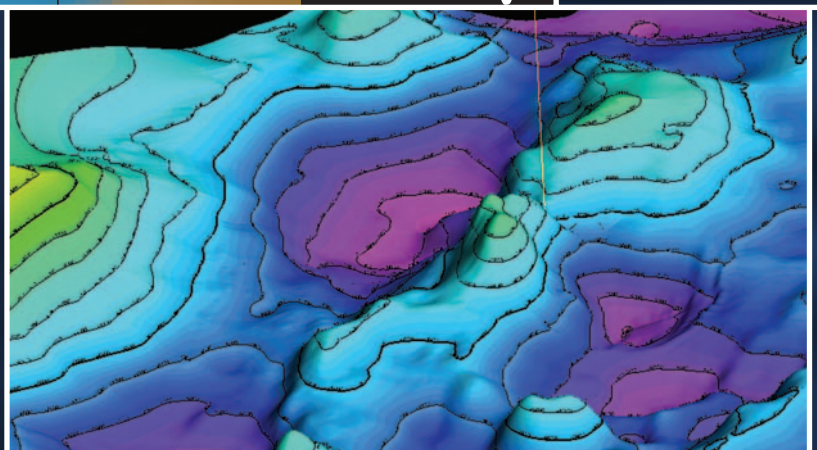
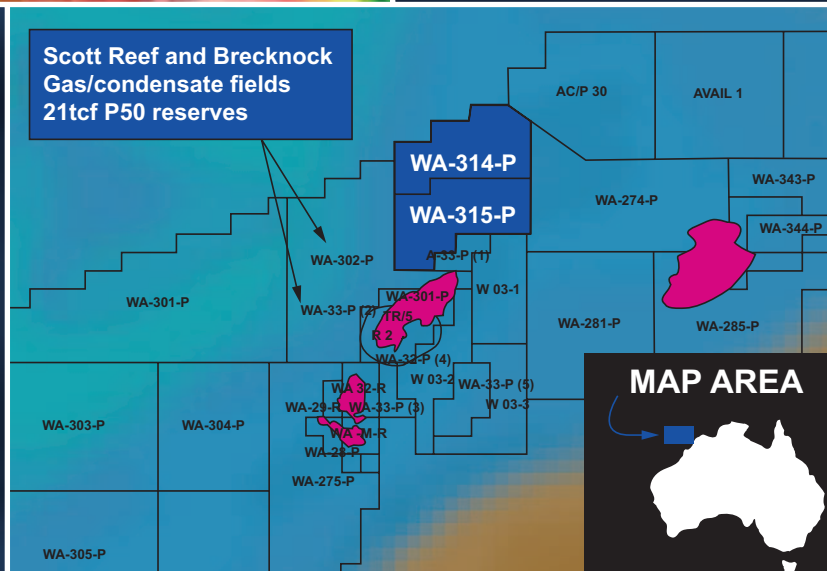
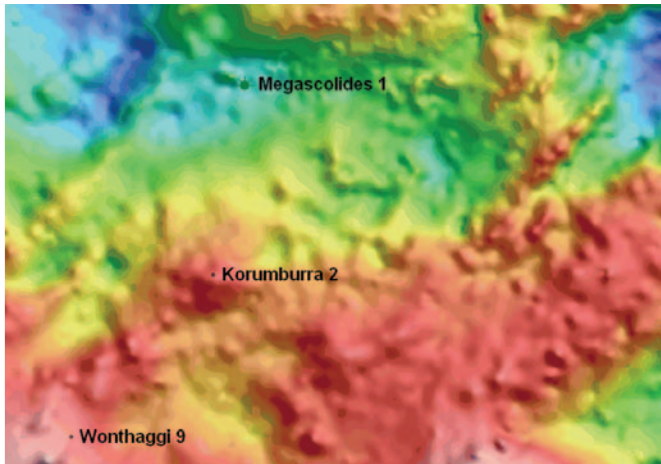




KARON
Gas Australia Ltd



Karoon Gas Australia Ltd
ABN 53 107 001 338
and Controlled Entities

FINANCIAL REPORT 2005

Karoon Gas Australia Ltd

ABN 53 107 001 338

and Controlled Entities

Financial Report



KAROON
Gas Australia Ltd

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2005 Annual Report

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- **Northern Browse Basin**

Financial Report

Summary of Activities

During this last financial year Karoon Gas has signed off on some high potential agreements and has carried out or participated in geological and geophysical work in all its acreage to progress exploration and development.

HIGHLIGHTS

- Farmed into WA-314-P & WA-315-P permits in the Northern Browse Basin approximately 300 km offshore from the Western Australian coast.
- Negotiated a farm-out (WA-314-P & WA-315-P) to BG International Ltd ("BG"), whereby BG earns a 60 percent interest in the permits by funding 90 percent of the guaranteed work program. Karoon will retain a 40 percent interest by funding 10 percent of the guaranteed work program, plus 40 percent of the cost of the extra 400 square kilometres of the seismic program.
- Raised A\$12.8 million in capital to fund its ongoing exploration activities. This raising included a Share Purchase Plan for Karoon Gas' Shareholders and a placement to sophisticated and institutional investors. The capital raising has also enabled the Company to broaden its shareholder base with the introduction of new institutions to its share register. Funds raised are largely being used for our share of the WA-314-P and WA-315-P work program with BG, as well as further exploration of the Gippsland Basin Acreage.
- With BG as operator, Karoon completed a high-resolution aeromagnetic survey in June 2005 over the entire permit areas of WA-314-P & WA-315-P. This data will help in identifying the areas for the 800-1200 square kilometre 3D seismic acquisition scheduled for commencement in October 2005. This is up to approximately 400 square kilometres over and above the 800 square kilometres required for the government guaranteed work program. 3D seismic will be used to further define prospects and pinpoint the best positions for drilling.
- Drilling of the Megascalides - 1 well in PEP 162 and EL 4537 in West Gippsland was completed in December 2004. Results were favourable and support further exploration to define Coal Bed Methane (CBM) and oil prospects. A 290-kilometre 2D seismic acquisition program is planned for the third/fourth quarters of 2005. Subject to seismic results, an exploration drilling program is planned for mid-2006.

Chairman's Report

Dear Fellow Shareholders

On behalf of the board of Directors, I take great pleasure in presenting to you the annual report for the year ending June 2005 from Karoon Gas Australia Ltd ("Karoon Gas").

This initial year has been very exciting for Karoon Gas. We have seen a remarkable upward trend in our stock price of approximately 800 percent, driven largely by our acquisition of high-quality exploration acreage in Western Australia. The opportunity to acquire the WA-314-P and WA-15-P permits in the Northern Browse Basin and the farmout contract with BG International Ltd ("BG"), has attracted much national and overseas attention. Karoon and BG, will be moving into seismic acquisition in late 2005 and a drilling program in mid-2006. Karoon Gas' Gippsland Permits have also shown promise having discovered gas-bearing coals CBM and oil.

Of great excitement at present is the exploration program beginning in permits WA-314-P and WA-315-P in the Northern Browse Basin. BG, Karoon Gas' Joint Venture Partner, began a permit-wide Aeromagnetic Survey in June 2005 to help position the area to be covered by the 3D seismic survey. The 3D seismic survey is scheduled to begin in the third/fourth quarter of 2005 in order to determine the best drill targets. We believe this area has the potential to contain up to 30 Trillion Cubic Feet (TCF) of gas and 300 million barrels (mmbbl) of condensate in seven large prospects. The giant gas fields of Brecknock and Scott Reef are located just south of WA-315-P and these locations have been proven to contain large gas and condensate reserves.

Karoon Gas has drilled for oil and gas in PEP 162 and EL 4537 in the Western Gippsland Basin, with the first drilling program being completed on 17 December 2004. Results of that drilling program were favourable, showing presence of gas-bearing black coals and 3 to 5 metres of net porous, permeable oil sands with good fluorescence. Data collected provides a sound basis for further exploration to determine the extent of the coals and define oil zone structural closures. Karoon is in the final stages of planning a 290-kilometre 2D seismic program to be acquired in October 2005 to follow up on the CBM and oil play potential in these permits.

The board is proud of our accomplishments so far in the young life of Karoon and look forward to a productive 2005-2006. This is a year that will see the unfolding of projects which will hopefully lead to increased growth and development of both the company and its shareholder value.

On behalf of the board, I would like to thank the shareholders for their support and take great pride in presenting this annual report.

Robert Hosking
Executive Chairman

Summary of Assets

Browse Basin Assets

Pursuant to the Liberty Farm-in Agreement, Karoon farmed into the Browse Basin Permits held by Liberty Petroleum in exchange for a royalty. The permits are 290 kilometres offshore, northwest of Broome and Derby in Western Australia. Karoon Gas will acquire a 100 percent interest in WA-314-P and WA-315-P by fulfilling the Year 2 minimum guaranteed work program of a 400-square kilometre seismic survey in each permit, which is expected to be completed in the fourth quarter of 2005.

Karoon has subsequently farmed out 60 percent of its interest in the Browse Basin Permits to BG International Ltd, a major international oil and gas company, that has agreed to fund 90 percent of the guaranteed minimum Year 2 and Year 3 work program commitments in accordance with the terms of the BG Farmout Agreement. Both Karoon and BG have an option to withdraw from the permits prior to undertaking the Year 2 3D seismic and Year 3 drilling commitments.

The directors believe that these permits offer potential for gas and condensate, sufficient to support a Liquefied Natural Gas (LNG) development that requires an approximate minimum economic quantity of 4 TCF of gas. Karoon has mapped seven leads, with risked reserves potential totals estimated to be approximately 30 TCF with 600 million barrels of condensate.

An independent report on the gas and condensate potential of the Browse Basin acreage and the oil and CBM potential of the Karoon Leases has been prepared by a geological consultant engaged by the Company and was presented in the May 2005 Prospectus.

Gippsland Basin Assets

Karoon Gas (through its 100 percent-owned subsidiary Karoon Gas Pty Ltd) has a 100 percent registered interest in PEP162 and EL4537, within the Western on-shore Gippsland Basin of Victoria. The area of PEP162 is extensive, covering some 2950 square kilometres and overlays EL4537, which covers 612 square kilometres. The permits are 100 kilometres east of Melbourne, and are close to existing oil and gas pipelines and infrastructure moving oil and gas from Bass Strait to the Melbourne area.

Karoon Gas Pty Ltd has previously conducted the exploration activities on its own behalf with that work showing the potential for a large CBM resource. After the drilling of Megascolides-1, it has been determined that there are large sections of interbedded black coal sequences present in the Narracan Trough. Based on a comparison with key criteria from producing CBM fields the conditions appear favorable for the development of a potential CBM resource, although not at the Megascolides-1 site.

On December 17, Megascolides-1 was drilled on the Northern Terrace of the Narracan Trough. This was the first deep well to be drilled in the Narracan Trough. Results were favorable with confirmation of the presence of gas-bearing black coals. A total of 15 metres of black coal, occurring as interbeds less than 1-metre thick, with a gas content of 100 standard cubic feet (scf) per ton and approximate gas saturation of 30 percent was penetrated. This well also identified a potential oil play, with the presence of a 3 to 5-metre section of net porous sands showing good fluorescence and high mud gas readings. Analysis of the extracted oil showed that a waxy crude oil was present. Petrophysical interpretation indicates up to 60 percent saturation is present in the reservoir with a porosity range between 12 percent and 15 percent.

With the presence of gas-bearing black coal across the Narracan Trough and the discovery of a potential oil play, further follow-up work is planned for the permits. Exploration work will include a 290-kilometre seismic program followed by one or two exploration wells in the first or second quarter of 2006.

2005 FINANCIAL REPORT



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DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2005

Directors' Report

The Directors present their report together with the financial report of Karoon Gas Australia Limited ("the Company") for the year ended 30 June 2005 and the auditors' report thereon.

Directors

The Directors of the Company at any time during or since the end of the financial year are:

Mr Robert Michael Hosking

Managing Director & Chairman

Appointed 11 November 2003

Robert is the founding Director of Karoon Gas and has more than 30 years of commercial experience in the administration of several companies. Robert has been involved in the oil and gas industry for nine years and was the founding Director/Shareholder of Nexus Energy. Robert was responsible for procuring PEP 162 and EL 4537 and managing all of the required work programs in relation to those permits, including raising funds and overseeing the geophysical and geological contractors.

Robert also has a background of more than 15 years' commercial experience in the steel industry. He jointly owned and managed businesses involved in the transglobal sourcing, shipping and distribution of steel-related products, with particular expertise gained in Europe and the Asia/Pacific Rim.

Member of the audit committee.

Mr Geoff Atkins

RMIT Dip. Civ Eng.

Non-Executive Director

Appointed 22 February 2005

Geoff has over 34 years' experience in investigation, planning, design, documentation and project management of numerous significant port, harbour and maritime projects, including container terminals, LNG jetties, cement, coal, bauxite, iron ore and other bulk terminals and naval bases. Geoff has gained substantial overseas experience completing marine projects in Indonesia, Malaysia, Thailand, Vietnam, Sri Lanka, India, South Africa, Namibia, New Zealand and the United Kingdom. LNG, oil, gas, bulk ports and other large maritime infrastructure projects have included the design of Woodside's LNG Jetty, tender design of Darwin LNG Jetty and investigations of proposed LNG marine terminals in Taiwan, Iran and Israel for BHP Petroleum and the West Kingfish and Cobia oil drilling platforms for ESSO/BHP in Bass Strait.

Mr Mark Alexander Smith

Dip. App. Geol, Bsc. (Geology)

Executive Director and Exploration manager

Appointed 1 December 2003.

Mark is a geologist with over 25 years of continuous experience as a geologist and exploration manager in petroleum exploration and development in Australia, Southeast Asia and North America. The bulk of this experience was gained while with BHP Petroleum. Mark has been directly involved with seven economic oil and gas discoveries.

Mark's geoscience skills cover regional basin and tectonic studies, acreage evaluations and gazettal, farm-ins/farm-outs, petroleum systems fairway assessments, prospect evaluations, risking and volumetric and fault seal prediction. Mark also has project and operations management experience in well site operations and management of onshore and offshore drilling operations.

Mr Stephen Power

B. Juris LLB

Non-Executive Director

Appointed 28 June 2005

Stephen Power is a commercial lawyer who has spent approximately 20 years providing advice to participants in the resources industry in Australia and overseas. Stephen is a partner in a boutique law firm that provides commercial advice to its predominantly listed client base. Stephen has extensive experience in all facets of commercial and resources law, including the oil and gas sector, both in an Australian and International context. Stephen regularly advises on farm-in arrangements, joint ventures, production agreements and other facets of resources-related commercial transactions. In addition to Stephen's experience in the resources area, Stephen has a significant practice advising on capital raisings, including the drafting of prospectuses, underwritings and related work, listing advice and the planning and implementation of mergers and acquisitions.

Stephen brings a sound commercial background gained through his extensive legal experience to the Board, which your Directors believe will be of benefit to the Board and the Company.

Mr Edward Munks

Non-Executive Director

Resigned 25 February 2005

Company Secretary

The following person held the position of company secretary at the end of the financial year: Hector Peeters, PNA
Mr Peeters was appointed company secretary in 2005

DIRECTORS REPORT continued

FOR THE YEAR ENDED 30 JUNE 2005

Directors' meetings

The number of Directors' meetings (including meetings of committees of Directors) and number of meetings attended by each of the Directors of the Company during the financial year were:

Director	Board Meetings		Audit Committee Meetings	
	A	B	A	B
Mr Robert Hosking	4	4	2	2
Mr Mark Smith	4	4	-	-
Mr Geoff Atkins	3	3	1	1
Mr Edward Munks	1	1	-	-
Mr Stephen Power	-	-	-	-

A – Number of meetings held during the time the Director held office during the year.

B – Number of meetings attended.

Principal activities

The principal activities of the Company during the course of the financial year were the investment in energy-related projects in the Western Gippsland Basin, a sedimentary basin in Victoria's south-east. Karoon has also acquired permits WA-314-P and WA-315-P in the Northern Browse Basin. These permits have been 60 percent farmed-out to BG International Ltd.

There were no other significant changes in the nature of the activities of the Company during the year other than disclosed in this annual report.

Review of operations

During the year, Karoon successfully drilled the Megascolides - 1 well and conducted geotechnical analysis of the company's exploration permits in the Western Gippsland Basin. The company's exploration permits in Victoria are relatively under-explored by industry standards and are located in an area close to major infrastructure and markets.

Karoon Gas acquired the right to farm-in at 100 percent, and subsequently farmed-out, a 60 percent interest in two large (approximately 2000 square kilometres each) Browse Basin Permits, WA-314-P and WA-315-P. Karoon Gas, with its joint venture partner BG International, has completed permit-wide aeromagnetic surveys over the two permits, to be followed by an 800-1200 square kilometre 3D seismic survey. All surveys are directed at assessing the prospectivity of identified leads. Drilling is expected to commence in the most prospective prospects in 2006.

Operating results

The consolidated loss of the consolidated entity for the year ended 30 June 2005 was \$626,450 (2004 : Loss \$178,301)

Significant changes in state of affairs

In September 2004 pursuant to the Liberty Farm-in Agreement, the Company acquired the rights from Liberty Petroleum to acquire the permits WA-314-P and WA-315-P by fulfilling the Year 2 minimum guaranteed work program of a 400 square kilometre seismic survey in each permit.

In December 2004 the company successfully drilled the Megascolides -1 well, that encountered the presence of gas-bearing black coals and 3-5 metres of deeper net porous, permeable oil sands.

In April 2004 pursuant to the BG farm-out Agreement, the Company farmed-out a 60 percent interest in its rights in the permits WA-314-P and WA-315-P.

During the year the Company raised \$13,104,889 in working capital, detailed in the following table:

Placement in June	10,000,000 shares at \$1.20
Share Purchase Plan in June	673,644 shares at \$1.20
Exercise of options	1,482,550 shares at \$0.20

Dividends

No dividend has been paid or declared by the Company to members since the end of the previous financial year.

Issue of options to employees

At 30 June 2005, there were 415,000 options outstanding as part of the Executive and Employee Options scheme. All options that are granted under the Employee Share Option scheme expire on their expiry date. Options may be exercised at any time by employees. These options do not entitle the holder to participate in any share issue of the company or any other body corporate. During the year the following options were issued to Employees or their related parties:

415,000 Issued on 25 February 2005 to the employees of the Company with an exercise price of \$1.25 each to acquire one ordinary fully paid share in the Company; expiry date 30 June 2006.

During the year no options were issued to Directors or their related parties, however, on 24 June the company announced that subject to the approval of shareholders at the Annual General Meeting, 4,500,000 Executive Options are to be issued to the Executive Directors. These will be issued in three tranches: 1,500,000 options exercisable at \$1.75, 1,500,000 options exercisable at \$2.00, 1,500,000 options exercisable at \$2.35. All of these options expire September 30 2008.

On 25 February the company announced that subject to the approval of shareholders at the Annual General Meeting, 500,000 Options are to be issued to Geoff Atkins. These options will have an exercise price of \$1.35 and will also be subject to a voluntary escrow period ending 25 February 2006 and will expire on the 30 June 2007.

On 28 June the company announced that subject to the approval of shareholders at the Annual General Meeting, 500,000 Options are to be issued to Stephen Power. These options will have an exercise price of \$1.65 and will expire on the 31 October 2007.

Environmental regulation

The consolidated entity is subject to a range of environmental laws and regulations with the most signified being:

- The Petroleum Act 1998 (Vic) and the Petroleum Regulations 2000 (Vic);
- Environment Protection and Biodiversity Conservation Act 1999
- Mineral Resources Development Act 1990 (Vic)
- The Aboriginal and Torres Strait Islander Heritage and Protection Act 1994 (Cth)
- The Archaeological and Aboriginal relics Preservation Act 1972 (Vic)

The Board believes that the Company has adequate systems in place for managing its environmental requirements and is not aware of any breach of those environmental requirements as they apply to the Company. No circumstances arose during the year that resulted in an incident to be reported under environmental legislation.

Events subsequent to balance date

Subsequent to the end of the financial year the economic entity completed an aeromagnetic survey over the permits WA-314-P and WA-315-P and is in the process of contracting through BG, the operator, a seismic company to carry out an 800-1200 kilometre 3D seismic survey over the above two permits.

Likely developments

The Company will continue to pursue its policy of investing in the energy sector during the next financial year. The consolidated entity's long-term objective is to achieve organic growth from exploration and development opportunities. The Company will be pursuing its strategy to gain access to quality assets with significant equity levels. Further information about likely developments in the operations of the Company and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Company.

Remuneration Report

The Board regularly reviews remuneration of its senior executives and Directors. This also includes responsibility for the Employee Share Option scheme. The executive remuneration structure is based on a number of factors, including length of service, particular experience of the individual concerned and overall performance of the company. It also involves a balance between fixed and incentive pay, reflecting short- and long-term performance objectives appropriate to the Company's circumstances and objectives. A proportion of executive remuneration is structured in a manner designed to link rewards to corporate and individual performance. This is done by considering the following remuneration components:

- Fixed remuneration;
- Performance-based remuneration;
- Equity-based remuneration within thresholds set by the Board.

DIRECTORS REPORT continued

FOR THE YEAR ENDED 30 JUNE 2005

The contracts for service between the company and specified executives are on a continuing basis, the terms of which are not expected to change in the immediate future. Upon retirement specified executives are paid employee benefit entitlements accrued to date of retirement. There has been no alteration to the terms of the bonuses paid since grant date.

Executive remuneration levels are competitively set with regard to the level of seniority, responsibility and effectiveness in carrying out these duties. Directors' remuneration levels are competitively set to attract the most qualified and experienced Directors.

Options are also issued under the Executive and Employee Share Option scheme. Non-executive Directors do not receive any performance-related remuneration. Options are valued under the Black and Scholes Methodology but have not been expensed during the period.

The Directors and executives receive a superannuation guarantee contribution required by the government, which is currently 9 percent, and do not receive any other retirement benefits. Some individuals, however, have chosen to sacrifice part of their salary to increase payments towards superannuation.

Details of Remuneration for the Year Ended 30 June 2005

The remuneration for each director and each of the three executive officers of the consolidated entity receiving the highest remuneration during the year was as follows:

	Primary		Post Employment		Equity	Other	Total
	Salary, Fees & Commissions	Superannuation Contributions	Cash Bonus	Superannuation	Options		
	\$	\$	\$	\$	\$	\$	\$
2005							
Mr Robert Hosking	260,000	-	-	-	-	-	260,000
Mr Mark Smith	171,179	-	-	-	-	-	171,179
Mr Geoff Atkins	10,417	938	-	-	-	-	11,355
Mr Stephen Power	-	-	-	-	-	-	-
	462,429	2,813	-	-	-	-	465,242
2004							
Mr Robert Hosking	91,000	-	-	-	-	-	91,000
Mr Mark Smith	29,596	-	-	-	-	-	29,596
Mr Edward Munks	2,083	-	-	-	-	-	2,083
Mrs Patricia Hosking	-	-	-	-	-	-	-
	122,679	-	-	-	-	-	122,679

DIRECTORS REPORT continued

FOR THE YEAR ENDED 30 JUNE 2005

Options issued as Part of Remuneration for the Year Ended 30 June 2005

Options are issued to executives as part of their remuneration to increase goal congruence between executives and shareholders.

	Granted number	Options granted as part of remuneration \$	Total remuneration represented by Options %	Options Exercised \$	Options Lapsed \$	Total \$
Directors						
Mr Robert Hosking	-	-	-	-	-	-
Mr Mark Smith	-	-	-	-	-	-
	-	-	-	-	-	-

Options

During or since the end of the financial year, the Company did not grant any options over unissued ordinary shares to any of the Directors, however, on 24 June the company announced that subject to the approval of shareholders at the Annual General Meeting, 4,500,000 Executive options are to be issued to the Executive Directors. These will be issued in three tranches: 1,500,000 options exercisable at \$1.75, 1,500,000 options exercisable at \$2.00, 1,500,000 options exercisable at \$2.35. All of these options expire September 30 2008.

On 25 February the company announced that subject to the approval of shareholders at the Annual General Meeting, 500,000 Options are to be issued to Geoff Atkins. These options will have an exercise price of \$1.35 and will also be subject to a voluntary escrow period, ending 25 February 2006, and will expire on the 30 June 2007.

On 28 June the company announced that subject to the approval of shareholders at the Annual General Meeting, 500,000 Options are to be issued to Stephen Power. These options will have an exercise price of \$1.65 and will expire on the 31 October 2007.

Directors' interests

The relevant interest of each Director in the shares, debentures, interests in registered schemes and rights or options over such instruments issued by the Company, as notified by the Directors to the Australian Stock Exchange in accordance with S205G(1) of the Corporations Act, at the date of this report is as follows:

	Ordinary Fully Paid Shares	Options
Mr Robert Hosking	8,208,335	4,603,752
Mr Mark Smith	1,210,000	1,105,000
Mr Geoff Atkins	152,500	75,000
Mr Stephen Power	10,000	5,000

Corporate governance

In recognising the need for the highest standards of corporate governance and accountability, the Directors of the parent entity support and have adhered to the principles of corporate governance. The consolidated entity's corporate governance statement is on pages 42 - 46 of this annual report.

Auditors

Mitchell Wilson & Partners continue in accordance with Section 327 of the Corporations Act.

Auditor's Independence Declaration

The lead auditor's independence declaration for the year ended 30 June 2005 has been received and can be found on page 41 of the annual report.

Dated Melbourne this 26th day of August of 2005.

Signed in accordance with a resolution of the Directors:



Robert Hosking
Executive Chairman

DIRECTORS REPORT continued

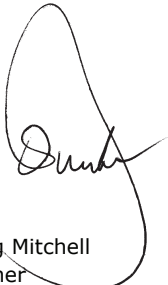
FOR THE YEAR ENDED 30 JUNE 2005

Auditor's Independence Declaration under Section 307C of the Corporations Act 2001 to the directors of Karoon Gas Australia Limited

I declare that, to the best of my knowledge and belief during the year ended 30 June 2005 there have been:

- i. No contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit, and
- ii. No contraventions of any applicable code of professional conduct in relation to the audit.

MITCHELL WILSON
Chartered Accountants

A handwritten signature in black ink, appearing to read 'Doug Mitchell', is written over a large, stylized, circular scribble.

Doug Mitchell
Partner
26th Day of August 2005

2005 FINANCIAL STATEMENTS



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STATEMENT OF FINANCIAL PERFORMANCE

FOR THE YEAR ENDED 30 JUNE 2005

	Note	Consolidated Entity		Parent Entity	
		2005	2004	2005	2004
		\$	\$	\$	\$
Revenues from ordinary activities	2	157,976	34,015	157,056	34,015
Accounting & Taxation Fees		(19,927)	(8,070)	(19,927)	(8,070)
Amortisation of goodwill on acquisition of Karoon Gas Pty Ltd		(17,126)	(10,031)	-	-
Audit fees		(15,000)	(7,000)	(12,000)	(5,000)
Computer Support		(8,994)	-	(8,994)	-
Consulting fees		(191,696)	(114,789)	(191,696)	(114,789)
Corporate promotion and annual report		(15,285)	(20,000)	(15,285)	(20,000)
Depreciation of plant and equipment		(48,099)	(2,156)	(48,099)	(2,156)
Directors' benefits		(30,479)	(2,083)	(30,479)	(2,083)
Legal fees		(109,468)	(1,650)	(109,468)	(1,650)
Operating lease rental expense		(24,960)	(8,320)	(24,960)	(8,320)
Other expenses from ordinary activities		(70,945)	(12,574)	(69,499)	(116)
Property costs		(51,206)	(8,435)	(51,106)	(8,361)
Salaries & Superannuation		(50,215)	(1,471)	(50,215)	(1,471)
Share registry and listing fees		(59,797)	(6,859)	(59,797)	(7,772)
Travel and accommodation		(71,229)	(8,878)	(71,229)	(6,210)
Loss from ordinary activities before income tax expense		(626,450)	(178,301)	(605,698)	(151,983)
Income tax (expense)/benefit relating to ordinary activities			-		-
Net loss from ordinary activities after income tax					
Expense attributable to members of the parent entity		(626,450)	(178,301)	(605,698)	(151,983)
Total changes in equity other than those resulting from transactions with owners as owners		(626,450)	(178,301)	(605,698)	(151,983)
Basic earnings per share		(\$0.0145)	(\$0.016)		
Diluted earning per share		(\$0.0095)	(\$0.011)		

The statement of financial performance is to be read in conjunction with the notes to the financial statements set out on pages 19 to 39

STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2005

	Note	Consolidated Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
Current assets					
Cash assets		12,796,605	4,225,633	12,757,094	4,208,593
Receivables	8	131,895	66,046	96,045	46,481
Inventory		195,402	195,402	-	-
Total current assets		13,123,902	4,487,081	12,853,139	4,255,073
Non-current assets					
Other financial assets	9	2,267	1,212	152,267	151,212
Receivables	8	-	-	3,204,948	241,455
Property, plant and equipment	10	117,763	46,795	117,763	46,795
Intangible assets	11	144,794	161,920	-	-
Other assets	12	2,984,934	71,394	-	-
Total non-current assets		3,249,758	281,321	3,474,978	439,462
Total assets		16,373,660	4,768,402	16,328,117	4,694,535
Current liabilities					
Payables	13	(154,733)	(189,764)	(94,949)	(119,787)
Provisions	14	(2,521)	-	-	-
Total current liabilities		(157,254)	(189,764)	(94,949)	(119,787)
Total liabilities		(157,254)	(189,764)	(94,949)	(119,787)
Net assets		16,216,406	4,578,638	16,233,168	4,574,748
Equity					
Contributed equity	15	16,990,949	4,726,731	16,990,849	4,726,731
Accumulated losses	16	(774,543)	(148,092)	(757,681)	(151,983)
Total equity		16,216,406	4,578,638	16,233,168	4,574,748

The statement of financial performance is to be read in conjunction with the notes to the financial statements set out on pages 19 to 39

STATEMENT OF CASH FLOW
 FOR THE YEAR ENDED 30 JUNE 2005

	Note	Consolidated Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
Cash flows from operating activities					
Receipt from Customers		443,780	12,865	147,253	5,156
Payments to suppliers		(1,149,296)	(144,128)	(876,417)	(116,904)
Interest received		157,976	34,015	157,056	34,015
Net cash flows used in operating activities	19	(547,540)	(97,248)	(572,108)	(77,733)
Cash flows from investing activities					
Purchase of property, plant and equipment		(119,067)	(48,951)	(119,067)	(48,951)
Purchase of investments		(40,437)	-	(1,055)	-
Payments for exploration and development expenditure		(2,986,202)	(204,899)	(59,894)	-
Net cash flows used in investing activities		(3,145,706)	(253,850)	(180,016)	(48,951)
Cash flows from financing activities					
Proceeds from issue of ordinary shares		12,264,218	4,576,731	12,264,118	4,576,731
Repayment of loans to parent entity		-	-	(2,963,493)	(241,455)
Net cash flows from financing activities		12,264,218	4,576,731	9,300,625	4,335,276
Net decrease in cash held		8,570,972	4,225,633	8,548,501	4,208,592
Cash at the beginning of the year		4,225,633	-	4,208,592	-
Cash at the end of the year		12,796,605	4,225,633	12,757,094	4,208,592

The statement of financial performance is to be read in conjunction with the notes to the financial statements set out on pages 19 to 39

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2005

1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The financial report is a general purpose financial report that has been prepared in accordance with Accounting Standards, Urgent Issues Group Consensus Views, other authoritative pronouncements of the Australian Accounting Standards Board and the Corporations Act 2001.

The financial report covers the consolidated entity of Karoon Gas Australia Limited and controlled entities, and Karoon Gas Australia Limited as an individual parent entity. Karoon Gas Australia Limited is a listed public company, incorporated and domiciled in Australia.

The financial report has been prepared on an accruals basis and is based on historical costs and does not take into account changing money values or, except where stated, current valuations of non-current assets. Cost is based on the fair values of the consideration given in exchange for assets.

The following is a summary of the material accounting policies adopted by the consolidated entity in the preparation of the financial report. The accounting policies have been consistently applied, unless otherwise stated.

a) Principles of consolidation

The consolidated accounts of the consolidated entity comprise the accounts of the parent entity, Karoon Gas Australia Limited and its controlled entity Karoon Gas Pty Ltd. Information on the controlled entity is contained in Note 23. All intercompany balances and transactions between the parent entity and controlled entity have been eliminated.

Where control of an entity is obtained during a financial year, its results are included in the consolidated statement of financial performance from the date on which control commences. Where control of an entity ceases during a financial year its results are included for that part of the year during which control existed.

Investments in joint ventures are accounted for as set out in note 1(r).

b) Revenue recognition

Revenues are recognised at fair value of the consideration received net of the amount of goods and services tax. Exchanges of goods or services of the same nature and value without any cash consideration are not recognised as revenues.

Rendering of services

Revenue from rendering services is recognized in the period in which the service is provided, having regard to the stage of completion of the contract.

Interest revenue

Interest revenue is recognised as it accrues.

c) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax ("GST"), except where the amount of GST incurred is not recoverable from the Australian Tax Office ("ATO"). In these circumstances the GST is recognized as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

d) Income tax

The consolidated entity adopts the income statement liability method of tax effect accounting.

Income tax expense is calculated on operating profit adjusted for permanent differences between taxable and accounting income. The tax effect of timing differences, which arise from items being brought to account in different periods for income tax and accounting purposes, is carried forward in the statement of financial position as a future income tax benefit or a provision for deferred income tax. Future income tax benefits are not brought to account unless realization of the asset is assured beyond reasonable doubt. Future income tax benefits relating to tax losses are only brought to account when their realization is virtually certain. The tax effects of capital losses are not recorded unless realisation is virtually certain.

The amount of benefit brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income tax legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

NOTES TO THE FINANCIAL STATEMENTS continued

FOR THE YEAR ENDED 30 JUNE 2005

d) Income tax (continued)

Karoo Gas Australia Limited and its wholly-owned Australian subsidiaries have formed an income tax consolidated group under the Tax Consolidation Regime from 1 July 2004. Karoo Gas Australia Limited is responsible for recognising the current and deferred tax assets and liabilities for the tax consolidated group. The tax consolidated group has entered a tax sharing agreement whereby each company in the group contributes to the income tax payable in proportion to their contribution to the net profit before tax of the tax consolidated group.

e) Acquisition of assets

All assets acquired including property, plant and equipment and intangibles other than goodwill are initially recorded at their cost of acquisition at the date of acquisition, being fair value of the consideration provided plus incidental costs directly attributable to the acquisition.

Expenditure (including that on internally generated assets other than research and development costs) is only recognised as an asset when the entity controls future economic benefits as a result of the costs incurred, it is probable that those future economic benefits will eventuate, and the costs can be measured reliably. Costs attributable to feasibility and alternative approach assessments are expensed as incurred.

f) Non-current assets

The carrying amounts of non-current assets are reviewed to determine whether they are in excess of their recoverable amount at balance date. If the carrying amount of a non-current asset exceeds its recoverable amount, the asset is written down to the lower amount.

g) Receivables

Trade debtors

Trade debtors to be settled within 45 days are carried at amounts due. The collectibility of debts is assessed at balance date and specific provision is made for any doubtful accounts.

h) Inventories

Inventories are carried at the lower of cost and net realisable value.

i) Investments

Associates

Investments in unlisted shares of associates are recognised in the financial statements by applying the equity method of accounting.

Controlled entities

Investments in controlled entities are valued in the parent entity's accounts at cost, less, where appropriate, a provision for diminution in value where the annual review by Directors has determined that cost is in excess of the recoverable amount from these assets.

j) Leased non-current assets

A distinction is made between finance leases which effectively transfer from the lessor to the lessee substantially all the risks and benefits incident to ownership of leased non-current assets, and operating leases under which the lessor effectively retains substantially all such risks and benefits.

Finance leases are capitalised. A lease asset and liability are established at the present value of minimum lease payments. Lease payments are allocated between the principal component of the lease liability and the interest expense.

The lease asset is amortised on a straight line basis over the term of the lease, or where it is likely that the consolidated entity will obtain ownership of the asset, the life of the asset. Lease assets held at the reporting date are being amortised over periods ranging from 2 to 4 years.

Other operating lease payments are charged to the statement of financial performance in the periods in which they are incurred, as this represents the pattern of benefits derived from the leased assets.

k) Property, plant and equipment

Depreciation and amortisation

All assets have limited useful lives and are depreciated/amortised using the straight line method over their estimated useful lives. The depreciation/amortisation rates and methods are reviewed annually to determine the most appropriate method.

NOTES TO THE FINANCIAL STATEMENTS continued

FOR THE YEAR ENDED 30 JUNE 2005

The depreciation/amortisation rates used for each class of asset, for the current and previous years, are as follows:

Plant and equipment	25 – 50%
---------------------	----------

Assets are depreciated or amortised from the month following their acquisition.

l) Payables

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether or not billed to the Company. Trade accounts payable are normally settled within 30 days.

m) Employee entitlements

Provision is made for the Company's liability for employee benefits arising from services rendered by employees to balance date. Employee benefits expected to be settled within one year together with entitlements arising from wages and salaries, annual leave and sick leave which will be settled after one year, have been measured at the amounts expected to be paid when the liability is settled, plus related on-costs. Other employee benefits payable later than one year have been measured at the present value of the estimated future cash outflows to be made for those benefits.

Contributions are made by the consolidated entity to employee superannuation funds and are charged as expenses when incurred.

n) Cash and cash equivalents

Cash and cash equivalents includes deposits held at call with a bank or financial institution and highly liquid investments with short periods to maturity that are readily convertible to cash on hand at the consolidated entity's option and are subject to insignificant risk of changes in value.

o) Going concern

On the basis of the consolidated entity's present level of operations, the Directors are of the opinion that the consolidated entity has the ability to raise additional working capital through the issue of additional new shares to meet its financial obligations for the next 12-month period from the date of signing the Directors' declaration.

p) Exploration and development expenditure

Exploration, evaluation and development expenditure incurred is accumulated in respect of each identifiable area of interest. These costs are only carried forward to the extent that they are expected to be recouped through the successful development of the area or where activities in the area have not yet reached a stage which permits reasonable

assessment of the existence of economically recoverable reserves.

Accumulated costs in relation to an abandoned area are written off in full against profit in the year in which the decision to abandon the area is made.

When production commences, the accumulated costs for the relevant area of interest are amortised over the life of the area according to the rate of depletion of the economically recoverable reserves.

A regular review is undertaken of each area of interest to determine the appropriateness of continuing to carry forward costs in relation to that area of interest

q) Joint Ventures

Joint Venture Operations

The proportionate interests in the assets, liabilities and expenses of a joint venture operation have been incorporated in the financial statements under the appropriate headings. Details of the joint venture are set out in Note 26.

r) Borrowing Costs

Borrowing costs are recognised as expenses in the period in which they are incurred.

Borrowing costs include finance lease charges.

s) Earnings per share

(i) *Basic earnings per share*

Basic earnings per share is determined by dividing net profit after income tax attributable to members of the company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

(ii) *Diluted earnings per share*

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

t) Intangibles

Software is valued at cost and amortised on a straight line basis over the life of the asset.

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Note	Consolidated Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
2. REVENUE FROM ORDINARY ACTIVITIES					
Rendering of services revenue from operating activities		-	-	-	-
Other revenues from operating activities					
Interest		157,976	34,015	157,056	34,015
Other revenue from outside operating activities					
Other revenue		-	-	-	-
Total other revenues		-	-	-	-
Total revenue from ordinary activities		157,976	34,015	157,056	34,015

3. LOSS FORM ORDINARY ACTIVITIES BEFORE INCOME TAX EXPENSE					
Loss from ordinary activities before income tax expense has been arrived at after charging/(crediting) the following items:					
Depreciation of plant and equipment		48,099	2,156	48,099	2,156
Amortisation of goodwill		17,126	10,031	-	-
Total depreciation and amortisation		65,225	12,187	48,099	2,156
Operating lease rental expense		24,960	8,320	24,960	8,320

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Note	Consolidated Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
4. AUDITORS' REMUNERATION					
Audit services		15,000	7,000	12,000	5,000
Other services		-	-	-	-
		15,000	7,000	12,000	5,000
5. TAXATION					
(a) Income tax expense					
Prima facie income tax expense/(benefit) calculated at 30% on the profit from ordinary activities		(187,935)	(53,490)	(181,709)	(45,595)
Increase in income tax expense due to:					
- Other non-deductible items		5,894	3,009	756	-
- Current year losses not brought to account		182,041	50,481	180,953	45,595
Income tax expense attributable to ordinary activities		-	-	-	-
The potential future income tax benefit arising from tax losses and timing differences has not been recognised as an asset because recovery of tax losses is not virtually certain and recovery of timing differences is not assured beyond any reasonable doubt.					
Tax losses carried forward at a rate of 30%		793,360	166,910	756,320	150,622
Timing differences		50,620	-	48,099	-

The potential future income tax benefit will only be obtained if:

- (i) the Company derives future assessable income of a nature and of an amount sufficient to enable the benefit from the deductions for the losses to be realised;
- (ii) the Company continues to comply with the conditions for deductibility imposed by tax legislation; and
- (iii) no changes in tax legislation adversely affect the Company in realizing the benefit from the deductions for the losses.

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
6. DIVIDENDS				
There were no ordinary dividends proposed/paid during the year ended 30 June 2005 by the Company.				
7. EARNINGS PER SHARE				
Earnings used in the calculation of basic and dilutive earnings per share	(626,450)	(178,301)		
(a) Basic loss per share	(\$0.0145)	(\$0.016)		
(b) Diluted loss per share	(\$0.0095)	(\$0.011)		
Weighted average number of ordinary shares used in the calculation of basic earnings per share	43,190,626	11,307,908		
Weighted average number of options outstanding	22,101,700	5,653,953		
Weighted average number of ordinary shares outstanding during the year used in calculating diluted earnings per share	65,689,663	16,861,861		
Potential ordinary shares				
Options outstanding at 30 June 2005 are considered to be potential ordinary shares for the purposes of determining diluted earnings per share.				
8. RECEIVABLES				
<i>Current</i>				
Trade debtors	131,895	66,046	96,045	46,481
Less: Provision for doubtful trade debts	-	-	-	-
Other debtors		-	-	-
Total current receivable	131,895	66,046	96,045	46,481
<i>Non-current</i>				
Karoo Gas Pty Ltd	-	-	3,204,948	241,455
Less: provision for doubtful debts	-	-	-	-
Total non-current receivables	-	-	3,204,948	241,455

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
9. OTHER FINANCIAL ASSETS				
<i>Non-current</i>				
Investment in subsidiary companies at cost	1,055	-	151,055	150,000
Formation Costs	1,212	1,212	1,212	1,212
Total	2,267	1,212	152,267	151,212
10. PROPERTY, PLANT AND EQUIPMENT				
<i>Plant and equipment</i>				
At cost	168,018	48,951	168,018	48,951
Accumulated depreciation	(50,255)	(2,156)	(50,255)	(2,156)
Total property, plant and equipment net book value	117,763	46,795	117,763	46,795
<i>Reconciliations</i>				
Reconciliations of the carrying amounts for each class of property, plant and equipment are set out below:				
<i>Plant and equipment</i>				
Carrying amount at beginning of year	46,795	-	46,795	-
Additions	119,067	48,951	119,067	48,951
Disposals	-	-	-	-
Depreciation	(48,099)	(2,156)	(48,099)	(2,156)
Carrying amount at end of year	117,763	46,795	117,763	46,795
11. INTANGIBLE ASSETS				
Goodwill on acquisition of Karoon Gas Pty Ltd	171,951	171,951	-	-
Less: amortisation of Goodwill	(27,157)	(10,031)	-	-
Total	(144,794)	(161,920)	-	-

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
12. OTHER ASSETS				
<i>Non-current</i>				
Exploration and evaluation costs carried forward in respect of areas of interest	2,984,934	71,394	-	-
Exploration and evaluation expenditure relates to the areas of interest in exploration phase for petroleum exploration permits PEP 162, WA-314-P & WA-315-P and minerals exploration Licence EL 4537.				
The expenditure is carried forward provided that:				
<ul style="list-style-type: none"> - Costs are expected to be recouped through successful development of the area or alternatively by its sale or; - Exploration and development expenditure activities in the specific areas have not reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves and active and subsequent operations in or in relation to the area are continuing. 				
13. PAYABLES				
<i>Current</i>				
Trade creditors	107,813	156,404	51,308	92,427
Other creditors and accruals	46,920	33,360	43,641	27,360
	154,733	189,764	94,949	119,787
14. PROVISIONS				
<i>Non-current</i>				
Employee entitlements	1,471	-	1,471	-
Other	1,050	-	1,050	-
Total	2,521	-	2,521	-
Number of employees at year end	2	2	2	2

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
15. CONTRIBUTED EQUITY				
Issued and paid-up share capital				
55,494,697 (2004 : 41,663,505) fully paid ordinary shares	18,252,592	5,127,703	18,252,592	5,127,703
Less: equity raising costs	(1,261,743)	(400,972)	(1,261,743)	(400,972)
	16,990,849	4,726,731	16,990,849	4,726,731
<i>Movements in share capital</i>				
Balance at the beginning of the financial year			5,147,703	-
<i>Shares issued</i>				
13,831,192 fully paid ordinary shares			13,104,889	5,147,703
Less: equity raising costs			(1,261,743)	(420,972)
			16,990,849	4,726,731
			No.	No.
At the beginning of the reporting period			41,663,505	-
Shares issued during year			13,831,194	41,663,505
At reporting date			55,494,699	41,663,505
<p> Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings. In the event of winding up of the Company, ordinary shareholders rank after all other creditors and are fully entitled to any proceeds of liquidation.</p>				
16. ACCUMULATED LOSSES				
(Accumulated losses) Retained profits at beginning of year	(148,092)	-	(151,983)	-
Retained profits acquired with purchase of Karoon Gas Pty Ltd	-	30,209	-	-
Net loss	(626,450)	(178,301)	(605,698)	(151,983)
Accumulated losses at end of year	(774,542)	(148,092)	(757,681)	(151,983)
17. TOTAL EQUITY RECONCILIATION				
Total equity at beginning of year		-		
Net loss recognised in the statement of financial performance	(774,542)	(148,092)	(757,681)	(151,983)
Contributions of equity	16,990,948	4,726,730	16,990,849	4,726,731
	16,216,406	4,578,638	16,233,168	4,574,748

NOTES TO THE FINANCIAL STATEMENTS continued

FOR THE YEAR ENDED 30 JUNE 2005

17. ADDITIONAL FINANCIAL INSTRUMENTS DISCLOSURE**a) Credit risk**

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date to recognised financial assets in the carrying amount of those assets, net of any provisions for doubtful debts, as disclosed in the statement of financial position and notes to the financial statements.

The consolidated entity does not have any material credit risk exposure to any single debtor or group of debtors under financial instruments entered into by the consolidated entity.

b) Net fair values

The net fair values of listed investments will be valued at the quoted market bid price at balance date adjusted for transaction costs expected to be incurred. For other assets and other liabilities the net fair value approximates their carrying value. No financial assets and financial liabilities are readily traded on organised markets in standardised form other than listed investments. Financial assets where the carrying amount exceeds net fair values have not been written down as the consolidated entity intends to hold these assets to maturity.

The aggregate net fair values and carrying amounts of financial assets and financial liabilities are disclosed in the statement of financial position and in the notes to the financial statements.

c) Interest rate risk

Interest rate risk exposures

The consolidated entity's exposure to interest rate risk and the effective weighted average interest rate for classes of financial assets and financial liabilities is set out below:

Note	Weighted Average Interest rate %	Floating Interest Rate \$	Fixed interest maturing in 1 year or less \$	Non-interest- bearing \$	Total \$
2005					
<i>Financial assets</i>					
Cash	5.35	12,796,605			12,796,605
Receivables		131,895			131,895
		12,928,500			12,928,500
<i>Financial liabilities</i>					
Payables				157,254	157,254
2004					
<i>Financial assets</i>					
Cash	5.15	4,225,633			4,225,633
Receivables				66,046	66,046
		4,225,633		66,046	4,291,679
<i>Financial liabilities</i>					
Payables				189,764	189,764

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
18. COMMITMENTS				
Operating lease commitments				
Future operating lease rentals not provided for in the financial statements and payable:				
Within one year	25,000	25,000	25,000	25,000
Later than one year but not later than five years	25,000	50,000	25,000	50,000
	50,000	75,000	50,000	75,000
Finance lease commitments				
The consolidated entity does not have any finance leases at balance date.				
Capital expenditure commitments				
Capital commitments for petroleum exploration permits payable				
- Not later than 1 year	14,000,000	1,603,800	-	-
- Later than 1 year but not later than 5 years	23,000,000	391,200	-	-
- Later than 5 years	-	-	-	-
	37,000,000	1,995,000	-	-

Capital expenditure commitments relate to work commitments pursuant to the award of petroleum exploration permit PEP 162, WA-314-P & WA-315-P and mineral exploration licence EL 4537.

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
19. NOTES TO THE STATEMENT OF CASH FLOWS				
(a) Reconciliation of cash				
For the purposes of the statement of cash flows, cash includes cash on hand and at bank, short-term deposits and short-term commercial bills. Cash as at the end of the financial year as shown in the statement of cash flows is as disclosed in the statement of financial position as "Cash Assets".				
(b) Reconciliation of loss from ordinary activities after income tax net cash provided by operating activities				
Loss from ordinary activities after income tax	(626,450)	(178,301)	(605,698)	(151,983)
Add/(less) non-cash items				
Write off of exploration expenditure	-	1,417	-	-
Amortisation	17,126	10,031	-	-
Depreciation	48,099	2,156	48,099	2,156
Cash flows excluded from loss from profit from ordinary activities attributable to operating activities:				
Formation expenses of company	-	-	-	(1,212)
Payments for security deposits	-	-	(8,628)	-
Change in assets and liabilities				
Decrease/(Increase) in receivables	(4,209)	(66,046)	(4,209)	(46,481)
Decrease/(Increase) in tax refundable	(14,486)	7,728	46,481	-
(Decrease)/Increase in payables	32,380	125,767	(48,150)	119,787
Net cash flow from operating activities	(547,540)	(97,248)	(572,108)	(77,733)

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

20. DIRECTORS' and EXECUTIVE REMUNERATION

(a) Names and positions held of parent entity directors and specified executives in office at any time during the financial year are:

Parent Entity Directors

Mr Robert Hosking	Chairman – Executive
Mr Mark Smith	Director – Executive
Mr Edward Munks	Director – Non Executive / Company Secretary (Resigned 25 February 2005)
Mr Geoff Atkins	Director – Non-Executive (Appointed 22 February 2005)
Mr Stephen Power	Director – Non-Executive (Appointed 28 June 2005)

Specified Executives

Mr Robert Hosking	Chairman – Executive
Mr Mark Smith	Director – Executive

(b) Disclosure in Directors' Remuneration

	Primary	Post Employment	Equity	Other		
	Salary, Fees & Commissions	Superannuation Contributions	Cash Bonus	Superannuation	Options	Total
	\$	\$	\$	\$	\$	\$
2005						
Mr Robert Hosking	260,000	-	-	-	-	260,000
Mr Mark Smith	171,179	-	-	-	-	171,179
Mr Geoff Atkins	10,417	938	-	-	-	11,355
Mr Stephen Power	-	-	-	-	-	-
	462,429	2,813	-	-	-	465,242
2004						
Mr Robert Hosking	91,000	-	-	-	-	91,000
Mr Mark Smith	29,596	-	-	-	-	29,596
Mr Edward Munks	2,083	-	-	-	-	2,083
Mrs Patricia Hosking	-	-	-	-	-	-
	122,679	-	-	-	-	122,679

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

(c) Option holdings

Number of options held by specified directors and executives

	Balance 1/7/04	Granted as remuneration	Options exercised	Balance 30/6/05	Total vested 30/6/05	Total exercisable 30/6/05	Total unexercisable 30/6/05
Parent Entity Directors							
Mr Robert Hosking	4,604,167	-	-	4,604,167	4,604,167	4,604,167	-
Mr Mark Smith	1,110,000	-	-	1,110,000	1,110,000	1,110,000	-
Mr Geoff Atkins	-	-	-	75,000	75,000	75,000	-
Mr Stephen Power	-	-	-	5,000	5,000	5,000	-
Specified Executives							
Mr Robert Hosking	4,604,167	-	-	4,604,167	4,604,167	4,604,167	-
Mr Mark Smith	1,110,000	-	-	1,110,000	1,110,000	1,110,000	-

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

(d) Shareholdings

Number of shares held by specified directors and executives

	Balance 1/7/04	Received as remuneration	Options exercised	Net change other	Balance 30/6/05
Parent Entity Directors					
Mr Robert Hosking	8,208,335	-	-	-	8,208,335
Mr Mark Smith	1,220,000	-	-	-	1,220,000
Mr Geoff Atkins	152,500	-	-	-	152,500
Mr Stephen Power	-	-	-	10,000	10,000
		-	-		
Total	9,580,835			10,000	9,590,835

(e) Remuneration practices

The company's policy for determining the nature and amount of emoluments of board members and senior executives of the company is as follows:

Executives

The executive remuneration structure is based on a number of factors, including length of service, particular experience of the individual concerned and overall performance of the company.

Non-executives

- Non-executive Directors are remunerated by way of fees in the form of cash and superannuation contributions,
- Non-executive Directors are not provided with retirement benefits other than statutory superannuation.

No Director has entered into a material contract with the Company since the end of the previous financial year, however there were 2 material contracts involving Directors' interests subsisting at the end. The Company has engaged Ropat Nominees Pty Ltd, a company in which Robert Hosking is a director and shareholder to procure that Mr Hosking provides the services of managing director to the company. The consultancy fee is \$250,000 per annum. The company has also entered into a lease with Ropat Nominees Pty Ltd in relation to an office for the Company's use. An annual rent of \$25,000 is payable by the Company. The term of both agreements is 3 years.

The company has also engaged IERS (Australia) Pty Ltd, a company in which Mark Smith is a director and shareholder, to procure that Mr Smith provide the services of exploration director to the company. The consultancy fee is \$250,000 per annum. The term of the agreement is 3 years.

Other transactions with the Company

During the year, a Director, Mr M Smith had an interest in IERS (Australia) Pty which incurred operating, expenses on behalf of the company. The value of transactions during the year was NIL (2004: \$3,026).

During the year, a Director, Mr R Hosking, had an interest in Ropat Nominees Pty Ltd (Ropat) which incurred operating, expenses on behalf of the company. The value of transactions during the year was NIL (2004: \$3,514).

NOTES TO THE FINANCIAL STATEMENTS continued

FOR THE YEAR ENDED 30 JUNE 2005

Other transactions with the Company

	Consolidated Entity		Parent Entity	
	2005	2004	2005	2004
	\$	\$	\$	\$
Loans to related entities				
Non-current				
Controlled entities				
- Karoon Gas Pty Ltd	-	-	3,253,698	241,455
- Eastern Pacific Coal Pty Ltd	-	-	-	-
	-	-	3,253,698	241,455

21. CONTINGENT LIABILITIES

The Directors are not aware of any contingent liabilities that are likely to have a material effect on the results of the consolidated entity except as disclosed in the final statements.

22. EVENTS SUBSEQUENT TO BALANCE DATE

Subsequent to the end of the financial year the economic entity completed an aeromagnetic survey over the permits WA-314-P and WA-315-P and is in the process of contracting through BG International the operator, a seismic company to carry out a 800 – 1200 kilometre 3D seismic survey over the above two permits.

Name	Country of incorporation	Percentage of equity interest held by the Consolidated entity		Investment		Contribution to Group profit	
		2005	2004	2005	2004	2005	2004
		%	%	\$	\$	\$	\$
Karoo Gas Pty Ltd	Australia	100%	100%	151,212	151,212	(3,526)	(8,736)
Eastern Pacific Coal Pty Ltd	Australia	100%	-	1,055	-	(100)	-

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

25. EMPLOYEE BENEFITS

Employee share option arrangement

During the year there no options were granted to employees under the Karoon Gas Australia Ltd Share Option

The closing share market price of an ordinary share of Karoon Gas Australia Limited on the Australian Stock Exchange at 30 June 2005 was \$1.70

	Economic Entity		Parent Entity	
	2005 No.	2004 No.	2005 No.	2004 No.
a) Movements in the number of share options held by employees are as follows:				
Opening balance	-	-	-	-
Granted during the year	-	-	415,000	-
Exercised during the year	-	-	-	-
Lapsed during the year	-	-	-	-
Closing balance	-	-	415,000	-

26. INTEREST IN JOINT VENTURES

Joint venture operation

	Consolidated Entity		Parent Entity	
	2005 \$	2004 \$	2005 \$	2004 \$
Non-current assets				
Other	-	-	-	-
Total non-current assets	-	-	-	-
Share of assets employed in joint venture	-	-	-	-

Note as at 30 June 2005, the joint venture with BG International did not have any assets or liabilities, as BG International were still to earn an interest in the permits by carrying out an airborne gravity survey.

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

27. IMPACTS OF ADOPTING AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

The company is preparing and managing the transition to Australian Equivalents to International Financial Reporting Standards (AIFRS) effective for financial years commencing 1 January 2005. The adoption of AIFRS will be reflected in the economic entity's and the parent entity's financial statements for the year ending 30 June 2006. On first time adoption of AIFRS, comparatives for the financial year ended 30 June 2005 are required to be re-stated. The majority of the AIFRS transitional adjustments will be made retrospectively against retained earnings at 1 July 2004.

The economic entity's management has assessed the significance of the expected changes and is preparing for their implementation. The impact of the alternative treatments and elections under AASB 1: First Time Adoption of Australian Equivalents to International Financial Reporting Standards has been considered where applicable.

The directors are of the opinion that the key material differences in the economic entity's accounting policies on conversion to AIFRS and the financial effect of these differences, where known, are as follows. Although the adjustments disclosed in this note are based on management's best knowledge of expected standards and interpretations, and current facts and circumstances, these may change. For example, amended or additional standards or interpretations may be issued by the AASB and the IASB. Therefore, until the company prepares its first full AIFRS financial statements, the possibility cannot be excluded that the accompanying disclosures may have to be adjusted.

Impact on the statements of financial performance

	Notes	Consolidated			Parent Entity		
		Existing GAAP \$	Effect of change \$	AIFRS \$	Existing GAAP \$	Effect of change \$	AIFRS \$
Revenues from ordinary activities		157,976		157,976	157,056		157,056
Accounting & Taxation Fees		(19,927)		(19,927)	(19,927)		(19,927)
Amortisation of goodwill on acquisition of Karoon Gas Pty Ltd		(17,126)	(144,794)	(161,920)	-		-
Audit fees		(15,000)		(15,000)	(12,000)		(12,000)
Computer Support		(8,994)		(8,994)	(8,994)		(8,994)
Consulting fees		(191,696)		(191,696)	(191,696)		(191,696)
Corporate promotion and annual report		(15,285)		(15,285)	(15,285)		(15,285)
Depreciation of plant and equipment		(48,099)		(48,099)	(48,099)		(48,099)
Directors benefits		(30,479)		(30,479)	(30,479)		(30,479)
Legal fees		(109,468)		(109,468)	(109,468)		(109,468)
Operating lease rental expense		(24,960)		(24,960)	(24,960)		(24,960)
Other expenses from ordinary activities		(70,945)		(70,945)	(69,499)		(69,499)
Property costs		(51,206)		(51,206)	(51,106)		(51,106)
Salaries & Superannuation		(50,215)	(94,122)	(144,337)	(50,215)	(94,122)	(144,337)
Share registry and listing fees		(59,797)		(59,797)	(59,797)		(59,797)
Travel and accommodation		(71,229)		(71,229)	(71,229)		(71,229)
Loss from ordinary activities before income tax expense		(626,450)	(238,916)	(865,366)	(605,698)	(94,122)	(699,820)
Income tax (expense)/benefit relating to ordinary activities		-	-	-	-	-	-
Net loss from ordinary activities after income tax		(626,450)	(238,916)	(865,366)	(605,698)	(94,122)	(699,820)
Expense attributable to members of the parent entity							
Total changes in equity other than those resulting from transactions with owners as owners		(626,450)	(238,916)	(865,366)	(605,698)	(94,122)	(699,820)
Basic earnings per share		(\$0.0145)		(0.0200)			
Diluted earning per share		(\$0.0095)		(0.0132)			

NOTES TO THE FINANCIAL STATEMENTS continued
FOR THE YEAR ENDED 30 JUNE 2005

27. IMPACTS OF ADOPTING AUSTRALIAN EQUIVALENTS TO IFRS (continued)

Impact on the statements of financial position

	Notes	Consolidated			Parent Entity		
		Existing GAAP \$	Effect of change \$	AIFRS \$	Existing GAAP \$	Effect of change \$	AIFRS \$
Current assets							
Cash assets		12,796,605		12,796,605	12,757,094		12,757,094
Receivables		131,895		131,895	96,045		96,045
Other		195,402		195,402			
Total current assets		13,123,902		13,123,902	12,853,139		12,853,139
Non-current assets							
Other financial assets		2,267		2,267	152,267		152,267
Receivables					3,204,948		3,204,948
Property, plant and equipment		117,763		117,763	117,763		117,763
Intangible assets		144,794	(144,794)	-	-		-
Other assets		2,984,934		2,984,934	-		-
Total non-current assets		3,249,758	(144,794)	3,104,964	3,474,978		3,474,978
Total assets		16,373,660	(144,794)	16,228,866	16,328,117		16,328,117
Current liabilities							
Payables		(154,733)		(154,733)	(94,949)		(94,949)
Provisions		(2,521)		(2,521)			
Total current liabilities		(157,254)		(157,254)	(94,949)		(94,949)
Total liabilities		(157,254)		(157,254)	(94,949)		(94,949)
Net assets		16,216,406	(144,794)	16,071,612	16,233,168		16,233,168
Equity							
Contributed equity		16,990,949		16,990,949	16,990,849		16,990,849
Accumulated losses		(774,543)	(144,794)	(919,337)	(757,681)		(757,681)
Total equity		16,216,406	(144,794)	16,071,612	16,233,168		16,233,168

NOTES TO THE FINANCIAL STATEMENTS continued

FOR THE YEAR ENDED 30 JUNE 2005

a) Income Tax

Under AASB112 Income Taxes, deferred tax balances are determined using the balance sheet method which calculates temporary differences based on the carrying amounts of an entity's assets and liabilities in the statement of financial position and their associated tax bases. In addition, current and deferred taxes attributable to amounts recognised directly in equity are also recognised directly in equity.

This will result in a change to the current accounting policy, under which deferred tax balances are determined using the income statement method, items are only tax-effected if they are included in the determination of pre-tax accounting profit or loss and/or taxable income or loss and current and deferred taxes cannot be recognised directly in equity.

(b) Equity-based compensation benefits

Under AASB 2 *Share-based Payment*, from 1 July 2004 the group is required to recognise an expense for those options that were issued to employees under the Karoon Gas Employee Share Option Plan after 7 November 2002 but that had not vested by 1 January 2005.

This will result in a change to the current accounting policy under which no expense is recognised for equity-based compensation.

If the policy required by AASB 2 had been applied during the year ended 30 June 2005, consolidated and parent entity retained profits at 30 June 2005 would have been \$238,916 lower, with a corresponding increase in the share-based payment reserve. For the year ended 30 June 2005, the consolidated and parent entity employee benefits expense would have been \$94,122 higher, with a corresponding increase in the net movement in the share-based payment reserve.

(c) Financial Instruments

The group will be taking advantage of the exemption available under AASB 1 to apply AASB 132 Financial Instruments: Disclosure and Presentation and AASB 139 Financial Instruments: Recognition and Measurement only from 1 July 2005. This allows the group to apply previous Australian generally accepted accounting principles (Australian GAAP) to the comparative information of financial instruments within the scope of AASB 132 and AASB 139 for the 30 June 2006 financial report.

Under AASB 132, the current classification of financial instruments issued by entities in the consolidated entity would not change.

AASB 139 is likely to have the following impacts.

Classification and measurement of financial assets and liabilities

Under AASB 139, financial assets held by entities in the consolidated entity will be classified as wither at fair value through profit or loss, held-to-maturity, available for sale or loans and receivables and, depending upon classification, measured at fair value or amortised cost.

Under AASB 139, investments in

- Loans and receivables and financial liabilities classifications will remain unchanged. Measurement of these instruments will initially be at fair value with subsequent measurement at amortised cost, using the effective interest rate method.

This will result in a change to the current accounting policy, under which financial assets are carried at the lower of cost and recoverable amount, with changes recognised in profit or loss.

As a result of the application of the exemption referred to above, there would have been no adjustment to classification or measurement of financial assets or liabilities from the application of AIFRS during the year ended 30 June 2005. Changes in classification and measurement will be recognised from July 2005.

DIRECTORS' DECLARATION
FOR THE YEAR ENDED 30 JUNE 2005

The Directors of the company declare that:

1. The financial statements and notes, as set out on pages 19 to 39 are in accordance with the Corporations Act 2001:
 - (a) comply with Accounting Standards and the Corporations Regulations 2001; and
 - (b) give a true and fair view of the financial position as at 30 June 2005 and of the performance for the year ended on that date of the Company and consolidated entity;
2. In the Directors' opinion there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the Board of Directors.

Dated at Melbourne this 26th day of August 2005



Robert Hosking
Director

INDEPENDENT AUDIT REPORT TO MEMBERS OF KAROON GAS AUSTRALIA LIMITED AND CONTROLLED ENTITIES

FOR THE YEAR ENDED 30 JUNE 2005

Scope

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for both Karoon Gas Australia Limited (the company) and Karoon Gas Australia Limited and Controlled Entities (the consolidated entity), for the year ended 30 June 2005. The consolidated entity comprises both the company and the entities it controlled during that year.

The directors of the company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Corporations Act 2001. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit approach

We conducted an independent audit in order to express an opinion to the members of the company. Our audit was conducted in accordance with Australian Auditing Standards, in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001, including compliance with Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

Independence

In conducting our audit, we followed applicable independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001.

Audit opinion

In our opinion, the financial report of Karoon Gas Australia Limited and Karoon Gas Australia Limited and Controlled Entities is in accordance with:

- (a) the Corporations Act 2001, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2005 and of their performance for the year ended on that date; and
 - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and
- (b) other mandatory financial reporting requirements in Australia.

Inherent Uncertainty Regarding Continuation as a Going Concern

Without qualification to the opinion expressed above, attention is drawn to the following matter. As indicated in Note 1(o) to the financial report, the Directors of Karoon Gas Australia Limited are of the opinion that the consolidated entity has the ability to farm-out its interest in its permits and seek additional sources of capital in order to meet future exploration expenditure commitments and working capital requirements. If the farm-outs do not occur or additional capital is not raised, there is uncertainty whether the company and the consolidated entity will be able to continue as a going concern and therefore whether it will realise its assets and extinguish its liabilities in the normal course of business and at the amounts in the financial report.

Mitchell Wilson & Partners
Chartered Accountants

Melbourne,

STATEMENT OF CORPORATE GOVERNANCE PRINCIPLES FOR THE YEAR ENDED 30 JUNE 2005

The Statement of Corporate Governance Principles establishes the framework for how the Board oversees the Company and performs its functions on behalf of shareholders. Karoons' objective is to achieve best practice in corporate governance and the Company's Directors and employees are committed to achieving this objective.

Structure of the Board of Directors

The Board is elected by shareholders to represent all shareholders. It is a Director's responsibility, in all decisions he or she is called upon to make concerning the consolidated entity's affairs, to conscientiously weigh the interests of shareholders in light of the circumstances and to consider the effects of such decisions on the interests of all shareholders.

The Company recognises the importance of having a Board comprising Directors with an appropriate range of background, skills and experience to suit the Company's current and future strategies and requirements.

Role of the Board

The Board is to oversee and direct the management of the Company with a view to increasing shareholder wealth by:

- defining and monitoring the strategic direction of the Company
- defining policies and procedures to ensure the Company operates within the legal, ethical and social requirements of its environment
- establishing control and accountability systems within the consolidated entity's operations to conform to the legal requirements and the expectations of shareholders and other stakeholders
- defining and monitoring the management of an effective risk assessment strategy
- securing funds to develop the Company's assets
- driving Company performance
- the Board will, from time to time, review and monitor the management and Company performance
- appoint and appraise the Executive Chairman and any other executive Director. Ensure that there are adequate plans and procedures for succession planning

- review and approve the remuneration of the CEO and senior management

Composition of the Board

The Board of Directors is constituted by four members, with two non-executive Directors. The skills, experience and expertise relevant to the position of each director who is in office at the date of the annual report and their term of office are detailed in the director's report.

The independent directors of the company are Geoff Atkins and Stephen Power.

When determining whether a non-executive director is independent the director must not fail any of the following materiality thresholds:

- less than 10% of company shares are held by the director and any entity or individual directly or indirectly associated with the director;
- none of the directors' income or the income of an individual or entity directly or indirectly associated with the director is derived from a contract with any member of the economic entity other than income derived as a director of the entity.

The Board's composition will be reviewed from time to time having regard to the growth of the consolidated entity's business with a view to eventually having a majority of independent Directors.

Under the Company's constitution, at each Annual General Meeting of shareholders, one third of the Directors (excluding the Managing Director) must resign, with Directors resigning by rotation based on the date of their appointment. Directors resigning by rotation may offer themselves for re-election.

**STATEMENT OF CORPORATE GOVERNANCE
PRINCIPLES continued**
FOR THE YEAR ENDED 30 JUNE 2005

Meeting schedule

The Board schedules meetings at least every two months with additional committee meetings, if and when required, to discuss technical and specific matters.

Relationship of Board with management

The management of the day-to-day business of the Company is conducted by or under the supervision of the executive chairman and is designated by the Board of Directors, which has clearly defined the limits of management's responsibilities. The Board will approve the corporate objectives that will be developed and implemented by the executive chairman and management.

The Board will adopt appropriate structures and procedures to ensure that the Board functions independently of management.

Board committees

The Board may establish appropriate committees to assist in its role at appropriate points in the Company's evolution.

The Board has established the following committee:

- Audit Committee

Composition of committees

A committee will be chaired by a Director appointed by the Board. It can consist of the following: a Director(s) or Secretary, and other members who possess skills and expertise suitable for carrying out the functions of the Committee as appointed by the Chairman of the Committee.

Audit Committee

The role of the Committee is to advise on the establishment and maintenance of a framework of internal control and the appropriate ethical standards for the management of the consolidated entity. The Company has formally adopted an Audit Committee charter.

The Audit Committee also gives the Board of Directors additional assurance regarding the quality and reliability of financial information prepared for use by the Board in determining policies or for inclusion in financial statements.

The Audit Committee presently consists of:

Mr R Hosking

Mr H Peeters

Mr G Atkins

The responsibilities of the Audit Committee include:

- liaising with external auditors and ensuring that the annual and half yearly statutory audits are conducted in an effective manner;
- reviewing internal controls and recommending improvements;
- reviewing the half year financial statements prior to lodgement of these documents with the Australian Stock Exchange, and any significant adjustments required as a result of the audit;
- reviewing the draft financial statements and the audit report and making the necessary recommendations to the Board for approval of the financial statements;
- reviewing treasury recommendations and making necessary recommendations to the Board for approval;
- reviewing and reporting on any special reviews deemed necessary by the Board.

The Committee reports to the full Board after each Committee Meeting and relevant papers and minutes are provided to all Directors.

Internal control

The Board acknowledges that it is responsible for the overall internal control framework. To assist in discharging this responsibility the Company has an established internal framework, which can be described as follows:

- Financial reporting – there is a comprehensive budgeting system with an annual budget approved by the Directors. Monthly actual results are reported against budget and revised forecasts for the year. A revised budget is prepared half yearly and approved by the Directors.

Functional specialty reporting – the Company has identified a number of key areas that are subject to:

- regular reporting to the Board such as treasury, legal and self insurance matters;

- Investment appraisal – the Company has clearly defined guidelines for capital expenditure. These include annual budgets and review procedures;
- Surplus funds – a policy of conservative and secure investment of surplus funds is applied.

Advice to Directors

Subject to the approval of the Board, an individual Director may engage an outside adviser at the expense of the Company in appropriate circumstances.

Fair dealings and related party transactions

A Director, or entities in which a Director has a significant interest and/or influence, who enters into a transaction with the Company must make full disclosure of all material elements of the transaction to the Chairman, or, if the Director involved is the Chairman, to the Board.

In addition, contracts with Directors, or entities in which Directors have a significant interest and/or influence, must be approved by the Audit Committee in advance of committing to the Company:

- contracts for the supply of goods and/or services which extend beyond one year, or where the total value of goods and/or services supplied under the contract will, in any one year, exceed \$25,000
- all agreements to lease and/or leases of property
- all agreements for acquisition or disposal of property except by way of public auction

Any Director who is a member of the Audit Committee and who has a significant interest and/or influence in relation to a contract to be approved by the Committee must absent themselves from the meeting and not participate in any vote to approve such contract.

Disclosure of information

The Company has an objective of honest and open disclosure of information in dealing with stakeholders, subject to appropriate commercial considerations associated with competitive and sensitive information. Such disclosure may, in appropriate circumstances, exceed statutory requirements.

The Company has developed a draft Market Disclosure policy to ensure the compliance of the Company with the various laws and Australian Stock Exchange Limited listing rules obligations in relation to disclosure of information to the market.

Share dealings

The Board of Directors has adopted a policy and procedure on dealing in Company securities by Directors and senior management, which provides that Directors and any employee who from time to time possess information that is inside information should never deal in the Company's securities.

It also provides guidance on the periods when securities can be dealt.

Policy and procedure for share trading

Directors, employees, any consultants and their respective associates who, from time to time, possess information that could be considered to be inside information:

- Should never engage in short-term trading of any Karoon securities;
- Should never deal in any Karoon Gas securities while in possession of inside information;
- Should never communicate, directly or indirectly, any information or cause the information to be communicated, to another person the insider knows, or ought reasonable to know would or would likely to deal in Karoon securities.

In addition the Chairman, or in his absence, the Company Secretary, or in his absence, the Exploration Manager, will from time to time, declare an embargo period on restricting dealings in Karoon securities.

The embargo periods may typically include periods of one month prior to the date of the release of:

- The half yearly announcement to the ASX
- The yearly announcement to the ASX
- Disclosure documents to acquire equity securities in Karoon

If in doubt notify the Chairman / Secretary before commencing any transaction.

Ethical standards and responsible decision making

The Directors, senior executives and employees are required to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of the consolidated entity.

The Company has developed a draft code of conduct for Directors and Officers of the Company.

Environment

The Company has an environmental policy and is committed to conducting all its activities in an environmentally responsible manner.

The role of shareholders

The Board aims to ensure that all shareholders are informed of all major developments affecting the consolidated entity's state of affairs. Information is communicated to the shareholders as follows:

- The annual report is distributed to all shareholders. The Board ensures that the annual report includes relevant information about the operations of the consolidated entity during the year, changes in the state of affairs of the consolidated entity and other disclosures required by the Corporations Act.
- Half yearly financial statements prepared in accordance with the requirements of the Corporations Act are subject to an audit review. The financial statements are sent to any shareholder who requests them.
- Proposed major changes in the consolidated entity which may impact on share ownership rights are submitted to a vote of shareholders.
- Shareholder newsletters are distributed to shareholders at least twice per year.
- The Company posts all reports, Australian Stock Exchange and media releases and copies of significant presentations on the Company's website – www.karooongas.com.au.

In addition, news announcements and other information are sent by email to all persons who have requested their details be added to the Company's electronic mailing list. If requested, the Company, where appropriate, will provide general information by email, facsimile or post.

Risk assessment and management

As part of the consolidated entity's strategy to implement an integrated framework of control, the Board continually identifies and monitors the key business and financial risks that could jeopardise the consolidated entity achieving its objectives. The Board is continually developing appropriate controls that would effectively manage those risks. These include:

- business plan
- regular budgeting and financial reporting
- procedures to manage financial exposures

- commitment and expenditure levels exceeding certain levels are submitted to the Board for approval

Management accountability

The Board encourages management accountability for the Company's financial reports by requiring the Executive Chairman to state in writing to the Board that:

- a) the Company's financial reports present a true and fair view, in all material respects, of the Company's financial condition and operational results and are in accordance with relevant accounting standards;
- b) the statement given above is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board; and
- c) the Company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

Role of the Company Secretary

Under the Corporate Governance principles all Directors have access to the Company Secretary and the appointment and removal of the Company Secretary is a matter for decision by the Board as a whole.

The Company Secretary supports the effectiveness of the Board by monitoring that Board policy and procedures are followed and co-ordinating the completion and dispatch of Board agenda and briefing materials.

The Company Secretary is accountable to the Board, through the Chairperson, on all governance matters.

Annual general meeting

The Company will ensure that the Annual General Meeting (AGM) is held in a manner that enables as many shareholders as possible to attend and encourages effective participation by shareholders.

The Company will request that its external auditor attend the Company's AGM and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report. The Chairperson of that meeting will allow a reasonable opportunity for members to ask questions about the Company's performance and operations and ask questions of the external auditor concerning the conduct of the audit and the preparation and content of the auditor's report.

Remuneration

As an overall policy, the Company will remunerate in such a way that it:

- motivates Directors and management to pursue the long-term growth and success of the Company within an appropriate control framework that demonstrates a clear relationship between key executive performance and remuneration.

Non-executives

- Non-executive Directors are remunerated by way of fees (in the form of cash and superannuation contributions).

SHAREHOLDER INFORMATION

AS AT 19 August 2005

Shareholdings as at 19 August 2005**Substantial shareholders**

The number of shares held by substantial shareholders are:

	Fully paid Ordinary shares	Options expiry 30 June 2006 exercise price \$0.20
Ropat Nominees Pty Ltd	8,188,334	4,094,167

Twenty largest shareholders

Name of holder	Number of ordinary Shares held	Percentage of Shares held
Ropat Nominees Pty Ltd	8,188,334	13.41
Westpac Custodian Nominees Limited	6,026,000	9.87
Summerlea Nominees Limited	4,148,888	6.79
National Nominees Limited	1,854,650	3.04
HSBC Custody Nominees (Australia) Limited – GSI ECISA	1,836,959	3.01
J P Morgan Nominees Australia Limited	1,512,000	2.48
IERS (Australia) Pty Ltd	1,210,000	1.98
CSFB Third Nominees Pty Ltd	1,015,058	1.66
Echo Beach Pty Ltd	800,000	1.31
HSBC Custody Nominees	753,416	1.23
Pressure Drop Pty Ltd	750,000	1.23
Doug Spong & Mare Spong	750,000	1.23
Delregal Pty Ltd	500,000	0.82
JP Morgan Nominees Australia Ltd	500,000	0.82
Bojan Nominees Pty Ltd	462,535	0.76
Invia Custodian Pty Ltd	450,000	0.74
Brian Dunn Investments Pty Ltd	438,000	0.72
Alimoc Pty Ltd	383,333	0.63
Donald James Erskine	379,550	0.62
Ross Stansfield-Smith	350,528	0.57
		47.94
Total shares on issue	32,309,251	52.92

SHAREHOLDER INFORMATION continued

AS AT 19 August 2005

Twenty largest quoted option holders (options expiring 30 June 2006, exercisable at \$0.20)

Name of holder	Number of Options held	Percentage of Options held
Ropat Nominees Pty Ltd	4,094,167	21.73
Summerlea Nominees Pty Ltd	1,150,400	6.11
Rose Burton Pty Ltd	750,000	3.98
J P Morgan Nominees Australia Limited	625,000	3.32
IERS (Australia) Pty Ltd	605,000	3.21
Mr Ross Stansfield-Smith	549,850	2.92
Echo Beach Pty Ltd	400,000	2.12
Pressure Drop Pty Ltd	375,000	1.99
Doug Spong & Mare Spong	375,000	1.99
Citicorp Nominees Pty Limited	305,000	1.62
Delregal Pty Ltd	250,000	1.33
JP Morgan Nominees Australia Ltd	250,000	1.33
National Nominees Limited	250,000	1.33
Brian Dunn Investments Pty Ltd	230,000	1.22
Alimoc Pty Ltd	191,667	1.02
Johlenam Pty Ltd	190,000	1.01
Kenneth Stevenson	166,666	0.88
Summerbay Investments Pty Ltd	165,000	0.88
Fortis Clearing Nominees P/L	153,338	0.81
Mrs Nicole Linda Caulfield	150,000	0.80
Total Options on issue	11,226,088	59.60

SHAREHOLDER INFORMATION continued

AS AT 19 August 2005

Distribution of share and option holdings

Number of holders by size of holdings at 19 August 2005 were as follows:

	Ordinary fully paid shares	Options expiry 31/06/06 exercisable @ 20 cents	Director options expiry 30/06/07 exercisable @ 25 cents	Options expiry ESOP 30/06/2006
1 - 1,000	123	-	-	-
1,001 - 5,000	390	145	-	-
5,001 - 10,000	301	47	-	-
10,001 - 100,000	406	188	-	5
100,001 and above	75	22	3	-
Total	1,295	402	3	5

Issued capital

(a) At 19 August 2005, the following securities in the parent entity were on issue:

	Number of Securities issued	Number of holders
Fully paid ordinary shares	61,076,274	1,295
Options Exercisable at \$0.20 by 30 June 2006	12,494,250	402
Options Exercisable at \$0.25 by 30 June 2007 – Unquoted	1,500,000	3
ESOP Exercisable at \$1.25 by 30 June 2006	415,000	5

(b) At 19 August 2005, 22 shareholders held less than a marketable parcel of fully paid ordinary shares and one option holder held less than a marketable parcel of options.

Voting rights

On a show of hands every member present in person or by proxy shall have one vote and upon a poll each share shall have one vote.

ADDITIONAL INFORMATION REQUIRED FOR LISTED COMPANIES**Schedule of interests**

As at 22 August 2005	Interest
Exploration Permits	%
PEP 162 Gippsland Basin	100
EL 4537 Gippsland Basin	100
WA-314-P	(i) 40
WA-315-P	(i) 40

Note (i) Subject to the completion by BG International to complete a minimum of 400 kilometres of 3D seismic acquisition in each permit. The above interests are held by Karoon Gas Pty Ltd and Karoon Gas Australia Ltd.

Karoon Gas Australia Limited

ABN 53 107 001 338

CORPORATE DIRECTORY

Directors

Mr R Hosking – Executive Chairman
Mr M Smith – Executive Director
Mr Geoff Atkins – Non-Executive Director
Mr Stephen Power – Non-Executive Director

Company Secretary

Mr Hector Peeters

Audit Committee

Mr Robert Hosking
Mr Hector Peeters
Mr Geoff Atkins

Auditors

Mitchell Wilson & Partners
261 -271 Wattleree Road
Malvern VIC 3144
Telephone: (03) 9500 0533
Facsimile: (03) 9500 0633

Bankers

National Australia Bank Limited
271 Collins Street
MELBOURNE VIC 3000
Telephone: (03) 9659 7600
Facsimile: (03) 9659 7902

Registered Office and Head Office

Suite 7A, 34 – 38 Lochiel Avenue
Mt Martha VIC 3934
Telephone: (03) 5974 1044
Facsimile: (03) 5974 1644
Email: rhosking@karoongas.com.au
Website: www.karoongas.com.au

Location of Share Registry

Computershare Investor Services Pty Ltd
Reserve Bank Building
Level 2, 45 St George's Terrace
PERTH WA 6000
Telephone: (08) 9323 2023
Website: www.computershare.com

Stock Exchange

The Company is listed on the Australian Stock Exchange.
The Home Exchange is Melbourne, Victoria.

Other Information

Karoon Gas Australia Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.

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