

Our rapid growth brings many opportunities but also new challenges. Effective risk management is a critical part of our strategy, business objectives and day to day activities.

Clear risk identification

The table opposite sets out the key risks facing Tullow, their potential impact and mitigation strategies developed. Risks are grouped into four main categories: strategic; financial; operational; and external. Effective risk management is critical to achieving our strategic objectives and protecting our people and reputation. Tullow manages and mitigates its risks by maintaining a balanced portfolio, through compliance with the terms of its licences and application of policies and procedures appropriate for an international oil and gas company of its size and scale and through the recruitment and retention of skilled personnel throughout its business.

Comprehensive risk management systems

Tullow has a systematic approach to risk identification and management and undertakes both 'top-down' (driven by the Board) and 'bottom-up' (originating from the business units and operations) processes facilitated by the Group's Internal Audit Function under the ultimate supervision of the Audit Committee. The Board, through the Audit Committee, completed a review of internal controls and risk management. No significant gaps or weaknesses were identified as part of the 2007 review.

Clear targets and responsibility

The Board's strategic risk identification process feeds into the annual strategy review as part of the overall annual planning cycle. Annual objectives and targets covering production, development and exploration are established for each business unit with the identification, management and reporting of risk as an integral part of the process. Tullow recognises that risk is inherent across its operations, and all activities with a potential corporate or business impact are subject to an appropriate review to ensure that risks can be mitigated and controlled.

Appropriate policies and procedures

Detailed procedures have been developed to support risk management across the activities of the Group and the application and consistency of these procedures is regularly reviewed by the Group's Internal Audit function. In addition the Group has also successfully applied for external certification of critical processes such as International Standards Organisation (ISO) 14001 certification for environmental management in the UK, Ireland, South Africa and Bangladesh and ISO 9001 quality certification for our UK gas receiving and processing terminal. The review process for each standard involves an assessment of the management of material risks and business and operational controls employed to mitigate such risks.

The Directors have ultimate responsibility for the effectiveness of the Group's risk management activities and internal control processes. Any system of internal control can provide only reasonable, and not absolute, assurance that material financial irregularities will be detected or that the risk of failure to achieve business objectives is eliminated. The Board's objective is to ensure Tullow has appropriate systems in place for the identification and management of risks.

Risk description and potential impact**Mitigation****Strategic risk**

Ineffective or poorly executed strategy fails to create shareholder value.

Ineffective mix of oil and gas interests	Spread of oil and gas interests across diverse geographical locations.
Insufficient portfolio balance	Annual formal review and validation of strategy by the Board.
Organic and acquisition-led growth	Consistent investment appraisal process and Board approval for acquisitions.
Inefficient capital allocation	Comprehensive annual budgeting process covering all expenditure approved by the Board. Effectively managing capital allocation.
Ineffective management processes	Policies and procedures appropriate for Tullow's size and scale.
Loss of key staff/succession planning	Remuneration policies to attract and retain staff and specific staff development and training policies implemented.

Financial risk

Asset performance and excessive leverage results in the Group being unable to meet its financial obligations.

Excessive or inappropriate debt	Access to competitive financing. Conservative approach to debt/equity financing. Maintain financial flexibility by portfolio management.
Inadequate or excessive hedging	Hedging strategy agreed by the Board utilises a mix of physical and derivative products appropriate to Tullow's size and production base.
Underperforming assets	Portfolio spread reduces dependence on a single asset. Regular asset financial performance reporting.
Industry cost inflation	Rigorous contracting procedures with competitive tendering.
Mis-priced corporate acquisitions	Consistent investment appraisal and Board approval for acquisitions.
Uninsured events	Comprehensive insurance programme.

Operational risk

Operational event impacts staff, contractors, communities or the environment leading to loss of reputation and/or revenue.

EHS incident	EHS standards set and monitored regularly across the Group.
Security incident	Integrated Management System covers day to day operational risks. Crisis management system implemented.
Key development failure	Technical, financial and Board approval for all projects and progress reports.
Failure to secure equipment, services and resources	Rigorous contract and procurement procedures. Comprehensive long-term planning to resource key projects.
Corruption or reputation risk	Consistent ethical standards established and documented.
Corporate and Social Responsibility	Social and community programmes. Social and ethical policies.
Sustained exploration failure	Exploration process validates programmes prior to Board approval.
Hostile acquisition	Robust defence strategies against hostile acquisitions. Effective investor engagement and ongoing communications programmes.

External Risks

The overall external political, industry or market environment may negatively impact on the Group's ability to independently manage and grow its business.

Political risk and fiscal change	Developing successful relationships with governments and communities.
Lack of control of key assets	Joint venturing with partners and governments.
Corporate governance failings	Regular review of compliance requirements.
Shareholder sentiment	Active engagement with the investor community.
Oil and gas price volatility	Hedging strategy agreed by the Board.