



27 May 2005

Dear Fellow Shareholder,

SHARE PURCHASE PLAN

The Directors of Karoon Gas Australia Limited ("Karoon") have announced a Share Purchase Plan ("SPP") to be offered to all Karoon shareholders. The non-renounceable SPP is capped at 2.5 million shares priced at A\$3 million and is not underwritten. The SPP is on the same terms as the placement to clients of E. L. & C. Baillieu Stockbroking Ltd announced earlier today under which approximately 10 million fully paid ordinary shares will be placed at a price of A\$1.20 subject to shareholder approval at the Company's upcoming general meeting on the 26th of May 2005.

The funds raised will principally be used to fund the Company's Browse Basin and Gippsland Basin exploration programmes. The funds required for the Browse Basin exploration programme include the Company's expenditure commitment pursuant to its farmout agreement with BG International Limited (as announced to the ASX on the 14th of April 2005, a copy of which is attached) for a permit wide 2D seismic data, 1200 sq km 3D seismic survey and 2 exploration wells.

As a shareholder in Karoon, I am pleased to invite you to participate in the Karoon Gas Australia Limited SPP by subscribing for up to 4,166 new shares worth A\$5,000 at a discount price to market, with no associated brokerage costs.

Each Director holding Karoon shares intends to take up the maximum allocation of 4,166 shares under the SPP (subject to the terms and conditions of the SPP).

Share Purchase Plan Details

The SPP provides smaller shareholders with the opportunity to increase their holdings into a more meaningful and financially viable parcel of shares.

The offer to participate under the SPP is non-renounceable and therefore you are not permitted to transfer your right to subscribe for shares under the SPP. Participation in the SPP is entirely optional and is subject to the terms and conditions specified in this letter and on the attached Application Form.

The number of shares to be issued under the SPP will be limited to a maximum of 2,500,000 shares, which would raise a maximum of A\$3 million. Directors reserve the right to scale back applications received for in excess of this amount.

This offer is open to all shareholders who are registered as holders of fully paid shares in Karoon at 5.00 pm Western Standard Time on the 6th of May 2005 ("the Record Date") and whose address as recorded in the register is in Australia or in any other jurisdiction within which it is lawful for the Company to offer shares under the SPP.

Where a member is expressly noted on the register as a trustee or nominee on account of another person ("Beneficiary"), the Beneficiary will be deemed to be the Eligible Shareholder and any relevant acceptance of the offer and issue of the shares will be made by or to the Beneficiary.

The subscription price under the SPP is A\$1.20 per share. This represents a 8% discount to the average market price of the Company's ordinary shares over the last 5 days on which sales in those shares were recorded before the date of announcement of this offer.

Shareholders are advised that the shares offered under the SPP are a speculative investment and the market price of the shares may change between the date of the offer and the date of the issue of shares under the SPP. Accordingly, the value of the shares received under the SPP may rise or fall.

Subscription Price

Eligible shareholders may apply for shares to a value of any one of the following amounts:

- A\$1,500 for 1,250 shares (minimum amount)
- A\$2,000 for 1,666 shares
- A\$3,000 for 2,500 shares
- A\$5,000 for 4,166 shares (maximum amount)

How to Participate in this Offer

This offer does not require disclosure for the purposes of Chapter 6D of the Corporations Act 2001. Shareholders must rely on their knowledge of Karoon and previous disclosures made by Karoon to the ASX and, if necessary, should consult their professional advisers before deciding whether or not to participate in the SPP.

In order to apply for shares under the offer, complete the enclosed Application Form in accordance with the instructions and forward the Form, together with your cheque, to Karoon's share registry in the reply-paid envelope provided.

Completed Application Forms and full payment must be received by Karoon's share registry no later than 5.00 pm Western Standard Time on the 17th of May 2005.

Timetable

The timetable for the SPP is as follows:

Record date	06 May 2005
Closing date	17 May 2005
Issue of shares and dispatch of holding statements	24 May 2005

Handling Fee

The Company will pay a broker stamping fee of 3% of the amount subscribed to brokers and other financial services licensees who submit applications for shares under the SPP on behalf of clients on Application Forms bearing their stamps.

Should you have any questions or require further information regarding the above, please do not hesitate to contact me on (03) 5974 1044.

Yours faithfully

Karoon Gas Australia Limited

**Robert Hosking
Chairman**