Falcon Oil & Gas Ltd.

Consolidated Financial Statements
Year Ended 31 December 2013

(Presented in U.S. Dollars)

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Falcon Oil & Gas Ltd.

We have audited the accompanying consolidated financial statements of Falcon Oil & Gas Ltd., which comprise the consolidated statement of financial position as at December 31, 2013 and the consolidated statements of operations and comprehensive loss, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Falcon Oil & Gas Ltd. as at December 31, 2013 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of the disclosures made in Note 2 to the financial statements concerning the Group's ability to continue as a going concern. Further funds will be required to finance the Group's planned work programme and settle historical liabilities. While the Directors are confident of being able to acquire the finance necessary to meet both capital and administrative obligations as they fall due, no committed facilities are in place.

These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Group's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Group was unable to continue as a going concern.

Other Matter

The comparative figures as at December 31, 2012 and for the year then audited were audited by another firm of Chartered Accountants who expressed an unqualified opinion in their report dated April 12, 2013.

BDO LLP

BDO LLP
London

29 April 2014

Falcon Oil & Gas Ltd.
Consolidated Statement of Operations and Comprehensive loss

	Notes	**Year Ended 31 December 2013 $'000**	Year Ended 31 December 2012 $'000
Revenue			
Oil and natural gas revenue	5	**17**	21
		17	21
Expenses			
Exploration and evaluation expenses	6	**(899)**	(1,654)
Production and operating expenses		**(27)**	(37)
Depreciation	14	**(307)**	(342)
General and administrative expenses		**(4,656)**	(6,206)
Share based compensation	19	**(693)**	(2,380)
Restructuring expenses	26	**-**	(792)
Write-down of inventories		**-**	(552)
Foreign exchange gain		**326**	-
Other income		**683**	276
		(5,573)	(11,687)
Results from operating activities		**(5,556)**	(11,666)
Fair value gain / (loss) – outstanding warrants	24	**3,895**	(2,019)
Finance income	7	**601**	81
Finance expense	7	**(2,510)**	(4,111)
Net finance expense		**(1,909)**	(4,030)
Loss and comprehensive loss for the year		**(3,570)**	(17,715)
Loss and comprehensive loss attributable to:			
Equity holders of the company		**(3,411)**	(17,441)
Non-controlling interests		**(159)**	(274)
Loss and comprehensive loss for the year		**(3,570)**	(17,715)
Loss per share attributable to equity holders of the company:			
Basic and diluted	8	**($0.004)**	($0.03)

The notes are an integral part of these consolidated financial statements.

On behalf of the Board:

'Gregory Smith'
Gregory Smith

'Philip O'Quigley'
Philip O'Quigley

Falcon Oil & Gas Ltd.
Consolidated Statement of Financial Position

	Notes	At 31 December 2013 $'000	At 31 December 2012 $'000
Assets			
Non-current assets			
Exploration and evaluation assets	13	**74,517**	74,019
Property, plant and equipment	14	**5,403**	5,703
Trade and other receivables	15 & 29	**77**	778
Restricted cash	17 & 29	**615**	873
		80,612	81,373
Current assets			
Cash and cash equivalents	16	**8,431**	2,884
Trade and other receivables	15	**473**	1,756
		8,904	4,640
Total assets		**89,516**	86,013
Equity and liabilities			
Equity attributable to owners of the parent			
Share capital	18	**382,853**	339,334
Contributed surplus		**42,463**	41,858
Retained deficit		**(350,605)**	(334,279)
		74,711	46,913
Non-controlling interests		**737**	10,882
Total equity		**75,448**	57,795
Liabilities			
Non-current liabilities			
Derivative financial liabilities	24	**448**	5,292
Decommissioning provision	25	**11,138**	10,955
		11,586	16,247
Current liabilities			
Accounts payable and accrued expenses	26	**1,533**	3,122
Convertible debentures	23	**-**	8,773
Derivative financial liabilities	24	**949**	26
Decommissioning provision	25	**-**	50
		2,482	11,971
Total liabilities		**14,068**	28,218
Total equity and liabilities		**89,516**	86,013

The notes are an integral part of these consolidated financial statements.

Falcon Oil & Gas Ltd.
Consolidated Statement of Changes in Equity

	Notes	Share capital $'000	Contributed surplus $'000	Retained deficit $'000	Equity interests of the parent $'000	Non-Controlling interests ("NCI") $'000	Total equity $'000
At 1 January 2012		339,006	39,654	(316,838)	**61,822**	11,156	**72,978**
Issuance of shares to former officer		54	-	-	**54**	-	**54**
Options exercised		274	(122)	-	**152**	-	**152**
Share based compensation		-	2,326	-	**2,326**	-	**2,326**
Net loss for the year		-	-	(17,441)	**(17,441)**	(274)	**(17,715)**
At 31 December 2012		339,334	41,858	(334,279)	**46,913**	10,882	57,795
Private placement	18	23,515	-	-	**23,515**	-	**23,515**
Share based compensation	19	-	693	-	**693**	-	**693**
Transaction with NCI	20	19,804	-	(12,915)	**6,889**	(9,986)	**(3,097)**
Options exercised		200	(88)	-	**112**	-	**112**
Net loss for the year		-	-	(3,411)	**(3,411)**	(159)	**(3,570)**
At 31 December 2013		382,853	42,463	(350,605)	**74,711**	737	**75,448**

The notes are an integral part of these consolidated financial statements.

Falcon Oil & Gas Ltd.
Consolidated Statement of Cash flows

		Year Ended 31 December	
		2013	2012
	Notes	**$'000**	$'000
Cash flows from operating activities			
Net loss for the year		**(3,570)**	(17,715)
Adjustments for:			
Share based compensation		**693**	2,380
Depreciation		**307**	342
Fair value (gain) / loss - outstanding warrants		**(3,895)**	2,019
Net finance expense		**1,909**	4,030
Other		**(383)**	-
Contribution to past costs - Chevron	6	**1,000**	-
Change in non-cash working capital	12	**(854)**	668
Interest paid		**(573)**	(1,061)
Interest received	7	**102**	66
Net cash used in operating activities		**(5,264)**	(9,271)
Cash flows from investing activities			
Decrease / (increase) in restricted cash		**258**	(335)
Exploration and evaluation assets		**(1,964)**	(2,834)
Proceeds from farm-out transaction – NIS		**1,500**	-
Property, plant and equipment		**(32)**	(325)
Net cash used in investing activities		**(238)**	(3,494)
Cash flows from financing activities			
Proceeds from exercise of share options		**112**	152
Proceeds from private placement – March 2013	18	**25,672**	-
Transaction costs relating to private placement – March 2013	18	**(2,157)**	-
Repayment of 11% debenture	23	**(10,197)**	-
Share acquisition in Falcon Oil & Gas Australia Ltd ("**Falcon Australia**")	20	**(3,000)**	-
Transaction costs associated with share acquisition in Falcon Australia	20	**(97)**	-
Net cash from financing activities		**10,333**	152
Change in cash and cash equivalents		**4,831**	(12,613)
Effect of exchange rates on cash & cash equivalents		**716**	139
Cash and cash equivalents at beginning of year		**2,884**	15,358
Cash and cash equivalents at end of year		**8,431**	2,884

The notes are an integral part of these consolidated financial statements.

1. General Information

Falcon Oil & Gas Ltd. ("**Falcon**") is an oil and gas company engaged in the acquisition, exploration and development of unconventional and conventional oil and gas assets. Falcon's interests are located in Australia, Hungary, South Africa and Canada.

Falcon is incorporated in British Columbia, Canada and headquartered in Dublin, Ireland with a technical team based in Budapest, Hungary. Falcon's Common Shares are traded on Toronto's TSX Venture Exchange ("**TSX-V**") (symbol: FO.V); AIM, a market operated by the London Stock Exchange (symbol: FOG) and ESM, a market regulated by the Irish Stock Exchange (symbol: FAC).

The information provided herein in respect of Falcon includes information in respect of its wholly-owned subsidiaries: Mako Energy Corporation, a Delaware company ("**Mako**"); TXM Oil and Gas Exploration Kft., a Hungarian limited liability company ("**TXM**"); TXM Marketing Trading & Service Kft., a Hungarian limited liability company ("**TXM Marketing**"); Falcon Oil & Gas Ireland Ltd., an Irish limited liability company ("**Falcon Ireland**"); Falcon Oil & Gas Holdings Ireland Ltd., an Irish limited liability company ("**Falcon Holdings Ireland**"); Falcon Oil & Gas USA Inc., a Colorado company ("**Falcon USA**"); Falcon Exploration and Production South Africa (Pty) Ltd., a South African limited liability company ("**Falcon South Africa**") and its 98.1% majority owned subsidiary, Falcon Oil & Gas Australia Limited, an Australian limited liability company ("**Falcon Australia**") (collectively, the "**Company**" or the "**Group**").

2. Accounting policies

The significant accounting policies adopted by the Group are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation and going concern

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") issued by the International Accounting Standards Board ("**IASB**") and Interpretations of the IFRS Interpretations Committee.

The Group's consolidated financial statement have been prepared on a going concern basis which assumes that the Group will be able to meet its liabilities as they fall due for the foreseeable future. For the year ended 31 December 2013, the Group incurred a net loss of $3.6 million and operating cash outflows of $5.3 million and as at 31 December 2013, had a retained deficit of $350.6 million.

During the year the Group raised net funds of $23.5 million through a brokered private placement on the AIM and ESM markets. These funds have been used in the year to repay the Group's 11% debenture ($10.2 million), acquire the 25.4% minority interest in Falcon Australia, ongoing operations and to reduce Falcon Australia's Overriding Royalty Interest on the Beetaloo Permits in Australia. As at 31 December 2013 the Group had a cash balance of $8.4 million.

The Group has forward looking cash commitments regarding its exploration licences of $3.5 million and overheads which need to be met within the next 12 months. As a result, notwithstanding the Group's recent fundraising, the Group's ability to continue as a going concern is dependent upon its ability to raise additional capital through the sale of additional Common Shares, other debt or equity instruments, asset dispositions or entering into joint arrangement with third parties. The Directors are confident that further funds can be raised and it is appropriate to prepare the financial statements on a going concern basis. However, there can be no certainty that any of the aforementioned transactions will complete. This indicates the existence of a material uncertainty related to events or conditions that may cast significant doubt about the Group's ability to continue as a going concern and, therefore, that it may be unable to realise its assets and discharge its liabilities in the normal course of business. These financial statements do not include the adjustments that would be required if the Group could not continue as a going concern.

2. Accounting policies (continued)

Historical cost convention

The consolidated financial statements have been prepared on the historical cost basis with the exception of certain derivative financial instruments, share options which are measured at fair value and trade and other receivables that are initially recognised at fair value, and subsequently measured at amortised cost less accumulated impairment losses.

Foreign currency translation

(i) Functional and presentation currency
The consolidated financial statements are presented in United States dollars ("**$**"), the functional currency of all Group entities. All amounts, except as otherwise indicated, are presented in thousands of dollars.

"**CDN$**" where referenced in the financial statements represents Canadian Dollars. "**£**" where referenced in the financial statements represent British Pounds Sterling. "**HUF**" where referenced in the financial statements represents Hungarian Forints. **"A$**" where referenced in the financial statements represents Australian Dollars.

(ii) Transactions and balances
Transactions in foreign currencies are translated to United States dollars, the functional currency of all group entities, at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to United States dollars at the period end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on translation are recognised in the statement of operations and comprehensive loss.

Basis of consolidation

These consolidated financial statements include the accounts of the Company and the accounts of its subsidiaries. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Company's equity. Non-controlling interests consists of the non – controlling interest at the date of the change in ownership plus the non-controlling interest's share of changes in equity since that date.

All of the Company's subsidiaries are wholly owned except for Falcon Australia of which approximately 98.1% of the outstanding Ordinary Shares are owned by Falcon. The consolidated financial statements include non-controlling interests representing the 1.9% portion of Falcon Australia's assets and liabilities not controlled by Falcon. The reporting dates of the Company and its subsidiaries are coterminous.

Intercompany balances and transactions, and any unrealised income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements, except when losses realised on intercompany transactions are evidence of impairment.

Financial assets

The Group classifies its financial assets in the following categories: at fair value through the statement of operations and comprehensive loss, loans and receivables and available-for-sale. The classification depends on the purposes for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(i) Financial assets at fair value through the statement of operations and comprehensive loss
Financial assets at fair value through the statement of operations and comprehensive loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purposes of selling in the short term. Derivatives are also categorized as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if expected to be settled within 12 months; otherwise, they are classified as non-current.

2. Accounting policies (continued)

(ii) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are initially recognised at fair value and subsequently recorded at amortised cost. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. The Group's loans and receivables comprise "trade and other receivables", "cash and cash equivalents" and "restricted cash" in the balance sheet.

(iii) Available-for-sale financial assets
Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They mainly include investments the Group would have in equity securities in which the Group does not have significant influence or control. They are included in non-current assets unless the investment matures or management intends to dispose of it within 12 months of the end of the reporting period.

Available-for-sale financial assets are carried at fair value. Changes in the fair value are recognised in other comprehensive income / loss. When available-for-sale financial assets are sold or impaired the accumulated fair value adjustments previously recognised in equity are included in the statement of operations and comprehensive loss as gains and losses. At 31 December 2013 and 31 December 2012, the Group had no assets categorised within this category.

Trade payables

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

Derivative financial instruments

Derivatives (including embedded derivatives) are initially recognised at fair value of the date a derivative contract is entered into and subsequently re-measured at their fair value at each reporting date. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group has not designated any derivatives as hedges as at 31 December 2013 or 31 December 2012.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related. Changes in the fair value of separable embedded derivatives are recognised immediately in the statement of operations and comprehensive loss.

Warrants

Warrants which do not meet the criteria to be classified as an equity instrument are classified at fair value through the statement of operations and comprehensive loss and are recorded on the statement of financial position at fair value. Transaction costs are recognised in the statement of operations and comprehensive loss as incurred.

Compound financial instruments - debentures

Compound financial instruments issued by the Group where the exercise of the conversion feature does not result in a fixed number of shares being issued for a fixed amount in the functional currency of the Company, are separated into a host contract, the note, and embedded derivatives.

The Group had a 11% convertible redeemable debenture in issue at 31 December 2012. The debentures and all outstanding interest were repaid at maturity, on 30 June 2013.

The liability component of a compound financial instrument is recognised initially at the fair value of a similar liability that does not have an equity conversion option. Subsequent to initial recognition, the liability component of the compound financial instrument is measured at amortised cost using the effective interest method.

2. Accounting policies (continued)

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period.

Overriding Royalty Interest

A financial liability will arise in relation to the Overriding Royalty Interests on the Group's Exploration licence when it becomes likely that an obligation will exist, which would occur when production commences

Call options

A financial liability will be recognised in relation to call options to reacquire overriding royalty interests on the Group's exploration assets when these become contractual under the agreement.

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognised as a deduction from equity, net of any tax effects.

Property, plant and equipment and intangible exploration assets

(i) Recognition and measurement
*- Exploration and evaluation ("**E&E**") expenditures*

Pre-license costs are recognised in the statement of operations and comprehensive loss as part of exploration and evaluation expenses as incurred.

E&E costs, including the costs of acquiring licenses and directly attributable general and administrative costs, initially are capitalised under full cost accounting, as either tangible or intangible exploration and evaluation assets according to the nature of the assets acquired. The costs are accumulated in cost centers by well, field or exploration area pending determination of technical feasibility and commercial viability.

E&E assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, or (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, E&E assets are allocated to cash-generating units.

The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proven reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proven reserves have been discovered. Upon determination of proven reserves, intangible exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from E&E assets to a separate category within tangible assets referred to as oil and natural gas interests.

Proceeds from disposal or farm-out transactions of intangible exploration assets are used to reduce the carrying amount of the assets. When proceeds exceed the carrying amount, the difference is recognised as a gain. When the Group disposes of its full interests, gains or losses are recognised in accordance with the policy for recognising gains or losses on sale of plant, property and equipment.

- Development and production costs

Items of property, plant and equipment, which include oil and gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development and production assets are grouped into cash generated units (**"CGUs"**) for impairment testing. When significant parts of an item of property, plant and equipment, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (major components).

Gains and losses on disposal of an item of property, plant and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised net within "other income" or "other expenses" in the statement of operations and comprehensive loss.

2. Accounting policies (continued)

- Other fixed assets

Costs incurred on office fixtures and fittings are stated at historical cost less accumulated depreciation and any recognised impairment.

(ii) Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognised as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognised in the statement of operations and comprehensive loss as incurred. Such capitalised oil and natural gas interests generally represent costs incurred in developing proved and / or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in the statement of operations and comprehensive loss as incurred.

(iii) Depletion, depreciation and amortisation

The net carrying value of development or production assets is depleted using the unit of production method by reference to the ratio of production in the year to the related proven and probable reserves, taking into account estimated future development and decommissioning costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually.

Proven and probable reserves are estimated using independent reserve engineer reports and represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50% statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and probable and a 50% statistical probability that it will be less. The equivalent statistical probabilities for the proven component of proven and probable reserves are 90% and 10%, respectively.

Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and
- evidence that the necessary production, transmission and transportation facilities are available or can be made available.

Reserves may only be considered proven and probable if the ability to produce is supported by either actual production or a conclusive formation test. The area of reservoir considered proven includes (a) that portion delineated by drilling and defined by gas-oil and / or oil-water contacts, if any, or both, and (b) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geophysical, geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of oil and natural gas controls the lower proved limit of the reservoir.

Reserves which can be produced economically through application of improved recovery techniques (such as fluid injection) are only included in the proven and probable classification when successful testing by a pilot project, the operation of an installed program in the reservoir, or other reasonable evidence (such as, experience of the same techniques on similar reservoirs or reservoir simulation studies) provides support for the engineering analysis on which the project or program was based.

For other assets, depreciation is recognised in the statement of operations and comprehensive loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment of two to twenty five years. For the pipeline, depreciation is recognised in the statement of operations and comprehensive loss on a usage basis over its estimated useful life. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

2. Accounting policies (continued)

Leased assets

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Minimum lease payments made under finance leases are apportioned between the finance expenses and the reduction of the outstanding liability. The finance expenses are allocated to each year during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are operating leases, which are not recognised on the Company's statement of financial position.

Payments made under operating leases are recognised in the statement of operations and comprehensive loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Impairment

(i) Financial assets
A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised within profit or loss in the statement of operations and comprehensive loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost the reversal is recognised in the statement of operations and comprehensive loss.

(ii) Non-financial assets
The carrying amounts of the Company's non-financial assets, other than E&E assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. E&E assets are assessed for impairment when they are reclassified to property, plant and equipment, as oil and natural gas interests, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets, the cash-generating unit (**"CGU"**). The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proven and probable reserves.

2. Accounting policies (continued)

E&E assets are allocated to related CGU when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to producing assets (oil and natural gas interests in property, plant and equipment).

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognised in the statement of operations and comprehensive loss. Impairment losses recognised in respect of CGU are allocated to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

Impairment losses recognised in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation or amortisation, if no impairment loss had been recognised.

Share based compensation

Share based compensation is measured at fair value at the grant date and expensed over the vesting period with a corresponding increase to contributed surplus. The amount recognised as expense is adjusted for an estimated forfeiture rate for options that will not vest, which is adjusted as actual forfeitures occur, until the shares are fully vested. Consideration paid upon the exercise of stock options, together with corresponding amounts previously recognised in contributed surplus, is recorded as an increase to share capital.

Provisions

A provision is recognised if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognised for future operating losses.

(i) Decommissioning provisions
The Company's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of site restoration and capitalised in the relevant asset category.

Decommissioning provisions are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the statement of financial position date. Subsequent to initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognised as finance costs whereas increases / decreases due to changes in the estimated future cash flows are recorded against the related asset. Actual costs incurred upon settlement of the decommissioning provisions are charged against the provision to the extent the provision was established.

(ii) Legal matters
A provision for legal matters is recognised when legal action is threatened or initiated, and management considers it probable that the legal actions will result in an obligation for the Company. The provision is determined based on the expected cash flows, including legal expenses, and considering the time value of money. When the legal matter relates to exploration and evaluation activities, the recognition of the provision and subsequent change in the expected cash flows is recorded in exploration and evaluation assets.

(iii) Restructuring provisions
Restructuring provisions comprise lease fulfillment obligations, employee termination payments and associated costs. Termination benefits are payable when employment is terminated before normal retirement date. The Group recognises these benefits when it is demonstrable committed to terminating the employment of current employees in line with a formal plan. The restructuring provision is classified within accrued expenses.

2. Accounting policies (continued)

Segment reporting

The operating segment is reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (**"CODM"**). The CODM is considered to be the Board of Directors.

Revenue

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the buyer which is usually when legal title passes to the external party. Revenue is measured net of discounts, customs duties and royalties. Royalty income is recognised as it accrues in accordance with the terms of the overriding royalty agreements.

Other income

Other income primarily consists of income from consulting services provided by the Group.

Finance income and expenses

Finance expense comprises interest expense on borrowings, accretion of the discount on provisions, changes in fair value of certain derivatives and impairment losses recognised on financial assets.

Borrowing costs incurred for the construction of qualifying assets are capitalised during the period of time that is required to complete and prepare the assets for their intended use or sale. All other borrowing costs are recognised in the statement of operations and comprehensive loss using the effective interest method. The capitalisation rate used to determine the amount of borrowing costs to be capitalised is the weighted average interest rate applicable to the Company's outstanding borrowings during the period.

Interest income is recognised as it accrues in the statement of operations and comprehensive loss, using the effective interest method.

Foreign currency gains and losses, reported under finance income and expenses, are those related to financing items.

Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the statement of operations and comprehensive loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the statement of financial position method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

2. Accounting policies (continued)

(Loss) / earnings per share

Basic (loss) / earnings per share is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted (loss) / earnings per share is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effect of dilutive instruments such as options granted to employees.

3. Critical accounting estimates and judgments

Preparation of financial statements pursuant to IFRS requires a significant number of judgemental assumptions and estimates to be made. This impacts the income and expenses recognised in the statement of operations and comprehensive loss together with the valuation of the assets and liabilities in the statement of financial position. Such estimates and judgements are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances and are subject to continual re-evaluation. It should be noted that the impact of valuation in some assumptions and estimates can have a material impact on the reported results.

The following are key sources of estimation uncertainty and critical accounting judgements in applying the Group's accounting policies:

Critical judgments
(i) Exploration and evaluation assets
The carrying value of exploration and evaluation assets was $74.5 million at 31 December 2013 (2012: $74.0 million). The Group has determined that there are no indicators of impairment present in accordance with IFRS 6 "Exploration for and evaluation of mineral interests" and thus impairment evaluations were not performed on these assets.

Management's conclusion that no facts or circumstances exist that suggested the exploration and evaluation assets may be impaired required judgment based on experience and the expected progress of current exploration and evaluation activities and the successful completion of farm - out projects.

The critical judgments were:

Falcon will secure participation by a new farm - in or joint venture partner for the development of the Beetaloo exploration permits in Australia. If Falcon is unable to secure participation by a new farm – in or joint venture partner, its ability to develop and realise its investment in the asset could be significantly curtailed.

Makó Trough, Hungary: Under the terms of the agreement with Naftna industrija Srbije jsc ("**NIS**"), NIS will earn 50% of the net production revenues from the initial three wells being drilled in the Algyő Play, and will have an option to acquire a right of first negotiation for future drilling operations in the Algyő Play, sharing any potential future costs and revenue with the Group, on terms to be negotiated. In the event that NIS decide not participate in any further drilling operations in the Algyő Play, Falcon will become responsible for 100% of any exploration and development costs in the Algyő Play under the Makó Production Licence. If the Group were unable to secure participation by a new farm-out or joint venture partner for the development of the Algyő Play, its ability to develop and realise its investment in the asset could be significantly curtailed. This could have an adverse effect on the Group's business, prospects, financial condition and results of operations.

Critical estimates

(ii) Going concern
The consolidated financial statements have been prepared on the going concern basis. In considering the financial position of the Group, the Group has considered the forecasted operating and capital expenditures for the foreseeable future and cash flows relating to its financing. Forecasting those cash flows requires significant judgment when estimating expected operating expenditure, capital expenditure, expected monies to be received from potential farm-in partners and proceeds from share issuances.

3. Critical accounting estimates and judgments (continued)

(iii) Decommissioning Provision
The decommissioning provision represents the Group's best estimate of the costs involved in the various exploration and production licence areas to return them to their original condition in accordance with the licence terms. These estimates include certain management assumptions with regard to future costs, inflation rates and discount rates.

4. Management of capital

The Group's objectives when managing capital are to safeguard its ability to continue as a going concern in order to explore and develop its petroleum and natural gas properties. The Group manages the components of shareholders' equity and its cash as capital, and makes adjustments to these components in response to the Group's business objectives and the economic climate. To maintain or adjust its capital structure, the Group may issue new common shares or debt instruments, or borrow money or acquire or convey interests in other assets. The Group does not anticipate the payment of dividends in the foreseeable future.

The Group's investment policy is to hold excess cash in highly-liquid, short-term instruments, such as rolling deposits with major European, Canadian or United States financial institutions, with initial maturity terms of less than three months from the original date of acquisition, selected with regard to the Group's anticipated liquidity requirements.

5. Segment information

Based on internal reporting information, it was determined that there is one reportable segment. All of the Company's operations are in the petroleum and natural gas industry with its principal business activity being in the acquisition, exploration and development of petroleum and natural gas properties. The Company has producing petroleum and natural gas properties located in Canada and considers the results from its operations to relate to the petroleum and natural gas properties. The Company has unproven petroleum and natural gas interests in Australia, South Africa and Hungary.

The key performance measures reviewed for the segment which management believes are the most relevant information when evaluating the results of the Group are:

- the progress and extent to which farm-out agreements have been executed over the Group's acreage; and
- cash flow, capital expenditure and operating expenses.

An analysis of the geographic areas is as follows:

	Australia $'000	South Africa $'000	Hungary $'000	Ireland $'000	Canada $'000	United States $'000	Total $'000
Year ended 31 December 2013							
Revenue	**-**	**-**	**-**	**-**	**17**	**-**	**17**
Net loss (i)	**(870)**	**(106)**	**(1,940)**	**14**	**(408)**	**(101)**	**(3,411)**
At 31 December 2013							
Capital assets (ii)	**51,444**	**-**	**28,332**	**144**	**-**	**-**	**79,920**

(i) Net (loss) / income attributable to equity holders of the company.
(ii) Capital assets consist of exploration & evaluation assets and property, plant and equipment.

5. Segment information (continued)

	Australia $'000	South Africa $'000	Hungary $'000	Ireland $'000	Canada $'000	United States $'000	Total $'000
Year ended 31 December 2012							
Revenue	-	-	8	-	13	-	21
Net (loss) / income [(i)]	(833)	668	(4,746)	-	(9,767)	(2,763)	(17,441)
At 31 December 2012							
Capital assets [(ii)]	49,873	-	29,665	184	-	-	79,722

(i) Net (loss) / income attributable to equity holders of the company.
(ii) Capital assets consist of exploration & evaluation assets and property, plant and equipment.

6. Exploration and evaluation expenses

Exploration and evaluation expenses consist of:

		For the year ended 31 December	
	Notes	**2013 $'000**	2012 $'000
Exploration and evaluation expenses		**(899)**	(2,654)
Recovery of past cost relating to South Africa	(i)	**-**	1,000
		(899)	(1,654)

(i) On 12 December 2012, Falcon entered into an exclusive cooperation agreement with Chevron to jointly seek exploration opportunities in the Karoo Basin. The Chevron Agreement provides for Falcon to work exclusively with Chevron for a period of five years to jointly seek to obtain exploration rights in the Karoo Basin subject to the parties mutually agreeing participation terms applicable to each right. As part of the Chevron Agreement, Chevron made a cash payment to Falcon of $1 million as a contribution to past costs. This was received in February 2013.

7. Finance income and expense

		For the year ended 31 December	
	Notes	**2013 $'000**	2012 $'000
Finance income			
Interest income on bank deposits		**102**	66
Derivative gains [(i)]	24	**26**	15
Net foreign exchange gain		**473**	-
		601	81
Finance expense			
Effective interest on loans and borrowings		**(2,352)**	(3,721)
Accretion of decommissioning provisions	25	**(158)**	(209)
Net foreign exchange loss		**-**	(181)
		(2,510)	(4,111)
Net finance expense		**(1,909)**	(4,030)

(i) Derivative gains - gains which arose on the convertible debt conversion feature of the debenture repaid as at 30 June 2013.

8. Net loss per share

Basic and diluted loss per share is calculated as follows:

	For the year ended 31 December	
	2013	2012
	$'000	$'000
Loss attributable to equity holders of the company	**(3,411)**	(17,441)
Weighted average number of common shares in issue - (thousands)	**835,951**	695,819
Loss / diluted loss per share	**($0.004)**	**($0.03)**

9. Income taxes

A reconciliation of the expected tax benefit computed by applying the combined federal and provincial Canadian tax rates of 25% (2012: 25%) to the loss before tax to the actual tax result is as follows:

	For the year ended 31 December	
	2013	2012
	$'000	*$'000
Loss before tax	**(3,570)**	(17,715)
Computed income tax benefit	**(893)**	(4,429)
Increase / (decrease) in income taxes resulting from:		
Effect of foreign income tax rates	**225**	93
Change in income tax rates in jurisdictions	**-**	(2,369)
Effect of change in foreign exchange rates	**-**	(234)
Unrecognised benefit of prior period loss carryforwards	**(8)**	1,781
Non-deductible stock based compensation	**173**	603
Derivatives	**(459)**	1,186
Other	**(377)**	82
Change in deferred tax benefits not recognised	**1,339**	3,287
Tax result	**-**	-

* Refer to note 29 - Comparatives

The Group's deductible differences included in the Group's unrecognised deferred tax asset are as follows:

	At 31 December
	2013
	$'000
Trading losses	**125,028**
E&E assets and property, plant and equipment	**174,745**
Other	**1,668**
	301,441

9. Income taxes (continued)

The Group's accumulated trading losses carryforwards as at 31 December 2013 to reduce future years' taxable income are as follows:

	2013 $'000	Expiration
Canada	**32,297**	2015 to 2033
United States	**17,385**	2027 to 2033
Hungary	**75,346**	No expiration
	125,028	

The other deductible temporary differences do not expire under current tax legislation. Deferred tax assets have not been recognised in respect of the tax losses, exploration and evaluation assets and other as it is not probable that future tax profit will be available against which the Group can utilise these benefits in the foreseeable future.

10. Directors' remuneration & transactions with key management personnel

Directors' remuneration is analysed as follows:

Executive directors[(i)]

	Year	Salary $'000	Pension contribution $'000	Other $'000	Bonus $'000	Director fees $'000	[(ii)] Share based payment $'000
Philip O'Quigley[(iii)]	**2013**	**365**	**60**	**6**	**200**	**-**	**172**
(appointed 25 September 2012)	2012	113	20	1	-	-	188
Dr. György Szabó	**2013**	**162**	**-**	**16**	**-**	**-**	**11**
	2012	180	-	17	-	-	112
Robert Macaulay [(iv)]	**2013**	**-**	**-**	**-**	**-**	**-**	**-**
(resigned 25 September 2012)	2012	142	-	-	-	17	84

(i) Directors' remuneration is fixed by the Compensation Committee of the board.

(ii) Share based payments represents the non-cash expense attributable to the relevant options held by each Director. For further details on the fair value calculation of these amounts, refer to note 19.

(iii) Philip O'Quigley was paid a bonus of US$200,000 in May 2013. The bonus was based on the average increase in the weighted market capitalisation of the Group from 1 May 2012 to 30 April 2013.The bonus was not determinable at 31 December 2012.

(iv) Robert Macaulay was appointed President and CEO in November 2010. He stepped down on 1 May 2012 and Philip O'Quigley was appointed on the same day. No amounts have been paid to Robert Macaulay in connection with his termination. Robert Macaulay remained on the Board of Directors as a non-executive Director until his resignation on 25 September 2012. Under the terms of his employment agreement, as President and Interim CEO, Robert Macaulay was awarded 300,000 shares in Falcon Oil & Gas Ltd, which were granted in December 2012. In addition the Group paid the cost of personal taxes relating to the granting of these shares.

10. Directors' remuneration & transactions with key management personnel (continued)

Non - executive directors

	Director fees[i]		Share - based payments[ii]			Other
	2013	2012	**2013**	2012	**2013**	2012
	$'000	$'000	**$'000**	$'000	**$'000**	$'000
John Craven	**48**	48	**102**	35	**-**	-
Daryl Gilbert	**42**	37	**13**	157	**-**	-
JoAchim Conrad	**36**	36	**17**	21	**-**	-
Gregory Smith	**42**	42	**13**	24	**-**	-
Igor Akhmerov [iii]	**42**	42	**123**	15	**137**	-
David Harris (appointed 25 September 2012)	**36**	9	**14**	-	**-**	-
Andrew Morris (resigned 25 September 2012)	**-**	32	**-**	-	**-**	-

(i) Directors' remuneration is fixed by the Compensation Committee of the board.

(ii) Share based payments represents the non-cash expense attributable to the relevant options held by each Director. For further details on the fair value calculation of these amounts, refer to note 19.

(iii) Igor Akhmerov received €100,000 (US$137,000) for consulting services to the Group in 2013.

Transactions with key management comprising Directors and other senior management

Key management personnel comprise the Board of Directors and Senior Management. The remuneration of key management personnel was as follows:

	For the year ended 31 December	
	2013	2012
	$'000	*$'000
Directors' fees	**246**	262
Salaries and other emoluments	**1,295**	1,059
Share based compensation	**625**	1,823
Defined contribution pension plans	**81**	50
Termination benefits	**-**	236
	2,247	3,430

* Refer to note 29 - Comparatives

Remuneration of Directors and Senior Management includes all amounts earned and awarded which are determinable to the Company's Board of Directors and Senior Management.

Senior Management includes the Group's Chief Executive Officer, Chief Financial Officer, the Managing Director of the Group's subsidiary (Falcon TXM) and the Group's Head of Technical and in 2012 the former Chief Operating Officer.

Directors' fees include Board and Committee fees. Short-term wages and benefits include salary, benefits and bonuses earned or awarded during the year. Share-based compensation includes expenses related to the Company's long-term incentive compensation.

11. Compensation expense and auditors' remuneration

(i) Compensation expense

The Company's consolidated statement of operations and comprehensive loss are prepared primarily by nature of expense, with the exception of compensation costs which are included in both exploration and evaluation expenses and general and administrative expenses, share based compensation which is reflected as a separate financial statement component and termination benefits which are reflected in restructuring costs. The following is a summary of total compensation:

	For the year ended 31 December	
	2013	2012
	$'000	*$'000
Exploration and evaluation expenses	**506**	1,004
General and administrative expenses	**2,078**	2,524
Share based compensation	**693**	2,410
Termination benefits	**-**	567
	3,277	6,505

* Refer to note 29 - Comparatives

(ii) Auditors' remuneration

Remuneration of the auditors for the audit of the Group financial statements of Falcon Oil & Gas Ltd and other services to the Group is as follows:

	For the year ended 31 December	
	2013	2012
	$'000	$'000
Audit fees – KPMG	**-**	183
Quarterly review fees – KPMG	**38**	65
Tax fees – KPMG	**-**	81
All other fees - KPMG	**14**	2
	52	331

The Group auditors changed during 2013. With effect from 12 November 2013, BDO LLP of London, United Kingdom ("**BDO**") was appointed as Group auditor. The incumbent, KPMG LLP of Calgary, Canada ("**KMPG**") resigned effective 12 November 2013. Fees presented in the table above are to the date of resignation. The above amounts exclude Canadian / Australian GST and European VAT as applicable. The amounts exclude the reimbursement of expenses.

	For the year ended 31 December	
	2013	2012
	$'000	$'000
Audit fees – BDO	**112**	-
September 2013 quarterly review fees – BDO	**15**	-
Tax fees – BDO	**-**	-
All other fees – BDO(i)	**88**	-
	215	-

(i) Prior to the appointment of BDO as auditors, £41,500 (US$63,252) was paid to PKF Accountants and Business Advisors ("**PKF**"), for works performed in relation to the Group's working capital report for its admission to trading on the AIM market of the London Stock Exchange and the ESM market of the Irish Stock Exchange. PKF subsequently merged with BDO during 2013.

11. Compensation expense and auditors' remuneration (continued)

The above amounts exclude Canadian / Australian GST and European VAT as applicable. The amounts exclude the reimbursement of expenses.

12. Supplemented cash flow information

Changes in non-cash working capital is comprised of:

	For the year ended 31 December	
	2013	2012
	$'000	$'000
Trade and other receivables	**337**	176
Write-down of inventories	**-**	552
Accounts payable and accrued expenses	**(1,191)**	(60)
	(854)	668

13. Exploration and Evaluation assets

	Australia $'000	**South Africa $'000**	**Hungary $'000**	**Total $'000**
At 1 January 2013	**49,873**	**-**	**24,146**	**74,019**
Additions	**1,571**	**-**	**-**	**1,571**
Farm out: net of costs	**-**	**-**	**(916)**	**(916)**
Disposals	**-**	**-**	**(207)**	**(207)**
Reclassification	**-**	**-**	**32**	**32**
Decommissioning provision	**-**	**-**	**18**	**18**
At 31 December 2013	**51,444**	**-**	**23,073**	**74,517**

	Australia $'000	South Africa $'000	Hungary $'000	Total $'000
At 1 January 2012	48,221	-	22,756	70,977
Additions	1,652	-	-	1,652
Disposals	-	-	(140)	(140)
Decommissioning provision	-	-	1,530	1,530
At 31 December 2012	49,873	-	24,146	74,019

E&E assets consist of the Group's exploration projects which are pending the determination of proven or probable reserves. Additions represent the Group's costs incurred on E&E assets during the period.

An impairment of intangible exploration assets, and any eventual reversal thereof, is recognised as additional depletion, depreciation and amortisation expense in the statement of operations and comprehensive loss as impairment of non-current assets.

As at 31 December 2013 and 31 December 2012, there were no indicators of impairment as defined by IFRS 6, and as such no impairment testing was performed.

13. Exploration and Evaluation assets (continued)

Beetaloo Basin, Northern Territory, Australia

Falcon Australia, Falcon's 98.1% owned subsidiary, is the registered holder of four exploration permits covering approximately 7 million acres in the Beetaloo Basin, a sparsely populated area of the Northern Territory.

In April 2011, Falcon Australia entered into a joint venture with Hess Australia (Beetaloo) Pty. Ltd ("**Hess**") whereby Hess agreed to collect seismic data over an area covering three of the four Beetaloo Exploration Permits, excluding an area covering approximately 100,000 acres (approximately 405 km^2) surrounding the Shenandoah-1 well-bore (the "**Hess Area of Interest**").

Under the terms of the E&P Agreement, Hess paid $20.0 million to the Company (i) as a participation fee for the exclusive right to conduct operations for the exploration, drilling, development and production of hydrocarbons from the Hess Area of Interest and (ii) as consideration for warrants to acquire 10,000,000 common shares in the capital of Falcon exercisable from 14 November 2011 through 13 January 2015 at an exercise price of CDN$0.19 per share (the "**Hess Warrants**") (note 24). The $20.0 million of gross proceeds received from Hess in 2011 were reduced by closing costs of $1.3 million resulting in net proceeds of $18.7 million which were allocated $17.7 million to the farm-in transaction and $1 million to the warrants.

In November 2011, Falcon Australia, in accordance with the work program for Permit EP-98, completed the testing and stimulation of the Shenandoah-1 well at its sole cost, and the well has been plugged and abandoned. Falcon Australia provided Hess with the data obtained from these activities, and Hess paid Falcon Australia $2.0 million.

Since the date of the agreement and during 2011 and 2012, Hess acquired 3,490 kilometres of 2D seismic data.

Hess had the option, valid until 30 June 2013, to acquire a 62.5% working interest in the Hess Area of Interest by committing to drill and evaluate five exploration wells at Hess' sole cost, one of which must have been a horizontal well. All costs to plug and abandon the five exploration wells would have been borne solely by Hess. Hess had also agreed, subject to proceeding to the development phase, to carry Falcon Australia, on a first development well, up to a gross cost of $10 million. Costs to drill wells after the five exploration wells and the first development well (and after the initial $10 million) would have been borne 62.5% by Hess and 37.5% by Falcon Australia.

However, Hess did not elect to commit to drilling the five wells required to earn their interest in the Beetaloo permits by the agreed deadline. Therefore, in accordance with the Participation Agreement (as amended), which granted Hess the first extension, failure to elect on time meant that Hess forfeited their right to earn 62.5% in three of the Beetaloo permits. Hess had requested a one month extension to allow them sufficient time to conclude a farm-out deal with a third party. However, the late request by Hess to defer the election date again was unanimously rejected by the Board for reasons outlined below:

- Falcon retained a 100% working interest in the Beetaloo exploration permits which put Falcon in a stronger position going forward;
- Hess had transferred a perpetual, royalty-free and irrevocable licence to Falcon over the 3,490 kilometres of seismic data acquired by them;
- The initial interpretation of 3,490 kilometres of new seismic data, acquired at no cost to Falcon, was extremely encouraging;
- Identification of a shale oil play in the northern part of the permits in addition to the shale gas and conventional plays throughout the acreage;
- Unsolicited interest from major oil and gas companies; and
- Falcon had already granted Hess an extension from August 2012 to June 2013.

Results of Seismic Program in Beetaloo Basin, Australia
As referred to above, under the terms of the 2011 Participation Agreement, in 2011 and 2012 Hess acquired 3,490 kilometres of 2D seismic data investing approximately $80 million during that period at no cost to Falcon. The seismic database, along with existing well data, provides a very solid platform to extrapolate a detailed structural and stratigraphic model for the main parts of the Beetaloo Basin.

13. Exploration and Evaluation assets (continued)

All the necessary elements of a productive unconventional and conventional petroleum system have been identified in multiple shales and sand reservoirs, and it is now clear that the Beetaloo Basin is an active petroleum system.

Three hydrocarbon plays have been identified:

- the shale gas potential in the basin centre;
- a shale oil play in the northern part of the permits; and
- conventional prospects throughout the acreage.

Recent interpretation of the seismic database mapped out several conventional drilling targets that are promising areas of hydrocarbons accumulation in the form of structural closures and traps.

Three (EP-76, EP-98 and EP-117) of Falcon Australia's four Beetaloo Permits were due for renewal at 31 December 2013. Application to extend the permits was made prior to the application due date of 30 September 2013. Receipt of the application has been acknowledged by the Department of Mines and Energy, Northern Territory of Australia. During the first term of the three permits, a significant work program was completed and a major work program is proposed for the period of the renewal. Falcon Australia has met all the Northern Territory Government's requirements for renewal. The renewal process is ongoing.

Karoo Basin, South Africa

Falcon holds a Technical Cooperation Permit ("**TCP**") covering an area of approximately 7.5 million acres (approximately 30,327 km^2) onshore Karoo Basin, South Africa.

The TCP grants Falcon an exclusive right to apply for an exploration right over the underlying acreage. In February 2011, a moratorium on the processing of all new applications relating to the exploration and production of shale gas in the Karoo Basin was put in place, and in April 2011 the processing of all existing applications was suspended whilst the South African Department of Mineral Resources conducted an environmental study on the effects of hydraulic stimulation and developed a system to regulate onshore exploration activities. In September 2012, the South African Government announced a decision to lift the moratorium on the processing of existing shale gas exploration permit applications following the publication of legislation, and consequently the company is awaiting exploration rights to be awarded. The proposed regulations were published in the Republic of South Africa Government Gazette for comment on 15 October 2013.

On 12 March 2014, South Africa's parliament passed "the Mineral and Petroleum Resources Development Amendment Bill" ("**MPRD Bill**") which amends the Mineral and Petroleum Resources Development Act (28 of 2002), South Africa's main petroleum law. This bill has been approved by the National Council of Provinces ("**NCOP**"). The Bill still needs to be sent to President's office for signing. Once it has been signed, a date for the commencement of the amendments will be published in the Government Gazette. Among the proposed changes, the law gives the state a free carried interest of 20% in new gas and oil exploration and production ventures. In addition to this 20% free carried interest, the government introduced a new clause entitling it to further participation in the form of an acquisition at an agreed price or production sharing agreements. No percentage limit on this entitlement has been stated in the amendments. The MPRD Bill stipulates that regulations must be promulgated to give effect to these provisions. The Department of Mineral Resources ("**DMR**") is in the process of formulating regulations, which are likely to limit the time and manner in which the Government will be entitled acquire further participating interests in petroleum operations.

In December 2012, Falcon entered into a cooperation agreement with Chevron Business Development South Africa Ltd. ("**Chevron**") to jointly seek unconventional exploration opportunities in the Karoo Basin. The Chevron Agreement provides for Falcon to work exclusively with Chevron for a period of five years to jointly seek to obtain exploration rights in the Karoo Basin subject to the parties mutually agreeing participation terms applicable to each right.

As part of the Chevron Agreement, Chevron made a cash payment to Falcon of $1 million as a contribution to past costs. This was received in February 2013. All expenditures and recoveries of costs associated with the TCP and with the application for the exploration permit are charged / credited to operations as E&E expenses.

13. Exploration and Evaluation assets (continued)

Makó Trough, Hungary

Falcon began operations in Hungary in 2005 and it is the most developed asset in the Group's portfolio. Falcon's subsidiary, TXM, holds the 35-year Makó Production Licence covering an area of approximately 245,775 acres (approximately 1,000 km^2) located in the Makó Trough, part of the greater Pannonian Basin of central Europe. The Makó Licence is located approximately ten kilometres from the MOL Group owned and operated Algyő field.

The Makó Licence area is transected by existing gas pipelines, including a 12 kilometre gas pipeline built by Falcon in 2007, which together offer potential access to local and international markets.

The Makó Trough contains two distinct plays:

- a play targeting gas prospects in the shallower Algyő Play at depths between 2,300 metres and 3,500 metres; and
- a deeper unconventional play targeting significant contingent resources in the Deep Makó Trough.

In January 2013, Falcon agreed a three-well drilling exploration programme with Naftna industrija Srbije jsc ("**NIS**"), 56% owned by Gazprom Group, to target the Algyő Play ("**the agreement area**"). NIS made a cash payment of $1.5 million to Falcon in 2013, which was recorded net of costs against the carrying amount of the E&E asset in Hungary; and agreed to drill three wells by mid July 2014. NIS will earn 50% of net production from the first three wells, and has the option to participate in any future drilling on terms to be negotiated, after paying Falcon $2.75 million. Falcon is to be fully carried on the drilling and testing of the initial three wells.

If NIS does not fulfill their drilling obligations under the participation agreement, TXM will retain 100% interest in the Agreement Area.

If the NIS earn-in is completed, NIS and TXM will share future exploration, appraisal and development costs and production in the Agreement Area in accordance with their participating interests held under a joint operating agreement.

Drilling operations on the first joint well between NIS and Falcon, Kútvölgy-1, were completed in July 2013, the well having reached total depth ("**TD**") of 3,305 metres. As anticipated, the top of the Algyő Formation was encountered at 2,985 metres, the well then penetrating an alternating sequence of sandstones, siltstones and shales over a gross interval of 320 metres to TD, with gas shows throughout. Two conventional cores were taken and extensive wireline logs were run. No operational problems or accidents occurred during drilling. Technical evaluation of the well results has been concluded. Testing operations on the well have started. The testing objectives are to determine reservoir quality and gas productivity from the target Algyő formation encountered in Kútvölgy-1. As announced by the Group on 3 March 2014, testing operations are anticipated to take 3 months.

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14. Property, plant and equipment

	Canadian natural gas interests $'000	**Pipeline and facilities $'000**	**Furniture and equipment $'000**	**Total $'000**
Cost:				
At 1 January 2013	**466**	**4,284**	**2,647**	**7,397**
Additions	**-**	**-**	**32**	**32**
Decommissioning provision	**-**	**7**	**-**	**7**
Reclassification	**-**	**(57)**	**25**	**(32)**
At 31 December 2013	**466**	**4,234**	**2,704**	**7,404**
Depreciation:				
At 1 January 2013	**(466)**	**-**	**(1,228)**	**(1,694)**
Depreciation	**-**	**-**	**(307)**	**(307)**
At 31 December 2013	**(466)**	**-**	**(1,535)**	**(2,001)**
Net book value:				
At 31 December 2013	**-**	**4,234**	**1,169**	**5,403**

	Canadian natural gas interests $'000	Pipeline and facilities $'000	Furniture and equipment $'000	Total $'000
Cost:				
At 1 January 2012	466	3,831	3,385	7,682
Additions	-	-	375	375
Decommissioning provision	-	453	-	453
Disposals	-	-	(1,113)	(1,113)
At 31 December 2012	466	4,284	2,647	7,397
Depreciation				
At 1 January 2012	(466)	-	(1,992)	(2,458)
Depreciation	-	-	(342)	(342)
Disposals	-	-	1,106	1,106
At 31 December 2012	(466)	-	(1,228)	(1,694)
Net book value:				
At 31 December 2012	-	4,284	1,419	5,703

15. Trade and other receivables

		At 31 December
	2013	2012
	$'000	$'000
Non-current		
Deposits	**73**	71
Other Prepayments	**4**	707
	77	778

			At 31 December
		2013	2012
	Note	**$'000**	$'000
Current			
Accounts receivable		**2**	8
Chevron receivable	6	**-**	1,000
Deposits		**41**	39
Prepayments		**266**	330
GST/ VAT receivable		**23**	339
Other receivables		**141**	40
		473	1,756

16. Cash and cash equivalents

Cash and cash equivalents includes cash on hand, deposits held on call with banks, other short term highly liquid investments with initial maturities of three months or less at inception and bank overdrafts where a legal right of offset exists. Bank overdrafts where no legal right of offset exists are shown within borrowings in current liabilities in the statement of financial position.

17. Restricted cash

Restricted cash includes cash held by financial institutions as collateral for ongoing Group operations.

18. Share capital

As at 31 December 2013 and 2012, the Company was authorised to issue an unlimited number of common shares, without par value. The following are the rights, preferences and restrictions attaching to the common shares:

- The Shareholders are entitled to one vote per Common Share at a shareholder meeting;
- The Company's articles do not impose any pre-emptive rights upon the transfer of the Common Shares;
- Subject to the Business Corporation Act (British Columbia, Canada) (**"BCA"**) and any regulatory or stock exchange requirements applicable to the Company, the articles of the Company do not contain any provisions relating to mandatory disclosure of an ownership interest in the Common Shares above a certain threshold;
- Shareholders are entitled to receive, on a pro rata basis, such dividends, if any, as and when declared by Falcon's board of directors at its discretion from funds legally available therefor, and upon the liquidation, dissolution or winding up of Falcon are entitled to receive on a pro rata basis the net assets of Falcon after payment of debts and other liabilities, in each case subject to the rights, privileges, restrictions and conditions attaching to any other series or class of shares ranking senior in priority to or on a pro rata basis with the holders of Common Shares with respect to dividends or liquidation. All rights are the same for residents or non-residents of Canada;

18. Share capital (continued)

- Annual general meetings must be held at least once in each calendar year and not more than 15 months after the last annual reference date. The directors may, whenever they see fit, call a meeting of Shareholders. The Company must send notice of the shareholder meeting at least 21 days before the meeting. A quorum for a meeting of Shareholders is two persons who are, or who represent by proxy, Shareholders who, in the aggregate, hold at least 5% of the issued shares entitled to be voted at the meeting. If there is only one Shareholder entitled to vote at a meeting of Shareholders, the quorum is one person who is, or who represents by proxy, that Shareholder, present in person or by proxy, may constitute the meeting;
- Pursuant to the BCA, the Company may by special resolution of the Shareholders vary or delete any special rights or restrictions attached to the Common Shares.

The following is a reconciliation of issued and outstanding common shares:

	Number of shares	**Share capital $'000**
At 1 January 2012	695,654,500	339,006
Options exercised	1,000,000	274
Issuance of shares to a former officer	300,000	54
At 31 December 2012	**696,954,500**	**339,334**
Private Placement – March 2013	**120,381,973**	**25,672**
Private Placement – March 2013 - expenses	**-**	**(2,157)**
	120,381,973	*23,515*
Shares issued to settle acquisition of Falcon Australia shares	**103,401,044**	**19,901**
Transaction costs associated with share acquisition in Falcon Australia	**-**	**(97)**
	103,401,044	*19,804*
Options exercised	**800,000**	**200**
At 31 December 2013	**921,537,517**	**382,853**

In Quarter 3 2012, the Company issued 600,000 Common Shares and subsequently in December 2012 issued 400,000 Common shares pursuant to exercises of stock options.

In December 2012, the Company issued 300,000 Common Shares to a former employee pursuant to his employment agreement.

On 14 March 2013 the Group announced its application for admission to trading on the AIM market of the London Stock Exchange and the ESM market of the Irish Stock Exchange, of the Company's existing share capital and an additional 120,381,973 new common shares in the capital of the Company issued pursuant to the concurrent conditional brokered private placement at a price of £0.14 (CDN$0.215) per share, raising gross proceeds of $25.7 million (£16.9 million). Trading in these shares commenced on AIM and ESM on 28 March 2013.

See note 20 for details of the acquisition of shares in Falcon Australia.

19. Share based compensation

The Group, in accordance with the policies of the TSX-V, may grant options to directors, officers, employees and consultants, to acquire up to 10% of the Company's issued and outstanding common stock. The exercise price of each option is based on the market price of the Company's stock at the date of grant, which may be discounted in accordance with TSX-V policies. The exercise price of all options granted to date has been based on the market price of the Company's stock at the date of grant, and no options have been granted at a discount to the market price. 6.9 million options granted in April 2013 were granted at a premium to the market price on the day of grant. The remaining 3 million granted in April 2013 were granted with reference to the market price. The options can be granted for a maximum term of five years. The Company records compensation expense over the vesting period based on the fair value at the grant date of the options granted. These amounts are recorded as contributed surplus.

Any consideration paid on the exercise of these options together with the related contributed surplus associated with the exercised options is recorded as share capital. The Group incurred share based expense of $0.7 million during the year ended 31 December 2013 (2012: $2.4 million).

During the year, the Company granted 9.9 million options at an average exercise price of CDN$0.23 (2012: 6 million at CDN$0.10) per option. The options granted during 2013 and 2012 all vest 1/3 equally at the anniversary date over three years.

A summary of the Group's stock option plan as of 31 December 2013 and 31 December 2012 and changes during the periods then ended, is presented below:

	Year ended 31 December 2013		Year ended 31 December 2012	
	Number of options	**Weighted average exercise price CDN$**	Number of options	Weighted average exercise price CDN$
Outstanding as at beginning of period	**32,837,000**	**0.35**	29,764,500	0.41
Granted	**9,900,000**	**0.23**	6,000,000	0.10
Expired	**(6,985,000)**	**1.15**	(978,333)	0.73
Forfeited	**-**	**-**	(949,167)	1.10
Exercised	**(800,000)**	**0.15**	(1,000,000)	0.15
Outstanding as at end of period	**34,952,000**	**0.16**	32,837,000	0.35
Exercisable as at end of period	**21,052,000**	**0.14**	21,323,667	0.48

The exercise prices of the outstanding options are as follows:

Date of grant	**Options**	**Exercise price CDN$**	**Date of Expiry**	**Weighted average contractual life remaining (years)**
30 August 2010	3,312,000	0.170	30 August 2015	1.66
23 May 2011	15,590,000	0.145	23 May 2016	2.39
1 June 2011	150,000	0.145	1 June 2016	2.42
1 May 2012	6,000,000	0.100	1 May 2017	3.33
30 April 2013	3,000,000	0.215	29 April 2018	4.33
30 April 2013	6,900,000	0.240	29 April 2018	4.33
	34,952,000			

19. Share based compensation (continued)

The fair value of the granted options in 2013 and 2012 was estimated using a Black Scholes model with the following inputs:

	2013	2012
Fair value as at grant date	**CDN$0.13 – CDN$0.12**	CDN$0.08
Share price as at grant date	**CDN$0.195**	CDN$0.10
Exercise price	**CDN$0.215 - CDN$0.24**	CDN$0.10
Volatility	**97%**	104%
Expected option life	**3.82 years**	5 years
Dividends	**Nil**	Nil
Risk - free interest rate	**1.075%**	1.59%

During the year ended 31 December 2012, of the $2.4 million charge, $1.1 million was as a result of allowing former Denver employees to retain their vested and unvested options in accordance with the terms of the original grant although they were made redundant. This was treated as accelerated vesting and modification under IFRS 2 “Share based payment”. The fair value of the modification was estimated using a Black Scholes model with the following weighted average inputs:

	2012
Fair value as at modification date	CDN$0.00 – CDN$0.08
Share price	CDN$0.12
Exercise price	CDN$0.145 – CDN$1.00
Volatility	91% - 106%
Option life	0.08 years – 3.92 years
Dividends	Nil
Risk-free interest rate	1.02% – 1.15%

20. Transaction with non-controlling interests

During 2013, Falcon acquired an additional 25.4% in its majority owned subsidiary Falcon Australia, bringing Falcon’s shareholding in this subsidiary to 98.1%. The non-controlling interests in Falcon Australia were 1.9% at 31 December 2013. The details reflecting this transaction in equity are as follows:

	Notes	**Share Capital $’000**	**Retained deficit $’000**	**Equity interests of the parent $’000**	**Non-Controlling interests $’000**	**Total equity $’000**
Cash consideration to Sweetpea	(i)	-	-	**-**	(3,000)	**(3,000)**
Issue of 97,860,000 shares to Sweetpea	(i)	18,830	-	**18,830**	(18,830)	**-**
Issue of 5,541,044 shares to acquire 1.2% of Falcon Australia	(ii)	1,071	-	**1,071**	(1,071)	**-**
Expenses associated with the issue of shares		(97)	-	**(97)**	-	**(97)**
Transaction with non – controlling interests	(iii)	-	(12,915)	**(12,915)**	12,915	**-**
		19,804	**(12,915)**	**6,889**	**(9,986)**	**(3,097)**

*(i) Acquisition of the 24.2% shareholding of Sweetpea Petroleum Pty Ltd (“**Sweetpea**”) in Falcon Australia*
During 2013, Falcon completed an agreement with Sweetpea, a wholly-owned subsidiary of PetroHunter Energy Corporation, to acquire its 50 million shares or 24.2% interest in Falcon Australia. Falcon’s shareholding in Falcon Australia increased to 200 million shares representing 96.9% of the issued share capital of Falcon Australia increasing from 150 million shares (72.7%).

20. Transaction with non-controlling interests (continued)

The terms of the Agreement included:

- cash consideration of $3 million, together with:
- the issue of 97.9 million Falcon shares ("**New Falcon Shares**") to Sweetpea. Based on Falcon's share price, at the time the share purchase was agreed between the parties of CDN$0.20, the total value of the consideration was CDN$22.6 million ($21.8 million).

Upon completion of the Agreement, Sweetpea's shareholding in the enlarged share capital of Falcon was 10.7%. The transaction closed on 17 July 2013. The New Falcon Shares will be held in an Escrow account with the New Falcon Shares locked up for three years, and Sweetpea, commencing from the date of closing, being permitted to sell 15% each year during the lock up period.

(ii) Acquisition of an additional 1.2% shareholding in Falcon Australia
On 24 July 2013, Falcon offered to purchase shares from certain of the remaining shareholders in Falcon Australia. The offer comprised of 2.25 common shares in Falcon for every one Falcon Australia ordinary share held. The valuation used in this offer was the same as used in the acquisition of Sweetpea's 24.2% holding in Falcon Australia. 1.2% of Falcon Australia's shareholders accepted the offer. As a result of this transaction, 5,541,044 new Falcon common shares were issued.

(iii) Transaction with non – controlling interests
This reflects the changes of Falcon's ownership in Falcon Australia. Changes in Falcon's ownership are accounted for as equity transactions, as Falcon Australia is already a majority controlled subsidiary. These entries reflect the change in the non-controlling interests in Falcon Australia reducing from 27.3% prior to the acquisition of the Sweetpea and other minority shareholders' shares to the remaining 1.9% held by the non – controlling interests.

21. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and / or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(i) *Cash & cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses*
The fair value of cash & cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. As at 31 December 2013 and 31 December 2012, the fair value of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses approximated their carrying value due to their short term to maturity.

(ii) *Derivatives*
The fair value of the private placement warrants, Hess warrants and the incentive stock options granted to employees is calculated using a Black Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behavior), expected dividends, and the risk-free interest rate (based on government bonds). A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of incentive stock options that vest.

(iii) *Convertible debentures*
The fair value of host contract of the convertible debentures was determined for disclosure purposes by calculating the present value of the expected future cash flow using the market rate of interest at the relevant reporting date.

22. Financial Instruments and risk management

(i) Fair Value

The following tables provide fair value measurement information for financial assets and liabilities as at 31 December 2013 and 2012. The carrying value of cash and cash equivalents, restricted cash, accounts receivable, and accounts payable and accrued expenses included in the consolidated statement of financial position approximate fair value due to the short term nature of those instruments.

	31 December 2013		31 December 2012	
	Carrying value $'000	**Fair value $'000**	Carrying value $'000	Fair value $'000
Financial assets:				
Cash and cash equivalents including restricted cash	**9,046**	**9,046**	3,757	3,757
Loans and receivables:				
Accounts receivable	**550**	**550**	*2,534	*2,534
Financial Liabilities:				
Other financial liabilities				
Accounts payable and accrued expenses	**1,533**	**1,533**	3,122	3,122
Convertible debentures	**-**	**-**	8,773	11,014

* Refer to note 29 - Comparatives

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

Level 1 Fair Value Measurements
- Level 1 fair value measurements are based on unadjusted quoted market prices.

Level 2 Fair Value Measurements
- Level 2 fair value measurements are based on valuation models and techniques where the significant inputs are derived from quoted indices.

Level 3 Fair Value Measurements
- Level 3 fair value measurements are based on unobservable information. No financial assets or liabilities have been valued using the Level 3 fair value measurements.

22. Financial Instruments and risk management (continued)

	Carrying amount $'000	Fair value $'000
31 December 2013		
Financial liabilities:		
Private placement warrants	949	949
Hess warrants	448	448
31 December 2012		
Financial liabilities:		
Conversion feature – convertible debt	26	26
Private placement warrants	4,505	4,505
Hess warrants	787	787

All instruments in the table are Level 2 instruments. Refer to note 24 for further details.

(ii) Financial risk disclosures

The Company thoroughly examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include credit risk, liquidity risk, market risk and other price risks. Where material, these risks are reviewed and monitored by the Board of Directors.

Credit Risk
The Company's credit risk is limited to cash, receivables and restricted cash. The Group maintains cash accounts at five financial institutions. The Group periodically evaluates the credit worthiness of financial institutions. The Group believes that credit risk associated with cash is minimal. Receivables are not significant to the Group. The Group's credit risk has not changed significantly from the prior year.

Liquidity Risk
The Group has in place a planning and budgeting process to help determine the funds required to support the Group's normal operating requirements on an ongoing basis and its planned capital expenditures. The Group's overall liquidity risk and going concern is discussed in note 2.

The following are the contractual maturities of financial liabilities, including estimated interest payments:

31 December 2013	**Carrying amount $'000**	**Contractual cash flows $'000**	**One year or less $'000**	**One to three years $'000**
Non-derivative financial liabilities				
Accounts payable and accrued expenses	**1,533**	**1,533**	**1,533**	**-**
Convertible debentures	**-**	**-**	**-**	**-**
	1,533	**1,533**	**1,533**	**-**
Derivative financial liabilities:				
Private placement warrants	**949**	**-**	**-**	**-**
Hess warrants	**448**	**-**	**-**	**-**
	1,397	**-**	**-**	**-**

22. Financial Instruments and risk management (continued)

31 December 2012	Carrying amount $'000	Contractual cash flows $'000	One year or less $'000	One to three years $'000
Non-derivative financial liabilities				
Accounts payable and accrued expenses	3,122	3,122	3,122	-
Convertible debentures	8,773	11,898	11,898	-
	11,895	15,020	15,020	-
Derivative financial liabilities:				
Convertible debt conversion feature	26	-	-	-
Private placement warrants	4,505	-	-	-
Hess warrants	787	-	-	-
	5,318	-	-	-

Currency Risk
Financial instruments that impact the Group's net loss due to currency fluctuations include Canadian dollar, Hungarian forint, Euro and Australian dollar denominated cash and cash equivalents, accounts receivable, reclamation deposits, accounts payable, and capital commitments for Hungarian and Australian operations.

The Company has a sterling cash balance, which exposes Falcon to fluctuations in exchange rates between sterling and U.S. dollars. A one cent strengthening / weakening of sterling against the U.S. dollar would decrease / increase total shareholders' equity and loss by less than $0.1 million.

The Company's exposure to other currencies, including the Hungarian forint, Euro and Australian dollar, does not result in a significant change to total shareholders' equity and income when the respective currencies strengthen or weaken by one cent against the U.S. dollar.

Interest Rate Risk
The Company has no significant exposure to interest rate risk as its debentures were repaid at 30 June 2013.

23. Convertible debentures

On 30 June 2009, the Group completed an offering of 11,910 units at a price of $865 (CDN$1,000) per unit (the "**Offering**"). Each unit consisted of one 11% convertible unsecured debenture in the principal amount of $779 (CDN$900) (each, a "**debenture**") that matured on the fourth anniversary of its issuance (30 June 2013) pursuant to the terms of a trust indenture dated 30 June 2009 (the "**Trust Indenture**"), and 250 common shares in the capital of Falcon (the "**Unit Shares**") (collectively, a "**Unit**"). The debentures accrued interest at an annual rate of 11% calculated and payable semi-annually in arrears on 1 January and 1 July in each year. The debentures were unsecured direct obligations of the Group.

The debentures and all outstanding interest were repaid at maturity, on 30 June 2013.

24. Derivative liabilities

Derivative liabilities consist of the fair value of the private placement warrants and the fair value of the Hess warrants. Changes in the fair value of the derivative liabilities are recorded in the Consolidated Statement of Operations and Comprehensive Loss. The composition of the derivative liabilities as at 31 December 2013 and 2012, and the changes therein for the years then ended, are as follows:

	Convertible Debt Conversion Feature $'000	**Private Placement Warrants $'000**	**Hess Warrants $'000**	**Total $'000**
At 1 January 2012	41	2,652	621	3,314
Derivative gains - debt conversion feature	(15)	-	-	(15)
Derivative loss - unrealised – outstanding warrants	-	1,853	166	2,019
At 31 December 2012	26	4,505	787	5,318
Derivative gains – debt conversion feature	**(26)**	**-**	**-**	**(26)**
Derivative gains – unrealised – outstanding warrants	**-**	**(3,556)**	**(339)**	**(3,895)**
At 31 December 2013	**-**	**949**	**448**	**1,397**

The fair value of the derivative liabilities is analysed between current and Non-current below:

	Private Placement Warrants $'000	**Hess Warrants $'000**	**Total $'000**
Non-current	-	448	448
Current	949	-	949
At 31 December 2013	**949**	**448**	**1,397**

The terms of the warrants are as follows:

Warrant issue	**Date of issue**	**Number of common shares issuable under warrants**	**Exercise Price CDN$**	**Proceeds from warrants* CDN$'000**	**Expiry date**
Private placement(i)	10 February 2011	33,400,000	0.18	-	10 February 2014
Private placement(i)	8 April 2011	31,887,500	0.18	-	8 April 2014
Hess(ii)	13 July 2011	10,000,000	0.19	1,900	13 January 2015
Total		**75,287,500**		**1,900**	

*Proceeds from warrants are subject to the warrant holders exercising their warrants. The warrants which expired on 10 February 2014 and 8 April 2014 were not exercised.

(i) In 2011, Falcon issued 87,050,000 units (the "**Units**") at $0.16 (CDN$0.15) per unit by way of a non-brokered private placement for aggregate gross proceeds of $13.7 million (CDN$13.1 million), before offering costs of $194. Each Unit consists of one common share in the capital of Falcon (each, a "**Common Share**") and three-quarters of one Common Share purchase warrant (each, a "**Warrant**"), each whole Warrant being exercisable into a Common Share for a period of 36 months from the date of its issuance at an exercise price of CDN$0.18 per share.

24. Derivative liabilities (continued)

(ii) Under the terms of the E&P Agreement (refer to note 13), Hess paid $20.0 million to the Company (i) as a participation fee for the exclusive right to conduct operations for the exploration, drilling, development and production of hydrocarbons from the Hess Area of Interest and (ii) as consideration for warrants to acquire 10,000,000 common shares in the capital of Falcon exercisable from 14 November 2011 through 13 January 2015 at an exercise price of CDN$0.19 per share (the "**Hess Warrants**").

The fair value of the warrants was estimated using a Black Scholes Model with the following inputs:

	Private Placement Warrants 31 December 2013	**Private Placement Warrants** 31 December 2013	**Hess Warrants** 31 December 2013
Number	33,400,000	31,887,500	10,000,000
Expiry	10 February 2014	8 April 2014	31 January 2015
Exercise price	**CDN$0.18**	**CDN$0.18**	**CDN$0.19**
Volatility	**37.12%**	**59.73%**	**70.97%**
Expected warrant life	**0.11 years**	**0.27 years**	**1.04 years**
Dividends	**Nil**	**Nil**	**Nil**
Risk-free rate	**1.13%**	**1.13%**	**1.13%**

	Private Placement Warrants 31 December 2012	**Private Placement Warrants** 31 December 2012	**Hess Warrants** 31 December 2012
Number	33,400,000	31,887,500	10,000,000
Expiry	10 February 2014	8 April 2014	31 January 2015
Exercise price	CDN$0.18	CDN$0.18	CDN $0.19
Volatility	89.73%	91.25%	82.51%
Expected warrant life	1.11 years	1.27 years	2.04 years
Dividends	Nil	Nil	Nil
Risk-free rate	1.14%	1.14%	1.14%

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25. Decommissioning Provision

A reconciliation of the decommissioning provision for the years ended 31 December 2013 and 2012 is provided below:

	2013 $'000	2012 $'000
Balance as at beginning of year	**11,005**	8,813
Revision to provisions	**25**	1,983
Utilised	**(50)**	-
Accretion	**158**	209
Balance as at end of year	**11,138**	11,005
Non-current	**11,138**	10,955
Current	**-**	50
Balance as at end of year	**11,138**	11,005

The Group's decommissioning provision results from its ownership interest in oil and natural gas assets. The total decommissioning provision is estimated based on the Group's net ownership interest in the wells, estimated costs to reclaim and abandon these wells and the estimated timing of the costs to be incurred in future years. The Group's has estimated the net present value of the decommissioning provision to be $11.1 million as at 31 December 2013 (2012: $11.0 million) based on an undiscounted total future liability of $13.4 million (2012: $13.3 million). These payments are expected to be made over approximately the next 20 years with the majority of costs to be incurred between 2027 and 2031. The discount factor, being the risk free rate related to the liability, was 1.3% as at 31 December 2013 (2012: 1.3%).

26. Accounts payable and accrued expenses

			At 31 December
	Notes	**2013 $'000**	2012 $'000
Current			
Accounts payable		**508**	939
Accrued expenses		**905**	1,793
Royalties payable		**22**	24
Restructuring provision	(i)	**98**	366
		1,533	3,122

26. Accounts payable and accrued expenses (continued)

(i) *Restructuring provision*
During 2012 the Group relocated its corporate headquarters from Denver, Colorado to Dublin, Ireland. The finance and executive function moved to Dublin while the primary technical function shifted to the company's Hungarian office in Budapest where the company operates exploration and producing interests. In connection with that decision, all individuals and consultants in Denver were terminated. The Denver office closed on 28 September 2012.

The movement in the provision to 31 December 2013 and 31 December 2012 is as follows:

	Severance & health benefits $'000	Rent expense net of sublease $'000	Other $'000	Total $'000
At 1 January 2012	-	-	-	-
Charged during the year	567	176	49	792
Utilised	(375)	(36)	(15)	(426)
At 31 December 2012	192	140	34	366
Utilised during the year	(192)	(48)	(28)	(268)
At 31 December 2013	**-**	**92**	**6**	**98**

27. Related party transactions

Key management personnel
Disclosures with regard to key management personnel are included in note 10.

The following are the related party transactions which occurred during the period:

Dr. György Szabó Consulting Agreement
On 27 February 2009, Dr. György Szabó (Executive Director and Co-Managing Director of Falcon –TXM) entered into a consulting agreement (the "**GS Consulting Agreement**") with Falcon TXM ("**TXM**"), pursuant to which Dr. Szabó agreed to act as Managing Director of TXM, to perform certain oil and gas services for TXM and to not compete directly or indirectly with TXM during his employment with TXM. Dr. Szabó is paid a monthly fee of $5,000. The GS Consulting Agreement contains standard confidentiality provisions. TXM may terminate the GS Consulting Agreement at any time, with or without cause, for any lawful reason whatsoever, upon TXM providing Dr. Szabó with sixty days' prior written notice. The GS Consulting Agreement expired on 31 December 2009, however Dr. Szabó has continued to provide general managerial services to TXM and to receive the same monthly fee. Dr. Szabó was paid $60,000 pursuant to the GS Consulting Agreement in the year ending 31 December 2013.

P&S Consulting Agreement
On 4 May 2005, P&S Mérnöki Kereskedelmi-Tanácsadó Bt. ("**P&S**") entered into a consulting agreement (the "**P&S Agreement**") with TXM, pursuant to which P&S agreed to provide certain consulting services to TXM in connection with TXM's objectives of drilling wells on the Makó and Tisza licences. The P&S Agreement was amended on 28 November 2005 and further amended on 1 June 2006, 1 January 2008, 1 January 2009 and 1 April 2010. P&S is wholly-owned by a family member of Dr. György Szabó, a current Director of the Company. Under the terms of the P&S Agreement, TXM was obligated to pay P&S a monthly services fee of HUF 750,000. The P&S Agreement contains standard confidentiality provisions and provides that P&S shall not compete with TXM during the term of the P&S Agreement.

27. Related party transactions (continued)

TXM may terminate the P&S Agreement at any time, with or without cause, for any lawful reason whatsoever, upon TXM providing P&S with 30 days, prior written notice. TXM and P&S have further amended the terms of the P&S Agreement by oral agreement. Pursuant to the amended P&S Agreement, P&S is paid a monthly fee of $8,500 (effective 1 January 2013) (2012: $10,000) plus reasonable expenses incurred by Dr. Szabó as an employee of P&S, such amounts thereafter paid to Dr. Szabó from P&S. P&S was paid $102,000 pursuant to the agreement in the year ending 31 December 2013.

Dr. Gábor Bada
On 28 December 2012, Dr. Bada entered into an employment agreement (the "**Bada Employment Agreement**") with TXM pursuant to which Dr. Bada agreed, subject to certain conditions, to perform certain geological services for TXM. In addition, on 1 January 2013, Dr. Bada verbally agreed the terms on which he was to provide geological services to TXM as a consultant. Dr. Bada will be paid a consultancy fee of $20,000 in 2013 in relation to this work. Dr. Bada invoices TXM through his company Senzus Kft. The Bada Employment Agreement contains standard confidentiality provisions. Dr. Gábor Bada received a consultancy fee of $20,000 through his company in the year ended 31 December 2013.

Oakridge Financial Management Inc.
The Group has engaged Oakridge Financial Management Inc. to assist in submitting returns to the Canadian Revenue Agency. Mr. Greg Smith, a current director of Falcon, is the sole shareholder in Oakridge Financial Management Inc.. The Group has incurred costs of approximately CDN$1,000 to Oakridge Financial Management Inc. during the year ended 31 December 2013.

March 2013 Private placement
On 14 March 2013 the Group announced its application for admission to trading on the AIM market of the London Stock Exchange and the ESM market of the Irish Stock Exchange, of the Company's existing share capital and an additional 120,381,973 new common shares in the capital of Falcon issued pursuant to the concurrent conditional brokered private placement at a price of £0.14 (CDN$0.215) per share, raising gross proceeds of $25.7 million (£16.9 million) (the "**Placing**"). The following related parties participated in the Placing:

Directors	**Previous shareholding**	**March 2013 Placing participation**	**Enlarged shareholding***	**% of enlarged share capital***
John Craven	500,000	2,357,143	2,857,143	0.35%
Philip O'Quigley	1,000,000	513,696	1,513,696	0.19%
Gregory Smith	420,000	50,000	470,000	0.06%
David Harris	-	150,000	150,000	0.02%

*immediately post-Placing.

April 2013 Stock Options
On 30 April 2013 a total of 3 million options were granted at an exercise price of CDN$0.215 to Eoin Grindley, Falcon's Chief Financial Officer pursuant to the terms of his employment contract. A further 5.5 million options were granted at an exercise price of CDN$0.24 (a 23% premium to the closing share price on 30 April 2013) to the following Falcon directors:

Directors	**Number of options granted**	**Total number of Options held after grant**
John Craven	2,000,000	3,100,000
Igor Akhmerov	2,500,000	2,900,000
Daryl Gilbert	200,000	2,900,000
Gregory Smith	200,000	1,000,000
Joachim Conrad	300,000	1,000,000
David Harris	300,000	300,000

A further 1.4 million options were granted to employees of Falcon at an exercise price of CDN$0.24 on 30 April 2013.

28. Overriding royalties

On 1 November 2013, Falcon announced that Falcon Australia, had entered into an agreement ("**the CRIAG Agreement**") with CR Innovations AG ("**CRIAG**") to acquire its 4% Overriding Royalty Interest ("**ORRI**") relating to its exploration permits in the Beetaloo Basin. The transaction details were:

- Falcon Australia made an initial payment to CRIAG of $999,000 on signing the CRIAG Agreement;
- Falcon Australia to make a second payment to CRIAG of $999,000 to acquire the first 3% (three fourths) of the ORRI upon completion of a farm-out deal in Australia;
- CRIAG has granted Falcon Australia a five year call option to acquire the remaining 1% (one fourth) for $5 million; and
- All ORRI's acquired under the CRIAG Agreement will be immediately cancelled by Falcon Australia.

On 17 December 2013, Falcon announced that Falcon Australia, had entered into an agreement with Malcolm John Gerrard, Territory Oil & Gas LLC and Tom Dugan Family Partnership LLC ("**TOG Group**") to acquire up to 7% (seven eighths) of the remaining 8% private ORRI over Falcon Australia's exploration permits in the Beetaloo Basin for the following consideration:

- Falcon Australia will make a payment to TOG Group of $5 million to acquire 5% (five eighths) of their ORRI only on completion of a Beetaloo farm-out transaction;
- TOG Group will grant Falcon Australia a five year call option to acquire a further 2% (two eighths) of their ORRI for a payment of $15 million;
- All ORRIs acquired under the Agreement will be immediately cancelled by Falcon Australia; and
- TOG Group will retain a 1% ORRI.

29. Comparatives

Comparative figures have been adjusted where necessary, to conform with changes in presentation or where additional analysis has been provided in the current period. The key reclassifications are:

- Restricted cash has been reclassified as a "non – current asset"
- Letter of credit in the amount of $0.5 million has been reclassified at 31 December 2012 from "trade and other receivables" to "restricted cash" both within "non – current assets".

30. Commitments and contingencies

(i) Lease commitments

The Group has entered into lease agreements for office space in:

- Denver, Colorado, expiring April 2015;
- Budapest, Hungary expiring 2 August 2015;
- Makó, Hungary expiring June 2014;
- Szeged, Hungary expiring June 2014;
- Dublin, Ireland, with a break clause exercisable in October 2017; and
- Sydney, Australia expiring October 2014.

30. Commitments and contingencies (continued)

The Group is obligated to pay the following minimum future rental commitments under non-cancelable operating leases at 31 December 2013 and 31 December 2012 during the following periods:

	As at 31 December 2013 $'000	As at 31 December 2012 $'000
2013	**-**	420
2014	**533**	427
2015	**284**	242
2016	**120**	97
2017	**100**	81
Thereafter	**-**	-
Total	**1,037**	1,267

As part of the Group's restructuring process in 2012, the Group sub-let its Denver premises. This sub lease rental income has not been included in the table above. A total amount of $0.2 million is expected to be received under the sublease ending April 2015.

(ii) Work program commitments
Australia - Beetaloo Basin, Northern Territory, Australia
Under the terms of Falcon Australia's exploration permit EP-99 Falcon Australia must spend a minimum of $1.5 million by 31 December 2014 in collecting 2D seismic data on acreage within exploration permit EP-99. Falcon Australia intends to meet this commitment either through a farm-out arrangement or through its own resources.

South Africa - Karoo Basin, South Africa
On granting of an approved exploration right in South Africa, the Group will be required to make a payment to the South African government of approximately $0.7 million.

Hungary - Makó Trough, Hungary
The Group is not committed to any independent technical operations in Hungary other than joint operations with NIS, and as such no material capital expenditures are expected.

(iii) Contractual commitments
Under existing agreements with two advisors, the Group is obligated to pay a success fee for services provided in relation to certain of the Group's assets. The success fees are based on the cash or cash equivalent value of the net amount received directly or indirectly by the Group. The agreements were terminated during 2011 and 2012 respectively, but payments will continue after termination until all relevant cash or cash equivalents amounts are settled.

31. Standards, Interpretations and Amendments to Published Standard that are not yet effective

Several new standards and amendments to existing standards and interpretations, which have been issued by the IASB, and which are expected to apply to the Group are not yet effective and have not been applied in preparing these financial statements. The Group does not expect adoption of these new standards and interpretations, to have a material impact on the financial statements.

An amendment to IAS 32 'Offsetting financial assets and financial liabilities' was issued in December 2011 and will be implemented by the Group from 1 January 2014. The amendment provides additional guidance on when financial assets and financial liabilities may be offset.

IFRS 9 'Financial instruments' was first issued in November 2009 and has since been amended several times. The Standard will eventually replace IAS 39 and covers the classification, measurement and derecognition of financial assets and financial liabilities together with a new hedge accounting model. The IASB intends to expand IFRS 9 to add new requirements for impairment and for it to become a complete replacement of IAS 39 in due course, although no date for its mandatory implementation has been set.

32. Approval of financial statements

These Consolidated Financial Statements were approved by the Board of Directors and authorised for issue on 29 April 2014.

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