Newfield Petroleum UK Limited

Directors' Report and Financial Statements
Year ended 31 December 2005

Registered number: 4487586

Directors' report

For the period ended 31 December 2005

The directors present their annual report on the affairs of the company, together with the financial statements and auditors' report for the year to 31 December 2005.

Principal activities and business review

Newfield Petroleum UK Limited ("Newfield") was incorporated on 16 July 2002. During the year the issued share capital was increased from 203,250 shares to 379,983 shares (£20,325,000 to £39,756,000).

During 2004, Newfield completed an acquisition of interests in six blocks in the Cleaver Bank North area of the Southern North Sea gas basin from Shell/Exxon and on 26th November 2004, the company, as operator, spudded the 49/10a-4 Grove well. This well was completed in February 2005 having found about 120 feet (net) of gas pay in the Leman and Barren Red Measures Sands. The 49/10a-5 appraisal well was spudded on 27th December 2005 and was suspended as a producer on 7th April 2006 and the 49/10a-6 well at the West Grove location was spudded on 9th June 2006. The development plan for the Grove gas field was approved by the Board and a production platform was installed during July 2006. First production is planned for late 2006.

The 47/10-8 Newark well, in which the company has a 60% interest, was spudded on 20th February 2005 but was unsuccessful and was plugged and abandoned as a dry hole.

In December, it was announced that the company had been awarded licences for blocks 47/5b, 48/7c and 48/8 as a result of a successful application in the 23rd Licensing Round. The company also made an application for blocks in the 24th Licensing Round in June 2006.

In June 2005, the sale of the company's interests in Windermere, Chiswick and block 49/4b was completed.

Future developments

The company is pursuing various acquisition and farm-in opportunities, in order to acquire a portfolio of interests and to find and develop significant new reserves.

Results and dividends

The company made a loss after taxation of £1,373,814 (2004 £10,254,755) for the year to 31 December 2005. The directors do not recommend the payment of a dividend.

Policy and practice on payment of creditors

It is company policy to agree settlement terms with suppliers of payment within thirty days of date of invoice. The average number of creditor days for the company was 25 days.

Employment policies

The company is committed to pursuing an equal opportunities policy covering recruitment and selection, training and development, appraisal and promotion. The company recognizes the diversity of its employees, its customers and the community at large and seeks to use employees' talents and abilities to the full. This approach extends to the fair treatment of people with disabilities, in relation to their recruitment, training and development. Full consideration is given to the retention of staff who become disabled during employment.

Employee communications

The company is committed to effective communications, which it maintains through regular information releases and staff briefings. Formal communications with employees take place through these channels.

Directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the company and of the profit or loss for that year. The directors are required to prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the company will continue in business.

The directors confirm that suitable accounting policies have been used and applied consistently. They also confirm that reasonable and prudent judgements and estimates have been made in preparing the financial statements for the year ended 31 December 2005 and that applicable accounting standards have been followed.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at the time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Directors and their interests

The directors who served during the period were as follows:

D. R. Phillips
W. D. Schneider
D. A. Trice

None of the directors who held office at 31 December 2005 had any beneficial interests in the shares, options to acquire shares, debentures or loan stock of the company requiring disclosure under Schedule 7 Companies Act 1985.

Directors' report (continued)

For the period ended 31 December 2005

Statement of disclosure of information to auditors

As of the date of this report the directors confirm that: so far as the directors are aware, there is no relevant audit information of which the company's auditors are unaware; and they have taken all steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Auditors

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office, and not having to be re-elected, will therefore do so for the ensuing year.

21 Dartmouth Street,
London
SW1H 9BP

28 September 2006

On behalf of the Board

D. R. Phillips
Director

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF NEWFIELD PETROLEUM UK LIMITED

We have audited the financial statements of Newfield Petroleum UK Limited for the year ended 31 December 2005 which comprise the Profit and Loss Account, the Balance Sheet and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors
As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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 1985. 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 other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments 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, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2005 and of its loss for the year then ended; and
- have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors, London
28 September 2006

Profit and loss account
For the period ended 31 December 2005

	Notes	2005 £	2004 £
Turnover	2	367,411	1,530,968
Cost of sales		(346,248)	(10,690,558)
Gross profit/(loss)		21,163	(9,159,590)
Administrative expenses	3	(1,475,096)	(1,072,915)
Operating (loss)	4	(1,453,933)	(10,232,505)
Interest receivable and similar income	5	224,295	11,300
Interest payable and similar charges	6	(62,878)	(33,550)
(Loss) on ordinary activities before taxation		(1,292,516)	(10,254,755)
Tax on (loss) on ordinary activities	7	(81,298)	-
(Loss) for the financial year	14	(1,373,814)	(10,254,755)
Retained (loss) at the beginning of the financial year		(11,566,083)	(1,311,328)
Retained (loss) at the end of the financial year		(12,939,897)	(11,566,083)

There were no recognised gains or losses during 2005 other than those included in the profit and loss account for the period.

Balance Sheet

31 December 2005

	Notes	2005 £	2004 £
Fixed assets			
Intangible assets	8	9,588,440	12,567,319
Tangible assets	8	18,050,903	1,197,413
		27,639,343	13,764,732
Current assets			
Debtors	9	519,203	375,871
Cash at bank and in hand		879,090	95,303
		1,398,293	471,174
Creditors			
Amounts falling due within one year	10	(1,427,018)	(4,798,510)
Net current assets		(28,725)	(4,327,336)
Total assets less current liabilities		27,610,618	9,437,396
Creditors			
Amounts falling due after more than one year	11	(360)	(749)
Provisions for liabilities and charges	12	(794,155)	(677,730)
Net assets		26,816,103	8,758,917
Capital and reserves – equity interests			
Equity:			
Called-up share capital	13	39,756,000	20,325,000
Profit and loss account	14	(12,939,897)	(11,566,083)
Total shareholder's funds	15	26,816,103	8,758,917

Signed on behalf of the Board

D R Phillips

D. R. Phillips Director

28 September 2006

Notes to financial statements

31 December 2005

1. Statement of principal accounting policies

A summary of the principal accounting policies, all of which have been applied consistently throughout the period, is set out below.

(a) Basis of accounting
The financial statements have been prepared under the historical cost convention in accordance with applicable financial reporting and accounting standards. The financial statements are prepared on a going concern basis, which the directors believe to be appropriate, as the parent company has confirmed that it will continue to provide financial support to the company for the foreseeable future. The directors have placed reliance upon the letter of continuing financial support described in note 18.

(b) Consortium accounting
The company's exploration, development and production activities are generally conducted in joint ventures with other companies and are accounted for as joint arrangements that are not entities under Financial Reporting Standard 9 ("FRS 9") such that the company accounts directly for its share of transactions conducted through the joint arrangement.

(c) Intangible oil and gas assets
Intangible oil and gas assets comprise the pre-licence, licence acquisition, exploration and appraisal costs relating either to unevaluated properties or properties waiting further evaluation. When a decision to develop these properties has been taken, or there is evidence of impairment, the costs are transferred to the tangible oil and gas assets cost pool.

(d) Exploration and development expenditure
The company follows the full-cost method of accounting for oil and gas properties as set out in the Statement of Recommended Practice "Accounting for Oil and Gas Exploration, Development, Production and Decommissioning Activities" published by the UK Oil Industry Accounting Committee. Proceeds from the disposal of interests are deducted from the cost pool.

(e) Depreciation
All capitalised costs within the pool of tangible oil and gas assets together with estimated future development costs are depreciated using the unit of production method based on commercial reserves. Other tangible fixed assets are depreciated on a straight-line basis over 3 years.

(f) Ceiling test
Each year management assesses the recoverability of the oil and gas asset pool by comparison with the estimated discounted future net revenues of proven reserves within the pool in accordance with Financial Reporting Standard 11. A provision is made where there has been impairment in the capitalised value of the cost pool.

(g) Commercial reserves
Commercial reserves are proved and probable developed and undeveloped oil and gas reserves, as defined in the Statement of Recommended Practice "Accounting for Oil and Gas Exploration, Development, Production and Decommissioning Activities" published by the Oil Industry Accounting Committee.

(h) Abandonment
Provision is made for the present value of the future cost of abandonment of production platforms, pipelines and terminal facilities. This provision is recognised when the asset is installed. The estimated costs, based on engineering cost levels prevailing at the balance sheet date, are computed on the basis of the latest assumptions as to the scope and method of abandonment. The corresponding amount is capitalised as part of tangible fixed assets and is amortised on a unit-of-production basis as part of the depreciation, depletion and amortisation charge. Any adjustment arising from the reassessment of estimated cost of decommissioning is capitalised, whilst the charge arising from the unwinding of the discount applied to the abandonment provision is treated as a component of the interest charge.

(i) Deferred taxation
Provision is made for deferred corporation tax at current rates of tax on timing differences between results stated in the financial statements and results computed for corporation tax purposes, only where it is expected that a taxation liability will arise in the foreseeable future when the timing differences reverse. Timing differences are differences between the company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not, there will be suitable profits in the foreseeable future from which the reversal of the underlying timing differences can be deducted. No deferred tax assets have been recognised as of 31 December 2005 or 31 December 2004.

(j) Foreign currency
Foreign currency transactions are translated at the average monthly exchange rate. Foreign currency balances at year-end are translated at the exchange rates ruling at the balance sheet date, except those covered by foreign exchange contracts in which case the forward exchange rate is used. Exchange gains and losses are recognised in the profit and loss account. Year-end exchange rates used were $1.72 (2005) and $1.92 (2004).

(k) Effect of changing estimates
Changes in reserve and throughput estimates, anticipated future development costs, future abandonment costs and other variables used in unit of production calculations are accounted for prospectively over the estimated remaining life of the relevant field, with effect from the beginning of the period in which they arise.

(l) Operating leases
Costs in respect of operating leases are charged on a straight-line basis over the lease term.

(m) Turnover
Turnover represents the invoiced value for the sale of oil, gas and condensate and is recognised upon delivery of the product.

(n) Cash flow statement and related party disclosures
The company is a wholly-owned subsidiary of Newfield Exploration Company and is included within the consolidated statements of Newfield Exploration Company, which are publicly available at the address set out in Note 18. Consequently, the company has taken advantage of the exemption from preparing a cashflow statement under the terms of FRS 1. The company is also exempt under the terms of FRS 8 from disclosing related party transactions with entities that are part of the Newfield Exploration Company group or investees of the Newfield Exploration Company.

2. Turnover

Turnover relates to principal activities of the business and arose wholly in the United Kingdom. Sales during the year to north west Europe amounted to £367,411 (2004 £1,530,968).

3. Administrative expenses

	2005	2004
	£	£
Overhead costs	(3,047,978)	(1,715,840)
Less amount capitalised	1,640,424	724,678
Depreciation of other fixed assets	(67,542)	(81,753)
	(1,475,096)	(1,072,915)

4. Operating loss

	2005	2004
	£	£
Operating loss for the period is stated after charging:		
Auditors' remuneration – audit fee	12,000	12,000
Employee costs	526,603	540,883
Depreciation of tangible assets	127,427	862,441
Depreciation of abandonment asset	70,201	53,465
Write off of oil and gas assets	-	9,131,741
Unrealised foreign currency loss	7,369	44,278
Operating lease costs – office rent	140,741	133,166

The average number of employees (excluding non-executive directors) during the period was	6	6

Employee costs in the period amounted to:

	£	£
Staff costs, excluding executive director	290,564	283,200
Social security costs	43,534	34,733
Directors' emoluments	192,505	136,650

5. Interest receivable and similar income

	2005	2004
	£	£
Bank interest	78,757	11,300
Other interest	145,288	-
Other income	250	-
	224,295	11,300

Other interest arises from the sale of the interests in the Windermere and Chiswick gas fields.

6. Interest payable and similar charges

	2005	2004
	£	£
Interest payable and similar charges	(46,948)	-
Unwinding of discount on decommissioning provision	(15,930)	(33,550)
	(62,878)	(33,550)

7. Tax on profit on ordinary activities

The charge for the year is made up as follows:

	2005	2004
	£	£
UK corporation tax (30%) on interest received	81,298	-

The tax charge for 2005 relates to interest received on the payment from the acquirer of the Windermere and Chiswick gas fields (see Note 5), and from temporary surplus funds.

Factors affecting the tax charge for the financial year

The tax assessed for the period is lower than the standard rate of corporation tax in the UK. The differences are explained below:

	2005	2004
	£	£
(Loss) on ordinary activities before taxation	(1,292,516)	(10,254,755)
(Loss) on ordinary activities multiplied by aggregate standard corporation tax rates in the UK – 30% (2004 – 30%)	(387,755)	(3,076,427)
Effects of:		
Expenses not deductible for tax purposes	(12,219)	28,900
Accelerated capital allowances and other timing differences	(7,430,498)	(1,753,246)
Losses not utilised	7,959,723	5,826,248
Supplemental oil and gas tax – 10% (2004 – 10%)	(129,251)	(1,025,475)
Current year current tax charge	-	-

No entry has been made in these accounts for a potential net deferred tax asset of £8,764,382 resulting from carry forward trading losses and accelerated capital allowances. A deferred tax asset would only be recognised where there is reasonable certainty that suitable taxable profits will be generated in the future.

8. Fixed Assets

	Intangible Assets Exploration and Appraisal Costs	Tangible Assets Oil & Gas	Office Equipment	Total
	£	£	£	£
Cost				
At 1 January 2005	21,699,060	2,076,677	259,800	24,035,537
Additions	7,573,619	11,315,903	104,592	18,994,114
Transfers	(19,684,239)	19,684,239	-	-
Disposals	-	(4,921,875)	-	(4,921,875)
At 31 December 2005	9,588,440	28,154,944	364,392	38,107,776
Depreciation				
At 1 January 2004	9,131,741	955,634	183,430	10,270,805
Transfers	(9,131,741)	9,131,741	-	-
Charge for year	-	130,086	67,542	197,628
At 31 December 2004	-	10,217,461	250,972	10,468,433
Net book value				
At 31 December 2005	9,588,440	17,937,483	113,420	27,639,343
At 31 December 2004	12,567,319	1,121,043	76,370	13,764,732

Oil and gas tangible assets relate to the development and evaluated property costs capitalised in the UK full cost pool and include abandonment costs capitalised, the net book amount of which at 31 December 2005 is £794,155 (2004 - £579,396).

The transfers from Intangible Assets to Tangible Assets represent amounts transferred to the oil and gas assets cost pool in accordance with accounting policy (c).

On 17 June 2005, the company completed the sale of its interests in Windermere, Chiswick and block 49/4b to CH4 Energy Limited for £4.9 million.

9. Debtors: due within one year

	2005	2004
	£	£
Trade debtors	-	226,511
Other debtors	236,228	7,887
Prepayments	282,975	149,360
	519,203	375,871

Other debtors mostly relates to refundable value added tax.

10. Creditors: Amounts falling due within one year

	2005	2004
	£	£
Trade creditors	1,039,759	4,693,919
Other creditors	208,501	68,330
Taxation and social security	178,758	36,261
	1,427,018	4,798,510

Other creditors mostly relates to payments to employees.

11. Creditors: Amounts falling due after more than one year

	2005	2004
	£	£
Amount due to parent company	360	749

Amounts due to parent company are unsecured and payable on demand. The parent company has confirmed that it will not demand repayment of the amounts due within one year.

12. Provisions for liabilities and charges

	Abandonment *provision*	**Deferred corporation tax**	**Total**
	£	£	£
At beginning of year	677,730	-	677,730
Amount released	(677,730)	-	(677,730)
Amounts provided	794,155	-	794,155
At end of year	794,155	-	794,155

The abandonment provision in the beginning of the year related to the company's interest in the Windermere gas field which was disposed of during the year. An additional provision was booked during the year in relation to the Grove gas field development.

13. Called-up share capital

	2005	2004
	£	£
Equity share capital		
Authorised:		
1,000,000 ordinary shares of £100 each	100,000,000	100,000,000
Allotted, called-up and fully paid:		
327,250 (2004: 203,250) Ordinary shares of £100 each	32,725,000	20,325,000
52,733 (2004: Nil) Ordinary shares of £133.33 each	7,031,000	-
	39,756,000	20,325,000

14. Movements on reserves

The movement on reserves for the period is as follows:

	Profit and Loss Account
	£
At 1 January 2005	(11,566,083)
Loss for the year	(1,373,814)
At 31 December 2005	(12,939,897)

15. Reconciliation of movement in shareholder's funds

	2005	2004
	£	£
Opening shareholder's funds	8,758,917	6,225,972
Loss for the period	(1,373,814)	(10,254,755)
Net proceeds of issue of equity share capital	19,431,000	12,787,700
Closing shareholder's funds	26,816,103	8,758,917

16. Guarantees and other financial commitments

The company rents office space for which the commitment at 31 December for the period to May 2006 was £46,500. The lease agreement was extended in May 2006 for a further twelve months.

17. Contingent liability

The company has agreed that, depending on the success of the development programme, further payments may be made to the seller of the Chiswick interest in line with the original Purchase Agreement. The maximum potential exposure is £1.4m. Following the sale of the Chiswick interest, the company may receive a payment which will reduce the contingent liability to £0.9m. Since the achievement of the targets is uncertain, management believe a provision is not necessary.

As part of the Cleaver Bank High acquisition the company has also agreed to pay deferred compensation to the sellers of this interest of up to $10m, depending on the field achieving certain production targets. Since the achievement of these targets is uncertain, management believes a provision is not necessary in this respect.

18. Ultimate parent company

The company is a subsidiary undertaking of Newfield Exploration Company, a company incorporated in the United States of America, which has agreed to provide continuing financial support to enable the company to continue its operations.

The largest group in which the results of Newfield Petroleum UK Limited are consolidated is that headed by Newfield Exploration Company, whose principal place of business is the United States of America. The consolidated accounts of this group are available to the public and may be obtained from 363 N. Sam Houston Pkwy. E, Suite 2020, Houston, Texas 77060, USA.