

# Independent Auditors' Report to the Members of Tullow Oil plc

We have audited the individual Company financial statements of Tullow Oil plc for the year ended 31 December 2005, which comprise the Balance Sheet and the related notes 1 to 11. These individual Company financial statements have been prepared under the accounting policies set out therein.

The Corporate Governance Statement and the Directors' Remuneration Report are included in the Group Annual Report of Tullow Oil plc for the year ended 31 December 2005. We have reported separately on the Group financial statements of Tullow Oil plc for the year ended 31 December 2005 and on the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. 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 auditors' 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' responsibilities for preparing the Annual Report and the individual Company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of Directors' responsibilities.

Our responsibility is to audit the individual Company financial statements in accordance with relevant United Kingdom legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the individual Company financial statements give a true and fair view in accordance with the relevant financial reporting framework and whether the individual Company financial statements have been properly prepared in accordance with the Companies Act 1985. We report to you if, in our opinion, the Directors' report is not consistent with the individual Company financial statements. We also report to you 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 the other information contained in the annual report for the above year as described in the contents section and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the individual Company financial statements.

## 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 individual Company financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the individual Company 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 individual Company 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 individual Company financial statements.

## Opinion

In our opinion:

- the individual Company 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
- the individual Company financial statements have been properly prepared in accordance with the Companies Act 1985.

## Deloitte & Touche LLP

Chartered Accountants and Registered Auditors  
London  
28 March 2006

# Company Balance Sheet

as at 31 December 2005

	Notes	2005 £'000	2004 £'000
<b>Fixed Assets</b>			
Investments	1	364,091	363,549
<b>Current Assets</b>			
Debtors	3	272,700	57,876
Cash at Bank and in Hand		26	–
		<b>272,726</b>	57,876
<b>Creditors – Amounts Falling Due Within One Year</b>			
Trade and Other Creditors	4	(2,157)	(2,600)
<b>Net Current Assets</b>		<b>270,569</b>	55,276
<b>Total Assets Less Current Liabilities</b>		<b>634,660</b>	418,825
<b>Creditors – Amounts Falling Due after more than One Year</b>			
Bank Loans	5	(190,038)	(96,295)
Loans from Subsidiary Undertakings		(126,715)	–
<b>Net Assets</b>		<b>317,907</b>	322,530
<b>Capital and Reserves</b>			
Called Up Equity Share Capital	6	64,744	64,537
Share Premium Account	6	123,019	121,656
Merger Reserve	7	122,336	122,336
Profit and Loss Account	8	7,808	14,001
<b>Equity Shareholders' Funds</b>		<b>317,907</b>	322,530

Approved by the Board on 28 March 2006

**Aidan Heavey**

Chief Executive Officer

**Tom Hickey**

Chief Financial Officer

The notes on pages 78 to 83 form part of these financial statements.

The Profit and Loss Account of the Company has not been presented separately in these financial statements as permitted by the provisions of Section 230 of the Companies Act 1985.

# Accounting policies

year ended 31 December 2004

## (a) Basis of Accounting

The financial statements have been prepared under the historical cost convention in accordance with the Companies Act 1985 and UK Generally Accepted Accounting Principles (UK GAAP). The following paragraphs describe the main accounting policies under UK GAAP, which have been applied consistently.

In accordance with the provisions of Section 230 of the Companies Act the Profit and Loss Account of the Company is not presented separately. In accordance with the exemptions available under FRS 1 "Cash Flow Statements" the Company has not presented a cash flow statement as the cash flow of the Company has been included in the Cash Flow Statement of Tullow Oil plc Group set out on page 46.

## (b) Investments

Fixed asset investments, including investments in subsidiaries, are stated at cost and reviewed for impairment if there are indications that the carrying value may not be recoverable.

## (c) Finance Cost and Debt

Finance costs of debt are allocated to periods over the term of the related debt at a constant rate on the carrying amount. Arrangement fees and issue costs are deducted from the debt proceeds and are amortised and charged to the profit and loss account as finance costs over the term of the debt.

## (d) Foreign Currencies

Sterling is the reporting currency of the Company. Transactions in foreign currencies are translated at the rates of exchange ruling at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date, with a corresponding charge or credit to the profit and loss account.

## (e) Share Issue Expenses and Share Premium Account

Costs of share issues are written off against the premium arising on the issues of share capital.

## (f) Taxation

Current and deferred tax, including UK corporation tax, is provided at amounts expected to be paid using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

## (g) Share Based Payments

The Company has applied the requirements of FRS 20 Share Based Payments. In accordance with the transitional provisions of that standard, only those awards that were granted after 7 November 2002, and had not vested at 1 January 2005, are included.

All share-based awards of the Company are equity settled as defined by FRS 20. The fair value of these awards has been determined at the date of grant of the award allowing for the effect of any market-based performance conditions. This fair value, adjusted by the Company's estimate of the number of awards that will eventually vest as a result of non-market conditions, is expensed uniformly over the vesting period.

The fair values were calculated using a binomial option pricing model with suitable modifications to allow for employee turnover after vesting and early exercise. Where necessary this model was supplemented with a Monte Carlo model. The inputs to the models include: the share price at date of grant; exercise price; expected volatility; expected dividends; risk free rate of interest; and patterns of exercise of the plan participants.

# Notes to the Financial Statements

## Note 1. Investments

	2005 £'000	2004 £'000
Shares at Cost in Subsidiary Undertakings	363,595	363,053
Unlisted Investments	447	447
Government Gilts	49	49
	<b>364,091</b>	363,549

At 31 December 2005 the Company's principal subsidiary undertakings were:

Name	%	Country of Operation	Country of Incorporation
<b>Directly Held</b>			
Tullow Oil Limited	100	Ireland	Ireland
Tullow Oil UK Limited	100	United Kingdom	Scotland
Tullow Oil SK Limited	100	United Kingdom	England & Wales
Tullow Oil SNS Limited	100	United Kingdom	England & Wales
Tullow Oil SPE Limited	100	United Kingdom	England & Wales
Energy Africa (Pty) Limited	100	South Africa	South Africa
Energy Africa Gabon Holdings Limited	50	Gabon	Isle of Man
<b>Indirectly Held</b>			
Energy Africa Holdings Limited	100	Isle of Man	British Virgin Islands
Tullow Oil International Limited	100	Channel Islands	Jersey
Tullow Pakistan (Developments) Limited	100	Pakistan	Jersey
Tullow Bangladesh Limited	95	Bangladesh	Jersey
Tullow Romania Limited	100	Romania	Jersey
Tullow Côte d'Ivoire Limited	100	Côte d'Ivoire	Jersey
Tullow Côte d'Ivoire Exploration Limited	100	Côte d'Ivoire	Jersey
Tullow India Operations Limited	90	India	Jersey
Tullow Cameroon Limited	100	Cameroon	Jersey
Tullow Gabon Operations Limited	100	Gabon	Jersey
Tullow Angola Limited	100	Angola	Jersey
Tullow Madagascar Limited	100	Madagascar	Jersey
Energy Africa Congo Limited	100	Congo	Isle of Man
Energy Africa Equatorial Guinea Limited	100	Equatorial Guinea	Isle of Man
Energy Africa Equatorial Guinea Exploration Limited	100	Equatorial Guinea	Isle of Man
Energy Africa Kudu Limited	100	Namibia	Isle of Man
Energy Africa Mauritania Limited	100	Mauritania	Isle of Man
Energy Africa Senegal Limited	100	Senegal	Isle of Man
Energy Africa Uganda Limited	100	Uganda	Isle of Man
Energy Africa UK Limited	100	England	England & Wales
Unitrust Holdings Limited	100	England	England & Wales
Energy Africa Gabon Holdings Limited	50	Gabon	Isle of Man
Energy Africa Gabon Limited	100	Isle of Man	Isle of Man
Energy Africa Gabon SA	100	Gabon	Gabon

Energy Africa Gabon Holdings Limited (EAGHL) is wholly owned by the Company, 50% is held directly and 50% by Energy Africa Limited (Energy Africa).

On 28 May 2004, the Company acquired 100% of the issued share capital of Energy Africa and the 50% of EAGHL not owned by Energy Africa.

The principal activity of all companies relates to oil and gas exploration, development and production.

## Note 2. Dividends

	2005 £'000	2004 £'000
Declared and Paid during Year		
Final Dividend for 2004: Stg1.25p (2004: Stg1p) per Ordinary Share	8,083	3,782
Interim Dividend for 2005: Stg1p (2004: Stg0.5p) per Ordinary Share	6,472	3,213
<b>Dividends Paid</b>	<b>14,555</b>	6,995
Proposed for Approval by Shareholders at the AGM		
Final Dividend for 2005: Stg 3p (2004: Stg1.25p)	19,423	8,083

## Note 3. Debtors

### Amounts falling due within one year

	2005 £'000	2004 £'000
Trade Debtors	–	351
Other Debtors	6,926	–
Prepayments	548	–
Due from Subsidiary Undertakings	265,226	57,525
	<b>272,700</b>	57,876

## Note 4. Trade and Other Creditors

### Amounts falling due within one year

	2005 £'000	2004 £'000
Other Creditors	849	1,181
Accruals	1,210	1,419
VAT	98	–
	<b>2,157</b>	2,600

## Note 5. Bank Loans and Overdrafts

### Amounts falling due after one year

	2005 £'000	2004 £'000
Term Loans Repayable		
– After One Year but within Two Years	–	96,295
– After Two Years but within Five Years	154,726	–
– After Five Years	35,312	–
	<b>190,038</b>	96,295

Company bank loans are stated net of unamortised arrangement fees of £6,836,671 (2004: £2,324,283).

Bank loans, overdrafts and guarantees are secured by fixed and floating charges over all the assets of the Group.

# Notes to the Financial Statements

continued

## Note 5. Bank Loans and Overdrafts (continued)

Wherever possible the Company conducts and manages its business in Sterling. At 31 December 2005 the only material monetary assets or liabilities of the Company that were not denominated in the functional currency were \$177 million (£102.9 million) cash drawings under the US\$850 million Borrowing Base Facility held as a hedge against US\$ denominated net assets in subsidiaries in the Company's Group Accounts.

### Interest Rate Risk

The interest rate profile of the Group's financial assets and liabilities at 31 December 2005 was as follows:

	Stg £'000	US\$ £'000	Total £'000
Cash at Bank on which no Interest is Received	26	–	26
Fixed Rate Debt	(42,500)	(34,286)	(76,786)
Floating Rate Debt	(51,516)	(68,573)	(120,089)
<b>Net Debt</b>	<b>(93,990)</b>	<b>(102,859)</b>	<b>(196,849)</b>

The profile at 31 December 2004 for comparison purposes was as follows:

	Stg £'000	US\$ £'000	Total £'000
Fixed Rate Debt	–	–	–
Floating Rate Debt	–	(98,619)	(98,619)
<b>Net Debt</b>	<b>–</b>	<b>(98,619)</b>	<b>(98,619)</b>

Floating rate debt comprises bank borrowings at interest rates fixed in advance from overnight to three months at rates determined by US Dollar LIBOR and Sterling LIBOR. Fixed rate debt comprises bank borrowings at interest rates fixed in advance for period greater than three months or bank borrowings where the interest rate has been fixed through interest rate hedging.

In September 2005 the Group completed an \$850 million refinancing exercise which consolidated existing borrowings into a single Borrowing Base Facility, which has created a more efficient Group financing structure and materially reduced the cash collateralisation of decommissioning Letters of Credit.

The Borrowing Base Facility incurs interest on outstanding debt at Sterling LIBOR plus a margin ranging from 110 basis points to 225 basis points depending on utilisation and concentration of non-OECD Assets and US Dollar LIBOR plus a margin ranging from 110 basis points to 225 basis points depending on utilisation and concentration of non-OECD Assets. The outstanding debt is repayable in variable amounts (determined semi-annually) over the period to 31 August 2012, or such other time as is determined by reference to the remaining reserves of the assets, whichever is earlier. There is no requirement under the Borrowing Base Facility to hedge interest rate exposure to Sterling LIBOR and US Dollar LIBOR. The Borrowing Base Facility states that consideration should be given to hedging at least 30% of the interest rate exposure to fluctuations in LIBOR for Sterling and US Dollars in respect of loans under the facility from time to time, net of relevant cash balances.

In the above table for 2005, £76.8 million of the gross debt has been shown as fixed rate debt as the particular bank borrowings were fixed in November 2005 for a six month duration.

In December 2005, the Company executed an interest rate hedging programme (effective February 2006), whereby 50% of the projected interest rate exposure to Sterling LIBOR and US Dollar LIBOR was hedged through the application of a series of interest rate swaps, options and zero cost collars. The effect of these derivatives limits the interest rate exposure to Sterling LIBOR at 5.7% and US Dollar LIBOR at 5.8%. The interest rate swaps, options and zero cost collars extend for a three year period for US Dollar and for an eighteen month period for Sterling LIBOR at varying notional principal amounts. The interest rate swaps, options and zero cost collars do not give rise to material differences between book and fair values. The hedged amounts are included in Floating Rate Debt in the above 2005 table as the interest rate hedging programme has an effective date of 24 February 2006.

## Note 6. Called Up Equity Share Capital and Share Premium Account

	2005 £'000	2004 £'000
<b>(a) Authorised</b>		
1,000,000,000 Ordinary Shares of Stg10p each	<b>100,000</b>	100,000
<b>(b) Allotted Equity Share Capital and Share Premium</b>		
	Equity Share Capital Allotted and Fully Paid Number	Share Premium £'000
Ordinary Shares of Stg10p each		
At 1 January 2004	377,841,915	37,784
Issues During the Year		
– Exercise of Share Options	4,553,474	454
– Acquisition of Energy Africa and EAGHL	132,973,351	13,299
– Placing in connection with Acquisition	130,000,000	13,000
At 1 January 2005	<b>645,368,740</b>	<b>64,537</b>
Issues during the year		
– Exercise of Share Options	<b>2,068,983</b>	<b>207</b>
<b>At 31 December 2005</b>	<b>647,437,723</b>	<b>64,744</b>

## Note 7. Merger Reserve

During 2004 the Company issued 132,987,422 ordinary shares relating to the acquisition of Energy Africa Limited and Energy Africa Gabon Holdings Limited. In accordance with the merger provisions of Section 131 of the Companies Act 1985, the company has transferred the premium on the shares issued of £122,335,483, using the market value at the date of the acquisition, to the Merger Reserve.

## Note 8. Profit and Loss Account

	2005 £'000	2004 £'000
At 1 January	<b>14,001</b>	171
Retained Profit for Financial Year	<b>7,489</b>	13,274
Share Based Payments	<b>1,403</b>	556
Currency Translation Adjustments	<b>(15,085)</b>	–
<b>At 31 December</b>	<b>7,808</b>	14,001

The Company has tax losses of £32 million (2004: £7.7 million) that are available indefinitely for offset against future non ring fence taxable profits in the Company. A deferred tax assets has not been recognised in respect of these losses as the Company does not anticipate making non ring fence profits in the foreseeable future.

The profit and loss account of the Company has not been presented separately in these financial statements as permitted by the provisions of Section 230 of the Companies Act 1985.

# Notes to the Financial Statements

continued

## Note 9. Share Based payments

### 2005 Performance Share Plan (PSP)

Under the PSP senior executives can receive conditional awards of rights over whole shares worth up to 150% of salary p.a. (200% in exceptional circumstances). Awards will vest under the PSP subject to a Total Shareholder Return (TSR) based performance condition under which the Company's TSR performance will be measured over the fixed three year period against both the constituents of the FTSE 250 Index (excluding investment trusts) (the 'Index') and a comparator group of Oil and Gas companies. Half of an award will be tested against the Index and the other half against the comparator group. The test is over a three year period starting on the 1 January prior to grant, and an individual must normally remain in employment for three years from grant for the shares to vest. No dividends are paid to participants over the vesting period. Further details in relation to the PSP award measurements are provided in the Remuneration Report.

The shares outstanding under the PSP are as follows:

	PSP Shares	Share price at grant
Outstanding at 1 January 2005	–	–
Granted	1,784,417	187.5
Outstanding at 31 December 2005	1,784,417	187.5

The inputs of the option valuation model were:

Risk free interest rate	4.1% p.a.
Expected volatility	33%
Dividend yield	0.93% p.a.

The expected life is the period from grant to vesting date. The weighted average fair value of the awards granted in 2005 was 112.8p per award.

The Company recognised a total expense of £311,000 (2004: nil) in respect of the PSP.

### 2000 Executive Share Option Scheme (ESOS)

The only share option scheme operated by the Company during the year was the 2000 ESOS. Options granted under the 2000 ESOS normally only become exercisable following the third anniversary of the date of the grant if the performance condition has been met. The awards are tested against the FTSE Index and 100% of awards will vest if the Company's TSR is above the median company of the Index over the three year period following grant. Options awarded under the 2000 ESOS before 24 May 2005 are subject to monthly re-testing on a rolling three year basis if the TSR performance criterion is not met. Options granted on or after 24 May 2005 are not subject to monthly re-testing.

Options have previously been granted under the 1988 ESOS and the 1998 ESOS. Options granted under the 1988 ESOS and the 1998 ESOS are not subject to performance conditions. All awards under the 1988 ESOS and the 1998 ESOS were made prior to 7 November 2002 and therefore, under the transitional provisions, they have not been accounted for in accordance with FRS 20 – Share Based Payments.

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the year.

	2005 number	2005 WAEP	2004 number	2004 WAEP
Outstanding as at 1 January	20,683,036	82.01	21,403,239	83.29
Granted during the year	3,808,600	169.03	3,924,000	111.23
Exercised during the year	(1,563,626)	79.43	(4,539,403)	113.22
Expired during the year	(938,450)	96.37	(104,800)	85.37
<b>Outstanding at 31 December</b>	<b>21,989,560</b>	<b>96.65</b>	20,683,036	82.01
<b>Exercisable at 31 December</b>	<b>9,299,210</b>	<b>68.59</b>	9,675,226	68.41

The weighted average share price at exercise for options exercised in 2005 was 79.43p.

Options outstanding at 31 December 2005 had exercise prices of 61p to 265p and remaining contractual life of one to ten years.

The principal inputs to the options valuation model were:

Risk free interest rate	3.6-5.2% p.a.
Expected volatility	33-55% p.a.
Dividend yield	0.0-2.0% p.a.
Employee turnover	From 0% – 10% pa depending on seniority
Early exercise:	At rates dependent upon seniority and potential gain from exercise

The fair values and expected lives of the options valued for FRS 20 were:

Award year	Weighted Average Exercise Price p	Weighted Average Fair value p	Weighted Average expected life from grant date years
2003	84.4	37.5	5.9
2004	112.6	52.8	4.6
2005	169.3	53.0	4.8

The Company recognised a total expense of £1,057,000 (2004: £545,000) in respect of the ESOS.

#### UK & Irish Share Incentive Plans (SIPs)

The SIP's were launched at the beginning of 2004. These are all employee plans, which have been set up in both the UK and Ireland that enable employees to make contributions out of salary up to prescribed limits each month, which are used by the Plan trustees to acquire Tullow shares ('Partnership shares'). The Company makes a matching contribution to the trustees to acquire a matching number of Tullow shares ('Matching shares') on a one-for-one basis. The SIPs have a three month accumulation period.

The fair value of a Matching share is the market value at grant adjusted for any options included. For this purpose, the grant date is the start of the accumulation period.

For the UK plan, Partnership shares are purchased at the lower of the market values at the start of the Accumulation Period and the purchase date. For the Irish plan, shares are bought at the market price at the purchase date.

Matching shares vest three years after grant and dividends are paid to the employee during this period.

The Company recognised a total expense of £31,000 (2004: £11,000) for the matching shares and £4,000 (2004: nil) for the partnership shares.

#### Note 10. Related Party Transactions

Transactions with the Directors of Tullow Oil plc are disclosed in the Remuneration Report on pages 35 to 41. The Company has taken advantage of the exemptions available under FRS 8 'Related Party Transactions' with regard to the non-disclosure of transactions with Group companies.

#### Note 11. Subsequent Events

There have been no material events affecting the Company since the Balance Sheet date.