



Falkland Oil and Gas is exclusively focused on offshore oil and gas exploration in the Falkland Islands.

Our objective is to define and prioritise about 20 prospects for drilling which could begin in 2007.

- > We are an oil and gas exploration company operating in the vast undrilled yet prospective south and east Falkland Basins.
- > We were admitted to London's Alternative Investment Market ("AIM") on 14 October 2004 and completed a placing and offer for subscription at an issue price of 40p raising £12 million before expenses.
- > Our licences cover 83,600 sq km; an area equivalent to 330 North Sea style blocks. FOGI has average equity of 90% in its licence areas.
- > Formed in May 2004, this is our first annual report and accounts.

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Highlights

27 May Falkland Oil and Gas formed

14 October Admission to AIM and successful placing and offer for subscription of New Ordinary Shares raising £12 million before expenses

7 December Awarded 100% licence for additional 50,000 sq km

28 December Commenced 9,450 km 2D seismic survey

11 March Richard Liddell appointed as a Non-Executive Director

7 April Patrick Bird appointed as Exploration Manager

3 May Announced preliminary results from 2D seismic – encouraging results exceed expectations

31 May £10 million placing of New Ordinary Shares (before expenses)



February 2005 David Hudd and John Armstrong alongside the GSI Admiral in Port Stanley, Falkland Islands. The GSI Admiral completed 9,450 km of 2D seismic data surveys over FOGL's licence areas.

Chairman's statement

Falkland Oil and Gas Limited ("FOGL") was formed in May 2004 to invest in an offshore oil exploration programme covering approximately 33,700 sq km south and east of the Falkland Islands. It was admitted to AIM in October 2004, raising £12 million (before expenses) through a simultaneous placing and offer for subscription. At that time, FOGL held a 77.5% interest in seven offshore production licences granted by the Government of the Falkland Islands. Hardman Resources Limited holds the remaining 22.5% interest in these licences.

Results

FOGL has made a great deal of progress since its IPO. In December 2004, the Company was awarded 100% interests in a number of licences over an additional 50,000 sq km adjacent to its existing licence areas. The 83,600 sq km area now held is equivalent to 330 North Sea style blocks prior to licence relinquishments: as large as the Southern Gas Basin and the Central Graben combined.

In December 2004 FOGL also commenced a 2D seismic survey. Initially planned to be 3,500 km, by completion in April the survey had covered 9,450 km and from preliminary data we have identified more than 130 leads, far in excess of the 8 leads identified at the time of the IPO.

The survey has indicated a larger and more diverse project than originally anticipated and has identified numerous possible drill targets, with indications that some could be of significant size. FOGL plans to conduct further seismic surveys targeting all the leads but with particular emphasis on the 50 most promising. The aim will be to develop about 20 high quality, technically sound and potentially economically viable drilling prospects.

Management

During the period, the Company also strengthened the management team. As anticipated at the time of the IPO, a second Non-Executive Director, Richard Liddell, has been appointed. He has twenty-five years experience in the oil and gas industry. Richard was Operations Director of Premier Oil plc from 1999 until 2003 and prior to that spent two years as Director of Development at BG Exploration and Production.

The expanded scale of the project required a full time Exploration Manager, and Patrick Bird joined FOGL to fill that role in April. Patrick has twenty-four years experience in the oil and gas industry including nine years at Premier Oil plc fulfilling various roles such as General Manager Exploration and General Manager, Pakistan.

Patrick replaces Jim Webb who had been acting as Project Manager for FOGL on a part-time basis and felt unable to commit to a full-time role. The Board wishes to thank Jim for his invaluable contribution to the Company, particularly during the IPO process.



A handwritten signature in white ink on a dark grey background, appearing to read "John D Armstrong".

John D Armstrong
Executive Chairman
9 June 2005

"Our objective now is to define and prioritise about 20 prospects for drilling which could begin in 2007."

“This is the most exciting project I’ve seen in many years.”

Objectives

The clear objective for FOGL is to deliver significant value to shareholders by progressing an aggressive yet focussed exploration programme. We intend to achieve this by conducting further 2D seismic in the second half of 2005 and possibly a 3D seismic survey. The Company then intends to develop a multi-well drilling programme which will be planned to begin in 2007.

In May, FOGL raised an additional £10 million (before expenses) through a placing of new ordinary shares at a price of 85p per share. These funds, together with existing cash resources, will be sufficient, in the opinion of the Directors and on the basis of current estimates, to fund our exploration plans and cover the Company’s overheads through 2006.

FOGL is also seeking to introduce new companies to the project across some or all of the licence acreage in the coming months by way of farmout or another appropriate arrangement. This approach targets the introduction of experienced oil and gas industry companies who can share the risk and upside in our project – but leaving sufficient equity with the Company to the benefit of FOGL shareholders.

The Falkland Islands

We continue to work closely with the Governor of the Falkland Islands and Falkland Islands Government representatives and Officials.

Outlook

At the time of the IPO, FOGL had a market capitalisation of £32 million. Since then the Company’s share price has increased significantly reflecting both the market’s interest in the project and the work that we have completed to date. The Board’s focus is on progressing the exploration programme with the aim of delivering significant value to shareholders.

“Significant progress has been made in the first year and there is already an enhanced possibility of the project being a success.”



John D Armstrong
Executive Chairman
9 June 2005

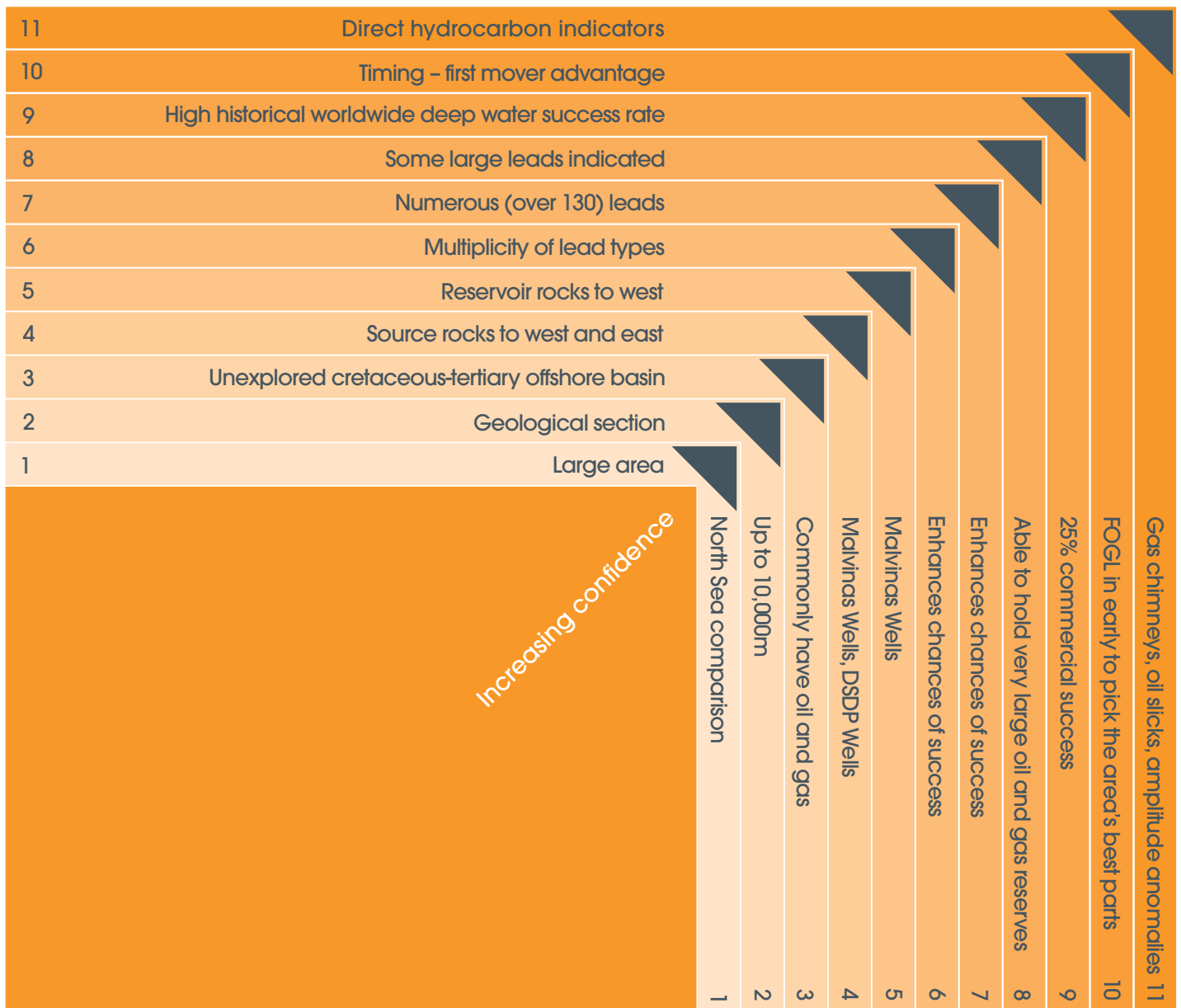
Operating and financial review

Operating review

Since the year-end, we have completed a 9,450 km 2D seismic survey which identified over 130 leads, across a number of different play types. The new seismic also indicated the presence of hydrocarbons as shown by gas chimneys and extensive amplitude anomalies. These together with the good oil source rocks drilled in the east of the basin (DSDP holes 330 and 511) provide evidence of a working oil and gas system in FOGL's area.

There are additional reasons to be optimistic. The licences cover an unexplored Cretaceous / Tertiary basin. Such types of basins hold the majority of the world's oil and most of them contain oil and gas. In addition, there are up to 10,000 metres of geological sedimentary section which is enough to contain plenty of source rocks, reservoirs and seals.

The following diagram sets out these particular features which make our project interesting:



“Initial results have exceeded expectations. The indications are that this is a larger and more diverse project than anticipated.”

Some of the leads are sizeable, ranging from 300 to 500 sq km. The new seismic data also indicate the presence of hydrocarbons as shown by gas chimneys and extensive amplitude anomalies.

Mapping of the recent seismic continues. Meantime a further 2D seismic survey has begun. The program comprises a committed 8,000 km through a further contract with GSI and this may be extended to 15,000 km. The Company is also considering a 3D seismic survey. The results of this work will be processed and interpreted to help us define an inventory of about 20 high-grade prospects. The target is to get a multi-well drilling programme in place and to begin drilling in 2007.

Two independent petroleum consultancies, Scott Pickford and MBA have each examined the initial processed seismic sections and verified that the conclusions the Company has drawn from that data, concerning the potential number of leads and the potential for those to contain hydrocarbons, are reasonable.



Patrick Bird
Exploration Manager
9 June 2005

“Encouraging signs that oil and gas could be present.”

Financial review

The financial results for the period to 31 March 2005 include the 10 months since the Company's formation on May 2004 and reflect its IPO and placing and offer for subscription in October 2004, which raised £12 million before expenses. On 3 June 2005, FOGL completed the placing of a further 11.8 million shares at 85p per share, raising a further £10 million before expenses.

Operating loss

The operating loss for the period was £460,133. After interest income, the loss on ordinary activities before taxation was £293,692.

Cash flow

Net cash outflow from operating activities for the period was £122,302. At the period-end, FOGL had cash of £11 million and was debt free.

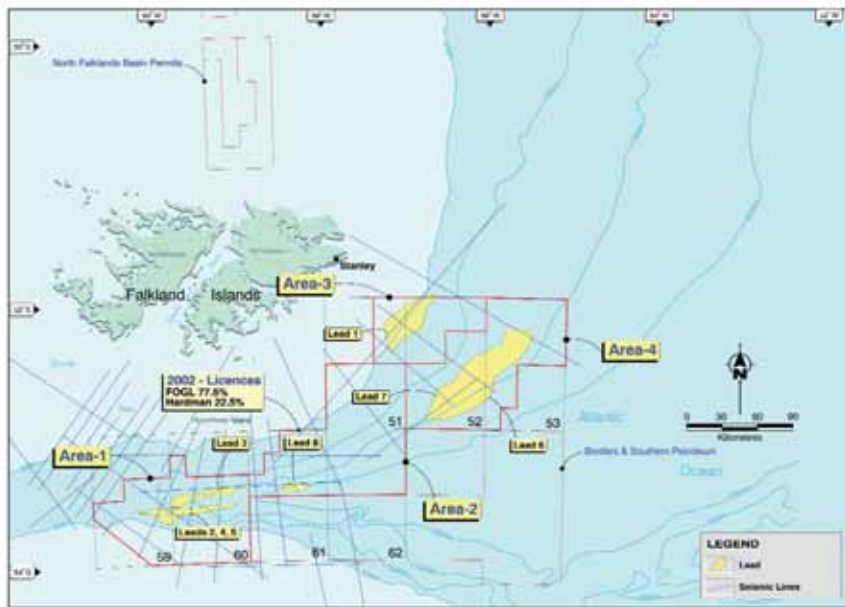
FOGL is currently in the process of recruiting a full time Financial Controller. Strengthening the finance team will help to ensure that the Company continues its focus on strong financial controls and can fully fund its extensive exploration programme.



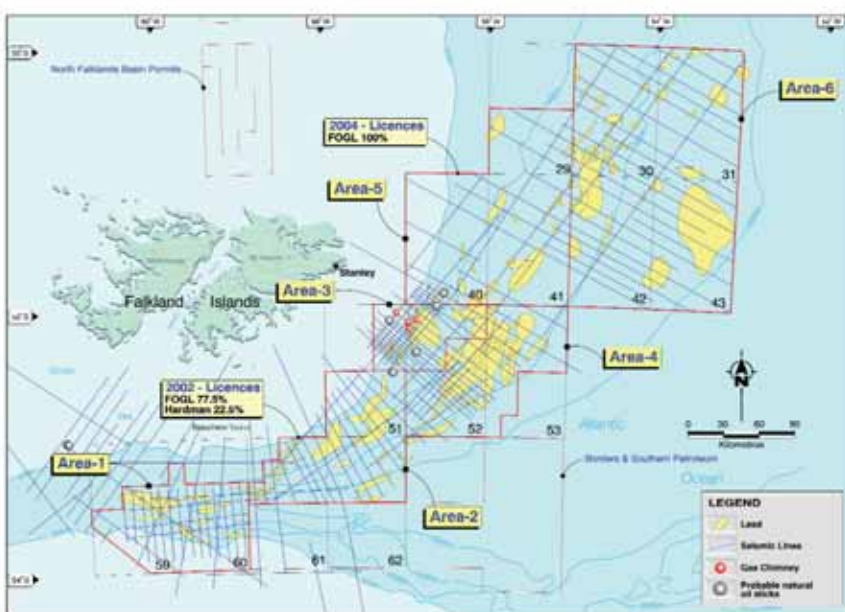
Timothy Jones
Finance Director
9 June 2005

Technical review

At the IPO, FOGL had identified 8 leads in a 33,700 sq km licence areas in which it holds a 77.5% interest.

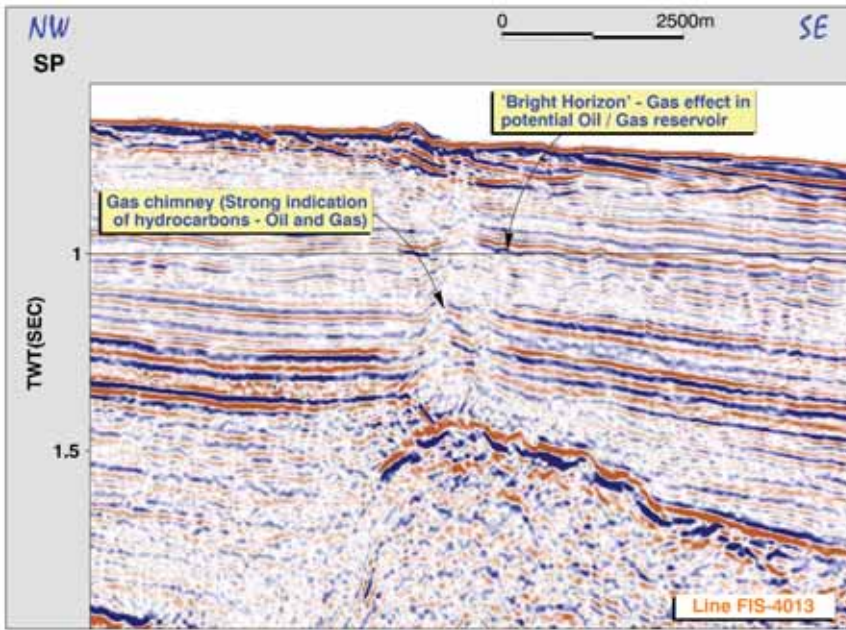


FOGL has now identified more than 130 leads spread across its initial licence area and the additional 50,000 sq km licence that was awarded 100% to FOGL in December 2004.

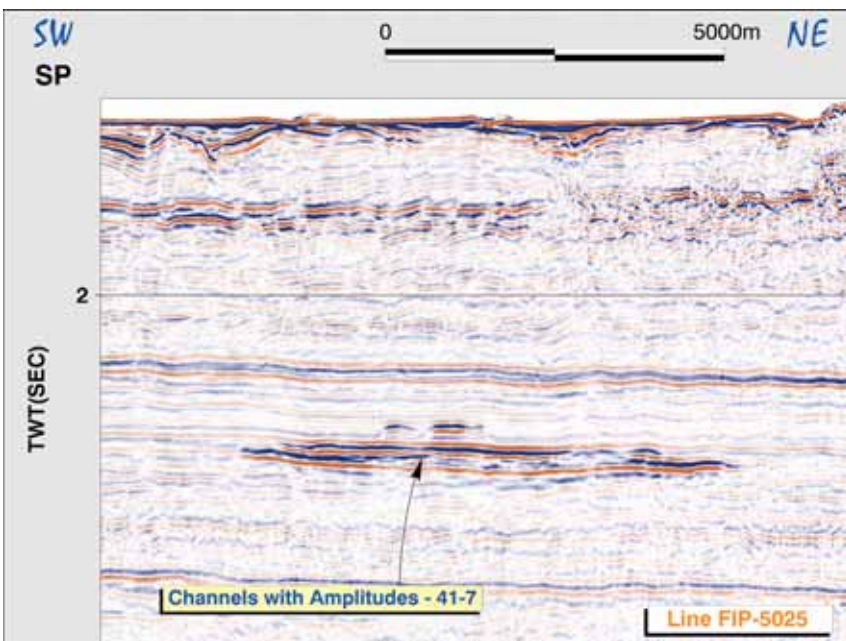


Notes:
 "Areas" referred to were defined for purpose of segmenting and presenting the large number of leads in the May reports posted on the Company's website.

The 19 Block relinquishment is being progressed which will reduce Block numbers to 311 and the total area to 78,898 sq km.



New seismic section showing gas and possibly oil leaking to the sea bed. Oil usually occurs together with the gas in these features. The bright horizon on this line is 12 km across.



New seismic section showing high amplitudes within a channel sand. This signifies the likely presence of gas possibly together with oil.

The Board and senior management



01	04
02	05
03	06

01 John Dennis Armstrong

Executive Chairman

Dr Armstrong joined the Board of the Company on its establishment. He joined Global Petroleum, an Australian listed company and one of the Company's major shareholders, in June 2002 as Executive Chairman. Dr Armstrong has had a 30 year career in the upstream oil and gas industry – most recently as a General Manager of Santos and before that as Exploration Manager for UNOCAL's Indonesian operations. He has a successful track record of finding and developing oil and gas fields. Dr Armstrong played an important role in growing Santos from a small local gas company to a company with operations throughout Australia and internationally.

04 Timothy Stephen Jones FCA

Finance Director

Timothy Jones qualified as a Chartered Accountant with Price Waterhouse in 1974 where his clients included a major UK offshore oil and gas operator. In 1983, he left Price Waterhouse to join a client as Financial Director before founding his own accountancy and consultancy practice in 1990. He now has clients in a range of business sectors and sits on the boards of a number of private companies. Mr Jones joined the Board in September 2004.

02 David Leslie Hudd FCA**

Deputy Chairman – Non-Executive

David Hudd, a Chartered Accountant, was a partner in Price Waterhouse until 1982. Since then he has been Chairman or Chief Executive of a number of listed companies, including, from 1992 to April 1998, Vardon plc, now Cannons Group PLC, a company he founded. He is currently Executive Chairman of Falkland Islands Holdings plc which he joined in March 2002 and which is a major shareholder in the Company. Mr Hudd is Non-Executive Chairman of API Group plc and of Betcorp Limited, an Australian listed company. He is also a Non-Executive Deputy Chairman of Falkland Gold and Minerals Limited and a Non-Executive Director of QA plc. Mr Hudd joined the Board on the formation of the Company in June 2004.

05 Richard Liddell**

Non-Executive Director

Richard Liddell joined the Board in March 2005 and has twenty-five years experience in the oil and gas industry. Richard was Operations Director of Premier Oil plc from 1999 until 2003 and prior to that spent two years as Director of Development at BG Exploration and Production. He previously held a number of positions during an eighteen-year spell at Phillips Petroleum Company.

03 Peter Francis Dighton

Commercial Director

Peter Dighton joined the Board in August 2004. A lawyer specialising in the planning, structuring and documentation of major energy projects and transactions, he is principal of Law Strategies Pty Ltd. Mr Dighton has undertaken projects in Australia, Papua New Guinea, Indonesia, India, Europe and the Middle East on behalf of oil majors, listed companies and government owned corporations. Mr Dighton is also a Director of Global Petroleum.

06 Patrick Bird

Exploration Manager

Patrick Bird joined FOGL in April 2005. He has twenty-four years experience in the oil and gas industry. For the previous nine years he worked for Premier Oil fulfilling various roles including: General Manager Exploration and General Manager, Pakistan. He has previously held exploration roles at Dragon Oil and at Scott Pickford, a consultancy specialising in geology, geophysics and petroleum engineering analyses. He began his career as a Petroleum Engineer for Shell International in 1981.

+ Audit Committee members

* Remuneration Committee members

Officers and advisers

Directors

John Armstrong Executive Chairman
David Hudd Deputy Chairman – Non-Executive
Peter Dighton Commercial Director
Timothy Jones Finance Director
Richard Liddell Non-Executive Director

Secretary

Chalmers Nominee Company (Falklands) Limited

Registered office

56 John Street, Stanley,
Falkland Islands, FIQQ 1ZZ

Nominated adviser and broker

KBC Peel Hunt Ltd

Bankers

Lloyds TSB Bank plc

Auditors

KPMG Audit Plc
Chartered Accountants

Solicitors

United Kingdom – Norton Rose
Falkland Islands – Ledingham Chalmers

Financial PR

College Hill Associates

Registrars

Capita IRG plc

Falkland Oil and Gas Limited is listed on the Alternative Investment Market (AIM) of the London Stock Exchange (symbol FOGL)

Contact details

Falkland Oil and Gas Limited
5 Charterhouse Square
London EC1M 6PX
t: +44 (0) 20 7490 4111
f: +44 (0) 20 7253 9208
e: info@fogl.co.uk
www.fogl.com

Social responsibility statement

The Company supports the growing awareness of social, environmental and ethical matters when considering business practices. This statement provides an outline of the policies that guide the Company and its employees when dealing with social, environmental and ethical matters in the workplace.

Code of conduct

The Company maintains and requires the highest ethical standards in carrying out its business activities in regard to dealing with gifts, hospitality, corruption, fraud, the use of inside information and whistle-blowing.

Equal opportunity and diversity

The Company promotes and supports the rights and opportunities of all people to seek, obtain and hold employment without discrimination. It is our policy to make every effort to provide a working environment free from bullying, harassment, intimidation and discrimination on the basis of disability, nationality, race, sex, sexual orientation, religion or belief.

Employee welfare

The Company aims to assist employees at all levels to improve their professional abilities and to develop their skills.

The Company will practice manpower and succession planning in regard to the quantity and type of employee resources that will be required in the future. Individual career progression activities are developed with this in mind.

Joint venture partners, contractors and suppliers

The Company is committed to being honest and fair in all its dealings with its partners, contractors and suppliers. The terms of business used by the Company aim to provide clarity and protection, and to ensure the delivery and receipt of products and services at agreed standards. The Company also closely guards information entrusted to it by its joint venture partners, contractors and suppliers, and seeks to ensure that it is never used improperly.

Operating responsibly and continuous improvement

The Company is committed to a proactive quality policy to ensure that stakeholders are satisfied with the Company's results and the way in which the business operates and to promote continuous improvement in the overall operation of the Company. In pursuit of these objectives, the Company will use recognised standards and models as benchmarks for its management system.

Environmental policy

The Company will adopt an environmental policy which will be reviewed regularly to set standards in compliance with industry guidelines and host government regulations.

Remuneration report

Remuneration Committee

The Company's Remuneration Committee comprises David Hudd and Richard Liddell.

The purpose of the Remuneration Committee is to:

- > make recommendations to the Board on an overall remuneration policy for Executive Directors and other senior executives in order to retain, attract and motivate high quality executives capable of achieving the Company's objectives; and
- > demonstrate to shareholders that the remuneration of the Executive Directors of the Company is set by a committee whose members have no personal interest in the outcome of their decision, and who will have due regard to the interests of the shareholders.

Procedures for developing policy and fixing remuneration

The Board has shown a commitment to formalising procedures for developing a remuneration policy, fixing executive remuneration and ensuring that no Director is involved in deciding his or her own remuneration. The Committee is authorised to obtain outside professional advice and expertise, and consults with the Chairman of the Company as necessary.

The Remuneration Committee is authorised by the Board to investigate any matter within its terms of the reference. It is authorised to seek any information that it requires from any employee.

Details of the remuneration policy

The basic fees to be paid to the Directors are recommended by the Remuneration Committee, and are subject to approval by the full Board.

Share options

The Company operates a share option scheme pursuant to which Directors and senior executives may be granted options to acquire ordinary shares in the Company at a fixed option price. During the period options were granted over a total of 2,044,100 ordinary shares.

Directors' service agreements

All service agreements for Directors are terminable by either party on between six and twelve months notice.

Directors' emoluments

The following emoluments were paid to Directors during the period ended 31 March 2005:

	£
John Armstrong	91,267
David Hudd	14,583
Peter Dighton	15,000
Timothy Jones	14,453
Richard Liddell	1,731
	137,034

Remuneration report continued

Directors' interests in shares

The Directors who held office at the end of the period and subsequently had the following interests in the issued share capital of the Company according to the register of Directors' interests.

	03/06/05	31/03/05
John Armstrong	50,000	25,000
David Hudd	300,000	250,000
Peter Dighton	36,765	25,000
Timothy Jones	163,235	75,000
Richard Liddell	58,824	-

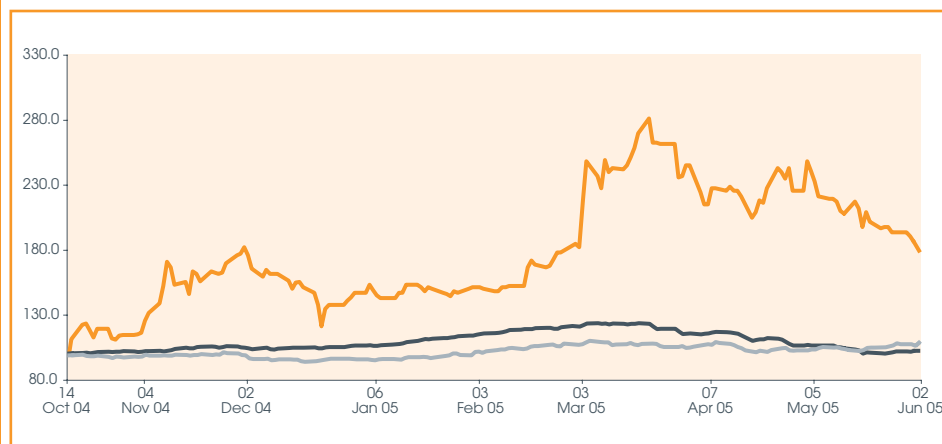
Directors' share options

The Directors who held office at the end of the financial period had the following interests in share options:

	Number of shares			Exercise dates	
	Exercise price of 40p	Exercise price of 60p	Exercise price of 127p	from	to
John Armstrong	375,000	375,000	-	13 October 2005	12 October 2011
David Hudd	225,000	225,000	-	13 October 2005	12 October 2011
Peter Dighton	150,000	150,000	-	13 October 2005	12 October 2011
Timothy Jones	150,000	150,000	-	13 October 2005	12 October 2011
Richard Liddell	-	-	118,100	24 March 2006	23 March 2012

The interests of the Directors to subscribe for ordinary shares have not changed since the period end.

Total shareholder return



Source: Perfect Analysis

The above graph compares the share price performance of the Company (by reference to total shareholder return) with that of the FTSE AIM and FTSE All-Share Oil and Gas sector.

By order of the Board

David Hudd
Chairman of the Remuneration Committee
9 June 2005

Corporate governance

The Combined Code

Falkland Oil and Gas Limited's shares are traded on AIM and as such FOGL is not subject to the requirements of the Combined Code on corporate governance, nor is it required to disclose its specific policies in relation to corporate governance.

The Board of Directors operates within the framework described below.

The workings of the Board and its Committees

The Board of Directors

The Board meets frequently to consider all aspects of the Company's activities. A formal schedule of matters reserved for the Board includes overall strategy and approval of major capital expenditure.

The Board consists of the Chairman, Deputy Chairman, Commercial Director, Finance Director, and an additional Non-Executive Director. All Directors have access to the advice and services of the Company Secretary and the Company's professional advisers.

Remuneration Committee

The Remuneration Committee comprises David Hudd and Richard Liddell, and is chaired by David Hudd. Its terms of reference are discussed in the remuneration report.

	Board
No. of meetings	8
Attendance	
John Armstrong	8
David Hudd	8
Peter Dighton	8
Timothy Jones	7
Richard Liddell*	5

*Richard Liddell joined the Board in March 2005.

Audit Committee

The Audit Committee comprises David Hudd and Richard Liddell, and is chaired by David Hudd. It is responsible for ensuring that the financial performance of the Company is properly reported on and monitored, and for reviewing the auditors' reports relating to accounts and internal control systems.

Relations with shareholders

Communications with shareholders are given a high priority by the Board of Directors who take responsibility for ensuring that a satisfactory dialogue takes place. Directors plan to meet with the Company's institutional shareholders following the announcement of interim and final results and at other appropriate times. The Directors are also in regular contact with stockbrokers' analysts. The Company has developed a website containing investor information to improve communications with individual investors and other interested parties.

Internal control

The Directors acknowledge their responsibility for the Company's system of internal control and for reviewing its effectiveness. The system of internal control is designed to manage the risk of failure to achieve the Company's strategic objectives. It cannot totally eliminate the risk of failure but will provide reasonable, although not absolute, assurance against material misstatement or loss.

Going concern

The Directors consider that the Company has adequate financial resources to enable it to continue in operation for at least 12 months. For this reason they continue to adopt the going concern basis in preparing the Financial Statements.

Directors' report

The Directors present their report and the financial statements for the period ended 31 March 2005.

Incorporation

The Company was incorporated in the Falkland Islands on 27 May 2004.

Principal activity and review of the business

The principal activity of the Company is that of oil and gas exploration.

Results and dividends

The results for the period are set out on page 16.

The Directors do not recommend payment of a final dividend.

Review of business and future developments

A review of the business and likely future developments of the Company are contained in the Chairman's statement on page 2 and 3.

Directors and Directors' interests

The Directors of the Company during the year are noted on page 8.

Details of Directors' interests in shares and share options are disclosed in the Remuneration Report on page 11 and 12.

Substantial shareholdings

At 3 June 2005, the Board had been formally notified of the following interests representing 3% or more of the Company's issued share capital.

	No. of Shares	Percentage of Issued Share Capital
RAB Capital plc	26,300,000	28.6
Falkland Islands Holdings plc	16,802,941	18.3
Dampier Oil Ltd	12,850,000	14.0

Note:

Dampier Oil Ltd is a wholly owned subsidiary of Global Petroleum Ltd.

Auditors

There will be a special resolution to re-appoint KPMG Audit Plc at the forthcoming Annual General Meeting and KPMG Audit Plc has acknowledged its willingness to accept.

Approved by the Board of Directors and signed on behalf of the Board.



Timothy Jones
Finance Director
9 June 2005

Statement of Directors' responsibilities

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

- > select suitable accounting policies and then apply them consistently;
- > make judgements and estimates that are reasonable and prudent;
- > state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- > prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1948. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Profit and loss account

for the 10 month period ended 31 March 2005

	Notes	10 month period ended 31/03/05 £
Administrative expenses		(460,133)
Operating loss	2	(460,133)
Interest income	3	166,441
Loss on ordinary activities before taxation		(293,692)
Tax on loss on ordinary activities	6	-
Loss on ordinary activities after taxation		(293,692)
Loss for the period		(293,692)
Loss per ordinary share – Basic and diluted	7	(0.48p)

There were no recognised gains or losses in the period other than those dealt with in the profit and loss account above.

The operating loss for the period arose from continuing operations.

Balance sheet

at 31 March 2005

	Notes	At 31/03/05 £	At 31/03/05 £
Fixed assets			
Intangible fixed assets	8		2,866,836
Tangible fixed assets	9		11,277
			2,878,113
Current assets			
Debtors	10	75,434	
Cash at bank and in hand		11,079,976	
		11,155,410	
Creditors: amounts falling due within one year	11	(656,844)	
Net current assets			10,498,566
Net assets			13,376,679
Capital and reserves			
Called up share capital	12		1,600
Share premium account	13		13,668,771
Profit and loss account	13		(293,692)
Shareholders' equity funds			13,376,679

These financial statements were approved by the Board on 9 June 2005 and signed on its behalf by



David Hudd
Director



Timothy Jones
Director

Cash flow statement

for the period ended 31 March 2005

	Period ended 31/03/05 £
Net cash outflow from operating activities	122,302
Returns on investments and servicing of finance	
Interest received	166,441
Capital expenditure and financial investment	
Expenditure in respect of intangible fixed assets	(2,866,836)
Expenditure in respect of tangible fixed assets	(12,302)
Cash outflow before financing	(2,590,395)
Financing	
Issue of ordinary share capital	14,697,514
Issue costs	(1,027,143)
	13,670,371
Increase in cash in the period	11,079,976
Reconciliation of operating loss to net cash outflow from operating activities	
Operating loss	(460,133)
Depreciation	1,025
Increase in debtors	(75,434)
Increase in creditors	656,844
Net cash outflow from operating activities	122,302

Reconciliation of movements in shareholders' equity funds

for the 10 month period ended 31 March 2005

	10 month period ended 31/03/05 £
Loss for the financial period	(293,692)
New share capital subscribed (net of issue costs)	13,670,371
Net addition to shareholders' equity funds	13,376,679
Opening shareholders' equity funds	-
Closing shareholders' equity funds	13,376,679

Notes to the financial statements

For the 10 month period ended 31 March 2005.

1. Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material to the financial statements.

1.1. Basis of preparation

The financial statements are prepared in accordance with applicable UK accounting standards and under the historical cost convention on a going concern basis.

The financial statements fall within the scope of the UK Oil Industry Accounting Committee's Statement of Recommended Practice "Accounting for Oil and Gas Exploration, Development, Production and Decommissioning Activities" and have been prepared in accordance with its provisions.

In common with many exploration companies, the Company raises finance for its exploration and appraisal activities in discrete tranches. Further funding is raised as and when required. When any of the Company's projects move to the development stage, specific financing will be required.

1.2. Joint arrangements

The Company has certain contractual arrangements with other participants to engage in joint activities that do not create an entity carrying on a trade or business of its own. The Company includes its share of assets, liabilities and cash flows in joint arrangements, measured in accordance with the terms of each arrangement, which is usually pro rata to the Company's interest in the joint arrangement.

1.3. Capitalisation of oil and gas expenditure

The Company applies the full-cost method of accounting under which all expenditure relating to the acquisition, exploration, appraisal and development of oil and gas interests, including an appropriate share of overheads, is capitalised. Capitalised costs are amortised on a unit of production basis. The Board regularly reviews the carrying values of intangible assets and writes down capitalised expenditure to the extent considered impaired. If no discoveries are made, the accumulated capitalised costs will be written off through the profit and loss account.

1.4. Deferred taxation

The charge for taxation is based on the results for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Full provision is made for the tax liability on all timing differences in accordance with FRS 19. Deferred tax balances are not subject to discounting.

1.5. Foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange prevailing at the balance sheet date. Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Exchange differences are taken to the Profit and Loss account.

1.6. Depreciation

Fixed assets are depreciated using the straight line method over their estimated useful lives, as follows:

Fixtures, fittings and equipment	4 years
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1.7. Leases

Operating lease rentals are charged to the profit and loss account on a straight line basis over the period of the lease.

1.8. Cash

Cash, for the purposes of the cash flow statement, comprises cash at bank and short term deposits.

Notes to the financial statements continued

2. Operating loss

10 month
period
ended
31/03/05
£

Operating loss is stated after charging:

Depreciation and other amounts written off tangible assets	1,025
Auditors' remuneration	30,000

3. Interest income

10 month
period
ended
31/03/05
£

Bank interest	166,441
---------------	---------

4. Employees

10 month
period
ended
31/03/05
£

Number of employees

The average monthly number of employees (including the Directors) during the period was:	3
--	---

Employment costs

Wages and salaries	140,286
Social security costs	4,820

5. Directors' emoluments

Details of Directors' emoluments are disclosed in the remuneration report on page 11.

6. Taxation

Factors affecting the tax charge for the current period

The current tax charge for the period is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below.

10 month period
ended
31/03/05
£

Current tax reconciliation

Loss on ordinary activities before tax	(293,692)
Current tax at 30%	(88,108)

Effects of:

Expenses not deductible for tax purposes	-
Tax losses carried forward	85,512
Pre-trading expenditures carried forward	2,596
Total current tax charge	-

Factors that may affect future current and total tax charges

The Company had tax losses carried forward on which no deferred tax asset is recognised. This may affect future tax charges should the Company produce taxable profits in the future periods.

Notes to the financial statements continued

7. Loss per share

The calculation of basic loss per ordinary share is based on a loss of £293,692 and on 61,510,000 ordinary shares, being the weighted average number of ordinary shares in issue during the period. There is no difference between the diluted loss per share and the basic loss per share presented as the Company reported a loss for the period and, in accordance with Financial Reporting Standard Number 14, the share options in issue are not considered dilutive.

8. Intangible fixed assets

	Exploration and appraisal costs £
Cost	
Additions	2,866,836
At 31 March 2005	2,866,836
Net book value	
At 31 March 2005	2,866,836

9. Tangible fixed assets

	Fixtures, fittings and equipment £
Cost	
Additions	12,302
At 31 March 2005	12,302
Depreciation	
Charge for the period	1,025
At 31 March 2005	1,025
Net book value	
At 31 March 2005	11,277

10. Debtors

	31/03/05 £
Sundry debtors	51,580
Prepayments and accrued income	23,854
	75,434

11. Creditors: amounts falling due within one year

	31/03/05 £
Trade creditors	24,992
Other taxes and social security costs	2,239
Other creditors	391
Accruals	629,222
	656,844

Notes to the financial statements continued

12. Share capital

31/03/05
£

Authorised	
120,000,000 Ordinary shares of 0.002p each	2,400
Allotted, called up and fully paid	
80,000,000 Ordinary shares of 0.002p each	1,600

- (a) The Company was incorporated with an authorised share capital of £2,000 divided into 2,000 ordinary shares of £1 each of which two were issued to the subscribers to the memorandum of association.
- (b) In consideration for Dampier Oil Limited ("Dampier"), Falkland Islands Company Limited ("FIC") and RAB Special Situations LP ("RAB") agreeing to pay subscription funds of US\$1.1 million, US\$0.5 million and US\$2.2 million respectively pursuant to a share subscription agreement dated 23 June 2004 and in consideration for FIC and Dampier agreeing to assign to the Company their Participating Interests in the relevant exploration licences, 289 shares, 257 shares, 454 shares (each of £1) were received by FIC, Dampier and RAB respectively.
- (c) On 30 September 2004, resolutions of the Company were passed:
- (i) subdividing each ordinary share of £1 each in the capital of the Company into 50,000 Shares of 0.002p each;
 - (ii) increasing the authorised share capital of the Company from £2,000 to £2,400 by the creation of an additional 20,000,000 Shares of 0.002p each; and
 - (iii) adopting new Articles of Association.
- (d) On 14 October 2004, under the terms of a placing and offer for subscription, 30,000,000 ordinary shares of 0.002p each were issued for cash at 40p per share.
- (e) On that date, the Company's shares were admitted to trading on the Alternative Investment Market of London Stock Exchange.

13. Reserves

	Share premium account £	Profit and loss account £
Premium on issue of shares	14,695,914	-
Loss for the period	-	(293,692)
Expenses of share issue	(1,027,143)	-
At 31 March 2005	13,668,771	(293,692)

Notes to the financial statements continued

14. Commitments

Commitments at the balance sheet date were as follows:

- (a) The Company has entered into a joint venture agreement with Hardman Resources Limited whereby it agreed to fund 80% of the expenditure on certain joint operations relating to the seismic survey conducted in late 2004 through April 2005. The agreed maximum joint venture expenditure is US\$4,500,000. After that figure is met further operations are to be funded by the Company and Hardman Resources Limited in accordance with their participating interests (77.5%/22.5%).
- (b) The Company has entered into a Seismic Agreement with ECL Pty Ltd for the provision of consulting services in relation to an offshore seismic programme in the Falkland Islands. The total commitment is for US\$82,500.
- (c) As a result of the conclusion of the survey referred to in 1, the Company has assumed its participating interest share (77.5%) including amounts which may be payable in the future under an agreement between the original joint venture participants and WesternGeco for the acquisition of seismic data. That agreement provides for payment to WesternGeco of a Drilling Bonus of US\$500,000 for the first well and US\$250,000 for each subsequent well, and a payment of 25% of net profit on the sale of any interests in the Petroleum Licences, up to a total maximum of US\$1,650,000.

The potential total amount payable by the Company under this commitment is US\$1,278,750.

- (d) The Company has entered into agreements with GSI for the acquisition of approximately 5,000 km of 2D seismic in the area held by it 100% and (through the operator Dampier Oil Limited) for approximately 4,000 km of 2D seismic in the area held with Hardman. The Company was granted non-exclusive licences to use the data acquired. The commitment to GSI was US\$1.5 million, apportioned across the areas, for mobilisation and demobilisation, together with kilometre rates for data depending on the streamer length.

15. Related party transactions

Management fees of £44,672 were paid to Dampier Oil Limited, a shareholder, during the period. Fees of £26,866 were paid to Law Strategies Pty, a Company controlled by Mr Dighton, during the period. Fees of £12,600 were paid to Timothy Jones and Co, a practice of which Mr Jones is principal, during the period.

16. Subsequent events

On 31 May 2005, the Company announced that it had placed 11,764,706 ordinary shares of 0.002p at a price of 85p per share, raising £10 million before expenses. This was completed on 3 June 2005.

Independent auditors' report to the members of Falkland Oil and Gas Limited

We have audited the financial statements on pages 16 to 23.

This report is made solely to the company's members, as a body, in accordance with the Companies Act 1948. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Directors' report and, as described on page 15, the financial statements in accordance with applicable Falkland Islands law and accounting standards. Our responsibilities, as independent auditors, are established in the Falkland Islands by statute, the UK Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1948. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the Company is not disclosed.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of the Company's affairs as at 31 March 2005 and of its loss for the period then ended and have been properly prepared in accordance with the Companies Act 1948.

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor
9 June 2005

Contact details
Falkland Oil and Gas Limited
5 Charterhouse Square
London EC1M 6PX
t: +44 (0) 20 7490 4111
f: +44 (0) 20 7253 9208
e: info@fogl.co.uk
www.fogl.com