

**First Ship Lease Trust
and its Subsidiaries**

**(Constituted in the Republic of Singapore pursuant to a
Deed of Trust dated 19 March 2007)**

**Annual Report
Year ended 31 December 2010**

Report of the Trustee-Manager of First Ship Lease Trust

The directors of FSL Trust Management Pte. Ltd., the Trustee-Manager of First Ship Lease Trust (the "Trust") and its subsidiaries (together referred to as the "Group"), are pleased to submit this annual report to the unitholders of the Trust, together with the audited financial statements for the financial year ended 31 December 2010.

Directors

The directors of the Trustee-Manager in office at the date of this report are as follows:

Wong Meng Meng (Chairman)
 Phang Thim Fatt
 Michael John Montesano III
 Philip Clausius
 Cheong Chee Tham

Directors' interests

According to the register kept by the Trustee-Manager for the purposes of Section 76 of the Singapore Business Trusts Act (the "Act"), particulars of interests of directors who held office at the end of the financial year in units of the Trust are as follows:

| Name of directors | Holdings at beginning of the year | | Holdings at end of the year | |
|----------------------------|--------------------------------------|---------------|--------------------------------|---------------|
| | <u>Direct</u> | <u>Deemed</u> | <u>Direct</u> | <u>Deemed</u> |
| The Trust | | | | |
| <u>Units</u> | | | | |
| Philip Clausius | - | 715,000 | - | 715,000 |
| Cheong Chee Tham | 148,500 | 44,000 | 148,500 | 44,000 |
| Michael John Montesano III | 13,200 | - | 13,200 | - |

Except as disclosed above, no director who held office at the end of the financial year had interests in units, debentures, warrants or unit options of the Trust, or of related corporations, either at the beginning or at the end of the financial year.

Except as disclosed above, neither at the end of, nor at any time during the financial year was the Trustee-Manager a party to any arrangement whose objects are, or one of whose objects is, to enable the directors of the Trustee-Manager to acquire benefits by means of the acquisition of units, debentures or unit options of the Trust.

Except as disclosed in note 22 to the financial statements, since the end of the last financial year, no director has received or become entitled to receive a benefit by reason of a contract made by the Trust or a related corporation with the director, or with a firm of which he is a member or with a company in which he has a substantial financial interest.

There were no changes in any of the above mentioned interests in the Trust between the end of the financial year and 21 January 2011.

Unit options

During the financial year, there were:

- (i) no options granted by the Trustee-Manager to any person to take up unissued units in the Trust; and
- (ii) no units issued by virtue of any exercise of option to take up unissued units of the Trust.

As at the end of the financial year, there were no unissued units of the Trust under option.

Audit committee

The members of the Audit Committee during the financial year and as at the date of this report comprise three independent and non-executive directors:

Phang Thim Fatt (Chairman)
Wong Meng Meng
Michael John Montesano III

The Audit Committee carried out its functions in accordance with Regulation 13(6) of the Singapore Business Trusts Regulations and the SGX Listing Manual.

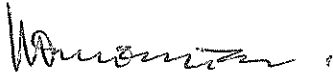
In performing its functions, the Audit Committee reviewed the overall scope of external audit and the assistance given by the Trustee-Manager's officers to the auditors. It met with the Trust's external auditors to discuss the scope and results of their audit. In addition, the Audit Committee reviewed the financial statements of the Group and the Trust before their submission to the Board of Directors of the Trustee-Manager.

The Audit Committee has recommended to the Board of Directors, the nomination of Messrs KPMG LLP for re-appointment as auditors of the Trust at the forthcoming Annual General Meeting of the unitholders.


Auditors

The auditors, KPMG LLP, have indicated their willingness to accept re-appointment.

For and on behalf of the Board of Directors of the Trustee-Manager



Wong Meng Meng
Chairman



Philip Clausius
Director

1 March 2011

Statement by Trustee-Manager

Statement and certification

In our opinion:

- (a) the financial statements set out on pages FS1 to FS37 are drawn up so as to give a true and fair view of the state of affairs of the Group and of the Trust as at 31 December 2010 and the results, changes in unitholders' funds and cash flows of the Group for the year ended on that date in accordance with the provisions of the Singapore Business Trusts Act and International Financial Reporting Standards; and
- (b) at the date of this statement, there are reasonable grounds to believe that the Trust will be able to pay its debts as and when they fall due.

With respect to the income statement of the Group for the year ended 31 December 2010:

- fees or charges paid or payable out of the trust property to the Trustee-Manager are in accordance with the Deed of Trust dated 19 March 2007;
- interested person transactions are not detrimental to the interests of all the unitholders as a whole based on the circumstances at the time of the transaction; and
- the Board is not aware of any violation of duties of the Trustee-Manager which would have a materially adverse effect on the business of the Trust or on the interests of all the unitholders as a whole.

The Board of Directors has, on the date of this statement, authorised the above statements and these financial statements for issue.

For and on behalf of the Board of Directors of the Trustee-Manager



Wong Meng Meng
Chairman



Philip Clausius
Director

1 March 2011

Statement by the Chief Executive Officer

In accordance with Section 86 of the Singapore Business Trusts Act, I certify that I am not aware of any violation of duties of the Trustee-Manager which would have a materially adverse effect on the business of the Trust or on the interests of all the unitholders of the Trust as a whole.

A handwritten signature in black ink, appearing to read 'Philip Clausius', written over a horizontal line.

Philip Clausius
Chief Executive Officer

1 March 2011



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Independent auditors' report

Unitholders of First Ship Lease Trust

Report on the financial statements

We have audited the financial statements of First Ship Lease Trust (the "Trust") (constituted in the Republic of Singapore pursuant to a Deed of Trust dated 19 March 2007) and its subsidiaries (the "Group"), which comprise the statements of financial position of the Group and the Trust as at 31 December 2010, the income statement, statement of comprehensive income, statement of changes in unitholders' funds and statement of cash flows of the Group for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages FS1 to FS37.

Trustee-Manager's responsibility for the financial statements

The Trustee-Manager is responsible for the preparation of financial statements that give a true and fair view in accordance with the provisions of the Singapore Business Trusts Act (the "Act") and International Financial Reporting Standards, and for devising and maintaining a system of internal accounting controls sufficient to provide a reasonable assurance that assets are safeguarded against loss from unauthorised use or disposition; and transactions are properly authorised and that they are recorded as necessary to permit the preparation of true and fair profit and loss accounts and balance sheets and to maintain accountability of assets.

Auditors' responsibility

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

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


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

Opinion

In our opinion, the consolidated financial statements of the Group and the statement of financial position of the Trust are properly drawn up in accordance with the provisions of the Act and International Financial Reporting Standards to give a true and fair view of the state of affairs of the Group and of the Trust as at 31 December 2010 and the results, changes in unitholders' funds and cash flows of the Group for the year ended on that date.

Report on other legal and regulatory requirements

In our opinion, the accounting and other records required by the Act to be kept by the Trustee-Manager and by those subsidiaries incorporated in Singapore of which we are the auditors, have been properly kept in accordance with the provisions of the Act.


KPMG LLP
Public Accountants and
Certified Public Accountants

Singapore
1 March 2011

Statements of financial position
As at 31 December 2010

| | | Group | | Trust | |
|--|------|----------------|----------------|----------------|----------------|
| | Note | 2010 | 2009 | 2010 | 2009 |
| | | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| Assets | | | | | |
| Vessels | 4 | 775,023 | 845,187 | - | - |
| Subsidiaries | 5 | - | - | 592,523 | 671,584 |
| Derivative assets | 6 | 476 | - | 476 | - |
| Non-current assets | | <u>775,499</u> | <u>845,187</u> | <u>592,999</u> | <u>671,584</u> |
| Derivative assets | 6 | 188 | - | 188 | - |
| Inventories | 7 | 738 | - | - | - |
| Deposits, prepayments and receivables | 8 | 3,758 | 1,282 | 90,743 | 96,255 |
| Cash and cash equivalents | 9 | 55,846 | 56,770 | 51,790 | 56,769 |
| Current assets | | <u>60,530</u> | <u>58,052</u> | <u>142,721</u> | <u>153,024</u> |
| Total assets | | <u>836,029</u> | <u>903,239</u> | <u>735,720</u> | <u>824,608</u> |
| Equity attributable to unitholders of the Trust | | | | | |
| Units in issue | 10 | 510,273 | 510,273 | 510,273 | 510,273 |
| Reserves | 11 | (167,825) | (129,536) | (262,466) | (205,846) |
| Total equity | | <u>342,448</u> | <u>380,737</u> | <u>247,807</u> | <u>304,427</u> |
| Liabilities | | | | | |
| Financial liabilities | 12 | 446,698 | 470,853 | 446,698 | 470,853 |
| Non-current liabilities | | <u>446,698</u> | <u>470,853</u> | <u>446,698</u> | <u>470,853</u> |
| Trade and other payables | 13 | 8,886 | 6,714 | 3,227 | 4,393 |
| Financial liabilities | 12 | 37,988 | 44,935 | 37,988 | 44,935 |
| Current tax payable | 9 | - | - | - | - |
| Current liabilities | | <u>46,883</u> | <u>51,649</u> | <u>41,215</u> | <u>49,328</u> |
| Total liabilities | | <u>493,581</u> | <u>522,502</u> | <u>487,913</u> | <u>520,181</u> |
| Total equity and liabilities | | <u>836,029</u> | <u>903,239</u> | <u>735,720</u> | <u>824,608</u> |

The accompanying notes form an integral part of these financial statements.

Consolidated income statement
Year ended 31 December 2010

| | Note | 2010 US\$'000 | 2009 US\$'000 |
|--|------|------------------|------------------|
| Revenue | 14 | 100,494 | 98,768 |
| Depreciation expense on vessels | | (59,058) | (61,295) |
| Impairment loss on vessels | 4 | (7,865) | - |
| Vessel operating expenses | | (5,474) | - |
| Management fees | | (3,563) | (3,959) |
| Trustee fees | | (175) | (183) |
| Other trust expenses | | (4,395) | (2,334) |
| Results from operating activities | | <u>19,964</u> | <u>30,997</u> |
| Finance income | 15 | 249 | 165 |
| Finance expenses | 15 | (25,903) | (22,753) |
| Net finance expenses | | <u>(25,654)</u> | <u>(22,588)</u> |
| (Loss)/Profit before income tax | 16 | (5,690) | 8,409 |
| Income tax (expense)/credit | 17 | (9) | 14 |
| (Loss)/Profit for the year | | <u>(5,699)</u> | <u>8,423</u> |
| Income available for distribution | 18 | <u>26,042</u> | <u>41,975</u> |
| Distribution per unit (US cents) | | <u>4.35</u> | <u>7.90</u> |
| Earnings per unit (US cents) | | | |
| Basic | 19 | <u>(0.95)</u> | 1.57 |
| Diluted | 19 | <u>(0.95)</u> | 1.57 |

The accompanying notes form an integral part of these financial statements.

Consolidated statement of comprehensive income
Year ended 31 December 2010

| | 2010 \$'000 | 2009 \$'000 |
|---|------------------------------|------------------------------|
| (Loss)/Profit for the year | (5,699) | 8,423 |
| Other comprehensive income | | |
| Translation differences relating to financial statements of foreign operations | (1,720) | 95 |
| Exchange differences on monetary items forming part of net investment in foreign operations | (2,659) | (161) |
| Effective portion of changes in fair value of cash flow hedges | (13,449) | (2,189) |
| Net change in fair value of cash flow hedges reclassified to income statement | 14,572 | 12,795 |
| Tax on other comprehensive income | - | - |
| Other comprehensive income for the year, net of income tax | (3,256) | 10,540 |
| Total comprehensive (loss)/income for the year | (8,955) | 18,963 |

The accompanying notes form an integral part of these financial statements.

Consolidated statement of changes in unitholders' funds
Year ended 31 December 2010

| | Note | Units in issue US\$'000 | Hedging reserve US\$'000 | Foreign currency translation reserve US\$'000 | Equity compensation reserve US\$'000 | Accumulated losses US\$'000 | Total equity US\$'000 |
|---|------|-------------------------------|--------------------------------|---|---|-----------------------------------|-----------------------------|
| Group | | | | | | | |
| At 1 January 2009 | | 477,642 | (37,726) | 3,502 | 590 | (65,838) | 378,170 |
| Total comprehensive income for the year | | - | 10,606 | (66) | - | 8,423 | 18,963 |
| Contribution by and distributions to unitholders: | | | | | | | |
| Units issued as payment for incentive fees | | 590 | - | - | (590) | - | - |
| Units issued pursuant to Distribution Reinvestment Scheme | | 3,811 | - | - | - | - | 3,811 |
| Units issued pursuant to equity placement | | 28,230 | - | - | - | - | 28,230 |
| Distribution to unitholders | 18 | - | - | - | - | (48,437) | (48,437) |
| At 31 December 2009 | | 510,273 | (27,120) | 3,436 | - | (105,852) | 380,737 |
| At 1 January 2010 | | | | | | | |
| Total comprehensive income for the year | | 510,273 | (27,120) | 3,436 | - | (105,852) | 380,737 |
| Contribution by and distributions to unitholders: | | | | | | | |
| Distribution to unitholders | | - | 1,123 | (4,379) | - | (5,699) | (8,955) |
| At 31 December 2010 | 18 | 510,273 | (25,997) | (943) | - | (140,885) | 342,448 |

The accompanying notes form an integral part of these financial statements.

Consolidated statement of cash flows
Year ended 31 December 2010

| | Note | 2010 US\$'000 | 2009 US\$'000 |
|---|------|------------------|------------------|
| Cash flows from operating activities | | | |
| (Loss)/Profit before income tax | | (5,690) | 8,409 |
| Adjustments for: | | | |
| Depreciation expense on vessels | | 59,058 | 61,295 |
| Impairment loss on vessels | | 7,865 | - |
| Amortisation of debt transaction costs | | 1,377 | 1,072 |
| Amortisation of initial direct costs | | 534 | 631 |
| Interest income | | (249) | (165) |
| Interest expense | | 24,565 | 23,368 |
| Ineffective portion of changes in fair value of interest rate swaps | | - | 376 |
| Unrealised foreign exchange gain | | (174) | (1,617) |
| | | 87,286 | 93,369 |
| Changes in deposits, prepayments and receivables | | (2,492) | (2,121) |
| Changes in inventories | | (738) | - |
| Changes in trade and other payables | | 1,655 | 766 |
| Lease income received in advance | | 523 | - |
| Cash generated from operations | | 86,234 | 92,014 |
| Income taxes paid | | - | (23) |
| Net cash from operating activities | | 86,234 | 91,991 |
| Cash flows from investing activities | | | |
| Costs incurred for dry-docking | | (1,496) | - |
| Interest received | | 244 | 192 |
| Net cash (used in)/from investing activities | | (1,252) | 192 |
| Cash flows from financing activities | | | |
| Proceeds from issuance of units (net of transaction costs) | | - | 28,230 |
| Distribution to unitholders | | (29,334) | (44,626) |
| Interest paid | | (24,572) | (24,917) |
| Repayment of secured bank loans | | (32,000) | (20,816) |
| Net cash used in financing activities | | (85,906) | (62,129) |
| Net (decrease)/increase in cash and cash equivalents | | (924) | 30,054 |
| Cash and cash equivalents at 1 January | | 56,770 | 26,716 |
| Cash and cash equivalents at 31 December | 9 | 55,846 | 56,770 |

The accompanying notes form an integral part of these financial statements.

Notes to the financial statements

These notes form an integral part of the financial statements.

The financial statements were authorised for issue by the Trustee-Manager on 1 March 2011.

1 Domicile and activities

First Ship Lease Trust (the "Trust") is a Singapore-domiciled business trust constituted pursuant to a Deed of Trust dated 19 March 2007 (the "Trust Deed") with FSL Trust Management Pte. Ltd. (the "Trustee-Manager"). The Trustee-Manager's registered office is 9 Temasek Boulevard, #19-03, Suntec Tower Two, Singapore 038989. The Trust Deed is governed by the laws of the Republic of Singapore. The Trustee-Manager is under a duty to take into custody and hold the assets of the Trust in trust for the unitholders.

The Trust was formally admitted to the Official List of the Singapore Exchange Securities Trading Limited on 27 March 2007.

The Trust is a provider of leasing services on a bareboat charter basis to the international shipping industry. It has a modern, high quality and diverse portfolio of 23 vessels consisting of nine product tankers, seven containerships, three chemical tankers, two dry bulk carriers and two crude oil tankers as at 31 December 2010. 21 vessels are employed on long-term bareboat leases and have a dollar-weighted average remaining lease period of approximately seven years (excluding extension periods and early buy-out options). The remaining two product tankers are currently trading in the product tanker spot market. The combined portfolio of vessels has a dollar-weighted average age of approximately five and a half years.

The consolidated financial statements relate to the Trust and its subsidiaries (together referred to as the "Group" and individually as "Group entities").

The Trust Deed provides the following fees payable to the Trustee-Manager:

Management fees

The Trustee-Manager is entitled to receive a management fee of 4.0% of the cash lease income in the relevant calendar year.

Any change in the structure of the management fee must be approved by an extraordinary resolution of a meeting of unitholders duly convened and held in accordance with the provisions of the Trust Deed.

The management fee payable to the Trustee-Manager is payable in the form of cash and/or units (as the Trustee-Manager may elect, such election to be irrevocable). Where the management fee is paid in cash, the amount is paid monthly, in arrears. Where the management fee is paid in the form of units, the amount is paid quarterly, in arrears.

Incentive fees

The Trustee-Manager is entitled to receive an incentive fee, payable quarterly and calculated as at 31 March, 30 June, 30 September and 31 December each year for the three-month period ending on each of the said dates. The incentive fee is determined on the basis of comparing the net distribution amount per unit against a benchmark quarterly distribution per unit in accordance with the formula stipulated in the Trust Deed.

The incentive fee payable to the Trustee-Manager is payable in the form of cash or, at the option of Trustee-Manager, by way of the issue of new units as soon as practicable after the end of the relevant quarter.

Any change in the structure of the incentive fees must be approved by an extraordinary resolution of a meeting of unitholders duly convened and held in accordance with the provisions of the Trust Deed.

Trustee fees

The Trustee-Manager is entitled to receive a trustee fee of 0.02% per annum of the value of the Trust Property (being all the assets of the Trust, as stipulated in the Trust Deed). The trustee fee is payable out of the Trust Property of the Trust in cash on a quarterly basis. Each quarterly payment shall be determined based on the value of the Trust Property as at the last day of the immediately preceding quarter and as reflected in the quarterly financial information of the Group for that quarter. The Trustee-Manager is also entitled to reimbursement of expenses incurred in the performance of its duties under the Trust Deed.

Any change in the structure of the trustee fee must be approved by an extraordinary resolution of a meeting of unitholders duly convened and held in accordance with the provisions of the Trust Deed.

Other fees

The Trustee-Manager is also entitled to the following:

- An acquisition fee amounting to 1.0% (or such lower percentage as may be determined by the Trustee-Manager in its absolute discretion) of the acquisition price of vessels acquired directly or indirectly by the Trust, pro-rated if applicable, to the proportion of the Trust's interest. The acquisition fee is payable in the form of cash and/or units (as the Trustee-Manager may elect, such election to be irrevocable and made before the payment of the acquisition fee). No acquisition fee is payable on the acquisition of the initial portfolio of vessels.
- A disposal fee amounting to 0.5% (or such lower percentage as may be determined by the Trustee-Manager in its absolute discretion) of the sale price of vessels disposed, pro-rated if applicable, to the proportion of the Trust's interest. The disposal fee is payable in cash.

Any increase in the acquisition fee or disposal fee above the permitted limit or any change in the structure of such fees shall be approved by an extraordinary resolution of a meeting of unitholders duly convened and held in accordance with the provisions of the Trust Deed.

2 Basis of preparation

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for financial derivatives and certain financial assets and financial liabilities which are stated at fair value and/or amortised cost as set out in the accounting policies under Note 3 of the financial statements.

(c) Functional and presentation currency

The financial statements are presented in United States ("US") dollars which is the Trust's functional currency. All financial information presented in US dollars has been rounded to the nearest thousand, unless otherwise stated.

(d) Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires the Trustee-Manager to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is included in the following notes:

- Note 3(f) – classification of leases
- Note 4 – impairment assessment and recoverable amounts of vessels; and depreciation, useful lives and residual values of vessels
- Note 20 – valuation of financial instruments

3 Significant accounting policies

The accounting policies used by the Group have been applied consistently to all periods presented in these financial statements, and have been applied consistently by Group entities.

(a) Consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed where necessary to align them with the policies adopted by the Group.

(ii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income or expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated only to the extent that there is no evidence of impairment.

(iii) Accounting for subsidiaries by the Trust

Investment in subsidiaries are stated in the Trust's statement of financial position at cost less accumulated impairment losses.

(b) Foreign currencies

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of the Group entities at the exchange rate at the date of the transaction. The functional currencies of the Group entities are the US dollar and the Euro. Monetary assets and liabilities denominated in foreign currencies at the end of the reporting period are retranslated to the functional currency at the exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined.

Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on the retranslation of monetary items that in substance form part of the Group's net investment in a foreign operation (see below).

(ii) Foreign operations

The assets and liabilities of foreign operations are translated to US dollars at exchange rates at the end of the reporting date. The income and expenses of foreign operations are translated to US dollars at exchange rates prevailing at the dates of the transactions.

Foreign currency differences are recognised in other comprehensive income, and presented within equity in the foreign currency translation reserve. When a foreign operation is disposed of, in part or in full, the relevant amount in the foreign exchange translation reserve is transferred to the income statement.

(iii) Net investment in a foreign operation

Exchange differences arising from monetary items that in substance form part of the Trust's net investment in a foreign operation are recognised in other comprehensive income, and are presented within equity in the foreign currency translation reserve in the consolidated financial statements. When the foreign operation is disposed of, the cumulative amount in the foreign currency translation reserve is transferred to the income statement as an adjustment to the profit or loss arising on disposal.

(c) Vessels

Vessels under operating lease are stated at cost less accumulated depreciation and impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the vessel as well as initial direct costs incurred in negotiating and arranging the operating lease of the vessel.

The cost of replacing part of an item of vessel is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably.

Depreciation on vessels leased on a bareboat charter basis under operating lease agreements is recognised in the income statement on a straight-line basis down to the estimated residual value at the end of the base lease term, which ranges from nine to twelve years. The estimated residual value is based on regression analysis of the median historical values for standard vessels obtained from third party sources, and for non-standard vessels obtained from specialised brokers.

In June 2010, due to the pre-mature termination of the bareboat charter operating lease arrangement of two vessels, these vessels' useful lives were revised from the original base lease term of seven years to economic useful life of 25 years. The revised useful life of 25 years is in line with the shipping industry practice for vessels deployed in the voyage spot and/or time charter basis. Arising from this change, the depreciation is recognised in the income statement on a straight-line basis down to the estimated residual value which is based on the average scrap steel price per light deadweight tonne at the end of 25 years. The effects of the revision of useful lives and residual value of these vessels constitute a change in estimates and have been applied prospectively from 1 June 2010. The financial effects are disclosed in Note 4 of the financial statements.

Depreciation methods, useful lives and residual values are reviewed, and adjusted as appropriate, at each reporting date.

Dry-docking costs are capitalised and depreciated on a straight-line basis over the period to the next scheduled dry-docking, which is generally five years.

(d) Inventories

Inventories comprise bunkers and consumable stores. Inventories are stated at the lower of cost and net realisable value. Cost is derived on a weighted average basis. Net realisable value is the estimated selling price in the ordinary course of business less applicable variable selling expenses. When inventories are consumed, the carrying amount of these inventories is recognised as an expense in the year in which the consumption occurs.

(e) Financial instruments

(i) Non-derivative financial instruments

Non-derivative financial instruments comprise trade and other receivables, deposits, cash and cash equivalents, financial liabilities, and trade and other payables.

Non-derivative financial instruments not recognised at fair value through profit or loss, are recognised initially at fair value plus, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured at amortised cost using the effective interest method, less any allowance for impairment losses.

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or transfers substantially all the risks and rewards of the asset. Regular purchases and sales of financial assets are accounted for at trade date, i.e. the date that the Group commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

Cash and cash equivalents comprise cash balances and bank deposits.

(ii) Derivative financial instruments and hedging activities

The Group holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures. Embedded derivatives are separate from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss.

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in the income statement when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for as described below.

Cash flow hedges

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in other comprehensive income and transferred to hedging reserve in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in the income statement.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases, the amount recognised in equity is transferred to the income statement in the same period that the hedged item affects profit or loss.

(iii) *Impairment of financial assets*

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

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

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

All impairment losses are recognised in the income statement.

An impairment loss in respect of financial assets measured at amortised cost is reversed if the subsequent increase in fair value can be related objectively to an event occurring after the impairment loss was recognised. The reversal is recognised in the income statement.

(iv) *Units in issue*

Units issued are classified as equity.

Unit issue costs represent expenses incurred in connection with the issue of units. All such expenses are deducted directly from unitholders' funds, net of any tax effects.

(f) **Leases**

When entities within the Group are lessors of an operating lease

The Group owns vessels and leases them to lessees under fixed and floating rate bareboat charter arrangements. These charters are classified as operating leases. In determining lease classification at inception, the Group evaluated the terms and conditions of the charter arrangement. As the present values of minimum lease payments do not amount to substantially the fair values of the vessels, and the purchase options are not expected to be sufficiently lower than the fair values at the date the options become exercisable, the Group judged that substantially all the risks and rewards of the vessels remain with the Group.

Lease income is recognised in the income statement on a straight-line basis over the lease term. Initial direct costs incurred by the Group in negotiating and arranging an operating lease added to the carrying amount of the leased asset are recognised as an expense in the income statement over the lease term on the same basis as the lease income.

(g) **Impairment – non-financial assets**

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the assets' recoverable amounts are estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the assets in the unit (group of units) on a pro rata basis.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit.

An impairment loss in respect of non-financial assets recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(h) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.

(i) Revenue recognition

Lease income receivable under operating leases is recognised in the income statement on a straight-line basis over the period of the respective lease terms.

For vessels deployed in the product tanker spot market, freight income is recognised based on percentage of completion method calculated on a discharge-to-discharge basis over the voyage period.

(j) Finance income and finance expense

Finance income comprises interest income on funds invested, net foreign currency gains and gains on hedging instruments that are recognised in the income statement. Interest income is recognised as it accrues, using the effective interest method.

Finance expense comprises interest expense on borrowings, net foreign currency losses, impairment losses recognised on financial assets, and losses on hedging instruments that are recognised in the income statement. All borrowing costs are recognised in the income statement using the effective interest method, except to the extent that they are capitalised as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to be prepared for its intended use or sale.

(k) Income tax expense

Income tax expense comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in other comprehensive income or equity.

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

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

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

The lease income derived by the Group's entities from the respective bareboat charter agreements qualifies for tax exemption under the Maritime Finance Incentive ("MFI") scheme, with effect from 19 March 2007. This tax exemption on the qualifying income will be granted for the remaining useful life of any vessel that is acquired by the Trust during the initial period of 10 years from the effective date. The distributions made out of the tax exempt income less allowable expenses will also be exempt from Singapore income tax in the hands of the unitholders.

The Group is subject to tax on its non-tax exempt income such as interest income at the prevailing corporate tax rate, after adjusting for allowable expenses.

(l) New standards and interpretations not adopted

The Group has not yet applied the following accounting standards (including the consequential amendments) and interpretations that have been issued as of the date of the statements of financial position but are not yet effective:

- *IFRS 9 Financial Instruments*

IFRS 9 will become effective for the Group's financial statements for the year ending 31 December 2013. IFRS 9 deals with classification and measurement of financial assets and financial liabilities, and the derecognition of financial assets and financial liabilities. The new standard uses a single approach to determine whether a financial asset is measured at amortised cost or fair value, replacing the many different rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments (its business model) and the contractual cash flow characteristics of the financial assets. Except as described below, the requirements with respect to the classification and measurement of financial liabilities and the derecognition of financial assets and financial liabilities have been carried forward without amendment from IAS 39. There are two substantive changes from the requirements in IAS 39 for classification and measurement of liabilities. These relate to the fair value option and to certain derivatives linked to unquoted equity instruments. The standard generally requires retrospective application in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, there are several exceptions to this principle and the transitional requirements are extensive. The Group is in the process of assessing the impact of adopting this standard.

- *IAS 24 Related Party Disclosures*

The revised IAS 24 clarifies the definition of a related party to simplify the identification of such relationships and to eliminate inconsistencies in its application. The revised IAS 24 expands the definition of a related party and would treat two entities as related to each other whenever a person (or a close member of that person's family) or a third party has control or joint control over the entity, or has significant influence over the entity. The application of this revised standard is not expected to have a significant impact on the consolidated financial statements.

- *Improvements to IFRSs 2010*

Improvements to IFRSs 2010 contain amendments to numerous accounting standards that result in accounting changes for presentation, recognition or measurement and disclosure purposes. The Group is in the process of assessing the impact of these amendments.

The initial application of these standards (and its consequential amendments) and interpretations is not expected to have any material impact on the Group's financial statements. The Group has not considered the impact of accounting standards issued after the date of the statements of financial position.

4

Vessels

| Group | Vessels US\$'000 | Initial direct costs US\$'000 | Total US\$'000 |
|--|---------------------|-------------------------------------|-------------------|
| Cost | | | |
| At 1 January 2009 | 983,377 | 6,163 | 989,540 |
| Cost adjustment | - | (39) | (39) |
| Translation differences on consolidation | 2,274 | - | 2,274 |
| At 31 December 2009 | 985,651 | 6,124 | 991,775 |
| Additions | 1,496 | - | 1,496 |
| Translation differences on consolidation | (6,015) | - | (6,015) |
| At 31 December 2010 | 981,132 | 6,124 | 987,256 |
| Accumulated depreciation/amortisation | | | |
| At 1 January 2009 | 83,391 | 545 | 83,936 |
| Depreciation/amortisation charge for the year | 61,295 | 631 | 61,926 |
| Translation differences on consolidation | 726 | - | 726 |
| At 31 December 2009 | 145,412 | 1,176 | 146,588 |
| Depreciation/amortisation charge for the year | 59,058 | 534 | 59,592 |
| Impairment loss | 7,639 | 226 | 7,865 |
| Translation differences on consolidation | (1,812) | - | (1,812) |
| At 31 December 2010 | 210,297 | 1,936 | 212,233 |
| Carrying amount | | | |
| At 1 January 2009 | 899,986 | 5,618 | 905,604 |
| At 31 December 2009 | 840,239 | 4,948 | 845,187 |
| At 31 December 2010 | 770,835 | 4,188 | 775,023 |

All of the Group's vessels, with a net carrying value of US\$770,835,000 (2009: US\$840,239,000), are mortgaged to financial institutions (see note 12).

Depreciation, useful lives and residual values of vessels

Vessels under operating lease

Vessels under operating lease are depreciated on a straight-line basis at rates which are calculated to write-down their cost to their estimated residual values at the end of the base lease term, excluding any early buy-out options or extended lease periods. At the reporting date, the Group considered the base lease term to be the period which the vessels are expected to be available for use by the lessees. Therefore, should there be any notification received from the lessees to exercise the early buy-out option or to extend the lease period beyond the base lease term, the depreciation expense of the Group's vessels in the future periods may therefore be revised. Except as disclosed in the following paragraphs, there were no changes in the useful lives of vessels noted for the current year.

The residual value is reviewed at each reporting date, with any change in estimate accounted for as a change in estimate prospectively. The residual value of each vessel under operating lease is estimated based on regression analysis of the median historical values for standard vessels obtained from third party sources, and for non-standard vessels obtained from specialised brokers. Factors such as asset price, quality and fungibility are also taken into consideration to determine the acceptable level of residual value. Any significant changes in the residual value of the Group's vessels in future periods can affect the depreciation expense. Based on the Group's re-assessment of the residual value of the Group's vessels at the financial year-end, no revision to the residual value previously estimated is considered necessary since any revised residual value would not have a material effect on the current year's depreciation expense and the carrying value of vessels as of 31 December 2010.

Vessels deployed in product tanker spot market

Vessels deployed in product tanker spot market are depreciated on a straight-line basis at rates which are calculated to write-down their cost to their estimated residual values at the end of the economic useful life of 25 years.

The residual value is reviewed at each reporting date, with any change in estimate accounted for as a change in estimate prospectively. The residual value of each vessel deployed in product tanker spot market is estimated based on the average scrap steel price per light deadweight tonne in recent years.

Change in estimates

Following the pre-mature termination of the long-term bareboat charter agreements, 'FSL Hamburg' and 'FSL Singapore' (formerly 'Nika I' and 'Verona I', respectively) are currently employed in the product tanker spot market with a view to place these vessels under time charter arrangement. With the change in charter arrangement, the expected useful life of the two vessels has been revised from 7 to 25 years and the basis of estimate for residual value has also changed. The change in the expected useful life and residual value of these two vessels constitute a change in estimates and the effects of the change have been applied prospectively.

The effects of these changes on depreciation expense (after accounting for impairment losses) in the current year and future years are as follows:

| | 2010 | 2011 to 2012 | 2013 |
|---|----------|--------------|----------|
| | US\$'000 | US\$'000 | US\$'000 |
| Decrease in annual depreciation expense | (2,956) | (5,068) | (3,761) |

Impairment assessment of vessels

Impairment loss is recognised when events and circumstances indicate that the vessel may be impaired and the carrying amounts of the vessels exceed the recoverable amounts. The recoverable amount for each vessel is determined based on the higher of fair value less costs to sell and value-in-use calculation.

Vessels under operating lease

The fair value is determined based on valuation report from independent shipbrokers. The valuation of vessels was prepared assuming a sale between a willing seller and a willing buyer and on a charter-free basis.

The value-in-use calculation uses cash flow projections based on the contractual cash flows over the period of the base lease term and projected residual value, discounted at rates which reflect the specific risks relating to each vessel.

The Group does not consider the vessels under operating leases to be impaired.

Vessels deployed in product tanker spot market

During the year, impairment losses of US\$7.9 million were recognised for 'FSL Hamburg' and 'FSL Singapore'. The decline in the vessels' recoverable amounts was caused by the premature termination of the long term bareboat charter agreements of these vessels. The recoverable amount of the vessels was determined based on value-in-use calculation using projected cash flows over the remaining useful life of about 21 years, discounted at 7.76%. The discount rate takes into account the time value of money and the risks specific to the vessels' estimated cash flows. The projected cash inflows were based on near-term freight rates forecasted by an independent industry consultant and observable historical trend of the daily charter income of a vessel of similar specifications under a one-year time charter arrangement. The projected cash outflows take into account existing and projected vessels' voyage and operating expenses. The terminal value of each vessel is determined based on the average scrap steel price per light deadweight tonne in recent years.

5 Subsidiaries

| | Trust | |
|---|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Equity investments, at cost | 119,259 | 119,259 |
| Amounts due from subsidiaries (non-trade) | 473,264 | 552,325 |
| | <u>592,523</u> | <u>671,584</u> |

Details of the subsidiaries are as follows:

| Name of subsidiaries | Country of Incorporation | Effective equity held by the Group | |
|----------------------|-----------------------------|---------------------------------------|-----------|
| | | 2010 % | 2009 % |
| FSL-1, Inc. | Marshall Islands | 100 | 100 |
| FSL-2, Inc. | Marshall Islands | 100 | 100 |
| FSL-3, Inc. | Marshall Islands | 100 | 100 |
| FSL-4, Inc. | Marshall Islands | 100 | 100 |
| FSL-5, Inc. | Marshall Islands | 100 | 100 |
| FSL-6, Inc. | Marshall Islands | 100 | 100 |
| FSL-7, Inc. | Marshall Islands | 100 | 100 |
| FSL-8, Inc. | Marshall Islands | 100 | 100 |

| Name of subsidiaries | Country of Incorporation | Effective equity held by the Group | |
|----------------------|--------------------------|------------------------------------|-----------|
| | | 2010 % | 2009 % |
| FSL-9 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-10 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-11 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-12 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-13 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-14, Inc. | Marshall Islands | 100 | 100 |
| FSL-15, Inc. | Marshall Islands | 100 | 100 |
| FSL-16, Inc. | Marshall Islands | 100 | 100 |
| FSL-18 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-19 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-20, Inc. | Marshall Islands | 100 | 100 |
| FSL-21, Inc. | Marshall Islands | 100 | 100 |
| FSL-22, Inc. | Marshall Islands | 100 | 100 |
| FSL-23 Pte. Ltd. | Singapore | 100 | 100 |
| FSL-24 Pte. Ltd. | Singapore | 100 | 100 |

KPMG LLP, Singapore are the auditors for all of the Singapore-incorporated subsidiaries. No statutory audit is required for subsidiaries incorporated in the Marshall Islands under the laws of incorporation.

The amounts due from subsidiaries are unsecured and interest-free. As the amounts are, in substance, part of the Trust's net investments in the subsidiaries, they are included as interests in subsidiaries and stated at cost less impairment losses.

All of the Singapore-flagged vessel-owning subsidiaries are subject to externally imposed capital requirements as required under Regulation 5 of the Merchant Shipping (Registry of Ships) Regulations. These subsidiaries have complied with the requirements during the financial year.

6 Derivative assets

| | Group and Trust | |
|-----------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Non-current | | |
| Financial derivatives | 476 | - |
| Current | | |
| Financial derivatives | 188 | - |

The derivative financial assets relate to the cumulative fair value change of hedged instruments designated as cash flow hedges. The following are the expected contractual undiscounted cash inflows of derivatives:

| | Carrying amount | Cash flows | | |
|---|--------------------|---------------------------|------------------|------------------------|
| | US\$'000 | Contractual cash flows | Within 1 year | Within 1 to 5 years |
| | | US\$'000 | US\$'000 | US\$'000 |
| Group and Trust | | | | |
| 2010 | | | | |
| Derivative financial assets | | | | |
| Cross currency swap contracts used for hedging | | | | |
| - inflow | 664 | 675 | 188 | 487 |

7

Inventories

| | Group | | Trust | |
|-------------------|------------------|------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 | 2010 US\$'000 | 2009 US\$'000 |
| Bunkers | 395 | - | - | - |
| Consumable stores | 343 | - | - | - |
| | 738 | - | - | - |

8

Deposits, prepayments and receivables

| | Group | | Trust | |
|--|------------------|------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 | 2010 US\$'000 | 2009 US\$'000 |
| Other receivables | 60 | 1,118 | 44 | 1,118 |
| Amounts due from subsidiaries (non-trade) | - | - | 90,586 | 95,085 |
| Deposits | 1,637 | - | - | - |
| Trade receivables | 1,803 | - | - | - |
| Loans and receivables | 3,500 | 1,118 | 90,630 | 96,203 |
| Prepayments | 258 | 164 | 113 | 52 |
| | 3,758 | 1,282 | 90,743 | 96,255 |

The amounts due from subsidiaries are unsecured, interest-free and repayable on demand. There is no allowance for doubtful debts arising from the outstanding balances.

Deposits pertain to security deposit posted with the Japanese Court for the release of a vessel, 'FSL Singapore'.

The ageing of trade receivables at the reporting date was:

| | Group | |
|-----------------------|-----------------|-----------------|
| | 2010 | 2009 |
| | US\$'000 | US\$'000 |
| Past due 1 – 30 days | 1,036 | - |
| Past due 31 – 60 days | 175 | - |
| Past due 61 – 90 days | 70 | - |
| More than 90 days | 522 | - |
| | <u>1,803</u> | <u>-</u> |

No impairment allowance is necessary for trade receivables, including the past due receivables as there are no indications from customers on their inability to pay their outstanding balances.

9 Cash and cash equivalents

| | Group | | Trust | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2010 | 2009 | 2010 | 2009 |
| | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| Restricted cash | 2,800 | - | 2,800 | - |
| Fixed deposits with financial institutions | 48,312 | 41,919 | 48,312 | 41,919 |
| Cash at bank | 4,734 | 14,851 | 678 | 14,850 |
| | <u>55,846</u> | <u>56,770</u> | <u>51,790</u> | <u>56,769</u> |

Restricted cash pertains to a banker's guarantee of US\$2.8 million, provided as security for the release of a vessel, 'FSL Hamburg'.

The weighted average effective interest rate relating to cash and cash equivalents at the reporting date for the Group and Trust is 0.25% (2009: 0.43%) per annum. Interest rates reprice at intervals within 3 months.

All the cash and cash equivalents are primarily denominated in the functional currencies of the Group entities.

10 Units in issue

| | Group and Trust | |
|---|------------------------|------------------|
| | 2010 | 2009 |
| | Number of | Number of |
| | units | units |
| | '000 | '000 |
| Fully paid units: | | |
| At 1 January | 598,665 | 501,270 |
| Issue of units pursuant to Distribution Reinvestment Scheme | - | 15,554 |
| Issue of units pursuant to equity placement | - | 80,000 |
| Issue of units as payment for incentive fees to the Trustee-Manager | - | 1,841 |
| At 31 December | <u>598,665</u> | <u>598,665</u> |

In 2009, the Trust carried out an equity placement exercise. The proceeds from the equity placement, earmarked for acquisition of vessels, had not been deployed as at 31 December 2010. The unit issue costs, comprising professional, advisory and other costs relating to the issuance of units in the Trust, were deducted directly against the unitholders' funds.

Each unit in the Trust represents an undivided interest in the Trust. The rights and interests of unitholders are contained in the Trust Deed and include the right to:

- receive income and other distributions attributable to the units held;
- participate in the termination of the Trust by receiving a share of all net cash proceeds derived from the realisation of the assets of the Trust less any liabilities, in accordance with their proportionate interests in the Trust;
- exercise one vote per unit at all unitholders' meetings; and
- receive audited accounts and the annual report of the Trust.

The restrictions of a unitholder include the following:

- a unitholder has no right to request the Trustee-Manager to transfer to him any assets (or part thereof) or of any estate or interest in any asset (or part thereof) of the Trust;
- a unitholder cannot give any directions to the Trustee-Manager (whether at a meeting of unitholders or otherwise) if it would require the Trustee-Manager to do or omit doing anything which may result in:
 - the Trust ceasing to comply with applicable laws and regulations; or
 - the exercise of any discretion expressly conferred to the Trustee-Manager by the Trust Deed.
- a unitholder's right is limited to the right to require due administration of the Trust in accordance with the provisions of the Trust Deed; and
- a unitholder has no right to request the Trustee-Manager to redeem his units while the units are listed on Singapore Exchange Securities Trading Limited.

A unitholder's liability is limited to the amount paid or payable for any units in the Trust. The provisions of the Trust Deed provide that no unitholders will be personally liable to indemnify the Trustee-Manager or any creditor of the Trustee-Manager in the event the liabilities of the Trust exceed its assets.

Capital management

The Trustee-Manager defines "capital" to include funds raised through the issuance of units, revenue reserves and proceeds raised from debt facilities. The Trustee-Manager's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the Trust. The Trustee-Manager monitors the distribution per unit, which is the annualised distribution to unitholders divided by total number of units.

The cash flows from the operating activities of the Trust are sufficient to fund the anticipated debt service, quarterly distributions to unitholders, payments to Trustee-Manager and working capital requirements. To the extent that financing for additional vessels is required, additional equity or debt securities may be issued or additional secured borrowings may be incurred.

There were no changes in the Trust's approach to capital management during the year.

The Trust is not subject to externally or regulatory imposed capital requirements.

11 Reserves

| | Group | | Trust | |
|--------------------------------------|------------------|------------------|------------------|------------------|
| | 2010 | 2009 | 2010 | 2009 |
| | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| Hedging reserve | (25,997) | (27,120) | (25,997) | (27,120) |
| Foreign currency translation reserve | (943) | 3,436 | - | - |
| Accumulated losses | (140,885) | (105,852) | (236,469) | (178,726) |
| | <u>(167,825)</u> | <u>(129,536)</u> | <u>(262,466)</u> | <u>(205,846)</u> |

The hedging reserve comprises the effective portion of the cumulative net changes in the fair value of cash flow hedging instruments until they are derecognised or impaired.

The foreign currency translation reserve comprises:

- (a) foreign exchange differences arising from the translation of the financial statements of foreign operations whose functional currencies are different from the functional currency of the Trust; and
- (b) foreign exchange differences on monetary items which form part of the Group's net investment in foreign operations provided certain conditions are met.

The accumulated losses refer to the cumulative accounting profits earned after deduction of distributions to unitholders. At the reporting date, the cumulative distributions were in excess of the cumulative accounting profits recorded, as allowed under the Singapore Business Trusts Act. The movement of the accumulated losses is disclosed in the Consolidated Statement of Changes in Unitholders' funds.

12 Financial liabilities

| | Group and Trust | |
|-----------------------|-----------------|----------------|
| | 2010 | 2009 |
| | US\$'000 | US\$'000 |
| Non-current | | |
| Secured bank loans | 432,409 | 456,292 |
| Financial derivatives | 14,289 | 14,561 |
| | <u>446,698</u> | <u>470,853</u> |
| Current | | |
| Secured bank loans | 25,240 | 32,000 |
| Financial derivatives | 12,748 | 12,935 |
| | <u>37,988</u> | <u>44,935</u> |

The Trust has substantially utilised the revolving credit facility of US\$515,000,000 ("combined facility") to finance the acquisition of vessels before any subsequent repayment of the borrowings.

In 2009, the Trustee-Manager successfully obtained an agreement from the secured lenders to reduce the minimum coverage ratio of the charter-free fair market value of the Trust's vessel portfolio over its outstanding indebtedness from 145% to 100% till 30 June 2011 (the "Amendment Period"). The Trust will also make quarterly loan repayments of US\$8 million (applied on a pro-rata basis to all the three tranches) during the Amendment Period.

As the combined facility is revolving in nature, the Trust will be able to re-draw on the committed but undrawn portion of the facility after the Amendment Period.

The combined facility is secured on the following:

- (i) a first priority mortgage over the Group's vessels in the portfolio;
- (ii) a first priority assignment of the Group's rights, title, interest in the insurances to and for each vessel, including insurance for hull and machinery, protection and indemnity and war risks; and
- (iii) a first priority assignment of the Group's rights, title and interest in and to the bareboat charter agreement and the charter income of each vessel.

Terms and debt repayment schedule

The terms and conditions of the outstanding bank loans are as follows:

| Group and Trust | | Nominal interest rate | Year of maturity | Face value US\$'000 | Carrying amount US\$'000 |
|-----------------------------|-------|--|--------------------------|---------------------------|--------------------------------|
| US\$ floating rate loans | (i) | US\$ 3-month LIBOR + 1.7% [#] | 2014 | 230,043 | 228,785 |
| | (ii) | US\$ 3-month LIBOR + 1.7% ^{##} | 2012 | 184,034 | 183,039 |
| | (iii) | US\$ 3-month LIBOR + 1.7% ^{##} | 2010 – 2012 [^] | 46,187 | 45,825 |
| | | | | 460,264* | 457,649 |

[#] This margin applies during the Amendment Period, and will be reduced to 1.25% per annum after the Amendment Period.

^{##} This margin applies during the Amendment Period, and will be reduced to 1.45% per annum after the Amendment Period.

[^] Commitment amount for this tranche was reduced to US\$61,250,000 on 20 September 2010 and will be further reduced by US\$3,750,000 every quarter thereafter.

* Before the deduction of unamortised debt transaction costs of US\$2,615,000.

The following are the expected contractual undiscounted cash outflows of non-derivative financial liabilities, including interest payments and excluding the impact of netting agreements:

| Group | Carrying amount US\$'000 | Cash flows | | |
|---|------------------------------------|---------------------------------------|------------------------------|------------------------------------|
| | | Contractual cash flows US\$'000 | Within 1 year US\$'000 | Within 1 to 5 years US\$'000 |
| 2010 | | | | |
| Non-derivative financial liabilities | | | | |
| US\$ floating rate loans | 459,001 | (487,013) | (34,192) | (452,821) |
| Trade and other payables | 3,261 | (3,261) | (3,261) | - |
| | <u>462,262</u> | <u>(490,274)</u> | <u>(37,453)</u> | <u>(452,821)</u> |
| 2009 | | | | |
| Non-derivative financial liabilities | | | | |
| US\$ floating rate loans | 489,667 | (548,216) | (42,716) | (505,500) |
| Trade and other payables | 1,606 | (1,606) | (1,606) | - |
| | <u>491,273</u> | <u>(549,822)</u> | <u>(44,322)</u> | <u>(505,500)</u> |
| Trust | | | | |
| 2010 | | | | |
| Non-derivative financial liabilities | | | | |
| US\$ floating rate loans | 459,001 | (487,013) | (34,192) | (452,821) |
| Trade and other payables | 284 | (284) | (284) | - |
| | <u>459,285</u> | <u>(487,297)</u> | <u>(34,476)</u> | <u>(452,821)</u> |
| 2009 | | | | |
| Non-derivative financial liabilities | | | | |
| US\$ floating rate loans | 489,667 | (548,216) | (42,716) | (505,500) |
| Trade and other payables | 1,444 | (1,444) | (1,444) | - |
| | <u>491,111</u> | <u>(549,660)</u> | <u>(44,160)</u> | <u>(505,500)</u> |

The derivative financial liabilities relate to the cumulative fair value change of hedged instruments designated as cash flow hedges. The following are the expected contractual undiscounted cash outflows of derivatives:

| Group and Trust | Carrying amount US\$'000 | Cash flows | | |
|---|------------------------------------|---------------------------------------|------------------------------|------------------------------------|
| | | Contractual cash flows US\$'000 | Within 1 year US\$'000 | Within 1 to 5 years US\$'000 |
| 2010 | | | | |
| Derivative financial liabilities | | | | |
| Interest rate swaps used for hedging | | | | |
| - outflow | <u>27,037</u> | <u>28,910</u> | <u>14,366</u> | <u>14,544</u> |

| | Carrying amount | Cash flows | | |
|---|--------------------|---------------------------|------------------|------------------------|
| | | Contractual cash flows | Within 1 year | Within 1 to 5 years |
| | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| Group and Trust | | | | |
| 2009 | | | | |
| Derivative financial liabilities | | | | |
| Interest rate swaps used for hedging | | | | |
| - outflow | 25,917 | (27,919) | (14,043) | (13,876) |
| Cross currency swap contracts used for hedging | | | | |
| - outflow | 1,579 | (1,641) | (497) | (1,144) |
| | <u>27,496</u> | <u>(29,560)</u> | <u>(14,540)</u> | <u>(15,020)</u> |

13 Trade and other payables

| | Group | | Trust | |
|-------------------------------------|------------------|------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 | 2010 US\$'000 | 2009 US\$'000 |
| Trade payables | 720 | 31 | 23 | 31 |
| Accrued financing expenses | 2,943 | 2,949 | 2,943 | 2,949 |
| Accrued operating expenses | 1,383 | 1,575 | 261 | 1,413 |
| Lease income received in advance | 2,682 | 2,159 | - | - |
| Other payables | 1,158 | - | - | - |
| | <u>8,886</u> | <u>6,714</u> | <u>3,227</u> | <u>4,393</u> |

14 Revenue

| | Group | |
|-------------------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Bareboat charter lease income | 94,559 | 98,768 |
| Freight income | 5,935 | - |
| | <u>100,494</u> | <u>98,768</u> |

Bareboat charter lease income relates to lease income derived from operating leases.

During the year, the charterers of two vessels 'FSL Hamburg' and 'FSL Singapore' requested the Trust to take delivery of these vessels on the basis that they did not intend to continue to make full lease payments under the bareboat charter lease agreements. Following the premature termination of the long-term bareboat charter agreements, the two vessels are employed in the product tanker spot market to derive freight income.

15 Finance income and expenses

| | Group | |
|---|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Recognised in the income statement | | |
| Interest income from cash and cash equivalents | 249 | 165 |
| Finance income | 249 | 165 |
| Interest expense: | | |
| - bank loans | 24,565 | 23,368 |
| - amortisation of debt transaction costs | 1,377 | 1,072 |
| - commitment and bank agency fees | 183 | 94 |
| Ineffective portion of changes in fair value of interest rate swaps | - | 376 |
| Net foreign exchange gain | (222) | (2,157) |
| Finance expenses | 25,903 | 22,753 |
| Net finance expenses recognised in income statement | (25,654) | (22,588) |

16 (Loss)/Profit before income tax

The following items have been included in arriving at (loss)/profit before income tax:

| | Group | |
|--------------------------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Non-audit fees paid/payable to: | | |
| - auditors of the Trust | 213 | 107 |
| - other auditors | 35 | 131 |
| Amortisation of initial direct costs | 534 | 631 |

17 Income tax expense/(credit)

| | Group | |
|--|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Current tax expense/(credit) | | |
| Current year | 9 | - |
| Over provision in prior year | - | (14) |
| | 9 | (14) |
| Reconciliation of effective tax rate | | |
| (Loss)/Profit before income tax | (5,690) | 8,409 |
| Tax calculated using Singapore tax rate of 17% (2009: 17%) | (967) | 1,430 |
| Income not subject to tax | (17,155) | (17,157) |
| Expenses not deductible for tax purposes | 18,131 | 15,727 |
| Over provision in prior year | - | (14) |
| | 9 | (14) |

18 Income available for distribution

| | Group | |
|---|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Income available for distribution to unitholders at the beginning of the year | 8,980 | 15,442 |
| (Loss)/Profit for the year | (5,699) | 8,423 |
| Net adjustments (Note A) | 31,741 | 33,552 |
| Income available for distribution | 26,042 | 41,975 |
| Distribution to unitholders: | | |
| For the period from 1 October 2009 to 31 December 2009 | | |
| - Distribution of US1.50 cents per unit (tax-exempt income) | (8,980) | - |
| For the period from 1 January 2010 to 31 March 2010 | | |
| - Distribution of US1.50 cents per unit (tax-exempt income) | (8,980) | - |
| For the period from 1 April 2010 to 30 June 2010 | | |
| - Distribution of US0.95 cents per unit (tax-exempt income) | (5,687) | - |
| For the period from 1 July 2010 to 30 September 2010 | | |
| - Distribution of US0.95 cents per unit (tax-exempt income) | (5,687) | - |
| For the period from 1 October 2008 to 31 December 2008 | | |
| - Distribution of US3.08 cents per unit (tax-exempt income) | - | (15,439) |
| For the period from 1 January 2009 to 31 March 2009 | | |
| - Distribution of US2.45 cents per unit (tax-exempt income) | - | (12,326) |
| For the period from 1 April 2009 to 30 June 2009 | | |
| - Distribution of US2.45 cents per unit (tax-exempt income) | - | (12,707) |
| For the period from 1 July 2009 to 30 September 2009 | | |
| - Distribution of US1.50 cents per unit (tax-exempt income) | - | (7,965) |
| | (29,334) | (48,437) |
| Income available for distribution to unitholders at the end of the year | 5,688 | 8,980 |

On 19 January 2011, the Trust declared a distribution of US0.95 cents per unit for the period from 1 October 2010 to 31 December 2010.

Note A

| | Group | |
|---|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Net adjustments comprise: | | |
| Non-cash adjustments: | | |
| - Depreciation expense on vessels | 58,996 | 61,295 |
| - Amortisation of debt transaction costs | 226 | 213 |
| - Amortisation of initial direct costs | 88 | 109 |
| - Unrealised foreign exchange gain | (174) | (1,617) |
| - Impairment loss on vessels | 7,865 | - |
| Ineffective portion of changes in fair value of interest rate swaps | - | 376 |
| | 67,001 | 60,376 |
| Repayment of secured bank loans | (32,000) | (17,005) |
| Amount not available for distribution | (3,260) | (9,819) |
| Net adjustments | 31,741 | 33,552 |

19 Earnings per unit

| | Group | |
|---|-----------------|----------|
| | 2010 | 2009 |
| | US\$'000 | US\$'000 |
| Basic and diluted earnings per unit is based on: | | |
| (Loss)/Profit for the year | (5,699) | 8,423 |
| | <hr/> | |
| | Number of units | |
| | '000 | '000 |
| Issued units at beginning of the year | 598,665 | 501,270 |
| Effect of units issued | - | 34,119 |
| Weighted average number of units at the end of the year | 598,665 | 535,389 |

20 Financial risk management

Overview

Risk management is integral to the whole business of the Group. The Group is exposed to credit, liquidity and market risks. The Group uses derivative financial instruments to hedge its interest rate and foreign currency risk exposures. The Group does not hold or issue derivative financial instruments for trading purposes.

Management uses natural hedges or closely monitors the Group's business risk exposures in connection with its financial assets and financial liabilities and adopts the appropriate measures including the use of other financial instruments when considered necessary to reduce any potential financial risk exposures or losses.

Credit risk

As part of the Trustee-Manager's due diligence activities and prior to the completion of a lease transaction, each new lessee is analysed individually for creditworthiness. The Trustee-Manager then incorporates the results from its due diligence activities into a risk-adjusted pricing model. This model incorporates a credit loss component which takes into account the likelihood of default, the level of recoverability following a default and the credit exposure at the time of default.

Upon the completion of a lease transaction, the Trustee-Manager conducts on-going credit reviews annually or semi-annually to monitor each lessee's financial performance and compliance with financial covenants (if any). In addition, the payment conduct of a lessee is monitored on a monthly basis.

The Group's credit risk is concentrated in lessees in the shipping industry; and the Group's maximum exposure to credit risk in the event that counterparties fail to perform their obligations as of 31 December 2010 in relation to each class of recognised financial assets is the carrying amount of those assets as indicated in the statements of financial position.

The Group does not expect to incur material credit losses on its financial assets. Cash and cash equivalents are placed with financial institutions which are regulated.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as and when they fall due. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of 30 days, including the servicing of financial obligations. The Group also ensures that it has sufficient cash for quarterly distributions to its unitholders. In conjunction with the agreement obtained from the secured lenders in September 2009 (see note 12), the Trust will be able to re-draw on the committed but undrawn portion of its credit facility after 30 June 2011. As at the reporting date, the undrawn portion of the credit facility is US\$47,236,000 (2009: US\$22,736,000) and there were no outstanding commitments for any acquisition of vessels.

Market risk

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates, will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters.

Interest rate risk

The Group adopts a policy of ensuring that 100% of its exposure to changes in interest rates on bank loans is hedged. Where natural hedges are not available, the Group manages the risk using interest rate swaps to convert the floating rates under the bank loans to fixed rates. Nine interest rate swaps, denominated in US dollar, have been entered into to achieve this purpose. The swaps mature over the next four years following the maturity of the related loan obligations. The all-in effective interest rates for these interest rate swaps range from 4.74% to 6.94% per annum (2009: 4.74% to 6.94% per annum).

As at 31 December 2010, the Group has interest rate swaps with a total notional contract amount of US\$376,074,000 (2009: US\$378,045,000), whereby it pays fixed interest rates ranging from 3.04% per annum to 5.24% per annum and receives a variable rate equal to the US\$3-month LIBOR. The Trust classifies these interest rate swaps as hedging instruments under the cash flow hedge model.

The net cumulative fair value change of these interest rate swaps as at 31 December 2010 is US\$27,037,000 (2009: US\$25,917,000). This amount is recognised as financial derivatives in "financial liabilities".

Sensitivity analysis

With respect to the interest rate swaps (designated as hedging instruments under cash flow hedge model), variable rate bank loans and certain floating rate lease agreements, a change of 50 bp in interest rate at the reporting date would increase (decrease) other comprehensive income and profit or loss by the amounts shown below. This analysis assumes that all other variables remain constant.

| | Other comprehensive income | | Profit or loss | |
|----------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| | 50 bp increase US\$'000 | 50 bp decrease US\$'000 | 50 bp increase US\$'000 | 50 bp decrease US\$'000 |
| Group and Trust | | | | |
| 31 December 2010 | | | | |
| Variable rate bank loans | - | - | (2,398) | 2,398 |
| Interest rate swaps | 4,605 | (3,794) | 1,925 | (1,925) |
| | 4,605 | (3,794) | (473) | 473 |
| Floating rate lease income | - | - | 673 | (673) |
| | 4,605 | (3,794) | 200 | (200) |
| 31 December 2009 | | | | |
| Variable rate bank loans | - | - | (2,562) | 2,562 |
| Interest rate swaps | 6,356 | (5,386) | 1,910 | (1,910) |
| | 6,356 | (5,386) | (652) | 652 |
| Floating rate lease income | - | - | 691 | (691) |
| | 6,356 | (5,386) | 39 | (39) |

The Group has entered into two floating rate lease arrangements ("host contracts") which are pegged to the US\$ 3-month LIBOR ("embedded derivatives"). These arrangements provide an economic hedge against the interest rate risk exposure arising from the respective loans relating to these leases.

The Trustee-Manager considers the economic characteristics and risks of these embedded derivatives to be closely related to the economic characteristics and risks of the host contracts. Accordingly, in respect of these embedded derivatives, no separate accounting from the host contracts is required as the embedded derivatives are essentially contingent rentals based on variable interest rates.

Foreign currency risk

The Group is exposed to foreign currency risk on certain lease income denominated in a currency other than the functional currency of the Trust. The currency giving rise to this risk is the Euro.

The Group hedges 100% of its forecasted lease income denominated in the Euro. As at 31 December 2010, the Group uses cross currency swap contracts with a total notional contract amount of US\$22,523,000 (2009: US\$31,979,000), to hedge the foreign currency risk associated with its forecasted Euro revenue. The net cumulative fair value gain for these cross currency swap contracts as at 31 December 2010 is US\$664,000 (2009: loss of US\$1,579,000). This amount is recognised as financial derivatives in "derivative assets".

In respect of other monetary assets and liabilities held in currencies other than the US dollar, the Group ensures that the net exposure is kept to an acceptable level by buying or selling foreign currencies at spot rates, where necessary, to address short term imbalances.

The Group's and the Trust's exposures to foreign currencies are as follows:

| | 31 December 2010 | | 31 December 2009 | |
|---------------------------------|------------------|---------------------------------|------------------|---------------------------------|
| | Euro US\$'000 | Singapore dollar US\$'000 | Euro US\$'000 | Singapore dollar US\$'000 |
| Group | | | | |
| Cross currency swap contracts * | | | | |
| (notional amounts) | 22,523 | - | 31,979 | - |
| Other receivables | - | 22 | - | 101 |
| Cash and cash equivalents | 533 | 245 | 11 | 1,189 |
| Trade payables | 53 | 40 | - | - |
| | <hr/> | | <hr/> | |
| Trust | | | | |
| Cross currency swap contracts * | | | | |
| (notional amounts) | 22,523 | - | 31,979 | - |
| Other receivables | - | 22 | - | 101 |
| Cash and cash equivalents | 10 | 205 | 11 | 1,189 |
| Trade payables | - | 22 | - | - |
| | <hr/> | | <hr/> | |

* Designated as hedging instruments under cash flow hedge model.

Sensitivity analysis

A 10% strengthening of US dollar against the following currencies at the reporting date would increase (decrease) other comprehensive income and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant.

| | Group | | Trust | |
|-------------------------|--|-------------------------------|--|-------------------------------|
| | Other comprehensive income US\$'000 | Profit or loss US\$'000 | Other comprehensive income US\$'000 | Profit or loss US\$'000 |
| 31 December 2010 | | | | |
| Euro | 2,149 | (54) | 2,149 | (1) |
| Singapore dollar | - | (25) | - | (23) |
| | <hr/> | | <hr/> | |
| 31 December 2009 | | | | |
| Euro | 3,239 | (1) | 3,239 | (1) |
| Singapore dollar | - | (117) | - | (117) |
| | <hr/> | | <hr/> | |

A 10% weakening of US dollar against the following currencies at the reporting date would increase (decrease) other comprehensive income and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant.

| | Group | | Trust | |
|-------------------------|--|-------------------------------|--|-------------------------------|
| | Other comprehensive income US\$'000 | Profit or loss US\$'000 | Other comprehensive income US\$'000 | Profit or loss US\$'000 |
| 31 December 2010 | | | | |
| Euro | (2,149) | 54 | (2,149) | 1 |
| Singapore dollar | - | 25 | - | 23 |
| 31 December 2009 | | | | |
| Euro | (3,239) | 1 | (3,239) | 1 |
| Singapore dollar | - | 117 | - | 117 |

Estimation of fair values

The following summarises the significant methods and assumptions used in estimating the fair values of financial instruments of the Group and the Trust.

Derivatives

The fair value of derivative instruments is calculated by reference to current forward exchange rates and interest rates for contracts with similar maturity profiles, and discounting the estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

Non-derivative financial liabilities

The Group believes that the carrying amount of the floating interest secured bank loans, which are repriced on a quarterly basis, closely reflects the corresponding fair values.

Other financial assets and liabilities

The carrying amounts of financial assets and liabilities with a maturity of less than one year (including trade and other receivables, cash and cash equivalents, trade receivables and trade and other payables) approximate their fair values because of the short period to maturity.

Interest rates used in determining fair values

The interest rates used to discount estimated cash flows, where applicable, are based on US\$ yield curve and Euro yield curve at the reporting date for interest rate swaps and cross currency swap contracts respectively, and were as follows:

| | 2010 % | 2009 % |
|-------------------------------|-------------|-------------|
| Interest rate swaps | 0.15 – 1.43 | 0.24 – 2.69 |
| Cross currency swap contracts | 0.19 – 1.64 | 0.09 – 2.78 |

Carrying amount of financial assets and liabilities

The following table summarises the carrying amount of financial assets and liabilities recorded at the end of the year by IAS 39 categories:

| | Group | | Trust | |
|---------------------------|-----------------------------|--|-----------------------------|--|
| | Loan and receivables | Financial liabilities at amortised cost | Loan and receivables | Financial liabilities at amortised cost |
| | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| 2010 | | | | |
| Deposits and receivables | 3,500 | - | 90,630 | - |
| Cash and cash equivalents | 55,846 | - | 51,790 | - |
| Trade and other payables | - | 8,886 | - | 3,227 |
| Secured bank loans | - | 457,649 | - | 457,649 |
| | <u>59,346</u> | <u>466,535</u> | <u>142,420</u> | <u>460,876</u> |
| 2009 | | | | |
| Other receivables | 1,118 | - | 96,203 | - |
| Cash and cash equivalents | 56,770 | - | 56,769 | - |
| Trade and other payables | - | 6,714 | - | 4,393 |
| Secured bank loans | - | 488,292 | - | 488,292 |
| | <u>57,888</u> | <u>495,006</u> | <u>152,972</u> | <u>492,685</u> |

Fair value hierarchy

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

- Level 1 : quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 : inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 : inputs for the asset or liability that are not based on observable market data (unobservable inputs).

| | Fair value measurement at the end of the reporting date using | | | |
|---|--|-----------------|-----------------|-----------------|
| | Level 1 | Level 2 | Level 3 | Total |
| | US\$'000 | US\$'000 | US\$'000 | US\$'000 |
| Group and Trust 31 December 2010 | | | | |
| Assets | | | | |
| Derivative assets | - | 664 | - | 664 |
| Liabilities | | | | |
| Derivative liabilities | - | 27,037 | - | 27,037 |

| | Fair value measurement at the end of the reporting date using | | | |
|-------------------------|--|---------------------|---------------------|-------------------|
| | Level 1 US\$'000 | Level 2 US\$'000 | Level 3 US\$'000 | Total US\$'000 |
| Group and Trust | | | | |
| 31 December 2009 | | | | |
| Liabilities | | | | |
| Derivative liabilities | - | 27,496 | - | 27,496 |

21 Commitments

The non-cancellable operating lease rentals receivable are as follows:

| | Group | |
|---------------------------------|------------------|------------------|
| | 2010 US\$'000 | 2009 US\$'000 |
| Within 1 year | 86,181 | 101,292 |
| After 1 year but within 5 years | 333,113 | 400,869 |
| After 5 years | 178,004 | 254,603 |
| | <u>597,298</u> | <u>756,764</u> |

Except for two lease agreements in which their base rental contains an adjustment which is pegged to US\$3-month LIBOR, the rental rates of the lease arrangements are fixed over the base lease term. The base lease terms under these non-cancellable leases range from nine to twelve years (2009: seven to twelve years). In nine lease agreements (2009: eleven lease agreements) held by the Group, the lessees have the options to extend the lease period beyond the base lease period up to ten years. The lessees also have the option to purchase the related vessels in all of the lease agreements.

22 Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common significant influence. Related parties may be individuals or other entities. The Trustee-Manager is a subsidiary of a substantial unitholder of the Trust.

Other than disclosed elsewhere in the financial statements, transactions with related parties are as follows:

| | Group | |
|---|-----------------|-----------------|
| | 2010 | 2009 |
| | US\$'000 | US\$'000 |
| Transactions with the Trustee-Manager: | | |
| Management fees | 3,563 | 3,959 |
| Trustee fees | 175 | 183 |
| Transactions with other related parties: | | |
| Directors' fees paid to non-executive directors | 184 | 173 |
| Lease rentals received from Schoeller Holdings Ltd * | (6,193) | (6,541) |
| Inspection fees paid to Columbia Shipmanagement Ltd * | 90 | 159 |
| Commission paid to United Product Tankers * | 54 | - |
| Commission paid to Columbia Shipmanagement Ltd * | 16 | - |
| Bunkers commission paid to United Fuel Services * | 9 | - |
| Port charges paid to Horizon Shipping Agencies * | 6 | - |

No separate consideration is paid to the Trustee-Manager (other than the fees disclosed above) for services rendered by the executive directors.

* Related parties of a unitholder who holds 26% of the Trust's issued units as at 31 December 2010.

23 Segment information

No operating segment information has been prepared as the Group has only one reportable segment. With respect to the presentation of geographical information, the Group deals with several lessees and the vessels are deployed to various parts of the world at the discretion and direction of these lessees. Accordingly, the Trustee-Manager does not consider it meaningful to allocate revenues and non-current assets to specific geographical areas.

Major customers

Each of the following customers accounted for more than 10% of the Group's total revenue:

| | Group | |
|------------------------|-----------------|-----------------|
| | 2010 | 2009 |
| | US\$'000 | US\$'000 |
| James Fisher | 11,770 | 11,804 |
| Groda Shipping/Rosneft | 11,667 | 15,111 |
| Geden | 11,623 | 12,290 |
| Berlian Laju Tanker | 14,153 | 14,153 |
| Evergreen Marine | 11,695 | 11,696 |
| Yang Ming Marine | 20,055 | 20,055 |
| | <u>80,963</u> | <u>85,109</u> |

24 Contingent liabilities

In June 2010, the Trustee-Manager was notified that 'FSL Singapore' was arrested at Shimotsu, Japan and 'FSL Hamburg' was arrested at Qingdao, the People's Republic of China on the basis of allegedly unpaid bunkers charges owed by our lessees to Singapore-based Daxin Petroleum Pte Ltd ("Daxin"). To secure the release of these two vessels, a security deposit of US\$1.6 million (see Note 8) was posted with the Japanese Court and a banker's guarantee of US\$2.8 million (see Note 9) was provided as security.

In the event that the courts in Japan and People's Republic of China rule in favour of Daxin, the security deposit and the banker's guarantee (a fixed deposit was pledged in connection to this) may be subjected to claim by the counterparties concerned.