with an undrawn \$250 million RBL credit facility together with a NOK 1 billion EFF facility, Faroe is now fully funded for all programme investments including the pending Brasse development, at 50% equity. The Company is also in a strong position to invest in new value-accretive developments and potential M&A activity.

Brasse project underpins Faroe's strategic focus on near-field exploration, appraisal and development

The Brasse licence in the Norwegian North Sea, operated by Faroe with a 50% equity stake, was awarded to Faroe in 2015 in the APA 2014 round. In the following summer of 2016 an exploration well and side-track were drilled, discovering material oil and gas volumes in a high quality reservoir. In the summer of 2017, appraisal drilling, including a drill stem test, was undertaken, proving up an increase in recoverable hydrocarbons of approximately 20%. By the end of 2017, development project feasibility was confirmed and Faroe booked net 2P Reserves of 30.7 mmboe. The concept selection phase has commenced with PDO submission expected in 2019. Gross plateau flow rates for the field have the potential to reach 30,000 boepd.

The Brasse field is now a core project with attractive economics, robust at low commodity prices. Brasse's close proximity to competing nearby infrastructure combined with its prolific reservoir qualities and location in shallow water will allow the field to be developed expediently and cost effectively. Significant further exploration and appraisal upside remains to be pursued in the licence and adjacent licence extensions recently awarded to Faroe.

The Brasse success underpins Faroe's strategic focus on near-field exploration and appraisal opportunities as we continue to pursue our consistent exploration-led business model. The Brasse project also establishes Faroe as a dynamic operator on the Norwegian Continental Shelf with less than three years passing from licence award to the booking of 2P Reserves on the field.

Chairman's and Chief Executive's statement

continued

Growth pushing ahead with two field PDOs approved in 2017 and a further PDO submitted for approval

In May 2017, the Oda partnership (Faroe 15%) received PDO approval from the MPE for development of the Oda oil field. Oda, located in the shallow waters of the Norwegian North Sea, and operated by Spirit Energy (formerly Centrica E&P and Bayerngas), is being developed as a four-slot seabed template with a subsea tie-back to the Ula platform (Faroe 20%) and will connect to the existing pipeline between Oselvar (Faroe 55% and operator) and Ula, using the Oselvar facilities at the Ula platform. Production from Oselvar is due to cease in Q2 2018 to allow the Oda tie-in to be undertaken, with the Oselvar partners being financially compensated accordingly. As part of that compensation, Faroe has already received in H1 2017 an initial net receipt from Oda partners of £7.8 million (net of Faroe's share, as an Oda partner, of compensation payments to the Oselvar partners) with further net compensation receipts to Faroe due in the coming months. First oil from Oda is scheduled for H1 2019.

MPE approval of the PDO for the Statoil-operated Njord Future Project and Bauge field (Faroe 7.5%) was granted in June 2017. The Njord Future Project together with the Bauge subsea tie-back are on budget and on timetable and production commencement is scheduled in 2020.

In December 2017 the PDO was submitted for the Fenja field in the Greater Njord Area (Faroe will hold 7.5% following completion of the recently announced partial sale to Suncor Energy Norge AS), comprising three horizontal production wells, one gas injector and two water injector wells. Fenja will be tied back to the Njord A floating production facility for processing and export via the Njord B FSO (floating storage and offloading vessel). The Fenja licence partners are planning to invest NOK 10.2 billion (approximately £900 million) with planned production start-up in Q1 2021 and a planned field life of 16 years.

Faroe continues to make significant investments in boosting production through infill drilling on the Tambar and Brage fields. On Tambar (Faroe 45%) the redevelopment project, encompassing infill drilling and a gas-lift installation, is making good progress with the first of two new Tambar wells on stream and the second expected very soon, and two new Brage (Faroe 14.3%) wells also brought on stream.

Successfully monetising discoveries through divestment

In February 2018 we announced the sale of a 17.5% working interest in the Fenja development, located in PL586 in the Norwegian Sea, to Suncor Energy Norge AS for a post-tax cash consideration of \$54.5 million. Upon completion, Faroe will retain a 7.5% stake in the Fenja development, underlining our support for the project, and aligning Faroe's equity at 7.5% across the entire Greater Njord Area, encompassing Fenja, Njord, Bauge and Hyme, constituting one of the most significant oil and gas investment projects underway offshore Norway. The transaction is expected to reduce Faroe's future capital expenditure on Fenja from £230 million to approximately £70 million, based on the operator's gross projected development cost of NOK 10.2 billion. As detailed in the PDO, the operator, VNG Norge AS, expects total gross recoverable reserves on Fenja of approximately 97 mmbbl (70% of which is oil). The transaction, which has a 1 January 2018 effective date, is expected to complete in 1H 2018.

This transaction marks a major milestone for Faroe, which has so far taken Fenja through exploration and appraisal drilling to the pre-development phase and further validates Faroe's business model of generating strong shareholder returns through exploration. Having held a significant interest in PL586 from its discovery, Faroe has now realised cash returns through this partial-monetisation, while retaining exposure to future cash flows from Fenja. Importantly, the transaction also frees up capital for investment in Faroe's flagship Brasse field which is expected to commence development in 2019, such that Faroe is fully funded for Brasse at its current 50% equity level.

Production portfolio performing well

Faroe's production portfolio performed very well in 2017, delivering net average production of 14,349 boepd in 2017 with an average opex per boe of \$26.5 for producing fields. Faroe's production is spread across a balanced and high quality portfolio of assets with an approximate geographic volume split currently of 80%/20% Norway/UK and an oil/gas split of 55%/45% respectively.

The production portfolio generated EBITDAX of £82.2 million, including the compensation payments recognised at Oselvar following Oda PDO consent in the period. Faroe has benefited from higher oil prices in 2017, and so far in 2018, as well as stronger gas prices. We continue to hedge a significant portion of production and currently have hedged to end-2018 approximately 60% of oil production with put options with an average floor of \$57 per barrel and 80% of gas production at an average price of 42p/therm, again mainly with put options (all on a post-tax basis).

Faroe's medium-term objective, as it unlocks value in its portfolio, is to reduce unit opex and full-cycle costs further, such that the Company grows increasingly profitable and robust. With a fully funded pipeline of ongoing investments in developments and producing fields, together with the maturing of existing discoveries, we are on target to reach our objective of more than doubling production to over 35,000 boepd in the medium term.

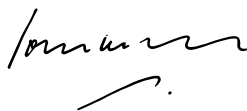
Outlook

Faroe now has an asset base with clear line of sight to deliver material growth in high value production to over 35,000 boepd on an organic and fully funded basis. We also expect to add further new organic projects to this growth plan through maturing a number of discoveries and infill wells as well as potential new discoveries generated from our ongoing exploration programme.

At the core of our value creation model, we actively manage our exploration portfolio in order to maintain a significant ongoing drilling programme from prospects matured in the portfolio. Faroe's exploration track record has been exceptional, with finding costs in Norway around \$1.20/boe. We are set to ramp up our E&A drilling in 2018 and 2019 with a total of six exploration and appraisal wells already scheduled, all capitalising on competitive rig rates and Norwegian State tax incentives, through which 78% of exploration and appraisal costs are recovered.

Faroe has an outstanding team of professionals, committed to the Company's ethos and strategy, and we are very grateful for their commitment and excellent achievements. Complementing our team and successful exploration model, Faroe also has a strong track record of growth through M&A, and we aim to capitalise on these strengths together with our excellent strategic and financial position, as we pursue value-accretive M&A opportunities in our core areas.

John Bentley
Chairman



Graham Stewart
Chief Executive

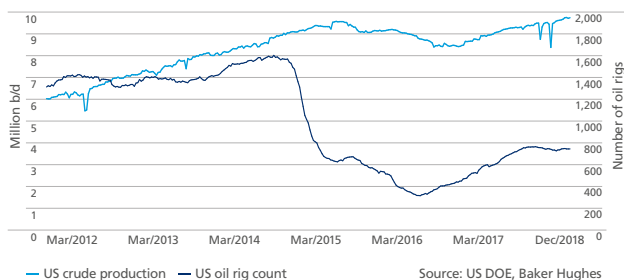


Market overview

Economic/political review and outlook

The global economy is estimated to have grown by 3% in 2017, an improvement on the 2.4% increase in 2016. The outlook for 2018 is for slightly stronger GDP growth of 3.1%. The world's largest economy, the US, is believed to have grown by 2.3% last year, whilst China's economy increased by 6.8%, both showing improvements since 2016.

US crude production and oil rig count



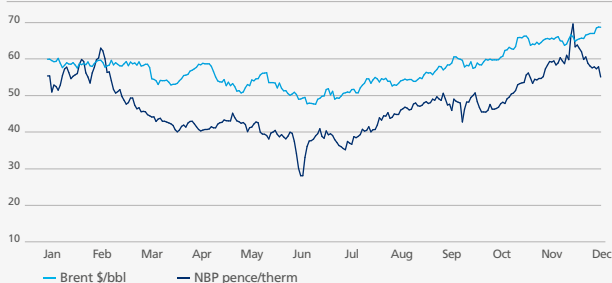
Key trends

- Higher than expected global economic growth in 2017 across a broad base of countries
- Combination of benign financing conditions, recovering commodity prices and rising confidence
- US economy forecast to grow further in 2018, with interest rate increases forecast and China growth expected to moderate slightly
- US rig count rose dramatically in 1H 2017, up from 525 rigs to 756 by mid-year, plateaued thereafter. Higher oil prices driving continued rise in US rig count in 2018
- Very strong Asian demand for LNG resulting in reduced supply to northern Europe, providing support for European gas prices

Commodity prices and outlook

The weakness in the oil price in the first half of 2017 was followed by a strong recovery in the second half. Initial concerns about an oversupply of oil due to a perceived recovery in US shale production were tempered by the positive impact of OPEC cutbacks on global supply levels. UK gas prices fell in 1H 2017 before recovering strongly.

Brent and NBP prices 2017



Key trends

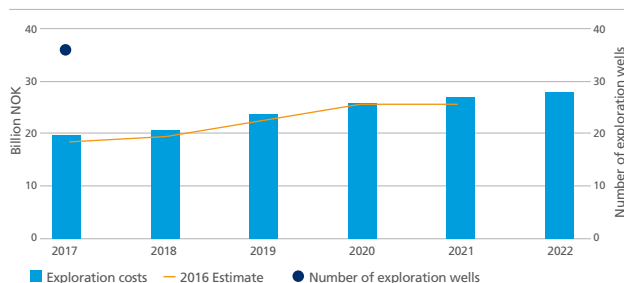
- Brent increased by 15% over the course of 2017, ending the year just below \$67 per barrel, averaging \$55 per barrel throughout the year
- Oil prices fell in 1H 2017 to a low of \$45 per barrel as concerns built over the increasing rig count in the US
- OPEC cutbacks, combined with growing instability in Venezuela, began to influence global oil stock levels in 2H 2017, leading to a sharp recovery in oil prices
- Brent increased by 47% from its low point in June to its peak in December 2017
- International Energy Agency ("IEA") estimates that global demand for oil increased by 1.7% to 97.8 million barrels per day in 2017, ahead of previous forecast levels, whilst supply increased by only 0.4% to 97.4 million barrels per day
- OECD oil inventories ended 2017 at 2.85 billion barrels, a material decrease of 4.5%
- UK National Balancing Point ("NBP") gas price fell 50% in H1 to 26p per therm before recovering to end the year virtually unchanged
- US shale production recovering strongly in the early part of 2018

Investment, costs and activity levels

Despite a recovery in the oil price during last year, drilling and development costs continued to decline. Compared to 2017, total investments are expected to increase slightly in 2018 and gradually thereafter.

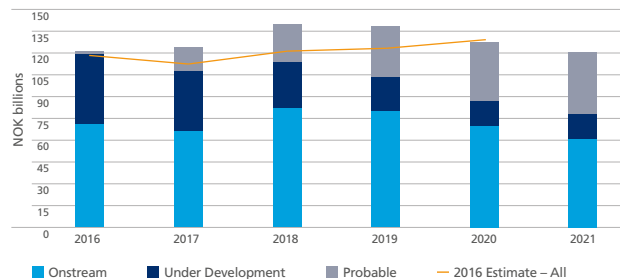
Norwegian exploration drilling in 2017 was on par with the prior year, with 36 E&A wells drilled resulting in 11 discoveries. A modest increase in the number of exploration wells and exploration costs is expected in the next few years.

Exploration costs and number of exploration wells



Exploration drilling picked up in the UK in 2017, with a total of 20 exploration wells drilled compared to 16 the previous year. Although the oil price recovered throughout the year, upstream development spend fell by 30% in the UK, reflecting the material capex reductions across the industry. Production of UK oil and gas at least showed some positive momentum, with the third consecutive year of growth.

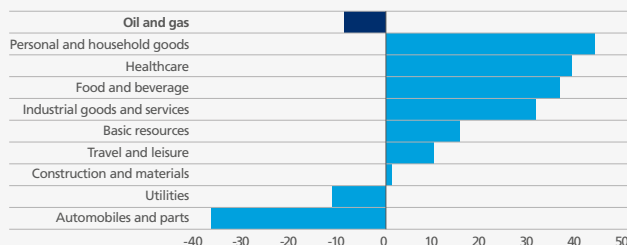
Norway investment forecast



Equity markets and E&P performance

The AIM-listed E&P stocks underperformed in 2017, partially reversing the sharp gains seen in 2016. Despite a 15% increase in the oil price in 2017, and a strong start to the year for the sector, investors remained concerned about funding and the general lack of exploration success.

Performance of AIM All-Share-Sectors 2017



Key trends

- AIM Oil & Gas Index (AXOIG) declined by 9% in 2017, compared to a 39% increase in 2016
- AIM All Share Index (AXX) increased 24% in 2017, versus 14% gain in 2016
- AXOIG fell 31% from its high in February 2017 to its low in August 2017 before rallying towards the year-end

Our strategy

Our strategy is to grow value from reserves and resources through monetising exploration and appraisal successes, participating in selective development projects and pursuing value accretive asset transactions.

Our strategic drivers

① Win licences

- Leverage our technical expertise
- Replenish exploration prospects
- Secure material equity stakes

② Drill and discover

- Drill up to five material wells per year
- Spread risk and cost optimally
- Partner with strong aligned companies

③ Monetise assets

- Exploit drilling success
- Trade assets across value cycle
- Maximise trade value

④ Generate revenue and create value for stakeholders

- Fund wells from cash flow
- Continue to build balanced production portfolio
- Achieve tax efficiency

We have built solid foundations in the three main elements of our business model:

Exploration

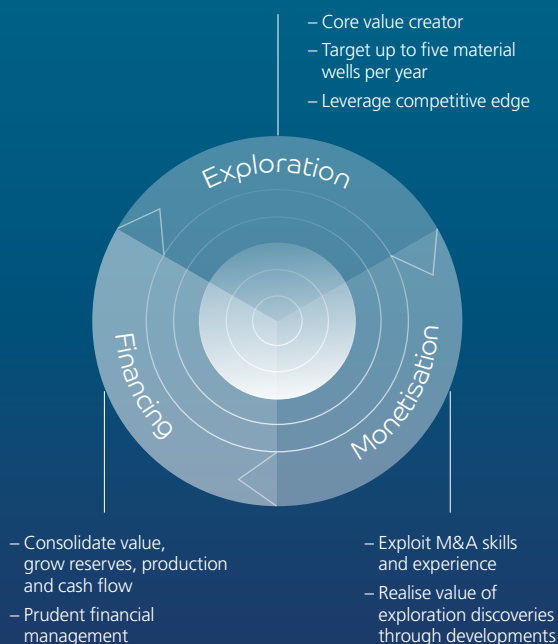
Applications, licence awards, prospect maturation, discoveries;

Monetisation

Appraisal, sale, buy, swap/trade into production; and

Financing

Strong cash reserves, cash flow, debt facilities and tax efficiency.



Key performance indicators

The Board has established the following Key Performance Indicators (KPIs) for the Group which are focused principally on managing the activities inherent in exploration, appraisal and production operations:

	Explanations	Performance	Strategic drivers
Health, Safety and Environment			
ZERO	A lost-time injury is defined as an occurrence that resulted in a fatality, permanent disability or time lost from work of one day/shift or more on Faroe operated assets.	No time was lost on operations during 2017 or 2016 on operated assets.	2
Operations			
Delivery of successful drilling campaign	Delivery of active and successful exploration drilling programme.	Completed three wells in the period with one success ¹ and Iris/Hades, was spudded in December 2017. Three wells were drilled in 2016 of which two were discoveries ² .	1 2
2017 4			
2016 3			
2015 5			
2014 4			
Growth in reserves	Growth in reserves.	Reserves increased by 20% over the period to 97.7 mmboe (adjusted for Fenja divestment).	2 3 4
2017 97.7			
2016 81.3			
2015 57.4			
2014 30.6			
Growth in resources	Growth in resources.	Contingent resources decreased by 13.2% to 79 mmboe, reflecting Brasse transfer to 2C.	1 2 3
2017 79.0			
2016 90.9			
2015 98.0			
2014 109.1			
Growth in production	Growth in production.	Economic production reduced from 17,395 boepd in 2016 to 14,349 boepd in 2017. Accounting production increased from 8,026 boepd in 2016 to 14,139 boepd in 2017.	3 4
2017 14,349			
2016 17,395			
2015 10,530			
2014 9,106			
Corporate and finance			
Total Shareholder Return (TSR %)	The total return of a stock to an investor (capital gain plus dividends).	The share price increased from 103p on 1 January 2017 to 105p on 31 December 2017.	3 4
2017 1.9			
2016 90			
2015 -49			
2014 -16			
EBITDAX	Earnings before interest, tax, depreciation, amortisation and exploration expenditure (EBITDAX).	EBITDAX increased from £25.8 million in 2016 to £82.2 million in 2017.	3 4
2017 82,200			
2016 25,800			
2015 60,448			
2014 59,088			
1 Brasse 2 Brasse and Njord North Flank			

1 Brasse

2 Brasse and Njord North Flank

Operational report

Our operational performance this year has been strong, significantly enhanced by the field development programme to deliver long-term profitable production growth.



14,349
boepd

total average economic
production for the full year



97.7¹
mmboe
2P Reserves

¹ After adjusting for Fenja sell down.

Helge Hammer
Chief Operating Officer

A handwritten signature in black ink, reading 'Helge Hammer'.

The Company has continued to make good progress across all areas of activity, delivering: production from the portfolio at the higher end of guidance; a substantial increase in the Company's 2P Reserve base; the successful operated appraisal programme on the Brasse discovery, and approval of two key new field development PDOs; and further new licence awards in Norway.

Exploration and appraisal

In the first half, Faroe participated in two E&A wells, the Eni-operated Boné exploration well in the Barents Sea (dry) and the Faroe-operated Brasse appraisal well (discovery). The Company also added four licences to the licence portfolio through awards in the 2016 Norwegian APA licensing round. The drilling programme continued with the Goanna exploration well (Faroe 30%) in August 2017. The well was unfortunately dry but Faroe was fully carried on the well cost. The OMV-operated Iris/Hades (formerly known as Aerosmith) exploration well in the Norwegian Sea (Faroe 20%) commenced in November 2017 and the results are expected soon. The Spirit Energy-operated Fogelberg appraisal well (currently Faroe 25%) commenced drilling in February 2018 and operations are ongoing. All of these wells are located in Norway where Faroe receives a tax rebate of 78% on all exploration and appraisal expenditure.

Following a partner withdrawal from the Fogelberg licence and two separate farm-out deals by Faroe, all of which are expected to complete in 1H 2018, Faroe's equity will reduce from 25% to 15%, with an effective date of 1 January 2018.

Norwegian licence round awards

In January 2018, Faroe was awarded eight new prospective exploration licences including four operatorships under the 2017 Norwegian APA Licence Round on the Norwegian Continental Shelf. Three of the licences are targeting new plays for the Company, namely the Blue Libelle prospect on the Tampen Spur on the north-western margin of the North Viking Graben (Faroe operator), the Århus prospect in the Åsta Graben, north of the Trym field, and the Skråmetindan prospect on the Cod Terrace in the Central Graben.

Production

Faroe achieved net average economic production of 14,349 boepd (2016: 17,395 boepd), a reduction over the previous year reflecting the work programmes being undertaken on some of the Company's fields and the temporary loss of production from the Njord and Hyme fields whilst the Njord Future Project continues. Average operating expenditure per barrel of oil equivalent (opex/boe) in the period was \$26.5 (excluding accrued tariff costs in relation to future upgrades) (2016: \$24.8). Faroe expects to see a material reduction in unit operating costs as its new low operating cost subsea fields come on production in the following years.

Faroe's production base is spread across a portfolio of oil and gas assets in Norway and the UK. Approximately 76% of total production came from Norwegian fields and approximately 54% of total production was oil. In Norway, the main producing fields are Trym, Tambar, Ula, Brage and Ringhorne East, and in the UK, the main fields are Schooner, Ketch and Blane.

The future of the Trym field beyond 2019 (Faroe 50% and operator) has been secured following the final investment decision to redevelop the Tyra host platform in Denmark (Faroe has no working interest in Tyra). Trym is now scheduled to produce for an extended period until 2H 2019 before being suspended temporarily in order to allow the Tyra redevelopment works to be carried out over a period of around three years. Trym production was temporarily shut in during Q1 2018 as a result of a pipeline integrity issue at the Tyra gathering hub, but resumed production in March 2018.

The redevelopment project on the Tambar field (Faroe 45%) continues with the drilling of two infill wells and the installation of gas lift in three existing wells designed to increase significantly production from the field. The two infill wells, which targeted undrained areas in the north and south of the field, have now been drilled with flow rates from both wells exceeding pre-drill expectations. The first well was brought on stream earlier this month and a second is expected later in March 2018. Initial production rates from the two wells are estimated to be in the range of 10,000-15,000 boepd (Faroe 4,500-6,750 boepd). It is expected that the overall investment programme including gas lift will extend field life by up to 10 years, with the additional benefit of lowering unit operating costs in the Ula hub area. The encouraging results from the infill campaign will be used to refine the field model and to plan further development of the Tambar reservoir.

On the Brage field (Faroe 14.3%), the Statfjord and the Fensfjord producer wells, drilled in 2017, have been brought on stream. The second Statfjord producer was completed in January 2018 and will be put on stream in the coming weeks. Based on drilling results, the well is expected to deliver production rates well above pre-drill expectations. A further horizontal well in the Sognefjord formation is being evaluated for drilling in 2H 2018.

On the Ula field (Faroe 20%), the operator continues to mature targets for a new infill campaign which is expected to commence in 2019. Potential infill targets include wells to expand the use of WAG (water alternating gas) injection to increase recovery, the deeper Triassic reservoir which has only one well in production today, as well as near field discoveries such as Ula North. The 4D seismic survey successfully acquired in 2017 will provide important new information when processing is complete in Q2 this year. A number of significant upgrades to the field facilities are also under way which will support long-term production.

Operational report

continued

In the UK, the operator Repsol Sinopec is now considering the selection of infill targets on the Blane field (Faroe 44.5%), following the successful completion of the subsea upgrades in 2017. Production from Schooner and Ketch is expected to cease in Q3 2018 with the closure of the export system and onshore gas facility at the Theddlethorpe terminal, operated by ConocoPhillips.

Development projects

Oda (Faroe 15%): this field is being developed as a subsea tie back to the Ula platform (Faroe 20%), approximately 13 kilometres to the east. The project, which is both on schedule and within budget, is now entering a busy offshore construction phase this spring with three wells being drilled in the field (two producers and one water injection well). First oil is scheduled for mid-2019, with gross plateau production expected to be 30,000 boepd (4,500 boepd net to Faroe). Production from the Oselvar field (Faroe operated 55%) is scheduled to cease in Q2 2018 to allow the Oda tie-in to be undertaken. Upon cessation of production the Oselvar owners (Faroe 55%) will receive a final compensation payment, dependent on the Oselvar field production level at the time it is shut in. An initial payment to Faroe of £7.4 million net was received in June 2017.

Njord and Bauge (Faroe 7.5%): the Njord Future project encompasses refurbishment of the Njord facilities to allow continued production and development of the Njord and Hyme fields and upgrading and modifications to enable the Bauge and Fenja fields to be tied back. The Njord Future Project is progressing on schedule and within budget. In 2018, key milestones include installation of blisters to enhance stability on all four columns, installation of column top extensions and deck boxes. Truss work reinforcement is also ongoing. Current timing is for the Njord A platform to be towed offshore during spring 2020. The Bauge development project is also progressing on schedule and within budget. Contracts for marine and drilling operations are currently being progressed. Njord and Hyme are expected to recommence production in Q4 2020 followed by first oil from Bauge shortly thereafter.

Fenja (Faroe 7.5% following completion in H1 2018): in December 2017, the PDO was submitted for the Fenja field in the Greater Njord Area comprising three horizontal production wells one gas injector well and two water injector wells, tied back to the Njord A floating production facility for processing and export via the Njord B FSO (floating storage and offloading vessel). The Fenja licence partners are planning to invest NOK 10.2 billion (approximately £900 million) with planned production start-up in Q1 2021 and a planned field life of 16 years. In February 2018, the Company announced a sale of a 17.5% interest in Fenja to Suncor for cash consideration of \$54.5 million, to reduce its interest to 7.5%, harmonise its equity interests with its other interests in the Njord area and to rebalance capital allocations across the portfolio. The sale is subject to final approval by the MPE.

Brasse (Faroe 50%): at the end of 2017, the Brasse feasibility study phase was completed confirming several attractive development solutions and export routes. The preliminary reservoir drainage plan includes three to six subsea production wells and possible water injection for pressure support. Gross plateau flow rates for this field have the potential to reach 30,000 boepd, and first production is targeted for 2021. The key project milestone for 2018 will be the Concept Selection including the selection of a reservoir drainage plan and a processing host. The PDO submission is expected in 2019.

Reserves & Resources

Reserves

The Company's internal estimate of Proven and Probable (2P) Reserves at 1 January 2018, prepared in accordance with the Petroleum Resource Management System guidelines endorsed by the Society of Petroleum Engineers, World Petroleum Congress, American Association of Petroleum Geologists and Society of

Petroleum Evaluation Engineers, has been estimated at 114.1 mmboe (1 January 2017: 81.3 mmboe) – increasing reserves by 40% over the year (before adjusting for the disposal of a 17.5% interest in the Fenja field). The significant increase (reserves replacement of approximately seven times) is a result of both the conversion of Brasse from 2C Contingent Resources to 2P

Reserves and incremental projects across the portfolio, which generated positive reserve revisions notably on Tambar. Adjusting for the divestment of a 17.5% interest in the Fenja field, announced in February 2018 and with an effective date of 1 January 2018, 2P Reserves at 1 January 2018 were 97.7 mmboe, which represents an increase of 20% year on year.

2P Reserves	Gas (bcf)			Liquids (mmbbls)			Total (mmboe)
	Norway	UK	Group	Norway	UK	Group	Group
1 January 2017	108.0	14.3	122.3	58.0	2.9	60.9	81.3
Revisions	7.5	(6.3)	1.2	8.0	(0.1)	7.9	8.2
Acquisitions	–	–	–	–	1.0	1.0	1.0
Transfer from 2C	32.1	–	32.1	23.5	–	23.5	28.8
Production	(9.2)	(4.6)	(13.8)	(2.4)	(0.4)	(2.8)	(5.2)
1 January 2018	138.4	3.4	141.8	87.1	3.4	90.5	114.1

Contingent Resources

At 1 January 2018, 2C Resources were estimated to be 86.0 mmboe (before adjusting for the disposal of a 17.5% interest in the Fenja field) representing a decrease of 5% over the year (1 January 2017: 90.9 mmboe). Additional Contingent Resources,

mainly in Ula, Tambar and Oselvar, did not fully compensate for the transfer of Brasse to reserves. Adjusting for the divestment of a 17.5% interest in the Fenja field, 2C Contingent Resources at 1 January 2018 were 78.6 mmboe, which represents a decrease of 14% year on year.

2C Contingent Resources	Gas (bcf)			Liquids (mmbbls)			Total (mmboe)
	Norway	UK	Group	Norway	UK	Group	Group
1 January 2017	150.6	–	150.6	65.8	–	65.8	90.9
Revisions	46.9	–	46.9	12.8	1.7	14.5	22.4
Acquisitions	7.6	–	7.6	0.5	–	0.5	1.8
Disposals	–	–	–	(0.3)	–	(0.3)	(0.3)
Discoveries	–	–	–	–	–	–	–
Transfer to 2P	(32.1)	–	(32.1)	(23.5)	–	(23.5)	(28.8)
1 January 2018	173.0	–	173.0	55.3	1.7	57.0	86.0

Helge Hammer
Chief Operating Officer



Finance review

Debut bond issue of \$100 million and partial divestment of Fenja development to Suncor mean that the Group is fully funded for its exploration and development programme.



Jonathan Cooper
Chief Financial Officer

A handwritten signature in black ink that reads "Jonathan Cooper". The signature is fluid and cursive, with the first name and last name clearly distinguishable.



£149.1m
gross cash position
(2016: £96.8 million)

£82.2m
EBITDAX
(2016: £25.8 million)

Overview

The year end gross cash position was £149.1 million, with net cash of £75.0 million (2016: gross/net £96.8 million). The increased cash position was due to the issue of a \$100 million senior unsecured bond in the Nordic bond market in November 2017 as well as EBITDAX increasing to £82.2 million in the year (2016: £25.8 million). Faroe's active exploration and appraisal programme in Norway, which benefits from the 78% exploration tax refund, has continued with four wells drilled in 2017, of which the Faroe-operated Brasse appraisal well resulted in an increase in estimated recoverable resource volumes and the Boné well (Faroe 20%) and Goanna (Faroe's costs fully carried for its interest of 30%) being dry. The Iris/Hades exploration well spudded in December 2017 and drilling is still in progress. In February 2018, the Group announced a partial divestment of the Fenja discovery for a cash consideration of \$54.5 million, reducing the Group's

exposure on future capital expenditure on Fenja to approximately £70 million, upon completion of the deal.

Adjusted revenue, including realised hedging losses of £1.9 million (2016: gain £4.7 million), averaged \$46 per boe (2016: \$42 per boe) after taking account of £30.7 million of underlift (2016: £7.0 million overlift), included in revenue and cost of sales. Opex per boe was \$30 in 2017 compared to \$31 in 2016 reflecting one off tariff costs in relation to future upgrades, operating costs on non producing and development assets, including Njord and Hyme opex post production suspension. Opex per boe on producing assets excluding accrued facility upgrade costs was \$26.5/boe (2016: \$24/boe). DD&A per boe increased by \$0.8 to \$11.3 boe (2016: \$10.5 boe).

Income statement

IFRS accounting revenue in the year was £152.9 million (2016: £94.8 million) and is different to 'adjusted revenue' of £181.8 million (2016: £92.5 million) as the former excludes volumes of oil and gas produced but not physically lifted in the period ("underlift") and realised hedging losses. In calculating IFRS revenue, the underlift movement of £30.7 million (2016: £7 million overlift) is credited to (i.e. reduces) cost of sales under IFRS. Faroe sells most of its oil under payment quantity contracts, and so has received payment for the outstanding underlift. The payment sits within deferred income on the balance sheet until the crude is lifted and then is released to IFRS revenue. The increase in revenue reflects higher accounting production, mainly due to the acquisition of interests in producing fields from DONG in December 2016, and a higher realised price per boe. Overall, the Company realised a £1.9 million loss (2016: £4.7 million gain) on its hedging and forwards sales activities in 2017.

Cost of sales, including depreciation of producing assets, but before impairment charges, was £132.5 million (2016: £96.7 million). Cost of sales excluding net underlift movement (see paragraph above) was £163.2 million (2016: £89.7 million) reflecting an increase in accounting production from 8,026 boepd to 14,139 boepd and one-off estimated future upgrade tariff costs of £9.5 million falling due to Ula as a result of the planned shut-down of Oselvar, and is partially offset by the estimated £2.0 million tariff receipt which is included in Revenue as a result of the Group's interest in Ula. Pre-tax impairment charges of £13.0 million (post-tax £6.6 million) (2016: £2.9 million and £0.9 million pre- and post-tax respectively) mainly related to Schooner and Ketch and were driven by an increase in abandonment cost estimates. The other impairment charge related to Brage. The Group made a gross profit for the year of £7.4 million (2016: loss £4.8 million).

Other income was £17.4 million (2016: expense £8.4 million), of which £18.2 million related to compensation income between Oselvar (Faroe 55%) and Oda (Faroe 15%) and was offset by a realised hedging loss of £1.9 million. £9.1 million of the compensation income was received in June 2017 following PDO approval of the Oda development. A further £9.1 million has been accrued and recognised as income and will be received in 2018 when Oselvar is taken offline. The compensation income is partially offset due to the Group's ownership of Oda, with capex costs of £1.3 million being paid in June 2017 and a further £1.2 million being accrued at the year end reflecting further compensation due to Oselvar for the planned shut down. EBITDAX in 2017 increased to £82.2 million compared to £25.8 million in 2016.

The Group made a post-tax gain of £0.7 million (pre-tax £7.2 million) on the disposal of Jotun, an asset due for abandonment. The Group paid £1.1 million on completion to Exxon of the disposal of Jotun, leading to a reduction in the pre-tax decommissioning provision of £8.2 million (post-tax £1.8 million).

Pre-tax exploration and evaluation expenses for the year were £25.9 million (post-tax: £6.9 million) (2016: £33.5 million and £14.5 million pre- and post-tax respectively). This includes pre-award exploration expenses of £4.3 million and write-offs of licence-specific exploration and evaluation expenditure of £21.5 million on previously capitalised licences where active exploration has now ceased. The majority of the exploration costs which were written off during the year related to PL716 (Boné), along with other exploration costs on a number of licences.

Expensed administration costs in 2017 were reduced to £7.7 million (2016: £10.2 million) mainly due to an additional charge in 2016 of £2.0 million following a true-up of 2015 timewriting rates, and due to increased activity on operated assets (in particular Brasse) leading to a higher G&A recharge to assets.

The Group's reported loss before tax was £13.7 million (2016: £61.6 million). Loss after tax was £11.4 million (2016: £32.9 million).

Hedging

In line with Group policy approximately 60% of post-tax production was hedged in 2017, with realised hedging losses, net of cost, of £1.9 million (2016: gain £4.7 million). The cost incurred for the 2017 hedges was £2.3 million (2016: £1.0 million). The hedging was predominantly with put options, with 93% of gas and 31% of oil production (post-tax) hedged in 2017.

Finance review

continued

At December 2017, the Group had entered into hedging contracts covering approximately 85% of 2018 total expected gas production (on a post-tax production basis) and 41% of expected oil production (on a post-tax production basis). The gas hedging contracts are put options and swaps with floors between 35 and 48 pence per therm. The oil hedging contracts are put options with an average strike price of \$55 per barrel. Unrealised hedging losses for the open hedge contracts for 2017 were £0.8 million (2016: £1.4 million) based on mark-to-market calculations and are recognised as derivative financial liabilities (2016: liabilities). The unrealised hedging losses (2016: losses) are shown as Other income/(expense) in the Income Statement, net of hedging costs of £2.3 million (2016: £2.6 million).

Further gas and oil hedges have been undertaken in 2018 following which approximately 60% of post-tax oil production is hedged in 2018 and 6% of post-tax oil production is hedged in 2019. The Company continues to monitor the commodity market and aims to extend the current hedging programme at opportune moments, taking a layered approach to its hedging strategy.

Faroe is subject to taxation under two regimes in Norway, namely: offshore where a special tax of 53% is applied, and onshore where the standard corporation tax rate is 25%. Hedging gains fall only within the onshore regime and hence the concept of hedging “post-tax production” which implies that in order to be fully hedged in Norway on a post-tax basis, approximately 29% of pre-tax barrels need to be hedged.

Taxation

In Norway, the Company benefits from a 78% exploration cost refund, meaning that for every £1 spent the Government will return 78p of eligible expenditure in the form of a rebate in the following year, to the extent it is not offset against current year profits from producing assets. Through the EFF, Faroe can borrow 96% of the 78p per £1 rebate, thereby maximising equity leverage in Norwegian exploration and minimising the need to farm down. The Norwegian tax system therefore ensures a cost-effective fiscal environment in which to explore, and also cushions the cash impact of falling oil prices, as lower profits from production result in an increased tax rebate.

The amount of tax receivable at 31 December 2017 was £35.6 million (2016: £41.8 million) which is the tax refund on exploration expenditure in Norway net of taxable profits generated by the Norwegian producing assets. The refund will be received in November 2018. The tax credit in the Income Statement was £2.3 million (2016: £28.7 million) and consisted mainly of the Norway tax receivable, and origination of timing differences of £32.3 million.

Development capex in Norway is depreciated on a straight-line basis over six years for tax purposes. In addition, an uplift of 21.6% can be offset against the 53% special tax. The uplift is taken on a straight-line basis over four years. This means that close to 90% of capex spend is recovered through the tax system. At December 2017, Faroe had carried forward tax capex balances of £107.6 million and carried forward capex uplift of £44.5 million in Norway. In addition, at December 2017, Faroe had carried forward tax losses in Norway of £21.0 million and £14.4 million for corporation tax and special tax respectively. At December 2017 the Group had unrelieved tax losses in the UK of £53.8 million which are available indefinitely for offset against future taxable profits.

In December 2017 the Company had a deferred tax asset of £114.5 million (2016: £122.1 million) in respect of carried forward tax losses, capex balances and uplifts in the UK and Norway, net of other temporary differences.

Balance sheet

Expenditure of £144.2 million (2016: £79.4 million) on intangible and tangible assets, prior to tax rebate, was made in the year, of which £47.7 million (post tax £10.5 million) related to exploration expenditure, primarily on Brasse and Boné. £93.2 million related to development expenditure, principally reflecting pre-sanction costs on the Oda field and the Njord capital enhancement project and drilling costs on the Tambar and Brage fields. The Group also completed the acquisition of an additional 13.9935% of Blane from JX Nippon, paying \$3.9 million (£2.8 million) on completion. The acquisition increases the Group's equity in the field to 44.5%.

During the period, the book value of Fenja (previously Pil & Bue) and Bauge was reclassified from intangible exploration assets to property, plant and equipment, totalling £58.7 million (pre tax: £12.9 million) following PDO submission and a clearly defined path and timeline to project sanction. £47.7 million of the £58.7 million related to the 17.5% interest in Fenja, which was divested in 2018, was subsequently classified as held for sale at the year end.

The Group recognises the discounted cost of decommissioning when obligations arise. The amount recognised is the present value of the estimated future expenditure determined by local conditions and requirements, net of any amounts carried by third parties. At 31 December 2017 the Group had decommissioning provisions of £262.4 million (2016: £267.1 million). The reduction in the provision is mainly due to movement in cost estimates and abandonment activity in the year, partly offset by the acquisition of additional interest in Blane. Most of the decommissioning expenditure is scheduled to be incurred from 2020 to 2035.

Cash flow

Closing cash was £149.1 million (2016: £96.8 million). Net cash at the year end was £75.0 million (2016: £96.8 million). In addition, restricted cash of £7.4 million relating to prepaid abandonment costs is included in Trade and Other Receivables. Faroe benefits significantly from an exploration financing credit facility of NOK 1,000 million for provision of 75% (as described above) of its eligible net exploration costs in Norway on a cash flow basis, such that only 25% of this expenditure is funded from Company equity. The EFF borrowings of NOK 365 million (£32.9 million) (2016: NOK 380 million, £35.8 million) are repaid when the tax rebate is received in November of the year following the related expenditure. In November 2017 the Company received the tax rebate for 2016 of £41.2 million, most of which was used to repay the 2016 utilisations of the EFF.

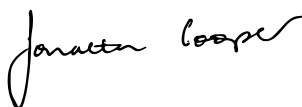
The Group also has a secured US\$250 million (approximately £203.0 million) reserve based lending facility which is available for both debt and issuance of letters of credit. At 31 December 2017 the calculated borrowing base amount was £174.6 million, of which £nil was drawn (2016: £nil million).

With a combination of the current cash in the business, cash flow from producing assets and headroom in the Group's bank facilities, the Group will be able to fund currently committed capital expenditure (exploration and development/ production). The pre-tax capital expenditure for 2018 is forecast to be approximately £255 million.

Dividend

The Directors do not recommend payment of a dividend.

Jonathan Cooper
Chief Financial Officer



Risk management and internal controls

The Board is responsible for establishing and maintaining the system of internal controls which has been in place throughout 2017.



The system of internal controls is vital in managing the risks that face the Group and safeguarding shareholders' interests. The Group's internal controls are designed to manage rather than eliminate risk as an element of risk is inherent in the activities of an oil and gas company. The Board's obligation is to be aware of the risks facing the Company, mitigate them where possible, insure against them where appropriate and manage the residual risk in accordance with the stated objectives of the Group.

A robust assessment of the principal risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity, is undertaken by the Board of Directors and Audit Committee. The effectiveness of the Group's system of internal control is also monitored on an ongoing basis by both the Audit Committee and the Board of Directors. At each meeting, the Audit Committee reviews those risks and associated controls which are predominantly financial whilst the Board of Directors reviews those risks that are predominantly operational or of a corporate nature. The process involves the review of the updated Risk Registers and discussion with key personnel as to the implementation of such control associated procedures.

An annual review of all risks, financial, operational and corporate, was undertaken in December 2017 by the Board of Directors which includes the members of the Audit Committee. This review involves the assessment of the Risk Registers and the Group's written procedures. Following the annual review it was considered that the internal controls in respect of the key risks that face the Group were appropriate.

Principal risks and uncertainties

Aside from the generic risks that face all businesses, the Group's business, financial condition or results of operations could be materially and adversely affected by any of the risks described below.

These risks should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties and additional risks and uncertainties that are not presently known to the Directors, or which they currently deem immaterial, may also have an adverse effect on the Group's operating results, financial condition and prospects.

Whilst the risks below have been laid out in order of priority, it should be stressed that in so doing both magnitude and probability have been combined, to assess the scale, which is imperfect e.g. the probability of a major uninsured event is low but the consequences potentially very significant.

Area	Description	Mitigation
Operational risks	The effective management of operational and HSES risk exposure is the number one priority for the Board of Directors and executive and management teams. As a participant in offshore exploration, development and production the Group is exposed to material risk in the event of there being a major process safety incident or operational accident, natural disasters, failure to comply with approved policies, and pandemics. The consequences of such risks materialising can be injuries, loss of life, environmental harm, disruption to business, activities and financial loss. Depending upon the cause and severity, the materialisation of such risks may have a material adverse effect on the Group's business.	These operational and HSES risks are managed by the Group through its dedicated HSES personnel and Business Management System, third parties and other operators the Group partners with. The Group maintains a programme of insurance to cover such exposure up to recognised industry limits but should an incident occur of a magnitude in excess of such limits, the Group would be fully exposed to the financial consequences.
Commodity prices	The market price of hydrocarbon products has been very volatile and may be at a level below the operating costs of the Group for an extended period. This not only reduces short-term cash flow needed to meet the Group's commitments in the short term but also reduces the debt capacity and economic value of the Group's projects which may be significantly reduced or rendered uneconomic, which in turn may lead to early abandonment. Early abandonment crystallises liabilities earlier and negatively impacts the Group's cash flow. There is a particular risk when committing to long-term development contracts or acquisitions based on assumed future hydrocarbon prices.	Where and when appropriate the Group will continue to put in place suitable hedging arrangements, in accordance with its hedging policy, to mitigate the risk of a fall in commodity prices but such arrangements will only cover the relatively short term, leaving the Group exposed to any longer-term decline in commodity prices, and in addition some of the hedging arrangements entered into by the Group also carry inherent delivery risks.

Principal risks and uncertainties

continued

Area	Description	Mitigation
Cash flow and financing risk	<p>The ability to finance firm commitments, participate in the Group's developments (notably the Greater Njord Project, Fenja, Oda, Brasse developments and Tambar infill project) and generally develop the Group's business depends upon:</p> <ul style="list-style-type: none"> – cash flow from the Group's producing assets: with a significant proportion of production derived from non-operated production, cash flow is dependent upon a combination of factors including field performance (both reservoir and facilities), commodity prices, fiscal regime and operating costs, all of which are substantially out of the control of the Group; and – finance from the equity capital markets, debt finance, exploration tax refund (in Norway along with the supporting exploration debt facility), farm downs and other means. <p>A number of the Group's development commitments and infill opportunities are long term in nature and there is no assurance that the Group will be successful in generating or obtaining the required financing. In those circumstances some interests may be relinquished, sold at an undervalue and/or the scope of operations reduced or ultimately the Group may default on its obligations.</p> <p>In the event that sufficient funds are not available to finance the business, it would have a material adverse effect on the Group's financial condition and its ability to conduct operations.</p>	<p>The Group seeks to mitigate these risks by:</p> <ul style="list-style-type: none"> – maintaining a diverse portfolio of oil and gas producing interests in both the UK and Norway; – rigid financial discipline and maintaining a strong balance sheet; – the Board reviewing and approving the financial strategy of the Group; – regular review of short-term and longer-term cash flow forecasts by senior management and the Board; – maintaining strong relations with its banking syndicate, bond holders and its institutional shareholders; and – where there is significant asset concentration risk, the arrangement of business interruption insurance.
Development risks	<p>The Group is participating in certain development and redevelopment projects notably the Oda development, the Njord Future Project (which incorporates the Bauge development) and is planning to participate in the Fenja and Brasse developments. The Group's ongoing development projects involve advanced engineering work, extensive procurement activities and complex construction work to be carried out under various contract packages at different locations, both offshore and onshore. Furthermore, the Group (together with its licence partners), must carry out drilling operations, install, test and commission offshore installations and obtain governmental approval to take them into use, prior to commencement of production. The complexity of such development projects makes them sensitive to circumstances which may affect the planned progress or sequence of the various activities, as this may result in delays or cost increases.</p> <p>The current or future projected target dates for production commencement may be delayed and significant cost overruns may incur due to delays, changes in any part of the development projects, technical difficulties, actual reserves not being as high as estimated at PDO, project mismanagement, equipment failure, natural disasters, political, economic, taxation, legal, regulatory uncertainties, terrorism and protests, which again may materially adversely affect the Group's future business, operating results, financial condition and cash flow. Ultimately, the Group may be unable to meet its ongoing share of expenditure and be forced to withdraw and/or default on its committed obligations, which would have a material adverse effect on the Group.</p>	<p>The Group is seeking to limit its exposure to any one development by taking measured equity participations in multiple developments. However, a consequence of such mitigation is to increase the probability of a development risk materialising by virtue of the greater number of projects.</p>
Production risk	<p>The Group has a hub strategy and is currently focused on three key hubs and hence, the Group's production of oil and gas is concentrated in a limited number of offshore fields and host facilities, in particular the Ula and Njord host facilities. If mechanical or technical problems, storms or other events or problems affect the production on one of these key offshore fields, facilities or the downstream infrastructure, it may have direct and significant impact on a substantial portion of the Group's production. Also if the actual reserves associated with any one of our fields are less than the estimated reserves, their continued operation and financial condition could be materially adversely affected.</p> <p>Long-term unscheduled or scheduled shutdowns of production may have a material impact on the business, as the Group will lose production income whilst also bearing its share of any continuing fixed operating expenditure along with associated remedial or repair works which may be unquantifiable at outset and/or subject to cost overruns.</p>	<p>For the longer term, the Group is seeking to balance these risks by building a portfolio of assets and multiple hubs that carry a range of differing technical and commercial risks, and limit the amount invested in any one project.</p>

Area	Description	Mitigation
Decommissioning costs	<p>Decommissioning cost estimates are based on subjective judgements and determinations which will change over time based on new information, costs and practices and such estimates may increase materially.</p> <p>The Group has an abandonment provision on its balance sheet to account for its expected share of decommissioning costs relating to its operations.</p> <p>The actual costs of decommissioning are expected to be paid from the Group's cash resources and cash flow generated from both the Group's existing and future producing assets. In accordance with the practice generally employed in offshore oilfield operations, the Group does not have a sinking fund other than where it is required to do so to meet the costs of decommissioning its producing assets.</p> <p>The estimated timing of decommissioning is dependent upon a number of factors and a material reduction in production levels or commodity prices and/or an increase in operating expenditure may bring forward such timing.</p> <p>Given the uncertainty of the scope, timing and cost of decommissioning, the associated liabilities may exceed the Group's cash resources to a point where the Group does not have the funds available to meet such costs.</p> <p>The Group plans to have adequate production profits to shelter the decommissioning costs. To the extent these past profits or production are not available, the Group is then exposed to much higher pre-tax abandonment costs.</p>	<p>The Group has a balanced portfolio of producing assets that are expected to decommission at different times to mitigate the overall cost impact. Notwithstanding that, the Group is reliant upon generating surplus funds from its portfolio of continuing and new producing assets to meet such liabilities.</p> <p>The Group has established a post-tax decommissioning provision fund to meet the costs of decommissioning its interests in the Ula, Tambar, Tambar East, Oselvar and Trym fields. However, in the event of early abandonment the fund may not be adequately funded to meet the cost of decommissioning.</p>
Uninsured liabilities	<p>There can be no assurance that the proceeds of insurance applicable to covered risks will be adequate to cover expenses relating to losses or liabilities. Accordingly, the Group may suffer material losses from uninsurable or uninsured risks or insufficient insurance coverage. In addition, the Group insures most of its assets in line with the insurance values prepared by the operators but there is no guarantee that such estimates will cover the full extent of any liability or indeed that such estimates are reflective of the actual replacement costs.</p>	<p>The Group maintains a range of energy and other insurance cover in accordance with industry practice.</p>
Loss of infrastructure	<p>The Group relies on third party infrastructure (including host platforms, pipelines and terminals) for the continuing operation of its producing assets. This infrastructure is in turn subject not only to the risk of physical damage but it also has economic thresholds governed by a combination of commodity prices and throughput often from other producing fields. If this third party infrastructure is no longer economic to operate it may lead to cessation of production leaving its satellite fields stranded without an export route; this risk has manifested itself with the planned closure of the Theddlethorpe Gas Treatment facility in Q3 2018 which will lead to the cessation of production of the Schooner and Ketch fields.</p>	<p>Whilst the Group assesses the risk to infrastructure when it acquires new assets, such assessment is based on assumed economics and production profiles which are hard to predict in the medium to long term.</p>
Exploration risk	<p>Drilling exploration wells is speculative, may be unprofitable and may result in a total loss of investment. The Group may not identify sufficient quantities of commercially exploitable deposits or successfully drill, complete or develop oil or gas in sufficient quantities to be profitable or commercially viable. Statistically, a relatively small number of properties that are explored are ultimately developed into producing hydrocarbon fields.</p> <p>Moreover, the high cost of offshore development may render discoveries uneconomic other than those that are very large or those which can be readily tied back to existing infrastructure.</p>	<p>The Group seeks to drill multiple targets that carry a range of differing technical and commercial risks and focuses on near-field prospects.</p>
Competition risk and cost inflation	<p>There remains strong competition within the petroleum industry for the acquisition of good quality hydrocarbon assets. The Group competes with other oil and gas companies, many of which have greater financial resources than the Group, for the acquisition of such properties, licences and other interests as well as for the recruitment and retention of skilled personnel. The challenge to management is to secure assets and recruit and retain key staff without having to pay excessive premiums.</p> <p>In the current market many capital and operating costs, from site surveys through to decommissioning, have decreased. However, capacity and services have also reduced and if the recovery in hydrocarbon prices is sustained we can expect a return of cost inflation which can have a major impact on both the cash outlay and economic viability of a project.</p> <p>There is also continuing competition for access to pipelines and other infrastructure which may delay the development of a field and thereby its economic value.</p>	<p>In formulating bids to acquire assets, the Group utilises experienced senior professionals within the Group to ensure that any bids are submitted at a competitive price that reflects the potential risk asset value and can generate appropriate returns for the Group's shareholders. Prior to any asset being evaluated, senior management review the target to ensure it fits within the parameters set at the commencement of each year.</p>

Principal risks and uncertainties

continued

Area	Description	Mitigation
Risks relating to acquisitions	<p>Part of the Group's strategy includes increasing oil and gas reserves and/or production through strategic business acquisitions. Although the Group performs a review of the companies, businesses and properties it acquires (or intends to acquire) to standards consistent with industry practices, such reviews are inherently incomplete. It is often not feasible to review in-depth every individual component involved in each acquisition. The Group will commonly focus its due diligence efforts on higher value components or factors and will review lower value interests on a sample basis. However, even where in-depth due diligence reviews are conducted, these may not reveal existing or potential problems, nor may they permit the Group to become sufficiently familiar with the properties or assets to fully assess their potential or limitations and deficiencies. In addition, in order to establish a value and offer a price for an acquisition the Group will make certain technical and economic assumptions as regards the continuing performance of the asset and its associated liabilities, particularly as regards decommissioning and in the event that those assumptions are incorrect the Group risks overpaying for such acquisition which may have a material adverse effect on the business.</p> <p>Risks commonly associated with acquisitions of companies or businesses include the difficulty of integrating the operations and personnel of the acquired business, problems with minority shareholders in acquired companies, the potential disruption of the Group's own business, the possibility that indemnification agreements with the sellers may be unenforceable or insufficient to cover potential liabilities and difficulties arising out of integration, as well as operational risks relating to the assets acquired. Furthermore, the value of any business the Group acquires or invests in may be less than the amount it pays and there can be no assurance that any acquisition by the Group will be successful and add value for the Company's shareholders.</p>	In formulating bids to acquire assets, the Group utilises experienced senior professionals within the Group and external advisers to test the technical, cost and economic assumptions made.
Fiscal risks	<p>The Group enters into commitments assuming a relatively stable fiscal system and any material change represents a risk to the Group's ability to fund its projects.</p> <p>A complaint has been lodged with the EFTA Surveillance Authority alleging that the cash reimbursement of the tax value of exploration costs in Norway constitutes illegal state aid. The Norwegian Government has disputed this allegation as the measure should not be regarded as state aid, because it is a non-selective part of a neutral tax system which treats all comparable undertakings alike. However, in the event that the complaint was upheld, it is possible, albeit very unlikely, that the historic amounts reimbursed to the Group could be reclaimed.</p>	<p>The Group operates in jurisdictions with sophisticated tax authorities capable of assessing the adverse impact of any change in legislation before it is enacted.</p> <p>In the very unlikely event that the Group had to repay the monies reimbursed to the Group in Norway under the exploration tax rebate system, it is expected that by the time that such demand was made the Group would be in a tax paying position and could offset, at least partially, such liability.</p>
Cyber risks	The Group is at risk of financial loss, reputational damage and general disruption from a failure of its IT systems or an attack for the purposes of espionage, extortion or to cause embarrassment. Any failure of or attack against the Group's IT systems may be difficult to prevent or detect, and the Group's internal policies to mitigate these risks may be inadequate or ineffective. The Group may not be able to recover any losses that may arise from a failure or attack.	The Group has a fully staffed IT department which ensure that the Group's systems are protected in so far as is practicable but no system is infallible.
Dependence upon executive management and technical staff	The Group is dependent upon its executive management and technical staff. There is a risk that the unexpected loss of services of any such member of staff could have a material adverse effect on the Group. The Group does not have any key person insurance in place for management. Attracting and retaining additional skilled personnel may be required to ensure development of the Group's business. The Group faces significant competition for skilled key personnel in the oil and gas sector. There is no assurance that the Group will successfully attract new personnel or retain existing key personnel required to continue to develop its business and to execute and implement its business strategy.	In order to mitigate this risk the Group has to offer competitive remuneration and retention packages including bonus and long-term incentive plans to incentivise loyalty and good performance from the existing highly skilled workforce.
Negative stakeholder reactions to operations and the Group's strategy	The Group's operational activities and its reputation could be significantly impacted if relationships with its stakeholders are not effectively managed. The Group places a high priority on managing these relationships.	This risk is mitigated through proactive engagement with investors, regulators, governments, lenders and communities where the Group has its activities.

Risk appetite

Faroe's risk appetite, in line with its strategy, is to seek exposure to a wide range of projects across the upstream exploration, development and production sector and to spread its capital and resources in proportion to the likelihood and impact of the associated risk and reward. Whilst the Group seeks to avoid excessive risk

concentration in any one project or any one part of the upstream exploration and production sector, it is developing a hub strategy which by definition necessitates asset concentration risk. As the Group grows and develops multiple hubs, the concentration risk will diminish but in the short to medium term the Group's risk profile will be higher as a result of this

hub strategy. The Group has appetite for geological risk, both in its exploration drilling and in field development drilling, up to certain financial thresholds, and for economic risks as regards the performance of its producing assets. The Group does not have appetite for risks regarding solvency, health and safety, environmental and reputational matters.

Viability statement

In accordance with provision C.2.2 of the UK Corporate Governance Code, the Directors have assessed the viability of the Company over a longer period than the 12 months required for the 'Going Concern' statement on page 45 in the Directors' Report. In its assessment of viability, the Board has considered the principal risks faced by the Group, relevant financial projections and sensitivities and the availability of adequate funding.

The period covered in this assessment is three years to 31 December 2020. The Board considers three years to be an appropriate timespan to provide a sufficient and reliable statement of the viability of the Group as it covers the material development and exploration commitments falling within the next three years.

Review of principal risks

The Group's principal risks and uncertainties are set out in detail on pages 29 to 33, and the impact of these has been taken into account in the period under review. The Group takes mitigating actions when available and appropriate, such as hedging of commodity and foreign exchange exposure, insurance and divestment of assets.

Aside from operational risks, the Board considers that commodity price volatility, and in particular a sustained low oil price, material cost overruns or delays on the Company's development assets along with a sustained interruption in production, particularly on one of the Company's key production hubs, are most likely to have the greatest impact on the continued viability of the Group during the three year period.

The Group has an undrawn RBL facility of \$250 million as well as a \$100 million senior unsecured bond, both of which mature in 2023. The Group also has an Exploration Financing Facility which matures in December 2020 of 1.5 billion NOK. Using these facilities, the Group has sufficient liquidity to meet material development expenditures that have been committed to over the forthcoming three year period. Continued access to these facilities at these amounts is an essential assumption in making this viability statement.

The potential impact of each of the Group's other principal risks on the liquidity of the Group during the forecast period, should that risk arise in its unmitigated form, has been assessed. The Board has considered the risk mitigation strategy as set out for each of those risks and believes that the

mitigation strategies should be sufficient to reduce the impact of each risk such that other than in extreme form, such as an uninsured major event, it would be unlikely to jeopardise the Group's viability during the three year period.

Review of financial projections

The Board regularly reviews financial projections including scenario testing of the base case assumptions. The projections used in the assessment of the Group's viability to December 2020 are based on the Group's most recent business plan which includes life of field production and expenditure forecasts on an asset-by-asset basis along with management's best estimate of future commodity prices.

Conclusion

Based on the Group's projections, the assessment of principal risks and uncertainties, along with mitigating actions, and the availability of funding, the Directors have a reasonable expectation that the Group will be able to continue operations and meet its liabilities as they fall due for the next three years to December 2020.

The Strategic Report, as set out on pages 2 to 39, has been approved by the Board.

Graham Stewart
Chief Executive
19 March 2018



Corporate and social responsibility report

Faroe Petroleum is committed to high standards of health, safety and environmental performance across all aspects of its business activities.

Overview

The health and safety of people, the protection of the environment and compliance with all applicable legal and internal requirements, as well as industry best practice, are critical to the overall success of the Group. The Faroe Business Management System (BMS) provides both the framework and mechanism for setting, monitoring and measuring suitable health, safety and environmental objectives as well as ensuring their continual improvement.

Providing a safe working environment for all of our staff is a core value and business priority. Safe and sustainable performance is monitored and reported regularly to the Board of Directors, which ensures that the necessary resources are provided to support HSE activities.





The Business Management System

The BMS is consistent with the internationally recognised requirements for Quality, Health, Safety and Environmental management (e.g. ISO 9001, HS (G) 65, OHSAS 18001 and ISO 14001). The BMS has been successfully verified for compliance with the OSPAR Recommendation 2003/5 (based on ISO 14001:2015) for Environmental Management for over three years. The third party independent OSPAR audit covers the scope of our UK assets although the BMS is applied in the same way across all of our operations. For Norwegian operations, aspects of the BMS are audited regularly by licence partners as well as by the petroleum safety and environmental authorities. The BMS policies, processes and procedures are applied to all operated drilling and production activities, and are used in planning and decision-making throughout the project lifecycle from acquisition of licences through to decommissioning.

The BMS is based upon a goal setting philosophy rather than a regimented and prescriptive approach to operations and business activity. It sets broad HSE expectations and provides a management framework for achieving goals in a systematic way, but allows sufficient flexibility to achieve this in a manner which best suits the business. The structure of the BMS is shown in the figure to the below:



Corporate and social responsibility report

continued



Safety performance

Over the period there were no reported breaches by the Group's staff of the requirements set out in the Personnel Handbook or those laid out in our HSE policies. All required monitoring and measuring activities associated with HSE performance, including scheduled HSE audits, took place as planned in 2017.

The Petroleum Safety Authority (PSA) in Norway is a regulator whose role it is to supervise safety, emergency preparedness and the working environment in Norwegian petroleum activities. The PSA also establishes standards for the petroleum industry which involves developing regulations, controlling companies' compliance and taking enforcement action. One of its main priorities is to ensure that the managers of companies maintain a strong HSE culture for both operated and non-operated activities. The Group's Norwegian subsidiary was

successfully audited by the PSA in 2014, in 2016 through the process of transfer of operatorship of the operated assets Trym and Oselvar and as part of the consents to drill Brasse in 2016 and 2017. In the same period, the Norwegian Environmental Agency gave consent to discharge permits for Brasse drilling.

The majority of the Group's activities are undertaken by contractors and other licence operators, operating on Faroe's behalf. To ensure safe operations and to comply with the regulations, Faroe follows up on contractors and partners through our audit, review and verification activities. These activities are based on risk evaluations. Despite this, whilst drilling wells on the Tambar field (operated by Aker BP) an employee of Maersk Drilling died and another was injured in December 2017 as a result of an accident on the Maersk Interceptor.

The Group will continue its efforts in carrying out the required risk assessments as a basis for decision-making as we see this as the main tool in preventing severe incidents. In 2017, for operations where Faroe is the licence operator, we achieved our target of zero fatalities and zero Lost Time Injuries (LTIs) across all of our operations having worked a total of 202,348 man hours during 2016 and 175,759 offshore man hours in 2017 across our assets in the UK and Norway.



Faroe team participating in Holmenkollstafetten in May 2017.

Workforce health and wellbeing

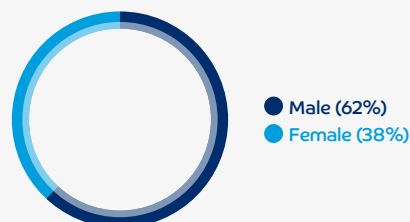
The Group is committed to providing a healthy and safe workplace. As part of this commitment, a Working Environment Committee was established in 2017 which meets quarterly to discuss the health, wellbeing and safety of the workforce.

The Group provides private medical cover for employees, which includes counselling for work/life issues such as stress and bereavement. The Group also provides pensions, insurance, income protection benefit and contributes towards gym memberships for employees.

Equal opportunities and discrimination

The Group is an equal opportunities employer and will recruit, employ and develop employees in line with best practice and based on the qualifications, experience and skills required for the work. Notwithstanding that the resources sector has historically been male dominated, at 31 December 2017, 38% of the Group's employees were female.

Gender diversity



2

Environment

As stated in the Group HSE Policy, Faroe is committed to respect and preserve the natural environment. Our policy is to minimise the undesirable effects on the environment resulting from our activities and work to prevent pollution. The Group assesses and manages the risks of its operations in order to improve its environmental performance on a continual basis.

Environmental management is an integral part of the BMS and includes the following activities: environmental permits, identification of main environmental aspects, chemical assessments and substitution plans, environmental reporting, environmental surveys/studies and assessments and oil spill preparedness plans.

Greenhouse gas (GHG) emissions

Faroe, as part of its annual HSE monitoring programme, reports the emissions of GHGs that have been generated as a result of its operated exploration and production activities. These GHG emissions are reported annually to the Norwegian Environment Agency and to BEIS (Department for Business, Energy & Industrial Strategy) in the UK.

The reported GHG emissions in carbon dioxide equivalent (CO₂e) includes emissions of carbon dioxide (CO₂), methane (CH₄) and nitrous oxide (N₂O), all of which are produced during combustion. 2016 forms the base year against which emissions trend over time.

Scope 1 GHG emissions includes subsea tie-backs in Norway, Trym and Oselvar (allocated emissions on host installations Ula and Harald to process Faroe's production), and Brasse exploration drilling including a well test. For the UK, the numbers include direct emissions from the Schooner and Ketch installations (normally not manned). The numbers provided in the table are the total emissions from these fields.

Scope 1 GHG emissions (tonnes)	2017	2016
Norway	54,867	71,044
UK	416	557

The total direct GHG emissions (operated and non-operated) during 2016 was 107,573 tonnes (net to Faroe).

Scope 2 GHG indirect emissions comprise those arising from generation of electricity supplied by the national grid and is hence limited to electricity used in the Faroe offices in Norway and the UK. For 2017 this equated to 79 tonnes of GHG.

Environmental releases

Faroe has a target of zero acute discharges to sea. Any spill, irrespective of size, is recorded and followed up internally and reported as required to authorities. Chemical spills above 0.1m³ in 2017 and 2016 were as follows:

Chemical spills > 0.1m ³	2017	2016
Norway	–	–
UK	–	1



ROV photo of the seabed in the Norwegian sea in a Faroe-operated area.

Corporate and social responsibility report

continued



Our ethics

The Chief Executive, together with the Board firmly believe that working with integrity and transparency are the core principles which underpin our behaviour in pursuing our strategic objectives. This is evidenced through the policies and procedures that are communicated to staff and contractors on a regular basis.

Working correctly

The Group strives to meet the highest standards of integrity and ethics as we undertake our daily activities. To ensure these values are core to the business, they are integrated within the Group's BMS through policies, procedures, project plans and further embedded with our staff and contractors through training and awareness initiatives. The key policies in place within the BMS for promoting ethical business conduct are:

- Business Ethics Policy;
- Personnel handbook (UK and Norway);
- Share-dealing Policy;
- Anti-facilitation of Tax Evasion Policy;
- Anti Bribery and Corruption Policy; and
- Whistle Blowing Policy.

All policies are reviewed and signed by the Chief Executive which further reinforces our ethos of conducting our business with integrity which is a core principle as we meet the requirements of our strategy. All these policies are available to our staff on the Group intranet and on annual reminder of their existence is circulated to all staff.

The Group operates in some of the most mature oil and gas jurisdictions in the world, the UK and Norway Continental Shelf (UKCS and NCS). This requires the Group to operate to very high regulatory standards for Environmental, Health and Safety legislation. Faroe prides itself on the pro-active and engaging relationships that it has with all stakeholders, in particular those with regulators to promote openness and transparency in all aspects of our operations.

The Group does not support political parties nor contribute to the funds of groups whose activities are calculated to promote partisan party interests.

Anti-bribery and corruption

A dedicated Anti Bribery and Corruption ('ABC') Policy is in place across the Group which expects the highest standard of behaviour and conduct of its Directors, officers and employees, together with all agents, co-ventures, contractors, suppliers and other third parties acting or purporting to act on its behalf or on behalf of any member of the Group. The ABC Policy sets out the main policies, procedures and mechanisms adopted by the Group following appropriate risk assessment that are intended to prevent and/or effectively combat instances of bribery or corruption in the course of the Group's business and ensure compliance with applicable anti-bribery and anti-corruption laws in those countries where the Group conducts business.

ABC performance in 2017

The ABC Policy in tandem with the Whistle Blowing Policy remained fit for purpose during our activities in 2017, but we commit to review and update them in 2018 in accordance with updates to guidance and legislation as well as to assure ourselves that what we have adopted is fit for our ever-evolving company.

Staff and contractors are reminded of the need to be familiar with these requirements, to ensure the high standards are adhered to.

Contractors working for Faroe are treated in the same way as if they were direct employees and must have a high level of business integrity and must commit to the principles of our Anti Bribery and Corruption Policy.

No reports were made under the ABC Policy in 2017 for those working for or on behalf of Faroe.

Operating transparently

The Group operates in such a way that it is easy for others to see what actions are performed as we undertake our business activities. This includes our internal stakeholders, employees, managers, the Board as well as our external stakeholders, which include our regulators, investors, suppliers and the wider community in which we work.

Employees are encouraged to air grievances in accordance with the Grievance Procedure within the employee handbook. No grievances were reported during our business activities in 2017.

The Board and management of the Group have a zero tolerance approach to modern slavery and are committed to ensuring that there is no modern slavery or human trafficking in any part of our business, including our supply chain.

In line with the requirements of the UK 2015 Modern Slavery Act, Faroe has been publishing on its website its annual statement detailing measures we have put in place to reduce the risk of modern slavery affecting our business and supply chain.

GHG emissions data for all of our operated assets are reported in accordance with the UK 2006 Companies Act. Details are provided in our Environment section on the previous page.

Maggie's Cancer Support Centre in Aberdeen is funded entirely by voluntary contributions from the local community.



4

Community

Faroe has a process for engaging with its varied stakeholders. Interested parties are assessed as to their requirements in relation to a project, after which they are engaged with according to their significance to the project.

The Group has strong relationships with academia and has invested in a variety of research and development activities within Universities in Norway with the aim to benefit the communities in which we operate. Faroe has also made donations to various charitable causes.

During 2016 and 2017, the Company committed significant amounts to support a number of geological and geophysical studies and projects at the University of Bergen and University of Stavanger. The Company also contributed to the student fund for masters students.

In 2014 and 2017 Faroe organised charity concerts called Rock'n'Oil. Over the two events a total of £90,000 was raised in aid of five charities: RNLI, Princes Trust, Maggie's, Place2Be and Momentum.

Faroe has also been one of the sponsors of the new Stavanger Konserthus which was opened in 2012. In 2017 Faroe was the main sponsor of the annual Stavanger Marathon and will also be the main sponsor in 2018.

Corporate governance introduction

The Group is committed to maintaining high standards of corporate governance to ensure that it is managed with openness, honesty and transparency.



John Bentley
Chairman

A handwritten signature in black ink, appearing to read 'John Bentley', with a stylized flourish at the end.

The Group's governance framework, which includes our Business Ethics Policy, is key to the way we work both internally and externally (the Group's Business Ethics Policy can be found on the website www.faroe-petroleum.com). The Board approves the Group's governance framework and the Audit Committee reviews its risk management and internal control processes.

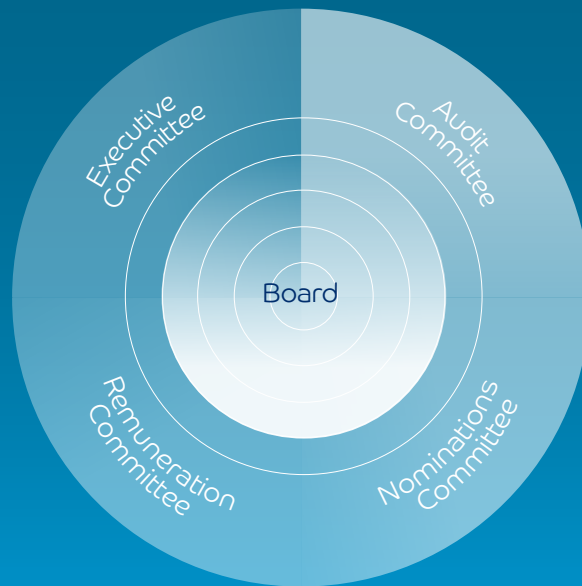
Whilst the Group is not bound to comply with the September 2014 edition of The UK Corporate Governance Code (the 'Code') or Schedule 8 of The Large and Medium-sized Companies and Groups (Accounts

and Reports) (Amendment) Regulations 2013 (the 'Regulations'), in relation to Directors' remuneration, the Group has elected to comply with the Code and the main principles of the Regulations.

The Group's commitment to strong corporate governance and risk management will remain central to the business during 2018 and on.

Our governance structure

The Group's governance structure with the Board and four Committees is designed to maintain the highest standards of personal and professional conduct throughout the organisation. The structure is in line with best practice and with the principles of the UK Corporate Governance Code.



Board diversity

Faroe Petroleum is an equal opportunities employer and we recognise that Directors and managers with diverse backgrounds, capabilities and experience gained from different sectors enhance the Group and strengthen governance.



Board gender

- Male (7)
- Female (1)



Board nationality

- British (6)
- Norwegian (2)



Board experience

- Oil and gas and Technical
- Financial
- Natural resources

Board of Directors

- Audit Committee
- Nominations Committee
- Remuneration Committee

John Bentley, 69
**Non-Executive
Chairman**

Year appointed
2007

Main Board meetings attended¹
8

Independent
Yes

Committee membership
○○○



John Bentley has over 40 years' experience in the natural resources sector. He served in a number of senior management positions in the Gencor Group in South Africa, the USA, UK and Brazil. In 1996 he was instrumental in floating Energy Africa Ltd on the Johannesburg stock exchange and was Chief Executive for the following five years. More recently he has served on the Board of Caracal Energy Inc and currently serves on the boards of Wentworth Resources Ltd, Africa Energy Corporation and Phoenix Global Resources. John, who holds a degree in Metallurgy from Brunel University, was appointed to the Board in September 2007.

Graham Stewart, 57
Chief Executive

Year appointed
2002

Main Board meetings attended¹
8

Independent
Executive Committee

Committee membership
○



Graham was instrumental in founding the Company in 1998, where he has been Chief Executive since December 2002. He holds an honours degree in Offshore Engineering from Heriot-Watt University and an MBA from Edinburgh University and has over 20 years' experience in oil and gas technical and commercial affairs. He was previously Finance and Commercial Director at Dana Petroleum and Commercial Director of the Petroleum Science and Technology Institute. Graham also serves on the board of Alopex Gold as a non-executive director.

Jonathan Cooper, 49
Chief Financial Officer

Year appointed
2013

Main Board meetings attended¹
7

Independent
Executive Committee

Committee membership
○



Jon is a chartered accountant by training having qualified with KPMG before joining Dresdner Kleinwort Benson (later Wasserstein) in their Oil & Gas Corporate Finance and Advisory Team. Jon is a Fellow of the ICAEW and also has a PhD in Mechanical Engineering from the University of Leeds. In 2006 he was appointed as an Executive Director of Gulf Keystone Petroleum, followed by Sterling Energy plc in 2008, where he was Finance Director. He subsequently joined Lamprell plc as Chief Financial Officer in 2011. Jon was appointed to the Board of Directors in July 2013.

Helge Hammer, 56
Chief Operating Officer

Year appointed
2006

Main Board meetings attended¹
7

Independent
Executive Committee

Committee membership
○



Helge joined the Company in 2006, where he is Chief Operating Officer. Prior to joining Faroe Petroleum he was Asset Manager and deputy Managing Director at Paladin Resources. He holds a degree in Petroleum Engineering from NTH University of Trondheim and in Economics from Institut Francais du Petrole in Paris. In addition, he worked for Shell for 13 years as a Reservoir Engineer, Team Leader and Business Manager in Norway, Oman, Australia and The Netherlands.

¹ Excludes procedural meetings called for the specific approval of transactions or matters that have the prior general approval of the full Board and are attended by a Committee of Executive Directors.

Timothy Read, 71 Senior Independent Non-Executive Director

Year appointed
2009

Main Board meetings attended¹
8

Independent
Yes

Committee membership
○ ○ ○



Tim was appointed to the Board as Non-Executive Director in March 2009. He has over 40 years' experience in the natural resource sector as an investment analyst, investment banker and corporate executive and director. He has extensive experience of all aspects of corporate finance, particularly M&A and equity markets. Between 1999 and 2006 he was the Chief Executive of Adastral Minerals Inc, and since then has acted as Non-Executive Director for several natural resource companies, including Cumerio SA (acquired in 2008) and Nevoro Inc (acquired in 2009). Tim, who is currently a Director of Lydian International, has a BA (Economics) from the University of Strathclyde in Glasgow and was made a Fellow of the Chartered Institute for Securities and Investment in 2000.

Roger Witts, 71 Independent Non-Executive Director

Year appointed
2007

Main Board meetings attended¹
8

Independent
Yes

Committee membership
○ ○ ○



Roger has over 40 years' experience in the oil and gas industry. Whilst he has broad senior management experience in the upstream industry, he has specific expertise in financial and tax planning, economic appraisal, debt finance and risk management. Roger qualified as a Chartered Accountant in 1970 with Coopers & Lybrand and then moved to The British Land Company in 1972 as financial controller of two quoted subsidiaries. His oil industry experience started with Petrofina in 1976 where he held a number of senior positions including Managing Director of a combustion engineering subsidiary and Finance Director of Fina Exploration Company. He was Finance Director of Thomson North Sea from 1984 to 1989 and of Seaford Resources from 1990 to 1997. Roger was appointed to the Board in May 2007 as part time Finance Director and became a Non-Executive Director in May 2009.

Jorunn Sætre, 61 Independent Non-Executive Director

Year appointed
2014

Main Board meetings attended¹
8

Independent
Yes

Committee membership
○ ○ ○



Jorunn was appointed to the Board as an Independent Non-Executive Director in September 2014.

She is a chemical engineer by background who progressed to senior positions with Halliburton in Norway, Europe and the USA over a 30 year period. Her roles included serving as Director of Halliburton's European Research Centre, Head of Halliburton's overall Scandinavian operations and responsibility for global Production Enhancement activities. In addition she worked for AGR as manager for business development, rig team and head of the Stavanger office until the end of 2017. In 2008, Jorunn was the first to be awarded the title of "Oil Woman of the Year" by the Stavanger Society of Petroleum Engineers. Jorunn is currently a member of the corporate assembly of Hydro ASA and a non-executive director of Oslo Bergen Trondheim Stavanger Idag.

Brent Cheshire, 62 Independent Non-Executive Director

Year appointed
2017

Main Board meetings attended¹
2

Independent
Yes

Committee membership
○ ○ ○



Brent commenced his career with Shell as a geologist in its exploration and production division, eventually spending 14 years with the Group. In 1991, he joined Amerada Hess, holding a number of senior positions, latterly as Senior Vice President for E&P Worldwide Technology, where he was responsible for all global technical activities. In 2004, he became DONG Energy's first UK employee, as managing director of its UK E&P business. Over the next 13 years, eventually becoming managing director of DONG Wind Power and Chairman of its entire UK operations; he developed the business into one of the largest acreage holders West of Shetland and the leading offshore wind developer in the UK. Brent was appointed to the Board in October 2017.

Directors' report

Performance of the business and future developments

The information of the performance of the business and future developments can be found in the Strategic Report.

Dividends

The Directors do not recommend the payment of a dividend for the year.

Future developments

Please refer to the Strategic Report for disclosure around future developments of the Group on pages 8 to 9.

Directors

The names and biographies of the Directors during the year are disclosed on pages 42 to 43.

Events since the balance sheet date

Details of significant post balance sheet events are set out in Note 31 in the Group financial statements.

Share capital and share options

Details of the share capital of the Company and options over shares of the Company are set out in Note 24 to the Group financial statements. Over the period the Company had three share incentive schemes by which Directors and employees may: (i) be granted options under a long-term incentive scheme to subscribe for nil cost shares in the Company; (ii) be issued shares under a co-investment plan; and (iii) be issued shares under a share incentive plan. The maximum aggregate number of new shares which may be issued in respect of these schemes is currently limited to 15% of the issued share capital. However, grants will be made each year on the basis that ordinarily expected vesting should not exceed 10% of the Company's issued Ordinary Share capital.

Composition of Group

Details concerning the subsidiary undertakings are given in Note 17 to the Group financial statements.

Substantial shareholdings

The Company has analysed its share register at 9 March 2018, the results of which indicate the following shareholders held 3% or more in the issued share capital of the Company:

Shareholder	Ordinary Shares	%
Delek Group	56,355,825	15.37
BlackRock	32,863,397	8.96
Aviva Investors	24,087,731	6.57
JPMorgan Asset Management	18,992,989	5.18
Invesco Perpetual	14,909,383	4.07
Legal & General Investment Management	11,841,374	3.23
AXA Framlington Investment Managers	11,316,338	3.09
Tjaldur	11,029,340	3.01

Directors' interests in share capital

The Directors' interests in the share capital of the Company at 8 March 2018 were as follows:

	8 March 2018		31 December 2017	
	Ordinary Shares	Options and Matching Shares	Ordinary Shares	Options and Matching Shares
John W S Bentley	172,270	–	172,270	–
Graham D Stewart	1,721,521	6,028,358	1,719,930	6,293,334
Helge A Hammer	813,956	3,736,317	812,548	3,925,885
Jonathan R Cooper	264,663	3,310,107	263,072	3,453,404
Brent Cheshire	–	–	–	–
Timothy P Read	160,000	–	160,000	–
Roger C Witts	109,180	–	109,180	–
Jorunn J Sætre	28,571	–	28,571	–

Health, safety, the environment and the community

The Group has a formal Health, Safety and Environmental Policy which requires all operations within the Group to pursue economic development whilst protecting the environment. The Directors aim not to damage the environment of the areas in which the Group operates, to meet all relevant regulatory and legislative requirements and to apply responsible standards of its own where relevant laws and regulations do not exist.

It is the policy of the Group to consider the health and welfare of employees by maintaining a safe place and system of work as required by legislation in each of the countries where the Group operates.

Auditors and their independence

A resolution to appoint auditors for the year to 31 December 2018 as approved by the Audit Committee will be proposed at the Annual General Meeting. The Company has a policy for approval of non-audit services by the auditor, to preserve independence.

Disclosure of information to auditors

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware; and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Going concern

The Group's business activities, together with the factors likely to affect the future development, performance and position, are set out in the Strategic Report. The financial position of the Group, its cash flows and liquidity position and borrowing facilities are described in the Financial Review section in the Strategic Report and in Note 22. Further information on the Group's exposure to financial risks and the management thereof is provided in Note 25.

The Board's review of the accounts, budgets and financial plan lead the Directors to believe that the Group has sufficient resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on a going concern basis.

Treasury & Risk Management Policy

The objective of the Group's Treasury and Risk Management Policy is to manage the Group's financial risks and to minimise the adverse effects of fluctuations in the financial markets on the value of the Group's financial assets and liabilities, on reported profitability and on the cash flows of the Group. Note 25 sets out the particular risks to which the Group is exposed, and how these are managed.

Directors' liabilities

The Company has granted indemnities to the Directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 2006. Such qualifying third party indemnity provision remains in force as at the date of approving the Directors' Report.

Interests in contracts

There have been no contracts or arrangements during the financial year in which a Director of the Company was materially interested and which were significant in relation to the Group's business.

Political donations

The Group made no political donations during the year ended 31 December 2017.

Graham Stewart
Chief Executive

19 March 2018



Board of Directors and Committees



John Bentley

Non-Executive Chairman

(A)(N)(R)(E)

Jonathan Cooper

Chief Financial Officer

(A)(N)(R)(E)

Tim Read

Senior Independent
Non-Executive Director

(A)(N)(R)(E)

(A) Audit Committee
(N) Nominations Committee
(R) Remuneration Committee
(E) Executive Committee

Jorunn Sætre

Non-Executive Director

(A)(N)(R)(E)

Graham Stewart

Chief Executive

(A)(N)(R)(E)

Helge Hammer

Chief Operating Officer

(A)(N)(R)(E)

Roger Witts FCA

Independent Non-Executive Director

(A)(N)(R)(E)

Brent Cheshire

Independent Non-Executive Director

(A)(N)(R)(E)

Statement of Directors' responsibilities

in respect of the financial statements

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and regulations. Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors are required to prepare financial statements under IFRSs as adopted by the European Union.

Under Company Law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group and Company for that period.

In preparing those financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether the Group and Company's financial statements have been prepared in accordance with IFRS as adopted by the European Union;
- make judgements and estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Directors' statement under the UK Corporate Governance Code

The Directors consider the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group and Company's performance, business model and strategy.

Graham Stewart
Chief Executive

19 March 2018



Corporate governance report

Corporate governance and the UK Corporate Governance Code

The Directors support high standards of corporate governance and whilst the Company is not required to comply with the Code, it has nevertheless elected to comply with it, and the Board considers that the Company has been in compliance throughout the period.

The Board is responsible for establishing and maintaining the system of internal controls which has been in place throughout 2017 and up to the date of approval of the Annual Report and Accounts. The responsibility for reviewing the effectiveness of the Group's internal controls and risk management systems on an ongoing basis is divided between the Audit Committee and the Board, as described below. The Directors confirm they continue to perform a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. The procedures performed are disclosed in the Audit Committee Report.

The workings of the Board and its Committees

The Board

At 31 December 2017 the Board included five Non-Executive Directors, one of whom is the Chairman, and three Executive Directors. The Board is responsible to the shareholders for the proper management of the Group. It meets regularly, as set down in the table on page 48, to review trading performance, set and monitor strategy, examine acquisition and divestment possibilities, approve major capital expenditure projects, monitor changes to the business environment and the risks the Group faces and other significant financing matters and report to shareholders. The Board delegates authority to the management for the day-to-day business under a set of delegated authorities which cover: routine operational matters, purchasing procedures, financial authority limits, contract approval procedures and the hiring of full time and temporary staff and consultants. Matters reserved for the Board

are communicated in advance of formal meetings. All of the Directors are subject to election by shareholders at the first Annual General Meeting of shareholders ('AGM') after their appointment to the Board and to re-election by shareholders at least once every three years. In addition, as required under the Code, any Non-Executive Director who has served on the Board in that capacity for more than nine years will be subject to annual re-election. Accordingly, Roger Witts and John Bentley who were appointed to the Board in June and September 2007 respectively will stand for re-election at the forthcoming AGM and at each AGM thereafter. Mr Read has served on the Board as a Non-Executive Director since March 2009 and will not be seeking re-election at the forthcoming AGM.

At the year end the Board comprised five independent Non-Executive Directors: John Bentley, Tim Read (Senior Independent Director), Brent Cheshire, Jorunn Sætre and Roger Witts. Mr Witts was an Executive Director of the Company until May 2009 and, as such, a period of more than the five years has passed as set down by the Code as a measure of independence. Ms Sætre is currently the Rig Team Leader and manager of the Stavanger office of the engineering support group AGR which in 2017 provided engineering services of a value of approximately £198,000 to the Group. The Board has nevertheless evaluated Mr Witts' and Ms Sætre's judgement, character and performance, and continues to be satisfied that they act as independent Directors and in the best interests of the Company and its shareholders and so continues to deem them to be independent.

Mr Cheshire was co-opted to the Board on 25 October 2017 and will stand for re-election at the forthcoming AGM, and will take over from Tim Read as Senior Independent Director on 1 April 2018 and will become Chairman of the Remuneration Committee following the 2018 Annual General Meeting.

The Chairman and Non-Executive Directors have other third party commitments including Directorships of other companies as disclosed in the Directors' biographies. The Company is satisfied that these associated commitments have no measurable impact on their ability to discharge their responsibilities effectively.

New Directors receive an induction on their appointment to the Board which covers the activities of the Group and its key business and financial risks, the Terms of Reference of the Board, and its Committees, and the latest financial information about the Group.

All Directors have access to the advice and services of the Company Secretary who is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with. In addition, the Company Secretary will ensure that the Directors receive appropriate training as necessary. The appointment and removal of the Company Secretary is a matter for the Board as a whole. All Directors are supplied with information in a timely manner in a form, and of a quality, appropriate to enable them to discharge their duties.

Corporate governance report

continued

Board performance

In accordance with Code provisions, the Company has a formal process of annual performance evaluation for the Board, its Committees and individual Directors. The performance evaluation of the Board and the Board Committees is primarily based upon answers to a detailed questionnaire. The areas covered in the questionnaire include the effectiveness of the Board and its Committees, performance against objectives, preparation for and performance at meetings and corporate governance matters.

Once a questionnaire has been completed by each member of the Board, the Chairman then reports the results of the process to the Board. The Board and its Committees are satisfied that they are operating effectively.

A performance evaluation of the Board, the Board Committees and individual Directors will continue to be conducted annually and the method for such review will continue to be reviewed by the Board in order to optimise the process.

The performance of the Executive Directors is reviewed by the Remuneration Committee and the bonuses payable to the Executive Directors are linked directly to the results of these reviews.

The Company has Directors' and Officers' liability insurance in place.

The following is a table of Board and Committee meetings during the year:

	Board meetings ¹	Nominations Committee	Audit Committee	Remuneration Committee
Meetings held during 2017	8	4	2	6
Attendance				
Executive Directors				
Graham D Stewart	8	2	–	–
Jonathan R Cooper	7	–	–	–
Helge A Hammer	7	–	–	–
Non-Executive Directors				
John W S Bentley	8	4	2	6
Brent Cheshire ²	2	–	–	–
Timothy P Read	8	4	2	6
Jorunn Sætre	8	4	2	6
Roger C Witts	8	4	2	6

¹ Excludes procedural meetings called for the specific approval of transactions or matters that have the prior general approval of the full Board and are attended by a Committee of Directors.

² Appointed to the Board on 25 October 2017 and to the Committees on 14 December 2017.

During 2017, certain Directors who were not Committee members attended meetings of the Audit Committee, Remuneration Committee and Nominations Committee by invitation. These details have not been included in the table. Where a Director is unable to attend meetings of the Board or of Board Committees, such Director is invited to review the relevant papers for the meetings and provide his or her comments to the Board or the Board Committees in advance of such meetings.

The following Committees deal with specified aspects of the Group's affairs.

Audit Committee

The make-up and workings of the Audit Committee are set out in the separate Audit Committee Report.

Remuneration Committee

The make-up and workings of the Remuneration Committee, together with details of the Directors' remuneration, interest in options and service contracts, are set out in the Report on Directors' Remuneration. No Director is involved in the decision of his or her own remuneration.

Nominations Committee

The Nominations Committee comprises John Bentley (Committee Chairman), Brent Cheshire (appointed 14 December 2017), Tim Read, Jorunn Sætre, Roger Witts and Graham Stewart. The Nominations Committee, which has Terms of Reference agreed by the Board and available on the Company's website, will meet as and when required to:

- consider, at the request of the Board, the making of any appointment or reappointment, to the Board; and
- provide advice and recommendations to the Board on any such appointment or re-appointment.

The Nominations Committee does use the services of independent consultants from time to time to assist in the identification of candidates for Non-Executive Directors and/or to benchmark candidates already identified by the Committee against possible candidates identified by consultants.

The Company is mindful of the guidance contained within the Code regarding progressive refreshment of the Board. A number of the Non-Executive Directors have been with the Company for in excess of six years and are approaching retirement in the normal course. After nine years as an Independent Non-Executive Director, Mr Read will be stepping down from the Board after the forthcoming AGM and during the period, the Committee resolved to appoint Brent Cheshire as a replacement Independent Non-Executive Director and this process will be repeated with the selection and appointment of further Independent Non-Executive Directors in due course.

The Company's policy is to attract and develop a highly qualified and diverse workforce, to ensure that all selection decisions are based on merit and that all recruitment activities are fair and non-discriminatory. We continue to focus on encouraging diversity of business skills and experience, recognising that Directors and managers with diverse skills sets, capabilities and experience gained from different backgrounds enhance the Group. Notwithstanding that the resources sector has historically been male dominated, at 31 December 2017, 38% of the Group's employees were female.

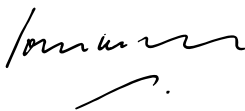
Relations with shareholders

Communication with shareholders is given high priority by the Board and is undertaken through press releases, general presentations at the time of the release of the annual and interim results and face-to-face meetings. The Group issues its results promptly to individual shareholders and also publishes the same on the Company's website (www.faroe-petroleum.com). Regular updates to record news in relation to the Company and operational reports are also published on the website.

In order to ensure that the members of the Board develop an understanding of the views and concerns of major shareholders there is regular dialogue with institutional shareholders including meetings after the announcement of the Company's annual and interim results. In addition, the Chairman and/or the Senior Independent Non-Executive Director ('SID') have held face-to-face meetings or spoken on the telephone with a number of the Company's major shareholders on a range of matters including strategy, executive remuneration, long-term incentive schemes and corporate governance issues. The SID is available to attend meetings with major shareholders without the Executive Directors present, if requested by shareholders. The Board uses the Annual General Meeting to communicate with private and institutional investors and welcomes their participation.

Signed on behalf of the Board by:

John Bentley
Non-executive Chairman
19 March 2018



Directors' Remuneration Committee report

Name	Meetings attended
Timothy P Read	6
John W S Bentley	6
Brent Cheshire	–
Jorunn Sætre	6
Roger C Witts	6



Introduction

The Directors' Remuneration Report for the year ended 31 December 2017 has been prepared by the Remuneration Committee and approved by the Board. The Committee is committed to transparent and quality disclosure, although does not fully comply with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations, due to being an AIM quoted Company.

Our report for 2017 covers the following matters:

- the Company's intended Executive remuneration policy for 2018 and beyond (the Directors' Remuneration Policy Report); and
- how the policy has been implemented in the year ended 31 December 2017 (the Annual Remuneration Report).

In recent months, the Committee reviewed the policy to ensure the senior executive remuneration package continues to reinforce appropriate behaviours and take account of trends in remuneration practices and shareholder guidelines. As a result, various changes have been made to the policy for 2018, including the following:

- Bonus deferral simplification – historically between 20% and 50% was deferred into shares; for 2018, any bonus in excess of 75% of salary shall be deferred for a minimum of one year
- Maximum bonus opportunity increase – this has been increased from 100% to 125% of salary with the intention that the enhanced opportunity will be linked to exceptional performance
- Minimum shareholding increase – currently 100% of salary, the minimum shareholding required for Executive Directors shall increase to 150% of salary by the end of 2019 and to 200% by the end of 2021.

No other changes to the policy have been made. The 2018 Remuneration Policy, and 2017 Remuneration Report, will be put to shareholders for an advisory vote at the 2018 AGM.

Performance of the Company in 2017

2017 has been another very good year for the Company with operational performance enhancing a general recovery in commodity prices and market sentiment. The Company has delivered across its business and some of the key achievements can be summarised as follows:

- Farming down the Company's interest in the Fenja development as part of the continuing portfolio management programme (announced in February 2018 and due to complete in H1 2018);
- Appraisal success increasing the resource base of Company's operated Brasse discovery and converting the resource to reserves to more than replace the Fenja reserves divested;

- Production average of approximately 14,300 boepd at the upper end of the original guidance range of 12,000-15,000 boepd; and
- Successfully raised \$100m through the issue of a bond to ensure the Company is financed through its committed projects.

Key decisions and pay outcomes in 2017

- Effective 1 January 2018 base salaries for the Directors have been increased by 10% following an extended period during which salaries were frozen (since 1 January 2015). The Committee recognises that the increases are above those normally expected but believes they are warranted by the strong performance of the Company over 2017.
- Annual bonuses are based on a scorecard of key performance indicators including corporate, operational (including HSE and growth in reserves and resources), financial and executive team performance measures. The scorecard outcome for 2017 reflected the Company's strong operating performance over the year and the Committee determined that an overall bonus payment of 75% of salary be awarded to the Executive Directors of which 20% was deferred.
- In June 2017, 53.5% of the 2014 award made to the Executive Directors vested under the Faroe Petroleum Incentive Plan (FPIP) following application of the three year performance test, with such shares being subject to a further two year holding period.
- In January 2018, 67% of the 2015 CIP awards made to the Executive Directors met the three year absolute TSR performance test.
- Awards were granted in 2017 under the 2016 Faroe Petroleum Co-Investment Plan (CIP) and under the 2016 Faroe Petroleum Incentive Plan (FPIP).

Shareholder feedback

The Board is committed to maintaining an open and transparent dialogue with shareholders. The objective of this report is to communicate clearly how much the Executive Directors are earning and how this is strongly linked to performance. In the first part of 2017, we consulted shareholders on proposed minor revisions to the CIP and FPIP concerning the termination of participants' employment as well as increasing the limit on fees payable to the Non-Executive Directors. We are pleased to report that at the 2017 Annual General Meeting, shareholders approved the amendments to the CIP and FPIP as well as the increase in the fee limit payable to the Non-Executive Directors.

Finally, this is my last report to you as Chair of the Remuneration Committee. I have happily served nine years on the Faroe Board and, now I am 71, I have decided to retire. Over these years, I have witnessed the Company's substantial growth in assets and production driven by its management and staff. It has also been a period of enormous change in the standards of reportage and the levels of transparency expected by the shareholders with respect to executive remuneration. Faroe has consistently tried to meet these proper expectations and I know that my successor Brent Cheshire will ensure that these efforts will continue undiminished.

Tim Read
**Remuneration
 Committee Chairman**
 19 March 2018



Directors' remuneration policy

The Remuneration Committee has established the policy on the remuneration of the Executive Directors and the Chairman and the Board has established a policy on the remuneration of the other Non-Executive Directors. The Policy will be put to shareholders for an advisory vote at the 2018 AGM, from which date it will become effective.

What is our remuneration policy?

Executive Directors

The policy on Directors' remuneration is that the overall remuneration package should be sufficiently competitive to attract and retain individuals of a quality capable of achieving the Company's objectives. The objective, if merited by performance, is for overall remuneration including salary, benefits, bonus and long-term incentives to be at or near the upper quartile for companies considered by the Committee to be comparable to Faroe. Remuneration policy is designed such that individuals are remunerated on a basis that is appropriate to their position, experience and value to the Company.

The main components of the remuneration policy and how they are linked to and support the Company's business strategy are summarised below:

Objective and link to strategy	Operation	Maximum opportunity	Performance assessment
Base salary			
Core element of remuneration, set at a level which is sufficiently competitive to recruit and retain individuals of the appropriate calibre and experience.	<p>Salaries are normally reviewed annually, and any changes are effective from 1 January each year.</p> <p>When determining salaries for the Executives the Committee takes into consideration:</p> <ul style="list-style-type: none"> – Company performance; – the performance of the individual Executive Director; – the individual Executive Director's experience and responsibilities; – pay and conditions throughout the Company. <p>Salaries together with other fixed benefits including pension are benchmarked periodically against comparable roles at companies of a similar size, complexity and in the Exploration & Production sector the objective is for total fixed remuneration to be in line with the median peer group.</p>	<p>When determining salary increases of the Executive Directors, the Committee takes into account the employment conditions and salary increases awarded to employees throughout the Company.</p> <p>Any salary increases in future years will be determined by the Committee.</p> <p>There is no maximum salary opportunity.</p>	Salary increases will be determined in accordance with the rationale set out under Operation (see Column 2).
Other benefits			
Support individuals in carrying out their roles.	<p>Reviewed periodically to ensure benefits remain market competitive.</p> <p>Benefits typically comprise life assurance cover, private healthcare arrangements and permanent health insurance and in Norway cash allowances in lieu of company car.</p>	Benefit values vary year on year depending on premiums and the maximum potential value is the cost of the provision of these benefits.	Not applicable.

Objective and link to strategy	Operation	Maximum opportunity	Performance assessment
Annual bonus			
Incentivises the achievement of a range of short-term performance targets that are key to the success of the Company.	<p>Executive Directors participate in an annual performance related bonus scheme.</p> <p>Bonus scheme awards are awarded annually at the year end.</p> <p>Performance period is one financial year with pay-out determined by the Committee following the year end.</p> <p>Any bonus in excess of 75% of salary will be deferred into shares for a minimum of one year.</p>	<p>Maximum bonus potential: 125% of salary.</p> <p>At threshold performance 20% of salary can be earned.</p> <p>There is no contractual obligation to pay bonuses.</p>	<p>A performance scorecard is used as a guide for the Committee, which reserves the right to override the formulaic outturn based on a broader assessment of overall Company performance.</p> <p>Performance targets are based on a range of corporate, operational, financial and executive team performance measures.</p> <p>The precise allocation between measures (as well as the weightings within these measures) will be determined by the Committee at the start of each year.</p>
Long-term incentives			
Incentivises the achievement of long-term financial performance and sustainable returns to shareholders in a way that aligns the interests of Executives and shareholders.	<p>Faroe Petroleum Co-Investment Plan (CIP):</p> <p>Under the CIP key employees can purchase shares in the Company (Investment Shares) using bonus deferral or other funds.</p> <p>Investment Shares will be matched (Matching Shares) by the Company provided participants still hold the shares and meet other certain performance criteria at the end of a three year period.</p>	<p>Employees can invest up to 100% of earned bonus in any financial year to purchase Investment Shares.</p> <p>The maximum match is 1:1 (i.e. one share for every Investment Share) (on a grossed up basis).</p> <p>At threshold performance 20% of the maximum match will be released.</p>	<p>The vesting of Matching Shares will be subject to continued employment with the Company, satisfaction of the performance targets and any other terms or conditions determined at the grant stage.</p> <p>Performance will be measured at the end of a three year performance period against absolute Total Shareholder Return ("TSR") targets and a relative TSR underpin.</p>
	<p>Faroe Petroleum Incentive Plan (FPIP):</p> <p>Under the FPIP (first approved by shareholders in 2013), the Committee may award annual grants of Nil-Cost Options, Conditional Share Awards or Phantom Shares.</p>	<p>On the grant of annual awards, the Committee will determine the maximum face value of the awards that can be granted to a participant in any calendar year.</p> <p>The maximum face value of the annual awards that can be granted is 250% of salary.</p> <p>At threshold performance 20% of an award will be released.</p>	<p>The vesting of awards will be subject to continued employment with the Company, satisfaction of the performance targets and any other terms or conditions determined at the grant stage.</p> <p>Performance will be measured at the end of a three year performance period against conditions which will include absolute TSR, relative TSR and possibly other measures that the Remuneration Committee considers appropriate. TSR measures have been selected as a transparent assessment of the successful execution of the business strategy and which capture the return delivered to shareholders.</p> <p>Any vested awards granted to the Executive Directors and senior executives will be required to be held for an additional two year holding period after the three year vesting period. Awards may be exercised during the holding period so long as the resultant shares are then held for such period (other than those which may be sold to meet any associated tax liabilities).</p> <p>The Committee may, at the time of vesting or at any time before, reduce the vesting level of awards in special circumstances and general malus principles will be applicable upon the discovery of deficient performance.</p>
	<p>Faroe Petroleum Share Incentive Plan (SIP):</p> <p>Employees can invest annually in shares of the Company and receive a match for every share purchased.</p> <p>This is a HMRC all employee approved plan.</p>	<p>Employees can invest up to an annual maximum of £1,500.</p> <p>The maximum match will be 2:1 (i.e. two shares for every Investment Share).</p>	<p>The vesting of Matching Shares will be subject to continued employment with the Company and any other terms or conditions determined at the grant stage at the end of a three year period.</p>

Directors' remuneration policy

continued

Objective and link to strategy	Operation	Maximum opportunity	Performance assessment
Pension			
To provide competitive levels of retirement benefit.	<p>In the UK the Company does not operate a pension scheme, but does, at the Directors' option, contribute to the personal pension plans of each Executive Director, or pays cash in lieu of such contributions.</p> <p>In the UK, where such contributions reach the maximum Annual Allowance or an Executive Director has accumulated an amount equivalent to the Lifetime Allowance, such excess contributions are paid as cash.</p> <p>In Norway, employees including Helge Hammer participate solely in a defined contribution scheme.</p>	<p>UK Executive Directors receive a contribution to a personal pension scheme or cash allowance in lieu of pension benefits up to 20% of salary.</p> <p>In Norway the Company contributes to a pension plan on behalf of the Norwegian Executive Director as follows:</p> <ul style="list-style-type: none"> – up to 25.1% of base salary up to approximately £101,500 (approximately NOK 1.1 million), which is paid into a defined contribution scheme; – 10% of base salary above approximately £101,500 (approximately NOK 1.1 million) which is used on personal pension schemes; and; – a further 10% of base salary above approximately £143,500 (approximately NOK 1.6 million) which is also used on personal pension schemes. <p>Defined contributions above the limit of NOK 1.1 million (as set for 2017) are a taxable benefit to the employee, and the Company meets the associated taxation on behalf of the Executive Director.</p>	Not applicable.
Shareholding requirement			
To align Executive Directors' interests with those of shareholders through build-up and retention of a personal shareholding.	<p>Executive Directors have five years to accumulate the required shareholding.</p> <p>Shares held that are no longer subject to performance conditions will count towards the requirement.</p>	Executive Directors are required to hold shares with a value equivalent to one times base salary, increasing to 150% of salary on 31 December 2019 and to 200% of salary by 31 December 2021.	Not applicable.

Non-Executive Directors

The table below sets out the key elements of the policy for Non-Executive Directors:

Objective and link to strategy	Operation	Maximum opportunity	Performance assessment
Fees			
Core element of remuneration, set at a level sufficient to attract individuals with appropriate knowledge and experience.	<p>Fee levels reflect market conditions and are sufficient to attract individuals with appropriate knowledge and experience.</p> <p>NEDs are paid a base fee and additional fees for Chairmanship of Committees.</p> <p>Fees may also be paid for additional time spent on the Company's business outside normal duties.</p> <p>Fees are reviewed annually with changes effective from 1 January each year.</p>	<p>Whilst there is no maximum individual fee level, fees are set at a level which is considered appropriate to attract and retain the calibre of individual required by the Company. However, the Company avoids paying more than necessary for this purpose.</p> <p>Fee increases may be made in line with market movements and to take into account the time commitment and duties involved.</p> <p>Non-Executive Directors do not participate in any variable remuneration elements or any other benefits arrangements.</p>	Fees will be determined in accordance with the rationale set out under Operation.

New appointments

The same principles as described above will be applied in setting the remuneration of a new Non-Executive Director. Remuneration will comprise fees only, to be paid at the prevailing rates of the Company's existing Non-Executive Directors.

Remuneration policy for other employees

The remuneration policy for Executive Directors is designed to be aligned with the Company's objectives. The remuneration arrangements for Executive Directors are cascaded as appropriate to other employees to ensure that their arrangements are also aligned with the Company's objectives:

- The Company's approach to salary reviews is consistent across the Company with consideration given to level of responsibility, experience, individual performance, salary levels in comparable companies and the Company's ability to pay
- All employees participate in the same annual bonus scheme as the Executive Directors with opportunities varying by organisational level
- Direct reports to the Executive Directors are eligible to participate in FPIP with vesting dependent on the same performance conditions as the Executive Directors, although award sizes vary by organisational level. Other employees are eligible to participate in a Restricted Stock Plan ('RSP') with vesting after three years dependent on continued employment, personal performance and absolute TSR performance conditions
- All employees are eligible to participate in the SIP on the same terms as the Executive Directors
- Pension and benefits arrangements vary according to location and so different arrangements are in place for different populations in the Company.

Directors' remuneration policy

continued

Service contracts and exit payment policy

The service and employment contracts of the Executive Directors are not of a fixed duration and therefore have no unexpired terms, but continuation in office as a Director is subject to re-election by shareholders as required under the Company's Articles of Association and in accordance with the provisions of the Code. The Company's policy is for Executive Directors to have service and employment contracts with provision for termination of no longer than 12 months' notice.

The Non-Executive Directors do not have service contracts. Letters of Appointment provide for termination of the appointment with three months' notice by either party.

When determining any loss of office payment for a departing individual the Committee will always seek to minimise cost to the Company whilst seeking to reflect the circumstances in place at the time. The Committee retains overriding discretion to make loss of office payments appropriate to the circumstances and applying the overriding principle that there should be no element of reward for failure.

Under the Executive Directors' service contracts, if notice is served by either party, the Executive Directors can continue to receive their full salary and other contractual benefits for the duration of their notice period during which time the Company may require them to continue to fulfil their normal duties or may assign a period of garden leave. All service contracts and letters of appointments are available for viewing at the Faroe registered office.

Where an Executive Director's employment is terminated after the end of a performance year but before an annual bonus payment is made, the Executive will remain eligible for an annual bonus award for that performance year subject to an assessment based on performance achieved over the period. No award will be made in the event of gross misconduct. Where an Executive Director's employment is terminated during a performance year, a pro-rata annual bonus for the period worked in that performance year may be payable, subject to an assessment based on performance achieved over the period.

On termination of an Executive Director's employment, unvested CIP and FPIP awards will lapse on cessation where such cessation is by reason of cause or, unless the Committee determines otherwise, resignation. In other 'good' leaver situations, unvested CIP and FPIP awards will continue and will vest to the extent the performance conditions are achieved and be subject to a time-based reduction unless the Committee determines such reductions should be disappplied.

At any time within three months of any change of control of the Company, an Executive Director having completed a minimum of 12 months' service may give notice to the Company to terminate his employment with three months' notice and be entitled to receive a sum equivalent to 12 months' salary and benefits (including pension) and 65% of the total bonus paid (if any) in the previous calendar year.

Consideration of employment conditions elsewhere in the Company in developing policy

In setting the remuneration policy for the Executive Directors, the pay and conditions of other Faroe employees are taken into account. The Committee is provided with data on the remuneration structure for senior members of staff below the Executive Director level and uses this information to ensure consistency of approach throughout the Company. The Company has not formally consulted with employees when drawing up the Directors' remuneration policy. However, the Company considers any informal feedback received from employees.

Consideration of shareholder views

The Committee takes the views of the shareholders very seriously and these views have been influential in shaping remuneration policy and practice. Shareholder views are considered when evaluating and setting ongoing remuneration strategy and the Committee commits to consulting with shareholders prior to any significant changes to its remuneration policy.

Director	Date of latest contract	Notice period by Company or Director
Executive Directors		
Graham Stewart	20 June 2017	12 months
Helge Hammer	29 May 2017	12 months
Jonathan Cooper	20 June 2017	12 months
Non-Executive Directors		
	Latest date of appointment	
John Bentley	1 September 2016	3 months
Timothy Read	1 March 2015	3 months
Roger Witts	1 May 2015	3 months
Jorunn Sætre	1 September 2017	3 months
Brent Cheshire	25 October 2017	3 months

Annual report on remuneration

This section of the remuneration report contains details of how the Company's remuneration policy was implemented during the financial year ending on 31 December 2017.

Single total figure of remuneration

Executive Directors

The remuneration of Executive Directors showing the breakdown between elements and comparative figures is shown below.

Executive Director (£'000)		Salary	Taxable benefits	Annual bonus ³	Long-term incentives ⁴	SIP	Pension	Total
Graham Stewart ¹	2017	376	5	282	336	–	75	1,074
	2016	376	3	344	–	–	75	798
Helge Hammer ²	2017	331	13	191	186	–	80	801
	2016	299	12	264	–	–	78	653
Jonathan Cooper	2017	254	4	190	181	–	51	680
	2016	254	3	233	–	–	51	541

1 Mr Stewart is a non-executive director of Alopex Gold Inc and received fees totalling approximately £14,000 during the period.

2 For 2016 and 2017 Mr Hammer's salary was set in Sterling but paid in NOK. Half of his salary is paid using a fixed exchange rate set at the beginning of the year (GBP1:NOK12.344 for 2016, GBP1:NOK10.638 for 2017) and the balance on a floating exchange rate that varies month to month.

3 20% of the 2017 bonus payment was deferred into Faroe shares. Mr Hammer's bonus is less than 75% due to changes in exchange rates.

4 Long-term incentives include the FPIP vestings.

Non-Executive Directors

The remuneration of Non-Executive Directors showing the breakdown between elements and comparative figures is shown below.

Non-Executive Director (£'000)		Basic fees	Additional fees	Other ⁴	Total fees
John Bentley ¹	2017	116	6	–	122
	2016	116	6	–	122
Timothy Read ²	2017	49	19	–	68
	2016	49	19	7	75
Roger Witts ³	2017	49	19	–	68
	2016	49	19	–	68
Jorunn Sætre	2017	44	–	–	44
	2016	49	–	–	49
Brent Cheshire ⁵	2017	9	–	–	9
	2016	–	–	–	–

1 Additional fees paid for Chairmanship of the Nominations Committee.

2 Additional fees paid for Senior Non-Executive Independent Directorship and Chairmanship of the Remuneration Committee.

3 Additional fees paid for Chairmanship of the Audit Committee.

4 Other fees reflect additional fees paid for additional time spent on activities which are outside his/her ordinary duties as a Director.

5 Brent Cheshire was appointed on 25 October 2017.

Annual report on remuneration

continued

Additional details in respect of single total figure table

Taxable benefits

Benefits typically comprise life assurance cover, private healthcare arrangements and permanent health insurance and in Norway a cash allowance in lieu of company car. The Company provided Executive Directors with the following benefits during the year:

Executive Director (£'000)		Company car or cash allowance	Life assurance cover, private healthcare arrangements and permanent health insurance
Graham Stewart	2017	–	5
	2016	–	3
Helge Hammer	2017	11	2
	2016	11	1
Jonathan Cooper	2017	–	4
	2016	–	3

Annual bonus scheme

For the Executive Directors, the maximum annual bonus for 2017 was 100% of salary with payment based on a performance scorecard comprising corporate, operational and financial goals. A summary of the relevant performance categories and their ascribed weightings is set out below:

Category	Weighting
Corporate, covering balance sheet strength, transactions (both acquisitions and disposals) and reputation	30%
Operational, covering HSEQ performance, operated assets, production targets, reserve and resource target	40%
Financial, covering performance against budget, gearing levels and hedging	15%
Personal performance	15%
Total	100%

At the start of the year, the Committee approved a range of targets for each of the performance categories, against which performance would be assessed and which would guide the Committee as to the appropriate bonus payment for the year. At the end of the financial year, performance was carefully reviewed against the targets set for the scorecard, and included a general overview by the Committee of the overall performance of the Company, including acquisition and disposal activities over the year. The targets are calibrated so that threshold performance triggers a bonus payment of 20% of salary. The strong performance during the year led to the Committee approving an overall bonus payment of 75% of salary.

Executive Director		Bonus payment £'000	Bonus payment % of base salary
Graham Stewart	2017 ¹	282	75.0%
Helge Hammer	2017 ¹	191	75.0%
Jonathan Cooper	2017 ¹	190	75.0%

¹ 20.0% of the bonuses paid to Executive Directors for 2017 have been deferred and will be applied in acquiring shares that will qualify as Investment Shares under the CIP and be subject to a three year holding period.

Long-term incentives

Awards granted under the CIP on 17 June 2014 did not meet the performance conditions (i.e. the satisfaction of the relative TSR underpin or the satisfaction of the absolute TSR targets) at the end of the three year performance period; consequently, these awards lapsed during 2017.

Awards granted under the FPIP on 17 June 2014 partially met the performance conditions at the end of the three year performance period resulting in 53.5% of the award granted vesting (which equates to 35.7% of maximum award). The following table details the vesting schedules and performance against targets for this award.

% of granted award vesting	Absolute TSR over 3 years from date of grant	Relative TSR ¹	Growth in proven and probable reserves replacement per share ²	Growth in risk contingent resources per share ²
150%	25% p.a.	90th	150%	200%
100%	20% p.a.	75th	130%	115%
55%	15% p.a.	60th	105%	85%
25%	10% p.a.	50th	100%	70%
0%	<10% p.a.	<50th	<100%	<70%
Faroe's performance	-12.4% p.a.	70th	159%	-27%
Weighting	33.3%	33.3%	16.7%	16.7%
Vesting of each element	0%	85.6%	150%	0%

1 Relative to a selected group of international exploration and production peers over three years from date of grant.

2 Between 1 January 2014 and 31 December 2016 and determined by the Competent Person.

The Executive Directors were entitled to the following shares on vesting (subject to an additional two year holding period).

Executive Director	Interest held	Vesting %	Interest vesting	Vesting date	Market price (p)	Vest-date value ¹
Graham Stewart	715,686	53.5%	382,892	17 June 2017	87.66	£335,643
Helge Hammer	396,781		212,278			£186,083
Jonathan Cooper	386,667		206,867			£181,340

1 Calculated as number of awards vesting multiplied by the closing share price preceding the vesting date of £0.8766.

2015 CIP awards

Awards of nil cost options granted under the CIP on 20 January 2015 were tested on 20 January 2018, at the end of a three year performance period. The testing of the award was based on a relative TSR underpin vs FTSE AIM Oil & Gas Index and absolute share price growth. The underpin was met, as the Company's TSR growth was higher than that of the FTSE AIM Oil & Gas Index over the period, and the Company's TSR over the period was 75.6%. As a result, 67.4% of the award met the performance targets as set out below:

Executive Director	Interest held	Performance test %	Interest meeting performance	Market price (p)	Estimated value ¹
Graham Stewart	811,306	67.4%	546,820	99.81	£545,781
Helge Hammer	580,436		391,214		£390,471
Jonathan Cooper	438,059		295,252		£294,691

1 Based on the three month variable weighted average price from 1 October to 31 December 2017.

Annual report on remuneration

continued

Total pension entitlements

The Company does not operate a pension scheme for the UK based Executive Directors, but does, at the Directors' option, contribute to the personal pension plans of each Executive Director, or pays cash in lieu of such contributions. UK Executive Directors receive a contribution to a personal pension scheme or cash allowance in lieu of pension benefits up to 20% of salary. Any such receipt above £10,000 is a taxable benefit paid by the Executive.

In Norway the Company contributes to a pension scheme on behalf of the employee up to 25.1% of base salary limit up to approximately £101,500 (approximately NOK 1.1 million). In addition the Company makes the following contributions to the employees which are paid into their personal pension plans:

- 10% of base salary above approximately £101,500 (approximately NOK 1.1 million); and
- for Helge Hammer and certain other senior managers the Company contributes a further 10% of base salary above approximately £143,500 (approximately NOK 1.6 million).

Defined contributions above the limit of NOK 1.1 million (as set for 2017) are a taxable benefit to the employee and the Company meets the associated taxation on behalf of Helge Hammer and the relevant employees.

Scheme interests awarded in 2017 financial year

The tables below set out the details of the long-term incentive awards granted in the 2017 financial year where vesting will be determined according to the achievement of performance conditions that will be tested in future reporting periods. No Non-Executive Directors received scheme interests during the financial year.

Co-Investment Plan (2016)

Following the purchase of two tranches of shares in the Company, deemed as Investment Shares under the CIP, the Committee granted the following Matching Awards on 12 January 2017 and 15 February 2017 to the Executive Directors:

Executive Director	Type of interest awarded	Date of award	Number of Investment Shares purchased	Face value of Matching Share award made ¹ (£000)	Number of Matching Shares granted	Percentage of award receivable for threshold performance	End of performance period	Exercise price £
Graham Stewart	Conditional share	12 Jan-17	73,398	144,052	138,512	20	11 Jan 2020	0.00
	Conditional share	15 Feb-17	9,905	20,888	18,713	20	14 Feb 2020	0.00
Helge Hammer	Conditional share	12 Jan-17	60,546	118,605	114,044	20	11 Jan 2020	0.00
	Conditional share	15 Feb-17	8,109	17,068	15,290	20	14 Feb 2020	0.00
Jonathan Cooper	Conditional share	12 Jan-17	49,563	97,274	93,533	20	11 Jan 2020	0.00
	Conditional share	15 Feb-17	6,689	14,105	12,636	20	14 Feb 2020	0.00

¹ Calculated as number of Investment Shares multiplied by the closing share price preceding the date of grant of £1.04 for the award dated 12 January 2017 and £1.11625 for the award dated 15 February 2017.

Under the CIP, these Matching Share awards will vest dependent upon the following performance criteria: (i) the satisfaction of a TSR underpin whereby no Matching Share awards will be released unless the TSR performance of the Company exceeds the return of the FTSE AIM Oil and Gas Index over the three year performance period; (ii) the satisfaction of absolute TSR targets over a three year performance period from the date of grant whereby 20% of the Matching Shares will be released for TSR of 8% per annum over the performance period and 100% will be released for TSR of 16% per annum over the performance period.

Faroe Petroleum Incentive Plan

On 28 July 2017, the Committee granted the following awards under the shareholder approved 2016 FPIP:

Executive Director	Type of interest awarded	Basis of award	Face value of award made ¹ £'000	Number of awards	Percentage of award receivable for threshold performance	End of performance period ²	Exercise price £	Performance conditions
Graham Stewart	Nil-Cost Option	250% of salary	940	1,192,277	20%	28 July 2020	0.00	See table below
Helge Hammer	Nil-Cost Option	200% of salary	560	710,293	20%	28 July 2020	0.00	
Jonathan Cooper	Nil-Cost Option	200% of salary	508	644,083	20%	28 July 2020	0.00	

1 Calculated as number of awards granted multiplied by the closing share price preceding the date of grant of £0.78884.

2 Any awards that vest at the end of the performance period for Executive Directors will be required to be held for an additional two year holding period. Awards may be exercised during the holding period so long as the resultant shares are then held for such period other than those which may be sold to meet any associated tax liabilities.

Vesting of the FPIP awards will be based on two equally weighted performance conditions, as set out in the following table:

Performance level	Vesting level ¹ (% of maximum opportunity at grant)	Relative TSR ² (50% weighting)	Absolute TSR (50% weighting)
Below Threshold	0%	Below Median TSR	Below 8% p.a.
Threshold	20%	Median TSR	8% p.a.
Good	100%	Median TSR + 15%	16% p.a.

1 Vesting will be calculated on a straight line basis between each vesting level.

2 Performance relative to a bespoke comparator group of international exploration & production companies, both onshore and offshore, with a range of market capitalisations.

Statement of Directors' shareholding and share interests

Directors' share interests at 31 December 2017 are set out below:

Director	Number of beneficially owned shares ¹	CIP		FPIP		SIP		Total interests held at 31 December 2017
		Total number of Investment Shares	Total number of Matching Shares subject to conditions	Interests subject to conditions ²	Vested and un-exercised	Total number of Partnership Shares	Total number of Matching Shares subject to conditions	
Executive								
G Stewart	1,327,851	386,123	1,665,860	3,733,905	881,659	5,956	11,912	8,013,266
H Hammer	532,633	274,083	1,168,526	2,224,455	521,240	5,832	11,664	4,738,433
J Cooper	39,534	217,582	1,015,205	2,017,103	409,184	5,956	11,912	3,716,476
Non-Executive								
J Bentley	172,270	—	—	—	—	—	—	172,270
T Read	160,000	—	—	—	—	—	—	160,000
R Witts	109,180	—	—	—	—	—	—	109,180
J Sætre	28,571	—	—	—	—	—	—	28,571
B Cheshire	—	—	—	—	—	—	—	—

1 Beneficial interests include shares held directly or indirectly by connected persons.

2 Including those of Nil-Cost Option interests granted under the FPIP in exchange for unvested and vested Share Option Scheme awards.

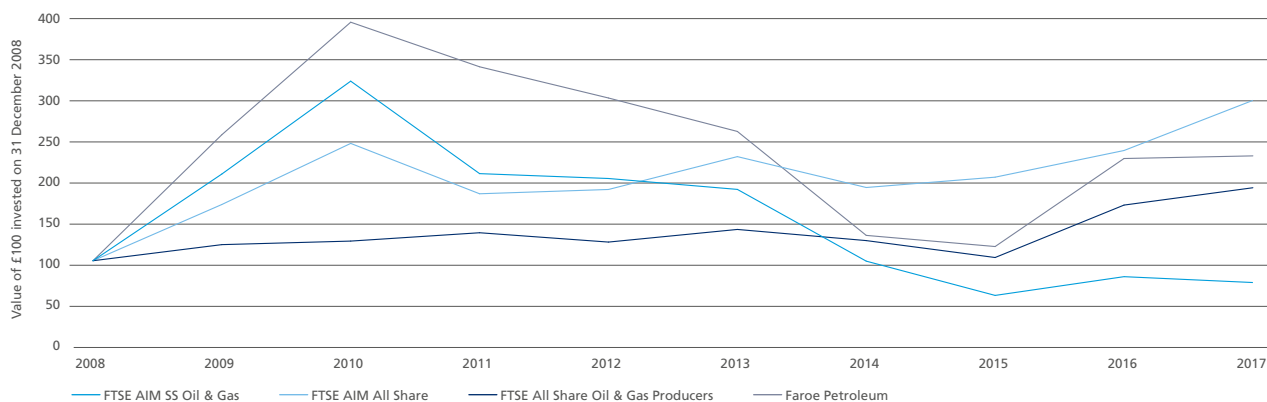
Annual report on remuneration continued

Dilution

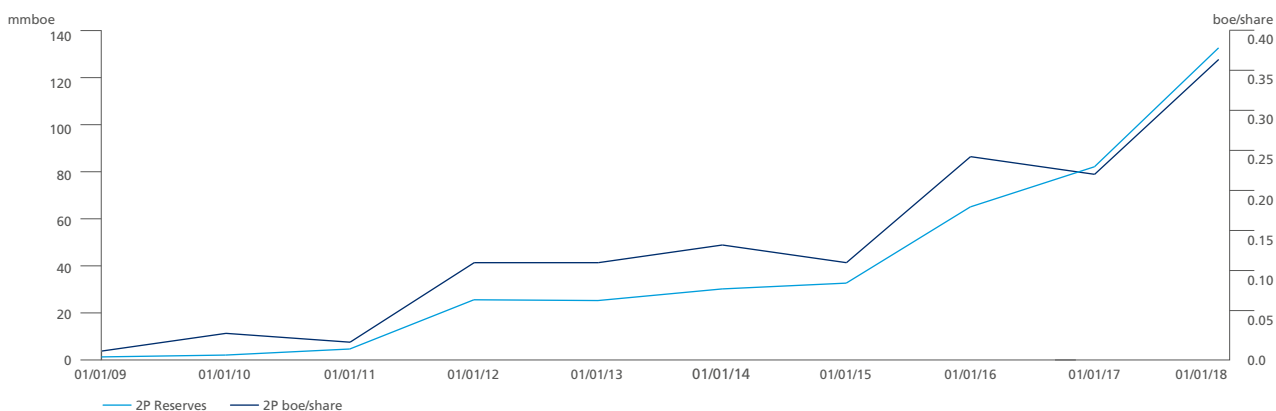
The Company funds FPIP and CIP awards using a combination of cash and newly issued shares. The maximum dilution limit available to fund such awards is 15% of share capital under the FPIP and CIP rules; however, equity grants each year are made on the basis that the estimated 'expected' vesting will be less than 10% (i.e. taking into account the likelihood that not all awards shall vest as a result of the performance conditions not being met in full). As of 31 January 2018, the maximum dilution which would result if all relevant outstanding FPIP/CIP awards were to vest would be 9.8%. Taking into account performance-to-date under the outstanding FPIP/CIP cycles, the Company estimates the 'expected' dilution to be 8.8%.

Performance graphs and Chief Executive Officer remuneration

The chart below shows the Company's performance compared with the performance of the FTSE AIM All Share Index, FTSE All Share Oil & Gas Producers Index and the FTSE AIM SS Oil & Gas Index.



The chart below shows the Company's performance in respect of growth in Proven and Probable (2P) Reserves and under the Competent Person Report¹, along with 2P Reserves (boe) per issued share, in the last nine years.



¹ Since 2012 the Company has reported its internal estimate of Proven plus Probable (2P) Reserves which are made according to the Petroleum Resource Management System guidelines endorsed by the Society of Petroleum Engineers. Whilst these internal estimates are broadly in line with the estimates generated by the Group's appointed independent engineer, the Remuneration Committee uses such independent estimates to assess performance to ensure independence.

The table below shows the change in the Chief Executive Officer's remuneration package over the past eight years:

Year	Name	Single figure of total remuneration (E'000)	Bonus pay-out (as % maximum opportunity)	Long-term incentive vesting (as % maximum opportunity)
2017		1,074	75%	53.5%
2016		798	92%	36%
2015		646	50%	–
2014	Graham	743	81%	–
2013	Stewart	553	35%	–
2012		567	30%	–
2011		677	92%	–
2010		629	100%	–

Percentage change of Chief Executive Officer's remuneration over 2017

The table below compares the percentage increase in the Chief Executive Officer's pay (including salary and fees, taxable benefits and annual bonus) with the wider employee population. The Company considers full-time employees to be an appropriate comparator group.

Year on year change (%)	Chief Executive Officer	Average employee pay
Base salary	10%	6%
Taxable benefits	67%	6%
Bonus	(18%)	(34%)

Implementation of remuneration policy in 2018

Base salary

Following a review of Executive Directors' salary levels, and in recognition of the salary freeze since January 2015, the Committee determined that the Executive Directors' salaries would increase by 10% for the year commencing 1 January 2018. The salaries for 2018 are therefore as follows:

Executive Director	Salary E'000
Graham Stewart	£414
Helge Hammer ¹	£305
Jonathan Cooper	£279

¹ From 2015 Mr Hammer's salary was set in Sterling but paid in NOK. Half of his salary is paid using a fixed exchange rate set at the beginning of the year (GBP1:NOK10.6382 for 2017) and the balance on a floating exchange rate that varies month to month.

Pension and benefits

Benefits and pensions offered in 2018 will be in line with the remuneration policy:

- UK Executive Directors (Graham Stewart and Jonathan Cooper) will continue to receive a contribution to a personal pension scheme or cash allowance in lieu of pension benefits up to 20% of salary. The Company will continue to contribute to the Norwegian defined contribution scheme of 10% of base salary above £101,500 (NOK 1.1m) and a further 10% of salary above £143,500 (NOK 1.6m) for Helge Hammer.
- Benefits will comprise life assurance cover, private healthcare arrangements, and permanent health insurance and in Norway cash allowances in lieu of a company car. Values will be of a similar level offered in 2017.

Annual report on remuneration

continued

Annual bonus

The maximum annual bonus opportunity will increase to 125% for Executive Directors in 2018, with up to 100% of salary linked to a performance scorecard which consists of corporate, operational, financial and team objectives, with the additional 25% of salary earned only for exceptional performance as determined by the Committee. Any earned bonus in excess of 75% of salary will be deferred into shares for a minimum of one year.

Long-term incentives in 2018

CIP

Upon ceasing to be in a 'close period' for dealing, the Executive Directors will invest shares in the CIP equivalent to 20% of the 2017 bonus payments, on which they will receive a match of 1:1, based on the gross pre-tax investment.

The absolute TSR performance condition attached to the vesting of these awards are as follows:

Performance level	Vesting level ¹ (% of maximum opportunity at grant)	Absolute TSR
Threshold	20%	8% p.a.
Stretch	100%	16% p.a.

¹ Vesting will be calculated on a straight line basis between each vesting level.

These awards are also subject to a relative TSR underpin where the Company's TSR is required to exceed the FTSE AIM Oil and Gas Index.

FPIP

It is anticipated that in 2018 Graham Stewart will receive an FPIP award of 250% of his salary and Helge Hammer and Jonathan Cooper will receive an FPIP award of 200% of salary.

The performance conditions attached to the vesting of these awards are based on relative and absolute TSR as follows:

Performance level	Vesting level ¹ (% of maximum opportunity at grant)	TSR outperformance ² (50% weighting)	Absolute TSR (50% weighting)
Threshold	20%	Median TSR	8% p.a.
Stretch	100%	Median TSR + 15% p.a.	16% p.a.

¹ Vesting will be calculated on a straight line basis between each vesting level.

² Performance relative to a bespoke comparator group of international exploration & production companies.

Non-Executive Director fees

Following a review of Non-Executive Director fees it was determined that the Chairman and NED base fees would be increased by 10%, effective 1 January 2018.

NED fee component	1 January 2017 £'000	1 January 2018 £'000	% change
Chairman fee	116	127	10
Average basic fee	49	54	10
Additional fee for Senior Independent Director role	11	11	–
Additional fee for Chairmanship of the Nominations Committee	6	6	–
Additional fee for Chairmanship of the Remuneration Committee	8	8	–
Additional fee for Chairmanship of the Audit Committee	19	19	–

Non-Executive Directors do not participate in any variable remuneration elements or any other benefits arrangements.

Consideration by the Directors of matters relating to Directors' remuneration

Members of the Committee

Director	Number of meetings held	Number of meetings attended
John Bentley	7	7
Timothy Read ¹	7	7
Roger Witts	7	7
Jorunn Sætre	7	7
Brent Cheshire ²	–	–

¹ Chairman of the Remuneration Committee.

² Appointed on 14 December 2017.

The members of the Committee have no personal financial interest other than as shareholders in matters to be decided, no potential conflicts of interest arising from cross Directorships and no day-to-day involvement in running the business.

Role of the Committee and activities

The Committee is responsible for recommending to the Board the remuneration policy for Executive Directors and the senior management and for setting the remuneration packages for each Executive Director. The Committee also has oversight of the remuneration policy and packages for other senior members of staff. The written Terms of Reference of the Committee are available on the Company's website and from the Company on request. The role of the Committee includes:

- Determining and agreeing with the Board the remuneration policy for all the Executive Directors;
- Ensuring that remuneration packages are competitive and determining individual remuneration packages for each Director;
- Determining whether the Directors should be eligible for annual bonuses and benefits under long-term incentive schemes;
- Considering any new long-term incentive schemes and associated performance criteria;
- Determining payouts or grants under all incentive schemes;
- Considering the pension contributions to the Directors and associated costs to the Company of basic salary increases and other changes in remuneration, especially for Directors close to retirement;
- Determining what compensation commitments exist under the Directors' service contracts;
- Determining notice or contract periods under the Directors' service contracts.

Advisers to the Committee

During the year the Committee sought independent advice from Mercer | Kepler which is a member of the Remuneration Consultants Group and, as such, voluntarily operates under the code of conduct in relation to executive remuneration consulting in the UK.

The Committee also sought the views of Graham Stewart during the year and Julian Riddick (Company Secretary). The Chief Executive and Company Secretary are given notice of all meetings and, at the request of the Chairman of the Committee, attend the meetings. In normal circumstances, the Chief Executive and the Company Secretary will be consulted on general policy matters and matters concerning the other Executives and employees. Neither the Chief Executive Officer nor the Company Secretary participates in discussions in relation to their own remuneration arrangements.

Statement of voting at general meeting

The table below shows the results of the advisory vote on the 2016 Directors' Remuneration Report at the 2017 AGM and other resolutions connected with remuneration:

Resolution	Votes For			Votes Against			Votes Withheld	
	Number of votes	%	Number of shareholders	Number of votes	%	Number of shareholders	Number of votes	Number of shareholders
2. 2016 Directors' Remuneration Report	258,926,654	95.1	137	1,329,825	0.5	18	12,095,879	12
8. Amendment of the FPIP and FPCIP	261,546,120	96.0	142	1,527,611	0.6	9	9,278,627	15
11. Increase in the limit of NED fees	266,989,818	98.0	151	67,249	0.0	8	5,295,291	6

Audit Committee report

Name	Meetings attended
Roger C Witts	4
John W S Bentley	4
Brent Cheshire	–
Timothy P Read	4
Jorunn Sætre	4



Summary of the role of the Audit Committee

The Audit Committee acknowledges and embraces its role of protecting the interests of shareholders in relation to the published financial information by the Company and the effectiveness of the audit thereof. The Audit Committee also plays a key role in ensuring that the report and accounts are fair, balanced and understandable and contain sufficient information on the Company's performance, business model and strategy.

The Audit Committee is governed by Terms of Reference which are available on the Company's website. These terms are agreed by the Board and subject to annual review, the last being in December 2017.

Composition of the Audit Committee and meetings

The Audit Committee comprises Roger Witts (Committee chairman), Brent Cheshire (appointed 14 December 2017), Tim Read, Jorunn Sætre and John Bentley and their summary biographies can be found on pages 42 and 43. Roger Witts and Tim Read are deemed to be members with recent and relevant financial experience.

The Audit Committee meets at least twice a year (four full Committee meetings and two sub-committee meetings in 2017) and meetings are attended by the Chief Executive and the Chief Financial Officer by invitation. At least once a year the Committee meets in private session with the external auditors. A record of Directors' attendance at meetings of the Audit Committee held during 2017 is given in the Directors' report on page 48.

Significant issues related to the financial statements

The significant issues that were considered by the Audit Committee in 2017 in relation to the financial statements and how these were addressed were as follows:

Going concern and working capital

The Group operates in an uncertain environment, exasperated by fluctuating commodity prices, with an increasing number of committed capital expenditure programmes and maintaining sufficient cash headroom for the business is essential. The Group has a strict budgetary discipline and advanced cash flow forecasting tools which enable management to monitor closely the Group's working capital forecasts. The working capital forecasts including sensitivity analyses are examined on an ongoing basis by the Audit Committee, and always when contemplating acquisitions and disposals, to enable the Board of Directors to report that the Group remains a going concern.

Business combination

The Audit Committee and management determined that the acquisition of an interest in a UK producing field during the year should be accounted for as a business combination under the requirements of IFRS 3. The main associated complexity was in respect of accounting for deferred tax, which also led to technical goodwill arising on acquisition. The technical goodwill was recognised mainly because of the requirement to recognise deferred tax assets and liabilities on the difference between the assigned fair values and tax bases of assets acquired and liabilities assumed. In Norway, licences can only be sold in a market after tax, based on a decision made by the Norwegian Ministry of Finance pursuant to the Petroleum Taxation Act Section 10. The assessment of fair value of such licences is therefore based on cash flows after tax. IFRS balance sheet values are pre-tax. In accordance with IAS 12, a provision is made for deferred tax corresponding to

the tax rate multiplied with the difference between the acquisition cost and the tax base. The offsetting entry to this deferred tax is goodwill. Hence, goodwill arises as a technical effect of deferred tax ("technical goodwill") and does not reflect a premium paid in excess of the fair value of the actual assets acquired.

Oil and gas assets

Oil and gas assets are split between exploration and evaluation assets (E&E) and development and production assets (D&P). Once active exploration is completed on an E&E asset it is assessed for impairment. If commercial reserves are not discovered, the E&E asset is written off to the Income Statement. The Audit Committee reviews management's rationale for writing off E&E assets at least twice a year ahead of the interim review and year-end audit. For D&P assets, an impairment review is carried out on an asset-by-asset basis and involves comparing the carrying value with its economic value. The Audit Committee reviews the assumptions used by management to ascertain the economic values in order to ensure that these are reasonable. The key assumptions include commodity prices, discount rate and inflation rate. The Audit Committee is satisfied with management's assumptions, particularly in relation to commodity prices. The Audit Committee takes cognisance of the views and experience of the Group technical staff and external consultants but accepts that responsibility for such impairments lies with the management and, ultimately, the Board.

Decommissioning provisions

A substantial portion of the Group's liabilities consist of decommissioning provisions (for the removal of platforms, subsea facilities, pipelines and the plugging of wells). The Group provides for these long-term liabilities using estimates of operators of the fields, or, for assets operated by Faroe, third party experts which are discounted for time. The Audit Committee recognises the inherent uncertainties of these estimates, particularly the timing of the decommissioning activities, for both the

Company's assets but also for the third party downstream facilities and infrastructure whose early abandonment could trigger the early decommissioning of the Company's fields. Due to this uncertainty and the materiality of the provisions, the Committee ensures that they are adequately reviewed for existing assets, and in asset acquisition considerations, but there will remain considerable uncertainty on the timing of decommissioning of downstream facilities and infrastructure.

External audit

Ernst & Young LLP were originally appointed as auditors to the Group in 2007 following a tender review. The Group conducted a further audit tender in 2015 following which Ernst & Young retained their appointment as auditors. To ensure independence, Ernst & Young LLP rotates the audit partner and the fourth audit partner has been appointed by rotation to conduct the 2018 audit.

The effectiveness of the external audit process is largely dependent on appropriate audit risk identification at the commencement of the audit process. Ernst & Young LLP prepared a detailed audit plan, identifying key risks which in 2017 included asset impairment and provisioning for decommissioning liabilities. As detailed above, these risks were reviewed during the year and the Audit Committee has challenged both management's assumptions and estimates and the tests undertaken by the auditors. We assess the effectiveness of the audit process in addressing these matters semi-annually. In addition, we also seek feedback from management on the effectiveness of the audit process.

For the 2017 financial year, management were satisfied that there had been appropriate focus and challenge on the primary areas of audit risk and assessed the quality of the audit process to be good. The Audit Committee concurred with the view of management.

Following a review of Ernst & Young's performance, the Audit Committee has recommended to the Board of Directors that they be reappointed as auditors to the Group in a resolution to be put to shareholders at the forthcoming Annual General Meeting.

Private meetings are held with the external auditor semi-annually to provide an opportunity for open dialogue and feedback from the Committee and the auditor without management being present. Matters typically discussed include the auditor's assessment of business risks and management activity thereon, the transparency of interactions with management and confirmation that there has been no restriction in scope placed on them by management. Informal meetings are also held from time to time between the Chairman of the Audit Committee and the external lead audit partner.

Non-audit services

The Audit Committee has established a policy for the supply of non-audit services by the external auditor to ensure that such services do not impair the auditor's independence or objectivity. The policy identifies services that the auditor may provide, services that are excluded in normal circumstances, sets limits to expenditure for non-audit services and establishes a reporting and review process by the Audit Committee.

As far as categories of services which it is acceptable for an auditor to provide, the governing principles are: the auditor cannot audit its own work, the auditor cannot perform management functions and the auditor cannot act as an advocate for the Group. Based upon these principles, specific categories of services have been identified that the auditor can provide.

Audit Committee report continued

Risk management and internal controls

The Board is responsible for establishing and maintaining the system of internal controls which has been in place throughout 2017. The system of internal controls is vital in managing the risks that face the Group and safeguarding shareholders' interests. The Group's internal controls are designed to manage rather than eliminate risk as an element of risk is inherent in the activities of an oil and gas company. The Board's obligation is to be aware of the risks facing the Company, mitigate them where possible, insure against them where appropriate and manage the residual risk in accordance with the stated objectives of the Group.

An ongoing assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity, is undertaken by the Board of Directors and Audit Committee. The effectiveness of the Group's system of internal control is also monitored on an ongoing basis by both the Audit Committee and the Board of Directors. At each meeting, the Audit Committee reviews those risks and associated controls which are predominantly financial whilst the Board of Directors reviews those risks that are predominantly operational or of a corporate nature. The process involves the review of the updated Risk Registers and discussion with key personnel as to the implementation of such control associated procedures.

An annual review of all risks, financial, operational and corporate, was undertaken in December 2017 by the Board of Directors which includes the members of the Audit Committee. This review involves the assessment of the Risk Registers and the Group's written procedures. Following that annual review it was considered that the internal controls in respect of the key risks that face the Group were appropriate.

The following describes the principal elements of the Group's internal control system and processes employed to review the effectiveness of such system:

Strategic plan

The Board sets the strategic direction for the Group which is then implemented by the Executive Directors and senior management which make up the Executive Committee. Goals are set at the commencement of each year by the Executive Committee and monitored thereafter by the Board.

Management structure

A formal schedule of matters is reserved for consideration and approval by the Board including all major decisions of financial, technical or organisational importance. The Group's internal control procedures require Board approval for all new projects and all major expenditure requires the approval of the Chief Executive. The Executive Committee meets regularly to discuss day-to-day operational matters.

Risk management

The Board is responsible for identifying the major business risks that face the Group and for determining appropriate risk mitigation in accordance with the Group's risk management policy which covers environmental, operational, financial and legal risks. Matrices setting out the principal risks faced by the Group, prepared by the Company Secretary and HSE Manager, are presented to the Board and Audit Committee for review at each quarterly meeting.

Liquidity and budgetary risk

Each year the Board approves the Group's business plan and budget and variance analysis is undertaken regularly throughout the year and reported to the Board which approves any material variation to the budget. Short-term and long-term cash flow forecasts are produced and reported to senior management and the Board on a regular basis. The Group produces and updates the rolling five year plan each year, which is also approved by the Board.

Internal audit

In 2017 an internal audit was undertaken to check that all bank transfers were being undertaken in accordance with the approved authority levels and procedures. Whilst there were no major findings, the audits did uncover a number of procedures that could be improved upon, and remedial action has been taken. In 2018, the internal audit function will focus on the Brasse HSEQ plan, procurement and the systems to protect against a cyber-attack.

Signed on behalf of the Audit Committee by:

Roger Witts
Chairman of the Audit Committee
19 March 2018



Independent auditors' report

to the members of Faroe Petroleum plc

Opinion

In our opinion:

- Faroe Petroleum plc's Group financial statements and parent company financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2017 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of Faroe Petroleum plc which comprise:

Group	Parent company
Consolidated balance sheet as at 31 December 2017	Balance sheet as at 31 December 2017
Consolidated income statement for the year then ended	Statement of changes in equity for the year then ended
Consolidated statement of comprehensive income for the year then ended	Statement of cash flows for the year then ended
Consolidated statement of changes in equity for the year then ended	Related notes 1 to 32 to the financial statements including a summary of significant accounting policies
Consolidated statement of cash flows for the year then ended	
Related notes 1 to 32 to the financial statements, including a summary of significant accounting policies	

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

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the Group and parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to listed entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Independent auditors’ report
to the members of Faroe Petroleum plc (continued)

Conclusions relating to principal risks, going concern and viability statement

We have nothing to report in respect of the following information in the annual report, in relation to which the ISAs(UK) require us to report to you whether we have anything material to add or draw attention to:

- the disclosures in the annual report set out on page 29 that describe the principal risks and explain how they are being managed or mitigated;
- the directors’ confirmation set out on page 28 in the annual report that they have carried out a robust assessment of the principal risks facing the entity, including those that would threaten its business model, future performance, solvency or liquidity;
- the directors’ statement set out on page 45 in the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and their identification of any material uncertainties to the entity’s ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements
- whether the directors’ statement in relation to going concern required under the Listing Rules in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit; or
- the directors’ explanation set out on page 33 in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the entity will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

Overview of our audit approach

Key audit matters	– The appropriateness of the carrying value of exploration and appraisal assets based on current operations and future planned activities is not supported
	– The appropriateness of the carrying value of development and production assets based on current operations and future planned activities is not supported
	– Oil and Gas reserves estimates are inaccurate, leading to incorrect accounting computations being applied
	– The appropriateness of the decommissioning estimates, given the level of subjectivity and complexity involved in the computations, with a number of key cost assumptions feeding into those calculations.
	– The timing of the recognition of revenue based on contractual and lifting arrangements, is incorrect
Audit scope	– We performed an audit of the complete financial information of three components and audit procedures on specific balances for a further one component.
	– The components where we performed full or specific audit procedures accounted for 100% of Loss before tax, 100% of Revenue and 100% of Total assets.
Materiality	– Overall group materiality of £5.6m which represents 0.8% of Total Assets.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Impairment or de-recognition of exploration and appraisal assets Refer to the Audit Committee Report (page 66); Accounting policies (Note 2); and Note 5 and 13 of the Consolidated Financial Statements</p> <p>The potential impairment of exploration and appraisal ('E&A') assets or the need to de-recognise the E&A assets is a key area of audit focus due to the significant value attached to E&A assets in the balance sheet.</p> <p>Management are required to make a number of significant judgements in determining the recognition of, and the carrying value of these assets and in determining whether there are any indicators of impairment. The change in oil prices will impact the current and future financial performance, as well as increase the risk of uncommercial exploration activities and the non-renewal of exploration licenses.</p> <p>This risk for the E&A assets is unchanged from the prior year.</p>	<p>In evaluating whether the carrying value of the exploration and appraisal assets was supported we;</p> <ul style="list-style-type: none"> – obtained evidence to support management's current and future planned activities on an asset by asset basis; – confirmed whether any firm committed activities were in existence, also taking into account any key licence decision points in order to satisfy ourselves over the future viability of each asset; – evaluated whether any indicators of impairment existed; – corroborated the carrying value of the exploration asset portfolio of the Group to the valuations made within the Competent Persons Report <p>We focused on this area as it involves complex and subjective judgements about the future results of the business.</p> <p>For E&A assets we performed full scope audit procedures over this risk area in one location, which covered 99% of the account balance.</p>	<p>We concluded that management's judgements in relation to the future demonstrable activities planned on those E&A assets which remained in the Balance Sheet as at 31 December 2017, and management's judgement's on E&A assets which were deemed to be sub-economic and consequently written off through the Income Statement were reasonable.</p>

Independent auditors' report

to the members of Faroe Petroleum plc (continued)

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Impairment of development and producing assets</p> <p>Refer to the Audit Committee Report (page 66); Accounting policies (Note 2); and Note 5 and 13 of the Consolidated Financial Statements</p> <p>The potential impairment of development and production ('D&P') assets is a key area of audit focus due to the significant value attached to D&P assets in the balance sheet.</p> <p>Management are required to make a number of significant judgements in determining the recognition of, and the carrying value of these assets and in determining whether there are any indicators of impairment. The change in oil prices will impact the current and future financial performance, as well as increase the risk of uncommercial exploration activities and the non-renewal of exploration licenses.</p> <p>This risk is unchanged from the prior year.</p>	<p>We focused on this area as it involves complex and subjective judgements about the future results of the business. In evaluating whether any impairment was necessary to the remaining carrying value of the D&P assets, our audit work involved obtaining evidence regarding its recoverable amount and how this compared to the amount at which the D&P assets were currently recorded. In assessing the carrying values of the D&P assets we;</p> <ul style="list-style-type: none"> – evaluated whether any indicators of impairment existed; – evaluated the appropriateness of the discount rate and inflation rate applied; – Reconciled the net book values within the impairment computations to those recorded within the finance system at the year-end; – corroborated the oil and gas reserves used in the impairment calculations to those determined by the Company's in-house specialists; – tested the pricing assumptions used for oil and gas within the impairment calculations; – corroborated the life of field activity via the cessation of production dates as estimated within the latest decommissioning cost estimates; and – assessed the forecast cash flows in the net present value computations including oil revenues, gas revenues, opex costs and capex costs, ensuring that forecast plans for the assets were in line with our current understanding of the business. <p>We also evaluated management's sensitivity analysis on D&P impairment testing in order to assess the potential impact of a range of possible outcomes; as well as performing our own sensitivity analysis. Sensitivities were applied for oil and gas pricing assumptions and discount rates.</p> <p>Additionally we evaluated the financial statement disclosures for compliance with the requirements of accounting standards.</p> <p>We performed full and specific scope audit procedures over this risk area in two locations, which covered 100% of the account balance.</p>	<p>We agreed with the adjustments booked by management at the year-end in relation to impairment and concluded that following these adjustments, the amounts booked for impairment were reasonable.</p>

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Estimation of Oil and Gas Reserves Refer to the Operational Report (page 20); and Accounting policies (Note 2) of the Consolidated Financial Statements</p> <p>This was considered to be a significant risk due to the subjective nature of reserves estimates and their impact on the financial statements through impairment and depreciation, depletion and amortisation (“DD&A”) calculations. This is a risk related to management override.</p> <p>Faroe undertakes an evaluation of its oil and gas reserves, using its own technical experts. An independent 3rd party is also engaged to evaluate the Group’s oil and gas reserves. Any differences between the two data sets are investigated and dealt with appropriately.</p> <p>This risk is unchanged from the prior year.</p>	<p>We gained an understanding of the Group’s internal process for reserves estimation and assessed management’s assumptions including commercial assumptions to ensure that they are based on supportable evidence. In doing so, we have:</p> <ul style="list-style-type: none"> – compared the internal reserve estimation balances to those derived from an external 3rd party reserves specialist and challenging any variations. – performed an analysis of the reasonableness of key assumptions and agreed key assumptions to corroborative evidence where possible, such as oil and gas pricing, production flow rates, near term operational plans for assets; and – confirmed the qualifications and expertise of the in-house reserves specialists and the 3rd party specialists; <p>Additionally we evaluated the financial statement disclosures for compliance with the requirements of accounting standards.</p> <p>We performed full and specific scope audit procedures over this risk area in two locations, which covered 100% of the account balance.</p>	<p>We concluded that management’s judgements in relation to the volume of reserves to be recognised and 2P reserves were appropriate.</p>

Independent auditors' report

to the members of Faroe Petroleum plc (continued)

Risk	Our response to the risk	Key observations communicated to the Audit Committee
<p>Decommissioning estimation Refer to the Audit Committee Report (page 66); Accounting policies (Note 2); and Note 23 of the Consolidated Financial Statements</p> <p>This was considered to be a significant risk due to the subjective nature of decommissioning, owing to the number of key assumptions involved in its estimation.</p> <p>It is a key area of audit focus due to the significant value attached to the decommissioning assets and provisions in the balance sheet.</p> <p>This risk is unchanged from the prior year.</p>	<p>We focused on this area as it involves complex and subjective judgements about the future decommissioning plans of both Faroe and of the Operators of fields in which Faroe has a non-operating interest. Our audit procedures included;</p> <ul style="list-style-type: none"> – obtaining an understanding of the third party operator gross cost estimates supplied to the Group; – agreeing the ownership entitlements applied to the cost estimates by management to external data; – evaluated the appropriateness of the discount and inflation rates applied; – evaluating the completeness of the estimates in light of any new drilling or developments undertaken; – assessing the reliance which we could place on external specialists employed to estimate the gross cost estimate for decommissioning; and – assessing the suitability of the estimated lives of each field through to the estimated dates of decommissioning. <p>Additionally we evaluated the financial statement disclosures for compliance with the requirements of accounting standards.</p> <p>We performed full and specific scope audit procedures over this risk area in two locations, which covered 100% of the account balance.</p>	<p>We agreed with the adjustments booked by management at the year-end in relation to decommissioning and concluded that following these adjustments the amounts booked in relation to decommissioning were reasonable.</p>
<p>Revenue Recognition Refer to the Accounting policies (Note 2); and Note 3 of the Consolidated Financial Statements</p> <p>As per ISA 240, there is a presumption to consider the risk of fraud in revenue recognition. As such we have focused on the recognition of revenue as a key area of audit focus. This is a risk of management override.</p> <p>This risk is unchanged from the prior year.</p>	<p>We have focused on the potential for mis-statement of revenue via the amounts calculated at the year end. Monthly sales patterns, production and liftings can be audited and corroborated to 3rd party evidence with limited risk of mis-statement, owing to the low volume and high value nature of the transactions. For our cut-off revenue recognition risk we performed the following audit procedures;</p> <ul style="list-style-type: none"> – Re-performed the calculation of the underlift/overlift volumes and pricing at the year-end; – Performed tests of details on all significant revenue streams (oil, gas and NGLs); – Performed additional substantive testing on all significant revenue streams; – Agreed volumes produced on a field by field basis to support; and – Corroborated the prices applied to sales to the contracts in place per field. <p>We performed full and specific scope audit procedures over this risk area in two locations, which covered 100% of the account balance.</p>	<p>We concluded that revenue recognised for the year ended 31 December 2017 was materially correct on the basis of the procedures performed both at group and by component audit teams.</p>

In the prior year, our auditor's report included a key audit matter in relation to incorrect accounting for business combinations. In the current year, we concluded that the management have had the relevant accounting experience from the prior year and that the likelihood of misstatement was lower. An overview of the scope of our audit

An overview of the scope of our audit

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the group and effectiveness of group wide controls, changes in the business environment and other factors when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, of the four reporting components of the Group, we selected three components covering entities within the United Kingdom and Norway, which represent the principal business units within the Group.

Of the four components selected, we performed an audit of the complete financial information of three components ("full scope components") which were selected based on their size or risk characteristics. For the remaining one component ("specific scope components"), we performed audit procedures on specific accounts within that component that we considered had the potential for the greatest impact on the significant accounts in the financial statements either because of the size of these accounts or their risk profile.

The reporting components where we performed audit procedures accounted for 100% (2016: 100%) of the Group's Loss before tax, 100% (2016: 100%) of the Group's Revenue and 100% (2016: 100%) of the Group's Total assets. For the current year, the full scope components contributed 99% (2016: 99%) of the Group's Loss before tax, 98% (2016: 97%) of the Group's Revenue and 99% (2016: 99%) of the Group's Total assets. The specific scope component contributed 1% (2016: 1%) of the Group's Loss before tax, 2% (2016: 3%) of the Group's Revenue and 1% (2016: 1%) of the Group's Total assets. The audit scope of these components may not have included testing of all significant accounts of the component but will have contributed to the coverage of significant tested for the Group.

Changes from the prior year

There have been no changes to scoping from the prior year.

Involvement with component teams

In establishing our overall approach to the Group audit, we determined the type of work that needed to be undertaken at each of the components by us, as the primary audit engagement team, or by component auditors from other EY global network firms operating under our instruction. Of the three full scope components, audit procedures were performed on two of these directly by the primary audit team. For the other full scope component, where the work was performed by component auditors, we determined the appropriate level of involvement to enable us to determine that sufficient audit evidence had been obtained as a basis for our opinion on the Group as a whole.

The Group audit team continued to follow a programme of planned visits that has been designed to ensure that the Senior Statutory Auditor visits the Norway component team annually. During the current year's audit cycle, one visit was undertaken by the primary audit team to the component team in Norway. The visit involved discussing the audit approach with the component team and any issues arising from their work, meeting with local management as part of the closing meeting and reviewing key audit working papers on risk areas. The primary team interacted regularly with the component teams where appropriate during various stages of the audit, reviewed key working papers and were responsible for the scope and direction of the audit process. This, together with the additional procedures performed at Group level, gave us appropriate evidence for our opinion on the Group financial statements.

Independent auditors' report

to the members of Faroe Petroleum plc (continued)

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group to be £5.6million (2016: £4.6million, which is 0.8% (2016: 0.8%) of Total Assets. We believe that Total Assets provides us with a base for materiality which relates to the balances which shareholders are most concerned with for Faroe Petroleum plc. The increase in the group's assets, reflecting the business growth, is reflected in our higher materiality level.

We determined materiality for the Parent Company to be £5.2 million (2016: £5.2million), which is 1.6% (2016: 1.6%) of Equity.

During the course of our audit, we reassessed initial materiality which was set at £5.1million based on 0.8% of Total Assets and it was increased to reflect the business growth.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group's overall control environment, our judgement was that performance materiality was 50% (2016: 50%) of our planning materiality, namely £2.8m (2016: £2.3m). We have set performance materiality at this percentage due to the misstatements identified in the prior year's audit.

Audit work at component locations for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £0.90m to £2.1m (2016: £0.6m to £1.8m).

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.28m (2016: £0.23m), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report set out on page 130, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

In this context, we also have nothing to report in regard to our responsibility to specifically address the following items in the other information and to report as uncorrected material misstatements of the other information where we conclude that those items meet the following conditions:

- **Fair, balanced and understandable set out on page 46** – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- **Audit committee reporting set out on page 66** – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee; or
- **Directors' statement of compliance with the UK Corporate Governance Code set out on page 46** – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit

Independent auditors' report

to the members of Faroe Petroleum plc (continued)

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 46, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group and parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

James Nisbet (Senior statutory auditor)

for and on behalf of Ernst & Young LLP, Statutory Auditor

Aberdeen

19 March 2018

Notes:

1. The maintenance and integrity of the Faroe Petroleum plc web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.
2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions

Group income statement

for the year ended 31 December 2017

	Note	2017 £000	2016 £000
Revenue	3	152,924	94,779
Cost of sales	4	(132,508)	(96,666)
Asset impairment	5	(12,992)	(2,923)
Gross profit/(loss)		7,424	(4,810)
Other income/(expense)	7	17,353	(8,412)
Gain on disposal of asset	7	7,229	–
Exploration and evaluation expenses		(25,851)	(33,468)
Administrative expenses		(7,678)	(10,189)
Operating loss	7	(1,523)	(56,879)
Finance revenue	9	4,790	6,423
Finance costs	9	(17,006)	(11,139)
Loss on ordinary activities before tax		(13,739)	(61,595)
Tax credit	11a	2,313	28,686
Loss for the year from continuing operations		(11,426)	(32,909)
Loss per share – basic (pence)	12	(3.1)	(10.5)
Loss per share – diluted (pence)	12	(3.1)	(10.5)

Group statement of other comprehensive income

for the year ended 31 December 2017

	Note	2017 €000	2016 €000
Loss for the year		(11,426)	(32,909)
Items that may be reclassified subsequently to profit or loss:			
Exchange differences on retranslation on foreign operations net of tax		(13,274)	21,855
Total comprehensive loss attributable to equity holders of the parent		(24,700)	(11,054)

Company statement of other comprehensive income

for the year ended 31 December 2017

	Note	2017 €000	2016 €000
(Loss)/profit for the year		(5,147)	14,455
Total comprehensive (loss)/profit attributable to equity holders of the parent		(5,147)	14,455

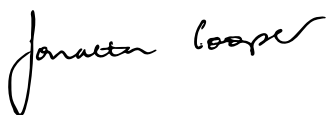
Group balance sheet

at 31 December 2017

	Note	2017 £000	2016 £000
Non-current assets			
Goodwill	14	9,386	7,744
Intangible assets	13	68,857	107,376
Property, plant and equipment: development & production	13	201,216	157,328
Property, plant and equipment: other	13	695	611
Deferred tax asset	11	114,499	122,055
		394,653	395,114
Current assets			
Inventories	18	10,644	10,456
Trade and other receivables	19	102,088	63,063
Current tax receivable	19	35,610	41,764
Cash and cash equivalents	20	149,084	96,769
		297,426	212,052
Assets held for sale	15	50,987	–
		348,413	212,052
Total assets		743,066	607,166
Current liabilities			
Trade and other payables	21	(113,989)	(53,900)
Current taxation payable		(65)	(31)
Provisions	23	(10,002)	–
Financial liabilities – borrowings	21	(32,948)	(35,845)
Financial liabilities – other	16	(767)	(1,383)
		(157,771)	(91,159)
Non-current liabilities			
Interest bearing loans and borrowings	22	(72,742)	–
Provisions	23	(254,697)	(269,469)
		(327,439)	(269,469)
Liabilities directly associated with assets held for sale	15	(31,854)	–
Total liabilities		(517,064)	(360,628)
Net assets		226,002	246,538
Equity attributable to equity holders			
Equity share capital	24	36,664	36,453
Share premium account		315,580	315,580
Cumulative translation reserve		6,381	17,740
Retained earnings		(130,708)	(123,235)
Reserves of a disposal group held for sale		(1,915)	–
Total equity		226,002	246,538

These financial statements were approved by the Board of Directors on 19 March 2018 and were signed on its behalf by:

Jonathan R Cooper
Chief Financial Officer



Company balance sheet

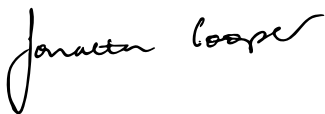
at 31 December 2017

	Note	2017 £000	2016 £000
Non-current assets			
Property, plant and equipment	13	38	64
Financial assets	16	256,269	227,896
Investments in subsidiary undertakings	17	51,805	49,904
		308,112	277,864
Current assets			
Trade and other receivables	19	398	462
Cash and cash equivalents	20	92,830	52,149
		93,228	52,611
Total assets		401,340	330,475
Current liabilities			
Trade and other payables	21	(1,519)	(1,871)
Provisions	23	(1,228)	–
		(2,747)	(1,871)
Non-current liabilities			
Interest bearing loans and borrowings	22	(72,742)	–
Provisions	23	–	(1,258)
		(72,742)	(1,258)
Total liabilities		(75,489)	(3,129)
Net assets		325,851	327,346
Equity attributable to equity holders			
Equity share capital	24	36,664	36,453
Share premium account		315,580	315,580
Retained earnings		(26,393)	(24,687)
Total equity		325,851	327,346

The Company's loss for the year was £5,147,000 (2016: profit £14,455,000).

These financial statements were approved by the Board of Directors on 19 March 2018 and were signed on its behalf by:

Jonathan R Cooper
Chief Financial Officer



Group cash flow statement

for the year ended 31 December 2017

	Note	2017 £000	2016 £000
Loss before tax		(13,739)	(61,595)
Depreciation, depletion and amortisation	7	45,179	23,369
Exploration asset write off	7	21,524	29,908
Unrealised hedging (gains)/losses	7	(369)	13,095
Asset impairment	5	12,992	2,923
Fair value of share based payment		4,948	4,408
Cash settlement of share options		(670)	–
Gain on disposal of asset	7	(7,229)	–
Disposal of decommissioning provision	7	(1,092)	–
Purchase of SIP shares		(216)	–
Movement in trade and other receivables		(42,263)	(24,478)
Movement in inventories		(188)	(4,534)
Movement in trade and other payables		61,728	22,865
Currency translation adjustments	9	(4,060)	(5,814)
Interest received	9	(730)	(609)
Interest and financing fees	9	17,006	11,139
Tax rebate		41,031	44,729
Net cash generated in operating activities		133,852	55,406
Investing activities			
Purchases of intangible and tangible assets		(144,239)	(79,447)
Interest received	9	730	609
Net cash used in investing activities		(143,509)	(78,838)
Financing activities			
Proceeds from interest bearing loans and borrowings	22	75,915	–
Issue costs of bond instruments	22	(1,920)	–
Proceeds from issue of equity instruments of the Group		–	66,901
Issue costs of shares		–	(4,145)
Repayments from borrowings		(1,404)	(19,931)
Interest and financing fees paid		(4,022)	(4,225)
Net cash inflow from financing activities		68,569	38,600
Net increase in cash and cash equivalents		58,912	15,168
Cash and cash equivalents at the beginning of the year		96,769	91,515
Effect of foreign exchange rate differences		(6,597)	(9,914)
Cash and cash equivalents at the end of the year	20	149,084	96,769

Company cash flow statement

for the year ended 31 December 2017

	Note	2017 £000	2016 £000
(Loss)/profit before tax		(5,147)	14,455
Depreciation charges	13	48	101
Fair value of share based payment		2,815	2,479
Cash cost of share based payment		(407)	–
Movement in trade and other receivables		64	(125)
Movement in trade and other payables		(352)	596
Currency translation adjustments		3,716	(16,758)
Inter-company service charge uplift		(223)	(266)
Interest received		(4,250)	(2,739)
Interest and financing fees		511	3
Net cash used in operating activities		(3,225)	(2,254)
Investing activities			
Purchases of property, plant and equipment	13	(22)	(1)
Loans to subsidiary undertakings		(28,373)	(65,477)
Investments in subsidiary undertakings		–	(944)
Interest received		207	2,739
Net cash used in investing activities		(28,188)	(63,683)
Financing activities			
Proceeds from issue of equity instruments of the Company		–	66,901
Issue costs of shares		–	(4,145)
Proceeds from interest bearing loans and borrowings	22	75,915	–
Issue costs of bond instruments	22	(1,920)	–
Interest paid		(3)	(3)
Net cash inflow from financing activities		73,992	62,753
Net increase/(decrease) in cash and cash equivalents		42,579	(3,184)
Cash and cash equivalents at the beginning of the year		52,149	37,576
Effect of foreign exchange rate differences		(1,898)	17,757
Cash and cash equivalents at the end of the year	20	92,830	52,149

Group statement of changes in equity

for the year ended 31 December 2017

	Share capital £000	Share premium account £000	Cumulative translation reserve £000	Retained earnings £000	Disposal group held for sale £000	Total £000
As at 1 January 2016	26,824	262,453	(4,055)	(92,866)	–	192,356
Loss for the year	–	–	–	(32,909)	–	(32,909)
Other comprehensive income:						
Gain on retranslation of foreign subsidiaries	–	–	21,855	–	–	21,855
Total comprehensive income/(loss)	–	–	21,855	(32,909)	–	(11,054)
Transfer to retained earnings	–	–	(60)	60	–	–
Issue of ordinary shares	9,629	57,272	–	–	–	66,901
Issue costs	–	(4,145)	–	–	–	(4,145)
Share based payments	–	–	–	2,480	–	2,480
As at 31 December 2016	36,453	315,580	17,740	(123,235)	–	246,538
Loss for the year	–	–	–	(11,426)	–	(11,426)
Other comprehensive income:						
Loss on retranslation of foreign subsidiaries	–	–	(13,274)	–	–	(13,274)
Total comprehensive loss	–	–	(13,274)	(11,426)	–	(24,700)
Issue of ordinary shares under EBT	211	–	–	(211)	–	–
Purchase of SIP shares	–	–	–	(216)	–	(216)
Share based payments	–	–	–	4,380	–	4,380
Asset held for sale	–	–	1,915	–	(1,915)	–
As at 31 December 2017	36,664	315,580	6,381	(130,708)	(1,915)	226,002

Share capital

The balance classified in share capital is the nominal value on issue of the Group's equity share capital, comprising 10p Ordinary Shares.

Share premium

The balance classified as share premium is the premium on issue of the Group's equity share capital, comprising 10p Ordinary Shares less any costs of issuing the shares.

Cumulative translation reserve

The cumulative translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Company statement of changes in equity

for the year ended 31 December 2017

	Share capital £000	Share premium account £000	Retained earnings £000	Total £000
As at 1 January 2016	26,824	262,453	(41,622)	247,655
Profit for the year	–	–	14,455	14,455
Total comprehensive profit	–	–	14,455	14,455
Issue of Ordinary Shares	9,629	57,272	–	66,901
Issue costs	–	(4,145)	–	(4,145)
Share based payments	–	–	2,480	2,480
As at 31 December 2016	36,453	315,580	(24,687)	327,346
Loss for the year	–	–	(5,147)	(5,147)
Total comprehensive loss	–	–	(5,147)	(5,147)
Issue of Ordinary Shares under EBT	211	–	–	211
Purchase of SIP shares	–	–	(939)	(939)
Share based payments	–	–	4,380	4,380
As at 31 December 2017	36,664	315,580	(26,393)	325,851

Share capital

The balance classified in share capital is the nominal value on issue of the Company's equity share capital, comprising 10p Ordinary Shares.

Share premium

The balance classified as share premium is the premium on issue of the Company's equity share capital, comprising 10p Ordinary Shares less any costs of issuing the shares.

Notes to the accounts

1 Authorisation of financial statements and statement of compliance with IFRS

The financial statements of Faroe Petroleum plc and its subsidiaries (the "Group") for the year ended 31 December 2017 were authorised for issue by the Board of Directors on 19 March 2018 and the Balance Sheet was signed on the Board's behalf by Jonathan Cooper. Faroe Petroleum plc, which is registered at 30 Crown Place, London, EC2A 4ES, is a public limited company incorporated in England and domiciled in Scotland.

The Group's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union as they apply to the financial statements of the Group for the year ended 31 December 2017. Faroe Petroleum plc is quoted on the Alternative Investment Market (AIM).

2 Accounting policies

Basis of preparation

The Group's financial statements, for the year ended 31 December 2017, have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). The Company's financial statements have been prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the Companies Act 2006. The Company has taken advantage of the exemption provided under section 408 of the Companies Act 2006 not to publish its individual Income Statement and related notes.

The Group intends to prepare the financial statements of the UK qualifying subsidiaries in accordance with Financial Reporting Standard 101: Reduced Disclosure Framework (FRS 101) and in accordance with applicable accounting standards.

The accounting policies which follow set out those policies which apply in preparing the financial statements for the year ended 31 December 2017.

The Group and Company financial statements have been prepared under the historical cost convention, except for certain fair value adjustments required by those accounting policies. The financial statements are presented in Sterling and all values are rounded to the nearest thousand pounds (£000) except where otherwise indicated.

The Directors believe that the Company has adequate resources to continue its operations for the foreseeable future. The bases for the Directors' considerations are disclosed in the Directors' Report. Thus the Directors continue to adopt the going concern basis of accounting in preparing the financial statements.

Accounting judgements and estimates

The Group's accounting policies make use of estimates and judgements in the following areas: Impairment, Depreciation, Decommissioning, Reserves and Share based payments. These are described in more detail in the relevant accounting policies.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Group as at 31 December 2017. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has all of the following:

- power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- exposure, or rights, to variable returns from its involvement with the investee; and
- the ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights result in control. To support this presumption and when the Group has less than a majority of the voting, or similar, rights of an investee, it considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- the contractual arrangement(s) with the other vote holders of the investee;
- rights arising from other contractual arrangements; and
- the Group's voting rights and potential voting rights.

Notes to the accounts

continued

2 Accounting policies continued

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests (NCI), even if this results in the NCI having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

Foreign currencies

The functional currency for the UK entities is Sterling and the functional currencies for Faroe Petroleum Norge AS and Føroya Kolvetni P/F are Norwegian Kroner and Danish Kroner respectively.

Transactions in foreign currencies during the year are recorded in the functional currency at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities are translated at the rate ruling on the Balance Sheet date and any gains and losses on translation are reflected in the Income Statement.

The assets and liabilities of foreign operations are translated into Sterling at the rate of exchange ruling at the Balance Sheet date. Income and expenses are translated at weighted average exchange rates for the year. The resulting exchange differences on assets and liabilities of such foreign operations are taken directly to a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the Income Statement.

Joint arrangements

Judgement is required to determine when the Group has joint control over an arrangement, which requires an assessment of the relevant activities and when the decisions in relation to those activities require unanimous consent. The Group has determined that the relevant activities for its joint arrangements are those relating to the operating and capital decisions of the arrangement, including the approval of the annual capital and operating expenditure work programme and budget for the joint arrangement, and the approval of chosen service providers for any major capital expenditure as required by the joint operating agreements applicable to the entity's joint arrangements. The considerations made in determining joint control are similar to those necessary to determine control over subsidiaries, as set out in Note 2. Judgement is also required to classify a joint arrangement. Classifying the arrangement requires the Group to assess their rights and obligations arising from the arrangement. Specifically, the Group considers:

- the structure of the joint arrangement – whether it is structured through a separate vehicle;
- when the arrangement is structured through a separate vehicle, the Group also considers the rights and obligations arising from:
 - the legal form of the separate vehicle;
 - the terms of the contractual arrangement; and
 - other facts and circumstances, considered on a case by case basis.

This assessment often requires significant judgement. A different conclusion about both joint control and whether the arrangement is a joint operation or a joint venture may materially impact the accounting. A complete list of the Group's joint operations is provided in Note 32.

A joint operation is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities, relating to the arrangements. In relation to its interests in joint operations, the Group recognises its:

- assets, including its share of any assets held jointly;
- liabilities, including its share of any liabilities incurred jointly;
- revenue from the sale of its share of the output arising from the joint operation;
- share of the revenue from the sale of the output by the joint operation; and
- expenses, including its share of any expenses incurred jointly.

Revenue

Revenue arising from the sale of goods is recognised when the significant risks and rewards of ownership have passed to the buyer and it can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods provided in the normal course of business, net of discounts, customs duties and sales taxes. Revenues associated with the sale of oil, natural gas, natural gas liquids, liquefied natural gas, petroleum and chemicals products and all other items are recognised when the title has passed, or has deemed to have passed, to the customer, in accordance with the commercial terms of each contract.

Generally, revenues from the production of oil and natural gas properties in which the Group has an interest with joint venture partners are recognised on the basis of the Group's working interest in those properties (the entitlement method). Differences between the production sold and the Group's share of production are recognised within cost of sales at market value.

Interest income is recognised on an accruals basis using the effective interest method.

Oil and gas expenditure – exploration and evaluation assets

Capitalisation

Pre-acquisition costs on oil and gas assets are recognised in the Income Statement when incurred. Costs incurred after rights to explore have been obtained, such as geological and geophysical surveys, drilling and commercial appraisal costs and other directly attributable costs of exploration and appraisal including technical and administrative costs, are capitalised as intangible exploration and evaluation ("E&E") assets. The assessment of what constitutes an individual E&E asset is based on technical criteria but essentially either a single licence area or contiguous licence areas with consistent geological features are designated as individual E&E assets.

E&E costs are not amortised prior to the conclusion of appraisal activities. Once active exploration is completed the asset is assessed for impairment. If commercial reserves are discovered then the carrying value of the E&E asset is reclassified as a development and production ("D&P") asset, following development sanction, but only after the carrying value is assessed for impairment and where appropriate its carrying value adjusted. If commercial reserves are not discovered the E&E asset is written off to the Income Statement.

Impairment

The Group's oil and gas assets are analysed into cash generating units ("CGU") for impairment review purposes, with E&E asset impairment testing being performed at a grouped CGU level. The current CGU consists of the Group's whole E&E portfolio. E&E assets are reviewed for impairment when circumstances arise which indicate that the carrying value of an E&E asset exceeds the recoverable amount. When reviewing E&E assets for impairment, the combined carrying value of the grouped CGU is compared with the grouped CGU's recoverable amount. The recoverable amount of a grouped CGU is determined as the higher of its fair value less costs to sell and value in use. Impairment losses resulting from an impairment review are written off to the Income Statement.

Oil and gas expenditure – development and production assets

Capitalisation

Costs of bringing a field into production, including the cost of facilities, wells and sub-sea equipment together with E&E assets reclassified in accordance with the above policy, are capitalised as a D&P asset. Normally each individual field development will form an individual D&P asset but there may be cases, such as phased developments, or multiple fields around a single production facility when fields are grouped together to form a single D&P asset.

Business combinations and goodwill

In order to consider an acquisition as a business combination, the acquired asset or group of assets must constitute a business. IFRS 3 describes a business as an integrated set of activities and assets conducted that is capable of being managed for the purpose of providing a return to investors. The combination consists of inputs and processes, which when combined have the ability to create outputs.

Acquired businesses are included in the financial statements from the transaction date, which is defined as the date on which the Company achieves control over the assets. Comparative figures are not adjusted for acquired, sold or liquidated businesses.

Acquisition cost equals the fair value of assets used as consideration, including contingent consideration, equity instruments issued and liabilities assumed in connection with the transfer of control. Acquisition cost is measured against the fair value of the acquired assets and liabilities assumed. Identifiable intangible assets are included in connection with acquisitions if they can be separated from other assets or meet the legal contractual criteria. When calculating the fair value, the tax implications of any re-evaluations are taken into consideration.

If the acquisition cost at the time of the acquisition exceeds the fair value of the acquired net assets, goodwill arises. In contrast, if the fair value of identifiable assets exceeds the acquisition cost on the acquisition date, the excess amount is taken to the Income Statement.

Notes to the accounts

continued

2 Accounting policies continued

Business combinations and goodwill continued

Goodwill is allocated to the cash generating units or groups of cash generating units that are expected to benefit from the business combination. The allocation of goodwill may vary depending on the basis for its initial recognition. The goodwill recognised is mainly related to the requirement to recognise deferred tax for the difference between the assigned fair values and the related tax base ("technical goodwill"). The valuation at fair value of licences is based on cash flows after tax, which is because the licences are sold in an after tax market based on decisions made by the Norwegian Ministry of Finance pursuant to the Petroleum Taxation Act Section 10. The purchaser is therefore not entitled to deduction for the consideration with tax effect through depreciation. In accordance with IAS 12 (paras 15 and 24) a provision is made for deferred tax corresponding to the difference between the acquisition cost and the transferred tax depreciation basis. The offsetting entry to this deferred tax is goodwill. Hence goodwill arises as a technical effect of deferred tax.

Technical goodwill is tested for impairment separately for each cash generating unit which gives rise to technical goodwill.

The estimation of fair value and goodwill may be adjusted up to 12 months after the acquisition date if new information has emerged about facts and circumstances that existed at the time of the acquisition and which, had they been known, would have affected the calculation of the amounts that were included from that date.

Acquisition related costs, except costs to issue debt or equity securities, are expensed as incurred.

Depreciation

All costs relating to a development are accumulated and not depreciated until the commencement of production. Depreciation is calculated on a unit of production basis based on the proven and probable reserves of the asset. Any re-assessment of reserves affects the depreciation rate prospectively. Significant items of plant and equipment will normally be fully depreciated over the life of the field. However, these items are assessed to consider if their useful lives differ from the expected life of the D&P asset and should this occur a different depreciation rate would be charged.

The key areas of estimation regarding depreciation and the associated unit of production calculation for oil and gas assets are:

- recoverable reserves; and
- future capital expenditure.

Impairment

A review is carried out for any indication that the carrying value of the Group's D&P assets may be impaired. The impairment review of D&P assets is carried out on an asset by asset basis and involves comparing the carrying value with the recoverable value of an asset. The recoverable amount of an asset is determined as the higher of its fair value less costs to sell and value in use. The value in use is determined from estimated future net cash flows. Any additional depreciation resulting from the impairment testing is charged to the Income Statement.

The future cash flows are adjusted for risks specific to the cash generating unit and are discounted using a pre-tax discount rate. The discount rate is derived from the Group's post-tax weighted average cost of capital and is adjusted where applicable to take into account any specific risks relating to the country where the cash generating unit is located, although other rates may be used if appropriate to the specific circumstances. In 2017 the rate used was 7.5% nominal (2016: 7.5% nominal). The discount rates applied in assessments of impairment are reassessed each year.

See Note 13 for the carrying value of oil and gas assets. Reserves and production volumes are also stated in the Review of Activities, primarily in the Producing Assets section.

Key assumptions used in the value-in-use calculations

The calculation of value-in-use for oil and gas assets under development or in production is most sensitive to the following assumptions:

- production volumes/recoverable reserves;
- commodity prices;
- fixed and variable operating costs;
- capital expenditure; and
- discount and inflation rates.

Production volumes/recoverable reserves

Annual estimates of oil and gas reserves are generated internally by the Company's reservoir engineers. These are reported annually to the Board in conjunction with an externally generated Competent Persons Report ('CPR'). The self certified estimated future production profiles are used in the life of the fields which in turn are used as a basis in the value-in-use calculation.

Commodity prices

An average of published forward prices and the long-term assumption for natural gas and Brent oil are used for the first three years of future cash flow and an inflated real price thereafter, in accordance with the Company's corporate assumptions. Field specific discounts and prices are used where applicable.

Fixed and variable operating costs

Typical examples of variable operating costs are pipeline tariffs, treatment charges and freight costs. Commercial agreements are in place for most of these costs and the assumptions used in the value-in-use calculation are sourced from these where available. Examples of fixed operating costs are platform costs and operator overheads. Fixed operating costs are based on operator budgets.

Capital expenditure

Field development is capital intensive and future capital expenditure has a significant bearing on the value of an oil and gas development asset. In addition, capital expenditure may be required for producing fields to increase production and/or extend the life of the field. Cost assumptions are based on operator budgets or specific contracts where available.

Discount and inflation rates – Discount rates reflect the current market assessment of the risks specific to the oil and gas sector and are based on the weighted average cost of capital for the Group. Where appropriate, the rates are adjusted to reflect the market assessment of any risk specific to the field for which future estimated cash flows have not been adjusted. The Group has applied a discount rate of 7.5% for the current year (2016: 7.5%). The inflation rate used in the calculation was 2.0% (2016: 2.0%).

Sensitivity to changes in assumptions

Following our review of the above assumptions and having performed a sensitivity analysis on the impairment reviews performed we conclude that commodity prices are the most sensitive assumption. A 10% change in commodity prices would result in a change of the impairment charge by £500,000 in the UK and £7,600,000 in Norway.

Oil and gas expenditure – acquisitions and disposals

Commercial transactions involving the acquisition of a D&P asset in exchange for an E&E or D&P asset are accounted for at fair value with the difference between the fair value and cost being recognised in the Income Statement as a gain or loss. When a commercial transaction involves a D&P asset and takes the form of a farm-in or farm-out agreement, the premium expected to be paid/received is treated as part of the consideration.

Fair value calculations are not carried out for commercial transactions involving the exchange of E&E assets. The capitalised costs of the disposed asset are transferred to the acquired asset. Farm-in and farm-out transactions of E&E assets are accounted for at cost. Costs are capitalised according to the Group's cost interest (net of premium received or paid) as costs are incurred.

Proceeds from the disposal of an E&E asset, or part of an E&E asset, are deducted from the capitalised costs and the difference recognised in the Income Statement as a gain or loss. Proceeds from the disposal of a D&P asset, or part of a D&P asset, are recognised in the Income Statement, after deducting the related net book value of the asset.

Notes to the accounts

continued

2 Accounting policies continued

Decommissioning

The Group recognises the discounted cost of decommissioning when the obligation to rectify environmental damage arises. The amount recognised is the present value of the estimated future expenditure determined by local conditions and requirements. A corresponding property, plant and equipment asset of an amount equal to the provision is created unless the associated activity resulted in an Income Statement write-off. This asset is subsequently depreciated as part of the capital cost on a unit of production basis. Any change to the present value of the estimated decommissioning cost is reflected as an adjustment to the provision and the property, plant and equipment asset. The unwinding of the discount on the decommissioning provision is included as an interest expense.

Where the Group has an asset with nil carrying value, and subsequently on the basis of new information makes an increase to the discounted cost of decommissioning, then such increase is taken to the Income Statement.

The key areas of estimation regarding decommissioning are:

- expected economic life of field, determined by factors such as
 - field reserves and future production profiles – see Operational Report
 - commodity prices
- inflation rate;
- nominal discount rate; and
- decommissioning cost estimates (and the basis for these estimates).

Certain gross cost estimates have been changed by operators in order to reflect the latest available information. Following the finalisation of the internal reserve estimates, cessation of production (“COP”) dates were also changed.

See Note 23 Provisions in respect of decommissioning obligations and explanation of discount rates.

Underlift/overlift

Lifting arrangements for oil and gas produced in certain fields are such that each participant may not receive its share of the overall production in each period. The difference between cumulative entitlement and cumulative production less stock is ‘underlift’ or ‘overlift’. Underlift and overlift are valued at market value and included within debtors (‘underlift’) or creditors (‘overlift’). Movements during an accounting period are adjusted through cost of sales, such that gross profit is recognised on an entitlement basis.

Other property, plant and equipment

Property, plant and equipment other than oil and gas assets are stated in the Balance Sheet at cost less accumulated depreciation. Depreciation is provided to write off the cost less the estimated residual value of the tangible fixed asset on a straight-line basis over their estimated useful lives as follows:

- IT equipment 3 to 4 years
- Other equipment 5 years

Financial assets

In the Group accounts, financial assets which are loans provided by the parent company to subsidiary undertakings are carried at cost. In the Company accounts, foreign currency gains and losses on such loans to subsidiary undertakings are recognised in the Income Statement.

Investments

Investments in subsidiaries are included in the financial statements at cost less provisions for impairment.

Trade creditors

Trade creditors 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 (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade creditors are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

Inventories

The Group’s share of any physical stock is accounted for at the lower of cost and net realisable value.

Taxation

The Income Statement tax charge/(credit) comprises both current and deferred tax. Tax is charged or credited in the Income Statement except on items related directly to equity, in which case it is recognised in equity. Current tax liabilities are payable on income for the year and are based on rates of tax enacted or substantively enacted at the Balance Sheet date.

Deferred income tax is provided in full on temporary differences between the carrying value of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, with the following exemptions:

- where the temporary differences arise on initial recognition of an asset or liability in a transaction (other than a business combination) that at the time of the transaction affects neither accounting nor taxable profit or loss;
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future; and
- deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, carried forward tax credits or tax losses can be utilised.

Key assumptions in determining the recoverability of the deferred tax asset

In considering the recoverability of the deferred tax asset in respect of carried forward tax losses at the year end, the Directors have considered that:

1. Based on current forecasts, the deferred tax asset in respect of the UK carried forward losses will be fully utilised by 2022;
2. The current forecasts are based on the same price assumptions used in the 2017 impairment tests, which are deemed to be reasonable;
3. The forecasts are derived from operator budgets and Life of Field models which are deemed to be reasonable; and
4. With regard to the Norwegian carried forward tax losses, the Norwegian Government refund any non-utilised tax losses if the activity of the Company ceases and therefore the asset is recoverable.

Pensions

Group employees and certain senior Norwegian employees receive contributions to personal pension plans, which are charged to the Income Statement on an accruals basis.

Trade and other receivables

Trade and other receivables, which generally have 30-60 day terms, are shown at face value less any provision for unrecoverable debt. Provision is made when there is objective evidence that the Group will not be able to recover balances in full. Balances are written off when the probability of recovery is assessed as being remote.

Operating leases

Rentals under operating leases are charged to the Income Statement on a straight line basis over the period of the lease.

Cash and cash equivalents

Cash and short-term deposits in the Balance Sheet comprise cash at banks and on hand and short-term deposits with a maturity of three months or less, which are subject to an insignificant risk of changes in value.

Share based payments

Employees (including senior executives) of the Group receive remuneration in the form of share-based payment transactions which may be equity settled or cash settled. The cost of equity-settled transactions with employees, for awards granted after 7 November 2002, is measured by reference to the fair value at the date on which they are granted. The fair value is determined by an external valuer using an appropriate pricing model.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the “vesting date”). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group’s best estimate of the number of equity instruments that will ultimately vest. The Income Statement charge or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

Notes to the accounts

continued

2 Accounting policies continued

Share based payments continued

The key areas of estimation regarding share based payments are:

- share price volatility; and
- estimated lapse rates.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, the minimum expense recognised is the expense if the terms had not been modified. An additional expense is recognised for any modification which increases the total fair value of the share based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

Cash-settled transactions relate to phantom options, where employees are entitled to a cash payment equivalent to the gain that would have been made by exercising options at notional price over a notional number of shares and then selling the shares at the date of exercise. The ultimate cost of a cash-settled transaction is the fair value of the cash paid at the settlement date. The cumulative cost recognised until settlement date is a liability on the face of the balance sheet and not a component of equity. The fair value of the liability is determined by an external valuer using an appropriate pricing model. All changes in the liability are recognised in profit or loss.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share.

Employee Benefit Trust

The substance of the relationship between the Group and the Employee Benefit Trust indicates that the Trust is a Special Purpose Entity (SPE) controlled by the Group. The activities of the Trust are being conducted on behalf of the Group in order to obtain benefits from its operation and on this basis the assets held by the Trust are consolidated into the Group's financial statements.

Held for sale assets

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sales transaction rather than through continuing use. The condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Interest bearing loans and borrowings

Interest bearing loans and borrowings are recognised initially at fair value, net of transaction costs incurred. Transaction costs are amortised over the life of the facility. Borrowing costs are stated at amortised cost using the effective interest method.

The effective interest method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or a shorter period to the net carrying amount of the financial liability where appropriate.

Interest on borrowing directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use, is added to the cost of those assets, until such time as the assets are substantially ready for their intended use. The Group has not borrowed against qualifying assets and has not capitalised any interest costs.

Derivative financial instruments and hedging

The Group uses derivative financial instruments to manage certain exposures to fluctuations in foreign currency exchange rates and commodity prices in addition to trading purposes. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at fair value. Derivatives relating to unquoted equity instruments are carried at cost where it is not possible to reliably measure their fair value subsequent to initial recognition. Derivatives are carried as assets when the fair value is positive and liabilities when the fair value is negative.

Financial liabilities at fair value through profit or loss are carried on the Balance Sheet at fair value, with realised and unrealised gains or losses arising from changes in fair value recognised in the Income Statement. Derivatives are classified as held for trading and are included in this category. Unrealised gains or losses are calculated by comparing the derivative contract pricing to forward curve data.

The use of derivative financial instruments is explained further in Note 25 and the Principal Risks and Uncertainties section of these financial statements.

Impact of new standards and interpretations

The Group applied for the first time certain standards and amendments, which are effective for annual periods beginning on or after 1 January 2017.

Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses: The objective of this amendment is to outline the basis for the recognition of deferred tax liabilities or assets regarding unrealised losses on debt instruments measured at fair value and in particular the recognition of deferred tax on such items. The interest bearing loan is measured at amortised cost and therefore this standard does not have an impact on the Group.

Amendments to IAS 7 – Disclosure Initiative: The objective of the Disclosure Initiative (amendments to IAS 7) is to require information to enable users of financial statements to evaluate changes in liabilities arising from financial activities. Liabilities arising from financing activities are liabilities for which cash was, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities. Please refer to Note 22 for the disclosure.

The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

The IASB and IFRIC have issued the following standards and interpretations with an effective date after the commencement date of the accounting period for these financial statements:

Title	Effective date (annual periods beginning on or after)
IFRS 9 Financial Instruments (issued 2010 and 2014)	1 January 2018
IFRS 15 Revenue from Contracts with Customers	1 January 2018
IFRS 16 Leases	1 January 2019
Clarifications to IFRS 15 Revenue from Contracts with Customers	1 January 2018
Amendments to IFRS 10 and IAS 28: Sale or contribution of assets between an investor and an associate or joint venture	Deferred
Hedge Accounting and amendments to IFRS 9, IFRS 7 and IAS 39	1 January 2018
Amendments to IFRS 7 and IFRS 9 Mandatory Effective Date and Transition Disclosures	1 January 2018
IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018
Annual improvements to IFRS 2014-2016 Cycle	1 January 2018
Amendments to IFRS 2 – Classification and Measurement of Share-Based Payment Transactions	1 January 2018
IFRIC 23 Uncertainty over Income Tax Treatments	1 January 2019

Management have performed an analysis of IFRS 15 Revenue from Contracts with Customers and concluded that there is no material impact on the recognition of revenue within the Group financial statements. Management have analysed all contracts with customers, and have not identified a material difference to revenue recognition because, other than the delivery of a commodity, no other performance obligations exist.

All other amendments as noted above are not believed to have a material impact on the financial statements of the Group. The Group will adopt these standards on the date at which they become effective. The Company is assessing the impact of IFRS 9 on the valuation of intercompany receivables.

Notes to the accounts

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3 Revenue

Revenue recognised in the Income Statement is analysed as follows:

	2017 £000	2016 £000
Oil sales	86,152	65,360
Gas sales	59,408	23,362
Condensate sales	3,033	3,530
Tariff income	4,331	2,527
Total revenue	152,924	94,779

4 Cost of sales

Cost of sales recognised in the Income Statement is analysed as follows:

	2017 £000	2016 £000
Operating costs	72,077	40,671
Commercial tariffs	44,386	24,524
Depreciation, depletion and amortisation – development and production assets	44,806	22,994
Movement in (underlift)/overlift during the year	(30,729)	6,985
Other cost of sales	1,968	1,492
Total cost of sales	132,508	96,666

5 Asset impairment

Impairment losses

An asset impairment charge of £12,992,000 (2016: £2,923,000) has been recognised during the year. The pre-tax impairment charge and the related movement in deferred tax were as follows:

	Pre-tax impairment £000	Movement in deferred tax £000	Post-tax impact £000
2017			
Brage	3,132	(2,443)	689
Schooner	5,693	(2,277)	3,416
Ketch	4,167	(1,667)	2,500
Total	12,992	(6,387)	6,605
2016			
Jotun	2,223	(1,734)	489
Schooner	200	(80)	120
Enoch	500	(200)	300
Total	2,923	(2,014)	909

The factors that led to the impairments in 2017 were as follows:

Brage: The impairment charge is principally driven by the technical downward revision in reserves. The recoverable amount is £22.6 million.

Schooner: The impairment charge is principally driven by the increase in the abandonment estimate and acceleration of cessation of production. The recoverable amount is deemed to be negligible and therefore was fully written off in 2017.

Ketch: The impairment charge is driven by the increase in the abandonment estimate and the acceleration of cessation of production. The recoverable amount is deemed to be negligible and was therefore fully written off in 2017.

The assumptions used for the impairment review are stated in Note 2.

6 Segmental reporting

The Group operates a single class of business being oil and gas exploration, appraisal, development and production and related activities in a single geographical area presently being Northwest Europe. Revenue from two key customers (2016: two key customers) which individually represent more than 10% of total sales were as follows: £73,988,000 and £8,926,000 arising from sales of oil in Norway and the UK respectively (2016: £45,620,000 and £17,244,000 Norway and UK respectively), £21,191,000 and £34,820,000 arising from sales of natural gas in the UK and Norway respectively (2016: £17,609,000 and £1,092,000 UK and Norway respectively) and £nil arising from sales of condensate in the UK and Norway (2016: £nil for UK and Norway). The Company has negligible revenue.

Capitalised Exploration and Evaluation costs are split £68,661,000 and £339,000 between Norway and UK respectively (2016: £107,208,000 and £168,000). Capitalised Development and Production costs are split £163,312,000 and £37,904,000 between the Norway and UK respectively (2016: £110,676,000 and £45,752,000 between Norway and UK respectively).

7 Group operating loss

	2017 £000	2016 £000
Group operating loss is stated after charging/(crediting)		
Exploration asset write off	21,524	29,908
Asset impairment (Note 5)	12,992	2,923
Pre-award exploration expenditure	4,327	3,560
Depletion, depreciation and amortisation – development and production assets	44,806	22,994
Depreciation of property, plant and equipment – other	373	375
Realised hedging losses/(gains)	1,859	(4,683)
Unrealised hedging (gains)/losses	(369)	13,095
Operating lease payments	927	706
Gain on disposal of asset	(7,229)	–
Other income	(18,843)	–

Other income/(expense) is made up of other income of £18.8 million (2016: £nil), realised hedging losses of £1.9 million (2016: gain £4.7 million) and unrealised hedging gains of £0.4 million (2016: loss £13.1 million). Other income of £18.8 million related to compensation income between Oselvar (Faroe 55%) and Oda (Faroe 15%). £9.1 million of the compensation income was received in June 2017 following PDO approval of the Oda development. A further £9.1 million has been accrued and recognised as income and will be received in 2018 when Oselvar is taken offline. The compensation income is partially offset due to the Group's ownership of Oda, with capex costs of £1.3 million being paid in June 2017 and a further £1.2 million being accrued at the year end reflecting further compensation due to Oselvar for the planned shut down.

The Group made a post-tax gain of £0.7 million (pre tax £7.2 million) on the disposal of Jotun, an asset due for abandonment. The Group paid £1.1 million on completion to Exxon, leading to a reduction in the pre-tax decommissioning provision of £8.2 million (post-tax £1.8 million).

Notes to the accounts

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8 Auditor's remuneration

The Group paid the following amounts to its auditor in respect of the audit of the financial statements and for other services provided to the Group:

	2017 £000	2016 £000
Audit of Group financial statements	95	95
Audit of subsidiaries pursuant to legislation	54	36
Other services – compliance tax services	41	19
Other advisory services	17	–
Other assurance services	–	98
	207	248

Fees paid to Ernst & Young LLP and its associates for non-audit services are not disclosed in the individual accounts of the Company as Group financial statements are prepared which are required to disclose such fees on a Group basis. Fees paid to Ernst & Young LLP and its associates for the audit of Faroe Petroleum plc itself as opposed to the Group in 2017 were £12,000 (2016: £12,000).

9 Finance revenue and cost

	2017 £000	2016 £000
Bank and other interest receivable	730	609
Total interest income for financial assets not at fair value through profit or loss	730	609
Realised exchange gain	4,060	5,814
Total finance revenue	4,790	6,423
Bank interest payable and other loans	(4,898)	(6,429)
Total interest expense for financial assets not at fair value through profit or loss	(4,898)	(6,429)
Unwinding of discount on decommissioning provision	(12,108)	(4,710)
Total finance cost	(17,006)	(11,139)

10 Employment costs

The aggregate payroll costs of staff and Directors were as follows:

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Wages and salaries	11,646	10,836	4,014	4,864
Social security costs	2,248	1,557	805	617
Pension costs	1,323	716	222	373
Share based payments charge (both equity settled and phantom options)	4,948	4,408	2,815	2,479
	20,165	17,517	7,856	8,333

Included in pension costs is a charge of £1,323,000 (2016: £716,000) and £222,000 (2016: £373,000) in respect of the defined contribution scheme for the Group and Company respectively.

The average number of persons employed by the Group (including Executive Directors) during the year was as follows:

	Group 2017 No.	Group 2016 No.	Company 2017 No.	Company 2016 No.
Technical	44	34	8	8
Finance & Commercial	26	24	15	14
Administration	10	10	4	5

Directors' emoluments:

	2017 £000	2016 £000
Directors' emoluments	1,957	2,103
Aggregate contributions to pension schemes ¹ :		
Defined contribution	206	204
Number of Directors accruing benefits under:		
Defined contribution schemes	3	3

The emoluments of the Directors in 2017:

	Fees/basic salary £'000	Annual bonus £'000	Benefits in kind £'000	2017 Total £'000	2016 Total £'000	2017 Pension ¹ £'000	2016 Pension £'000
Aggregate remuneration	1,272	663	22	1,957	2,103	206	204

¹ Pension contributions made to UK Executive Directors in excess of the Annual Allowance or Lifetime Allowance are paid as salary (but such sums are not taken into account when calculating any bonus or option award).

During the year, the Directors made total gains of £1.6 million on the exercise of share options.

Full details of amounts paid to Directors can be found in the Report on Directors' Remuneration.

The emoluments of the Directors in 2016:

	Fees/basic salary £'000	Annual bonus £'000	Benefits in kind £'000	2016 Total £'000	2015 Total £'000	2016 Pension ¹ £'000	2015 Pension £'000
Aggregate remuneration	1,244	841	18	2,103	2,065	204	246

Notes to the accounts

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11 Taxation

(a) Tax on loss on ordinary activities

	2017 £000	2016 £000
Current taxation		
Overseas tax credit	35,610	41,764
UK tax charge	(71)	(214)
Current tax credit	35,539	41,550
Amounts under provided in previous year	138	195
Total current tax credit	35,677	41,745
Deferred taxation		
Origination of temporary differences	(34,660)	(11,316)
Change of tax rate	525	–
Not provided in earlier years	1,843	75
Total deferred tax charge	(32,292)	(11,241)
Foreign exchange differences		
Differences arising from the use of year end and average exchange rates	(1,072)	(1,818)
Total foreign exchange differences	(1,072)	(1,818)
Total tax credit in the Income Statement	2,313	28,686

There are no items charged to equity with any current or deferred tax effect.

(b) Reconciliation of the total tax credit

The tax credit in the Income Statement for the year is lower than the inside ring fence rate of corporation tax in the UK of 40% (2016: 40%). The differences are reconciled below:

	2017 £000	2016 £000
Tax reconciliation		
Loss on ordinary activities before tax	(13,739)	(61,595)
Tax at 40% (2016: 40%)	(5,496)	(24,638)
Expenses not deductible for tax purposes	923	5,268
Prior year adjustments	(1,981)	(270)
Income not taxable	(1,328)	(1,296)
Ring fence expenditure supplement and field allowances	(32)	(77)
Effect of foreign profits/losses charged at different rate of tax	10,725	(10,647)
Effect of profits/losses taxed at 20.0% (2016: 20.0%)	1,068	(1,991)
Foreign exchange differences	(4,379)	(1,058)
Movement in unrecognised deferred tax	1,309	(1,228)
Change of ring fence rate	163	6,163
Other	3,719	2,119
Other adjustments on acquisition	–	1,161
Norwegian allowances uplift	(7,004)	(2,192)
Total tax credit	(2,313)	(28,686)

The 2017 overseas tax credit of £35,610,000 (2016: £41,764,000) represents a tax refund on net exploration expenditure and is due for repayment in November 2018.

The reconciliation of the total tax credit has been based upon the UK ring fence corporation tax rate of 30% (2016: 30%) and the UK supplementary charge which was 10% (2016: 10%) giving a combined rate of 40% (2016: 40%). The UK oil and gas activities of the Group were subject to this rate during 2017.

Group

As at 31 December 2017 the Group has gross ring fence tax losses in the UK of £53,818,000 (2016: £58,128,277) that are available indefinitely for offset against future taxable profits. A deferred tax asset has been recognised in respect of these losses and other deductible temporary differences arising in the UK as it is probable that they will be used in the foreseeable future.

At December 2017, Faroe had carried forward tax capex balances of £107.6 million and carried forward capex uplift of £44.5 million in Norway. In addition, at December 2017, Faroe had carried forward tax losses in Norway of £21.0 million and £14.4 million for corporation tax and special tax respectively.

(c) Unrecognised tax losses

Company

The Company has net excess management expenses of £13,121,000 (2016: £10,087,000). A deferred tax asset has not been recognised in respect of losses as there is uncertainty whether the losses may be used to offset future taxable profits.

(d) Deferred tax liability

The provision for deferred tax liabilities included in the Balance Sheet is as follows:

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Deferred tax liability				
Difference between net book value and tax value	(1,066)	(83,247)	—	—
Recognised deferred tax liability ¹	(1,066)	(83,247)	—	—

¹ The change in the deferred tax liability is not equal to the origination of temporary difference as in Note 11 (a) mainly because of the Business Combination as described in Note 14 and foreign exchange differences.

(e) Deferred tax assets

Deferred tax assets included in the Balance Sheet are as follows:

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Recognised deferred tax assets				
Differences between accumulated depreciation and capital allowances	40,098	164,464	—	—
Tax losses	21,400	34,087	—	—
Other temporary differences	24,468	6,751	—	—
Recognised deferred tax asset	85,966	205,302	—	—

The difference between the net deferred tax asset of £84.9 million and the £114.5 million relates to the deferred tax liability on the Fenja asset, which was classified as held for sale at year end and is disclosed in Note 15.

Unrecognised deferred tax assets

	57	84	57	84
Difference between accumulated depreciation and capital allowances				
Other temporary differences	2,156	2,237	2,156	2,237
Excess management expenses	2,542	2,036	2,542	2,036
Unrecognised deferred tax asset	4,755	4,357	4,755	4,357

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11 Taxation continued

In considering the recoverability of the deferred tax asset in respect of carried forward tax losses at the year end, the Directors have considered that:

- Based on current forecasts, the deferred tax asset in respect of the UK carried forward losses will be fully utilised by 2022;
- The current forecasts are based on the same price assumptions used in the 2017 impairment tests, which are deemed to be reasonable;
- The forecasts are derived from operator budgets and Life of Field models which are reasonable; and
- With regard to the Norwegian carried forward tax losses, the Norwegian Government refund any non-utilised tax losses if the activity of the Company ceases and therefore the asset is recoverable.

12 Earnings per share

Basic earnings per share amounts are calculated by dividing 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 share amounts are calculated by dividing the profit 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 on the conversion of all the dilutive potential Ordinary Shares into Ordinary Shares.

The following reflects the loss and share data used in the basic and diluted loss per share computations:

	2017 £000	2016 £000
Loss attributable to equity holders of the parent	(11,426)	(32,909)

	2017 Thousands	2016 Thousands
Basic weighted average number of shares	365,983	311,583
Dilutive potential of Ordinary Shares granted into share based incentive schemes	–	–
Diluted weighted average number of shares	365,983	311,583

There have been no other transactions involving Ordinary Shares or potential Ordinary Shares between the reporting date and the date of completion of these financial statements.

	2017 Pence	2016 Pence
Loss per share (basic)	(3.1)	(10.5)
Loss per share (diluted)	(3.1)	(10.5)

13 Intangible assets and property, plant and equipment

	Intangible	Property, plant and equipment		
	Exploration and evaluation costs £000	Development and production costs £000	Other £000	Total £000
Group				
Cost				
At 1 January 2016	73,521	377,654	3,279	454,454
Additions	47,516	8,035	418	55,969
Business Combination (Note 14)	–	48,747	–	48,747
Effect of changes to decommissioning assets	–	(92)	–	(92)
Write-offs	(29,908)	–	–	(29,908)
Exchange adjustments	16,247	13,738	65	30,050
At 31 December 2016 and 1 January 2017	107,376	448,082	3,762	559,220
Additions	47,743	93,197	492	141,432
Business Combination (Note 14)	–	8,925	–	8,925
Reclassifications	(58,670)	58,670	–	–
Effect of changes to decommissioning assets	–	(5,014)	–	(5,014)
Write-offs	(21,524)	–	–	(21,524)
Exchange adjustments	(6,068)	(6,343)	(35)	(12,446)
Assets held for sale	–	(47,749)	–	(47,749)
As at 31 December 2017	68,857	549,768	4,219	622,844
Depreciation and impairment				
At 1 January 2016	–	267,060	2,776	269,836
Impairment	–	700	–	700
Depreciation charge for year (Note 4)	–	22,994	375	23,369
At 31 December 2016 and 1 January 2017	–	290,754	3,151	293,905
Impairment	–	12,992	–	12,992
Depreciation charge for year (Note 4)	–	44,806	373	45,179
At 31 December 2017	–	348,552	3,524	352,076
Net book value				
At 31 December 2017	68,857	201,216	695	270,768
At 31 December 2016	107,376	157,328	611	265,315

Notes to the accounts

continued

13 Intangible assets and property, plant and equipment continued

The E&E write-offs in 2017 of £21,524,000 (2016: £29,908,000) relate to licences where active exploration has been completed and commercial reserves have not been discovered.

The carrying amount of the Fenja licence as at 31 December 2017 was £68,214,000 (2016: £52,741,000). The entry into the Fenja licence followed a farm-in deal between Faroe and VNG Norge in February 2013. The licence is located on the Halten Terrace. During the year £12,000,000 was capitalised and the full book value was transferred to D&P at year end following project sanction in December. At the year end, the asset was classified as held for sale and this is discussed in Note 15.

The carrying amount of the Brasse licence as at 31 December 2017 was £34,900,000 (2016: £25,100,000). The Brasse feasibility study was completed during 2017 confirming several attractive development solutions and export routes. During the year £17,400,000 was capitalised.

The carrying amount of the Fogelberg licence as at 31 December 2017 was £19,000,000 (2016: £14,329,000). Fogelberg was discovered in April 2010, with a volume range of 105-530 bcf. A concept for developing the Fogelberg gas discovery has been selected. During the year, £3,760,000 was capitalised; the other movement related to foreign exchange.

On 31 October, the Group acquired an additional 13.9935% interest in the Blane field from JX Nippon Exploration and Production (U.K.) Limited for a cash consideration of \$5.25 million as at 1 January 2017. The net consideration, after adjustments, was \$3.9 million.

On 6 December 2016, the Group acquired a package of interests in producing Norwegian oil and gas assets from DONG E&P Norge AS ("DONG"), which is a 100% wholly owned subsidiary of DONG Energy A/S, for a cash consideration of \$70.2 million. The net consideration on 6 December 2016 after adjustments was £24.7 million. Please refer to Note 14 for further information on the acquisition.

A provision for decommissioning the oil and gas assets is recognised in full when the related facilities are installed. The extent to which a provision is required depends on the legal requirements for decommissioning, the costs, the timing of work and the discount rate to be applied.

Property, plant
and equipment
Other
£000

Company	
Cost	
At 1 January 2016	730
Additions	1
At 31 December 2016 and 1 January 2017	731
Additions	22
At 31 December 2017	753
Depreciation	
At 1 January 2016	566
Charge for year	101
At 31 December 2016 and 1 January 2017	667
Charge for year	48
At 31 December 2017	715
Net book value	
At 31 December 2017	38
At 31 December 2016	64

14 Goodwill

	Group E000
As at 1 January 2017	7,744
Acquisition	1,975
Foreign exchange	(333)
	9,386

Acquisition of increased Blane interest from JX Nippon Exploration and Production (U.K.) Limited

On 31 October 2017, the Group acquired an additional 13.9935% interest in the Blane field from JX Nippon Exploration and Production (U.K.) Limited ("JXN"), which is a 100% wholly owned subsidiary of JX Nippon Oil and Gas Exploration Corporation, for a cash consideration of \$5.25 million as at 1 January 2017. Net consideration after adjustments was \$3.9 million. The acquisition added 2P Reserves of 1 mmboe and increases the Group's aggregate production by approximately 210 economic boepd in 2017. Further, the acquisition is a strategic fit as it is tied into Ula, which is one of Faroe's key hubs.

The acquisition has been accounted for using the acquisition method, with completion of the transaction occurring on 31 October 2017, following settlement of the agreed consideration. For tax purposes, the effective date was 1 January 2017. The acquisition of interests from JXN is deemed to meet the IFRS definition of a business and is accounted for using the acquisition method of accounting in accordance with IFRS 3. A purchase price allocation (PPA) has been performed to allocate the cash consideration to fair value of assets and liabilities from JXN. The PPA is performed as of the acquisition date, 31 October 2017.

Each identifiable asset and liability is measured at its acquisition date fair value based on guidance in IFRS 13. The standard defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly fashion between willing market participants at the measurement date.

Trade receivables are recognised at gross contractual amounts due as they relate to large and creditworthy customers. Historically, there has been no significant uncollectible trade receivables with regard to the product sales of Blane.

The Group consolidated financial statements include the results of the acquired assets for the two month period from the acquisition date.

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continued

14 Goodwill continued

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

	Fair value recognised on acquisition £000
Non-current assets	
Property, plant and equipment: development and production	8,925
	8,925
Current assets	
Trade receivables and inventory	504
Total assets	9,429
Current liabilities	
Accruals	(1,575)
Non-current liabilities	
Provisions	(5,956)
Deferred tax liability	(1,066)
Total liabilities	(8,597)
 Total identifiable net assets at fair value	 832
Goodwill arising on acquisition	1,975
Purchase consideration transferred	2,807
Analysis of cash flows on acquisition	
Net cash acquired with the assets	–
Cash paid	(2,807)
Net cash outflow	(2,807)

The above valuation is based on currently available information about the fair values as at the acquisition date. If new information becomes available within 12 months from the acquisition date, the Company may change the fair value assessment in the PPA, in accordance with IFRS 3.

From the date of acquisition, the assets acquired have contributed £nil million of revenue and £1.0 million to the net profit before tax from the continuing operations of the Group. If the combination had taken place at the beginning of the year, revenue from continuing operations would have been £159.2 million and the loss from continuing operations would have been £13.8 million.

£2.0 million of goodwill was recognised in respect of the assets acquired from JXN, partly because of the requirement to recognise deferred tax assets and liabilities for the temporary difference between the assigned fair values and tax bases of assets acquired and liabilities assumed. Licences under development and licences in production can only be sold in a market after tax. The assessment of fair value of such licences is therefore based on cash flows after tax. Nevertheless, in accordance with IAS 12 Sections 15 and 19, a provision is made for deferred tax corresponding to the tax rate multiplied with the difference between the acquisition cost and the tax base. The offsetting entry to this deferred tax is goodwill. Hence, £1.1 million of the goodwill arises as a technical effect of deferred tax ("technical goodwill"), and the remainder is due to differences in the perceived fair value of the asset between the buyer and seller.

None of the goodwill recognised will be deductible for income tax purposes.

Acquisition related costs of £50,000 have been expensed and are included in administrative expenses in the Income Statement and are part of operating cash flows in the Group Cash Flow Statement.

Acquisition of a package of interests in producing Norwegian oil and gas assets from DONG E&P Norge AS

On 6 December 2016, the Group acquired a package of interests in producing Norwegian oil and gas assets from DONG for cash consideration of \$70.2 million as at 1 January 2016. The net consideration on 6 December 2016 after adjustments was £24.7 million. The Group has acquired interests in five Norwegian North Sea producing oil and gas fields Ula (20%), Tambar (45%), Tambar East Unit (37.8%), Oselvar (55%) and Trym (50%). The acquisition added 2P Reserves of 19.8 mmbbl and increase the Group's aggregate production by approximately 9,900 economic boepd in 2016. Further, the acquisition created a new strategic hub for Faroe, centred around the Ula platform, in a core area in offshore Norway.

The acquisition has been accounted for using the acquisition method, with the Group obtaining control of the acquired assets on 6 December 2016, following settlement of the agreed consideration. For tax purposes, the effective date was 1 January 2016. The acquisition of interests from DONG is deemed to meet the IFRS definition of a business and is accounted for using the acquisition method of accounting in accordance with IFRS 3.

Each identifiable asset and liability is measured at its acquisition date fair value based on guidance in IFRS 13. The standard defines fair value as the price that would be received to sell an asset or transfer a liability in an orderly fashion between willing market participants at the measurement date.

Trade receivables are recognised at gross contractual amounts due as they relate to large and creditworthy customers. Historically, there has been no significant uncollectible trade receivables in DONG.

The Group consolidated financial statements include the results of the acquired assets for the 26 day period from the acquisition date. The fair values of the identifiable assets and liabilities of the acquired assets as at the date of acquisition were:

	Fair value recognised on acquisition £000
Non-current assets	
Property, plant and equipment: development and production	48,747
Deferred tax assets	125,234
	173,981
Current assets	
Trade receivables	13,129
	13,129
Total assets	187,110
Current liabilities	
Accruals	(2,753)
Non-current liabilities	
Provisions	(167,379)
Total liabilities	(170,132)
Total identifiable net assets at fair value	16,978
Goodwill arising on acquisition	7,744
Purchase consideration transferred	24,722
Analysis of cash flows on acquisition	
Net cash acquired with the assets	—
Cash paid	(24,722)
Net cash outflow	(24,722)

From the date of acquisition, the assets acquired have contributed £8.8 million of revenue and £2 million to the net profit before tax from the continuing operations of the Group. If the combination had taken place at the beginning of the year, revenue from continuing operations would have been £185.5 million and the profit from continuing operations would have been £8 million.

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continued

14 Goodwill continued

£7.7 million of goodwill was recognised in respect of the assets acquired from DONG, because of the requirement to recognise deferred tax assets and liabilities for the difference between the assigned fair values and tax bases of assets acquired and liabilities assumed. Licences under development and licences in production can only be sold in a market after tax, based on a decision made by the Norwegian Ministry of Finance pursuant to the Petroleum Taxation Act Section 10. The assessment of fair value of such licences is therefore based on cash flows after tax. Nevertheless, in accordance with IAS 12 Sections 15 and 19, a provision is made for deferred tax corresponding to the tax rate multiplied with the difference between the acquisition cost and the tax base. The offsetting entry to this deferred tax is goodwill. Hence, goodwill arises as a technical effect of deferred tax ("technical goodwill").

None of the goodwill recognised will be deductible for income tax purposes.

Acquisition related costs of £331,897 have been expensed and are included in administrative expenses in the Income Statement and are part of operating cash flows in the Group Cash Flow Statement.

15 Held for sale assets

On 12 February 2018, the Group publicly announced the farm down of the Fenja development asset from a working interest of 25% to 7.5% to Suncor Energy Norge AS for a cash consideration of \$54.5 million due upon completion. The transaction is expected to complete during the first half of 2018. Prior to the year end, the Board had approved plans to farm down the Fenja asset and the transaction is expected to complete within one year of the reporting date.

The major classes of assets and liabilities for the 17.5% interest in Fenja classified as held for sale as at 31 December 2017 are as follows:

	2017 £000
Assets	
Property, plant and equipment: development	47,749
Current assets	3,238
Assets held for sale	50,987
Liabilities	
Current liabilities	(2,255)
Deferred tax liability	(29,599)
Liabilities directly associated with assets held for sale	31,854
Net assets directly associated with assets held for sale	19,133
Amounts included in reserves	
Cumulative translation reserve	(1,915)

16 Financial assets and liabilities

	Cost and net book value 2017 £000	Cost and net book value 2016 £000
Group		
Financial liabilities – current		
Derivative financial instruments	(767)	(1,383)
Company		
Financial assets – non-current		
Loans to subsidiaries	256,269	227,896

Unquoted equity investments are held at cost less impairment charges because the fair value of the financial asset cannot be reliably measured.

17 Investments in subsidiary undertakings

Company Investments in
subsidiary undertakings
£000

Cost and net book value	
At 1 January 2016	48,960
Additions	944
At 31 December 2016	49,904
Additions	1,901
At 31 December 2017	51,805

At 31 December 2017, the subsidiary undertakings of the Company and Group were:

Company	Country of incorporation	Nature of business	Proportion of shares and voting rights held
Føroya Kolvetni P/F	Faroe Islands	Oil and gas exploration	100% ordinary
Faroe Petroleum (U.K.) Limited	England	Oil and gas exploration	100% ordinary
Faroe Petroleum Norge AS	Norway	Oil and gas exploration	100% ordinary
Faroe Petroleum (Energy) Limited	England	Investment activities	100% ordinary
Faroe Petroleum SIP Employment Benefit Trust Limited	England	Employee Benefit Trust company	100% ordinary
Faroe Petroleum Employment Benefit Trust Limited	England	Employee Benefit Trust company	100% ordinary
Faroe Petroleum (ROGB) Limited	England	Oil and gas exploration	100% ordinary

The registered office for each of the English companies above is 30 Crown Place, London, EC2A 4ES, with Faroe Petroleum Norge AS being registered at Badehusgata 37, 4014 Stavanger, Norway and Føroya Kolvetni P/F registered at Arsfrasn 2012, Skras.nr.2688, Faroe Islands.

18 Inventories

	2017 £000	2016 £000
Materials and equipment	10,644	10,456

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19 Trade and other receivables

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Amounts falling due within one year:				
Trade receivables	17,301	21,439	–	–
Restricted cash deposits	7,430	11,828	–	–
Other receivables	70,175	21,994	213	280
Prepayments and accrued income	7,182	7,802	185	182
	102,088	63,063	398	462
Current tax receivable	35,610	41,764	–	–
Total receivables	137,698	104,827	398	462

The current tax receivable in 2017 relates to a tax rebate in Norway of 78% of Norwegian net exploration expenditure.

The restricted cash balance relating to monies held in escrow was \$10,000,000 (£7,430,000) (2016: \$14,539,000, £11,828,000).

The credit quality of trade and other receivables that are neither past due nor impaired is assessed by reference to external credit ratings where available, otherwise historical information relating to counterparty default rates is used.

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Counterparties with internal credit rating	87,476	43,433	213	280
	87,476	43,433	213	280

20 Cash and cash equivalents

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Cash at bank and in hand	108,363	46,731	77,820	12,113
Short-term deposits	40,721	50,038	15,010	40,036
	149,084	96,769	92,830	52,149

Cash at bank earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates. If the Group is required to utilise a deposit, there is access to a deposit at any point in the term. The fair value of cash and cash equivalents is £149,084,000 (2016: £96,769,000). At 31 December 2017, the Group had available £174,558,000 (2016: £108,116,000) of undrawn committed borrowing facilities in respect of which all conditions precedent had been met. The fair value of cash and cash equivalents of the Company is £92,830,000 (2016: £52,149,000).

21 Trade and other payables and current financial liabilities

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Amounts falling due within one year:				
Trade payables	21,569	13,035	213	188
Other payables	515	8,234	730	838
Deferred income	24,999	95	–	–
Accruals	66,906	32,536	576	845
Trade and other payables	113,989	53,900	1,519	1,871
Exploration Financing Facility	32,948	35,845	–	–
Reserve Based Lending Facility	–	–	–	–
Short-term bank borrowing	32,948	35,845	–	–

Exploration Financing Facility (EFF)

This facility, dated 19 December 2016, was granted in favour of Faroe Petroleum Norge AS and has an aggregate commitment of NOK 1.0 billion (approximately £90.3 million). In addition to the committed NOK 1 billion, a further NOK 0.5 billion (£45.1 million) is available on an uncommitted accordion basis. Utilisations can be made under the facility up until 31 December 2019. Interest charged on utilisations is based on the NIBOR rate prevailing at the time and a margin of 1.3% (2016: 1.3%). At 31 December 2017 NOK 365 million (£32.9 million) was utilised under the facility (2016: NOK 380 million (£35.8 million)). The facility is secured against the annual Norwegian tax rebate under which 78% of all allowable expenditure is repaid to the claimant (together with interest thereon) 12 months after the end of the tax year.

Reserve Based Lending Facility (RBL)

This facility, dated 19 December 2016, was granted to Faroe Petroleum (U.K.) Limited and Faroe Petroleum Norge AS. The facility has an aggregate amount of US\$250 million and will amortise over the loan life which matures on 31 December 2023. Interest charged on utilisations is based on the LIBOR, NIBOR or EUROBOR rates (depending on the currency of the drawdown) plus a margin ranging from 3.0% to 4.0% (2016: 3.0% to 4.0%) (depending on the total facility utilised and the contribution by development assets). At 31 December 2017, Faroe Petroleum Norge AS had utilised US\$13.9 million (£10.3 million) (2016: US\$16.4 million (£13.3 million) and 28,968,000DKK (£3.4 million)) as cover for a Letter of Credit and drawn £nil (2016 £nil). Faroe Petroleum (U.K.) Limited had drawn £nil (2016: £nil million) under the facility and had utilised £32.0 million (2016: £29.5 million) as cover for Letters of Credit.

22 Interest bearing loans and borrowings

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Short-term debt:				
Bank loans	32,948	35,845	–	–
Long-term debt:				
Senior loan notes	72,742	–	72,742	–
Total borrowings	105,690	35,845	72,742	–

A maturity analysis showing the ageing profile of the total borrowings is shown in Note 25.

At the year end, the Group's principal credit facilities comprised:

- Short-term debt which is described in Note 21; and
- Senior loan notes which are described below.

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22 Interest bearing loans and borrowings continued

On 21 November 2017, the Group issued a \$100 million senior unsecured bond in the Nordic bond market, with a fixed coupon of 8% payable semi annually. The final maturity is expected on 28 April 2023. The senior notes are listed on the Nordic ABM on 17 January 2018.

	Group 2017 £000
Bonds – net	
Total liability component at 1 January 2017	–
New bond issue	75,915
Foreign exchange	(1,762)
Debt issue costs	(1,920)
Interest charged	509
Total borrowings	72,742

The total interest charged on new bonds has been calculated by applying an effective interest rate of 8.45% to the liability component for the period. The non cash accrual of interest will increase the liability component (as the cash interest is only paid at 8%).

23 Provisions

	Decommissioning provision £000	Other provision £000	Total £000
Group			
At 1 January 2016	85,903	1,215	87,118
Asset acquisition	167,379	–	167,379
Employee benefits	–	1,925	1,925
Additions	1,151	–	1,151
Exchange adjustments	12,034	(24)	12,010
Utilised	(4,121)	(703)	(4,824)
Unwinding of discount (Note 9)	4,710	–	4,710
At 31 December 2016 and 1 January 2017	267,056	2,413	269,469
Asset acquisition	5,956	–	5,956
Disposal (Note 7)	(8,186)	–	(8,186)
Employee benefits	–	586	586
Revisions to abandonment estimates	(5,014)	–	(5,014)
Exchange adjustments	(8,903)	41	(8,862)
Utilised	(667)	(691)	(1,358)
Unwinding of discount (Note 9)	12,108	–	12,108
At 31 December 2017	262,350	2,349	264,699
Current provision	(7,653)	(2,349)	(10,002)
Long-term provision	254,697	–	254,697

	Other provision £000	Total £000
Company		
At 1 January 2016	526	526
Employee benefits	974	974
Utilised	(242)	(242)
At 31 December 2016 and 1 January 2017	1,258	1,258
Employee benefits	340	340
Utilised	(370)	(370)
At 31 December 2017	1,228	1,228

Decommissioning

The total decommissioning provision of £262,350,000 (2016: £267,056,000) relates primarily to the Group's production and development facilities. The decommissioning provision is recorded as the Group's share of the decommissioning cost expected to be incurred. These costs are expected to be incurred at various intervals over the next 18 years. The economic life and the timing of the decommissioning liabilities are dependent on Government legislation, commodity prices and the future production profiles of the production and development facilities. In addition, the costs of decommissioning are subject to inflationary changes in the service costs of third parties.

Other provisions

The provision for employee benefits relates to phantom shares which were awarded as part of the FPIP scheme, and is shown as a current liability. Further details of the FPIP scheme are disclosed in Note 27.

24 Called up share capital

	Group and Company 2017 £000		Group and Company 2016 £000	
Authorised				
366,642,990 (2016: 364,526,610) Ordinary Shares of £0.10	36,664			36,453
Issued and fully paid				
366,642,990 (2016: 364,526,610) Ordinary Shares of £0.10	36,664			36,453
	2017 Thousands	2016 Thousands	2017 £000	2016 £000
Ordinary Shares of £0.10 each				
At 1 January	364,526	268,235	36,453	26,824
Share issue	2,116	96,291	211	9,629
	366,642	364,526	36,664	36,453

At 31 December 2017 the issued share capital of the Company was represented by 366,642,990 Ordinary Shares of £0.10 each (2016: 364,526,610). At 31 December 2017, there were 32,864,958 (2016: 30,370,098) outstanding options under various share option schemes, exercisable over various periods up to 2021, to acquire shares of the Company at prices of £nil (2016: £nil). Further details are contained in Note 27.

Notes to the accounts

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25 Financial instruments, financial risk factors and capital management

Fair value of financial assets and liabilities

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments, including those classified under discontinued operations that are carried in the financial statements.

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Financial assets				
Loans and receivables				
Cash	149,084	96,769	92,830	52,149
Trade and other receivables	87,476	43,433	213	280
Restricted cash	7,430	11,828	–	–
Loans to subsidiaries	–	–	256,269	227,896
Financial liabilities				
Amortised cost				
Trade and other payables	(47,083)	(21,364)	(964)	(1,075)
Derivative financial liabilities	(767)	(1,383)	–	–
Short-term bank borrowing	(32,948)	(35,845)	–	–
Interest bearing loans and borrowings	(71,631)	–	(71,631)	–
	91,561	93,438	276,717	279,250

There is no material difference between the carrying value and the fair value of the financial instruments due to their short-term nature, other than interest bearing loans and borrowings which mature in 2023.

The Group and Company are exposed to financial risks arising out of market risks (e.g. commodity prices, foreign currency exchange rates and interest rates), credit risks and liquidity risks. Details of these areas of risk are described below.

Within the above analysis, only the commodity pricing derivative contracts are deemed to be a level 2 financial instrument within a fair value hierarchy. Derivative financial assets are valued using the year end forward curves for oil and gas and applying those to the open hedge contract at the year end.

As shown below, the interest bearing loans and borrowings are shown as level 1 (quoted prices in active markets) due to the fact that the interest bearing loans and borrowings are listed on the Nordic ABM.

Fair value measurement hierarchy for liabilities as at 31 December 2017

	Date of valuation	Total 2017 £000	Level 1 2017 £000
Liabilities for which fair values are disclosed			
Interest bearing loans and borrowings			
Fixed rate borrowings	31 December 2017	71,631	71,631
		71,631	71,631

(a) Market risk

Market risk is the risk arising from possible market price movements and their impact on the future performance of the business. The Group is currently exposed to commodity price risks in the form of oil and gas prices, movement in foreign currency exchange rates and interest rates. The Company is exposed to movement in foreign currency exchange rates and interest rates.

(i) Commodity price risk

The Group is exposed to commodity price risk. Excluding hedging, adjusted revenue averaged \$46.2 (2016: \$40) per boe and a 10% increase or decrease in oil and gas prices would have an £18,365,000 (2016: £8,779,000) impact on adjusted revenue. Any significant change in commodity prices would lead to cost efficiency measures and therefore the Group has not quantified the impact on profit/(loss) before tax or equity. Therefore, where and when appropriate the Group will put in place suitable hedging arrangements to mitigate the risk of a fall in commodity prices. At December 2017, the Group had entered into hedging arrangements covering approximately 85% of 2018 total expected gas production (on a post-tax production basis) and 41% of expected oil production. The gas hedging contracts are put options and swaps with floors between 35 and 48 pence per therm. The oil hedging contracts are put options with an average strike price of \$55 per barrel. The unrealised hedging gain arising from these instruments was £369,000. The Company is not directly subject to commodity price risk.

(ii) Foreign currency exchange risk

The Group and Company have potential currency exposures in respect of items denominated in foreign currencies relating to transactional exposure in respect of operating costs and capital expenditure incurred in currencies other than the functional currency of operations. Currency risk in respect of non-functional currency expenditure is reviewed by the Board. There are no material currency hedging arrangements in place. Loans to foreign subsidiaries with a functional currency other than British Pounds are denominated in the functional currency of the subsidiaries. Foreign currency exchange differences arising on these loans are recognised in the Company's Income Statement as a gain or loss. In the Group accounts, these differences are taken to equity in such circumstances whereby the subsidiary would be unable to raise funds on the open market.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar and NOK exchange rates, being the currencies which the Group is primarily exposed to, with all other variables held constant, on the Group's loss before tax and the Group's equity.

	Increase/decrease in FX rate £000	Effect on profit/(loss) pre tax £000	Effect on equity £000
2017 – USD	+/-10%	8,692/(8,692)	–
2017 – NOK	+/-10%	19,431/(19,431)	–
2016 – USD	+/-10%	12,231/(12,231)	–
2016 – NOK	+/-10%	23,997/(23,997)	–

(iii) Interest rate risk

The Group is exposed to interest rate risks through the Group's bank loan in Norway and the UK (see Note 21 for terms). The possible effect of changes in interest rates is shown in the table below:

	Increase/ decrease in basis points	Effect on profit/(loss) pre tax £000
2017		
Norwegian kroner	+/-10	643 /(643)
British pounds	+/-10	–/ –
2016		
Norwegian kroner	+/-10	312/(312)
British pounds	+/-10	20/(20)

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25 Financial instruments, financial risk factors and capital management continued

(b) Credit risk

Credit risk is the risk that a customer or partner fails to pay amounts due causing financial loss to the Group and Company. The Group has limited exposure to such credit risk and has put procedures in place to mitigate such risks. The maximum individual exposure for the Group at 31 December 2017 was £nil (2016: £nil). For credit quality of trade and other receivables, please refer to Note 19. The Company had no exposure to credit risk at 31 December 2017 (2016: £nil) from customers or partners. The exposure to subsidiaries failing to repay loans to the Company at 31 December 2017 was £256,269,000 (2016: £227,896,000).

With respect to credit risk arising from the other financial assets of the Group, which comprise cash, short-term investments and derivative financial assets, the Group's exposure to credit risk arises from the default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments. The Group limits its counterparty credit risk on these assets by dealing only with financial institutions with credit ratings of at least A or equivalent.

(c) Liquidity risk

The ability to finance firm commitments and develop the Group's business depends upon: (i) cash flow from the Group's producing assets; and (ii) finance from the capital markets, debt finance, tax rebates (in Norway), farm downs and other means. In the event that sufficient funds are not available to finance the business it would have a material adverse effect on the Group's financial condition and its ability to conduct operations. The Group seeks to mitigate these risks by maintaining a portfolio of oil and gas producing interests in both the UK and Norway. The Board reviews and approves the financial strategy of the Group. Short-term and longer-term cash flow forecasts are reported to senior management and the Board. The Group seeks to maintain strong relations with its banking syndicate and its shareholders.

The table below shows the maturity analysis of the Group's financial liabilities.

	On demand £000	Less than 3 months £000	3 to 12 months £000	1 to 5 years £000	>5 years £000	Total £000
31 December 2017						
Trade and other payables	–	47,032	–	–	–	47,032
Short-term bank borrowing*	–	–	33,959	–	–	33,959
Long-term bank borrowing	–	–	5,930	99,818	–	105,748
31 December 2016						
Trade and other payables	–	21,364	–	–	–	21,364
Short-term bank borrowing*	–	–	38,082	–	–	38,082

*Includes the interest borne on these short-term bank borrowings.

The Company's financial liabilities consist of trade and other payables of £943,000 (2016: £1,026,000) which are due within three months and interest bearing loans and borrowings of £72.7 million (2016: £nil) and mature in 2023.

Capital management

The Group defines capital as the total equity of the Company. The objective of the Group's capital management is to ensure that it makes the maximum use of its capital to support its business and maximise shareholder value. There are no external constraints on the Group's capital.

The Group monitors capital on the basis of the gearing ratio. This ratio is calculated as borrowings divided by total equity. Borrowings include current and non-current debt.

As the Group's primary focus is on exploration, equity is the principal form of funding. The Group's policy is to utilise debt where possible. A committed reserve based lending facility is in place to finance its exploration and production and development assets' operations activity.

The Group's policy is to utilise debt where possible. The EFF banking facility has been arranged in Norway to bridge the tax rebate receivable and the RBL banking facility is in place to finance operations and further growth in the business.

At 31 December 2017 the net debt ratio was 46.8% (2016: 14.5%).

	2017 £'000	2016 £'000
Borrowing	105,690	35,845
Equity	226,002	246,638
Debt ratio	46.8%	14.5%

26 Pension scheme

In the UK and for certain Norwegian employees the Group makes contributions to defined contributions schemes nominated by employees for which the pension cost for the year amounted to £1,323,000 (2016: £716,000). There were accrued contributions of £21,000 (2016: £49,000).

27 Share based payments

During the year, the Company operated three share schemes to incentivise employees: the Faroe Petroleum Co-Investment Plan (CIP), the Share Incentive Plan (SIP); and the Faroe Petroleum Incentive Plan (FPIP), details of which are summarised below:

CIP

Under this plan key employees can invest up to 100% of their bonus in any financial year to purchase Company shares ("Investment Shares"). Investment Shares will be matched by new shares to be issued by the Company dependent upon the Company's performance over a three year period. The maximum match will be 1:1 but on a grossed up basis (i.e. assuming an investment was made on pre-tax basis) but will require the Company to satisfy stretching share price growth targets and be subject to a comparative total shareholder return underpin.

	2017 CIP share awards No	2016 CIP share awards No
Outstanding at beginning of the year	8,673,924	7,570,169
Granted during the year	920,185	2,223,153
Lapsed during the year	(487,017)	(1,119,398)
Forfeited during the year	—	—
Exercised during the year	—	—
Outstanding at the end of the year	9,107,092	8,673,924

The estimated fair value of the share award under the CIP and the inputs used in the Monte Carlo Simulation model to calculate the fair values are as follows. The CIP awards outstanding at 31 December 2017 have a weighted average remaining contractual life of 0.5 years and an exercise price of £nil.

The range of exercise prices for the CIP plan in 2017 was £nil (2016: £nil).

SIP

Under this scheme employees commit to invest a monthly amount of up to an annual maximum of £1,500 through market purchases of the Company's shares and for every share purchased the Company will match it with two Matching Shares. The Matching Shares are released at the end of a three year holding period.

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27 Share based payments continued

FPIP

Under the scheme awards will be granted in the form of whole shares as either Nil-Cost Options or cash equivalent phantom options.

The options will vest after three years, dependent upon the Company's performance over the three year period.

In the case of a Phantom Share, the Award Holder is entitled to receive a cash payment to the extent that the Award has vested. In the case of a Nil-Cost Option, the Award Holder is entitled to exercise the Nil-Cost Option at any time during the Exercise Period to the extent that the option has vested. Options are forfeited if the employee leaves the Group before the options are exercised.

The Group has applied the requirements of IFRS 2 'Share-based payment' and has elected to adopt the exemption to apply IFRS 2 only to awards made after 7 November 2002 and which had not vested on 1 January 2006.

The Group recognised total expenses of £4,947,579 (2016: £4,408,000), all of which related to sharebased payment transactions under the Current Schemes.

Date of grant	Fair value (£)	Share price at grant (£)	Exercise price (£)	Volatility of share price	Expected life (yrs.)	Risk-free rate	Dividend yield
30-May-07	0.47	1.15	0.00	39.82%	3.00	5.73%	0.00%
12-Sep-08	0.63	1.37	0.00	41.53%	3.00	4.50%	0.00%
23-Sep-08	0.60	1.27	0.00	42.47%	3.00	4.52%	0.00%
13-May-10	0.66	1.19	0.00	62.91%	3.00	1.69%	0.00%
19-Nov-10	0.94	1.74	0.00	64.02%	3.00	1.41%	0.00%
12-Apr-11	0.95	1.82	0.00	63.13%	3.00	1.80%	0.00%
22-Dec-11	0.73	1.53	0.00	53.09%	3.00	0.51%	0.00%
28-May-12	0.64	1.56	0.00	45.97%	3.00	0.34%	0.00%
4-Jan-13	0.55	1.39	0.00	43.55%	3.00	0.65%	0.00%
24-Jul-13	0.39	1.12	0.00	39.77%	3.00	0.66%	0.00%
17-Jun-14	0.40	1.26	0.00	35.96%	3.00	1.46%	0.00%
20-Jan-15	0.20	0.69	0.00	35.83%	3.00	0.71%	0.00%
28-Jan-16	0.19	0.49	0.00	39.73%	3.00	0.65%	0.00%
12-Jan-17	0.53	1.00	0.00	43.02%	3.00	0.26%	0.00%
23-Jan-17	0.56	1.06	0.00	42.63%	3.00	0.31%	0.00%
16-Feb-17	0.54	1.10	0.00	42.77%	3.00	0.21%	0.00%

Share Incentive Plan

During 2011 the Group introduced a Share Incentive Plan.

	2017 SIP share awards No	2016 SIP share awards No
Matching Shares outstanding at the beginning of the period	496,148	403,890
Matching Shares purchased during the period	215,340	214,168
Matching Shares forfeited during the period	—	(464)
Matching Shares exercised during the period	(87,748)	(121,446)
Outstanding at the end of the period	623,740	496,148

The estimated fair value of the share award under the SIP and the inputs used in the Black Scholes Simulation model to calculate the fair values are as follows. The SIP awards outstanding at 31 December 2017 have a weighted average remaining contractual life of 1.4 years.

The range of Matching Share exercise prices for the SIP plan in 2017 was £nil (2016: £nil).

Date of grant	Fair value (£)	Share price at grant (£)	Expected life (yrs.)
5-Jan-15	0.60	0.60	3.00
26-Jan-15	0.70	0.70	3.00
25-Feb-15	0.78	0.78	3.00
27-Mar-15	0.84	0.84	3.00
28-Apr-15	0.86	0.86	3.00
26-May-15	0.80	0.80	3.00
26-Jun-15	0.89	0.89	3.00
5-Aug-15	0.80	0.80	3.00
28-Aug-15	0.73	0.73	3.00
30-Sep-15	0.67	0.67	3.00
30-Oct-15	0.72	0.72	3.00
30-Nov-15	0.54	0.54	3.00
31-Dec-15	0.54	0.54	3.00
29-Jan-16	0.53	0.53	3.00
29-Feb-16	0.64	0.64	3.00
31-Mar-16	0.65	0.65	3.00
29-Apr-16	0.79	0.79	3.00
31-May-16	0.74	0.74	3.00
30-Jun-16	0.68	0.68	3.00
29-Jul-16	0.67	0.67	3.00
31-Aug-16	0.66	0.66	3.00
30-Sep-16	0.71	0.71	3.00
31-Oct-16	0.79	0.79	3.00
30-Nov-16	0.75	0.75	3.00
3-Jan-17	1.05	1.05	3.00
31-Jan-17	1.01	1.01	3.00
28-Feb-17	1.03	1.03	3.00
31-Mar-17	1.00	1.00	3.00
28-Apr-17	0.94	0.94	3.00
23-May-17	0.99	0.99	3.00
28-Jun-17	0.84	0.84	3.00
31-Jul-17	0.88	0.88	3.00
31-Aug-17	0.86	0.86	3.00
27-Sep-17	0.97	0.97	3.00
31-Oct-17	1.02	1.02	3.00
30-Nov-17	1.02	1.02	3.00

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27 Share based payments continued

Faroe Petroleum Investment Plan

	2017 FPIP share awards No	2016 FPIP share awards No
Outstanding at the beginning of the period	21,200,028	18,509,001
Granted during the period ¹	6,670,935	6,788,169
Lapsed during the period	(1,684,089)	(1,820,287)
Forfeited during the period	(162,197)	(418,526)
Exercised during the period ²	(2,890,551)	(1,858,329)
Outstanding at the end of the period ³	23,134,126	21,200,028

1 6,670,935 (2016: 6,738,947) relate to award of Nil Cost Options.

2 The range of FPIP exercise prices in 2017 was nil (2016: £nil).

3 The FPIP awards outstanding at 31 December 2017 had a weighted average remaining contractual life of 1.7 years (2016: 2.36 years), with a weighted average exercise price of £nil (2016: £nil).

The estimated fair values of FPIP awards, and the inputs used in the Monte Carlo/ Black Scholes Simulation model to calculate those fair values, are as follows:

Date of grant	Fair value (£)	Share price at grant (£)	Exercise price (£)	Volatility of share price	Expected life (yrs.)	Risk-free rate	Dividend yield
17-Jun-14	0.67	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	0.67	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.26	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.26	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.26	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.07	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.07	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	0.67	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.26	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.26	1.26	0.00	35.98%	3.10	1.46%	0.00%
17-Jun-14	1.07	1.26	0.00	35.98%	3.10	1.46%	0.00%
30-Jun-14	0.64	1.24	0.00	35.84%	3.07	1.42%	0.00%
30-Jun-14	1.24	1.24	0.00	35.84%	3.07	1.42%	0.00%
30-Jun-14	1.24	1.24	0.00	35.84%	3.07	1.42%	0.00%
30-Jun-14	1.03	1.24	0.00	35.84%	3.07	1.42%	0.00%
31-Dec-14	0.04	0.61	0.00	35.16%	2.56	0.65%	0.00%
31-Dec-14	0.60	0.61	0.00	35.16%	2.56	0.65%	0.00%
31-Dec-14	0.60	0.61	0.00	35.16%	2.56	0.65%	0.00%
31-Dec-14	0.34	0.61	0.00	35.16%	2.56	0.65%	0.00%
20-Jan-15	0.37	0.69	0.00	37.18%	3.51	0.81%	0.00%
20-Jan-15	0.68	0.69	0.00	37.18%	3.51	0.81%	0.00%
20-Jan-15	0.68	0.69	0.00	37.18%	3.51	0.81%	0.00%
20-Jan-15	0.58	0.69	0.00	37.18%	3.51	0.81%	0.00%
31-Mar-15	0.45	0.81	0.00	37.18%	3.32	0.73%	0.00%
31-Mar-15	0.81	0.81	0.00	37.18%	3.32	0.73%	0.00%
31-Mar-15	0.81	0.81	0.00	37.18%	3.32	0.73%	0.00%

Date of grant	Fair value (£)	Share price at grant (£)	Exercise price (£)	Volatility of share price	Expected life (yrs.)	Risk-free rate	Dividend yield
31-Mar-15	0.69	0.81	0.00	37.18%	3.32	0.73%	0.00%
8-Jun-15	0.04	0.61	0.00	35.16%	2.13	0.65%	0.00%
8-Jun-15	0.60	0.61	0.00	35.16%	2.13	0.65%	0.00%
8-Jun-15	0.60	0.61	0.00	35.16%	2.13	0.65%	0.00%
8-Jun-15	0.34	0.61	0.00	35.16%	2.13	0.65%	0.00%
15-Jun-15	0.45	0.82	0.00	37.64%	5.11	0.92%	0.00%
15-Jun-15	0.45	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.82	0.82	0.00	37.64%	5.11	0.92%	0.00%
15-Jun-15	0.82	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.82	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.69	0.82	0.00	37.64%	5.11	0.92%	0.00%
15-Jun-15	0.69	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.45	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.82	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.82	0.82	0.00	37.64%	3.11	0.92%	0.00%
15-Jun-15	0.69	0.82	0.00	37.64%	3.11	0.92%	0.00%
30-Jun-15	0.16	0.85	0.00	38.79%	2.07	0.67%	0.00%
30-Jun-15	0.85	0.85	0.00	38.79%	2.07	0.67%	0.00%
30-Jun-15	0.85	0.85	0.00	38.79%	2.07	0.67%	0.00%
30-Jun-15	0.94	0.85	0.00	38.79%	2.07	0.67%	0.00%
30-Jun-15	0.48	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.73	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.48	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.73	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.48	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.73	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.48	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.85	0.85	0.00	37.75%	3.07	0.96%	0.00%
30-Jun-15	0.73	0.85	0.00	37.75%	3.07	0.96%	0.00%
31-Dec-15	0.64	0.54	0.00	44.03%	0.56	0.29%	0.00%
31-Dec-15	0.02	0.54	0.00	43.81%	1.56	0.53%	0.00%
31-Dec-15	0.54	0.54	0.00	43.81%	1.56	0.53%	0.00%
31-Dec-15	0.54	0.54	0.00	43.81%	1.56	0.53%	0.00%
31-Dec-15	0.54	0.54	0.00	43.81%	1.56	0.53%	0.00%
31-Dec-15	0.28	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.45	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.28	0.54	0.00	39.98%	2.56	0.83%	0.00%

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27 Share based payments continued

Date of grant	Fair value (€)	Share price at grant (€)	Exercise price (€)	Volatility of share price	Expected life (yrs.)	Risk-free rate	Dividend yield
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.45	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.28	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.54	0.54	0.00	39.98%	2.56	0.83%	0.00%
31-Dec-15	0.45	0.54	0.00	39.98%	2.56	0.83%	0.00%
30-Jun-16	0.72	0.68	0.00	53.56%	0.07	0.04%	0.00%
30-Jun-16	0.02	0.68	0.00	44.82%	1.07	0.11%	0.00%
30-Jun-16	0.68	0.68	0.00	44.82%	1.07	0.11%	0.00%
30-Jun-16	0.68	0.68	0.00	44.82%	1.07	0.11%	0.00%
30-Jun-16	0.69	0.68	0.00	44.82%	1.07	0.11%	0.00%
30-Jun-16	0.22	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.55	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.22	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.55	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.22	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.68	0.68	0.00	44.30%	2.06	0.08%	0.00%
30-Jun-16	0.55	0.68	0.00	44.30%	2.06	0.08%	0.00%
24-Jul-16	0.73	0.68	0.00	53.56%	0.07	0.04%	0.00%
9-Aug-16	0.31	0.67	–	41.61%	3.00	0.01%	0.00%
9-Aug-16	0.99	0.67	–	41.61%	3.00	0.01%	0.00%
9-Aug-16	0.48	0.67	–	41.61%	3.00	0.01%	0.00%
31-Dec-16	0.06	1.04	0.00	40.80%	0.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	40.80%	0.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	40.80%	0.56	0.00%	0.00%
31-Dec-16	1.14	1.04	0.00	40.80%	0.56	0.00%	0.00%
31-Dec-16	0.36	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	0.86	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	0.36	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	0.85	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	0.27	1.04	0.00	43.70%	1.56	0.00%	0.00%

Date of grant	Fair value (£)	Share price at grant (£)	Exercise price (£)	Volatility of share price	Expected life (yrs.)	Risk-free rate	Dividend yield
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	1.03	1.04	0.00	43.70%	1.56	0.00%	0.00%
31-Dec-16	0.84	1.04	0.00	43.70%	1.56	0.00%	0.00%
10-Apr-17	0.66	1.02	0.00	42.41%	2.33	0.08%	0.00%
10-Apr-17	0.81	1.02	0.00	42.41%	2.33	0.08%	0.00%
30-Jun-17	–	0.83	0.00	34.18%	0.07	0.30%	0.00%
30-Jun-17	0.83	0.83	0.00	34.18%	0.07	0.30%	0.00%
30-Jun-17	0.83	0.83	0.00	34.18%	0.07	0.30%	0.00%
30-Jun-17	0.76	0.83	0.00	34.18%	0.07	0.30%	0.00%
30-Jun-17	0.16	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.66	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.16	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.66	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.16	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.66	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.16	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.83	0.83	0.00	36.28%	1.07	0.29%	0.00%
30-Jun-17	0.66	0.83	0.00	36.28%	1.07	0.29%	0.00%
24-Jul-17	–	0.91	0.00	0.00%	–	0.00%	0.00%
24-Jul-17	0.91	0.91	0.00	0.00%	–	0.00%	0.00%
24-Jul-17	0.91	0.91	0.00	0.00%	–	0.00%	0.00%
24-Jul-17	0.91	0.91	0.00	0.00%	–	0.00%	0.00%
28-Jul-17	0.40	0.86	0.00	42.38%	3.00	0.28%	0.00%
28-Jul-17	1.25	0.86	0.00	42.38%	3.00	0.28%	0.00%
28-Jul-17	0.72	0.86	0.00	42.38%	3.00	0.28%	0.00%
31-Dec-17	0.22	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.13	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	0.22	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.13	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	0.22	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.05	1.05	0.00	26.77%	0.56	0.34%	0.00%
31-Dec-17	1.13	1.05	0.00	26.77%	0.56	0.34%	0.00%
24-Jul-13	0.68	0.61	0.00	39.77%	5.00	0.66%	0.00%
24-Jul-13	0.98	0.88	0.00	39.77%	5.00	0.66%	0.00%
24-Jul-13	1.11	1.00	0.00	39.77%	5.00	0.66%	0.00%

Notes to the accounts

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28 Commitments

Pre-tax capital commitments at the end of the financial year for which no provision has been made, in relation to the Group's licences, amount to £378,516,000 (2016: £69,532,000) as follows:

	2017 £000	2016 £000
Group		
UKCS contracted	428	–
Norway contracted	378,088	69,532
Total	378,516	69,532

Company

As at 31 December 2017, the Company has no future capital commitments (2016: £nil). The Company has provided a guarantee for all the licence costs of its subsidiaries.

29 Obligations under operating leases

Obligations under non-cancellable operating leases for land and buildings are as follows:

	Group 2017 £000	Group 2016 £000	Company 2017 £000	Company 2016 £000
Future minimum lease payments under non-cancellable leases:				
Within one year	587	716	281	281
Two to five years	1,866	1,341	770	1,051
After five years	208	208	208	208
	2,661	2,265	1,259	1,540

Rentals due under operating leases are charged against income on a straight line basis over the term of the lease. In 2017 lease payments (net) of £927,000 (2016: £706,000) were charged against income (see Note 7). The operating leases relate predominantly to office leases with rent payable on a quarterly basis.

30 Related party disclosures

For the purpose of related party disclosure in accordance with IAS 24, only Directors are considered to be key management personnel.

Compensation of key management personnel:

	2017 £000	2016 £000
Short-term employee benefits	2,495	2,383
Post-employment benefits	206	204
Sharebased payment	1,842	1,348
	4,543	3,935

Jorunn Sætre, who is an Independent Non-Executive Director, is currently the Rig Team Leader and manager of the Stavanger office of the engineering support Group AGR which in 2017 provided engineering services of a value of approximately £197,920 (2016: £359,476).

During the year the Company entered into transactions, in the ordinary course of business, with other related parties, all within the Group. Trading balances outstanding at 31 December 2017 with other related parties are as follows:

	2017 £000	2016 £000
Loans to subsidiaries	256,269	226,727

The terms of the loans to subsidiaries are summarised in the table below.

Subsidiary	Loan facility	Maturity	Interest rate
Faroe Petroleum (UK) Limited	£100,000,000	31 December 2018 ¹	LIBOR +3%
Faroe Petroleum Norge AS	NOK 1,560,000,000	31 December 2018 ¹	LIBOR +3%
Faroe Petroleum (ROGB) Limited	£1,000,000	31 December 2018 ¹	LIBOR +3%

¹ These loans only fall due when the subsidiaries' current assets exceed total liabilities (excluding loans payable to the ultimate parent company). Accordingly, the Company has disclosed these receivables as long term due to the fact that these loans are unlikely to be repaid by 31 December 2018.

31 Subsequent events

Farm down of Fenja to Suncor Energy Norge AS

In February 2018, the Company executed a farm-down agreement with Suncor for Licence PL586 in Norway. Under the terms of the farm-down agreement, upon completion 17.5% of the Company's working interest in the Fenja development located in the Norwegian Sea will be sold for a cash consideration of \$54.5 million (excluding tax balances). The Company will retain a 7.5% working interest.

Norwegian exploration licence awards

On 17 January 2018, the Company announced that it has been awarded eight new prospective exploration licences, under the 2017 Norwegian APA licence round on the Norwegian Continental Shelf. Due to the nature of the oil and gas industry it is not possible to quantify the financial effect of these licence awards.

Fogelberg appraisal well in Norwegian Sea

On 5 February 2018, the Company announced that drilling on the Fogelberg appraisal well and contingent side-track 6506/9 – 4A & 4S in the Norwegian Sea had commenced drilling.

Fogelberg equity

Following three separate transactions on the Fogelberg licence PL433, all of which are expected to complete in 1H 2018, Faroe's equity will be 15%, with an effective date of 1 January 2018. The Company's equity at 31 December 2017 was 25%.

Notes to the accounts

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32 Joint operations

Fields in production or under development as at 31 December 2017:

Country	Licence	Block	Field name	Field operator	Field % interest
UK	P.559	204/ 24a,	East Foinaven	B.P. Exploration Operating Company Ltd	10.00
UK	P.803	204/ 25b	East Foinaven	B.P. Exploration Operating Company Ltd	10.00
UK	P039	53/4d	Wissey	Tullow Oil UK Limited	18.75
UK	P611	44/24a	Minke	Engie E&P UK Ltd	5.89
UK	P454	44/29b	Minke	Engie E&P UK Ltd	5.89
UK	P611	44/24a	Orca	Engie E&P UK Ltd	3.24
UK	P454	44/29b	Minke	Engie E&P UK Ltd	5.89
Netherlands	D15	D15	Orca	Engie E&P Nederland B.V	3.24
Netherlands	D18a	D18a	Orca	Engie E&P Nederland B.V	3.24
UK	P516	44/26a	Schooner	Faroe Petroleum (U.K.) Limited	60.00
UK	P453	44/28b	Ketch	Faroe Petroleum (U.K.) Limited	60.00
UK	P520	49/1a	Topaz	RWE Dea UK Limited	7.50
UK	P111	30/3 A Upper	Blane	Repsol Norge AS	44.5
Norway	PL107	6407/7	Njord	Statoil Petroleum AS	7.50
Norway	PL107C	6407/7	Njord	Statoil Petroleum AS	7.50
Norway	PL132	6407/10	Njord	Statoil Petroleum AS	7.50
Norway	PL348	6407/8,9	Hyme	Statoil Petroleum AS	7.50
Norway	PL348b	6407/8	Hyme	Statoil Petroleum AS	7.50
UK	P.219	15/5	Enoch	Repsol Sinopec North Sea Limited	13.86
Norway	PL048D	15/5	Enoch	Repsol Sinopec Resources UK Limited	1.86
Norway	PL053B	30/6	Brage	Statoil Petroleum AS	14.26
Norway	PL055	31/4	Brage	Statoil Petroleum AS	14.26
Norway	PL055B	31/4	Brage	Statoil Petroleum AS	14.26
Norway	PL055D	31/4	Brage Extension	Statoil Petroleum AS	14.26
Norway	PL185	31/7	Brage	Statoil Petroleum AS	14.26
Norway	PL169E	25/8	Ringhorne East	Exxon Expl & Prod Norway AS	7.80
Norway	PL147	3/7	Trym	Faroe Petroleum Norge AS	50.0
Norway	PL274	1/3	Oselvar	Faroe Petroleum Norge AS	55.0
Norway	PL274 CS	1/2	Oselvar	Faroe Petroleum Norge AS	55.0
Norway	PL300	2/1,	Tambar	Aker BP ASA	45.0
Norway	PL065	1/3	Tambar	Aker BP ASA	45.0
Norway	PL019	7/12	Ula	Aker BP ASA	20.0

Exploration acreage and discoveries as at 31 December 2017:

Country	Licence	Block	Field name	Field operator	License % interest
Norway	PL433	6506/9 part, 12 part	Fogelberg	Spirit Energy Norge AS	28.30
Norway	PL644	6506/8,10,11	Iris/Hades	OMV (Norge) AS	20.00
Norway	PL644B	6506/11	Iris/Hades Extension	OMV (Norge) AS	20.00
Norway	PL586	6406/11,12	Fenja	VNG Norge AS	25.00
Norway	PL749	6306/4	Seychelles	Spirit Energy Norge AS	20.00
Norway	PL006C	2/5 part	SE Tor	Faroe Petroleum Norge AS	85.00
Norway	PL405	8/10	Oda	Spirit Energy Norge AS	15.00
Norway	PL627/627B	25/5,6,8,9	Shango	Total E&P Norge AS	20.00
Norway	PL740	30/9, 31/7	Brasse	Faroe Petroleum Norge AS	50.00
Norway	PL740B	31/4.7	Brasse extension	Faroe Petroleum Norge AS	50.00
Norway	PL793	6407/7.8.10 & 11	Portrush	A/S Norske Shell	20.00
Norway	PL836S	6406/2, 3	Yoshi	Wintershall Norge AS	30.00
Norway	PL810	2/1,7/12,8/10	Katie	Faroe Petroleum Norge AS	40.00
Norway	PL870	25/6,9,26/7	Pabow	Statoil Petroleum AS	20.00
Norway	PL881	33/9	Goanna	Wellesley Petroleum AS	30.00
Norway	PL888	6507/7	Canela	Faroe Petroleum Norge AS	40.00
Norway	PL811	7/9, 12, 8/7, 10	Gullaxy	Centrica Resources Norge AS	20.00
Norway	PL825	30/3, 6	Rungne	Faroe Petroleum Norge AS	40.00
Norway	PL845	6609/6, 6610/4,5,6	Grønøy	ConocoPhillips Skandinavia AS	20.00
Ireland	16/23	Corrib East	Slyne basin	Faroe Petroleum (U.K.) Limited	20.00
Part blocks					
Ireland	17/1	48/28.29,30,49/26, 57/3, 4 & 5	Celtic Sea	Faroe Petroleum (U.K.) Limited	100.00 ¹
Blocks 57/7 and					
part blocks 57/6,					
Ireland	17/2	8,9 &12	Celtic Sea	Faroe Petroleum (U.K.) Limited	100.00 ¹

1 Licensing options, not jointly controlled – belongs 100% to the Group.

2 Not jointly controlled – belongs 100% to the Group.

Notes to the accounts

continued

32 Joint operations continued

Fields in production or under development as at 31 December 2016:

Country	Licence	Block	Field name	Field operator	Field % interest
UK	P.558	204/ 24a,	East Foinaven	B.P. Exploration Operating Company Ltd	10.00
UK	P.803	204/ 25b	East Foinaven	B.P. Exploration Operating Company Ltd	10.00
UK	P039	53/4d	Wissey	Tullow Oil UK Limited	18.75
UK	P611	44/24a	Minke	GDF SUEZ E&P UK Ltd	5.89
UK	P454	44/29b	Minke	GDF SUEZ E&P UK Ltd	5.89
UK	P611	44/24a	Orca	GDF SUEZ E&P UK Ltd	3.24
UK	P454	44/29b	Minke	GDF SUEZ E&P UK Ltd	5.89
Netherlands	D15	D15	Orca	GDF Production Nederland B.V	3.24
Netherlands	D18a	D18a	Orca	GDF Production Nederland B.V	3.24
UK	P689	43/30a	Schooner	Faroe Petroleum (U.K.) Limited	6.9
UK	P516	44/26a	Schooner	Faroe Petroleum (U.K.) Limited	53.10
UK	P453	44/28b	Ketch	Faroe Petroleum (U.K.) Limited	60.00
UK	P520	49/1a	Topaz	RWE Dea UK Limited	7.50
UK	P111	30/3 A Upper	Blane	Talisman Energy Norge AS	30.5047
Norway	PL107	6407/7	Njord	Statoil Petroleum AS	7.50
Norway	PL107C	6407/7	Njord	Statoil Petroleum AS	7.50
Norway	PL132	6407/10	Njord	Statoil Petroleum AS	7.50
Norway	PL348	6407/8,9	Hyme	Statoil Petroleum AS	7.50
Norway	PL348b	6407/8	Hyme	Statoil Petroleum AS	7.50
UK	P.219	15/5	Enoch	Talisman Energy Norge AS	12.50
Norway	PL048D	15/5	Enoch	Talisman Energy Norge AS	1.86
Norway	PL053B	30/6	Brage	Statoil Petroleum AS	14.26
Norway	PL055	31/4	Brage	Statoil Petroleum AS	14.26
Norway	PL055B	31/4	Brage	Statoil Petroleum AS	14.26
Norway	PL055D	31/4	Brage Extension	Statoil Petroleum AS	14.26
Norway	PL185	31/7	Brage	Statoil Petroleum AS	14.26
Norway	PL103b	25/7	Jotun	Det norske oljeselskap ASA	3.00
Norway	PL169E	25/8	Ringhorne East	Statoil Petroleum AS	7.80
Norway	PL147	3/7	Trym	Faroe Petroleum Norge AS	50.0
Norway	PL274	1/2, 1/3	Oselvar	Faroe Petroleum Norge AS	55.0
Norway	PL300	2/1,	Tambar	Aker BP	45.0
Norway	PL065	1/3	Tambar	Aker BP	45.0
Norway	PL019	7/12	Ula	Aker BP	20.0

Exploration acreage and discoveries as at 31 December 2016:

Country	Licence	Block	Field name	Field operator	License % interest
UK	P218	15/21a rest, 21f rest	Perth	Deo Petroleum UK Limited	34.62
UK	P588	15/21b rest, 21c all	Perth	Deo Petroleum UK Limited	34.62
UK	P324	14/20c	Lowlander	Faroe Petroleum (U.K.) Limited	100.00 ²
UK	P.2156	15/11 & 15/16f	Fynn	Parkmead E&P Limited	25.00
Norway	PL433	6506/9 part, 12 part	Fogelberg	Centrica Resources Norge AS	25.00
Norway	PL475	6406/3, 6407/1 part	Rodriguez	Wintershall Norge AS	20.00
Norway	PL348C	6407/8	Bister	Statoil Petroleum AS	7.50
Norway	PL644	6506/8,10,11	Aerosmith	OMV (Norge) AS	20.00
Norway	PL644B	6506/11	Aerosmith extension	OMV (Norge) AS	20.00
Norway	PL586	6406/11,12	Pil	VNG	25.00
Norway	PL749	6306/4	Seychelles	Centrica Resources Norge AS	20.00
Norway	PL753	6407/7,8	Zircon	VNG	30.00
Norway	PL006C	2/5 part	SE Tor	Faroe Petroleum Norge AS	85.00
Norway	PL405	7/9,12, 8/7,8,10,11	Butch	Centrica Resources Norge AS	15.00
Norway	PL627/ 627B	25/5,6,8,9	Shango	Total E&P Norge AS	20.00
Norway	PL740	30/9 and 31/7	Brasse	Faroe Petroleum Norge AS	50.00
Norway	PL793	6407/7.8.10 & 11	Portrush	Shell	20.00
Norway	PL794	6407/7 & 10	Rosapenna	Statoil Petroleum AS	20.00
Norway	PL836S	6406/2, 3	Yoshi	Wintershall Norge AS	30.00
Norway	PL810	2/1,7/12,8/10	Katie	Faroe Petroleum Norge AS	40.00
Norway	PL811	7/9, 12, 8/7, 10	Gullaxy	Centrica Resources Norge AS	20.00
Norway	PL825	30/3, 6	Rungne	Faroe Petroleum Norge AS	40.00
Norway	PL845	6609/6, 6610,4,5,6	Grønøy	ConocoPhillips Skandinavia AS	20.00
Norway	PL611	7223/3,6 7224/1,2,3,4,5	Kvalross	Wintershall Norge AS	40.00
Norway	PL716	7318/11,12	Dazzler	Eni Norge AS	20.00
Ireland	16/03	Slyne Basin	Slyne basin	Faroe Petroleum (U.K.) Limited	100.00 ¹

¹ Licensing options, not jointly controlled – belongs 100% to the Group.

² Not jointly controlled – belongs 100% to the Group.

Other information

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Glossary

"APA"	awards in pre-defined areas
"bcf"	billions of standard cubic feet
"boe"	barrels of oil equivalent
"boepd"	barrels of oil equivalent per day
"Contingent Resources"	those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations by application of development projects but which are not currently considered to be commercially recoverable due to one or more contingencies. Contingent Resources are a class of discovered recoverable resources
"EBITDAX"	earnings before interest, taxation, depreciation, amortisation and exploration expenditure (gross profit plus depreciation and impairment on producing assets)
"net to gross ratio"	the total amount of pay footage divided by the total thickness of the reservoir interval
"net to Faroe"	the portion that is attributed to the equity interests of Faroe
"PL"	production licence
"PRMS"	the 2007 Petroleum Resources Management System (PRMS) prepared by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers (SPE) and reviewed and jointly sponsored by the World Petroleum Council (WPC), the American Association of Petroleum Geologists (AAPG) and the Society of Petroleum Evaluation Engineers (SPEE)
"Proved Reserves" or "1P"	those quantities of petroleum, which, by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under defined economic conditions, operating methods, and government regulations. If deterministic methods are used, the term reasonable certainty is intended to express a high degree of confidence that the quantities will be recovered. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate
"Proved + Probable Reserves" or "2P"	when added to 1P, those additional Reserves which analysis of geoscience and engineering data indicate are less likely to be recovered than 1P but more certain to be recovered than 3P. It is equally likely that actual remaining quantities recovered will be greater than or less than the sum of the estimated Proved plus Probable Reserves (2P). In this context, when probabilistic methods are used, there should be at least a 50% probability that the actual quantities recovered will equal or exceed the 2P estimate
"Proved + Probable + Possible Reserves" or "3P"	when added to 2P, those additional reserves which analysis of geoscience and engineering data suggest are less likely to be recoverable than 2P. The total quantities ultimately recovered have a low probability of exceeding the sum of Proved plus Probable plus Possible (3P) Reserves, which is equivalent to the high estimate scenario. In this context, when probabilistic methods are used, there should be at least a 10% probability that the actual quantities recovered will equal or exceed the 3P estimate
"reserves"	reserves are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions. Reserves must further satisfy four criteria: they must be discovered, recoverable, commercial and remaining (as of the evaluation date) based on the development project(s) applied. Reserves are further categorised in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterised by development and production status
"STOIP"	stock tank oil initially in place



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