KAROON GAS AUSTRALIA LIMITED AND CONTROLLED ENTITIES
ABN 53 107 001 338

HALF-YEAR FINANCIAL REPORT
31 DECEMBER 2007

For further information please contact:

Scott Hosking: Company Secretary or
Telephone: 03 59741044
Fax: 03 59741644
Email: scotthosking@karoongas.com.au
Web: www.karoongas.com.au

Ian Howarth Farrington National
Telephone: 0407 822 319
Email: ian.howarth@farrington.com.au

CONSOLIDATED FINANCIAL REPORT FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

This interim financial report does not include all the notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the annual report for the year ended 30 June 2007 and any public announcements made by Karoon Gas Australia Limited during the interim reporting period in accordance with the continuous disclosure requirements of the *Corporations Act 2001.*

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DIRECTORS' REPORT

FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

Your directors submit the financial report of the consolidated group for the half-year ended 31 December 2007.

Directors

The names and particulars of the directors of the Company who held office during or since the end of the half-year are:

Mr Robert Hosking - Executive Chairman
Mr Mark Smith - Executive Director and Exploration Manager
Mr Geoff Atkins - Non-Executive Director
Mr Stephen Power - Non-Executive Director

Review of Operations

- 3D Seismic survey in permit WA-398-P underway to define new well locations.
- Five Brazilian offshore exploration blocks offered to Karoon.
- Farmin to Peru Block Z38, in the offshore Tumbes Basin offshore Peru.
- Karoon acquired a 67% interest in Timor Sea Permit AC/P8 adjacent to Laminaria field.
- Karoon was offered Peru Block 144 in the Maranon Basin, Peru.

AUSTRALIA

Browse Basin Permits WA-314-P, WA-315-P and WA-398-P

WA-314-P and WA-315-P

Interpretation of the seismic data acquired in 2006 and 2007, continued over the first half of the financial year. Results have confirmed prior assessments and will be used to further define prospects to target and plan the wells for a drilling program later in the year.

The Sedco-703 drilling rig has been contracted for 200 - 225 days and is expected to start drilling in the third quarter of 2008.

Karoon Gas is a 49% interest holder in oil and gas exploration permits WA-314-P and WA-315-P in the offshore Browse Basin located 350 km offshore from the North-Western Australian coastline. Karoon's Joint Venture Partner and Operator in WA-314-P and WA-315-P is ConocoPhillips.

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DIRECTORS' REPORT (cont)

WA-398-P Endurance 3D Seismic Acquisition

A 3D seismic program was contracted with Fugro-Geoteam AS using the vessel the Geo Atlantic. The 3D seismic survey started on January 10 and will cover 1400 sq kms within WA-398-P with a further 500 sq kms approximately outside the permit boundaries.

The survey is now 60% complete and is expected to be completed by the end of the first quarter 2008.

This seismic data will be utilized for the further definition of prospects in WA-398-P and to aid in defining well sites for the drilling program later in 2008/2009

Karoon is a 40% interest holder of WA-398-P, directly south of Karoon's adjacent permits WA-314-P and WA-315-P. ConocoPhillips is Karoon's joint venture partner and operator of the permit.

Bonaparte Basin AC/P8

Karoon entered into an agreement with Woodside Energy Ltd to acquire its 66.67% interest in petroleum permit AC/P8. The permit is located in the Australian waters in the Timor Sea approximately 500 kms north west of Darwin.

The acquisition is conditional on approval of the extension of the permit for a further 5 year term under the relevant legislation for which applications have been filed with the relevant authorities. Karoon is confident that the applications will be successful.

Karoon believes the AC/P8 permit offers good exploration potential, due to its location in an existing oil and gas producing province and its close proximity to several large producing oilfields including the Woodside operated Laminara and Corallina fields.

The AC/P8 permit contains two prospects and at least three leads which will need to be further defined by Karoon and its new joint venture partner Talisman Oil and Gas.

This exciting acquisition represents a major new exploration interest for Karoon and continues the company's strong organic growth.

Gippsland Basin EL 4537

Karoon (through its 100% owned subsidiary Karoon Gas Pty Ltd) has a 100% registered interest EL4537, located within the western on-shore Gippsland Basin of Victoria.

After the 2 well drilling program finished earlier this year, Karoon is reviewing its options in regards to this acreage.

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DIRECTORS' REPORT (cont)

WORLDWIDE

Brazil

In November 2007, Karoon successfully bid for five offshore exploration blocks in the Santos basin adjacent to the state of Santa Catarina, Brazil, just south of Rio De Janeiro.

Karoon was awarded blocks 1037, 1101, 1102, 1165 and 1166 covering 850 square kilometres by ANP (National Agency of Petroleum) in Brazil. The regulatory body of the Brazillian petroleum industry.

Karoon believes the blocks offer good exploration potential in the hundreds of millions of barrels of oil and trillions of cubic feet of gas range.

The blocks are located in an existing oil and gas producing province in close proximity to several large oil and gas producing fields including the Caravela and Coral fields 100km to the south-west and the Merluza field 100km to the north-west. .

Karoon will complete the acquisition of these blocks in March 2008 at an award ceremony in Brazil, at which time Karoon will pay signature bonuses and bid bonds to ANP.

The work program Karoon has submitted for the award of these blocks consists of extensive geological analysis work including the purchase, reprocessing and interpretation of existing seismic. On three of the blocks there is a requirement to acquire a further 170 square kilometres of 3D seismic in the first 3 year term. In the optional second term of 2 years, one well is required to be drilled in each block.

This exciting acquisition represents a major new exploration interest for Karoon and continues the company's strong organic growth.

Peru Z-38

Subsequent to the end of the quarter, Karoon Gas Australia Ltd signed a Farmin Agreement with Vietnam American Exploration Company LLC (Vamex) for the exploration of Block Z38 located in the offshore Tumbes Basin in Northern Peru.

Subject to the receipt of regulatory approvals, Karoon will earn an initial 20% interest in the block by funding a new 2,000 km 2D seismic survey. Karoon also has the option of earning an additional 40% interest in the block by acquiring a further 670 sq km of new, 3D, seismic data.

The geotechnical analysis of the existing data indicates that the block is prospective for both oil and gas. Preliminary economic evaluation by Karoon indicates that any offshore discovery could be rapidly developed due to the close proximity of existing oil and gas infrastructure.

The farmin further represents Karoon's strategy of diversifying its asset base by securing large equity interests in prospective exploration areas.

Vamex is a 100% subsidiary of Pitkin Petroleum, a United Kingdom independent oil and gas company. Vamex is an active explorer in South East Asia and South America.

Peru 144

During the quarter, Karoon was offered and accepted Block 144 in the onshore Maranon Basin in Peru.

Subject to the receipt of regulatory approvals, Karoon will earn an initial 100% interest in the block by carrying out the Primary Term work program of 1000km 2D seismic reprocessing. In the optional Secondary Term the work program includes the acquisition and interpretation of a 300 km 2D seismic survey. In each of the optional Third and Fourth terms the work program is to drill one (1) well.

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DIRECTORS' REPORT (cont)

The geotechnical analysis of the existing data indicates that the block is prospective for both oil and gas.

Forward plans

Karoon aims to complete the seismic acquisition with its joint venture partner, ConocoPhiliips, in the Browse Basin. Karoon looks forward to a successful drilling program in these permits.

In the coming months Karoon will finalise the acquisition of its farmin interest in the Peru Z38 acreage by signing a supreme decree in Lima. At that time Karoon, along with its Peruvian joint venture partner, Vamex, will continue to work through its geological work commitments.

On the 12th March, Karoon's Subsidiary Karoon Petroleo and Gas Ltda will sign the concession agreements and assume control of the Brazilian exploration blocks in the Santos Basin.

In the coming months Karoon will complete the negotiation of the work program for the AC/P8 block, with the regulatory authorities.

Auditor's Declaration

The lead auditor's independence declaration under section 307C of the *Corporations Act 2001* is set out on page 7 for the half-year ended 31 December 2007.

This report is signed in accordance with a resolution of the Board of Directors.

Robert Hosking
Executive Chairman
7th March 2008

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TO THE DIRECTORS OF KAROON GAS AUSTRALIA LIMITED

I declare that, to the best of my knowledge and belief, during the half-yearly ended 31 December 2007 there have been no contraventions of:

1. The auditor independence requirements as set out in the Corporations Act 2001 in relation to the review; and

2. Any applicable code of professional conduct in relation to the review.

Mitchell Wilson & Partners

Doug Mitchell
Partner
7th March 2008

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CONSOLIDATED INCOME STATEMENT FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

	Notes	*31 Dec 2007* *$*	*31 Dec 2006* *$*
Revenues from ordinary activities		2,521,697	639,014
Sundry income		19,801	18,182
Consultancy fees		(203,328)	(609,737)
Computer Support		(251,494)	(116,715)
Employee expenses		(817,589)	(101,519)
Directors fees and superannuation		(43,600)	(32,700)
Exploration Expenditure Written Off		(1,062,152)	(179,743)
Foreign Exchange Variation		(588,878)	(542,757)
Depreciation and amortisation		(164,443)	(79,909)
Legal Fees		(64,697)	(188,606)
Travel and accommodation expenses		(107,182)	(108,067)
Property and Office costs		(131,424)	(62,430)
Share Registry and listing fees		(116,034)	(56,271)
Other expenses from ordinary activities		(278,216)	(172,786)
Profit/(Loss) from ordinary activities before income tax expense	**(2)**	**(1,287,539)**	**(1,594,044)**
Income tax expense relating to ordinary activities		-	-
Net Profit/(Loss) from ordinary activities after income tax attributable to members of the parent entity		**(1,287,539)**	**(1,594,044)**
Total changes in equity other than those resulting form transactions with owners as owners		**(1,287,539)**	**(1,594,044)**
Basic earnings per share		(0.0112)	(0.0187)
Diluted earnings per share		(0.0104)	(0,0173)

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CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2007

	Notes	*31 Dec 2007* *$*	*30 June 2007* *$*
CURRENT ASSETS			
Cash and Cash Equivalents		130,797,821	76,411,604
Receivables		253,130	176,227
Inventories		17,916	17,916
Total Current Assets		**131,068,867**	**76,605,747**
NON-CURRENT ASSETS			
Property, plant and equipment		420,486	453,681
Intangible Assets	1 (r)	1,108,482	129,975
Other – Exploration & Development		7,788,130	6,361,370
Total Non-Current Assets		**9,317,098**	**6,945,026**
Total Assets		**140,385,965**	**83,550,773**
CURRENT LIABILITIES			
Payables		(6,503,882)	(2,463,093)
Provisions		(40,923)	(61,500)
Total Current Liabilities		**(6,544,805)**	**(2,524,593)**
Total Liabilities		**(6,544,805)**	**(2,524,593)**
Net Assets		**133,841,160**	**81,026,179**
EQUITY			
Contributed equity		150,830,252	96,727,732
Accumulated Losses	1 (r)	(19,650,863)	(18,363,324)
Reserve		2,661,771	2,661,771
Total Equity		**133,841,160**	**81,026,179**

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

	Issued Capital Ordinary *$*	*Retained Earnings* *$*	*Share Based Payments Reserve* *$*	*Total* *$*
Balance at 1.7.2006	**34,267,889**	**(3,610,525)**	**2,452,521**	**33,109,885**
Shares issued during the year	22,207,150	-	-	22,207,150
Exercise of Options	250,000	-	-	250,000
Transaction costs arising on share issues	(925,107)	-	-	(925,107)
Profit attributable to members of parent entity	-	(1,594,043)	-	(1,594,043)
Sub-total	**55,799,932**	**(5,204,568)**	**2,452,521**	**53,047,885**
Dividends paid or provided for				
Balance at 31.12.2006	**55,799,932**	**(5,204,568)**	**2,452,521**	**53,047,885**
Balance at 1.7.2007	**96,727,732**	**(18,252,782)**	**2,661,771**	**81,136,721**
Shares issued during the year	51,060,000	-	-	51,060,000
Exercise of Options	5,010,900	-	-	5,010,900
Transaction costs arising on share issues	(1,968,380)	-	-	(1,968,380)
Profit attributable to members of parent entity	-	(1,287,540)	-	(1,287,540)
Goodwill Impairment Loss	-	(110,541)	-	(110,541)
Sub-total	**150,830,252**	**(19,650,863)**	**2,661,771**	**133,841,160**
Dividends paid or provided for				
Balance at 31.12.2007	**150,830,252**	**(19,650,863)**	**2,661,771**	**133,841,160**

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CONSOLIDATED CASH FLOW STATEMENT
FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

	31 Dec 2007 $	31 Dec 2006 $
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipt from Customers (inclusive of goods and services tax)	-	-
Payments to suppliers (inclusive of goods and services tax)	(3,525,398)	(1,256,082)
Interest received	2,521,697	639,014
Net cash flows used in operating activities	**(1,003,701)**	**(617,068)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant and equipment (inclusive of goods and services tax)	(109,756)	(112,204)
Purchase of investments	(1,000,000)	
Refunds (Payments) for exploration and development expenditure	(3,476,130)	5,517,230
Net cash flows used in investing activities	**(4,585,886)**	**5,405,026**
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issue of ordinary shares	54,102,520	21,532,013
Net cash flows from Financing Activities	**54,102,520**	**21,532,013**
Net increase (decrease) in cash held	**48,512,933**	**26,319,971**
Cash at the beginning of the year	**76,411,604**	**15,701,319**
Effects of exchange rate changes on the balance of cash and cash equivalents held in foreign currency	(588,878)	542,757
Cash at the end of the year	**124,335,660**	**42,564,047**

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NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT

The half-year consolidated financial statements are a general purpose financial report prepared in accordance with the requirements of the *Corporations Act 2001*, Australian Accounting Standard AASB 134: Interim Financial Reporting, Urgent Issues Group Interpretations and other authoritative pronouncements of the Australian Accounting Standards Board.

It is recommended that this financial report be read in conjunction with the annual financial report for the year ended 30 June 2007 and any public announcements made by Karoon Gas Australia Limited and its controlled entities during the half-year in accordance with continuous disclosure requirements arising under the *Corporations Act 2001*.

Reporting Basis and Conventions

The half-year report has been prepared on an accruals basis and is based on historical costs modified by the revaluation of selected non-current assets, financial assets and financial liabilities for which the fair value basis of accounting has been applied.

The half-year report does not include full disclosures of the type normally included in an annual financial report.

ACCOUNTING POLICIES

Principles Of Consolidation

The consolidated financial statements incorporate the assets and liabilities of all entities controlled by Karoon Gas Australia Limited ('company' or 'parent entity') as at 31 December 2007 and the results of all controlled entities for the half year then ended. Karoon Gas Australia Limited and its controlled entities together are referred to in this financial report as the consolidated entity. The effects of all transactions between entities in the consolidated entity are eliminated in full.

Subsidiaries are all those entities over which the consolidated entity has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the consolidated entity controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the consolidated entity. They are de-consolidated from the date that control ceases.

The purchase method of accounting will be used to account for the acquisition of subsidiaries by the consolidated entity.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the group.

All controlled entities have a June financial year end.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

Income Tax

The charge for current income tax expense is based on the profit for the year adjusted for any non-assessable or disallowable items. It is calculated using tax rates that have been enacted or are substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on either accounting profit or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future tax profits will be available against which deductible temporary differences can be utilised.

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

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

Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of manufactured products includes direct materials, direct labour and an appropriate portion of variable and fixed overheads. Overheads are applied on the basis of normal operating capacity. Costs are assigned on the basis of weighted average costs.

Property, Plant And Equipment

Each class of property, plant and equipment is carried at cost or fair value less, where applicable, any accumulated depreciation and impairment losses.

Plant and equipment are measured on the cost basis less depreciation and impairment losses.

The carrying amount of plant and equipment is reviewed annually by directors to ensure it is not in excess of the recoverable amount from these assets. The recoverable amount is assessed on the basis of the expected net cash flows that will be received from the assets employment and subsequent disposal. The expected net cash flows have been discounted to their present values in determining recoverable amounts.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

The cost of fixed assets constructed within the economic entity includes the cost of materials, direct labour, borrowing costs and an appropriate proportion of fixed and variable overheads.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of land and buildings are credited to a revaluation reserve in shareholders' equity. Decreases that offset previous increases of the same asset are charged against fair value reserves directly in equity; all other decreases are charged to the income statement.

Each year the difference between depreciation based on the revalued carrying amount of the asset charged to the income statement and depreciation based on the asset's original cost is transferred from the revaluation reserve to retained earnings.

Depreciation

The depreciable amount of all fixed assets including building and capitalised lease assets, but excluding freehold land, is depreciated on a straight line basis over their useful lives to the economic entity commencing from the time the asset is held ready for use. Leasehold improvements are depreciated over the shorter of either the unexpired period of the lease or the estimated useful lives of the improvements.

The depreciation rates used for each class of depreciable assets are:

Class of Fixed Asset	*Depreciation Rate*
Furniture & Fittings	25%
Motor Vehicles	50%
Office Equipment	40%
Computer Hardware	40%
Computer Software	50%

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These gains and losses are included in the income statement. When revalued assets are sold, amounts included in the revaluation reserve relating to that asset are transferred to retained earnings.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

a. EXPLORATION AND EVALUATION EXPENDITURE

Exploration and evaluation expenditure incurred is accumulated in respect of each identifiable area of interest. These costs are only carried forward on the balance sheet where rights to tenure are current and to the extent that costs are expected to be recouped through either the successful development of the area or where activities in the area have not yet reached a stage that permits reasonable assessment of the existence of economically recoverable reserves and active and significant exploration activity in, or in relation to, the area is continuing.

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

Accumulated costs in relation to an abandoned area are written off in full in the income statement during the period in which the decision to abandon the area is made.

Provision for restoration is recognized when there is a legal or constructive obligation to do so. A corresponding restoration asset amount (included in exploration and evaluation expenditure carried forward) of an amount equivalent to the provision is also created. The amount recognised is the estimated cost of restoration, discounted to its net present value and is reassessed each year in accordance with local conditions and requirements. Changes in the estimates of restoration cost estimates are dealt with prospectively by recording an adjustment to the provision and a corresponding adjustment to the restoration asset. The unwinding of the discount on the restoration provision is included in the income statement.

Where it is established that economically recoverable reserves exist in a particular area of interest, the carrying amount attributable to that discovery is reclassified as a development asset.

b. LEASES

Leases of fixed assets where substantially all the risks and benefits incidental to the ownership of the asset, but not the legal ownership that are transferred to entities in the economic entity are classified as finance leases.

Finance leases are capitalised by recording an asset and a liability at the lower of the amounts equal to the fair value of the leased property or the present value of the minimum lease payments, including any guaranteed residual values. Lease payments are allocated between the reduction of the lease liability and the lease interest expense for the period.

Leased assets are depreciated on a straight-line basis over their estimated useful lives where it is likely that the economic entity will obtain ownership of the asset or over the term of the lease.

Lease payments for operating leases, where substantially all the risks and benefits remain with the lessor, are charged as expenses in the periods in which they are incurred.

Lease incentives under operating leases are recognised as a liability and amortised on a straight-line basis over the life of the lease term.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

c. FINANCIAL INSTRUMENTS

Financial instruments are initially measured at cost on trade date, which includes transaction costs, when the related contractual rights or obligations exist. Subsequent to initial recognition these instruments are measured as set out below.

Financial assets at fair value through profit and loss

A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management and within the requirement of AASB 139: Recognition & Measurement of Financial Instruments. Derivatives are also recognized as held for trading unless they are designated as hedges. Realised and recognized gains and losses arising from changes in the fair value of these assets are included in the income statement in the period in which they arise.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are stated at amortised cost using the effective interest rate method.

Held-to-maturity investments

These investments have fixed maturities, and it is the group's intention to hold these investments to maturity. Any held-to-maturity investments held by the group are stated at amortised cost using the effective interest rate method.

Available-for-sale financial assets

Available for sale financial assets include any financial assets not included in the above categories. Available-for-sale financial assets are reflected at fair value. Unrealised gains and losses arising from changes in fair value are taken directly to equity.

Financial liabilities

Non-derivative financial liabilities are recognized at amortised cost, comprising original debt less principal payments and recognized.

Derivative instruments

Derivative instruments are measured at fair value. Gains and losses arising from changes in fair value are taken to the income statement unless they are designated as hedges.

Fair value

Fair value is determined based on current bid prices for all quoted investments. Valuation techniques are applied to determine the fair value for all unlisted securities, including recent arm's length transactions, reference to similar instruments and option pricing models.

Impairment

At each reporting date, the group assess whether there is objective evidence that a financial instrument has been impaired. In the case of available-for sale financial instruments, a prolonged decline in the value of the instrument is considered to determine whether impairment has arisen. Impairment losses are recognized in the income statement.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

d. IMPAIRMENT OF ASSETS

At each reporting date, the group reviews the carrying values of its tangible and intangible assets to determine whether there is any indication that those assets have been impaired. If such an indication exists, the recoverable amount of the asset, being the higher of the asset's fair value less costs to sell and value in use, is compared to the asset's carrying value. Any excess of the asset's carrying value over its recoverable amount is expensed to the income statement.

Impairment testing is performed annually for goodwill and intangible assets with indefinite lives.

Where it is not possible to estimate the recoverable amount of an individual asset, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

e. INTERESTS IN JOINT VENTURES

The economic entity's share of the assets, liabilities, revenue and expenses of joint venture operations are included in the appropriate items of the consolidated statements of financial performance and financial position.

The economic entity's interests in joint venture entities are brought to account using the equity method of accounting in the consolidated financial statements. The parent entity's interests in joint venture entities are brought to account using the cost method.

f. FOREIGN CURRENCY TRANSACTIONS AND BALANCES

Functional and presentation currency

The functional currency of each of the group's entities is measured using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in Australian dollars which is the parent entity's functional and presentation currency.

Transaction and balances

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the year-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined.

Exchange differences arising on the translation of monetary items are recognised in the income statement, except where deferred in equity as a qualifying cash flow or net investment hedge.

Exchange difference arising on the translation of non-monetary items are recognised directly in equity to the extent that the gain or loss is directly recognised in equity, otherwise the exchange difference is recognised in the income statement.

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

Group companies

The financial results and position of foreign operations whose functional currency is different from the group's presentation currency are translated as follows:

Assets and liabilities are translated at year-end exchange rates prevailing at that reporting date.

Income and expenses are translated at average exchange rates for the period.

Retained profits are translated at the exchange rates prevailing at the date of the transaction.

Exchange differences arising on translation of foreign operations are transferred directly to the group's foreign currency translation reserve in the balance sheet. These differences are recognised in the income statement in the period in which the operation is disposed.

g. EMPLOYEE BENEFITS

Provision is made for the company's liability for employee benefits arising from services rendered by employees to balance date. Employee benefits that are expected to be settled within one year have been measured at the amounts expected to be paid when the liability is settled, plus related on-costs. Employee benefits payable later than one year have been measured at the present value of the estimated future cash outflows to be made for those benefits.

h. PROVISIONS

Provisions are recognised when the group has a legal or constructive obligation, as a result of past events, for which it is probable that an outflow of economic benefits will results and that outflow can be reliably measured.

i. CASH AND CASH EQUIVALENTS

Cash and cash equivalents includes cash on hand, deposits held at call with banks, other short - term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within short-borrowings in current liabilities on the balance sheet.

j. REVENUE

Revenue from the sale of goods is recognised upon the delivery of goods to customers.

Interest revenue is recognised on a proportional basis taking into account the interest rates applicable to the financial assets.

Dividend revenue is recognised when the right to receive a dividend has been established. Dividends received from associates and joint venture entities are accounted for in accordance with the equity method of accounting.

Revenue from the rendering of a service is recognised upon the delivery of the service to the customers.

All revenue is stated net of the amount of goods and services tax (GST).

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NOTE 1: BASIS OF PREPARATION OF HALF YEAR FINANCIAL REPORT (cont)

k. GOODS AND SERVICES TAX (GST)

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the balance sheet are shown inclusive of GST.

Cash flows are presented in the cash flow statement on a gross basis, except for the GST component of investing and financing activities, which are disclosed as operating cash flows.

l. COMPARATIVE FIGURES

When required by Accounting Standards, comparative figures have been adjusted to conform to changes in presentation for the current financial year.

m. ADDITIONAL DISCLOSURES

In the June 2007 Consolidated Entity's Income Statement an amount of $824,085 representing services revenue from subsidiaries was overstated in the line items Revenues from Ordinary Activities and Exploration and Evaluation Expenditure Expensed or Written Off. An amendment has been made to the June 2007 comparatives, which has resulted in a nil effect to the profit and loss attributed to members.

Under AASB 3 Business Combinations paragraphs 54 and 55 goodwill is no longer amortised but is subject to annual impairment testing. In the June 2007 financial statement an amount of $17,126 was incorrectly charged to Depreciation and Amortisation expense. A subsequent amendment has been made to the 30 June 2007 Consolidated Balance Sheet to correctly reflect the accounting treatment of the goodwill. This has resulted in the reversal of $61,409 of accumulated amortisation of goodwill in the consolidated Balance Sheet which has a corresponding effect of reducing Intangible assets to $129,975 and increasing Accumulated Losses to $18,363,324.

Impairment of Assets

At each reporting date, the group reviews the carrying values of its tangible and intangible assets to determine whether there is any indication that those assets have been impaired. If such an indication exists, the recoverable amount of the asset, being the higher of the asset's fair value less costs to sell and value in use, is compared to the asset's carrying value. Any excess of the asset's carrying value over its recoverable amount is expensed to the income statement. Impairment testing is performed annually for goodwill. Accordingly as a result of Impairment Testing an amount of $110,542 was written off under the transition from AGAAP to AIFRS rule, resulting in a prior year adjustment of reducing goodwill and a corresponding increase to accumulated losses of $110,542. Prior period comparatives have been adjusted to reflect this change.

In Note 2 Revenue of the 2007 Annual Report, sundry income was understated as a result of a disclosure error. The actual amount was $61,066. This had no effect on the profit and loss attributed to members.

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NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

NOTE 2: PROFIT FOR THE PERIOD

	Consolidated Group	
	31 Dec 2007	*31 Dec 2006*
	$	*$*
The following revenue and expense items are relevant in explaining the financial performance for the interim period		
Write-off of capitalised exploration expenditure	1,062,152	179,743

NOTE 3: DIVIDENDS

No dividends were paid or proposed in the reporting period.

NOTE 4: CONTINGENT LIABILITIES

There has been no change in contingent liabilities since the last annual reporting date, 30 June 2007.

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NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2007

NOTE 5: SEGMENT INFORMATION

	Economic Entity
31 DECEMBER 2007	
Total Segment Revenue	2,541,499
Revenue from Ordinary Activities	2,541,499
Segment Result	(1,459,490)
Loss from ordinary activities before income tax expense	(1,459,490)

	Economic Entity
31 December 2006	
Total Segment Revenue	656,549
Revenue from Ordinary Activities	656,549
Segment Result	(1,401,244)
Loss from ordinary activities before income tax expense	(1,401,244)

NOTE 6: EVENTS SUBSEQUENT TO REPORTING DATE

The WA-398-P Endurance 3D Seismic Survey is continuing, currently the seismic acquisition is 60% complete.

On the 12 March, Karoon Petroleo and Gas Ltda, a 100% owned subsidiary of Karoon, will sign the concession agreements and take title over the Brazilian Exploration blocks 1037, 1101, 1102, 1165 and 1166.

In the coming months concession agreements will be executed with Peru Petro for the Peruvian Permits, Z38 and 144. The agreements are currently held by Peru Petro for final supreme decree by the relevant authorities.

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DIRECTORS' DECLARATION FOR THE HALF-YEAR ENDED 31 DECEMBER 2007.

The directors of the company declare that:

1. The financial statements and notes, as set out on pages 7-20:
   (a) Comply with all relevant Accounting Standards and the Corporations Regulations and
   (b) Give a true and fair view of the consolidated entity's financial position as at 31 December 2007 and of its performance for the half year ended on that date.

2. In directors' opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

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

Robert Hosking
Executive Chairman
7 March 2008

For further information please contact:

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Fax: 03 59741644
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Web: www.karoongas.com.au

Ian Howarth Farrington National
Telephone: 0407 822 319
Email: ian.howarth@farrington.com.au

INDEPENDENT REVIEW REPORT FOR THE HALF-YEAR ENDED 31 DECEMBER 2007.

INDEPENDENT REVIEW REPORT
TO THE MEMBERS OF KAROON GAS AUSTRALIA LIMITED

We have reviewed the accompanying half-year financial report of Karoon Gas Australia Limited and Controlled Entities (the consolidated entity) which comprises the balance sheet as at 31 December 2007, and the income statement, statement of changes in equity and cash flow statement for the half-year ended on that date, a statement of accounting policies, other selected explanatory notes and the directors' declaration.

Directors' Responsibility for the Half-Year Financial Report

The directors of the consolidated entity are responsible for the preparation and fair presentation of the half-year financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the half-year financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on *Review Engagements ASRE 2410 Review of an Interim Financial Report Performed by the Independent Auditor of the Entity,* in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at 31 December 2007 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134: Interim Financial Reporting and the *Corporations Regulations 2001*. As the auditor of Karoon Gas Australia Limited and Controlled Entities, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, provided to the directors of Karoon Gas Australia Limited and Controlled Entities on 5 February 2008 would be in the same terms if provided to the directors as at the date of this auditor's review report.

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INDEPENDENT REVIEW REPORT (cont)

Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Karoon Gas Australia Limited and Controlled Entities is not in accordance with the *Corporations Act 2001* including:

A. Giving a true and fair view of the consolidated entity's financial position as at 31 December 2007 and of its performance for the half-year ended on that date; and

B. Complying with Accounting Standard AASB 134 Interim Financial Reporting and Corporations Regulations 2001.

Mitchell Wilson & Partners

Doug Mitchell
Partner
07 March 2008

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