Xcite Energy Limited

Annual Report and Financial Statements

for the year ended December 31, 2008

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Contents

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.

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.

A. Murray Sinclair was a Non-Executive Director of the Company and Chairman of the Audit Committee until his resignation on November 4, 2008. Since June 2003, Mr. Sinclair has been the Managing Director of Quest Capital Corp., an asset-backed lending organisation listed on the TSX, AMEX and AIM Stock Exchanges which focuses on providing financial services, specifically mortgages and bridge loans, to small and mid-cap companies. Since December 1996, Mr. Sinclair has also been a director of Quest Management Corp., a management company wholly-owned by Quest Capital Corp. Mr. Sinclair serves on the board of directors of a number of public companies.

Chairman's and Chief Executive's Review

The highlight of the year has undoubtedly been the successful drilling and testing of the 9/3b-5 appraisal well on Bentley, the now officially recognised name of the field by the UK Department of Energy and Climate Change. Previous operators of Block 9/3b in the 1970's and 1980's had been unable to flow the reservoir to surface, but 9/3b-5 demonstrated that the previous challenges presented by the relatively heavy, viscous crude oil and unconsolidated formation could be overcome with the application of modern drilling and completion techniques. The test was not designed to achieve headline flow rates, but if its results are used to model an appropriate horizontal completion in the Bentley reservoir they show that flow rates of up to 6,000 barrels per day can be obtained depending on the completions used and well efficiencies. The Bentley reservoir fluid was confirmed to be very similar in character and properties to the Bressay oil field, approximately 6 km to the North West and operated by StatoilHydro.

Drilling the 9/3b-5 well also fulfilled a licence obligation for Xcite Energy Resources Limited ("XER") and, as a consequence, the promote licence awarded in 2003 successfully moved into its second four-year term and converted to a conventional licence. As part of this change in status, a 50% relinquishment of acreage was required and this was achieved with full retention of the Bentley Field, the Bentley East prospect, Lead B and two further leads in the lower Jurassic formation.

Since completing the well the XER team has undertaken extensive analysis and studies to determine the optimum route for commercial development of the large resource that forms Bentley. Your Board now believes that commercial development is possible and this position is supported by the updated Competent Person's Report ("CPR") from RPS Energy, a division of RPS Group plc, that attributes to Bentley Contingent Resources - Development Pending, the highest category of Contingent Resources before the Reserves category under latest industry classification. This is a significant step up from the previous category of Resources prior to the drilling of the 9/3b-5 well.

In addition to this important category improvement, RPS Energy has assigned a significantly higher volume of recoverable resources to Bentley in the Low and Base cases reported. The Low case now reported is 72 million barrels ("MMbbls") (previously 37 MMbbls), and the Base case is 122.5 MMbbls (previously 68 MMbbls). It should also be noted that there is significant potential upside in the recoverable volumes reported from a range of reservoir parameters, which will be investigated in the next reservoir intervention.

Finally, and most significantly for our shareholders, the probability of commercial success for the Bentley field as reported by RPS Energy has increased from 50% to 70%.

Using these increased volumes of recoverable oil and the detailed full field development plan assumptions, the gross NPV_{10} of the field in the Base case has increased from US$460 million ("MM") to US$780MM and, with the increased probability of commercial success, the 'risked' NPV_{10} has increased from US$230MM to US$546MM; an increase of over 200%.

The combination of higher resources categorisation, increased recoverable volumes of oil, significantly increased economic value and an improved probability of commercial success, provides the strongest vindication for the XER team's approach to and work programme for the Bentley 9/3b-5 well. We would like to take this opportunity to thank the XER team for their work during the year that has demonstrated and detailed how the potential of the Bentley field should be developed and transformed into real value for the Company's shareholders.

Your Board views this new CPR as a major success and a robust justification of the investment made by shareholders in the Company and in the potentially world class Bentley asset. It is also encouraging to note that StatoilHydro has made public its intention to proceed with full field development of the nearby Bressay field and forecasts first oil in 2014.

The currently proposed path to development for Bentley is via an Early Production System (EPS) followed by the full field development. This EPS will be designed to address the remaining issues arising from the 9/3b-5 well as outlined in the CPR and, therefore, better delineate the range of potential performance of the Bentley field and the range of recoverable reserves. This, in turn, would upgrade the Bentley classification from Contingent Resources to Reserves. The important information obtained from the EPS will also allow us to optimise the full field development facilities to take maximum advantage of the significant upside potential that we believe exists in the field.

Although crude oil prices have fallen back sharply from the peak seen in 2008, the longer term prices used for Bentley in the CPR are widely forecast to return, thus supporting its economic development with the current high cost assumptions. Moreover, if the current high costs fall in response to lower oil prices, the Bentley field would demonstrate commercial development economics at current oil prices.

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 throughout year and Murray Sinclair chaired the Audit Committee until his resignation from the Board in November. We appreciate the contribution that Murray was able to make to the Company during its first year and we are pleased to welcome Tim Jones to the Board and as Chairman of the Audit Committee in his place.

There will not be many corporate reports at present that do not feel it necessary and appropriate to make mention of the current financial conditions and the effect that these have had both on their own activities and on the industry sector in which they operate. The Company, together with many others in its sector, has seen its share price decay to a level that, by any reasonable measure, bears little correlation to its underlying asset value.

Our belief remains in the value of the Bentley field as a potentially world class asset, which has been increased significantly with the success of the 9/3b-5 well and the subsequent study work that has been completed during 2008. The new CPR from RPS Energy bears witness to this, with the higher resources classification, the increase in recoverable volumes and the improved probability of commercial success.

Until such time as confidence is restored and the global equity and credit markets return to a semblance of normality, it is unlikely that the asset value will be reflected in the Company's share price. It will, therefore, be difficult for the Company to make significant commitments to move forward with the EPS programme until such time as the market conditions improve. However, we are currently pursuing a number of financing initiatives that are designed to see the Company through to the other side of the current financial turbulence, probably towards the end of 2010, together with commercial initiatives involving farm-in partners and production sharing contractors to facilitate further work on the field. There is no certainty of success with these initiatives, but the Board and the management team are focused on this programme to restore shareholder value.

Roger Ramshaw	**Richard Smith**
Chairman	Chief Executive Officer
March 26, 2009	

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, 2008. This MD&A is dated March 26, 2009. These documents and additional information about XEL 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, 2008, which include the results of the operating subsidiary Xcite Energy Resources Limited ("XER") for the twelve months to December 31, 2008. The comparative results comprise the fourteen months to December 31, 2007. 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, 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 twelve months to December 31, 2008 and the comparative of the fourteen months 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 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 and therefore they comply with Article 4 of the EU IAS Regulation.

	12 Months ended December 31	14 Months ended December 31
	2008	2007
	£	£
Net loss	**(554,021)**	(730,289)

Loss per share (basic and diluted)	**(0.01p)**	(0.02p)
Total assets	**23,860,469**	27,732,099

Liquidity and Capital Resources

The cash balance as at December 31, 2008 was £1.83 million, compared with £21.07 million as at December 31, 2007, the decrease being attributable to the operating costs of the Group during the period, of which the major part was the significant spend on drilling the Bentley 9/3b-5 appraisal well in the first quarter of 2008. This was offset by additional investment in share capital of £0.48 million during the year.

Following the success of the drill stem test in February 2008, the remaining proceeds from the 2007 financings are being used to plan for the development of the Bentley field, including fluid and reservoir studies, field development studies and marketing and refining studies, together with the review of other business development opportunities and general corporate working capital requirements.

Lease and Contractual Commitments

As at December 31, 2008 the Group has no material lease or contractual commitments.

Operations and Administrative Expenses

The Group is in the development phase and as such no revenue is yet being generated from the Group's assets. A number of important milestones as set out in the original Prospectus for the Initial Public Offering ("IPO") have been achieved in the period under review, principally being the successful testing of the Bentley 9/3b-5 appraisal well, together with the extensive work programme of data analysis and studies to determine the optimum route for commercial development of the large resource that forms Bentley.

As a result of this work programme, the updated Competent Person's Report (CPR) from RPS Energy attributes Contingent Resources (Development Pending) – the highest category of Contingent Resources before the Reserves category under latest SPE terminology - to Bentley and a significant step up from the previous category of Contingent Resources prior to the 9/3b-5 well. In addition to this important category improvement in the resources definition, RPS Energy has assigned a significantly higher volume of recoverable resources to Bentley. Finally and most significantly for our shareholders, the probability of commercial success for the Bentley reservoir as reported by RPS Energy has increased from 50% to 70%.

In the period under review, total costs of £15.41 million (14 months to December 31, 2007: £4.48 million) have been capitalised as Exploration and Evaluation ("E&E") Assets in Intangible Assets relating to the Bentley field in Block 9/3b. This reflects the technical and commercial work that has been done by XER during the year in both drilling the 9/3b-5 appraisal well and the subsequent work programme of data analysis and studies. These costs have been capitalised in accordance with the Group's accounting policies and will be amortised against the revenue from production, if any, from the Bentley field.

The Group has not incurred any additional material research and development costs or deferred development costs over and above those costs capitalised as E&E assets. Administrative expenses charged to Income Statement during the year were £0.88 million (fourteen months to December 31, 2007: £0.98 million), which for the year under review did not include any costs relating to the private placement or the IPO in 2007 (fourteen months to December 31, 2007: £0.48 million). Expenditure incurred during the year of £0.79 million (fourteen months to December 31, 2007: £0.50 million) represent a proportion of remuneration costs of certain Executive Directors and the costs of operating as a public company, including investor relations, Non-Executive Director fees and stock exchange fees. In addition, the Group has expensed £0.09 million in respect of costs incurred in reviewing certain assets relating to a UK licensing round (fourteen months to December 31, 2007: £nil).

Share Options, Warrants and Rights

In the year to December 31, 2008, the Company issued aggregate share options to Non-Executive Directors and management of 550,000 under the Stock Option Plan. The total expense to the Group in respect of share based payment transactions under the Stock Option Plan is £0.13 million (2007: £0.84 million). Of this total, £0.05 million (2007: £0.32 million) has been charged to the Income Statement and £0.08 million (2007: £0.52 million) has been capitalised under intangible assets in accordance with the Company's accounting policy.

Income

Interest income received on funds invested up to December 31, 2008 amounted to £0.35 million (2007: £0.25 million).

Related Party Transactions

Related party transactions are detailed in Note 16 to the financial statements.

Disclosure Controls and Procedures

In conformance with the Canadian Securities Administrators Multilateral 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, 2008 is given below.

	Board	**Audit Committee**	**Remuneration and Nominating**
Richard E. Smith	5	N/A	N/A
Rupert E. Cole	5	5	N/A
Stephen A. Kew	5	N/A	N/A
Roger S. Ramshaw	5	5	5
Gregory J. Moroney	5	5	5
Scott R. Cochlan (1)	5	N/A	N/A
A. Murray Sinclair (2)	4	4	4

(1) Since date of appointment January 18, 2008
(2) To date of resignation November 4, 2008

Outstanding Share Capital

The following table outlines the ordinary share issues, warrants and share option exercises during the year.

	Ordinary Shares
As at January 1, 2008	**60,550,000**
Issue of shares through Broker warrant exercise	812,500
Issue of shares through warrant exercise	51,300
As at December 31, 2008	**61,413,800**

As at the date of signing these financial statements, the number of shares in issue was 61,413,800 as set out in Note 12.

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 heavy crude 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 reserve 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 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.

Financial Instruments and Other Derivatives

Details regarding the Group's policies in respect of financial instruments are disclosed in Notes 1 and 11 to the financial statements.

2009 Outlook

The current status of the global equity and credit markets and the consequent effect on the Company's share price compared with its underlying asset value, will make it difficult for the Company to raise additional finance and to make significant commitments to move forward with the next phase of the work programme on the Bentley field.

The Company is currently pursuing a number of financing initiatives that are designed to see it through to the other side of the current financial turbulence, probably towards the end of 2010, together with commercial initiatives involving farm-in partners and production sharing contractors to facilitate further work on the Bentley field. There is no certainty of success with these initiatives and, following the successful drilling and testing of the 9/3b-5 appraisal well in early 2008, the Group's long term prospects are dependent on the investment of significant capital sums for the commercialisation of the Bentley field.

The Company has sufficient existing resources to meet its financial obligations to March 2010 based on a minimum spend profile, but is reliant on securing additional funding in order to finance working capital beyond that time and to facilitate progress on the next reservoir intervention on the Bentley field. Although the Directors expect to be able to raise funds for these purposes, they have no binding agreements in place at the current time.

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 MI 52-110. The chairman of the Remuneration and Nominating Committee is Gregory J. Moroney.

Basic salary and benefits

The remuneration of the Executive Directors during the twelve-month financial period (2007: fourteen-month financial period) was as follows:

	Basic Salary £	Other compensation (a) £	**2008 Total £**	2007 Total £
Richard E. Smith	175,000	37,900	**212,900**	230,117
Rupert E. Cole	175,000	37,900	**212,900**	230,117
Stephen A. Kew	175,000	37,900	**212,900**	190,271

(a) 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 Groups' 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 and A. Murray Sinclair in their capacity as Non-Executive Directors of the Group fees of £32,250 (2007: £13,500), £7,500 (2007: £6,000), £7,500 (2007: £nil) and £4,500 (2007: £nil) respectively. Charges in respect of share based payments for the Non-Executive Directors in the year to December 31, 2008 were £46,803 (2007: £86,441).

Beneficial Interests

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

	Shares	Options	Warrants(1)
Richard E. Smith	6,300,000	1,000,000	-
Rupert E. Cole	6,300,000	1,000,000	-
Stephen A. Kew	6,300,000	1,000,000	-
Roger S. Ramshaw	-	200,000	-
Gregory J. Moroney	-	100,000	67,575
A. Murray Sinclair (2)	-	-	-
Scott R. Cochlan (3)	25,000	100,000	-

(1) See Note 12 for information about these warrants.
(2) In accordance with the conditions of the Group Stock Option Plan, a total of 100,000 share options granted to A. Murray Sinclair at the date of the Initial Public Offering expired on February 4, 2009, being 90 days from the date of resignation as a Non-Executive Director of November 4, 2008.
(3) 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.

All 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 above) with an exercise price of CAD$1.60 (£0.805) and a term of five years. Further details of the stock options in issue are given in Note 12 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 26, 2009

Report of the Independent Auditors

To the Shareholders of Xcite Energy Limited

We have audited the consolidated financial statements of Xcite Energy Limited and its subsidiary (collectively referred to as the "Group") for the year ended December 31, 2008, which comprise the Consolidated Income Statement, the Consolidated Statement of Recognised Income and Expense, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, and related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The Group's directors are responsible for the preparation of the financial statements in accordance with International Financial Reporting Standard (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. 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; 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.

All of the current directors are responsible for having taken all the steps that they ought to have taken to make themselves aware of any information needed by the Group's auditors for the purposes of their audit and to establish that the auditors are aware of that information.

Our responsibility is to audit the financial statements in accordance with International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view. We read the Management's Discussion and Analysis, the Chairman's and Chief Executive's Review and the Report of the Remuneration and Nominating Committee and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. We also report to you if we have not received all the information and explanations we require for our audit.

This report is made solely to the Group's shareholders as a body. Our audit work has been undertaken so that we might state to the Group's shareholders 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 shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the Group financial statements give a true and fair view, in accordance with International Financial Reporting Standards as adopted by the European Union, of the state of the Group's affairs as at December 31, 2008 and of the results of its operations and its cash flows for the year then ended.

BDO Stoy Hayward LLP
Chartered Accountants
Epsom, Surrey, England.
March 26, 2009

Xcite Energy Limited
For the year ended December 31, 2008

Consolidated Income Statement (in Pounds Sterling)

	Note	**12 months ended December 31 2008 £**	14 months ended December 31 2007 £
Administrative expenses		**(881,461)**	(981,846)
Operating loss	3	**(881,461)**	(981,846)
Finance income – bank interest		**344,910**	251,557
Loss before taxation		**(536,551)**	(730,289)
Tax expense	5	**(17,470)**	-
Loss for the period attributable to Equity holders of the Company		**(554,021)**	(730,289)
Loss per share attributable to Equity holders of the Parent Company			
- basic and diluted	6	**(0.01p)**	(0.02p)

All results relate to continuing operations.

Consolidated Statement of Recognised Income and Expense (in Pounds Sterling)

	12 months ended December 31 2008 £	12 months ended December 31 2007 £
Retained loss for the financial period	**(554,021)**	(730,289)
Total recognised income and expense for the period	**(554,021)**	(730,289)
Attributable to:		
Equity holders of the Company	**(554,021)**	(730,289)

The notes on pages 20 to 39 form part of these financial statements.

Consolidated Balance Sheet (in Pounds Sterling)

	Note	December 31 2008 £	December 31 2007 £
Assets			
Non-current assets			
Intangible assets	7	**21,996,871**	6,582,176
Property, plant and equipment	8	**21,317**	-
Total non-current assets		**22,018,188**	6,582,176
Current assets			
Trade and other receivables	9	**14,098**	82,789
Cash and cash equivalents		**1,828,183**	21,067,134
Total current assets		**1,842,281**	21,149,923
Total assets		**23,860,469**	27,732,099
Liabilities			
Current liabilities			
Trade and other payables	10	**1,110,611**	5,042,672
Total current liabilities		**1,110,611**	5,042,672
Net assets		**22,749,858**	22,689,427
Equity			
Share capital	12	**22,252,625**	21,774,150
Retained earnings	13	**(1,182,669)**	(730,422)
Merger reserve	13	**218**	218
Other reserves	13	**1,679,684**	1,645,481
Total equity		**22,749,858**	22,689,427

The notes on pages 20 to 39 form part of these financial statements. These financial statements were approved by the Board of Directors and authorised for issue on March 26, 2009 and were signed on its behalf by:

Richard Smith
Chief Executive Officer

Rupert Cole
Chief Financial Officer

Xcite Energy Limited
For the year ended December 31, 2008

Consolidated Cash Flow Statement (in Pounds Sterling)

	12 months ended December 31 2008	14 months ended December 31 2007
	£	£
Net cash flow from operating activities		
Loss for the period before tax	**(536,551)**	(730,289)
Adjustment for interest income	**(344,910)**	(251,557)
Adjustment for share based payments	**51,757**	322,171
Adjustment for depreciation	**6,173**	-
Adjustment for share issue costs	**-**	484,534
Movement in working capital		
- Trade and other receivables	**68,691**	(79,657)
- Trade and other payables	**(3,932,061)**	2,794,137
Foreign corporation tax paid	**(17,470)**	-
Net cash flow from operations	**(4,704,371)**	2,539,339
Cash flow from investing activities		
Additions to exploration and evaluation assets	**(15,330,475)**	(3,960,419)
Purchase of property, plant and equipment	**(27,490)**	-
Interest income	**344,910**	251,557
Net cash flow from investing activities	**(15,013,055)**	(3,708,862)
Cash flow from financing activities		
Net proceeds from issue of new shares	**478,475**	22,094,279
Cash flow from financing activities	**478,475**	22,094,279
Net (decrease)/increase in cash and cash equivalents	**(19,238,951)**	20,924,756
Cash and cash equivalents as at the beginning of the period	**21,067,134**	142,378
Cash and cash equivalents as at the end of the period	**1,828,183**	21,067,134
Cash and cash equivalents comprise:		
Cash available on demand	**1,828,183**	21,067,134

The notes on pages 20 to 39 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 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 IAS Regulation.

The consolidated financial statements have been prepared on a going concern basis, taking into account that the Company has sufficient existing resources to meet its financial obligations to March 2010 based on a minimum spend profile, but is reliant on securing additional funding in order to finance working capital beyond that time and to facilitate progress on the next reservoir intervention on the Bentley field. Although the Directors expect to be able to raise funds for these purposes, they have no binding agreements in place at the current time.

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 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 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 similarly 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 profit 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 12. 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 equipment 3-5 years

New standards and interpretations not yet applied

The following new standards and interpretations, which have been issued by the IASB and the IFRIC, are effective for future periods and have not been adopted early in these financial statements. A description of these standards and interpretations, together with (where applicable) an indication of the effect of adopting them, is set out below. None are expected to have a material effect on the reported results or financial position of the Group.

The IASB issued a revised IAS 1 'Presentation of Financial Statements' in September 2007 effective for accounting periods beginning on or after 1 January 2009. This was endorsed by the European Financial Reporting Advisory Group (EFRAG) in December 2008.

The IASB published revisions to IAS 32 'Financial Instruments: Presentation' and consequential revisions to other standards in February 2008 to improve the accounting for and disclosure of puttable financial instruments. The revisions are effective for accounting periods beginning on or after 1 January 2009 but together they may be adopted earlier. This was endorsed in January 2009.

The IASB published amendments to IFRS 1 and IAS 27 "Cost of an Investment in a Subsidiary, Jointly-Controlled Entity or Associate" in May 2008 and it was endorsed in January 2009. A first-time adopter now may use as deemed cost of an investment in a subsidiary, jointly-controller entity or associate either the fair value at the entity's transition to IFRS or the previous GAAP carrying amount at that date. Investors no longer need to determine whether dividends received have been paid from pre or post-acquisition profits, all such dividends now being treated as income in the income statement. The amendments also clarify how to determine the cost of an investment in accordance with IAS 27 when a parent reorganises the operating structure of its group by establishing a new entity as its parent and this new parent obtains control of the original parent by issuing equity instruments in exchange for existing equity instruments of the original parent. Entities are required to apply these amendments for annual periods beginning on or after 1 January 2009, and earlier adoption is permitted.

The IASB issued in May 2008 as part of its Annual Improvements Project an Exposure Draft discussing proposed improvements to existing IFRSs. The Annual Improvements Project has the intention of dealing with a relatively high number of small amendments to existing standards. Most amendments will be effective 1 January 2009.

The IASB published a revised IFRS 3 ‘Business Combinations’ and related revisions to IAS 27 ‘Consolidated and Separate Financial Statements’ following the completion in January 2008 of its project on the acquisition and disposal of subsidiaries. The standards improve convergence with US GAAP and provide new guidance on accounting for changes in interests in subsidiaries. The cost of an acquisition will comprise only consideration paid to vendors for equity; other costs will be expensed immediately. Groups will only account for goodwill on acquisition of a subsidiary; subsequent changes in interest will be recognised in equity and only on a loss of control will there be a profit or loss on disposal to be recognised in income. The changes are effective for accounting periods beginning on or after 1 July 2009, but both standards may be adopted together for accounting periods beginning on or after 1 July 2007.

The Exposure Draft “Proposed Amendments to IFRS 2 - Vesting Conditions and Cancellations” was issued in February 2006, with the final standard being issued in January 2008 and endorsed in December 2008. The amendment requires that vesting conditions be restricted to service conditions and non-market performance conditions. Cancellations by parties other than the entity will be accounted for in the same way as cancellations by the entity. The amendments will be applied retrospectively in annual periods beginning on or after 1 January 2009.

Amendment to IAS 23 ‘Borrowing Costs’ was issued in May 2007, endorsed in December 2008 and is effective for accounting periods beginning on or after 1 January 2009. The amendment requires borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset to be added to the cost of that asset.

IFRIC 12 ‘Service Concession Arrangements’ was issued in November 2006 and is effective for annual periods beginning on or after 1 January 2008. IFRIC 12 prohibits private sector operators from recognising as their own those infrastructure assets which are owned by the grantor.

IFRIC 13 ‘Customer Loyalty Programmes’ was issued in June 2007, endorsed in December 2008 and is effective for annual periods beginning on or after 1 July 2008. IFRIC 13 requires the fair value of revenue relating to customer loyalty rewards to be deferred until all related obligations to the customer have been fulfilled.

IFRIC 14 ‘IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction’ was issued in June 2007, endorsed in December 2008 and is effective for annual periods beginning on or after 1 January 2008. IFRIC 14 clarifies how any asset to be recognised should be determined, in particular where a minimum funding requirement exists.

IFRS 8 ‘Operating Segments’ was issued in November 2006 and is effective for annual periods beginning on or after 1 January 2009. It requires reportable operating segments to be based on the entity’s own internal reporting structure. It also extends the scope and disclosure requirements of IAS 14 Segmental Reporting, the standard which it is replacing. IFRS 8 will require the publication of segment reports, which will, as a minimum, disclose net result and total assets on a segment by segment basis based on management’s own internal accounting information.

Further new standards and interpretations issued by EFRAG during the year but not considered to be currently applicable to the Group include IFRIC 16 ‘Hedges of a Net Investment in A Foreign Operation’, IFRIC 17 ‘Distributions of Non-Cash Assets to Owners’ and IFRIC 18 ‘Transfers of Assets from Customers’.

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 1 'First Time Adoption of IFRS (revised)';
- IFRIC 12 'Service Concession Arrangements';
- IFRS 3 'Business Combinations (revised)'; and
- Amendments to IAS 27 'Consolidated and Separate Financial Statements'.

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 on ordinary activities is stated after charging the following:

	12 months ended December 31 2008	12 months ended December 31 2007
	£	£
Auditors' remuneration:		
- Group audit fee	**15,000**	25,000
- Audit of subsidiary pursuant to legislation	**20,000**	20,000
- Tax advisory	**17,200**	9,500
- Fees in respect of Initial Public Offering	**-**	65,000
- Non-statutory audit and advisory fees (1)	**-**	39,500

(1) Pursuant to the Initial Public Offering, the Group's auditors provided non-statutory audit and advisory services to XER for the period from incorporation to July 2007.

The Group incurred total charges in respect of equity-settled share based payments in the current year of £135,977 (2007: £840,818). Of this, £89,174 (2007: £691,529) was in respect of employees (see Note 4). In accordance with the Group's accounting policy, £84,220 (2007: £518,647) has been capitalised within E&E assets and the balance of £51,757 (2007: £322,171) 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 financial period was as follows:

	12 months ended December 31 2008	14 months ended December 31 2007
Technical and administration	**7**	4

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

	12 months ended December 31 2008	14 months ended December 31 2007
	£	£
Wages and salaries	**1,045,969**	704,367
Social security costs	**129,393**	87,731
Share based payments	**89,174**	691,529
	1,264,536	1,483,627

b) Executive Directors' emoluments

	12 months ended December 31 2008	14 months ended December 31 2007
	£	£
Wages and salaries	**638,700**	650,505
Social security costs	**80,237**	81,115
Share based payments charge	**-**	648,309
	718,937	1,379,929

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 and A.Murray Sinclair in their capacity as Non-Executive Directors of the Group fees of £36,750 (2007: £13,500), £11,250 (2007: £6,000), £9,000 (2007: £nil) and £4,500 (2007: £nil) respectively. Charges in respect of share based payments for the Non-Executive Directors in the year to December 31, 2008 were £46,803 (2007: £86,441).

5 Tax Expense

	12 months ended December 31 2008	14 months ended December 31 2007
	£	£
Current tax		
UK tax on income for the period	**7,987**	-
Adjustments in respect of prior years	**9,483**	-
Tax on loss on ordinary activities	**17,470**	-

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

	12 months ended December 31 2008	14 months ended December 31 2007
	£	£
Loss on ordinary activities before tax	**(536,551)**	(730,289)
Loss on ordinary activities multiplied by the standard rate of corporation tax in the British Virgin Islands of 0% (2007: 0%)	**-**	-
Effects of:		
UK Tax suffered on income	**7,987**	-
Prior period adjustments relating to UK Tax	**9,483**	-
Current tax charge for the period	**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 30% or 19% where the profits fall within the limits of the small companies rate (2007: 30% or 20%).

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 twelve month period ended December 31, 2008 is based on a twelve month period loss of £554,021 (fourteen months to December 31, 2007: loss of £730,289) and on shares of 61,336,321 (fourteen months to December 31, 2007: 32,380,357), being the weighted average number of ordinary shares in issue during the period.

Details of potentially dilutive financial instruments are given in Note 12 to these financial statements. No new shares have been issued since the year end.

7 Intangible Assets

	Licence Fees	
	2008	2007
Exploration and Evaluation Assets	**£**	£
Opening cost and carrying value at the beginning of the period	**126,567**	66,297
Additions	**126,720**	60,270
Closing cost and carrying value at December 31	**253,287**	126,567

	Appraisal and Exploration Costs	
	2008	2007
	£	£
Opening cost and carrying value at the beginning of the period	**6,455,609**	2,036,813
Additions	**15,287,975**	4,676,479
Contributions to costs received	**-**	(257,683)
Closing cost and carrying value at December 31	**21,743,584**	6,455,609

	Total	
	2008	2007
	£	£
Opening cost and carrying value at the beginning of the period	**6,582,176**	2,103,110
Additions	**15,414,695**	4,736,749
Contributions to costs received	**-**	(257,683)
Closing cost and carrying value at December 31	**21,996,871**	6,582,176

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
At November 1, 2006	£
Cost and net book amount	**-**
At December 31, 2007	
Cost and net book amount	**-**
Year ended December 31, 2008	
Opening net book amount at January 1	-
Additions	27,490
Depreciation charge	6,173
Closing net book amount at December 31	**21,317**
At December 31, 2008	
Cost or valuation	27,490
Accumulated depreciation	6,173
Net book amount	**21,317**

9 Trade and Other Receivables

	December 31 2008 £	December 31 2007 £
Indirect taxes receivable	**10,173**	79,114
Other receivables	**3,925**	3,675
	14,098	82,789

10 Trade and Other Payables

	December 31 2008 £	December 31 2007 £
Trade payables	**150,092**	2,857,762
Social security and other taxes payable	**47,318**	33,919
Accruals and other payables	**913,201**	2,150,991
	1,110,611	5,042,672

11 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

Receivables relate to an office rent deposit. As such, it is regarded as low risk. Credit risk also arises from cash and cash equivalents and deposits held by banks and financial institutions. For banks and financial institutions, only independently rated parties with a minimum rating of "AA" or better are accepted.

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. It operates according to the policies and guidelines established by the Board. Cash management is carried out centrally.

	Carrying Amount	
	December 31	December 31
	2008	2007
	£	£
Financial assets – loans and receivables measured at amortised cost		
- Cash	**1,828,183**	21,067,134
- Receivables (current)	**3,925**	3,925
	1,832,108	21,071,059
Financial liabilities – measured at amortised cost		
- Payables (current)	**1,063,293**	5,008,753

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	December 31
	2008	2007
	£	£
Sterling	**1,063,293**	2,773,686
CAD$	**-**	62,947
USD$	**-**	2,172,120
	1,063,293	5,008,753

	Floating rate assets	**Interest free assets**	**Total**
	December 31	**December 31**	**December 31**
	2008 £	**2008 £**	**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**

	Floating rate assets	Interest free assets	Total
	December 31	December 31	December 31
	2007 £	2007 £	2007 £
Sterling	16,460,016	3,675	16,463,691
USD$	4,607,118	-	4,607,118
	21,067,134	3,675	21,070,809

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, 2008 would decrease/increase by £47,652 (December 31, 2007; loss would decrease/increase by £25,650).

12 Share Capital

	Number of shares December 31 2008	Number of shares December 31 2007
Authorised		
- Ordinary shares of no par value each	**Unlimited**	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value each	**61,413,800**	60,550,000

	£ Value of shares December 31 2008	£ Value of shares December 31 2007
Authorised		
- Ordinary shares of no par value each	**Unlimited**	Unlimited
Issued and fully paid up		
- Ordinary shares of no par value each	**22,252,625**	21,774,150

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 January 31, 2008 Thomas Weisel Partners (UK) Limited exercised a total of 700,000 Private Placement Broker Warrants for a consideration of US$700,000.

On February 7, 2008 Wellington West Capital Markets Inc. exercised a total of 112,500 Initial Public Offering Broker Warrants for a consideration of CAD$180,000.

On February 15, 2008 and March 12, 2008 respectively the Company received consideration of US$75,000 and US$1,950 in respect of the exercise of 50,000 and 1,300 Shareholder Warrants.

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, 2008 there were 4,350,000 options outstanding (2007: 3,800,000).

On the date of the Initial Public Offering on November 16, 2007 the Company issued a total of 3,800,000 share options with an average exercise price of CAD$1.60.

On January 18, 2008 the Company issued a total of 100,000 share options with an average exercise price of CAD$2.09. On June 19, 2008 the Company issued a further 450,000 share options with an average exercise price of CAD$1.60. No share options were exercised during the year ended December 31, 2008 (period ended December 31, 2007: nil).

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 financial periods at the following dates:

Grant Date	January 18, 2008	June 19, 2008	November 16, 2007
Share bid price	CAD$2.05	CAD$1.30	CAD$1.45
Exercise price	CAD$2.09	CAD$1.60	CAD$1.60
Expected volatility	50.0%	50.0%	31.0%
Expected life	5 years	5 years	5 years
Expected dividends	0.0%	0.0%	0.0%
Risk-free interest rate	3.54%	3.44%	3.97%

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, 2008 was £0.13 million (2007: £0.84 million). Of this total, £0.05 million (2007: £0.32 million) has been charged to the Income Statement and £0.08 million (2007: £0.52 million) has been capitalised under intangible assets in accordance with the Group's accounting policy.

Share warrants

The Group had the following outstanding warrants over the ordinary share capital of the Company at December 31, 2008:

Security	Holder	Number of ordinary shares	Exercise price	Market price at grant date	Expiry date
Shareholder Warrants (1)	Shareholders of the company	9,948,700	US$1.50	US$1.00	May 7, 2009
PP Broker warrants (2)	Thomas Weisel Partners (UK) Limited	700,000	US$1.00	US$1.00	June 26, 2009
IPO Broker warrants (3)	Various	1,012,500	CAD$1.60	CAD$1.60	Nov 15, 2009
Warrants (4)	Ammonite	163,500	US$1.00	US$1.00	Nov 15, 2009

(1) On June 26, 2007, pursuant to the Private Placement, XEL issued 20,000,000 units consisting of ordinary shares and 20,000,000 half-warrants at US$1.00 per unit. Each whole warrant entitles the holder to purchase one ordinary share in XEL at an exercise price of US$1.50 per share at any time until May 7, 2009. On February 15, 2008 the Company received consideration of US$75,000 in respect of the exercise of 50,000 of such warrants and on March 12, 2008 the Company received consideration of US$1,950 in respect of the exercise of 1,300 of such warrants.

(2) Pursuant to the Private Placement ("PP"), the Company issued to Thomas Weisel Partners (UK) Limited (formerly Westwind Partners (UK) Limited) 1,400,000 broker warrants to purchase 1,400,000 ordinary shares at an exercise price of US$1.00 at any time until June 26, 2009. On January 31, 2008 Thomas Weisel Partners (UK) Limited exercised a total of 700,000 of these warrants for a consideration of US$700,000.

(3) Pursuant to the Initial Public Offering ("IPO"), XEL issued a total of 1,125,000 broker warrants to the following institutions: Thomas Weisel Partners (UK) Limited 843,750 (75%); Mirabaud Securities LLP (formerly Mirabaud Securities Limited) 112,500 (10%); Wellington West Capital Markets Inc. 112,500 (10%); and MGI Securities 56,250 (5%), with each warrant entitling the holder to purchase one ordinary share in XEL at an exercise price of CAD$1.60 at any time until November 15, 2009. On February 7, 2008, Wellington West Capital Markets Inc. exercised a total of 112,500 of these warrants for a consideration of CAD$180,000.

(4) XER entered into an agreement with Ammonite Capital Partners L.P. ("Ammonite") in January 2007 in connection with its proposed funding activities. The agreement contained provisions for XER to award Ammonite warrants over ordinary shares in XER under certain circumstances. XEL assumed responsibility for this agreement at the time that XEL acquired XER. The agreement provided for Ammonite to receive a total of 163,500 warrants, each over one ordinary share in XEL (the "Ammonite Warrants"), with each warrant entitling the holder to purchase one ordinary share in XEL at an exercise price of US$1.00 at any time until November 15, 2009.

The following input assumptions were used in the option pricing model for the respective warrants:

	Warrants[1]	PP Broker Warrants[2]	IPO Broker Warrants[3]	Warrants[4]
Share bid price	US$1.00	US$1.00	CAD$1.45	US$1.00
Exercise price	US$1.50	US$1.00	CAD$1.60	US$1.00
Expected volatility	36.0%	36.0%	36.0%	36.0%
Expected life	2 years	2 years	2 years	2 years
Expected dividends	0.0%	0.0%	0.0%	0.0%
Risk-free interest rate	4.77%	4.77%	3.97%	4.77%

Notes (1) to (4) above refer to instrument classifications given above.

13 Retained Earnings and Other Reserves

	Retained Earnings	**Merger Reserve**	**Other Reserves**	**Total**
	£	**£**	**£**	**£**
At November 1, 2006	(133)	218	-	85
Loss for the period to December 31, 2007	(730,289)	-	-	(730,289)
Fair value of share options and warrants	-	-	1,645,481	1,645,481
At December 31, 2007	(730,422)	218	1,645,481	915,277
Transfer upon exercise of share warrants	101,774	-	(101,774)	-
Fair value of share options issued in the year	-	-	135,977	135,977
Loss for the year to December 31, 2008	(554,021)	-	-	(554,021)
At December 31, 2008	**(1,182,669)**	**218**	**1,679,684**	**497,233**

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

- Retained Earnings: Cumulative profits recognised in the Group Income Statement 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.

14 Commitments and contingencies

At December 31, 2008 the Company had total commitments under non-cancellable operating leases expiring as follows:

	2008	2007
	£	£
Within one year	**593**	593

15 Subsequent events

Competent Person's Report

On February 20, 2009 the Company announced the results of the new Competent Person's Report ("CPR") as undertaken by RPS Energy, following the successful drilling and testing of the 9/3b-5 well on the Bentley field in early 2008. The outcome of the new CPR was a classification of the Bentley field as Contingent Resources - Development Pending, the highest category of Contingent Resources before the Reserves category under latest industry classification. This is a significant step up from the previous category of Resources prior to the 9/3b-5 well.

In addition to this important category improvement in the resources definition, RPS Energy has assigned a significantly higher volume of recoverable resources to Bentley in the Low and Base cases reported. The Low case now reported is 72 million barrels ("MMbbls") (previously 37 MMbbls), and the Base case is 122.5 MMbbls (previously 68 MMbbls). It should also be noted that there is significant potential upside in the recoverable volumes reported from a range of reservoir parameters, which will be investigated in the next reservoir intervention.

Finally and most significantly for shareholders, the probability of commercial success for the Bentley field as reported by RPS Energy has increased from 50% to 70%.

Using these increased volumes of recoverable oil and the detailed full field development plan assumptions, the gross NPV_{10} of the field in the Base case has increased from US$460 million ("MM") to US$780MM and, with the increased probability of commercial success, the 'risked' NPV_{10} has increased from US$230MM to US$546MM; an increase of over 200%.

16 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 Xcite Energy Resources Limited ("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 £12.36 million during the year to December 31, 2008 (period to December 31, 2007: £8.48 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 Executive Directors have received remuneration, details of which are given in Note 4 to these financial statements. The Executive Directors have also been granted certain share options over the ordinary share capital of the parent undertaking, details of which are given in these financial statements.

Xcite Energy Limited
For the year ended December 31, 2008

Officers and Principal Advisors

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

Non-Executive Directors
Roger S. Ramshaw
A. Murray Sinclair (resigned November 4, 2008)
Gregory J. Moroney
Scott R. Cochlan
Timothy S. Jones (appointed March 19, 2009)

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Stock exchanges
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Code: XEL.L

TSX Venture, Toronto Stock Exchange
Code: XEL.V