

# Corporate Governance

year ended 31 December 2005

The Tullow Board is committed to business integrity and high ethical values across the Group's activities. As an essential part of this commitment, the Board supports high standards of corporate governance.

## Compliance with FRC Combined Code on Corporate Governance

This report describes how the Company has applied the principles set out in Section 1 of the Combined Code on Corporate Governance (the Code) published by the Financial Reporting Council. It also discloses the extent to which the Company has complied with the provisions of the Code.

The Board considers that the Company has complied with the provisions of the Code throughout the year under review (and subsequently up to the date of this report) with the following two exceptions:

- Throughout 2005, the Board comprised a non-executive Chairman, five Executive Directors and four independent non-executive Directors. As independent non-executive Directors therefore comprise less than half of the Board, the Board's composition is not as recommended by the Code.

On 16 February 2006, it was announced that Adrian Nel would be retiring as Exploration Director with effect from the conclusion of the AGM to be held on 31 May 2006. The appointment of Paul McDade, Chief Operating Officer, to the Board was made with effect from 29 March 2006. Separately, in 2005, the Nominations Committee commenced the process to recruit an additional independent non-executive Director.

Following the retirement of Adrian Nel, and once the appointment of a new independent non-executive director has been made, half of the Board will then consist of independent non-executive Directors.

- Throughout 2005, Pat Plunkett (the Company Chairman) continued as Chairman of the Remuneration Committee. Consequently, that Committee is not made up solely of

independent non-executive Directors. The Board remains of the view that Pat Plunkett should continue in this role since he brings considerable knowledge of the management roles and responsibilities within the Group which enables him to discharge his duties in an informed and properly independent manner. The Board also considers that as he and Rohan Courtney have been members of the Committee throughout the period of major growth enjoyed by the Company in the last five years, they bring a long term perspective and continuity to the Committee.

Details of how Tullow has applied the principles of the Code in relation to Directors' remuneration are contained in the Directors' Remuneration Report on page 35.

## Board of Directors

**Composition** Following the appointment of Paul McDade as an Executive Director, the Board will comprise a non-executive Chairman, six Executive Directors and four non-executive Directors. Each of the Executive Directors has extensive knowledge of the oil and gas industry. The majority of the non-executive Directors either have held, or currently hold, senior appointments in oil and gas companies or companies with energy interests and, together, the non-executive Directors bring a broad range of business and commercial experience to the Board. Biographies of the Board members are set out on page 27.

**Role of the Board** The Board is accountable to shareholders for the creation and delivery of strong, sustainable financial performance and long-term shareholder value. To achieve this, the Board directs and monitors the Group's affairs within a framework of controls which enable risk to be assessed and managed effectively. It sets the Group's strategic aims, ensuring that the necessary resources are in place to achieve those aims, and reviews management and financial performance. The Board also has responsibility for setting the Group's core values and standards of business conduct and for ensuring that these, together with the Group's obligations to its stakeholders, are widely understood throughout the Group.

# Corporate Governance

continued

**Chairman and Chief Executive** There is a clear separation of the roles of the Chairman and the Chief Executive. The division of responsibilities has been agreed and set out in writing by the Board.

The Chairman's key responsibilities are the effective running of the Board, ensuring that the Board plays a full and constructive part in the development and determination of the Group's strategy, and acting as guardian of the Board's decision-making process.

The key responsibilities of the Chief Executive are managing the Group's business, proposing and developing the Group's strategy and overall commercial objectives in consultation with the Board and, as leader of the executive team, implementing the decisions of the Board and its Committees. In addition, the Chief Executive is responsible for maintaining regular dialogue with major shareholders as part of the Company's overall investor relations programme.

## Non-Executive Directors

**Appointment** Non-executive Directors are appointed for an initial term of three years. Thereafter, they may serve one or more three year terms subject to satisfactory performance. The letters of appointment of each non-executive Director are available for inspection.

**Meetings of Non-Executive Directors** In addition to their attendance at Board and, as appropriate, Committee meetings, the non-executive Directors also met formally on two occasions during 2005 without executive management present. The non-executive Directors examine and review the performance of the executive management; this review process is in part dealt with by the Board Committees referred to below. Separately, the Chairman and Chief Executive held informal meetings with the non-executive Directors to discuss issues affecting the Group such as target objectives, remuneration matters etc.

**Senior Independent Director** The Senior Independent Director is Rohan Courtney. In this role he is available to shareholders who have concerns that cannot be resolved through discussion with the Chief Executive or Chairman.

**Independence** The Board considers each of the current non-executive Directors to be independent of management and free from any business or other relationships that could materially interfere with the exercise of their independent judgement. The Board recognises that Rohan Courtney's independence may be called into question, given that he has served on the Board for more than nine years. Nevertheless, the Board considers that Mr Courtney's independence is not prejudiced or compromised by his length of service; when taken with his experience and knowledge of the Group's business, he remains an independent, challenging and valuable contributor to the Board. Rohan Courtney will be proposed for re-election at this year's Annual General Meeting (AGM).

**Election and re-election** All Directors are required by the Company's articles of association to be elected by shareholders at the first AGM after their appointment. Subsequently, Directors are subject to re-election by shareholders at least every three years.

## How the Board operates

**Board meetings** The Board meets regularly during the year and on an ad hoc basis as required. The attendance record of each Director is shown in the table on page 31. During 2005 the Board met on ten occasions including a formal strategy review held with senior management in November. In addition to the formal meetings of the Board, the Chairman and Chief Executive maintain frequent contact with the other Directors to discuss any issues of concern they may have relating to the Group or as regards their area of responsibility and to keep them fully briefed on ongoing matters relating to the Group's operations.

**Information flow** Directors have access to a regular supply of financial, operational and strategic information to assist them in the discharge of their duties. Such information is provided as part of the normal management reporting cycle undertaken by senior management. Board papers are generally circulated seven days in advance of Board meetings. In addition, each Board meeting includes a review of the history, performance and future potential of an individual asset or business unit designed to ensure that all material assets are considered on a cyclical basis and to enable Board members to familiarise themselves with the key assets and operations of the Group.

**Independent professional advice** All Directors and Committees have access to independent professional advice, at the Company's expense, as and when required.

**Insurance cover** The Company maintains Directors' and Officers' Liability insurance cover, the level of which is reviewed annually.

**Matters reserved and delegations** A formal schedule of matters reserved for Board approval is in place and is reviewed annually. The matters reserved include: the Group's overall strategy, approval of annual and interim results, material acquisitions and disposals, material contracts and major capital expenditure projects and budgets. Subject to those reserved matters, the Board delegates authority for the management of the business primarily to the Chief Executive and a senior executive committee. Certain other matters are delegated to the Audit, Remuneration and Nominations Committees, each of which is described in more detail below.

**Attendance at meetings** The attendance of Directors at Board meetings and Committee members at Committee meetings during 2005 was as follows:

No. of Meetings	Board (10)	Audit (6)	Remuneration (6)	Nominations (3)
Pat Plunkett	10	–	6	3
Aidan Heavey	10	–	–	2
David Bamford	10	6	6	3
Rohan Courtney	10	6	6	3
Tom Hickey	9	–	–	–
Steven McTiernan	10	6	6	3
Graham Martin	9	–	–	–
Adrian Nel	10	–	–	–
Matthew O'Donoghue	10	–	–	–
Clare Spottiswoode	8	6	6	3

**Performance evaluation** In 2004, the Board conducted a detailed evaluation of its own performance and its Committees and of individual directors with the assistance of an independent facilitator. This review focused on such matters as Board composition and strategic capability, ongoing development, external and internal relationships, risk management, and conduct of Board and Committee meetings. In December 2005, the Board commissioned a follow-up to the evaluation conducted in 2004. Overall, it was concluded that the Board continues to operate in an effective manner and that there were no items arising from the follow-up review which, in the Board's view, gave rise to material concern. The Board is also satisfied that no individual or group of individuals dominates the Board's decision making. Certain matters for improvement were identified from the evaluation and these are being addressed. The Board intends to continue to conduct evaluations on an annual basis, although the scope and format may be varied as deemed appropriate.

The Chairman has had conversations with each of the directors on their individual performance. Separately, the non-executive Directors have reviewed the performance of the Chairman in his absence.

**Induction** Detailed training and briefing is provided to Directors on appointment, taking into account their individual background and experience. This includes a visit to the key offices of the Group to meet line management from each functional discipline and business unit. The Company Secretary also provides new Directors with an overview of their duties as Directors, corporate governance policies and established Board procedures as part of the induction process.

**Continuing Professional Development** All members of the Board have access to appropriate training in respect of their obligations and duties as Directors. During the year, briefings on particular subject matters were given, including corporate governance, the introduction of International Financial Reporting Standards and the new Listing and Disclosure Rules.

## Committees

The Board has established the following principal Committees, each of which has written terms of reference (approved by the Board) setting out its authority and duties. Copies of the terms of reference can be viewed on the investor relations section of the Company's website [www.tulloil.com](http://www.tulloil.com) or can be obtained from the Company Secretary.

### Audit Committee

This Committee currently comprises Rohan Courtney (Chairman), David Bamford, Steven McTiernan and Clare Spottiswoode.

Rohan Courtney and Steven McTiernan both have extensive banking and financial experience, whilst Clare Spottiswoode has had experience as a member of the audit committees of three other public companies. Based upon this, the Board is satisfied that, in aggregate, the Audit Committee members have the appropriate level of recent and relevant financial experience.

The main responsibilities of the Committee are:

- Monitoring the integrity of the financial statements and formal announcements relating to the Group's financial performance;
- Reviewing significant financial reporting issues and accounting policies and disclosures in financial reports;
- Reviewing the effectiveness of the Group's internal control procedures and risk management systems;
- Reviewing the company's whistle-blowing procedures;
- Making recommendations to the Board as to the appointment or re-appointment of the Group's external auditors; and
- Overseeing the selection of new auditors and overseeing the relationship with the external auditor.

The Group's auditors, Deloitte & Touche LLP, were re-appointed in 2004 following a tender process. The Committee monitors the level of audit and non-audit services provided by the Company's auditors. Non-audit services are normally limited to assignments that are closely related to the annual audit or where the work is of such a nature that a detailed understanding of the Group is necessary. A breakdown of the fees paid to the external auditors in respect of audit and non-audit work is included in note 3 of the accounts on page 52. In addition to processes put in place to ensure segregation of audit and non-audit roles, as part of the assurance process in relation to the audit, Deloitte are required to confirm to the Committee that they have both the appropriate independence and objectivity to allow them to continue to serve the members of the Company. No matters of concern were identified by the Committee.

# Corporate Governance

continued

The Chief Financial Officer and a representative of the external auditors normally attend meetings of the Audit Committee, at the invitation of the Committee. The Chairman of the Board also attends meetings of the Committee by invitation. The external auditors have unrestricted access to the Committee Chairman.

During 2005 the Audit Committee met on a total of six occasions. The key work undertaken by the Committee was as follows:-

## Transition to IFRS

Tullow adopted IFRS with effect from 1 January 2004 (with the exception of IAS39 which was adopted with effect from 1 January 2005). The Committee was closely involved along with Group senior management and representatives from the external Auditors in the selection and approval of appropriate accounting policies and also in the review and approval of the 2004 IFRS results statement published on 23 August 2005. This exercise was undertaken to ensure that Tullow's IFRS accounting policies and disclosures, most notably in relation to Oil and Gas Interests (IFRS 6), Acquisition and Business Combinations (IAS 12) and Financial Derivatives (IAS 39) are appropriate to the nature of Tullow's business and its stage of development.

## Review of Annual and Interim Results

The Committee held a number of meetings to review both the 2004 annual and the 2005 interim results, the latter representing Tullow's first IFRS Reports. During 2005, Tullow completed the Schooner and Ketch acquisition and also divested certain UK and African oil and gas interests. Consequently, the Committee gave detailed consideration to the fair values attributed to the acquired assets and accounting for and disclosure of the relevant profit or loss on disposals.

## Establishment of a Group Internal Audit Function

During 2005, the Committee approved the recruitment of a Group Internal Audit Manager with a view to establishing an internal audit function within Tullow. The Chairman of the Audit Committee assisted Executive Management in the recruitment process. The Internal Audit Manager, who has extensive oil industry experience will have direct access and responsibility to the Audit Committee.

## Nominations Committee

The current members of the Nominations Committee, are Pat Plunkett (Chairman), Aidan Heavey, Rohan Courtney, Steven McTiernan, Clare Spottiswoode and David Bamford.

The main responsibilities of the Committee are:

- Reviewing the structure, size and composition of the Board and making recommendations to the Board with regard to any changes required;
- Succession planning for Directors and other senior executives;

- Identifying and nominating, for Board approval, candidates to fill Board vacancies as and when they arise;
- Reviewing annually the time commitment required of non-executive Directors;
- Making recommendations to the Board with regard to membership of the Audit and Remuneration Committees in consultation with the Chairman of each Committee.

The Committee met three times in 2005, primarily to review board appointment and succession issues. Towards the end of the year the Committee drew up a specification and commenced the search for a new non-executive director. A firm of external search consultants was appointed to identify suitable candidates for this role. The Committee is expected to make a recommendation to the Board for the appointment of a new independent non-executive director in the near future.

Separately, in view of the impending retirement of Adrian Nel as Exploration Director, the Committee agreed in conjunction with senior management on the specification for a new senior exploration executive to assume responsibility for the Company's exploration activities upon Mr Nel's retirement. External search consultants were appointed for this appointment and, on the Committee's recommendation the Board, in February 2006, approved the appointment of Angus McCoss as General Manager Exploration. Mr McCoss will join Tullow in April 2006.

In March 2006, the Board endorsed the Committee's recommendation that Paul McDade, Chief Operating Officer be appointed to the Board.

## Remuneration Committee

The Directors Remuneration Report on pages 35 to 41 contains details of the Remuneration Committee.

## Shareholder Relations

Communication with shareholders is given high priority and there is regular dialogue with institutional investors, as well as general presentations to analysts at the time of the release of the annual and interim results. The Board receives regular investor relations reports covering key investor meetings and activities, as well as shareholder and investor feedback. The Group issues its results promptly to individual shareholders and also publishes them on the Investor Relations section of the Company's website. The Company's website address is [www.tulloil.com](http://www.tulloil.com). Regular updates to record news in relation to the Company and the status of exploration and development programmes are also included on the website. Shareholders and other interested parties can subscribe to receive these news updates by e-mail by registering online on the website.

The Chairman is available to meet with institutional shareholders to discuss any issues and gain an understanding of any concerns in relation to the Company's governance and strategy. Non-executive Directors have the opportunity to attend meetings with major shareholders and are available to attend if requested to do so.

At the AGM, a business presentation is provided for shareholders' benefit and individual shareholders are given the opportunity to put questions to the Chairman, the chairmen of the principal Board Committees and to other members of the Board. In addition, the Board is committed to maintaining strong links with its significant Irish shareholder base and holds a business presentation in Ireland following the AGM, to allow these shareholders similar access to the directors. Notice of the AGM is sent to shareholders at least 20 working days before the meeting and details of proxy votes for and against each resolution, together with abstentions, are made available after the vote has been dealt with on a show of hands.

#### Internal Controls

In September 1999, the Turnbull Guidance (Internal Control: Guidance for Directors on the Combined Code) was published.

The Directors acknowledge their responsibility for the Group's and the Company's systems of internal control, which are designed to safeguard the assets of the Group and to ensure the reliability of financial information for both internal use and external publication. The Group's internal control procedures require Board, technical and financial approval for all projects. All major expenditures require senior management approval at the appropriate stages of each transaction. Overall control is ensured by a regular detailed reporting system covering both technical progress of projects and the state of the Group's financial affairs. The Board has put in place procedures for identifying, evaluating and managing any significant risks that face the Group.

Any system of internal control can provide only reasonable, and not absolute, assurance that material financial irregularities will be detected or that the risk of failure to achieve business objectives is eliminated. The Directors, having reviewed the effectiveness of the system of internal financial, operational and compliance controls and risk management, consider that the system of internal control operated effectively throughout the financial year and up to the date on which the financial statements were signed.

During 2005, the Audit Committee (in conjunction with executive management) approved the establishment of an internal audit function for the first time and in March 2006 an internal audit manager was recruited to join Tullow. He reports to the Audit Committee and has responsibility for evaluating and developing the Group's overall control environment, operating efficiency and risk identification and management at operating, regional and corporate levels. In fulfilling his role, the Group Internal Audit Manager, will operate under a Charter approved by the Committee and will have regular access to the Committee without reference to executive management.

#### Going Concern

After making enquiries, the Directors have a reasonable expectation that the Company and the Group as a whole have adequate resources to continue in operational existence for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the financial statements.