Xcite Energy Limited

Annual Report and Financial Statements

for the year ended December 31, 2009

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Board of Directors

Roger S. Ramshaw is the Chairman and a Non-Executive Director of the Company. From 2002 until his retirement in 2003, Mr. Ramshaw was Chairman and Managing Director of ConocoPhillips (UK) Ltd, where he led the company's exploration, development and production business on the UK Continental Shelf. From 1999 to 2002, he was President of Conoco Venezuela Ltd. Mr. Ramshaw has over 30 years of domestic and international experience in operations, project and commercial activity in the petroleum industry.

Richard E. Smith is Chief Executive Officer and Director of XER and the Company. From 2000 until joining XER in 2003, Mr. Smith was Programme Director at Granherne, formerly of the Halliburton group of companies, where he was responsible for the creation and formation of a business providing programme management services to clients in the international onshore and offshore oil and gas business. Mr. Smith is a Chartered Engineer and has over 25 years of experience in engineering and business management in onshore and offshore oil and gas projects. He is a Fellow of the Institute of Civil Engineers and a Corporate Member of the Institute of Marine Engineers and the Royal Institute of Naval Architects.

Rupert E. Cole is Chief Financial Officer and Director of XER and the Company. From 2002 until joining XER in 2003, Mr. Cole was Programme Management Business Adviser at Granherne, a company within the Halliburton group of companies, providing strategic, commercial and financial advice to upstream oil and gas services providers. From 1990 to 1996, Mr. Cole was Finance Director at Harpur, an international downstream service provider to major oil companies. Mr. Cole is a Chartered Accountant and has over 20 years of experience in corporate finance.

Stephen A. Kew is Exploration and Development Director of XER and the Company. Mr. Kew has been a director for 3 Sigma Limited since 1999, a petroleum engineering consultancy company in the upstream oil and gas business. Mr. Kew is a Petroleum Engineer and has over 35 years of development engineering and project management experience in the oil and gas industry, including previous experience in respect of Block 9/3b. He is an associate of the Institution of Chemical Engineers, a member of the Society of Petroleum Engineers and former President of the Scottish Oil Club.

Gregory J. Moroney is a Non-Executive Director of the Company and Chairman of the Remuneration and Nominating Committee. Mr. Moroney is the Founding and Managing Member of Energy Capital Advisors LLC of Greenwich, Connecticut, which he founded in 2003 to assist independent energy companies and energy fund managers in North America in their fund-raising activities. Mr. Moroney is also a director of BreitBurn Energy Partners, L.P., an oil and gas limited partnership listed on NASDAQ. From 1993 to 2002, he was head of the Structured Finance Group for the Energy and Natural Resource Sector - Western Hemisphere at Deutsche Bank Securities in New York. Mr. Moroney has over 25 years of experience as an energy finance specialist. In 2009 he moved to Jupiter, Florida, where he continues his consulting activities.

Scott R. Cochlan was appointed as a Non-Executive Director of the Company on January 18, 2008 and is a member of the Remuneration and Nominating Committee. Mr. Cochlan is a partner at the law firm of Blake, Cassels & Graydon LLP in the securities group. Mr. Cochlan has represented senior and junior public issuers in numerous aspects of general corporate law and securities regulatory matters including corporate governance, continuous disclosure, regulatory compliance and transaction negotiation and completion. Mr. Cochlan also has extensive experience in representing both issuers and underwriters in a wide variety of complex private and public financing matters (equity and debt), including cross-border financings, mergers, acquisitions and other business reorganizations and restructurings. Mr. Cochlan holds a law degree from the

University of Calgary and a B.A. from the University of Western Ontario. Mr. Cochlan has received a number of recognitions as a leading lawyer in his field.

Timothy S. Jones was appointed as a Non-Executive Director of the Company on March 19, 2009 and also as Chairman of the Audit Committee on that date. Mr. Jones is a Chartered Accountant with 20 years experience in professional practice covering a number of industries including oil and gas. Following major public company roles, he formed his own accountancy and consulting practice to focus on the oil and gas sector, where he specialises in providing advice to AIM listed companies. He is currently on the board of a number of AIM listed natural resources companies.

Chairman's and Chief Executive's Review

The 9/3b-5 well and subsequent study work in 2008 demonstrated that the Bentley field was one of the largest undeveloped fields in the UK sector of the North Sea but, as we warned last year, the exceptional conditions in the global equity and credit market impeded the progress we had hoped to make during 2009. It was not possible to make the significant commitments required to move forward with the Early Production System (EPS) programme and, now that oil prices have recovered from their slump and other market conditions have improved, we intend to continue with the Bentley work programme to demonstrate the commerciality of the Bentley field and to categorise its resources as reserves.

Despite the constraints of the credit markets, a number of important steps were taken during the year. The Competent Person's Report by RPS Energy had been conducted using the original seismic data, so it was encouraging that the reprocessing of the 3D seismic data announced in June 2009 confirmed higher estimates of petroleum initially in place ("PIIP") for the field and consequent potential recoverable reserves. The PIIP for the Most-Likely structure was estimated to be 689 million barrels of oil equivalent ("MMbbls"), with a range of 521 to 886MMbbls for Down-Side and Up-Side structures, respectively, and evaluation of a full field development showed a range of potential recoverable resources from 109 to 220MMbbls, with a Base Case of 160MMbbls.

The most significant achievements from the hard work of 2009, which were formally announced at the end of the year and early in 2010, were the securing of the important building blocks of the 'Bentley Alliance', the innovative commercial structure that Xcite Energy Resources Limited ("XER") has created to take the Bentley field into development. Fugro Well Services Limited signed an agreement to drill a geotechnical test well as part of the necessary preparation for the 9/3b-R pre-development well on the Bentley field. Applied Drilling Technology International, the well management arm of Transocean Drilling U.K. Limited, signed a letter of intent for the provision of a heavy duty, deep water jack-up drilling unit to undertake the drilling and testing of the 9/3b-R well in 2010. AMEC plc has signed an agreement to provide its technical expertise, engineering and project management skills to assist the Bentley Alliance demonstrate the reserves potential of the Bentley field and subsequently bring it into production.

An important underpinning of the field development and the economics of the field was provided when BP Oil International Limited ("BPOI"), a wholly owned subsidiary of BP plc, signed a Supply and Offtake agreement to market and sell the Bentley crude oil in return for a fee per barrel which incentivises them to maximise the price per barrel achieved for XER by minimising the discount to Brent crude. In addition, when XER moves to full field development of Bentley, BP will procure $20 million of financing from a commercial bank with credit support to assist in the process.

Finally, we were pleased to welcome Challenger Minerals (North Sea) Limited ("CMNS") as a farm-in partner in the Bentley field, through an undertaking to provide $4 million towards the cost of the 9/3b-R well in exchange for 4% of the Bentley field; a deal that applied a pre-money value of $100 million to the Bentley field. This will be enacted through an earn-in mechanism which, when the $4 million is paid, will allow CMNS to join the Bentley field licence at any time prior to the commencement of the first phase development of the field. This is a fitting final piece of the Bentley Alliance, which creates important additional synergies as we move ahead to drill the 9/3b-R well and beyond.

We would also like to note the new field allowance for heavy oil fields such as Bentley, which was introduced by the UK Chancellor in the 2009 Budget. Although this does not diminish our front-end financing

requirements it does increase the size of the ultimate field value. As a result of this allowance, we estimate the overall corporation tax applicable to the Bentley field is reduced by GBP£160 million and the net present value of the field, as presented in the Base Case of the February 2009 Competent Person's Report, is increased by more than US$100 million.

We were pleased in October 2009 to raise gross proceeds of approximately £2.1 million (CAN$3.8 million) from investors in the UK and Canada, in what was generally considered a very difficult time to secure new capital. Since then, we have again returned successfully to the capital markets earlier in March 2010 to enable the financing of the 9/3b-R well, for which we received encouraging support from a good range of blue chip institutional investors. This financing comprised the £2.7 million ($4 million) CMNS farm-in undertaking, together with an equity share issue to raise approximately £23.5 million (approx $36 million) net of costs, which in aggregate provides adequate funds for the 9/3b-R well and working capital for the foreseeable future.

The Board has continued to refine its implementation of the appropriate practices of good governance taking guidance from the 'Guidance for Smaller Quoted Companies' of the Quoted Companies Alliance, 2004. Greg Moroney chaired the Remuneration & Nominating Committee and Tim Jones chaired the Audit Committee with effect from March 19, 2009.

Finally, we would like to take this opportunity to thank the small, dedicated XER team for all their work and commitment during the year. In spite of the difficulties and setbacks caused by the continuing financial crisis, they have maintained focus and, thanks to their efforts, we can now move forward to demonstrate the potential of the Bentley field and transform it into real value for the Company's shareholders.

Roger Ramshaw
Chairman
March 24, 2010

Richard Smith
Chief Executive Officer

Management Discussion and Analysis

The Management's Discussion and Analysis ("MD&A") of the operating and financial results of Xcite Energy Limited ("XEL" or the "Company") should be read in conjunction with the Company's audited consolidated financial statements and related notes for the year ended December 31, 2009. This MD&A is dated March 24, 2010. These documents and additional information about XEL, including its annual information form dated December 8, 2009, are available on SEDAR at www.sedar.com.

XEL is an oil issuer and disclosures pertaining to oil activities are presented in accordance with National Instrument 51-101 ("NI-51-101").

This MD&A includes an analysis of the XEL results for the twelve month period to December 31, 2009, which include the results of the operating subsidiary Xcite Energy Resources Limited ("XER") for the twelve months to December 31, 2009. The comparative results comprise the twelve months to December 31, 2008. In this MD&A, XEL and XER are together defined as the "Group". All figures and the comparatives figures contained herein are expressed in Pounds Sterling unless otherwise noted.

Certain statements in this MD&A may be regarded as "forward-looking statements" including outlook on oil prices, estimates of future production, estimated completion dates of constructions and development projects, business plans for drilling and exploration, estimated amount and timing of capital expenditures and anticipated future debt levels. Forward-looking statements often, but not always, are identified by the use of words such as "seek", "anticipate", "believe", "plan", "estimate", "expect", "targeting" and "intend" and statements that an event or result "may", "will", "should", "could" or "might" occur or be achieved and other similar expressions.

Information concerning reserves may also be deemed to be forward-looking statements as such estimates involve the implied assessment that the resources described can be profitably produced in the future. These statements are based on current expectations, estimates and projections that involve a number of risks and uncertainties, including crude oil resource estimations, crude oil prices, exchange rates, interest rates, prevailing rates of taxation (see "Risk Management" section below), which could cause actual results to differ from those anticipated by the Group. The reader should not place undue importance on forward-looking statements and should not rely upon this information as of any other date. While the Company may elect to, it is under no obligation and does not undertake to update this information at any particular time, unless required by applicable securities law.

Summary of Results

The following table summarises the Group's performance in the year to December 31, 2009 and the comparatives of the year to December 31, 2008 and the fourteen month period to December 31, 2007. The Group has no trading revenue in either period. The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations issued by the International Accounting Standards Board ("IASB"). The consolidated financial statements of the Company have also been prepared in accordance with IFRS's adopted by the European Union ("EU") and therefore they comply with Article 4 of the EU International Accounting Standards Regulation.

	Year ended December 31	Year ended December 31	14 months ended December 31
	2009	2008	2007
	£	£	£
Net loss	**(880,218)**	(554,021)	(730,289)
Loss per share (basic and diluted) in pence	**(1.4p)**	(0.9p)	(2.2p)
Total assets	**24,789,744**	23,860,469	27,732,099
Long term liabilities (deferred tax)	**505,167**	-	-

When comparing the current year against past performance, the net loss variations have arisen primarily as a result of reduced interest income, coupled with an increased tax charge, whilst administrative expenses have remained consistent year on year. The deferred tax balance has arisen in the current year as a result of a Research and Development ("R&D") tax rebate.

The following table summarises the Group's performance for the eight most recent quarters. All of these results are unaudited. The Group has no trading revenue in these periods.

	Q4 09	Q3 09	Q2 09	Q1 09	Q4 08	Q3 08	Q2 08	Q1 08
	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s	£'000s
Net loss	(359)	(249)	(145)	(127)	(205)	(90)	(281)	22
EPS *	(0.5p)	(0.4p)	(0.2p)	(0.2p)	(0.3p)	(0.1p)	(0.5p)	0.0p
Total assets	24,790	23,240	23,507	23,779	23,860	24,005	25,185	27,787
Long term liabilities	505	-	-	-	-	-	-	-

* (Loss)/earnings per share (basic and diluted) in pence

Fourth Quarter Highlights

The Company is not influenced by seasonality to any significant extent. The variations noted above in the quarterly net loss have arisen in line with the execution of the development programme for the Bentley field and in the work undertaken in leading to the formation of the Bentley Alliance. The increased net loss for Q409 has arisen mainly due to additional share-based payment charges in relation to the Company's Share Option Plan.

Liquidity and Capital Resources

The cash balance as at December 31, 2009 was £1.7 million, compared with £1.8 million as at December 31, 2008. During the year to December 31, 2009 the Group continued to use funds on deposit to meet its working capital requirements as they fell due.

Based on the nature of the appraisal and development expenditure being incurred in defining the Bentley field, the Group pursued and successfully claimed a Research & Development ("R&D") rebate from the UK Tax Authorities in September 2009, providing XER with additional cash of £0.4 million. A deferred tax provision of £0.5 million has been recognised in the current year as a result of this R&D rebate.

In October 2009 the Group completed a successful Private Placement of £2.1 million which, after costs, brought in £1.9 million of new funding.

A further funding success with the capital markets was completed in March 2010 to enable the financing of the 9/3b-R well, thereby engaging a good range of blue chip institutional investors whom we welcome to the register. This financing comprised the £2.7 million from the Challenger Minerals (North Sea) Limited ("CMNS") farm-in undertaking, together with an equity share issue to raise approximately £25 million gross and £23.5 million net of costs, which in aggregate provides adequate funds for the 9/3b-R well and working capital for the foreseeable future.

Lease and Contractual Commitments

As at December 31, 2009 the Group has no material lease or contractual commitments.

Operations and Administrative Expenses

It has without doubt been a challenging year for the Group, with cost control being a priority while still making significant progress in our understanding of and plans to take the Bentley field into development as rapidly as possible. Based on the fund raising closed earlier in March 2010, we are now able to look forward to the next part of this work programme, which will involve the drilling and flow testing of the 9/3b-R pre-development well on the Bentley field.

In the absence of revenue streams from the Group's assets, ensuring value for money on each pound invested has been a priority for the Group. The year has been characterised by further developing the Bentley Alliance, the management and operational structure created by XER as the vehicle to direct the Bentley field to full field development, more of which is described below.

In comparison to 2008, the Group's expenditure during 2009 was much reduced, the primary reason being due to the drilling of the 9/3b-5 well in early 2008 with no equivalent Bentley field work programme during 2009. During 2009, a total of £1.0 million was charged to Exploration and Evaluation ("E&E") assets (year ending December 31, 2008: £15.4 million), representing various technical and commercial studies into further defining the Bentley field, principally in respect of wages and salaries and the licence payment to The Department of Energy and Climate Change ("DECC") in respect of XER's obligations under the UK North Sea licence of the Bentley field for the forthcoming licensing period.

In addition, the Group charged to the Income Statement total administrative expenses of £0.8 million compared to £0.9 million in the year to December 31, 2008. Such expenses represent the costs of operating as a public company, including a proportion of the remuneration costs of certain Executive Directors, Non-Executive Director fees, Nominated Advisor, stockbrokers, registrars and stock exchange fees.

It should also be noted there is a new field allowance for heavy oil fields such as Bentley, which was introduced by the UK Chancellor in the 2009 Budget. Although this does not diminish our front-end financing requirements it does increase the size of the ultimate field value. As a result of this allowance, we estimate the overall corporation tax applicable to the Bentley field is reduced by GBP£160 million and the net present value of the field, as presented in the Base Case of the February 2009 Competent Person's Report, prepared by RPS Energy, a division of RPS Group plc, is increased by more than US$100 million.

Related Party Transactions

XEL has continued to provide a loan facility its wholly owned subsidiary, XER, to finance XER's operational requirements, with net cash funding of £1.78 million during the year to December 31, 2009 (year to December 31, 2008: £12.36 million). No interest is payable on the outstanding loan balance from XEL, which is unsecured and repayable on demand. The total balance owing by XER to XEL at December 31, 2009 was £22.60 million (as at December 31, 2008: £20.82 million).

The Executive Directors have received remuneration, details of which are given in Note 4 to the financial statements. The Executive and Non-Executive Directors have also been granted share options over the ordinary share capital of the Company during year, details of which are given below.

Share Options, Warrants and Rights

In the year to December 31, 2009, the Company issued aggregate share options to Non-Executive Directors, contractors and management of 2,250,000 under the Stock Option Plan (2008: 550,000 aggregate share options issued). The total expense to the Group in respect of share based payment transactions under the Stock Option Plan was £0.25 million (2008: £0.13 million). Of this total, £0.13 million (2008: £0.05 million) has been charged to the Income Statement and £0.12 million (2008: £0.08 million) has been capitalised under intangible assets in accordance with the Company's accounting policy.

As at the date of signing this MD&A there were 6,530,000 options outstanding (2008: 4,350,000).

Income

Interest income received on funds invested up to December 31, 2009 amounted to £6,053 (2008: £344,910). The decline in interest generated on funds invested during the year in comparison to 2008 was as a result of a significant reduction in bank interest rates, coupled with continued working capital requirements that reduced the funds on deposit.

During the continued uncertainties of the financial markets during the year, management has maintained its policy of keeping cash deposits with banks with "AA" rating or better. The policy of the Group is to ensure that all cash balances earn a market rate of interest and that interest rate exposures are regularly reviewed and managed.

Disclosure Controls and Procedures

In conformance with the Canadian Securities Administrators National Instrument 52-109, the Company has filed certificates signed by the Chief Executive Officer and the Chief Financial Officer that, amongst other things, deal with the matter of disclosure controls and procedures.

The Board meets at least quarterly during the year and on an ad hoc basis as required. The attendance record of each Director during the twelve months to December 31, 2009 is given below.

	Board	Audit Committee	Remuneration and Nominating Committee
Richard E. Smith	7	N/A	N/A
Rupert E. Cole	7	5	N/A
Stephen A. Kew	7	N/A	N/A
Roger S. Ramshaw	7	5	5
Gregory J. Moroney	7	5	5
Scott R. Cochlan	7	N/A	5
Timothy S. Jones (1)	6	4	N/A

(1) Since date of appointment March 19, 2009

Outstanding Share Capital

The following table sets out the ordinary shares issued during the year. No warrants or share options were exercised during 2009.

	Ordinary Shares
As at January 1, 2009	**61,413,800**
Issue of ordinary shares through Private Placement	10,141,998
As at December 31, 2009	**71,555,798**

As at the date of signing this MD&A, the number of shares in issue was 133,528,192 as set out in Note 13 to the financial statements, following the issue of an additional 61,972,394 shares during the public offering completed pursuant to a short-form prospectus dated March 10, 2010.

Risk Management

The principal risk factors facing the Group are as follows:

Exploration and development

The nature of oil exploration is such that there is no assurance that exploration activities will be successful. Industry statistics show that few properties that are explored go on to being fully developed. Operations can also be adversely affected by weather conditions and drilling rig and other operating equipment availability outwith the control of the Group.

Commodity pricing

The Group has no control over the market price of crude oil. Suitable hedging arrangements will be considered to mitigate the volatility of oil prices when the Group enters into the production phase.

Financing

Future field development will depend upon the ability of the Group to secure financing, whether this is by joint venture projects, farm down arrangements, public financing or other means.

Currency

The Group's reporting and functional currency is Pounds Sterling. However, the market for crude oil is in US Dollars. The Group does not currently engage in active hedging to minimise exchange rate risk although this will remain under review as the Group approaches the production phase.

Resource estimation

Oil resource estimation techniques are inherently judgemental and involve a high degree of technical interpretation and modelling techniques. Incorrect resource estimation may result in inappropriate capital investment decisions being made.

Significant Accounting Judgements and Estimates

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Directors make estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual costs. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying value of assets and liabilities within the next financial period are discussed below.

(a) Income taxes

There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(b) Fair value of share options and warrants

The Company has valued the fair value of outstanding share options and warrants over the Company's shares using the Black-Scholes valuation methodology. The Company uses judgement to derive such valuation model assumptions that are mainly based on market conditions existing at the option issue date.

(c) Impairment of Exploration and Evaluation ("E&E") assets

A review is performed at the end of each financial period for any indication that the value of the Group's E&E assets may be subject to impairment. In the event of any such indication, an impairment test is carried out and, if necessary, an impairment charge is made representing the surplus of capitalised cost over estimated recoverable value of the related commercial oil reserves. Estimated recoverable value is based upon anticipated discounted net cash flows attributable to such oil reserves.

Changes in Accounting Policies

During the year the Group has adopted a number of new standards and amendments to standards which become mandatory for the first time for the financial year beginning January 1, 2009. The most significant adoption was that of IAS 1 (revised). The Group has elected under IAS 1 (revised) to present two statements: an income statement and a statement of comprehensive income. These consolidated financial statements have been prepared under the revised disclosure requirements. No restatements were required to prior period comparatives as a result of this adoption.

Whilst the Group has adopted IFRIC 13, IFRIC 14, IFRIC 15 and IFRIC 16 during the year, these are not considered relevant for the Group and have therefore had no impact in the consolidated financial statements.

Financial Instruments and Other Derivatives

Details regarding the Group's policies in respect of financial instruments are disclosed in Notes 1 and 12 to the financial statements.

2010 Outlook

The most significant achievements from the hard work of 2009, which were formally announced at the end of the year and early in 2010, were the securing of the important building blocks of the 'Bentley Alliance', the innovative commercial structure that Xcite Energy Resources Limited ("XER") has created to take the Bentley field into development. Fugro Well Services Limited signed an agreement to drill a geotechnical test well as part of the necessary preparation for the 9/3b-R pre-development well on the Bentley field. Applied Drilling Technology International, the well management arm of Transocean Drilling U.K. Limited, signed a letter of intent for the provision of a heavy duty, deep water jack-up drilling unit to undertake the drilling and testing of the 9/3b-R well in 2010. AMEC plc has signed an agreement to provide its technical expertise, engineering and project management skills to assist the Bentley Alliance demonstrate the reserves potential of the Bentley field and subsequently bring it into production.

An important underpinning of the field development and the economics of the field was provided when BP Oil International Limited ("BPOI"), a wholly owned subsidiary of BP plc, signed a Supply and Offtake agreement to market and sell the Bentley crude oil in return for a fee per barrel which incentivises them to maximise the price per barrel achieved for XER by minimising the discount to Brent crude. In addition, when XER moves to full field development of Bentley, BP will procure $20 million of financing from a commercial bank with credit support to assist in the process.

Finally, the Company was pleased to welcome Challenger Minerals (North Sea) Limited ("CMNS") as a farm-in partner in the Bentley field, through an undertaking to provide $4 million (£2.7 million) towards the cost of the 9/3b-R well in exchange for 4% of the Bentley field; a deal that applied a pre-money value of $100 million to the Bentley field. This will be enacted through an earn-in mechanism which, when the $4 million is paid, will allow CMNS to join the Bentley field licence at any time prior to the commencement of the first phase development of the field. This is a fitting final piece of the Bentley Alliance, which creates important additional synergies as the Company moves ahead to drill the 9/3b-R well and beyond.

As noted above, a further funding success with the capital markets was completed in March 2010 to enable the financing of the 9/3b-R well. This financing comprised the £2.7 million from the CMNS farm-in undertaking, together with an equity share issue to raise approximately £25 million gross and £23.5 million

net of costs, which in aggregate provides adequate funds for the 9/3b-R well and working capital for the foreseeable future. Based on this, the Company can now look forward to demonstrating the potential of the Bentley field and confirming its value as a significant North Sea oil field.

Report of the Remuneration and Nominating Committee

The Remuneration and Nominating Committee, in accordance with its written charter, reviews and makes recommendations to the Board concerning the appointment, remuneration and benefits and performance of executive management and Directors.

The Remuneration and Nominating Committee consists of three Non-Executive Directors, two of whom are independent within the meaning of National Instrument 52-110. The chairman of the Remuneration and Nominating Committee is Gregory J. Moroney.

Basic salary and benefits

The remuneration of the Executive Directors, who are the key personnel, for the year ended December 31, 2009, was as follows:

	Basic salary	Other compensation (i)	Share based payments	**2009 Total**	2008 Total
	£	£	£	**£**	£
Richard E. Smith	175,000	37,900	21,257	**234,157**	212,900
Rupert E. Cole	175,000	37,900	21,257	**234,157**	212,900
Stephen A. Kew	175,000	37,900	21,257	**234,157**	212,900

(i) Other compensation comprises cash allowances in lieu of pension contributions, company car and fuel allowances, private healthcare allowances and allowances for life insurance and permanent health insurance cover.

The XER service contracts for Mr Smith, Mr Cole and Mr Kew were signed on September 1, 2003 and last amended on October 24, 2007.

The Group's policy is to review salary and benefits annually against market data and analysis and to adjust accordingly where the Remuneration and Nominating Committee believes it is appropriate; no changes to Executive remuneration have been made during the year. The service and employment contracts for the Executive Directors are not of fixed duration but continuation in office as a director is subject to annual re-election by shareholders. The Group's policy is for Executive Directors to have service and employment contracts with provision for termination of no longer than twelve months notice.

The fees for the Non-Executive Directors in respect of their duties are determined by the Board and are reviewed on an annual basis; no changes to Non-Executive fees have been made during the year. Letters of Appointment for the Non-Executive Directors provide for termination of the appointment with one month notice by either party. In accordance with the Company's Articles of Association, Non-Executive Directors will retire after a term of two years at which point they may, subject to being eligible, offer themselves for re-election.

All Non-Executive Directors receive remuneration at the rate of £1,500 per day in respect of their services to the Group. During the year the Group paid to Roger Ramshaw, Gregory Moroney, Scott Cochlan, Timothy Jones and A. Murray Sinclair in their capacity as Non-Executive Directors of the Group fees of £21,750 (2008: £36,750), £12,000 (2008: £11,250), £9,000 (2008: £9,000), £15,750 (2008: £nil) and £nil (2008: £4,500) respectively. Charges in respect of share based payments for the Non-Executive Directors in the year to December 31, 2009 were £92,789 (2008: £46,803).

Beneficial Interests

The beneficial interests of the Directors in the ordinary share capital of the Company are as follows:

	Shares	Option Tranche 1	Option Tranche 2	Option Tranche 3	Total Options
Stephen A. Kew	6,314,285	1,000,000	-	100,000	1,100,000
Rupert E. Cole	6,300,000	1,000,000	-	100,000	1,100,000
Richard E. Smith	6,300,000	1,000,000	-	100,000	1,100,000
Roger S. Ramshaw	-	200,000	-	100,000	300,000
Gregory J. Moroney	-	100,000	-	100,000	200,000
Scott R. Cochlan (i)	25,000	100,000	-	100,000	200,000
Timothy S. Jones	50,000	-	100,000	100,000	200,000

Tranche 1- These share options, which vested immediately, were granted to the Directors on November 16, 2007 at the date of the Initial Public Offering (except for Scott R. Cochlan as noted below) with an exercise price of CAD$1.60 (£0.805) and a term of five years.

Tranche 2 - Timothy S. Jones was appointed to the Board on March 19, 2009 and on April 23, 2009, 100,000 share options were awarded and vested immediately with an exercise price of CAD$0.29 (£0.16) and a term of five years.

Tranche 3 - These share options, which vested immediately, were granted to the Directors on November 30, 2009 with an exercise price of CAD$0.74 (£0.42) and a term of five years.

(i) Scott R. Cochlan was appointed to the Board on January 18, 2008 at which time 100,000 share options were awarded and vested immediately with an exercise price of CAD$2.09 (£1.04) and a term of five years.

Further details of the stock options in issue are given in Note 13 to the financial statements. There has been no trading of shares by the Directors since the year end.

Share options

An element of the Group's reward strategy is through the implementation of the Stock Option Plan, the purpose of which is to provide an incentive to the Directors, officers, employees, consultants and other personnel of the Group ("Optionees") to achieve the objectives of the Group; to give suitable recognition to the ability and industry of such persons who contribute materially to the success of the Group; and to attract and retain persons of experience and ability, by providing them with the opportunity to acquire an increased proprietary interest in the Company.

The Stock Option Plan is an unapproved stock option plan which is not intended to qualify for HM Revenue & Customs in the UK but complies with the rules and policies of the TSX-Venture stock exchange.

The Stock Option Plan is administered by the Remuneration and Nominating Committee. The number of options granted to an Optionee and the exercise price thereof are set at the time of grant, subject to any limitations imposed by the Stock Option Plan or any relevant regulatory authority, provided that if the ordinary shares are listed on a stock exchange, the exercise price shall not be lower than the market price of the ordinary shares on the date of the grant, where "market price" is defined as the highest closing trading

price of the ordinary shares on any stock exchange on which the ordinary shares are listed on the day of grant.

The exercise of an option may be conditional on the performance of the Company and, if the Remuneration and Nominating Committee so determines, on the performance of a subsidiary and/or the performance of the Optionee over such period and measured against such objective criteria as shall be determined by the Remuneration and Nominating Committee and notified in writing to the Optionee when the option is granted.

Signed on behalf of the Remuneration and Nominating Committee by:

Gregory J. Moroney
Non-Executive Director
March 24, 2010

Report of the Independent Auditors

To the Members of Xcite Energy Limited

We have audited the consolidated financial statements of Xcite Energy Limited, which comprise the consolidation of the parent company Xcite Energy Limited and its subsidiary Xcite Energy Resources Limited (collectively referred to as the "Group"), for the year ended December 31, 2009, which comprise the Consolidated Income Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Changes in Equity, the Consolidated Statement of Financial Position, the Consolidated Statement of Cash Flows, and related notes. These financial statements have been prepared under the accounting policies set out therein. The financial reporting framework that has been applied in their preparation is International Financial Reporting Standards (IFRS) as adopted by the European Union.

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

Respective responsibilities of directors and auditors

The Group's directors are responsible for the preparation of the financial statements in accordance with IFRS as adopted by the European Union.

The directors prepare financial statements for each financial period which give a true and fair view of the state of affairs of the Group and of the profit or loss of the Group for that period. The directors are also required to prepare financial statements in accordance with the rules of the London Stock Exchange for companies trading securities on the Alternative Investment Market and with those relating to companies trading securities on the Venture Exchange of the Toronto Stock Exchange. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the European Union and comply with IFRS as issued by the IASB, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for ensuring the annual report and the financial statements are made available on a website. Financial statements are published on the company's website in accordance with legislation in

the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the company's website is the responsibility of the directors. The directors' responsibility also extends to the ongoing integrity of the financial statements contained therein. Our responsibility is to audit the financial statements in accordance with International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. This included an assessment of whether the accounting policies are appropriate to the group's and parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Group's affairs as at December 31, 2009 and of the Group's loss for the year then ended and;

- have been properly prepared in accordance with IFRS as adopted by the European Union.

Separate opinion in relation to IFRS

As explained in note 1 to the consolidated financial statements, the Group, in addition to complying with its obligation to prepare consolidated financial statements in accordance with IFRS as adopted by the European Union, has also complied with IFRS as issued by the IASB

In our opinion, the consolidated financial statements give a fair and true view of the Group's affairs at December 31, 2009, and of the Group's loss for the year then ended in accordance with IFRS as issued by the IASB.

BDO LLP
Epsom
United Kingdom
March 24, 2010

Xcite Energy Limited
For the year ended December 31, 2009

Consolidated Income Statement (in Pounds Sterling)

	Note	**Year ended December 31 2009 £**	Year ended December 31 2008 £
Administrative expenses		**(789,127)**	(881,461)
Operating loss	3	**(789,127)**	(881,461)
Finance income – bank interest		**6,053**	344,910
Loss before taxation		**(783,074)**	(536,551)
Tax expense	5	**(97,144)**	(17,470)
Loss for the year attributable to Equity holders of the Company		**(880,218)**	(554,021)
Loss per share attributable to Equity holders of the Parent Company			
- basic and diluted	6	**(1.4p)**	(0.9p)

All results relate to continuing operations.

Consolidated Statement of Comprehensive Income (in Pounds Sterling)

	Year ended December 31 2009 £	Year ended December 31 2008 £
Loss for the year	**(880,218)**	(554,021)
Total comprehensive income for the year	**(880,218)**	(554,021)
Attributable to:		
Equity holders of the Company	**(880,218)**	(554,021)

The notes on pages 23 to 41 form part of these financial statements.

Xcite Energy Limited
For the year ended December 31, 2009

Consolidated Statement of Changes in Equity (in Pounds Sterling)

	Share Capital	Retained Earnings	Merger Reserve	Other Reserves	Total
	£	£	£	£	£
At January 1, 2008	21,774,150	(730,422)	218	1,645,481	22,689,427
Loss for the year to December 31, 2008	-	(554,021)	-	-	(554,021)
Total comprehensive loss for the year ended December 31, 2008	**-**	**(554,021)**	**-**	**-**	**(554,021)**
Transactions with owners:					
Issue of shares	478,475	-	-	-	478,475
Transfer upon exercise of share warrants	-	101,774	-	(101,774)	-
Fair value of share warrants and options	-	-	-	135,977	135,977
At January 1, 2009	**22,252,625**	**(1,182,669)**	**218**	**1,679,684**	**22,749,858**
Loss for the year to December 31, 2009	-	(880,218)	-	-	(880,218)
Total comprehensive loss for the year ended December 31, 2009	**-**	**(880,218)**	**-**	**-**	**(880,218)**
Transactions with owners:					
Issue of shares	1,947,646	-	-	**-**	**1,947,646**
Fair value of share warrants and options	-	-	-	**255,982**	**255,982**
At December 31, 2009	**24,200,271**	**(2,062,887)**	**218**	**1,935,666**	**24,073,268**

The notes on pages 23 to 41 form part of these financial statements.

Consolidated Statement of Financial Position (in Pounds Sterling)

	Note	**December 31 2009 £**	December 31 2008 £
Assets			
Non-current assets			
Intangible assets	7	**23,022,835**	21,996,871
Property, plant and equipment	8	**12,775**	21,317
Total non-current assets		**23,035,610**	22,018,188
Current assets			
Trade and other receivables	9	**17,767**	14,098
Cash and cash equivalents		**1,736,367**	1,828,183
Total current assets		**1,754,134**	1,842,281
Total assets		**24,789,744**	23,860,469
Liabilities			
Non-current liabilities			
Deferred tax	10	**505,167**	-
Total non-current liabilities		**505,167**	**-**
Current liabilities			
Trade and other payables	11	**211,309**	1,110,611
Total current liabilities		**211,309**	1,110,611
Net assets		**24,073,268**	22,749,858
Equity			
Share capital	13	**24,200,271**	22,252,625
Retained earnings	14	**(2,062,887)**	(1,182,669)
Merger reserve	14	**218**	218
Other reserves	14	**1,935,666**	1,679,684
Total equity		**24,073,268**	22,749,858

The notes on pages 23 to 41 form part of these financial statements. These financial statements were approved by the Board of Directors and authorised for issue on March 24, 2010 and were signed on its behalf by:

Richard Smith
Chief Executive Officer

Rupert Cole
Chief Financial Officer

Consolidated Statement of Cash Flows (in Pounds Sterling)

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Net cash flow from operating activities		
Loss for the period before tax	**(783,074)**	(536,551)
Adjustment for interest income	**(6,053)**	(344,910)
Adjustment for share based payments	**132,925**	51,757
Adjustment for depreciation	**9,287**	6,173
Movement in working capital		
- Trade and other receivables	**(3,669)**	68,691
- Trade and other payables	**(899,302)**	(3,932,061)
Foreign corporation tax received/(paid)	**7,813**	(17,470)
Net cash flow from operations	**(1,542,073)**	(4,704,371)
Cash flow from investing activities		
Additions to exploration and evaluation assets	**(902,907)**	(15,330,475)
Purchase of property, plant and equipment	**(745)**	(27,490)
Research & Development tax claim	**400,210**	-
Interest income	**6,053**	344,910
Net cash flow from investing activities	**(497,389)**	(15,013,055)
Cash flow from financing activities		
Net proceeds from issue of new shares	**1,947,646**	478,475
Cash flow from financing activities	**1,947,646**	478,475
Net decrease in cash and cash equivalents	**(91,816)**	(19,238,951)
Cash and cash equivalents at the beginning of the year	**1,828,183**	21,067,134
Cash and cash equivalents at the end of the year	**1,736,367**	1,828,183
Cash and cash equivalents comprise:		
Cash available on demand	**1,736,367**	1,828,183

The notes on pages 23 to 41 form part of these financial statements.

Notes to the Consolidated Financial Statements

1 Accounting Policies

Basis of preparation

The principal accounting policies adopted in the preparation of the consolidated financial statements are set out below.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations issued by the International Accounting Standards Board ("IASB"). The consolidated financial statements have also been prepared in accordance with IFRSs adopted by The European Union and they comply, therefore, with Article 4 of the EU International Accounting Standards ("IAS") Regulation.

The consolidated financial statements have been prepared on a going concern basis, taking into account the 2010 Outlook in the Management Discussion and Analysis on page 11 of these financial statements.

Basis of consolidation

The Company was incorporated with the sole purpose of acquiring its controlling interest in its directly held, wholly owned, subsidiary Xcite Energy Resources Limited ("XER"). XER was acquired on June 26, 2006 through a transaction under common control, as defined in IFRS 3 *Business Combinations*. As a result of the transaction, the equity shareholders of Xcite Energy Limited ("XEL" or the "Company") and XER became the equity shareholders of the combined entities. The Directors note that transactions under common control and those that involve a new shell company (XEL) with no business of its own acquiring a controlling interest in an existing entity (XER), are outside the scope of IFRS 3 and that there is no guidance elsewhere in IFRS covering such transactions.

IFRS contains specific guidance to be followed where a transaction falls outside the scope of IFRS. This guidance is included at paragraphs 10 to 12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.* This requires, *inter alia*, that where IFRS does not include guidance for a particular issue, the Directors may also consider the most recent pronouncements of other standard setting bodies that use a similar conceptual framework to develop accounting standards. In this regard it is noted that the UK Accounting Standards Board ("ASB") has issued an accounting standard covering acquisitions and mergers ("FRS 6"). FRS 6 allows for merger accounting to be applied where two or more companies are combined to form one group on terms such that the equity shareholders in each company become the equity shareholders in the combined entity.

Having considered the requirements of IAS 8, and the guidance included within FRS 6, it is considered appropriate to apply an accounting treatment similar to "merger accounting" as described by FRS 6 when dealing with the transaction in which the Company acquired its controlling interest in XER (together the "Group") in order to provide a true and fair view. The effect of the above is:

- New shares issued by XEL as consideration for the merger are recorded at their nominal amount in books of XEL;
- The net assets of XER and XEL are combined using existing book values;

- No amount is recognised as consideration for goodwill or negative goodwill; and
- The consolidated profit and loss includes profits of each company for the entire period, regardless of the date of the merger, and the comparative amounts in the consolidated accounts are restated to the aggregate of the amounts recorded by the two companies.

Revenue

Revenue arises from the sale of oil produced from the Bentley field on the UK Continental Shelf and reflects the actual sales value, net of value-added-tax ("VAT")and overriding royalties. Revenues are recognised when the risks and rewards of ownership together with effective control are transferred to the customer and the amount of revenue and associated costs incurred in respect of the relevant transaction can be reliably measured. Revenue is not recognised unless it is probable that the economic benefits associated with the sales transaction will flow to the Group.

Finance income is recognised on an accruals basis and is disclosed separately on the face of the Income Statement.

Foreign currency

The functional currency of the Group is Pounds Sterling. Transactions entered into by the Group in a currency other than the functional currency are recorded at the rates ruling when the transactions occur. Foreign currency monetary assets and liabilities are translated at the rates ruling at the Balance Sheet date. Exchange differences arising on the retranslation of unsettled monetary assets and liabilities are recognised immediately in the Income Statement.

Financial assets

The Group's financial assets are classified as loans and receivables and comprise the following:

Other receivables – these are measured on initial recognition at fair value and are subsequently measured at amortised cost. Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset value is impaired.

Cash and cash equivalents – comprise cash on hand and cash on deposit with an original maturity of less than three months and are subject to an insignificant risk of changes in value.

Financial liabilities

The Group's financial liabilities comprise trade and other payables and are recognised on initial recognition at fair value and are subsequently measured at amortised cost.

Current taxation

The total tax expense represents the sum of current and deferred tax. Current tax is based on the taxable result for the period. The taxable result may differ from the net result as reported in the Income Statement as it may exclude certain items of income or expense that are taxable or deductible in other periods and it further excludes items that are never taxable or deductible.

The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the Balance Sheet date.

Deferred taxation

Deferred tax assets and liabilities are recognised where the carrying amount of an asset or liability in the Balance Sheet differs to its tax base.

Recognition of deferred tax assets is restricted to those instances where it is probable that taxable profit will be available against which the difference can be utilised. The amount of the asset or liability is determined using tax rates that have been enacted or substantively enacted by the Balance Sheet date and are expected to apply when the deferred tax liabilities/assets are settled/recovered. Deferred tax assets and liabilities are offset when the Company has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority on either:

- The same taxable group company; or
- Different group entities which intend either to settle current tax assets and liabilities on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax assets or liabilities are expected to be settled or recovered.

Share based payments

The Company has a Stock Option Plan as described in Note 13. The share based payment expense arising under this Stock Option Plan is recorded in the Income Statement, or as a direct reduction in share capital where the charge relates to the issue of such share capital, or as an increase in exploration and evaluation assets for all options granted in the period, with a corresponding increase recorded in other reserves. The share based expense is calculated on the estimated fair values at the time of the grant and the expense is recognised over the vesting period of the options. Upon the exercise of the stock options, consideration paid is recorded as an increase in share capital and amounts previously recorded in other reserves are transferred to retained earnings. In the event that vested options expire unexercised, previously recognised share based payment expense associated with such stock options is not reversed.

The Black-Scholes model is used to value all share based payments.

Where equity instruments are granted to persons other than employees, the Income Statement is charged with the fair value of the goods and services received.

Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual costs. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying value of assets and liabilities within the next financial period are discussed below.

(a) Income taxes

There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Company recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(b) Fair value of share options and warrants

The Group has valued the fair value of the outstanding share options and warrants over the Company's shares using the Black-Scholes valuation methodology. The Group uses judgement to derive such valuation model assumptions that are mainly based on market conditions existing at the Balance Sheet date.

(c) Impairment of Exploration and Evaluation ("E&E") assets

A review is performed at the end of each financial period for any indication that the value of the Group's E&E assets may be subject to impairment. In the event of any such indication, an impairment test is carried out and, if necessary, an impairment charge is made representing the surplus of capitalised cost over estimated recoverable value of the related commercial oil reserves. Estimated recoverable value is based upon anticipated discounted net cash flows attributable to such oil reserves.

Intangible fixed assets – Exploration and Evaluation Assets

Capitalisation

Certain costs (other than payments to acquire the legal right to explore) incurred prior to acquiring the rights to explore are charged directly to the Income Statement. All costs incurred after the rights to explore an area have been obtained, such as geological and geophysical costs and other direct costs of exploration (drilling, trenching, sampling and technical feasibility and commercial viability activities) and appraisal are accumulated and capitalised as intangible Exploration and Evaluation ("E&E") assets.

E&E costs are not amortised prior to the conclusion of appraisal activities. At completion of appraisal activities if technical feasibility is demonstrated and commercial reserves are discovered, then, following development sanction, the carrying value of the relevant E&E asset will be reclassified as a development and production asset, but only after the carrying value of the relevant E&E asset has been assessed for impairment, and where appropriate, its carrying value adjusted. If after completion of appraisal in an area it is not possible to determine technical feasibility and commercial viability, or if the legal right to explore expires or if the Company decides not to continue exploration and evaluation, the carrying value of the E&E asset is written off to the Income Statement in the period the relevant events occur.

Impairment

If and when facts and circumstances indicate that the carrying value of an E&E asset may exceed its recoverable amount an impairment review is performed. This is carried out by identifying groups of assets, within the E&E asset, which together form the Cash Generating Unit ("CGU") and comparing the carrying value of the CGU with its recoverable amount. Any shortfall in carrying value, the impairment loss, is written off directly to the Income Statement. The recoverable amount of the CGU is determined as the higher of its fair value less costs to sell and its value in use.

Property, plant and equipment

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. All repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation on assets is calculated using the straight-line method to allocate their cost over their estimated useful life, as follows:

- Furniture, fittings and computing equipment 3-5 years

New accounting standards adopted during the year

The following new standards and amendments to standards are mandatory for the first time for the financial year beginning January 1, 2009:

- IAS 1 (revised) 'Presentation of Financial Statements' prohibits the presentation of items of income and expense (that is 'non-owner changes in equity') in the statement of changes in equity, requiring 'non-owner changes in equity' to be presented separately from owner changes in equity. All 'non-owner changes in equity' are required to be shown in a performance statement. The Group has elected to present two statements: an income statement and a statement of comprehensive income. These consolidated financial statements have been prepared under the revised presentation requirements for primary statements.

- IFRS 8 'Operating Segments' replaces IAS 14 'Segment Reporting'. Adoption of IFRS 8 has resulted in no changes in the Group's identification of reporting segments.

- Amendment to IAS 32 'Classification of Rights Issues' was proposed to clarify the classification of instruments that give the holder the right to acquire an entity's own equity instruments at a fixed price when that price is stated in a currency other than the entity's functional currency. The amendment was applied retrospectively but had no impact upon the Group or its prior period comparatives.

- Amendment to IFRS 'Share-based Payment: Vesting Conditions and Cancellations' became effective January 01, 2009 and sought to clarify that vesting conditions are service and performance conditions only. This amendment had no impact upon the Group or its prior period comparatives.

- In March 2009 the IASB issued Amendment to IFRS 7 'Improving Disclosures About Financial Instruments', in part as a response to the world-wide credit crisis, to introduce a fair value hierarchy and to enhance liquidity risk disclosures. The amendment was endorsed and became effective January 1, 2009.

- 'Improvements to IFRSs (2008)' was issued in May 2008 and sought to clarify the requirements of IFRSs and eliminate inconsistencies between Standards. The adoption had no impact upon the Group or its prior period comparatives.

- Amendments to IFRIC 9 and IAS 39 'Embedded Derivatives' were issued in March 2009. The proposed amendments clarify that entities are required to assess whether hybrid contracts reclassified out of the fair value through profit or loss category contain embedded derivatives that require separation and that assessment has to be made based on the conditions that existed at the time of the initial recognition of the contracts. The amendments were endorsed and became effective January 1, 2009.

Whilst the Group has also adopted the following amendments and interpretations during the financial year, these are not considered relevant for the Group and have therefore had no impact in these financial statements:

- Amendment to IAS 23 'Borrowing costs';
- Amendments to IAS 32 and IAS 1 'Puttable Financial Instruments and Obligations Arising on Liquidation';
- Amendments to IAS 39 and IFRS 7 'Reclassification of Financial Instruments';
- Amendments to IFRS 1 and IAS 27 'Cost of an Investment in a Subsidiary, Jointly-Controlled Entity of Associate';
- Revised IFRS 3 'Business Combinations';
- Amendments to IAS 27 'Consolidated and Separate Financial Statements';
- Amendment to IAS 39 'Financial Instruments: Recognition and Measurement; Eligible Hedged Items';
- IFRIC 13 'Customer Loyalty Programmes';
- IFRIC 15 'Agreements for the Construction of Real Estate';
- IFRIC 16 'Hedges of a Net Investment in a Foreign Operation';
- IFRIC 17 'Distribution of Non-Cash Assets to Owners';
- IFRIC 18 'Transfer of Assets From Customers'; and
- IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments'.

New standards and interpretations not yet applied

The new standards and interpretations listed under the "Status of EU Endorsement" section below, which have been issued by the IASB and the IFRIC, have yet to be endorsed by the European Union and/or are effective for future periods and thus have not been adopted in these consolidated financial statements. A description of these standards and interpretations, together with (where applicable) an indication of the effect of adopting them, is set out in the section below. None are expected to have a material effect on the reported results or financial position of the Group.

In June 2007 the IASB issued an exposure draft on the amendments to IFRS 2 'Share-based Payment'. The proposals in the exposure draft respond to requests for guidance on how an entity that receives goods or services from its suppliers (including employees) should account for the certain cash-settled arrangements. The proposed amendment to IFRS 2 clarifies that IFRS 2 can apply even if the entity that receives the goods or services from its suppliers has no obligation to make the required shared-based cash payments.

Status of EU endorsement

Entities in EU Member States which report in accordance with EU-endorsed IFRS can only apply IFRSs and IFRICs where the endorsement process has been completed at the date of approval of their financial statements. Of the standards and interpretations listed above, the following had not yet been endorsed by the European Union at the date these consolidated financial statements were authorised for issue:

- IFRS 9 'Financial Instruments';
- Amendment to IFRIC 14 'Prepayments of a Minimum Funding Requirement';
- IFRIC 19 'Extinguishing Financial Liabilities with Equity Instruments';
- 'Improvements to IFRSs (2009)';
- Amendments to IFRS 2 'Group Cash-settled Share-based Payment Transactions';

- Amendments to IFRS 1 'Additional Exemptions for First-Time Adopters'; and
- Revised IAS 24 'Related Party Disclosures'.

2 Segment Information

The Group only operates in a single business and geographical segment. The Group's single line of business is the appraisal and development of oil and gas reserves and the geographical segment in which it currently operates is the North Sea.

3 Operating Loss

The operating loss is stated after charging the following:

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Auditors' remuneration:		
- Group audit fee	15,000	15,000
- Audit of subsidiary pursuant to legislation	20,000	20,000
- Tax advisory	21,758	17,200

The Group incurred total charges in respect of equity-settled share based payments in the current year of £255,982 (2008: £135,977). Of this, £154,386 (2008: £89,174) was in respect of employees (see Note 4). In accordance with the Group's accounting policy, £123,057 (2008: £84,220) has been capitalised within E&E assets and the balance of £132,925 (2008: £51,757) has been expensed within operating loss.

4 Staff Costs and Directors' Emoluments

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

	Year ended December 31 2009	Year ended December 31 2008
Technical and administration	**7**	7

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

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Wages and salaries	**1,137,280**	1,045,969
Social security costs	**140,219**	129,393
Share based payments	**154,386**	89,174
	1,431,885	1,264,536

b) Executive Directors' emoluments

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Wages and salaries	**638,700**	638,700
Social security costs	**79,587**	80,237
Share based payments charge	**64,611**	-
	782,898	718,937

The Executive Directors comprise the key management personnel of the Group.

In addition to the above, during the year the Group paid to Roger Ramshaw, Gregory Moroney, Scott Cochlan, Timothy Jones and A. Murray Sinclair in their capacity as Non-Executive Directors of the Group fees of £21,750 (2008: £36,750), £12,000 (2008: £11,250), £9,000 (2008: £9,000), £15,750 (2008: £nil) and £nil (2008: £4,500) respectively. Charges in respect of share based payments for the Non-Executive Directors in the year to December 31, 2009 were £92,789 (2008: £46,803).

5 Tax Expense

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Current tax		
UK tax on income for the year	**-**	7,987
Research & Development tax credit	**(400,210)**	-
Adjustments in respect of prior years	**(7,813)**	9,483
Total current tax	**(408,023)**	17,470

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Deferred tax		
Origination of temporary differences (see note 10)	**505,167**	-
Total deferred tax	**505,167**	-
Total tax charge	**97,144**	17,470

The tax assessed for the year is different to the standard rate of corporation tax in the British Virgin Islands (0%). The differences are explained below.

	Year ended December 31 2009	Year ended December 31 2008
	£	£
Loss before tax	**(783,074)**	(536,551)
Loss before tax multiplied by the standard rate of corporation tax in the British Virgin Islands of 0% (2008: 0%)	-	-
Effects of:		
UK Tax suffered on income	-	(7,987)
Prior period adjustments relating to UK Tax	7,813	(9,483)
Research & Development tax credit	400,210	-
Temporary differences	(505,167)	-
Tax charge for the year	**(97,144)**	(17,470)

Current tax is calculated at the rates prevailing in the respective jurisdictions. XEL is incorporated in the British Virgin Islands, a jurisdiction subject to a tax exemption. XER is incorporated in the UK and therefore subject to current tax on taxable profits at a rate of 28% or 21% where the profits fall within the limits of the small companies rate (2008: 30% or 19%).

From April 1, 2008 the standard rate of corporation tax in the UK decreased to 28% and the small companies' rate increased to 21%. XER is, however, considered to be a company which profits from oil extraction and oil rights in the UK and the UK Continental Shelf and, therefore, from April 1, 2008 continued to be subject to corporation tax on taxable profits at a rate of 30% or 19% where the profits fall within the limit of the small companies rate.

6 Loss per Share

The basic loss per share is calculated by dividing the loss attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. The calculation of basic loss per ordinary share for the year ended December 31, 2009 is based on a loss of £880,218 (year to December 31, 2008: loss of £554,021) and on shares of 63,775,635 (year to December 31, 2008: 61,336,321), being the weighted average number of ordinary shares in issue during the year.

Details of potentially dilutive financial instruments are given in Note 13 of these financial statements. In connection with the equity fund raising, which was completed on March 18, 2010, a total of 61,972,394 new shares have been issued since the year end. This also is set out in more detail in Note 13 to these financial statements.

7 Intangible Assets

	Licence Fees	
	2009	2008
Exploration and Evaluation Assets	**£**	£
Opening cost and carrying value at January 1	**253,287**	126,567
Additions	**221,760**	126,720
Closing cost and carrying value at December 31	**475,047**	253,287

	Appraisal and Exploration Costs	
	2009	2008
	£	£
Opening cost and carrying value at January 1	**21,743,584**	6,455,609
Net additions	**804,204**	15,287,975
Closing cost and carrying value at December 31	**22,547,788**	21,743,584

	Total	
	2009	2008
	£	£
Opening cost and carrying value at January 1	**21,996,871**	6,582,176
Net additions	**1,025,964**	15,414,695
Closing cost and carrying value at December 31	**23,022,835**	21,996,871

The costs associated with the continuing appraisal of Block 9/3b have been capitalised in accordance with the Group's accounting policy in Note 1.

Based on the Group's success in drilling its final appraisal well on Block 9/3b, and in view of the forecast revenue streams and cash flows of this project, the Directors are satisfied that the carrying amount of the related intangible assets as disclosed above will be recovered in full and that there is no need for any impairment provision. The situation will be monitored by Management and adjustments made in future periods if future events indicate that such adjustments are appropriate.

8 Property, Plant and Equipment

	Furniture, fittings and computing equipment
Year ended December 31, 2008	£
Opening net book amount at January 1, 2008	-
Additions	27,490
Depreciation charge	6,173
Closing net book amount at December 31, 2008	21,317
At December 31, 2008	
Cost or valuation	27,490
Accumulated depreciation	6,173
Cost and net book amount	21,317
Year ended December 31, 2009	
Opening net book amount at January 1, 2009	21,317
Additions	745
Depreciation charge	9,287
Closing net book amount at December 31, 2009	**12,775**
At December 31, 2009	
Cost or valuation	28,235
Accumulated depreciation	15,460
Net book amount	**12,775**

9 Trade and Other Receivables

	December 31 2009	December 31 2008
	£	£
Indirect taxes receivable	**13,842**	10,173
Other receivables	**3,925**	3,925
	17,767	14,098

10 Deferred tax

	December 31 2009	December 31 2008
	£	£
At January 1	**-**	-
Profit and loss charge	**505,167**	-
At December 31	**505,167**	-

The total deferred tax liability at December 31, 2009 comprised temporary differences arising from a R&D tax claim in the UK. As at December 31, 2009 the Group had pre-trading losses of £714,499 (December 31, 2008; pre-trading losses of £519,454). No deferred tax asset has been recognised on these losses until such time as the Group is expected to have sufficient taxable profits in future periods against which the asset can be relieved.

11 Trade and Other Payables

	December 31 2009	December 31 2008
	£	£
Trade payables	**118,739**	150,092
Social security and other taxes payable	**46,527**	47,318
Accruals and other payables	**46,043**	913,201
	211,309	1,110,611

12 Financial Instruments

The Group's principal financial instruments are other receivables, trade and other payables and cash, which are denominated in various currencies. The main purpose of these financial instruments is to finance the Group's ongoing operational requirements.

The Group does not currently trade in derivative financial instruments. The principal financial risks faced by the Group are credit risk, liquidity and foreign currency risk. Policies for the management of these risks, which have been consistently applied throughout the period, are shown below.

Non-market risk

a) Credit risk

Group management has a responsibility to minimise the risk of default on credit advanced to customers and on deposits held by suppliers. At present the Group has no customers and therefore advances no credit. Deposits held by suppliers comprise an office rent deposit recorded as receivables and, as such, it is regarded as low risk. On this basis, Group management is satisfied that any credit risk has been minimised.

Credit risk also arises from cash and cash equivalents and deposits held by banks and financial institutions. To minimise the credit risk on banks and financial institution deposits, only independently rated parties with a minimum rating of "AA" or better are used by the Group to hold such deposits.

b) Liquidity risk

Group management has responsibility for reducing exposure to liquidity risk and for ensuring that adequate funds are available to meet anticipated requirements. The Group's objective is to ensure that sufficient liquid resources are available to meet its obligations on time. Liquidity risk is managed on a consolidated basis by forecasting operational requirements and financial commitments. It operates according to the policies and guidelines established by the Board. Cash management is carried out centrally.

	Carrying Amount	
	December 31 2009	December 31 2008
	£	£
Financial assets – loans and receivables measured at amortised cost		
- Cash	**1,736,367**	1,828,183
- Receivables (current)	**3,925**	3,925
	1,740,292	1,832,108
Financial liabilities – measured at amortised cost		
- Payables (current)	**164,782**	1,063,293

The Management believes that as all financial instruments are short term, the fair values for all such items equate to their carrying amount.

The accounting policies for financial assets and financial liabilities are disclosed in Note 1.

Market risk

c) Interest rate and foreign currency risks

The currency and interest profile of the Group's financial assets and liabilities are as follows:

	Interest Free Liabilities	
	December 31 2009	December 31 2008
	£	£
Sterling	**158,756**	1,063,293
CAD$	**6,026**	-
	164,782	1,063,293

	Floating rate assets	**Interest free assets**	**Total**
	December 31 2009 £	**December 31 2009 £**	**December 31 2009 £**
Sterling	**1,681,622**	**3,675**	**1,685,297**
CAD$	**53,437**	**250**	**53,687**
USD$	**1,308**	**-**	**1,308**
	1,736,367	**3,925**	**1,740,292**

	Floating rate assets	Interest free assets	Total
	December 31 2008 £	December 31 2008 £	December 31 2008 £
Sterling	1,788,298	3,675	1,791,973
CAD$	34,833	250	35,083
USD$	5,052	-	5,052
	1,828,183	3,925	1,832,108

Sterling floating rate assets earn interest at circa 25 basis points below the Bank of England Base Rate per annum. US$ floating rate assets earn interest at circa 25 basis points below the Federal Reserve Rate per annum. Cash deposits are only kept with banks with "AA" rating or better. The policy of the Group is to

ensure that all cash balances earn a market rate of interest and that interest rate exposures are regularly reviewed and managed.

Foreign currency risk arises where purchase transactions are undertaken in a currency other than Sterling (transactional risk) and where non-Sterling financial derivatives are held at the Balance Sheet date (translational risk). The group is exposed to exchange rate movements in the US Dollar and, to a lesser extent, the Canadian Dollar and the Euro. In light of the infrequency and relative small value of such non-Sterling denominated transactions and balances, the Group considers that at present its foreign currency risk is not material. The Group will continue to monitor its exposure to such foreign currency risks and will manage future risks using derivative financial instruments as considered appropriate.

As the Company is at the development stage, it is not yet subject to significant exposure to the Sterling/US Dollar exchange rate fluctuations.

(d) Interest rate sensitivity analysis

Interest rate sensitivity analysis has been determined based on the exposure to interest rates for financial instruments during the financial period.

Based on the Group's cash balances during the year, if interest rates had been 50 basis points higher/lower and all other variables were held constant, the Group's loss for the year ended December 31, 2009 would decrease/increase by £5,777 (December 31, 2008; loss would decrease/increase by £47,652).

13 Share Capital

	Number of shares December 31 2009	Number of shares December 31 2008
Authorised		
- Ordinary shares of no par value each	**Unlimited**	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value each	**71,555,798**	61,413,800

	£ Value of shares December 31 2009	£ Value of shares December 31 2008
Authorised		
- Ordinary shares of no par value each	**Unlimited**	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value each	**24,200,271**	22,252,625

Xcite Energy Limited is registered in the British Virgin Islands under the BVI Business Companies Act 2004. Under BVI laws and regulations there is no concept of "share premium", and all proceeds from the sale of no par value equity shares is deemed to be share capital of the Company.

Shares issued

On October 7, 2009 the Company announced the closing of the private placement of an additional 10,141,998 new ordinary shares, raising gross proceeds of £2.1 million (CAD$3.8 million).

Stock Option Plan

An element of the Group's remuneration and reward strategy is through the implementation and use of the Stock Option Plan, the purpose of which is to provide an incentive to the Directors, officers and key employees of the Group to achieve the objectives of the Group; to give suitable recognition to the ability and industry of such persons who contribute materially to the success of the Group; and to attract and retain persons of experience and ability, by providing them with the opportunity to acquire an increased proprietary interest in the Company.

The Stock Option Plan is administered by the Remuneration and Nominating Committee. At December 31, 2009 there were 6,530,000 options outstanding (2008: 4,350,000).

On January 8, 2009 the Company issued a total of 850,000 share options with an exercise price of CAD$0.10. On April 23, 2009 the Company issued a further 100,000 share options with an exercise price of CAD$0.29. On October 12, 2009 the Company issued a further 200,000 share options with an exercise price of CAD$0.37. On November 30, 2009 the Company issued a further 1,100,000 share options with an exercise price of CAD$0.74. Whilst no share options were exercised during the year ended December 31, 2009 (year ended December 31, 2008: nil) a total of 70,000 share options expired following the resignation of a Non-Executive Director, in accordance with the Stock Option Plan rules.

Details of the Directors' interests in ordinary shares held under the Stock Option Plan are given in the Report of the Remuneration and Nominating Committee.

The following assumptions were used in the share option pricing model for the grant of options during the year at the following dates:

Grant Date	January 8, 2009	April 23, 2009	October 12, 2009	November 30, 2009
Share bid price	CAD$0.04	CAD$0.25	CAD$0.37	CAD$0.73
Exercise price	CAD$0.10	CAD$0.29	CAD$0.37	CAD$0.74
Expected volatility	55%	59%	60%	59%
Expected life	5 years	5 years	5 years	5 years
Expected dividends	0.0%	0.0%	0.0%	0.0%
Risk-free interest rate	1.83%	2.01%	2.86%	2.41%

The expected share price volatility was determined by a review of the share trading performance of comparable oil and gas companies in the same industry sector.

The total cost to the Group in respect of equity-settled share based payment transactions under the Stock Option Plan in the year to December 31, 2009 was £0.25 million (2008: £0.13 million). Of this total, £0.13 million (2008: £0.05 million) has been charged to the Income Statement and £0.12 million (2008: £0.08 million) has been capitalised under intangible assets in accordance with the Group's accounting policy.

Share warrants

On May 7, 2009 a total of 9,948,700 shareholder warrants over the ordinary share capital of the Company expired. On June 26, 2009 and November 15, 2009 a total of 700,000 and 1,012,500 broker warrants over the ordinary share capital of the Company expired respectively. On November 15, 2009 a total of 163,500 Ammonite warrants over the ordinary share capital of the Company expired.

The Group had no outstanding warrants over the ordinary share capital of the Company at December 31, 2009 (as at December 31, 2008: 11,824,700 warrants).

14 Owners' equity

The following explains the nature and purpose of each reserve within owners' equity:

- Retained Earnings: Cumulative profits recognised in the Group Consolidated Statement of Comprehensive Income less cumulative losses and distributions made.

- Merger Reserve: The difference between the nominal value of the shares issued to acquire a subsidiary and the nominal value of the shares acquired.

- Other Reserves: The fair value of share based payments and warrants granted over ordinary shares in the Company at the date of grant.

15 Commitments and contingencies

At December 31, 2009 the Company had total commitments under non-cancellable operating leases expiring as follows:

	2009	2008
	£	£
Within one year	**593**	593

16 Subsequent events

The most significant achievements from 2009, which were formally announced at the end of the year and early in 2010, were the securing of the important building blocks of the 'Bentley Alliance', the innovative

commercial structure that Xcite Energy Resources Limited ("XER") has created to take the Bentley field into development.

Since the balance sheet date, Applied Drilling Technology International, the well management arm of Transocean Drilling U.K. Limited, signed a letter of intent for the provision of a heavy duty, deep water jack-up drilling unit to undertake the drilling and testing of the 9/3b-R well in 2010. AMEC plc has signed an agreement to provide its technical expertise, engineering and project management skills to assist the Bentley Alliance demonstrate the reserves potential of the Bentley field and subsequently bring it into production.

An important underpinning of the field development and the economics of the field was provided when BP Oil International Limited ("BPOI"), a wholly owned subsidiary of BP plc, signed a Supply and Offtake agreement to market and sell the Bentley crude oil in return for a fee per barrel which incentivises them to maximise the price per barrel achieved for XER by minimising the discount to Brent crude. In addition, when XER moves to full field development of Bentley, BP will procure $20 million of financing from a commercial bank with credit support to assist in the process.

Finally, the Company was pleased to welcome Challenger Minerals (North Sea) Limited ("CMNS") as a farm-in partner in the Bentley field, through an undertaking to provide $4 million (£2.7 million) towards the cost of the 9/3b-R well in exchange for 4% of the Bentley field; a deal that applied a pre-money value of $100 million to the Bentley field. This will be enacted through an earn-in mechanism which, when the $4 million is paid, will allow CMNS to join the Bentley field licence at any time prior to the commencement of the first phase development of the field. This is a fitting final piece of the Bentley Alliance, which creates important additional synergies as the Company moves ahead to drill the 9/3b-R well and beyond.

As noted above, a further funding success with the capital markets was completed in March 2010 to enable the financing of the 9/3b-R well. This financing comprised the £2.7 million from the CMNS farm-in undertaking, together with an equity share issue to raise approximately £25 million gross and £23.5 million net of costs, which in aggregate provides adequate funds for the 9/3b-R well and working capital for the foreseeable future. Based on this, the Company can now look forward to demonstrating the potential of the Bentley field and confirming its value as a significant North Sea oil field.

17 Related parties

XEL is a company incorporated in the British Virgin Islands and whose registered office is at Geneva Place, Waterfront Drive, PO Box 3469 Road Town, Tortola, VG1110, British Virgin Islands. The Group defines related parties as:

- The Group's Executive and Non-Executive Directors;
- The Company's subsidiary XER;
- The Company's key management; and
- Companies in which the Executive Directors exercise significant influence.

XEL provided, using a loan facility, its wholly owned subsidiary, XER, with net cash funding of £1.78 million during the year to December 31, 2009 (year to December 31, 2008: £12.36 million) to finance XER's

operational requirements. No interest is payable on the outstanding loan balance from XEL, which is unsecured and repayable on demand. The total balance owing by XER to XEL at December 31, 2009 was £22.60 million (as at December 31, 2008: £20.82 million).

The Executive Directors have received remuneration, details of which are given in Note 4 to these financial statements. The Executive and Non-Executive Directors have also been granted certain share options over the ordinary share capital of the Company, details of which are given in these financial statements.

Officers and Principal Advisors

Directors
Richard E. Smith
Rupert E. Cole (Company Secretary)
Stephen A. Kew

Non-Executive Directors
Roger S. Ramshaw
Gregory J. Moroney
Scott R. Cochlan
Timothy S. Jones

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Stock exchanges
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Code: XEL.L

TSX, TSX-Venture Exchange
Code: XEL.V