

COMPANY NO. 5147938

BORDERS & SOUTHERN PETROLEUM PLC
ANNUAL REPORT AND
AUDITED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED
30 JUNE 2005

Borders & Southern Petroleum plc

Borders & Southern Petroleum plc (or “the Company”) is a UK based Company engaged in the exploration of hydrocarbons. The Company’s shares are listed on the Alternative Investment Market of the London Stock Exchange (AIM).

Highlights

- Company incorporated June 2004
 - Awarded first exploration licences in the Falkland Islands with an effective date of 1 November 2004
 - Listed on AIM May 2005, raising £10 million (gross)
 - Successfully completed first operated seismic programme June 2005
-

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Chairman's Statement

Borders & Southern Petroleum has experienced an exciting 12 months. The Company has made significant advances from its incorporation in June 2004, ending the financial year with the completion of its first operated seismic campaign. During this period we have put in place a strong Board of Directors with a good blend of commercial and technical oil industry experience.

In October 2004 the Company was awarded its first exploration acreage, an area of nearly 20,000 sq km in the South Falkland Basin. In particular, we wanted to test the fold belt trend located some 150 km to the south of the Falkland Islands. This east-west oriented belt contains numerous large simple structures that could form effective traps for hydrocarbons. The 2D seismic acquired in June 2005 was focused on defining these structures and assessing their prospectivity.

In May 2005 the Company listed on the Alternative Investment Market of the London Stock Exchange and raised £10 million (gross). This was in order to fund its initial work programme in the Falkland Islands and the screening of new projects.

Within the next couple of months we anticipate that the interpretation of the Falkland Islands 2D seismic will be completed, giving us a better understanding of the hydrocarbon potential of the basin and in particular the fold belt. An operational update will be released before the end of the year together with an outline of our future work programme.

We currently have a strong balance sheet with enough cash reserves to cover further seismic acquisitions in the Falkland Islands should it be needed. Over the next 12 months we will also be looking to develop our exploration portfolio by adding new projects in countries and basins that meet our strategy and investment criteria.

Borders & Southern Petroleum has made great progress over the last 12 months and we look forward to further developments in the coming year.

Harry Dobson
Non-Executive Chairman

Operational Review

Licence award

In June 2004, having screened the legacy offshore seismic database in the Falkland Islands, we applied for exploration acreage in the South Falkland Basin, and were subsequently awarded five production licences with an effective date of 1 November 2004. The licences cover an area of 19,598 sq km and occur in water depths of between 200 to 3,000 metres. Very little seismic data had previously been acquired in this area, but the few lines that did exist showed evidence of a fold belt trend, oriented east-west, extending from Argentina in the west into international waters in the east. Globally, many fold belts form prolific hydrocarbon provinces and our aim was to investigate the potential of this one. There have been no wells drilled in the South Falkland Basin to date.

The Production Licences were awarded with a work programme obligation that comprised seismic reprocessing and play fairway mapping in the first twelve months, the acquisition of 2,500 km of 2D seismic within three years, and the drilling of one well in years four to six. Optional exit points were placed after twelve months and three years, to mitigate the situation where the prospectivity could not be confirmed.

Country	Licence	Blocks	Area	Interest
Falkland Islands	PL 018	Q61, blocks 16 to 30	3,668 sq km	100% Operator
Falkland Islands	PL 019	Q62, blocks 16 to 30	3,668 sq km	100% Operator
Falkland Islands	PL 020	Q63, blocks 16 to 30	3,668 sq km	100% Operator
Falkland Islands	PL 021	Q64, blocks 1 to 30	7,381 sq km	100% Operator
Falkland Islands	PL 022	Q73, blocks 1 to 5	1,213 sq km	100% Operator

Regional evaluation

The evaluation of the basin commenced in November 2004 with regional play fairway mapping and petroleum system analysis, utilising all the existing seismic and well data. This regional analysis was undertaken to provide insight into our own acreage, particularly the distribution of source rocks, reservoirs and seals. The evaluation included the Magallanes and Malvinas Basins located to the west of the Falkland Islands, the Falkland Plateau Basin to the east, and the Bredasdorp Basin off the south coast of South Africa. The completed regional study demonstrated that the geology is similar across all these basins and that hydrocarbon discoveries have been made in all the basins that have been tested by exploration wells. This provides great encouragement to our efforts in the untested South Falkland Basin.

Seismic acquisition

To further assess the potential of our acreage Geophysical Services Incorporated (GSI) were contracted to acquire new 2D seismic data.

Specifically, our objective was to define and map structural closures and assess their prospectivity. The completion of the seismic survey in June 2005 has significantly accelerated our work programme. After only seven months of the initial three year licence term, we had completed our 2D seismic obligation. A total of 2,862 km of new data was acquired, which exceeded our

minimum work programme obligation of 2,500 km. The survey, acquired by the GSI Admiral vessel, was conducted without major health, safety or environmental incidents.

Seismic interpretation

The 2D seismic data has recently been processed by GSI in Calgary and the interpretation is underway. An operational update will be given once the interpretation has been completed. However, a preliminary review of the high quality seismic data has confirmed the presence of a major fold and thrust belt with its associated foreland basin within the Company's acreage. These seismic lines reveal considerably more structures than originally anticipated and include numerous large anticlines, tilted fault blocks and sub-thrust structures capable of trapping significant volume of hydrocarbons. The data also reveals seismic amplitude anomalies associated with many of the structures.

Building the portfolio

The Company's strategy is to build a portfolio of exploration acreage in different basins and countries. We are targeting large acreage positions that have the potential to contain multiple high value prospects and where the geological risks can be constrained by rigorous technical work.

Industry outlook

Whilst there may be some softening over the next 12 months, oil prices are anticipated to remain at relatively high levels. This is likely to cause an increase in exploration activity throughout the industry, creating increased demand for seismic vessels and drilling rigs, which will be reflected in higher prices for these services. Additionally, greater competition for acreage is likely to occur. We will take time to build the portfolio, ensuring any new project meets our stringent investment criteria, and is of similar high quality to the South Falkland Basin acreage.

Howard Obee
Chief Executive

Financial Review

During the year, the Company raised a total of £11.84 million (after costs) through a combination of private and public capital raisings, the main part of which (£9.5 million after costs) was raised at the time of the AIM listing. The capital raised to date has been applied as follows:

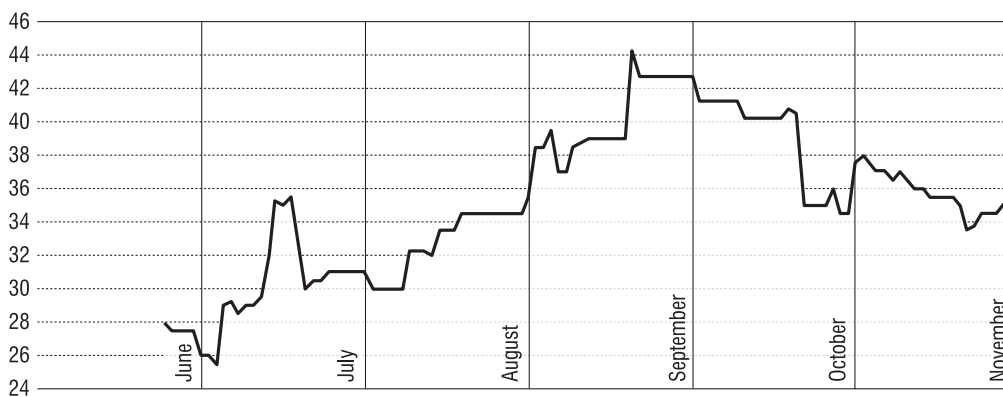
	£million
Capital Raised (after costs)	£11.84
Less:	
Purchase of 2D Seismic and office equipment	£1.35
Overheads and working capital (net of interest)	<u>£0.07</u>
Cash at 30 June 20005	<u><u>£10.42</u></u>

The cash at 30 June 2005 was held in pounds sterling in either current accounts or short term cash deposits. It is the Company's intention to continue to hold this cash on current or short term deposits until required. Post balance date, the Company converted around £3.75 million into US\$6.57 million in order to provide for any future costs payable in US\$.

The Company has sufficient funds to finance current exploration expenditure commitments and to cover general overheads for at least the next financial year.

Peter Fleming
Finance Director

Borders & Southern Petroleum plc Share Price (pence)



Board of Directors

David Harry Williamson Dobson (Non-Executive Chairman) age 57

Harry Dobson is a former investment banker and senior partner of Yorkton Securities. He currently engages in various private equity and venture capital activities in North America and Europe, and has acted as Chairman of a number of resource companies (including American Pacific Mining Company Inc. and Lytton Minerals Limited). He is currently the Chairman of Kirkland Lake Gold Inc. (a Toronto Stock Exchange and AIM quoted Company) and Rambler Metals and Mining plc (an AIM quoted Company). He is experienced in the organisation and funding of resource projects, including those located in inaccessible locations.

Howard Kevin Obee (Chief Executive) age 45

Howard Obee was appointed Chief Executive when the Company was incorporated in June 2004. He has a PhD in structural geology from Imperial College, and has spent 20 years in the oil industry, initially with BP (1985-1992), and subsequently with BHP Billiton (1992-2004). He trained as an exploration geologist, but has been appointed to various technical and commercial roles, incorporating exploration, new ventures, strategic planning, and business development. His most recent roles for BHP Billiton were West Africa Asset Team Leader, and Exploration Manager, London. He has experience of executing seismic and drilling programmes in frontier basins, including those in deep water.

Peter William Fleming (Finance Director) age 43

Peter Fleming has over 12 years of upstream oil and gas experience, the majority of which was gained at BHP Billiton both in London and Melbourne. Whilst at BHP Billiton, Peter held senior positions in exploration and business development, investment evaluation, acquisitions and disposals and strategic planning. Prior to joining BHP Billiton, he worked for Bridge Oil and Banque Indosuez. He holds Masters degrees in Business Administration and Finance.

Stephen James Douglas Posford (Non-Executive Director) age 58

Stephen Posford was a partner of stockbrokers W.Greenwell & Co. In 1986, he became Managing Director of Greenwell Montagu Gilt Edged, and in 1989 moved to Salomon Brothers to head up their proprietary trading department in London. He then became Salomon Brothers European CEO before retiring in 1996.

Christopher Nigel Hurst-Brown (Non-Executive Director) age 53

Since qualifying as a Chartered Accountant, Nigel Hurst-Brown has pursued a career in fund management. From 1986-1990 he was Chairman of Lloyd's Investment Managers. In 1990 he moved to Mercury Asset Management as a main board Director and following Mercury's acquisition by Merrill Lynch in 1997 became a Managing Director of Merrill Lynch Investment Managers. Currently he is Chief Executive of Hotchkis and Wiley (UK) Limited and a member of the Executive Committee of its US parent Hotchkis and Wiley Capital Management LLC.

Board of Directors *continued*

Number of Board Meetings	8
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Attendance:

Harry Dobson	6
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Howard Obee	8
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Peter Fleming*	4
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Steven Posford	7
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Nigel Hurst-Brown*	2
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* Peter Fleming and Nigel Hurst-Brown joined the board on 5 April 2005.

Directors' Report

For the Period Ended 30 June 2005

The Directors are pleased to present the report and the audited financial statements of the Company for the period from 8 June 2004 to 30 June 2005.

Principal activities

The Company was incorporated on 8 June 2004 and received its certificate to commence trading on 2 July 2004. The principal activity in the period was the exploration for oil and gas.

Shares held by the Directors

The beneficial and other interests of the Directors and their families in the shares of the Company as at the date of their appointment to the Board and 30 June 2005, were as follows:

		At 30 Jun 2005	At date of appointment
David Harry Williamson Dobson	appointed 8 Jun 2004	25,000,000	—
Stephen James Douglas Posford	appointed 8 Jun 2004	25,000,000	—
Howard Kevin Obee	appointed 28 Jun 2004	10,000,000	—
Christopher Nigel Hurst - Brown	appointed 5 Apr 2005	1,000,000	1,000,000
Peter William Fleming	appointed 5 Apr 2005	2,200,000	2,000,000

William Tester and Howard Thomas were both appointed directors of the Company on 8 June 2004 and both resigned on 8 June 2004.

No right to subscribe for shares in or debentures of the Company was granted or exercised in the period.

The ordinary shares in which Mr D H W Dobson is interested in are held by the Zila Corporation, a Company owned by the Whitmill Trust Company Limited, as trustee of The Lotus Trust of which he is a beneficiary.

All directors who are shareholders have undertaken not to dispose of any ordinary shares and have each undertaken to procure that any person who is connected with that Director will not dispose of any ordinary shares, except in certain limited circumstances, during the 12 month following the Company's admission to the Alternative Investment Market of the London Stock Exchange on 24 May 2005.

In the period between 30 June 2005 and 9 November 2005 there was no change in these holdings.

Directors Responsibility for the Financial Statements

Company law requires the Directors to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;

Directors' Report

For the Period Ended 30 June 2005 continued

- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.
- the Directors are responsible for maintaining proper accounting records, for safeguarding the assets of the Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Business review

A review on the operations of the Company is contained in the Operational Review on pages 2 – 3.

Results and dividends

The Company's results for the period ended 30 June 2005 are set out on page 14.

The Directors do not recommend the payment of a dividend for the period.

Substantial shareholders

At 9 November 2005 the following had notified the company of disclosable interests in 3% or more of the nominal value of the Company's shares carrying voting rights:

Name	Number of Ordinary shares	% of share capital
Zila Corporation	25,000,000	19.58
Stephen James Douglas Posford	25,000,000	19.58
BNY (OCS) Nominees Limited	12,922,500	10.12
Morstan Nominees Limited	11,856,250	9.29
Howard Kevin Obee	10,000,000	7.83
Merrill Lynch International	7,589,816	5.94
LBPB Nominees Limited	6,210,089	4.86
HSBC Global Custody Nominee (UK) Limited	5,772,980	4.52

5,000,000 of the Ordinary Shares held by Zila Corporation are registered in the name of Valerie Huxley, who holds such shares as nominee for the Zila Corporation.

Health, safety & environment

Borders & Southern Petroleum has an overriding commitment to health, safety and environmental responsibility. The Company works closely with host governments and communities in the countries in which it operates, together with its contractors and partners, to ensure internationally recognised standards are implemented and maintained along with compliance to local legislation.

Directors' Report

For the Period Ended 30 June 2005 *continued*

The Company's exploration activities in the Falkland Islands are subject to the relevant environmental protection acts. The Company closely monitors its activities to ensure to the best of its knowledge there is no potential for the breach of such regulations. There have been no convictions in relation to breaches of these Acts recorded against the Company during the reporting period.

Payment policy and practice

It is the Company's policy to settle the terms of payment with suppliers when agreeing the terms of the transaction, to ensure that suppliers are aware of these terms and to abide by them. Trade creditors at the period end amount to 66 days of average supplies for the period.

Political and charitable donations

There were no political or charitable contributions made by the Company during the period ended 30 June 2005.

Post balance sheet events

There has not been any matter or circumstance that has arisen since the balance sheet date which has significantly affected, or may significantly affect, the operations of the Company.

Auditors

In accordance with Section 385 of the Companies Act 1985, a resolution proposing that BDO Stoy Hayward LLP be reappointed as auditors of the Company and the Directors be authorised to fix their remuneration will be put to the next Annual General Meeting.

By order of the Board

H K Obee

Chief Executive

Corporate Governance

Audit committee report

The Board has established an Audit Committee comprising Mr. Hurst-Brown (Chairman), Mr. Dobson and Mr. Posford, all independent, non-executive Directors.

The Audit Committee meets at least biannually and is responsible for:

- The integrity of the financial statements of the Company and related disclosures, based on adequate books, records and internal controls and selection and consistent application of appropriate accounting policies;
- The appropriateness of the Company's internal financial controls;
- The independent auditors' qualifications, independence, and performance; and
- The compliance by the Company with legal and regulatory requirements.

Remuneration committee

The Board has established a Remuneration Committee comprising Mr. Hurst-Brown (Chairman), Mr. Dobson and Mr. Posford, all independent non-executive Directors.

The Remuneration Committee meets at least annually and is responsible for:

- Reviewing the performance of the CEO and other Executive Directors and senior management of the Company and determines their remuneration and the basis of their service agreements with due regard to the interests of Shareholders;
- The payment of any bonuses to the CEO, other Executive Directors and senior management; and
- Making recommendations to the Board with respect to equity-based incentive plans and to act as a preparatory body for the Board of Directors in the management of any Company award and option plans.

Directors' remuneration and service contracts

On 18 May 2005, all the Company's Directors each entered into a service agreement with the Company.

The remuneration of the Directors for the period ended 30 June 2005 was as follows:

	Basic salary £
David Harry Williamson Dobson	—
Peter William Fleming	5,000
Christopher Nigel Hurst – Brown	—
Howard Kevin Obee	30,000
Stephen James Douglas Posford	—
	<u>35,000</u>

Pensions

The Company does not operate a pension scheme for its Directors or employees.

Independent Auditors' Report to the Shareholders of Borders & Southern Petroleum plc

We have audited the financial statements of Borders and Southern Petroleum Plc for the period ended 30 June 2005 on pages 15 to 24 which have been prepared under the accounting policies set out on pages 17 to 18.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Report of the Directors is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the Company is not disclosed.

We read other information contained in the annual report and consider whether it is consistent with the audited financial statements. This other information comprises only the Report of the Directors and the Chairman's Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

Basis of audit opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by

Independent Auditors' Report to the Shareholders of Borders & Southern Petroleum plc *continued*

fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company at 30 June 2005 and of the loss for the period then ended, and have been properly prepared in accordance with Companies Act 1985.

BDO STOY HAYWARD LLP

Chartered Accountants
and Registered Auditors
London

14 November 2005

Profit and Loss Account

From 8 June 2004 to 30 June 2005

	Notes	£
Administrative expenses		<u>(204,785)</u>
OPERATING LOSS	4	(204,785)
Interest receivable	7	<u>63,539</u>
LOSS ON ORDINARY ACTIVITIES BEFORE TAXATION		(141,246)
Taxation	8	<u>—</u>
LOSS RETAINED FOR THE PERIOD	15	<u>(141,246)</u>
Loss per share – basic and diluted	2	(0.26p)

All amounts above amounts are in respect of continuing activities.

All recognised gains and losses in the current period are included in the profit and loss account.

The accompanying notes on pages 17 to 24 form an integral part of these financial statements

Balance Sheet

At 30 June 2005

	Notes	£	£
FIXED ASSETS			
Intangible Assets	9		1,497,668
Tangible assets	10		<u>14,965</u>
			1,512,633
CURRENT ASSETS			
Debtors	11	142,790	
Cash at bank and demand deposits		<u>10,416,100</u>	
		10,558,890	
CREDITORS: amounts falling due within one year	12	<u>(331,546)</u>	
NET CURRENT ASSETS			<u>10,227,344</u>
TOTAL ASSETS LESS CURRENT LIABILITIES			11,739,977
Provision for liabilities and charges	13		<u>(42,955)</u>
NET ASSETS			<u><u>11,697,022</u></u>
CAPITAL AND RESERVES			
Called up share capital	14		1,276,875
Share premium account	15		10,561,393
Profit and loss account (deficit)			<u>(141,246)</u>
EQUITY SHAREHOLDERS' FUNDS	16		<u><u>11,697,022</u></u>

The accounts were approved by the board on 28 October 2005

H K Obee
Chief Executive

P W Fleming
Finance Director

The accompanying notes on pages 17 to 24 form an integral part of these financial statements

Cash Flow Statement

For the Period from 8 June 2004 to 30 June 2005

	Notes	£	£
NET CASH OUTFLOW FROM OPERATING ACTIVITIES	17		(140,147)
RETURN ON INVESTMENTS AND SERVICING OF FINANCE			
Interest received			63,539
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT			
Purchase of tangible fixed assets		(18,685)	
Exploration and evaluation expenditure		<u>(1,326,875)</u>	
			<u>(1,345,560)</u>
CASH INFLOW BEFORE USE OF LIQUID RESOURCES AND FINANCING			(1,422,168)
MANAGEMENT OF LIQUID RESOURCES			
Deposit on demand			(10,000,000)
FINANCING			
Share capital issued, net of issue costs			<u>11,838,268</u>
INCREASE IN CASH	19		<u>416,100</u>

The accompanying notes on pages 17 to 24 form an integral part of these financial statements

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005

1. Accounting Policies

Basis of preparation and going concern

The accounts have been prepared in accordance with the historical cost convention and in accordance with the applicable accounting standards and the Statement of Recommended Practice "Accounting for Oil and Gas Exploration, Development, Production and Decommissioning Activities".

The financial statements have been prepared on a going concern basis. The Company's ability to continue as a going concern is contingent upon its ability to raise sufficient funds to cover future exploration and development commitments.

Turnover

At the end of the period the Company had not commenced commercial production from its exploration sites and therefore has no turnover in the period.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at historical costs less accumulated depreciation.

Depreciation is calculated on a straight line method to write off the cost of the assets less their estimated residual values over their expected useful lives. The annual rates used are:

- Computer equipment – 33 $\frac{1}{3}$ %.

Assets are depreciated from the date of acquisition.

Exploration and evaluation expenditure

The Company has adopted the full cost accounting policy for expenditure on oil and gas projects. All costs associated with oil exploration are capitalised on a project-by-project basis, pending determination of feasibility of the project. Costs incurred include appropriate technical and administrative expenses but not general overheads. If an exploration project is successful, the related expenditures will be transferred to tangible fixed assets and amortised over the estimated life of the commercial reserves. Where a licence is relinquished, a project is abandoned, or is considered to be of no further value to the Company the related costs are written off. All capitalised costs are reviewed annually against the underlying value of oil and gas reserves, unless the expenditure relates to an area where it is too early to make a decision about the value of the assets.

Impairment tests

When there is an indication that the value of an assets may be impaired, the net amount at which the asset is recorded is assessed for recoverability against the discounted future estimated net cash flows expected to be generated from the estimated remaining commercial reserves. The assessment is made on the basis of future oil prices, exchange rate and cost levels as forecast at the balance sheet date. A provision is made by way of an additional depreciation charge, where the carrying value of the asset exceeds the discounted future net cash flows to be derived from its estimated remaining commercial reserves.

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

1. Accounting Policies continued

Leasing and hire purchase commitments

Assets obtained under hire purchase contracts and finance leases are capitalised as tangible assets and depreciated over the shorter of the lease term and their useful lives. Obligations under such agreements are included in creditors net of the finance charge allocated to future periods. The finance element of the rental payment is charged to the profit and loss account so as to produce a constant periodic rate of charge on the net obligation outstanding in each period. All other leases are regarded as operating leases and the payments made under them are charged to the profit and loss account on a straight line basis over the lease term.

Foreign currency

Foreign currency transactions are translated at the rates ruling when they occurred. Foreign currency monetary assets and liabilities are translated at the rate of exchange ruling at the balance sheet date. Any differences are taken to the profit and loss account.

Financial instruments

In relation to the disclosures made in Note 25:

- Short term debtors and creditors are not treated as financial assets or financial liabilities except for currency disclosures;
- The Company does not hold or issue derivative financial instruments for trading purposes; and
- Forward exchange contracts are used to fix the exchange rate of committed and anticipated foreign currency transactions. Gains and losses arising on such hedges are not recognised until the transaction occurs.

The Company has not made use of any derivative financial instruments in the period.

Deferred taxation

Deferred tax balances are recognised in respect of all timing differences that have originated but not reversed by the balance sheet date except that the recognition of deferred tax assets is limited to the extent that the Company anticipates making sufficient taxable profits in the future to absorb the reversal of the underlying timing differences.

Deferred tax balances are not discounted.

Liquid resources

For the purpose of the cash flow statement, liquid resources are defined as current asset investments and short term deposits.

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

2. Earnings/(Loss) per Share

The calculation of the basic earnings per share is based on the loss attributable to ordinary shareholders divided by the weighted average number of shares in issue during the period. The loss for the financial period is £141,246 and the average number of shares in issue for the year was 55,413,437.

The Company has no outstanding warrants or options at the balance sheet date and accordingly there are no potentially dilutive shares in issue at the period end.

3. Segmental Analysis

For the purpose of segmental information the operations of the Company consist of one class of business, the exploration for hydrocarbon liquids and gas.

During the period the Company's exploration and evaluation activities took place solely in the Falkland Islands. These costs are capitalised in accordance with the accounting policies as set out in note 1 above, and do not affect the operating loss of the Company. The operating loss for the period as shown in the Profit and Loss account has been incurred wholly in the United Kingdom.

Net assets as analysed as follows:

	£
United kingdom	10,363,420
Falkland Islands	<u>1,333,582</u>
	<u>11,697,022</u>

4. Operating Loss

	£
Operating loss is stated after charging:	
Depreciation of tangible assets	3,720
Auditors' remuneration	<u>12,500</u>

Fees paid to the auditors of £33,055 for services relating to the Company's admission to the Alternative investment Market of the London Stock Exchange have been set off against the share premium account.

5. Employees (Including Directors)

	£
Staff costs consist of:	
Wages and salaries	36,744
Social security costs	<u>3,216</u>
	<u>39,960</u>

The average number of employees (including Directors) during the period was 4.

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

6. Director's Emoluments

	£
Emoluments	<u>35,000</u>

The emolument relating to the highest paid director during the period was £30,000.

7. Interest Receivable

	£
Bank interest	<u>63,539</u>

8. Taxation

	£
Current tax	—
Deferred tax	—
Tax on loss on ordinary activities	<u>—</u>

At 30 June 2005, the Company has unrelieved tax losses of £114,833 that are available for offset against future taxable trading profits.

Factors affecting tax charge for period:

	£
Loss on ordinary activities before tax	<u>(141,246)</u>
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 30%	(42,374)
Effect of:	
Expenses not deductible for tax purposes	9,050
Capital allowances for the period in excess of depreciation	(1,126)
Trading losses carried forward	<u>34,450</u>
Current tax charge for period	<u>—</u>

9. Intangible Fixed Assets

	Unevaluated oil & gas properties £
Cost	
Additions during the period	<u>1,497,668</u>
At 30 June 2005	<u>1,497,668</u>

Exploration costs have been incurred wholly in the Falkland Islands.

Included within the above expenditure is an amount of £86,933 relating to costs capitalised in respect of decommissioning activities.

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

10. Tangible Fixed Assets

	Computer equipment £
Cost	
Additions during the period	18,685
At 30 June 2005	<u>18,685</u>
Depreciation	
Charge for the period	3,720
At 30 June 2005	<u>3,720</u>
Net book value	
At 30 June 2005	<u><u>14,965</u></u>

11. Debtors

	£
Other debtors	121,512
Prepayments	<u>21,278</u>
	<u><u>142,790</u></u>

12. Creditors: amounts falling due within one year

	£
Trade creditors	167,735
Other taxation and social security	10,198
Other creditors	29,830
Accruals	<u>123,783</u>
	<u><u>331,546</u></u>

13. Provision for Liabilities and Charges

	£
Demobilisation costs – charged in the period and balance carried forward	<u>42,955</u>

The Company is obliged under the terms of its licence to pay for demobilisation costs to a pre-agreed sum set out within the licence.

14. Share Capital

	£
Authorised	
750,000,000 Ordinary shares of £0.01 each	<u>7,500,000</u>
Allotted, called up and fully paid	
127,687,500 Ordinary shares of £0.01 each	<u><u>1,276,875</u></u>

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

14. Share Capital continued

The Company was incorporated with an authorised share capital of £7.5 million divided into 750 million ordinary shares of £0.01 each. On incorporation, 2 ordinary shares of £0.01 each were issued at par. Subsequently, the Company has issued the following shares:

Date of issue of shares	Number of shares issued	Shares issued		Consideration
22 June 2004	9,999,998	Ordinary shares £0.01 each	£100,000	At par
29 September 2004	53,250,000	Ordinary shares £0.01 each	£532,500	At par
11 February 2005	2,000,000	Ordinary shares £0.01 each	£20,000	At par
5 May 2005	12,437,500	Ordinary shares £0.01 each	£1,990,000	(£0.16 per share)
18 May 2005	50,000,000	Ordinary shares £0.01 each	£10,000,000	(£0.20 per share)

15. Reserves

	Profit and loss account £	Share premium account £
Loss for the period	(141,246)	—
Premium on issue of ordinary shares	—	11,365,625
Share issue costs	—	(804,232)
At 30 June 2005	<u>(141,246)</u>	<u>10,561,393</u>

16. Reconciliation of Movements in Shareholders' Funds

Loss for the period	(141,246)
New share capital issued	12,642,500
Share issue costs	(804,232)
Net addition to shareholders' funds	<u>11,697,022</u>
Closing shareholders' funds	<u>11,697,022</u>

17. Net Cash Outflow from Operating Activities

Operating loss	(204,785)
Depreciation	3,720
Increase in debtors	(142,790)
Increase in creditors	<u>203,708</u>
Net cash outflow from operating activities	<u>(140,147)</u>

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

18. Analysis of Changes in Net Funds

	At 8 June 2004	Cash flows	At 30 June 2005
	£	£	£
Cash at bank	—	416,100	416,100
	—	416,100	416,100
Short term deposit	—	10,000,000	10,000,000
Total	—	10,416,100	10,416,100

19. Reconciliation of Net Cash Flow to Movement in Net Funds

	At 30 June 2005
	£
Increase in cash	416,100
Increase in short term deposits	10,000,000
Net funds are 30 June 2005	10,416,100

20. Related Party Disclosures

There are no transactions with Directors or other related parties disclosable under FRS 8.

21. Leasing Commitments

At 30 June 2005 the Company had commitments under operating leases expiring as follows:

	Land and buildings
	£
In one year or less	21,810

22. Exploration Expenditure Commitments

Under production licences acquired by the Company, annual licence payments of £33,256 are payable for the next two years.

At 30 June 2005, the Company is obliged to reprocess seismic data, construct structural modeling, to prepare a regional interpretation of play fairways and provide analysis to the Falkland Island Government. The directors estimate this cost to be £55,426.

23. Contingent Liabilities

The Company had no contingent liabilities as at 30 June 2005.

24. Controlling Parties

So far as the Directors are not aware there are not any persons who, directly or indirectly could exercise control over the Company.

Notes Forming Part of the Financial Statements for the Period Ended 30 June 2005 continued

25. Financial Instruments

This note provides the narrative and numerical disclosures required by FRS 13 "Derivatives and Other Financial Instruments: Disclosures". As permitted by FRS 13, short term debtors and creditors have been excluded from the disclosures, other than where they relate to currency disclosures.

The main risks arising from the Company's operations are interest rate risk and foreign currency translation risk. The Company monitors risk on a regular basis and takes appropriate measures to ensure risks are managed in a controlled manner.

a) Interest rate risk

The Company's financial assets and liabilities accrue interest at prevailing floating rates in the United Kingdom or at pre-arranged fixed rates, as described further below. The Company does not currently use derivative instruments to manage its interest rate risk.

b) Foreign currency translation risk

The functional currency of the oil and gas exploration and evaluation activities of the Company is USD\$, services and treasury functions is £ sterling. Balances are held in £ sterling and USD\$ are purchased when required and used to meet exploration and evaluation needs. At the balance sheet date there were monetary liabilities of £180,753 denominated in USD\$.

Subsequent to the Balance Sheet date the Company entered into a forward exchange contract to sell £3.75 million for US\$6.57 million as a means of managing its foreign currency translation and transaction risk.

Interest rate risk profile of financial assets:

	£
Pounds sterling	10,416,100
At 30 June 2005	<u>10,416,100</u>

At 30 June 2005 the Company held cash at bank and in demand deposits under its control of £10,416,100, which forms the majority of its working capital. A balance of £416,100 relates to deposits placed with banking institutions that are available on demand which carry interest at prevailing United Kingdom deposit floating rates. In addition, the Company has restricted deposits of £10,000,000 with weighted average fixed interest rate of 4.743% for three months.

Fair values

The fair values of the Company's financial assets and liabilities at 30 June 2005 are materially equivalent to their carrying value as disclosed in the Balance Sheet and related notes.

Corporate Directory

Company Number	5147938
Directors	David Harry Williamson Dobson (Non-Executive Chairman) Howard Kevin Obee (Chief Executive) Peter William Fleming (Finance Director) Christopher Nigel Hurst-Brown (Non – Executive) Stephen James Douglas Posford (Non – Executive)
Company Secretary	William John Walton Slack
Registered Office	3 Copthall Avenue London EC2R 7BH
Nominated Advisor	Insinger de Beaufort 131 Finsbury Pavement London EC2A 1NT
Solicitors to the Company as to English Law	Denton Wilde Sapte 1 Fleet Place London EC4M 7WS
Solicitors to the Company as to Falkland Islands Law	Ledingham Chalmers 56 John Street Stanley Falkland Islands
Stockbroker	Ocean Equities Limited 3 Copthall Avenue London EC2R 7BH
Registrars	Capita Registrars Northern House Woodsome Park Fenay Bridge Huddersfield HD8 0LA
Bankers	Lloyds TSB Bank plc 19 – 21 The Quadrant Richmond Surrey PW9 1BP
Independent auditors	BDO Stoy Hayward LLP 8 Baker Street London W1U 3LL