ANNUAL REPORT 2011

Karoon
Gas Australia Ltd

CONTENTS

2010-2011 HIGHLIGHTS SUMMARY

Australia

- The Karoon and ConocoPhillips joint venture received Government environmental approval to conduct drilling in the Browse Basin, which is now expected to start during the fourth quarter calendar year 2011.

- Subsequent to the end of the financial year, the 'Transocean Legend' drilling rig was contracted by the joint venture to drill five wells in the Browse Basin permits, with options for three additional wells.

- Processing and interpretation results from the 2,828 square kilometres of 3D seismic data acquired over the greater Poseidon trend resulted in better definition of Poseidon and several surrounding prospects.

- Karoon increased its equity interest in the WA-314-P permit from 40% to 90%.

Brazil

- Several new leads and prospects in the pre, sub and post salt formations have been defined within Karoon's wholly owned Santos Basin Blocks, in preparation for drilling in the first half of calendar year 2012.

- The 'Blackford Dolphin' semi-submersible drilling rig was contracted to drill three wells in Karoon's wholly owned Santos Basin Blocks.

- Karoon executed farm-in and Joint Operating Agreements with Petróleo Brasileiro SA ('Petrobras') to acquire a 20% interest in two Blocks, S-M-1352 and S-M-1354 in the Santos Basin, Brazil, which are subject to regulatory approvals in Brazil.

- Discovery of hydrocarbons and a subsequent drill stem test in the Maruja exploration well in Block S-M-1352. The production test achieved an equipment constrained stabilised production flow rate of 4,675 barrels of 38 gravity API oil and 0.8 million cubic feet of gas per day through a 1/2 inch choke.

Peru

- Processing and interpretation of 1,500 square kilometres of new 3D seismic data was completed.

- Several new leads and prospects have been defined in Block Z-38 for preparation of a planned drilling program during calendar year 2012.

- Receipt of regulatory approval to increase Karoon's equity interest in Block Z-38 to 75%, subject to the completion of farm-in obligations.

- Entry into the second phase of exploration in Block 144, including the acquisition of 300 kilometres of 2D seismic data.

Capital Raising Activities

- A total of $292.5 million in new funding was raised through a $186.4 million share placement to sophisticated and professional investors during September 2010, $81.8 million through a share purchase plan completed during October 2010 and $24.2 million from the exercise of unlisted options throughout the year.

CHAIRMAN'S REPORT

The 2011 financial year can be summarised as busy technically and commercially with exciting outcomes from seismic work and preparations for drilling getting underway. The year was spent assessing the results of the three seismic acquisition programs completed in 2009-2010 in Australia, Brazil and Peru. Karoon also farmed into Santos Basin Blocks with Petrobras, which led to participation in the light oil discovery at Maruja-1. Preparations have also commenced for Karoon's first Brazilian offshore drilling campaign to start during calendar year 2012.

Results from the three different 3D seismic acquisitions conducted in 2009-2010 have been very encouraging. Interpretation of each seismic data set has added more leads and prospects to Karoon's portfolio. This has the potential to significantly increase the Company's current risked prospective resources.

Seismic work has now progressed to a point where new drilling targets can be selected in Australia, Brazil and Peru and drilling rigs have been contracted for Australia and Brazil. Karoon expects to have a rig secured for Peru in early calendar year 2012. In preparation for the commencement of drilling in Brazil and Peru, Karoon is building a highly experienced drilling team of industry experts with a history in the region. Well planning and logistical work for Brazil will be ongoing into calendar year 2012.

Karoon was encouraged by the outstanding drill stem test at Kronos-1 in the Browse Basin northwest Australia. This test provided legitimacy to the reservoirs in the greater Poseidon trend and this information, when viewed with the Poseidon 3D seismic data, creates a better understanding of the greater Poseidon trend. There are now additional prospects in the immediate area around Poseidon that have the potential to add to the prospectivity of the Poseidon trend.

After delays in obtaining necessary Australian environmental regulatory approvals, Karoon is progressing to the phase-2 drilling campaign in the coming months. The Karoon/ConocoPhillips Joint Venture will be utilising the 'Transocean Legend' drilling rig, the same rig that drilled and tested Kronos-1. The rig is contracted for five firm wells and three optional wells. This new drilling campaign will be targeted at exploring further untested fault block culminations within the greater Poseidon structure, in preparation for decision making on future development of the area. At the completion of this drilling campaign, Karoon is optimistic that the program results will provide the necessary information and certainty to conduct gas sales negotiations and arrange financing for a potential project.

Karoon's Brazilian operations have seen a large amount of activity over the financial year both in the corporate and geological sense. While seismic processing and interpretation has yielded good results during the financial year, Karoon's attempted initial public offering ('IPO') of its South American assets was not successful due to a poor market environment. Karoon proposed to list 30% of its South American asset base on the Brazilian Stock Exchange, the BM&FBOVESPA in São Paulo. However, market conditions in the immediate period around the offering close date were not favourable, with a distinct change in sentiment as a result of both a temporary over supply of Brazilian equities through the largest capital raising in market history and poor performance of recent IPOs.

In the period around the IPO, Karoon moved to secure a specialist team in South America with excellent results. This team of advisers and geotechnical staff have proven themselves and added significant depth of expertise and knowledge to the Karoon team.

Work on Karoon's Santos Basin acreage data is continuing. Karoon has further confirmation of the majority of its existing prospects and now has additional prospects and leads at the pre, sub and post salt levels.

The signing of the 'Blackford Dolphin' semi-submersible drilling rig contract to commence drilling in the Santos Basin in the first half of calendar year 2012 for a firm commitment of three wells will allow Karoon to start testing the suite of prospects by targeting the lowest risk, highest value targets.

During August 2010, Karoon signed a farm-in agreement with Petrobras in the Maruja Block. This agreement was the culmination of a significant amount of work both commercially and technically. Two exploration wells and one appraisal well were drilled. The outcome of these wells was the discovery, subsequent drill stem test and the first appraisal of the Maruja field. Karoon hopes to have more news on the forward plan for the Maruja field in the coming months.

The Peruvian 3D seismic is nearing final interpretation, with positive outcomes. This seismic data has delineated several new prospects and leads at several geological levels. When the seismic is compiled with oil bearing drop core results and third party well data from existing discoveries in the Tumbes and Talara Basins, a very compelling geological case can be built. Karoon is now preparing to commence planning for drilling late calendar year 2012.

While investing funds to conduct drilling and acquire 3D seismic data, Karoon's share price suffered as a result of turbulent, volatile and risk averse markets. However, I am encouraged to see the recent seismic results and the signing of rigs for Brazil and Australia for drilling in the immediate term. On current geological information the prospective resource potential of the Company has received a significant boost. The upcoming period is sure to create some interest in the Company given the expected amount of news flow coming to market regularly over the next eighteen months. During this period, Karoon will have the completed seismic processing, the expected farm-out of Peru and Brazil and the further drilling of five firm wells at Poseidon, three wells in Brazil and two wells in Peru.

We, as Directors and management of Karoon, are working diligently to capitalise on the Company's prospective value by preparing the company for the upcoming global drilling campaign. This should see Karoon emerge as a serious LNG player and global production company. We are confident the work completed in 2010-2011 puts Karoon in a commanding position over its future and provides the basis for growth in the upcoming financial years.

The Board of Directors would like to thank Karoon shareholders for their continued support.

Mr Robert Hosking
Executive Chairman

13 September 2011
Melbourne

Australia

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

Karoon acquired its interest in exploration permits WA-314-P and WA-315-P in the Browse Basin during 2005, adding WA-398-P during 2007. The permits are located in the Browse Basin, 350 kilometres offshore from the northwestern Australian coast and have a combined area of 7,828 square kilometres.

Karoon and its joint venture partner, ConocoPhillips (Browse Basin) Pty Ltd, drilled the Poseidon-1 gas discovery during 2009 with follow-up wells Poseidon-2 and Kronos-1 drilled between July 2009 and June 2010. The Kronos-1 well discovered a separate accumulation with a gas water contact significantly deeper than that determined at Poseidon-1. A facilities constrained drill stem test at Kronos-1 flowed 26 million cubic feet of gas per day through a ½ inch choke.

The Browse Basin now has several gas discoveries, some of which are at a mature appraisal stage and as developments will provide feed gas to major new infrastructure projects in the northwest of Australia. Over the financial year, several potential LNG projects in the Browse Basin were reported as nearing Final Investment Decision ('FID'). As more projects reach FID, the Browse Basin will become a major new hydrocarbon-producing province offshore northwest Australia. FID on a 3.6 million tonne per annum ('MMtpa') floating LNG facility for the Prelude and Concerto gas fields was reportedly made during May 2011. The Inpex operated Ichthys project received Federal Government environmental approvals during June 2010 for an 8.4 MMtpa plant in Darwin and is progressing towards FID. Woodside as the operator of Torosa, Brecknock and Callance gas fields is currently working towards a development decision. Karoon anticipates, that at the completion of the phase-2 drilling in the greater Poseidon trend, the ConocoPhillips/Karoon joint venture will be in a position to move towards adding significantly to the Browse Basin development projects.

Seismic Processing and Interpretation

During the financial year, processing of the 2,828 square kilometre Poseidon 3D seismic survey was completed. The data acquired from the 2009/2010 drilling campaign was analysed and integrated with the new seismic data and the interpretation is forming the basis for planning the next phase in the exploration of the greater Poseidon trend. Several potential well locations were identified and the joint venture commenced preparations for a new drilling campaign.

The joint venture also embarked on the reprocessing of 2D and 3D seismic data over WA-314-P to improve the quality of the subsurface imaging over key exploration trends. The reprocessing project is scheduled to be complete by the end of 2011. The data will then be reinterpreted with the objective of determining potential well locations, one of which will be drilled as part of the phase-2 Browse drilling campaign.

Drilling Management

Throughout the financial year, the Operator conducted preparations to commence drilling, including the submission of the required environmental approval requests to the Department of Sustainability, Environment, Water, Population and Communities ('DSEWPaC'). The DSEWPaC has now approved the EPBC Act Application for the phase-2 drilling campaign.

Subsequent to the financial year end, the semi-submersible drilling rig 'Transocean Legend' was secured for the drilling of a minimum of five wells with options for three additional wells. The Transocean Legend is expected to commence drilling during the fourth quarter of 2011, with at least one well to be drilled in WA-314-P during the drilling campaign.

The drilling campaign is expected to continue for up to two years and is designed to gain greater confidence in the contingent gas resource base with a view to quickly moving forward to selection of a development concept and progressing to the next stage in realising the potential of the Browse Basin acreage.

Equity Interests

During November 2010, Karoon and ConocoPhillips executed an agreement whereby Karoon acquired an additional 50% interest in WA-314-P, taking Karoon's equity interest to 90%. ConocoPhillips will retain a 10% interest in the permit and also remain as Operator. Karoon has the right to determine the final location, depth and target for the commitment well to be drilled on WA-314-P in the upcoming drilling program.

Karoon holds 40% of WA-315-P and WA-398-P, with ConocoPhillips retaining the other 60% interest.

Bonaparte Basin Permit AC/P8

During the financial year, Karoon completed the geological and geophysical evaluation of AC/P8 in preparation for a decision on proceeding into the secondary term of the permit, which carries a commitment to drill an exploration well.

Although the AC/P8 permit is located in an existing oil and gas producing province and is close to several producing oilfields, the joint venture has been unable to identify a prospect that offers a drilling target that would meet the joint venture's minimum economic and probability of success/risk criteria.

The joint venture has the option to apply to surrender the permit before its third anniversary during October 2011. The joint venture has agreed to surrender the permit and subsequent to the end of the financial year, the joint venture applied to the relevant government authorities to surrender the permit.

Equity Interests

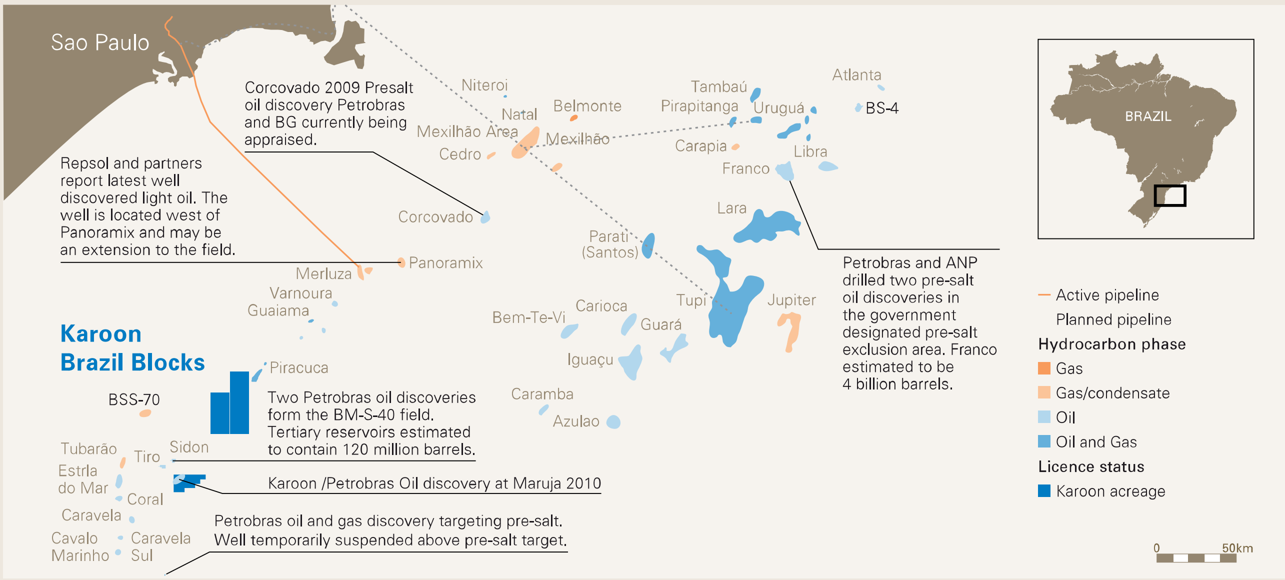
Karoon is the Operator and 66.67% equity holder of AC/P8. Its joint venture partner is Talisman Oil & Gas (Australia) Pty Limited, currently holding 33.33%.

South America

Brazil

During March 2008, Karoon was awarded 100% participation in five offshore exploration Blocks S-M-1037, S-M-1101, S-M-1102, S-M-1165 and S-M-1166 in the Santos Basin, Brazil. The five blocks total 865 square kilometres. During August 2010, Karoon signed joint venture agreements to acquire a 20% participation in Blocks S-M-1352 and S-M-1354, with the remaining 80% interest owned by Petrobras, subject to Agencia Nacional do Petróleo, ('ANP') approval.

Santos Basin Blocks S-M-1037, S-M-1101, S-M-1102, S-M-1165 & S-M-1166



Karoon's Santos Basin Blocks are located 112 kilometres off the coast from the Santa Catarina region of Brazil, south of Rio de Janeiro. The Basin has recently yielded multiple oil discoveries. Discoveries announced in the period since Karoon acquired the first of its Santos Basin Block interests include the Tupi, Carioca, Libra, and other large-scale pre-salt oilfields. During late 2009, Petrobras announced the discovery of a 550 million barrel in place resource in the Piracucá field, just five kilometres to the north-east of Karoon's blocks.

During the last three years, other discoveries have also been made in similar geological features to the prospects mapped in Karoon's current acreage such as Tiro, Sidon, Guaiama, Panoramix and Vampira fields. Karoon is analysing all available exploratory information from these discoveries. This new information, when utilised alongside recent seismic data, has contributed to the delineation of prospects within the acreage. Karoon's economic assessments of its blocks indicate that new fields could be rapidly brought into production due to the relatively shallow water depths of 300-400 metres and proximity to existing oil and gas infrastructure.

Seismic Acquisition, Processing and Interpretation

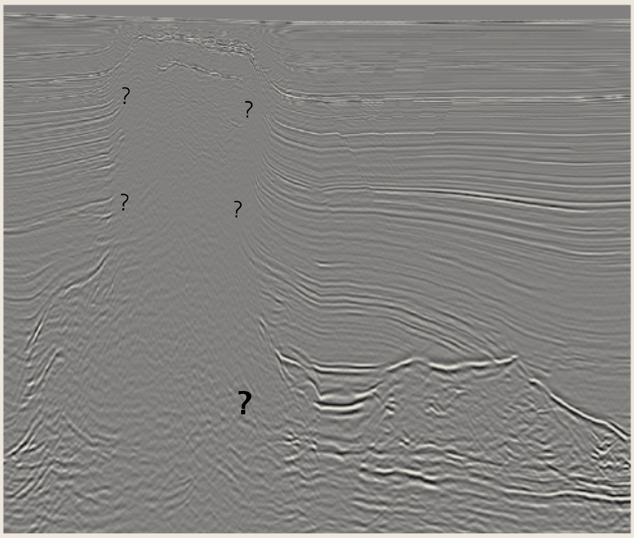
During 2010, Karoon completed a proprietary, wide azimuth ('WAZ') 3D seismic acquisition program, covering an area of 750 square kilometres. This was the first application of WAZ technology in Brazil. This specialised method of acquiring 3D seismic is designed to better image above, around and under salt bodies in the basin. In addition, Karoon merged its existing conventional 3D data, purchased in 2009, with the WAZ into one combined dataset to provide a full multi-azimuth ('MAZ') 3D survey. This data benefits from the application of other state-of-the-art technology, which is yielding excellent structural imaging below the salt. The data is being processed to provide the best possible imaging of structure and amplitude plays that will provide Karoon with the best chance of success in the upcoming drilling campaign.

During September 2011, Karoon received the final processed seismic dataset. Intermediary products were made available earlier to commence interpretation ahead of the completion of final delivery, primarily to assist with well planning. This newly acquired seismic data fulfilled the first period work program commitments for the blocks and is being used by Karoon for the upcoming drilling campaign.

Figure 1 on the following page shows a comparison of seismic quality for the 'old' pre-existing 3D in the area with the new 3D data after it has been exposed using the technology outlined above. This snapshot demonstrates the progress made through processing and the greatly improved imaging of the salt illuminating both the sub-salt and pre-salt play potential.

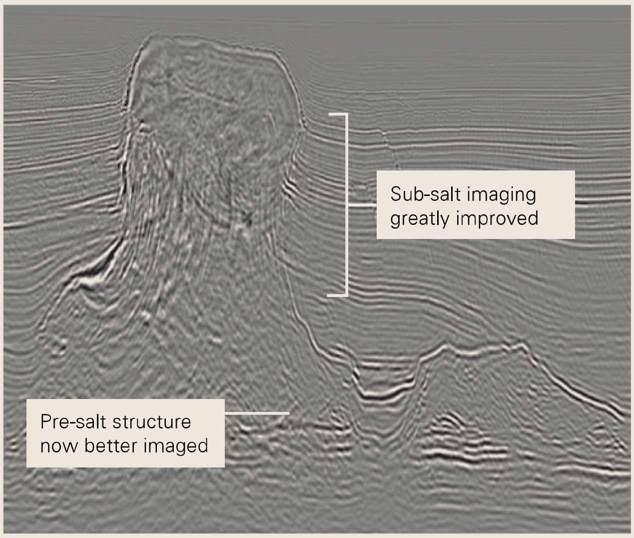
Figure 1. Comparison of seismic quality showing the 'old' pre-existing 3D in the area with the new 3D data after it has been exposed using the technology outlined above.

Early 'Legacy' Data
Pre-stack time mitigation converted to depth



Shallow salt bodies with steep flanks are commonly problematic to image properly, often requiring different acquisition as well as processing techniques which industry has developed over time.

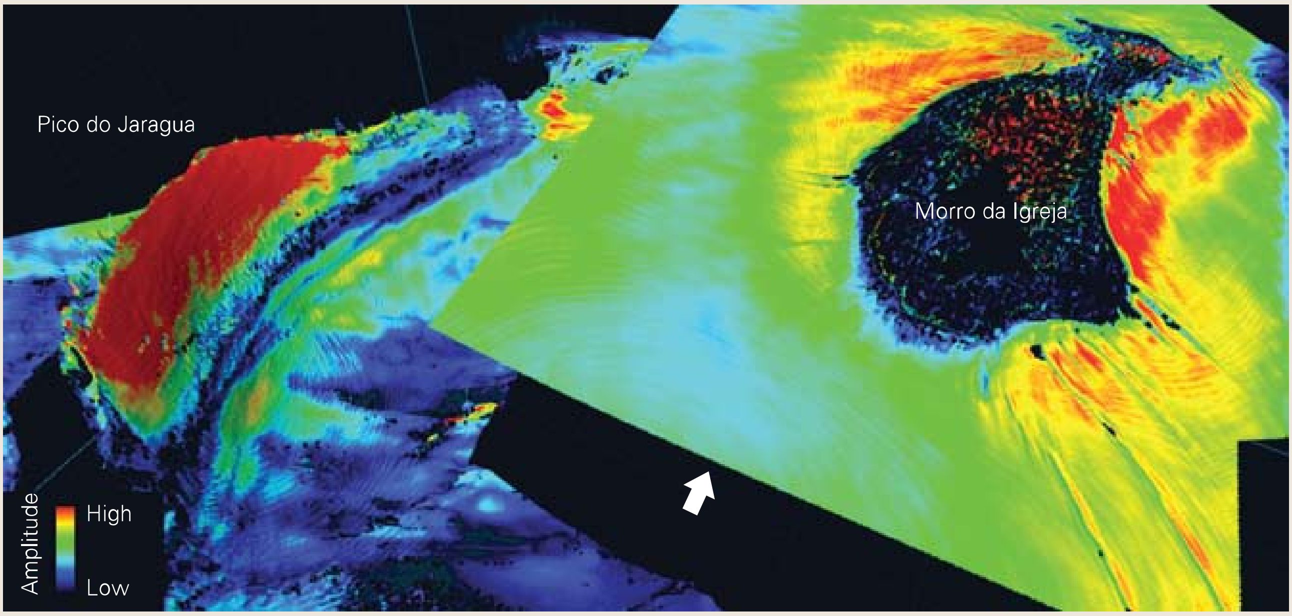
New Data
Multi-Azimuth 3D (MAZ) using reverse time mitigation (RTM)



By acquiring wide-azimuth data in the opposite direction to legacy data and combining the datasets, using state-of-the-art processing techniques has yielded much better results. Salt edges, flanks and below salt are now apparent which has illuminated new sub-salt and pre-salt plays (e.g. around Morro da Igreja salt structure).

Results are very encouraging on the new seismic datasets. Interpretation has confirmed the main post-salt amplitude supported prospects defined on earlier 3D data and further validates these prospects, providing better definition and understanding of their potential.

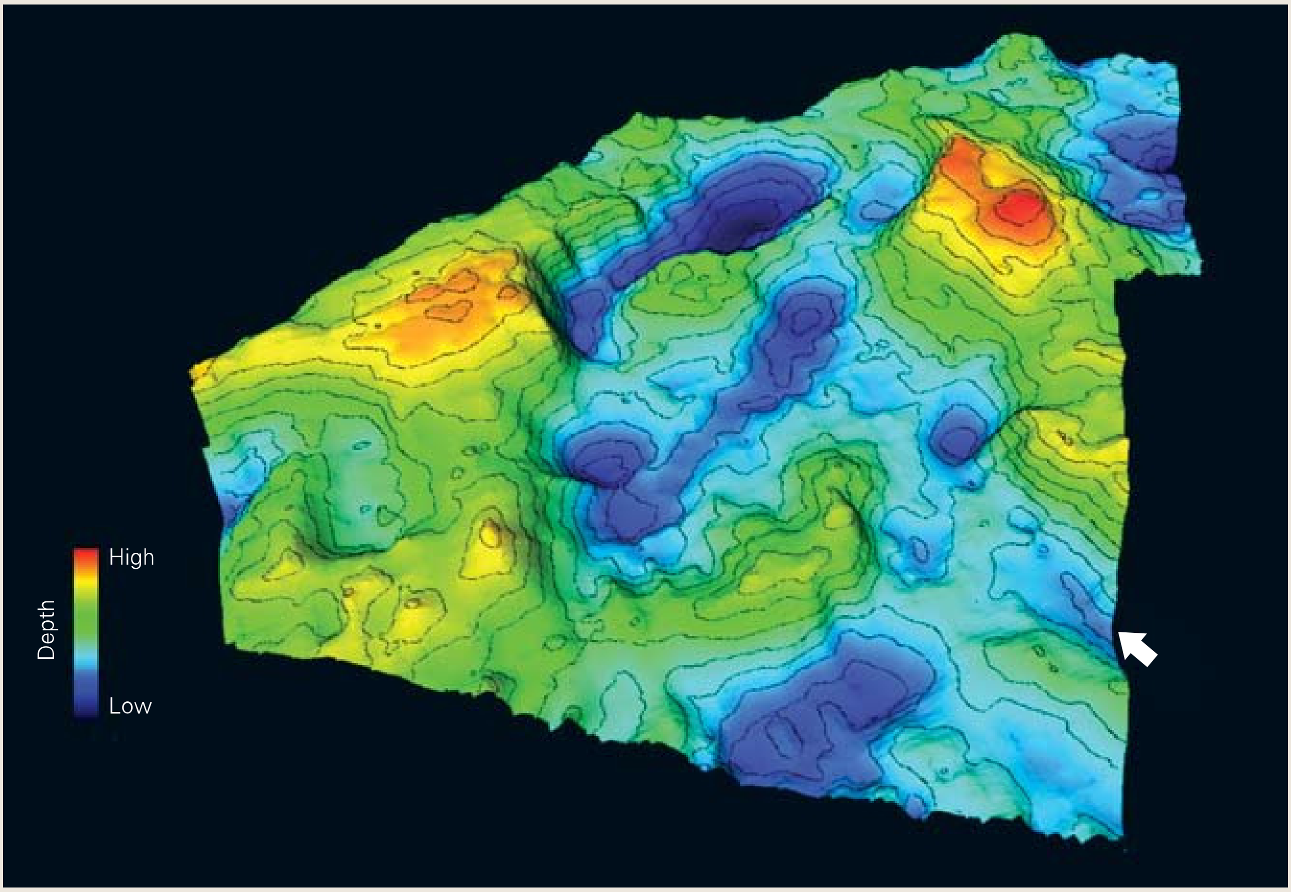
Figure 2. 3D Prospective view across Pico do Jaragua and Morro da Igreja region to demonstrate significant amplitude anomalies at the Santonian and Oligocene levels. Level based on the WAZ ABM intermediate 3D.



An anomaly at the Santonian level on the flank of the Pico do Jaragua salt diapir (seen on the left of Figure 2, at depth) was seen in a dataset purchased during 2008 and remains very well developed on this new data. The amplitudes show the same strong concordance to depth, which is interpreted to be the result of a hydrocarbon fluid contact and a direct indication of hydrocarbons ('DHI'). At the Oligocene level around the Morro da Igreja salt diapir (seen on the right Figure 2 in the shallow) there are also strong amplitude anomalies that rim the salt body which, although in part are faulted, show concordance to depth. This relationship with amplitude to depth provides strong DHI, which helps to reduce risk and allow better quantification of potential volumes ahead of drilling.

The improved quality of the intermediate MAZ 3D seismic data has also facilitated mapping and interpretation to commence at the pre-salt level. Figure 3 on the following page demonstrates the current mapping at this level with clearly defined structural high trends where there are a number of sizeable closures.

Figure 3. 3D Perspective view across the Karoon acreage to demonstrate the mapped large closures at the base of salt, or top pre-salt level. Closures mapped as indicated in greens, yellows and reds.



Drilling

The Blackford Dolphin semi-submersible drilling rig has now been contracted and it is expected to commence drilling during the first half of calendar year 2012. Karoon has a firm commitment to drill three wells. The Karoon drilling team is well advanced in preparations for drilling with environmental and regulatory approval processes underway. Supply bases have been contracted and long lead inventory items are currently being delivered. Drill targets are expected to be finalised at the completion of the interpretation later during calendar year 2011. Karoon also recommenced a farm-out process during September 2011, with initial data room bookings in place and several potential joint venture partners showing an interest in participation.

Equity Interests

Karoon currently has a 100% equity interest in Blocks S-M-1037, S-M-1101, S-M-1102, S-M-1165 and S-M-1166.

Santos Basin Blocks S-M-1352 and S-M-1354

During August 2010, Karoon entered into agreements with Petrobras to farm-in to two contiguous Blocks S-M-1352 and S-M-1354 to earn a 20% interest. Karoon is currently awaiting regulatory approval from the ANP at the date of this Annual Report. During the financial year, Petrobras drilled two exploration wells, one well on each block to satisfy work programs.

The first well, Quasi-1, was drilled on Block S-M-1354, did not make a discovery and was plugged and abandoned in September 2010. This block expired during November 2010 and was formally relinquished by Petrobras during January 2011.

The second well in the campaign, Maruja-1, drilled in Block S-M-1352, discovered high quality light oil of 38 gravity API within a Oligocene aged sandstone reservoir. A full wire-line and pressure sampling program concluded that the reservoir was of high quality with excellent porosity and permeability. This reservoir interval was drill stem tested ('DST'), which although constrained by surface tubing, flowed oil at a maximum stabilised rate of 4,675 barrels of oil per day and 0.8 million cubic feet of gas per day through a ½ inch choke with a flowing well head pressure of 1050 psia. The well was then suspended during January 2011 and may be used as part of a longer production test in preparation for any eventual development that may occur.

The joint venture deemed that commercial flow rates could be achieved from Maruja-1 and requested and subsequently received approval for an evaluation licence from the ANP for an area defining the Maruja field. This evaluation permit included the drilling of an appraisal well and the reduction of Block S-M-1352 to the area around Maruja field.

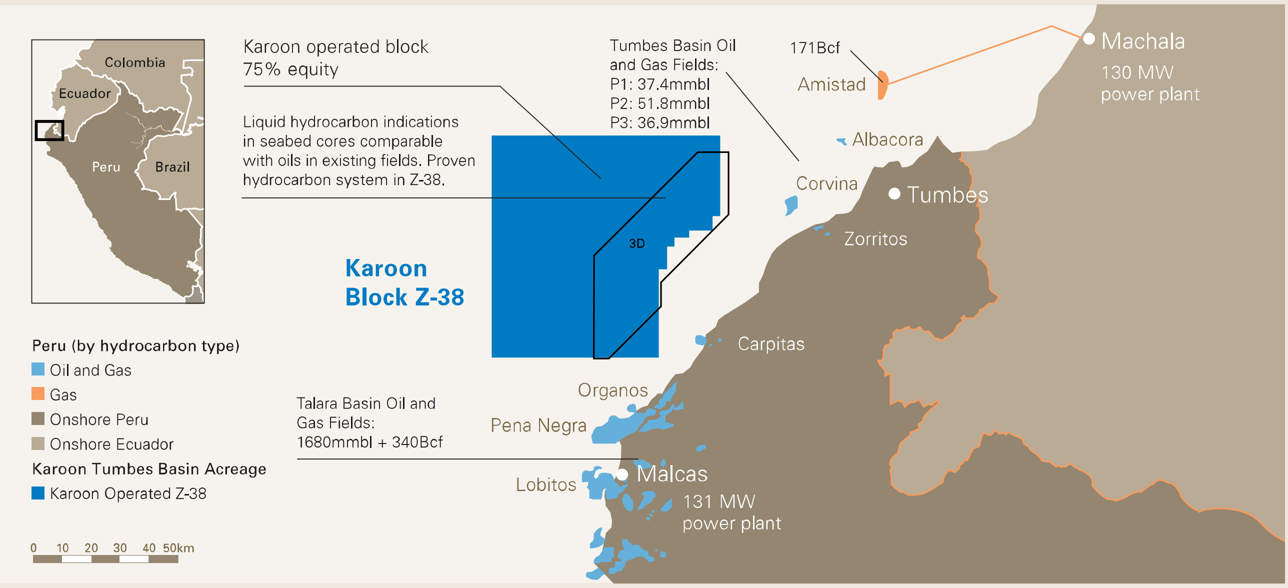
During February 2011, Petrobras commenced the drilling of an appraisal well, Maruja-2, with a location designed to intersect reservoir at over 80 metres down dip and 4.5 kilometres from the initial discovery well. This well found good quality reservoirs contained below the oil/water contact at this location but no hydrocarbons were recovered. A side track well, was also drilled from the initial Maruja-2 well bore, to test further up-dip on the structure. This well encountered a very similar sandstone reservoir of excellent quality, but was also found to be below the oil water contact at this location. The well was plugged and abandoned during April 2011. The confirmation of good quality reservoir in a location on the edge of the interpreted Maruja field demonstrated the continuity of the sands, assisting in the understanding of the field.

An evaluation using all of the newly acquired well data is underway and reprocessing of the existing 3D seismic has commenced to better define and evaluate this field.

Equity Interests

Subject to ANP approval, Karoon will receive a 20% equity interest in Block S-M-1352 with Petrobras holding the remaining 80% equity interest.

Peru Block Z-38



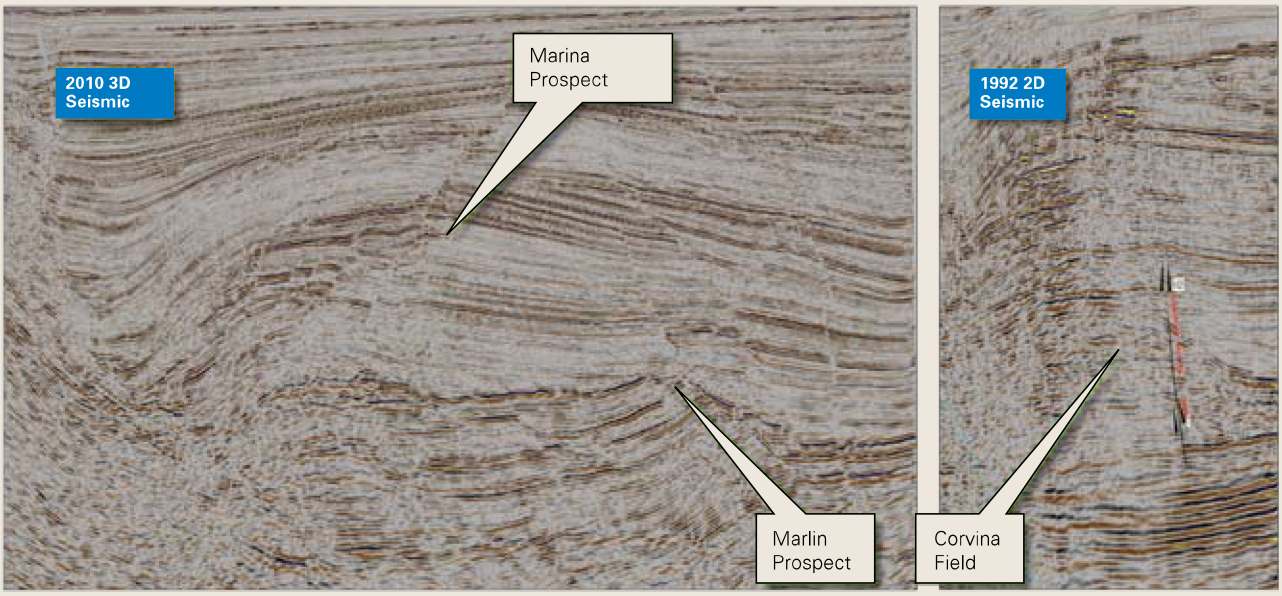
During January 2008, Karoon signed a farm-in agreement to acquire a 20% participating interest in Block Z-38, an offshore block of 4,750 square kilometres located in the Tumbes Basin, 10 kilometres from the northwest coast of Peru. This region has historically been very productive with the first discoveries late in the 1800s, however, much of the offshore portion of the basin remains relatively underexplored. The Talara Basin, to the south of the block continues to produce oil and gas and the Talara Basin has to date produced more than 1.6 billion barrels of oil.

In October 2009, Karoon was approved by the regulator as Operator of the block and negotiated to increase its participating interest in Block Z-38 to 75%. This new participating equity has received further regulatory approval and planning is now underway for a two well drilling campaign to satisfy the third year work commitments.

3D Seismic Interpretation

Interpretation of the new 1,500 square kilometre 3D seismic program was completed during the financial year, fulfilling the second year work program commitments. Detailed prospect oriented interpretation indicates the presence of fifteen prospects and leads. The new prospects vary significantly in size with each of the four largest having an estimate of mean unrisked prospective resource of over 250 million barrels of oil plus significant volumes of gas.

Block Z-38 is interpreted to contain thicker sections of Miocene rocks, of which the two main regional reservoir depositional cycles are interpreted to be well developed. These depositional cycles are in the Zoritos and Tumbes sequences. Reservoirs at both these levels in Block Z-38 are interpreted to be turbidite sands, likely to offer better reservoir quality than the sands seen in the Corvina field which are poorer quality, poorly sorted deltaic sands.



During July 2010, Karoon conducted a seabed coring program. As a result, oil fluorescence was observed in a number of the cores, four of which were further analysed. Oil samples from surrounding fields were collected and have now been analysed with results integrated into Karoon's drop core program analysis and previously published well information. This work confirms that the oil and gas in Block Z-38 is very likely sourced from the same Tertiary source rocks that accumulated in the Tumbes and Talara Basin fields nearby. Karoon believes that this work demonstrates an extension of the known petroleum system and derisks 'source rock' in the Z-38 Block.

Combining drop core results with the 3D seismic and offset well information from surrounding fields has resulted in the development of a geological model that is very supportive of the presence of a diverse range of potentially large commercial oil and gas fields where all the required petroleum system elements are in place.

Drill Planning

During the financial year the Environmental Impact Assessment ('EIA') report was prepared. Regulatory approval applications and planning for the upcoming drilling campaigns is currently continuing. Drilling in the block is expected to commence late in calendar year 2012, with two firm wells and additional optional wells likely. Karoon will be utilising its existing South American drilling team, who have commenced preparations for the drilling and have sought expressions of interest for rigs and services. Karoon is in discussions with other offshore Peruvian Operators to form a 'rig club' with the aim of providing a more cost effective and attractive contract for the drilling rig operator.

Preparations are being made to commence a farm-out of Block Z-38. A data room is being set up for potential companies to review information, commencing during September 2011.

Equity Interest

Karoon is currently the Operator and after completion of the farm-in obligation of the drilling of two wells, Karoon's equity interest in Block Z-38 will be 75%. The remaining 25% equity interest will be held by Vietnam American Exploration Company LLC.

Peru Block 144

Block 144 is located within the onshore Maranon Basin, on the eastern side of the Andes mountain range. The block was awarded to Karoon in April 2009. During the financial year, Karoon continued its geotechnical, social and environmental work in the block and completed the reprocessing of an existing 1,000 kilometres of 2D seismic data.

Seismic Reprocessing and Interpretation

Geophysical interpretation using the reprocessed data has identified the presence of a four-way dip closed structure in the southern portion of the block. This prospect, named Patria, has an estimated net mean prospective resource of approximately 120 million barrels. The Patria prospect is located in proximity to a navigable river and an underutilised oil export pipeline from the Maranon Basin to the Pacific Ocean, offering potential lower cost development opportunities.

The assessment of the reprocessed seismic allowed Karoon to make a decision to commence the next exploratory phase in this block, with a commitment to acquire 300 kilometres of 2D seismic. The new seismic acquisition is expected to be concentrated in the area of the Patria Prospect. Karoon has commenced EIA application works for the seismic acquisition. The new exploration phase will span 24 months, until June 2013.

Equity Interest

Karoon currently has a 100% participating interest in Peru Block 144.

DIRECTORS' REPORT

The Board of Directors submits its Directors' Report on Karoon Gas Australia Ltd and its subsidiaries (the 'Group') for the financial year ended 30 June 2011 (the 'financial year').

Board of Directors

Under the Company's Constitution, the minimum number of Directors that may comprise the Board of Directors is currently three and the maximum number of Directors is 10. Directors are elected and re-elected at annual general meetings of the Company.

The names of the Directors of Karoon Gas Australia Ltd (the 'Company') during the financial year and up to the date of this Directors' Report are set out below:

Mr Robert M Hosking

Executive Chairman

Appointed 11 November 2003.

Robert is the founding Director of the Company and has more than 30 years of commercial experience in the management of several companies. Robert has been involved in the oil and gas industry for 15 years and was the founding director/shareholder of Nexus Energy Limited.

Robert also has a background of more than 17 years commercial experience in the steel industry. He jointly owned and managed businesses involved in the transglobal sourcing, shipping and distribution of steel-related products, with particular expertise gained in Europe and the Asia/Pacific Rim.

Member of the Nomination Committee.

Mr Mark A Smith

Dip. App. Geol, Bsc. (Geology)

Executive Director
and Exploration Director

Appointed 20 November 2003.

Mark has more than 30 years experience as a geologist and exploration manager in petroleum exploration and development in Australia, South East Asia and North America. The bulk of this experience was gained while working with BHP Petroleum. Mark has been directly involved with 11 economic oil and gas discoveries.

Mark has geosciences skills in regional basin and tectonic studies, petroleum systems fairway assessments, prospect evaluations, risking and volumetrics, fault seal prediction and well-site operations. His management skills cover general and human resources management, acreage evaluation and acquisition projects, farm-ins/farm-outs, well-site operations management and management of onshore and offshore drilling operations.

Mr Geoff Atkins

FIE Aust. RMIT Dip. Civ Eng.

Independent Non-Executive Director

Appointed 22 February 2005.

Geoff has over 40 years experience in investigation, planning, design, documentation and project management of numerous significant port, harbour and maritime projects, including container terminals, LNG jetties, heavy lift wharves, cement, coal, bauxite, iron ore and other bulk terminals and naval bases.

Geoff has gained substantial overseas experience completing marine projects in Indonesia, Malaysia, Thailand, Vietnam, Sri Lanka, India, South Africa, Namibia, New Zealand and the United Kingdom. LNG, oil, gas, bulk ports and other large maritime infrastructure projects that Geoff has been involved in have included the design of Woodside Petroleum Ltd's LNG Jetty, tender design of ConocoPhillips' Darwin LNG Jetty and concept designs for the Sunrise LNG Jetty. Geoff has also been involved in investigations of proposed LNG marine terminals in Taiwan, Iran and Israel for BHP Petroleum and the West Kingfish and Cobia oil drilling platforms for ESSO/BHP in Bass Strait.

Chairman of the Audit Committee, Chairman of the Remuneration Committee and Member of the Nomination Committee.

Mr Clark Davey
B. Commerce, FTIA, MAICD

Independent Non-Executive Director

Appointed 1 October 2010.

Clark has over 30 years experience in the Australian natural resources industry as a taxation consultant to oil and gas and mining companies. Clark was a partner at Price Waterhouse and PricewaterhouseCoopers specialising in the natural resources industry. For a number of years he held resource industry leadership roles within both firms. Clark is a member of the Taxation Institute of Australia and the Australian Institute of Company Directors.

Clark brings a wealth of taxation and business advisory knowledge and experience to the Company, including experience with company income tax, petroleum resource rent taxation in Australia and assisting with accounting and capital management. He has assisted many Australian companies with tax management of their joint venture interests and has had considerable experience with merger and acquisition transactions. He has also assisted companies expand their resource industry interests internationally.

Chairman of the Nomination Committee, Member of the Audit Committee and Remuneration Committee.

Mr Stephen Power
B. Juris LLB

Non-Executive Director

Appointed 28 June 2005.

Stephen is a commercial lawyer who has spent over 20 years providing advice to participants in the resources industry in Australia and overseas. Stephen is a partner in a boutique law firm that provides commercial advice to its predominantly listed client base. Stephen has extensive experience in all facets of commercial and resources law, including the oil and gas sector, both in an Australian and international context. Stephen regularly advises on farm-in arrangements, joint ventures, production agreements and other facets of resources-related commercial transactions. In addition to his experience in the resources area, Stephen has a significant practice advising on capital raisings, including the drafting of prospectuses, underwritings and related work, listing advice and the planning and implementation of mergers and acquisitions.

Other current directorships include executive chairman of listed public company Antipa Minerals Limited.

Member of the Audit Committee and Remuneration Committee.

Mr Scott Hosking
B. Commerce

Company Secretary

Appointed as Company Secretary of the Company on 10 March 2006.

Scott has a significant international financial and commercial management background with expertise in equity capital raisings. He has been involved with several commercial ventures over the past 13 years with experience in international trade, finance and internal corporate management. He has previously held support positions to Company Secretaries of listed companies and was involved in the listing of Karoon Gas Australia Ltd.

Meetings

The number of Directors' meetings (including meetings of committees of Directors) and number of meetings attended by each Director of the Company during the financial year were:

Director	Board Meetings		Audit Committee Meetings		Remuneration Committee Meetings	
	A	B	A	B	A	B
Mr Robert Hosking	11	9	1	1	-	-
Mr Mark Smith	11	10	-	-	-	-
Mr Geoff Atkins	11	11	4	4	2	2
Mr Clark Davey	6	6	3	3	2	2
Mr Stephen Power	11	11	4	4	2	2

A. The number of meetings held during the time the Director held office during the financial year.
B. The number of meetings attended during the time the Director held office during the financial year.

Directors' Interests in the Company's Shares and Options

As at the date of this Directors' Report, the Directors held the following number of ordinary shares and options over unissued ordinary shares in the Company:

Director	Ordinary Shares, Fully Paid	Unlisted Other Share Options
Mr Robert Hosking	12,524,462	-
Mr Mark Smith	3,002,037	-
Mr Geoff Atkins	696,784	500,000
Mr Clark Davey	13,144	500,000
Mr Stephen Power	602,142	500,000

Principal Activities

The principal activity of the Company during the course of the financial year continued to be investment in hydrocarbon exploration and evaluation in Australia, Brazil and Peru.

Significant Changes in State of Affairs

During the financial year, the Company successfully completed $292,461,747 in new equity capital raisings:

- 26,631,929 ordinary shares were issued during September 2010 to sophisticated and professional investors via a share placement at $7.00 per ordinary share that raised gross proceeds of $186,423,503;
- 11,692,642 ordinary shares were issued during October 2010 to shareholders via a share purchase plan at $7.00 per ordinary share that raised gross proceeds of $81,848,494; and
- 5,550,000 unlisted options were exercised during the financial year that raised gross proceeds of $24,189,750.

Results

The consolidated result of the Group for the financial year was a loss after income tax expense of $23,304,914 (2010: $14,893,839). The loss for the financial year was largely attributable to net foreign currency losses of $10,440,658, costs of $5,673,914 associated with the proposed public offering on the BM&FBOVESPA in São Paulo (Brazil) and exploration and evaluation expenditure of $3,881,892 for AC/P8 written off.

Financial Position

The net assets of the Group increased by $256,163,753 from 30 June 2010 to $617,867,324 during the financial year. This net increase was largely due to the following:

- Gross proceeds of $292,461,747 raised from the issue of fully paid ordinary shares in the Company.

The Group's working capital, being current assets less current liabilities, has increased from $91,010,773 as at 30 June 2010 to $311,643,637 as at 30 June 2011.

Review of Operations

Information on the operations of the Group is set out in the 2010-2011 Operations review on pages 5 to 14 of this Annual Report.

Future Developments, Business Strategies and Prospects, and Expected Results of Operations

Other than the matters included in this Directors' Report or elsewhere in the Annual Report, future developments, business strategies and prospects of the Company and the expected results of those operations have not been disclosed as the Directors believe that their inclusion would most likely result in unreasonable prejudice to the Company and/or the Group.

Dividends

No dividend has been paid or declared by the Company to shareholders since the end of the previous financial year. The Company intends to pay future dividends during financial periods when appropriate to do so.

Options

As at the date of this Directors' Report, the details of options over unissued ordinary shares in the Company were as follows:

Type of Option	Grant Date	Date of Expiry	Exercise Price Per Option	Number Under Option
ESOP options	29 June 2009	30 October 2011	$6.84	200,000
Other share options	23 November 2009	12 November 2013	$14.07	1,000,000
ESOP options	23 November 2009	12 November 2013	$14.07	530,000
ESOP options	9 December 2009	18 November 2013	$11.50	1,600,000
ESOP options	25 March 2010	18 November 2013	$11.50	100,000
ESOP options	3 September 2010	31 October 2014	$9.77	945,000
ESOP options	12 January 2011	31 October 2014	$9.77	300,000
Other share options	18 November 2010	18 November 2014	$9.48	500,000
ESOP options	18 November 2010	18 November 2014	$9.77	100,000
				5,275,000

During the financial year, the following ordinary shares of the Company were issued on the exercise of options granted. No amounts are unpaid on any of the ordinary shares issued:

Type of Option	Grant Date	Amount Paid Per Ordinary Share	Number of Ordinary Shares Issued
Other share options	27 November 2007	$2.95	500,000
Other share options	22 January 2008	$2.95	500,000
Other share options	27 November 2008	$4.00	250,000
Other share options	1 August 2008	$4.50	750,000
Other share options	27 November 2008	$4.50	750,000
Other share options	1 August 2008	$5.00	750,000
Other share options	27 November 2008	$5.00	750,000
ESOP options	27 November 2007	$2.95	205,000
ESOP options	3 November 2008	$4.00	90,000
ESOP options	3 November 2008	$5.00	905,000
ESOP options	28 November 2008	$5.00	100,000
			5,550,000

No fully paid ordinary shares have been issued since 30 June 2011 as a result of the exercise of Employee Share Option Plan ('ESOP') options and other share options since that date.

For details of options issued to Directors, other key management personnel and the five highest remunerated executives of the Group and Company as remuneration, refer to the Remuneration Report in this Directors' Report.

Information relating to the Company's ESOP and other share options, including details of options granted, exercised, cancelled, forfeited and expired during the financial year and options outstanding at the end of the financial year, is set out in Note 27 of the financial statements.

No option holder has any right under the options to participate in any other share issue of the Company or any other entity.

Indemnification of Directors and Officers

An indemnity agreement has been entered into between an insurance company and the Directors of the Company named earlier in this Directors' Report and with the full time executive officers, directors and secretaries of all Australian subsidiaries. Under this agreement, the insurance company has agreed to indemnify these Directors, full time executive officers, directors and secretaries against any claim or for any expenses or costs which may arise as a result of work performed in their respective capacities. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

As approved by shareholders at the Annual General Meeting held on 12 November 2009, the Company will continue to pay those Director insurance premiums for a period of ten years following termination of their directorships of the Company and will provide each Director with access, upon ceasing for any reason to be a Director of the Company and for a period of ten years following cessation, to any Company records which are either prepared or provided to the Director during the time period they were a Director of the Company.

Proceedings on Behalf of the Company

No person has applied to the Court under Section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

The Company was not a party to any such proceeding during the financial year.

Corporate Governance

In recognising the need for the highest standards of corporate governance and accountability, the Directors support the ASX Corporate Governance Council Principles and Recommendations. The Company's Statement of Corporate Governance is set out on pages 84 to 91 of this Annual Report.

Environmental Regulation

The Company and its subsidiaries are subject to a range of relevant Commonwealth, State and International environmental laws including:

- Environment Protection and Biodiversity Conservation Act 1999 (Cth);
- Petroleum (Submerged Lands) Act 1967 (Cth);
- Petroleum (Submerged Lands) (Management of Environment) Regulations 1999 (Cth);
- The Aboriginal and Torres Strait Islander Heritage and Protection Act 1994 (Cth);
- The Brazilian Federal Constitution (Brazil);
- The Brazilian Petroleum Law (Law No. 9,478, of August 6, 1997) (Brazil);
- The Brazilian Civil Code (Law No. 10,406, of January 19, 2002) (Brazil);
- The Brazilian Corporations Law (Law No. 6,404, of December 15, 1976) (Brazil);
- The Brazilian Bid Law (Law No. 8,666, of June 21, 1993) (Brazil);
- The Brazilian Federal Environmental Law (Law No. 6,938, of August 31, 1981) (Brazil);
- National – Ministry of Energy and Mines – Supreme Decree No. 042-2005-EM – Unique Comprised Text of the Organic Law of Hydrocarbons (which text of the law was approved by Law No. 26221) (Peru);
- National – Congress of the Republic – Law No. 28611 – General Environmental Law (Peru);

- National – Ministry of Energy and Mines – Supreme Decree No. 015-2006-EM – Regulations for Environmental Protection in Hydrocarbon Activities (Peru);
- National – Ministry of Energy and Mines – Supreme Decree No. 043-2007-EM – Safety Rules for Hydrocarbon Activities (Peru);
- National – Ministry of Energy and Mines – Supreme Decree No. 032-2004-EM Rules of Hydrocarbon Exploration and Exploitation Activities (Peru); and
- National – Ministry of Energy and Mines – Supreme Decree No. 052-93-EM – Safety Rules for Hydrocarbon Storage (Peru).

The Board of Directors believes the Company has adequate systems in place for managing its environmental obligations and is not aware of any breach of those environmental obligations as they apply to the Company and/or Group. No circumstances arose during the financial year that required an incident to be reported by the Company and/or Group under environmental legislation.

Greenhouse Gas and Energy Data Reporting Requirements

A carbon tax, or similar regime, has not yet been introduced by the Australian Federal Government. However, greenhouse gas emissions, energy consumption and energy production reporting obligations under the *National Greenhouse and Energy Reporting Act 2007* ('NGER Act') apply.

The Group was not required to register and report greenhouse gas emissions, energy consumption and energy production under the NGER Act for this financial year as it did not meet any of the relevant thresholds from activities conducted within the specified Australian territory between 1 July 2010 and 30 June 2011.

Similarly, the Group's current exploration, as the Operator of AC/P8, is not expected to result in it meeting one of the thresholds under the NGER Act for the next reporting period and, therefore, it is not expected that it will be required to register and report under the NGER Act for the next reporting period.

However, the Company is in the process of assessing a cost effective, reliable and environmentally efficient method of dealing with its future greenhouse gas emissions, energy consumption and energy production reporting obligations.

Non-Audit Services

The Company may decide to engage its external auditor, PricewaterhouseCoopers, on assignments additional to its statutory audit duties where the external auditor's expertise and experience with the Company and/or Group are important.

Details of the amounts paid or payable to the external auditor for non-audit services provided during the financial year are set out in Note 7 of the financial statements.

The Board of Directors has considered the position and, in accordance with written advice received from the Audit Committee, is satisfied that the provision of non-audit services is compatible with the general standard of independence for external auditors imposed by the *Corporations Act 2001*. The Board of Directors is satisfied that the provision of non-audit services by the external auditor did not compromise the external auditor independence requirements of the *Corporations Act 2001* for the following reasons:

(a) all non-audit services have been reviewed by the Audit Committee to ensure they do not impact the impartiality and objectivity of the external auditor; and

(b) none of the services undermine the general principles relating to external auditor independence as set out in *APES 110 'Code of Ethics for Professional Accountants'*, including reviewing or auditing the external auditor's own work, acting in a management or a decision making capacity for the Group, acting as advocate for the Group or jointly sharing economic risk and reward.

External Auditor's Independence Declaration

A copy of the external Auditor's Independence Declaration for the financial year, as required under Section 307C of the *Corporations Act 2001*, is set out on page 31.

No officer of the Company has previously belonged to an audit practice auditing the Company during the financial year.

Remuneration Report (Audited)

The Remuneration Report forms part of this Directors' Report. The information provided in the Remuneration Report has been audited by the external auditor as required by Section 308(3C) of the *Corporations Act 2001*.

The Remuneration Report sets out remuneration information for Karoon Gas Australia Ltd Executive Directors, Non-Executive Directors, other key management personnel and the five highest remunerated executives of the Group and Company.

The Directors and executives disclosed in the Remuneration Report during the financial year are as follows:

Name	Position
Directors	
Mr Robert Hosking	Executive Chairman
Mr Mark Smith	Executive Director and Exploration Director
Mr Geoff Atkins	Independent Non-Executive Director
Mr Clark Davey	Independent Non-Executive Director
Mr Stephen Power	Non-Executive Director
Other key management personnel (Group)	
Mr Scott Hosking	Company Secretary and Chief Financial Officer (Group)
Mr Tim Hosking	Chief Executive Officer South America
Mr Lino Barro	Engineering Manager
Mr Edward Munks	Chief Operating Officer
Other persons who are among the five highest paid remunerated Group and/or Company executives	
Mr Juliano Macedo	Executive Director of Karoon Petróleo & Gas SA

All of the above persons were also Directors or other executives during the previous financial year, except for Mr Clark Davey, Mr Edward Munks and Mr Juliano Macedo.

The Remuneration Report is set out under the following main headings:

A. Remuneration policy (used to determine the nature and amount of remuneration).
B. Details of remuneration.
C. Service agreements.
D. Share-based remuneration.
E. Additional information.

Where appropriate, information which is included in other parts of the financial statements is included in this Directors' Report by reference.

A. Remuneration Policy

The Board of Directors annually reviews remuneration of its Directors and executives aided by the Remuneration Committee. Remuneration includes base salaries and equity-based bonuses and incentive schemes.

The Board of Directors has established a Remuneration Committee which provides overview and recommendations on recruitment, retention and termination policies and procedures for senior executives and the remuneration framework for Directors. The Statement of Corporate Governance provides further information on the role of this committee.

Non-Executive Directors' fees are determined within an aggregate directors' fee pool limit, which is periodically recommended for approval by shareholders. As approved by shareholders at the Annual General Meeting held on 18 November 2010, the maximum aggregate amount, including superannuation contribution, that may be paid to Non-Executive Directors of the Company as remuneration for their services was increased by $200,000 to $400,000 for any financial year. At the same meeting, shareholders approved the remuneration of Directors of the Company for their services as Non-Executive Directors of Karoon Petróleo & Gas SA, a subsidiary of the Company, at $500,000 for any financial year. The maximum aggregate amount payable to Non-Executive Directors of the Company from the Group is $900,000 p.a.

Non-Executive Directors do not receive any performance-related remuneration.

The remuneration structure is based on a number of factors including length of service, particular experience, responsibilities of the individual and the overall performance of the Company. Remuneration involves a balance between fixed and incentive pay, reflecting short and long term performance objectives appropriate to the Company's circumstances and objectives. A proportion of executive remuneration is structured in a manner designed to align the success of the Company with the employees who contributed.

This is achieved by considering the following remuneration components:

- fixed base remuneration; and
- equity-based remuneration within limits set by the Board of Directors.

Options are issued under either the Company's ESOP (to employees) or via other share options (to Directors).

The Directors, other key management personnel and executives of the Company receive a superannuation contribution as required by the Australian Federal Government, which is currently 9.0% p.a., and do not receive any other retirement benefits. Individuals, however, may choose to sacrifice part of their salary to increase payments towards superannuation. It is at their discretion to seek individual financial advice concerning each of their own personal superannuation funds.

Upon retirement, executives are paid employee benefit entitlements accrued to date of retirement.

Relationship Between the Remuneration Policy and Company Performance

Notwithstanding that the Group is still in the exploration and evaluation phase of activities and is still incurring operating losses (excluding net foreign currency losses), the Company believes this policy is effective in increasing long term shareholder wealth through share price appreciation, strengthening the Group's asset base and prospective resources.

The tables below set out summary information about the Group's earnings and movements in shareholder wealth to 30 June 2011:

Financial Year Ended	30 June 2007 $	30 June 2008 $	30 June 2009 $	30 June 2010 $	30 June 2011 $
Revenue	2,878,695	5,320,930	4,868,541	6,459,623	**14,225,048**
Profit (loss) before income tax	(14,642,257)	(6,055,339)	4,452,766	(14,665,017)	**(23,304,914)**
Profit (loss) for financial year	(14,642,257)	(6,055,339)	4,452,766	(14,893,839)	**(23,304,914)**
Net assets at end of financial year	81,136,721	130,742,056	334,658,839	361,703,571	**617,867,324**

Financial Year Ended	30 June 2007 $	30 June 2008 $	30 June 2009 $	30 June 2010 $	30 June 2011 $
Share price at beginning of financial year	1.45	2.38	4.54	9.09	**5.95**
Share price at end of financial year	2.38	4.54	9.09	5.95	**5.23**
Basic profit (loss) per ordinary share	(0.2035)	(0.0485)	0.0302	(0.0842)	**(0.1119)**
Diluted profit (loss) per ordinary share	(0.2035)	(0.0485)	0.0300	(0.0842)	**(0.1119)**

Remuneration Report (Audited) (continued)

B. Details of Remuneration

Details of the remuneration of the Directors, the key management personnel of the Group (as identified in accordance with *AASB 124 'Related Party Disclosures'* as those who had authority for planning, directing and controlling the Group and/or Company activities during the financial year) and the five highest paid executives of the Company and Group are set out in the following tables.

Ended 30 June 2011	Short Term Benefits		Post-Employment Benefits		Long-Term Benefits	Share-based Payments Expense		
Name	Cash Salary and Fees $	Non-Monetary Benefits $	Superannuation Contributions $	Social Security and Indemnity Fund Contributions $	Long Service Leave Provision $	Options $	Remuneration Consisting of Options* %	Total Remuneration $
Executive Directors								
Mr Robert Hosking	409,786	28,895	6,881	-	-	-	-	445,562
Mr Mark Smith	382,263	17,143	34,404	-	13,780	-	-	447,590
Non-Executive Directors								
Mr Geoff Atkins	73,395	2,005	6,606	-	-	399,635	83.0	481,641
Mr Clark Davey *(appointed 1 Oct 2010)*	55,046	2,005	4,954	-	-	282,381	82.0	344,386
Mr Stephen Power	73,394	-	6,606	-	-	399,635	83.3	479,635
Total Directors' remuneration	**993,884**	**50,048**	**59,451**	**-**	**13,780**	**1,081,651**		**2,198,814**
Other key management personnel (Group)								
Mr Scott Hosking^#	252,294	13,462	22,706	-	6,035	267,000	47.6	561,497
Mr Tim Hosking^#†	309,516	12,700	11,043	51,695	-	-	-	384,954
Mr Lino Barro^#	284,862	-	25,638	-	5,833	590,410	65.1	906,743
Mr Edward Munks^# *(appointed 1 Jan 2011)*	126,580	1,648	-	-	-	105,341	45.1	233,569
Total other key management personnel remuneration (Group)	**973,252**	**27,810**	**59,387**	**51,695**	**11,868**	**962,751**		**2,086,763**
Total key management personnel remuneration (Group)	**1,967,136**	**77,858**	**118,838**	**51,695**	**25,648**	**2,044,402**		**4,285,577**
Other Group executive								
Mr Juliano Macedo^ *(appointed 31 Aug 2010)*	262,638	17,685	-	84,239	-	-	-	364,562

* The percentage of total remuneration consisting of options, based on the value of options expensed in the consolidated statement of comprehensive income during the financial year.

† Mr Tim Hosking was appointed Chief Executive Officer South America on 1 December 2010. Before this appointment he was the Company's South American General Manager. Amounts shown above include all Mr Tim Hosking's remuneration during the financial year.

^,# Denotes one of the five highest paid executives of the Group (^) and/or Company (#), as required to be disclosed under the *Corporations Act 2001*.

Ended 30 June 2010	Short Term Benefits		Post-Employment Benefits	Long-Term Benefits	Share-based Payments Expense		
Name	**Cash Salary and Fees $**	**Non-Monetary Benefits $**	**Super-annuation Contributions $**	**Long Service Leave Provision $**	**Options $**	**Remuneration Consisting of Options* %**	**Total Remuneration $**
Executive Directors							
Mr Robert Hosking	400,000	9,925	-	-	305,607	42.7	715,532
Mr Mark Smith	366,972	5,780	33,027	-	281,778	41.0	687,557
Non-Executive Directors							
Mr Geoff Atkins	55,000	-	4,950	-	263,836	81.5	323,786
Mr Stephen Power	55,000	-	4,950	-	263,836	81.5	323,786
Total Directors' remuneration	**876,972**	**15,705**	**42,927**	**-**	**1,115,057**		**2,050,661**
Other key management personnel (Group)							
Mr Scott Hosking^#	229,358	3,934	20,642	-	720,000	73.9	973,934
Mr Tim Hosking^#	201,835	3,141	18,165	-	552,000	71.2	775,141
Mr Lino Barro^#	275,229	-	24,771	-	324,611	52.0	624,611
Mr David Ormerod^#	247,706	-	22,294	-	167,020	38.2	437,020
Mr Jorg Bein^#	243,119	-	21,881	-	324,611	55.1	589,611
Total other key management personnel remuneration (Group)	**1,197,247**	**7,075**	**107,753**	**-**	**2,088,242**		**3,400,317**
Total key management personnel remuneration (Group)	**2,074,219**	**22,780**	**150,680**	**-**	**3,203,299**		**5,450,978**

* The percentage of total remuneration consisting of options, based on the value of options expensed in the consolidated statement of comprehensive income during the previous financial year.

^,# Denotes one of the five highest paid executives of the Group (^) and/or Company (#), as required to be disclosed under the *Corporations Act 2001*.

The amounts disclosed for the remuneration of Directors and other key management personnel include the assessed fair values of options granted during the financial year, at the date they were granted. The value attributable to options is allocated to particular financial periods in accordance with *AASB 2 'Share-based Payment'*, which requires the value of an option at grant date to be allocated equally over the period from grant date to vesting date, adjusted for not meeting the vesting condition. For options that vest immediately, the value is disclosed as remuneration immediately, in accordance with the accounting policy described in Note 1(p) of the financial statements.

Fair values of options are assessed under the Black-Scholes option pricing model. The Black-Scholes option pricing model takes into account the exercise price, the term of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

Remuneration Report (Audited) (continued)

The options have been granted subject to continued employment with the Company but are not subject to the individual meeting pre-determined performance criteria (for example, profitability and sales targets), given the Company is still in the exploration and evaluation phase of activities.

Options have vesting periods of zero to four years, dependent upon the tranche of options being granted and the time elapsed between formal approval and issue of options.

Further information on options is set out in Note 27 of the financial statements.

The Board has prepared a policy in relation to an individual limiting his or her exposure to risk in relation to securities (including options).

Amounts disclosed for remuneration of Directors, other key management personnel and other Group executive exclude insurance premiums paid by the Company in respect of directors' and officers' liability insurance contracts, as the contracts do not specify premiums paid in respect of individual Directors and officers. Information relating to insurance contracts is set out in this Directors' Report.

C. Service Agreements

Remuneration and other terms of employment for the Executive Chairman, Executive Director, Chief Financial Officer, other key management personnel and other Group executive are formalised in either service agreements or employment contracts. Each of these agreements provide for the provision of benefits including health insurance, car allowances and participation, when eligible, in the Company's ESOP or other share options. Other major provisions of the agreements relating to remuneration are set out below.

Details of existing contracts between the Group and the Executive Directors, other key management personnel and other Group executives are as follows:

Name	Term	Expiry	Notice/ Termination Period	Termination Payments	Related Entity	Share Option Eligible	Base Salary (Including Post Employment Benefit Entitlements) Amount
Executive Directors							
Mr Robert Hosking	From 1 May 2011, ongoing	Ongoing	In writing 6 months	Change of control: one year	Ropat Nominees Pty Ltd Hosking Superannuation Fund	Yes	$500,000^
Mr Mark Smith	From 1 May 2011, ongoing	Ongoing	In writing 6 months	Change of control: one year	IERS (Australia) Pty Ltd Bonnie Doon Superannuation Fund	Yes	$500,000^
Other key management personnel (Group)							
Mr Scott Hosking	Ongoing	Ongoing	In writing 3 months	Change of control: one year		Yes	$275,000
Mr Tim Hosking	From 1 December 2010, ongoing	Ongoing	In writing 3 months	Change of control: one year		Yes	$407,800
Mr Lino Barro	Ongoing	Ongoing	In writing 3 months	Change of control: one year	Barro Superannuation Fund	Yes	$310,500

Name	Term	Expiry	Notice/ Termination Period	Termination Payments	Related Entity	Share Option Eligible	Base Salary (Including Post Employment Benefit Entitlements) Amount
Mr Edward Munks	From 1 January 2011, ongoing	Ongoing	In writing 6 months	Change of control: one year	International Corporate Services Pty Ltd	Yes	$436,000
Other Group executive							
Mr Juliano Macedo	From 1 November 2010, ongoing	Ongoing	In writing 1 month			Yes	$407,800

^ Contract terms specify annual base salaries of $550,000 and $600,000 commencing 1 July 2012 and 1 July 2013 respectively. Minimum guaranteed equity remuneration, which is subject to shareholder approval, of 200,000 other share options per annum is also included, together with the provision of additional other share options that are subject to key performance indicators: total shareholder return ('TSR') expansion to equal or outperform the ASX 200 Energy index in the reporting period prior to each tranche (weighting 50%); TSR to exceed 10% p.a. (weighting 25%); and the maintenance of a zero incident safety record in the previous reporting period (weighting 25%).

The contracts for service between the Company, other key management personnel and other Group executive are on a continuing basis, the terms of which are not expected to change in the immediate future.

D. Share-based Remuneration

The Company has one ESOP, which was approved by shareholders at the 2009 Annual General Meeting.

Options are issued to other key management personnel as part of their remuneration to increase goal congruence between senior executives and shareholders in accordance with the Senior Executive Remuneration Policy.

The Company also grants other share options to Directors. Options issued to Directors are approved on a case-by-case basis by shareholders at relevant general meetings.

During the financial year 900,000 options over unissued ordinary shares of the Company were issued to Directors and other key management personnel (refer to Note 28(c) of the financial statements).

The terms and conditions of each grant of options over unissued ordinary shares in the Company affecting remuneration in the current or a future financial year are as follows:

Grant Date	Date Vested and Exercisable	Expiry Date	Exercise Price Per Option	Fair Value Per Option at Grant Date	% Vested
ESOP options					
9 December 2009	13 November 2011	18 November 2013	$11.50	$3.32	-
3 September 2010	31 October 2012	31 October 2014	$9.77	$1.92	-
12 January 2011	31 October 2012	31 October 2014	$9.77	$2.03	-
18 November 2010	18 November 2010	18 November 2014	$9.77	$2.67	100.0
Other share options					
23 November 2009	12 November 2012	12 November 2013	$14.07	$2.40	-
18 November 2010	18 November 2013	18 November 2014	$9.48	$2.75	-

Options are granted for no consideration. When exercisable, each option is convertible into one ordinary share of the Company.

Remuneration Report (Audited) (continued)

ESOP options expire between two and a half and four years after they are granted. The exercise price of ESOP options, issued during the financial year, was based on the volume weighted average price at which the Company's ordinary shares traded on the ASX during the 180 days of trading days before the ESOP options were offered.

The exercise price of other share options is based on the weighted average price at which the Company's ordinary shares traded on the ASX during the 180 days of trading days before the options were offered.

If there is a change of control in the Company, all unexercised options become immediately exercisable.

The option exercise prices are subject to adjustment in certain circumstances as per ASX Listing Rule 6.22.2.

Options granted carry no dividend or voting rights.

Further information on options is set out in Note 27 of the financial statements.

Number of Options Provided as Remuneration During the Financial Year

Details of options over unissued ordinary shares in the Company provided as remuneration to each Director and each of the other key management personnel are set out below:

Name	Number of Options Granted During Financial Year	Value of Options at Grant Date*	Number of Options Vested During Financial Year
Executive Directors			
Mr Robert Hosking	-	-	-
Mr Mark Smith	-	-	-
Non-Executive Directors			
Mr Geoff Atkins	-	-	-
Mr Clark Davey	500,000	$1,375,000	-
Mr Stephen Power	-	-	-
Other key management personnel (Group)			
Mr Scott Hosking	100,000	$267,000	100,000
Mr Tim Hosking	-	-	-
Mr Lino Barro	100,000	$192,000	-
Mr Edward Munks	200,000	$406,000	-
Total key management personnel (Group)	900,000	$2,240,000	100,000

* The value at grant date, calculated in accordance with AASB 2, of options granted during the financial year as part of their remuneration.

No options over unissued ordinary shares in the Company lapsed during the financial year.

Shares Issued on the Exercise of Options Provided as Remuneration

Details of fully paid ordinary shares in the Company issued as a result of the exercise of remuneration options to each Director and other key management personnel during the financial year are set out below:

Name	Date of Exercise of Options	Number of Ordinary Shares Issued	Value at Exercise Date*	Amount Paid Per Ordinary Share
Executive Directors				
Mr Robert Hosking	25 February 2011	750,000	$1,537,500	$5.00
	25 February 2011	750,000	$1,912,500	$4.50
	2 May 2011	250,000	$625,000	$4.00
Mr Mark Smith	25 February 2011	750,000	$1,537,500	$5.00
	25 February 2011	750,000	$1,912,500	$4.50

Name	Date of Exercise of Options	Number of Ordinary Shares Issued	Value at Exercise Date*	Amount Paid Per Ordinary Share
Non-Executive Directors				
Mr Geoff Atkins	30 September 2010	220,000	$1,012,000	$2.95
	1 October 2010	280,000	$1,436,400	$2.95
Mr Clark Davey	-	-	-	-
Mr Stephen Power	23 September 2010	200,000	$924,000	$2.95
	30 September 2010	300,000	$1,380,000	$2.95
Other key management personnel (Group)				
Mr Scott Hosking	12 October 2010	100,000	$628,000	$2.95
	11 April 2011	50,000	$124,000	$5.00
	2 May 2011	50,000	$75,000	$5.00
Mr Tim Hosking	-	-	-	-
Mr Lino Barro	14 February 2011	100,000	$273,000	$5.00
Mr Edward Munks	22 March 2011	15,000	$23,250	$5.00
	11 April 2011	15,000	$37,200	$5.00

* The value at exercise date of options that were granted as part of their remuneration and were exercised during the financial year has been determined as the intrinsic value of the options at that date.

No amounts are unpaid on any ordinary shares issued on the exercise of the above remuneration options.

E. Additional Information

Details of Remuneration – Options

For each grant of options in current or previous financial years which results in an amount being disclosed in the Remuneration Report as a share-based payment expense in the financial year to Directors and other key management personnel, the percentage of the grant that vested in the financial year and the percentage that was forfeited because the individual did not meet the service criteria is set out below:

Name	Financial Year End Granted	Vested %	Forfeited %	Financial Years in Which Options May Vest	Maximum Total Value of Grant Yet to Vest
Executive Directors					
Mr Robert Hosking	-	-	-	-	-
Mr Mark Smith	-	-	-	-	-
Non-Executive Directors					
Mr Geoff Atkins	2010	-	-	30 June 2013	$536,529
Mr Clark Davey	2011	-	-	30 June 2014	$1,092,619
Mr Stephen Power	2010	-	-	30 June 2013	$536,529
Other key management personnel (Group)					
Mr Scott Hosking	2011	100.0	-	-	-
Mr Tim Hosking	-	-	-	-	-
Mr Lino Barro	2010	-	-	30 June 2012	$190,287
	2011	-	-	30 June 2013	$117,982
Mr Edward Munks	2011	-	-	30 June 2013	$300,659

No options will vest if the service criteria conditions are not met, therefore the minimum value of the option yet to vest is $Nil.

The maximum value of options yet to vest was determined as the amount of the grant date fair value of the options that is yet to be expensed in the consolidated statement of comprehensive income.

Loans to Directors and Other Key Management Personnel

There were no loans to Directors or other key management personnel during the financial year.

Other Transactions with Directors and Other Key Management Personnel

Refer to Note 29 of the financial statements for other transactions with Directors and other key management personnel during the financial year.

Matters Arising Subsequent to the End of the Financial Year

Other than the matters disclosed in Note 31 of the financial statements, there has not been any matter or circumstance which has arisen since 30 June 2011 that has significantly affected, or may significantly affect:

(a) the Group's operations in future financial years;

(b) the results of those operations in future financial years; or

(c) the Group's state of affairs in future financial years.

This Directors' Report, incorporating the Remuneration Report, is made in accordance with a resolution of the Directors.

On behalf of the Directors:

Mr Robert Hosking
Executive Chairman

13 September 2011
Melbourne

AUDITOR'S INDEPENDENCE DECLARATION

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
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As lead auditor for the audit of Karoon Gas Australia Ltd for the year ended 30 June 2011, I declare that to the best of my knowledge and belief, there have been:

(a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

(b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Karoon Gas Australia Ltd and the subsidiaries it controlled during the period.

Charles Christie
Partner
PricewaterhouseCoopers

Melbourne
13 September 2011

FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2011

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2011

	Note	Consolidated 2011 $	Consolidated 2010 $
Revenue	4	**14,225,048**	6,459,623
Other income	4	**-**	914
Total revenue and other income		**14,225,048**	6,460,537
Computer support		**(623,097)**	(489,646)
Consulting fees		**(985,930)**	(822,971)
Depreciation and amortisation expense	5	**(531,245)**	(415,667)
Employee benefits expense (net)		**(8,529,761)**	(6,719,729)
Exploration and evaluation expenditure expensed or written off	5	**(4,662,554)**	(136,812)
Farm-out costs		**(258,385)**	(89,112)
Finance costs	5	**(456,290)**	(244,275)
Insurance expense		**(575,172)**	(215,429)
Legal fees		**(349,722)**	(452,202)
Net foreign currency losses		**(10,440,658)**	(8,514,337)
Property costs		**(775,632)**	(274,646)
Share registry and listing fees		**(518,330)**	(485,285)
Telephone and communication expenses		**(286,075)**	(164,276)
Travel and accommodation expenses		**(754,146)**	(842,774)
Brazilian initial public offering expenses		**(5,673,914)**	(407,317)
Other expenses		**(2,109,051)**	(851,076)
Total expenses		**(37,529,962)**	(21,125,554)
Loss before income tax		**(23,304,914)**	(14,665,017)
Income tax expense	6	**-**	(228,822)
Loss for financial year		**(23,304,914)**	(14,893,839)
Other comprehensive income (loss):			
Exchange differences arising from the translation of financial statements of foreign subsidiaries		**(9,347,931)**	2,833,583
Income tax relating to components of other comprehensive loss		**-**	-
Other comprehensive income (loss) for financial year, net of tax		**(9,347,931)**	2,833,583
Total comprehensive loss for financial year		**(32,652,845)**	(12,060,256)
Earnings per share for loss attributable to equity holders of the Company:			
Basic loss per ordinary share	9	**(0.1119)**	(0.0842)
Diluted loss per ordinary share	9	**(0.1119)**	(0.0842)

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 30 JUNE 2011

	Note	Consolidated 2011 $	2010 $
Current assets			
Cash and cash equivalents	10	**266,839,144**	87,122,836
Receivables	11	**4,003,566**	4,873,578
Inventories	12	**279,892**	360,081
Security deposits	13	**41,301,743**	12,091,872
Other assets	14	**3,525,878**	710,376
Total current assets		**315,950,223**	105,158,743
Non-current assets			
Plant and equipment	15	**2,216,532**	607,552
Intangible assets	16	**480,041**	354,922
Exploration and evaluation expenditure carried forward	17	**276,465,002**	265,243,372
Security deposits	13	**26,058,837**	4,547,690
Other assets	14	**1,102,759**	-
Total non-current assets		**306,323,171**	270,753,536
Total assets		**622,273,394**	375,912,279
Current liabilities			
Trade and other payables	18	**4,306,586**	13,912,243
Income tax liability	6	**-**	235,727
Total current liabilities		**4,306,586**	14,147,970
Non-current liabilities			
Provisions	19	**99,484**	60,738
Total non-current liabilities		**99,484**	60,738
Total liabilities		**4,406,070**	14,208,708
Net assets		**617,867,324**	361,703,571
Equity			
Issued capital	20	**664,894,335**	381,147,212
Accumulated losses		**(58,015,354)**	(34,710,440)
Share-based payments reserve		**18,348,582**	13,279,107
Foreign currency translation reserve		**(7,360,239)**	1,987,692
Total equity		**617,867,324**	361,703,571

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2011

	Consolidated				
	Issued Capital $	Accumulated Losses $	Share-based Payments Reserve $	Foreign Currency Translation Reserve $	Total Equity $
Balance as at 1 July 2009	**347,331,271**	**(19,816,601)**	**7,990,060**	**(845,891)**	**334,658,839**
Loss for financial year	-	(14,893,839)	-	-	(14,893,839)
Exchange differences arising from the translation of financial statements of foreign subsidiaries	-	-	-	2,833,583	2,833,583
Total comprehensive loss for financial year	**-**	**(14,893,839)**	**-**	**2,833,583**	**(12,060,256)**
Transactions with owners in their capacity as owners:					
Ordinary shares issued	34,104,259	-	-	-	34,104,259
Transaction costs arising on ordinary shares issued	(288,318)	-	-	-	(288,318)
Share-based payments expense	-	-	5,289,047	-	5,289,047
	33,815,941	-	5,289,047	-	39,104,988
Balance as at 30 June 2010	**381,147,212**	**(34,710,440)**	**13,279,107**	**1,987,692**	**361,703,571**
Loss for financial year	**-**	**(23,304,914)**	**-**	**-**	**(23,304,914)**
Exchange differences arising from the translation of financial statements of foreign subsidiaries	**-**	**-**	**-**	**(9,347,931)**	**(9,347,931)**
Total comprehensive loss for financial year	**-**	**(23,304,914)**	**-**	**(9,347,931)**	**(32,652,845)**
Transactions with owners in their capacity as owners:					
Ordinary shares issued	**292,461,747**	**-**	**-**	**-**	**292,461,747**
Transaction costs arising on ordinary shares issued	**(8,714,624)**	**-**	**-**	**-**	**(8,714,624)**
Share-based payments expense	**-**	**-**	**5,069,475**	**-**	**5,069,475**
	283,747,123	**-**	**5,069,475**	**-**	**288,816,598**
Balance as at 30 June 2011	**664,894,335**	**(58,015,354)**	**18,348,582**	**(7,360,239)**	**617,867,324**

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2011

		Consolidated	
	Note	2011 $	2010 $
Cash flows from operating activities			
Receipts from customers (inclusive of GST refunds)		**1,669,745**	571,428
Payments to suppliers and employees (inclusive of GST)		**(16,636,777)**	(6,951,002)
Payments for exploration and evaluation expenditure expensed		**(683,108)**	(136,812)
Interest received		**10,324,046**	4,954,195
Interest and other costs of finance paid		**(456,290)**	(244,275)
Income taxes paid		**(220,227)**	-
Net cash flows used in operating activities	26(a)	**(6,002,611)**	(1,806,466)
Cash flows from investing activities			
Purchase of plant and equipment		**(2,058,087)**	(235,204)
Purchase of computer software		**(320,991)**	(283,677)
Payments for exploration and evaluation expenditure capitalised		**(34,129,282)**	(157,420,044)
Payment of security deposits		**(51,875,314)**	(1,767,942)
Proceeds from disposal of non-current assets		**31,374**	-
Net cash flows used in investing activities		**(88,352,300)**	(159,706,867)
Cash flows from financing activities			
Proceeds from issue of ordinary shares		**292,461,747**	29,592,031
Payments for transaction costs arising on ordinary shares issued		**(8,714,624)**	(800,819)
Net cash flows provided by financing activities		**283,747,123**	28,791,212
Net increase (decrease) in cash and cash equivalents		**189,392,212**	(132,722,121)
Cash and cash equivalents at beginning of financial year		**87,122,836**	228,238,280
Effect of exchange rate changes on the balance of cash and cash equivalents held in foreign currencies		**(9,675,904)**	(8,393,323)
Cash and cash equivalents at end of financial year	10	**266,839,144**	87,122,836

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2011

Note 1. Summary of Significant Accounting Policies

Karoon Gas Australia Ltd (the 'Company') is a public company limited by shares and is listed on the ASX. It is incorporated and domiciled in Australia. The registered office of Karoon Gas Australia Ltd and the principal place of business is Office 7A, 34-38 Lochiel Avenue, Mount Martha, VIC, 3934. The technical office is located at Level 25, 367 Collins Street, Melbourne, VIC, 3000.

The financial statements are for the consolidated entity consisting of Karoon Gas Australia Ltd and its subsidiaries (the 'Group').

The nature of the operations and principal activities of the Group are described in the Directors' Report.

The following is a summary of significant accounting policies adopted by the Group in the preparation of these consolidated financial statements. The accounting policies have been consistently applied to all the financial years presented, unless otherwise stated.

(a) Basis of Preparation

These general purpose financial statements have been prepared in accordance with the requirements of the *Corporations Act 2001*, relevant Australian Accounting Standards, Urgent Issues Group Interpretations and other authoritative pronouncements of the Australian Accounting Standards Board ('AASB').

Where necessary, comparative information has been reclassified to achieve consistency in disclosure with financial year amounts and other disclosures.

Historical Cost Convention

The financial statements have been prepared on an accrual basis under the historical cost convention as modified, when relevant, by the revaluation of selected financial assets and financial liabilities for which the fair value basis of accounting has been applied.

Compliance with International Financial Reporting Standards

The financial statements comply with International Financial Reporting Standards as issued by the International Accounting Standards Board ('IASB').

Going Concern

On the basis of the present level of operations and after consideration of the Group's ability to:

(i) farm-out its interests in exploration permits/Blocks in order to fund future exploration expenditure commitments;

(ii) raise capital through the issue of new ordinary shares in the Company to meet working capital requirements and/or shortfalls in exploration expenditure commitments; and/or

(iii) manage its existing cash and future cash flows to meet its current obligations and future plans,

the Directors are of the opinion that for the next 12 month period from the date of signing the Directors' Declaration, the Group and Company will have sufficient liquidity to meet their existing commitments and accordingly present the financial statements on a going concern basis.

Significant Accounting Estimates, Assumptions and Judgements

The preparation of financial statements requires the use of certain significant accounting estimates. It also requires management to exercise its judgement in the process of applying Group accounting policies. The areas involving a high degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 2.

Change in Accounting Policy

The Group has applied revised Australian Accounting Standard *AASB 107 'Statement of Cash Flows'* issued by the AASB, which was mandatory to apply to the current reporting period.

Under the revised accounting standard, only exploration and evaluation expenditure that is capitalised may be presented as cash flows from investing activities. Under the Group's previous accounting policy, all cash flows associated with exploration and evaluation expenditure (comprising both amounts expensed and capitalised) were classified as cash flows from investing activities. The change in accounting policy increased net cash outflows used in operating activities and decreased net cash outflows used in investing activities for the previous financial year by $136,812.

Note 1. Summary of Significant Accounting Policies (continued)

(b) Principles of Consolidation

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Karoon Gas Australia Ltd as at 30 June 2011 and the results of all subsidiaries for the financial year then ended.

A subsidiary is any entity controlled by Karoon Gas Australia Ltd whereby it has the power to control the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Interests in subsidiaries are set out in Note 21.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves allocating the cost of the business combination to the fair value of the assets acquired, liabilities and contingent liabilities assumed at the date of acquisition. Acquisition related costs are expensed as incurred and the associated cash flows are classified as operating activities in the consolidated statement of cash flows.

All subsidiaries have a financial year end of June, with the exception of: Karoon Petróleo & Gas SA; KEI (Peru 112) Pty Ltd, Sucursal del Peru; and KEI (Peru Z38) Pty Ltd, Sucursal del Peru. These subsidiaries and branches have a financial year end of December in accordance with relevant Brazilian and Peruvian tax and accounting regulations respectively.

Accounting policies of subsidiaries have been changed, where necessary, to ensure consistency with the policies applied by the Group.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated on consolidation. Unrealised losses are also eliminated, unless the transaction provides evidence of the impairment of the asset transferred.

Where subsidiaries have entered or left the Group during the financial year, their operating results are included or excluded from the date control was obtained or until the date control ceased respectively.

(c) Segment Information

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for assessing performance and in determining the allocation of resources of the operating segments, has been identified as the Executive Chairman and the Executive Director/Exploration Director.

(d) Revenue

Revenue is recognised and measured at the fair value of the consideration received or receivable to the extent it is probable that economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Sales Revenue

Revenue from the sale of goods is recognised upon the delivery of goods to the buyer and all significant risks and rewards of ownership are transferred. Revenue from the rendering of a service is recognised upon the delivery of the service. All revenue is stated net of the amount of GST.

Dividend Revenue

Dividend revenue is recognised when the right to receive a dividend has been established.

Interest Income

Interest income is recognised using the effective interest rate method, which, for floating rate financial assets, is the rate inherent in the relevant financial asset.

(e) Foreign Currency Transactions and Balances

Functional and Presentation Currency

Items included in the financial statements of each of the Group's subsidiaries are measured using the currency of the primary economic environment in which the subsidiary or branch operates (the 'functional currency'). The financial statements are presented in Australian dollars, which is the Company's functional and presentation currency.

Transactions and Balances

Foreign currency transactions are translated into the functional currency using the foreign exchange rates prevailing at the dates of the transactions. Foreign currency gains and losses resulting from the settlement of such transactions and from the translation at financial year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated statement of comprehensive income.

Non-monetary items measured at historical cost continue to be carried at the foreign exchange rate at the date of transaction. Foreign exchange differences 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 foreign exchange differences are recognised in the consolidated statement of comprehensive income.

Group Companies

The results and financial position of foreign subsidiaries that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities are translated at end of reporting period foreign exchange rates prevailing at the end of each reporting period;
- income and expenses are translated at average foreign exchange rates for the financial period; and
- all resulting foreign exchange differences are recognised in other comprehensive income.

On consolidation, foreign exchange differences arising on translation of foreign subsidiary financial statements are transferred directly to the foreign currency translation reserve in the consolidated statement of financial position. The relevant differences are recognised in the consolidated statement of comprehensive income during the financial period when the investment in a foreign subsidiary is disposed.

(f) Income Taxes and Other Taxes

Current Tax

Current income tax expense is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or loss for the financial period. It is calculated using tax rates that have been enacted or are substantively enacted by the end of each reporting period. Current tax for current and prior financial periods is recognised as a liability (or asset) to the extent that it is unpaid or (refundable).

Deferred Tax

Deferred tax is accounted for using the statement of financial position liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. The tax base of an asset or liability is the amount attributed to that asset or liability for income taxation purposes.

No deferred tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

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

Note 1. Summary of Significant Accounting Policies (continued)

(f) Income Taxes and Other Taxes (continued)

Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary tax differences or unused tax losses and tax offsets can be utilised.

Deferred tax assets and tax liabilities are offset when there is a legally enforceable right to offset current tax assets and tax liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the Group has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

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 Group will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by law.

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 ATO. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or equity or as part of an item of expense.

Receivables and payables in the consolidated statement of financial position are shown inclusive of GST.

The net amount of GST recoverable from, or payable to, the ATO is included as current other receivables or sundry payables respectively in the consolidated statement of financial position.

Cash flows are included on a gross basis in the consolidated statement of cash flows. The GST components of cash flows arising from investing and financing activities, which are recoverable from, or payable to, the ATO, are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the ATO.

(g) Cash and Cash Equivalents

Cash and cash equivalents in the consolidated statement of financial position and for presentation in the statement of cash flows comprise cash at banks and on hand (including share of joint venture operation cash balances) and short term bank deposits that are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value.

(h) Receivables

Receivables, which generally have 30 day terms, are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less any accumulated impairment losses. They are presented as current assets unless collection is not expected for more than 12 months after the reporting date.

Cash flows relating to receivables are not discounted if the effect of discounting would be immaterial.

Collectability of receivables is reviewed on an ongoing basis. Individual receivables that are known to be uncollectible are written off when identified.

Receivables are tested for impairment in accordance with the accounting policy described in Note 1(n). An impairment provision is recognised when there is objective evidence that the Group will not be able to collect the receivable. The amount of the impairment loss is the receivable's carrying amount compared to the present value of estimated future cash flows, discounted when material, at the original effective interest rate.

(i) Inventories

Inventories are measured at the lower of cost and net realisable value. Inventories are represented by assets acquired from third parties, in the form of casing and other drilling inventory to be consumed or used in exploration and evaluation activities.

The cost of casing and other drilling inventory includes direct materials, direct labour and transportation costs.

(j) Security Deposits

Certain financial assets have been pledged as security for performance guarantees, performance bonds and bank guarantees related to exploration permits and operating lease rental agreements. Their realisation may be restricted subject to terms and conditions attached to the relevant exploration permit agreements or operating lease rental agreements.

Security deposits are non-derivative financial assets that are not quoted in an active market. Security deposits are initially recognised at cost. Such assets are subsequently carried at amortised cost using the effective interest method. They are included in current assets, except for those with maturities greater than 12 months after the end of the reporting period which are classified as non-current assets.

Security deposits are derecognised when the terms and conditions attached to the relevant exploration permit agreements or operating lease rental agreements have expired or been transferred.

Security deposits are tested for impairment in accordance with the accounting policy described in Note 1(n).

(k) Plant and Equipment

Plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Such cost includes the cost of replacing parts that are eligible for capitalisation when the cost of replacing the parts is incurred. Similarly, when each major inspection is performed, its cost is recognised in the carrying amount of the plant and equipment as a replacement only if it is eligible for capitalisation. All other repairs and maintenance are recognised as an expense in the consolidated statement of comprehensive income as incurred.

Commencing from the time the plant and equipment is held ready for use, depreciation expense is calculated on a straight-line basis to allocate their cost amount, net of their residual values, over their estimated useful lives ranging from two to ten years.

Plant and equipment residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at the end of each reporting period.

Gains and losses on disposals are determined by comparing proceeds with the net carrying amount. These gains and losses are included in the consolidated statement of comprehensive income.

Plant and equipment are tested for impairment in accordance with the accounting policy described in Note 1(n).

(l) Intangibles

Computer Software

Computer software is stated at cost less accumulated amortisation and any accumulated impairment losses. Computer software costs have a finite life.

Commencing from the time the computer software is held ready for use, amortisation expense is calculated on a straight-line basis to allocate their cost amount, net of their residual values, over their estimated useful lives ranging from two to two and half years.

The assets' residual values, useful lives and amortisation methods are reviewed, and adjusted if appropriate, at the end of each reporting period.

Computer software is tested for impairment in accordance with the accounting policy described in Note 1(n).

Goodwill

Goodwill recognised in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is not amortised.

Note 1. Summary of Significant Accounting Policies (continued)

(l) Intangibles (continued)

Impairment of Goodwill

For the purpose of impairment testing at the end of each reporting period, goodwill recognised in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units) to which the goodwill relates.

An impairment loss is recognised as an expense in the consolidated statement of comprehensive income for the amount by which the asset's carrying amount exceeds its estimated recoverable amount.

Any impairment loss recognised for goodwill is not subsequently reversed.

(m) Exploration and Evaluation Expenditure

Expenditure on exploration and evaluation activities is accounted for in accordance with the 'area of interest' method of *AASB 6 'Exploration for and Evaluation of Mineral Resources'*. Exploration and evaluation expenditure is capitalised at cost, as an intangible, provided the right to tenure of the area of interest is current and either:

- the exploration and evaluation activities are expected to be recouped through successful development and exploitation of the area of interest or, alternatively, by its sale; or
- exploration and evaluation activities in the area of interest have not at the end of the reporting period reached a stage that permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active and significant operations in, or in relation to, the area of interest are continuing.

Otherwise, exploration and evaluation expenditure is expensed as incurred.

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

As capitalised exploration and evaluation expenditure is not available for use, it is not amortised.

Cash flows associated with exploration and evaluation expenditure (comprising amounts capitalised) are classified as investing activities in the consolidated statement of cash flows. Whereas, cash flows associated with exploration and evaluation expenditure expensed are classified as operating activities in the consolidated statement of cash flows.

When the technical feasibility and commercial viability of extracting economically recoverable reserves have been demonstrated, any related capitalised exploration and evaluation expenditure is reclassified as development expenditure in the consolidated statement of financial position. Prior to reclassification, capitalised exploration and evaluation expenditure is assessed for impairment.

Farm-out

The Group does not record any exploration and evaluation expenditure made by a farmee. It also does not recognise any gain or loss on its exploration and evaluation farm-out arrangements but redesignates any exploration and evaluation expenditure previously capitalised in relation to the whole area of interest as relating to the partial interest retained.

Any cash consideration received on sale or farm-out of an area within an exploration area of interest is offset against the carrying value of the particular area involved. Where the total carrying value of an area of interest has been recouped in this manner, the balance of the proceeds is brought to account in the consolidated statement of comprehensive income as a gain on disposal.

Impairment of Capitalised Exploration and Evaluation Expenditure

The carrying value of capitalised exploration and evaluation expenditure is assessed for impairment at the asset or cash-generating unit level (which usually is represented by an exploration permit) whenever facts and circumstances (as defined in AASB 6) suggest that the carrying amount of the asset may exceed its recoverable amount. If any indication of impairment exists, an estimate of the asset's recoverable amount is calculated.

An impairment loss exists when the carrying amount of an asset or cash-generating unit exceeds its estimated recoverable amount. The asset or cash-generating unit is then written-down to its recoverable amount. Impairment losses are recognised as an expense in the consolidated statement of comprehensive income.

Capitalised exploration and evaluation expenditure that suffered impairment are tested for possible reversal of the impairment loss whenever facts or changes in circumstances indicate that the impairment may have reversed.

(n) Impairment of Assets (Other than Goodwill and Capitalised Exploration and Evaluation Expenditure)

All other current and non-current assets (other than inventories and deferred tax assets) are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

At the end of each reporting period, the Group conducts an internal review of asset values, which is used as a source of information to assess for any indicators of impairment. External factors, such as changes in economic conditions, are also monitored to assess for indicators of impairment. If any indication of impairment exists, an estimate of the asset's recoverable amount is calculated.

An impairment loss exists when the carrying amount of an asset or cash-generating unit exceeds its estimated recoverable amount. The asset is then written-down to its recoverable amount. Recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets or groups of assets (cash-generating units).

Impairment losses are recognised as an expense in the consolidated statement of comprehensive income.

Assets that suffered impairment are tested for possible reversal of the impairment loss whenever events or changes in circumstances indicate that the impairment may have reversed.

(o) Trade and Other Payables

Trade and other payables are carried at amortised cost. Due to their short term nature they are not discounted. They represent liabilities for goods and services provided to the Group prior to the end of the reporting period that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of goods and services. The amounts are unsecured and are usually paid within 30 days of recognition. They are presented as current liabilities unless payment is not due within 12 months from the reporting date.

(p) Employee Benefits

Wages, Salaries, Annual Leave and Personal Leave

Liabilities for wages and salaries, including non-monetary benefits, annual leave and accumulating personal leave expected to be settled within one year after the end of the reporting period in which the employees render the related services are recognised in respect of employees' services up to the end of the reporting period. They are measured at the amounts expected to be paid when the liabilities are settled plus related on-costs. Expenses for non-accumulating personal leave are recognised when the leave is taken and are measured at the rates paid or payable.

Share-based Payments

Share-based remuneration benefits are provided to employees via the Company's ESOP and Directors via other share options (refer Note 27).

Note 1. Summary of Significant Accounting Policies (continued)

(p) Employee Benefits (continued)

The fair value of options granted is recognised as a share-based payments expense in the consolidated statement of comprehensive income with a corresponding increase in the share-based payments reserve in equity. The total amount to be expensed is determined by reference to the fair value of the options granted, which includes any market performance conditions but excludes the impact of any service and non-market performance vesting conditions and the impact of any non-vesting conditions. Non-market performance vesting conditions are included in assumptions about the number of options that are expected to vest.

The fair value is measured at grant date. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the non-market performance vesting conditions. It recognises the impact of the revision to original estimates, if any, in the consolidated statement of comprehensive income, with a corresponding adjustment to equity. For options that vest immediately, the value is expensed immediately.

The fair value at grant date is independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the impact of dilution, the non-tradeable nature of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

The Group has elected to retain any amounts originally recognised in the share-based payments reserve, regardless of whether the associated options are exercised or lapse unexercised.

(q) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are not recognised for future operating losses.

When it is expected that some or all of a provision is to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is included in the consolidated statement of comprehensive income, net of any reimbursement.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period using a discounted cash flow methodology. If the effect of the time value of money is material, provisions are discounted using a pre-tax rate that reflects the time value of money and the risks specific to the obligation. The increase in the provision resulting from the passage of time is recognised as finance costs in the consolidated statement of comprehensive income.

Long Service Leave

A provision has been recognised for employee entitlements relating to long service leave measured at the present value of estimated future cash outflows. In determining the provision, consideration is given to employee wage increases and the probability that the employee may satisfy vesting requirements. The cash outflows are discounted using market yields on Australian government bonds with terms of maturity that match the expected timing of cash outflows.

Restoration

Restoration costs incurred during exploration and evaluation activities are provided when the obligation to incur such costs arises, a corresponding restoration asset (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 present value, and is reassessed at the end of each reporting period in accordance with local conditions and requirements. Expected future payments are discounted using market yields at the end of each reporting period on Australian government bonds with terms to maturity and currency that match, as closely as possible, the estimated future cash outflows. Changes in the estimates of restoration costs 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 within finance costs in the consolidated statement of comprehensive income.

(r) Issued Capital

Ordinary shares are classified as equity.

Cash received from shareholders and investors at the end of the reporting period, pending allotment and issue of fully paid ordinary shares, is held as funds in escrow in the consolidated statement of financial position.

Transaction costs directly attributable to the issue of new ordinary shares or options are shown in equity as a deduction, net of any related income tax benefit, from the proceeds. Transaction costs are the costs that are incurred directly in connection with the issue of new ordinary shares and which would not have been incurred had those ordinary shares not been issued. These directly attributable transaction costs include registration and other regulatory fees, amounts paid to legal, accounting and other professional advisers, printing costs and marketing costs.

The costs of an equity raising that is abandoned are recognised as an expense in the consolidated statement of comprehensive income.

(s) Interests in Joint Venture Operations

The proportionate interests in the assets, liabilities, revenue and expenses of a joint venture operation are incorporated in the financial statements under the appropriate headings.

The Group's share of assets and liabilities employed in joint venture operations is set out in Note 23.

(t) Leases

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Group as a Lessee

Leases in which a significant portion of the risks and rewards of ownership are not transferred to the Group as lessee are classified as operating leases. Operating lease payments (net of any incentives received from the lessor) are recognised as an expense in the consolidated statement of comprehensive income on a straight-line basis over the financial period of the lease.

(u) Earnings Per Share

Basic Earnings Per Share

Basic earnings per ordinary share is calculated by dividing the profit or loss attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for any bonus elements in ordinary shares issued during the financial year.

Diluted Earnings Per Share

Diluted earnings per ordinary share adjusts the figures used in the determination of basic earnings per ordinary share to take into account the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

(v) Parent Company Financial Information

The financial information for the Parent Company, Karoon Gas Australia Ltd, disclosed in Note 30 has been prepared on the same basis as the consolidated financial statements, except as set out below:

Investments in Subsidiaries

Investments in subsidiaries are accounted for at cost in the financial statements of Karoon Gas Australia Ltd.

The Parent Company does not designate any investments in subsidiaries as being subject to the requirements of Australian Accounting Standards specifically applicable to financial instruments. They are held for strategic and not trading purposes.

Investments in subsidiaries and receivables from subsidiaries are tested for impairment in accordance with the accounting policy described in Note 1(n).

Note 1. Summary of Significant Accounting Policies (continued)

(v) Parent Company Financial Information (continued)

Tax Consolidation

The Parent Company and its wholly owned Australian subsidiaries are part of an income tax-consolidated group under Australian taxation law. Karoon Gas Australia Ltd is the head entity in the income tax-consolidated group. Tax expense/income, deferred liabilities and deferred assets arising from temporary tax differences of the members of the income tax-consolidated group are recognised in the separate financial statements of the members of the income tax-consolidated group using the 'stand alone taxpayer' approach by reference to the carrying amounts in the separate financial statements of each company and the tax values applying under tax consolidation. Current tax liabilities and tax assets and deferred tax assets arising from unused tax losses and tax credits of members of the income tax-consolidated group are recognised by the Parent Company (as head entity of the income tax-consolidated group).

Due to the existence of a tax funding agreement between the companies in the income tax-consolidated group, each company contributes to the income tax payable or receivable in proportion to their contribution to the income tax-consolidated group's taxable income. Differences between the amounts of net tax assets and tax liabilities derecognised and the net amounts recognised pursuant to the funding agreement are recognised as either a contribution by, or distribution to, the head entity.

(w) New Australian Accounting Standards and Interpretations for Application in Future Financial Years

Certain new Australian Accounting Standards and Interpretations have been published that are not mandatory for this financial year. The Group's assessment of the impact of the relevant new Australian Accounting Standards and Interpretations is set out below:

(i) AASB 9 'Financial Instruments', AASB 2009-11 'Amendments to Australian Accounting Standards arising from AASB 9' and AASB 2010-7 'Amendments to Australian Accounting Standards arising from AASB 9' (December 2010) (effective for annual reporting periods beginning on or after 1 January 2013)

AASB 9 Financial Instruments addresses the classification, measurement and derecognition of financial assets and financial liabilities. The standard is not applicable until 1 January 2013 but is available for early adoption. The Group is yet to assess AASB 9's full impact. The Group has not yet decided when to adopt AASB 9.

(ii) Revised AASB 124 'Related Party Disclosures' and AASB 2009-12 'Amendments to Australian Accounting Standards' (effective for annual reporting periods beginning on or after 1 January 2011)

During December 2009, the AASB issued a revised *AASB 124 'Related Party Disclosures'*. It is effective for accounting periods beginning on or after 1 January 2011 and must be applied retrospectively. The amendment clarifies and simplifies the definition of a related party. The Group will apply the amended standard from 1 July 2011. When the amendments are applied, the Group will need to disclose all transactions between its subsidiaries, including commitments. The Group is yet to assess its full impact. However, initial indications are that it will have limited impact.

(iii) AASB 1053 'Application of Tiers of Australian Accounting Standards' and AASB 2010-2 'Amendments to Australian Accounting Standards arising from Reduced Disclosure Requirements' (effective 1 July 2013)

On 30 June 2010, the AASB officially introduced a revised differential reporting framework in Australia. Under this framework, a two-tier differential reporting regime applies to all entities that prepare general purpose financial statements. Karoon Gas Australia Ltd is listed on the ASX; as such it is ineligible to adopt these two new Australian Accounting Standards. As a consequence, there will be no impact on the financial statements.

(iv) IFRS 10 'Consolidated Financial Statements', IFRS 11 'Joint Arrangements', IFRS 12 'Disclosure of Interests in Other Entities' and revised IAS 27 'Separate Financial Statements' and IAS 28 'Investments in Associates and Joint Ventures' (effective 1 January 2013)

During May 2011, the IASB issued a suite of five new and amended standards which address the accounting for joint arrangements, consolidated financial statements and associated disclosures. The AASB is expected to issue equivalent Australian Accounting Standards shortly.

IFRS 10 replaces all of the guidance on control and consolidation in *IAS 27 'Consolidated and Separate Financial Statements'*, and *SIC-12 'Consolidation – Special Purpose Entities'*. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single economic entity remains unchanged, as do the mechanics of consolidation. However, the standard introduces a single definition of control that applies to all entities. It focuses on the need to have both power and rights or exposure to variable returns before control is present. Power is the current ability to direct the activities that significantly influence returns. Returns must vary and can be positive, negative or both. There is also new guidance on participating and protective rights and on agent/principal relationships. The Group does not expect the new standard to have any impact on its composition.

IFRS 11 introduces a principles based approach to accounting for joint arrangements. The focus is no longer on the legal structure of joint arrangements but rather on how rights and obligations are shared by the parties to the joint arrangement. Based on the assessment of rights and obligations, a joint arrangement will be classified as either a joint operation or joint venture. Joint ventures are accounted for using the equity method, the choice to proportionately consolidate will no longer be permitted. Parties to a joint operation will account for their share of revenues, expenses, assets and liabilities in much the same way as under the previous standard. IFRS 11 also provides guidance for parties that participate in joint arrangements but do not share joint control. As the Group is only a participant in joint venture operations, this standard will not have any impact on its financial statements.

IFRS 12 sets out the required disclosures for entities reporting under the above two new standards, IFRS 10 and IFRS 11, and replaces the disclosure requirements currently found in IAS 28. Application of this standard by the Group will not affect any of the amounts recognised in the financial statements.

IAS 27 is renamed Separate Financial Statements and is now a standard dealing solely with separate financial statements. Application of this standard by the Group will not affect any of the amounts recognised in the financial statements.

Amendments to IAS 28 provide clarification that an entity continues to apply the equity method and does not remeasure its retained interest as part of ownership changes where a joint venture becomes an associate, and vice versa. The amendments also introduce a partial disposal concept. Application of this standard by the Group will not affect any of the amounts recognised in the financial statements.

The Group does not expect to adopt the relevant new Australian Accounting Standards before their operative date.

(v) IFRS 13 'Fair Value Measurement' (effective 1 January 2013)

IFRS 13 was released during May 2011. The AASB is expected to issue an equivalent Australian Accounting Standard shortly. IFRS 13 explains how to measure fair value and aims to enhance fair value disclosures. The Group does not use fair value measurements extensively. It is therefore unlikely that the new rules will have a significant impact on any of the amounts recognised in the financial statements or disclosed in the notes to the financial statements. The Group does not intend to adopt the new standard before its operative date, which means that it would be first applied in the reporting period ending 30 June 2014.

(vi) Revised IAS 1 'Presentation of Financial Statements' (effective 1 July 2012)

During June 2011, the IASB made an amendment to *IAS 1 'Presentation of Financial Statements'*. The AASB is expected to make equivalent changes to *AASB 101 'Presentation of Financial Statements'* shortly. The amendment requires entities to separate items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future. It will not affect the measurement of any of the items recognised in the statement of comprehensive income. The Group does not intend to adopt the new standard before its operative date, which means that it would be first applied in the reporting period ending 30 June 2013.

(vii) AASB 2011-4 'Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements' (effective 1 July 2013)

During July 2011, the AASB decided to remove the individual key management personnel disclosure requirements from *AASB 124 'Related Party Disclosures'*, to achieve consistency with the international equivalent standard and remove a duplication of the requirements with the *Corporations Act 2001*. While this will reduce the disclosures that are currently required in the notes to the financial statements, it will not affect any of the amounts recognised in the financial statements. The amendments apply from 1 July 2013 and cannot be adopted early.

The Group has not early adopted any of the above reporting requirements.

Note 2. Significant Accounting Estimates, Assumptions and Judgements

Revenues and expenses and the carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. In applying the Group's significant accounting policies, the Board of Directors and management evaluate estimates and judgements based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data obtained both externally and within the Group.

Significant estimates, assumptions and/or judgements made by the Board of Directors and management in the preparation of the financial statements were:

(a) Capitalised Exploration and Evaluation Expenditure

The future recoverability of capitalised exploration and evaluation expenditure is dependent on a number of factors, including whether the Group decides to exploit the related exploration permit itself or, if not, whether it successfully recovers the related exploration and evaluation asset through sale. Factors that could affect the future recoverability include the level of economically recoverable reserves, future technological changes which could impact the cost of development, future legal changes (including changes to environmental and restoration obligations) and changes to commodity prices. To the extent that capitalised exploration and evaluation expenditure is determined not to be recoverable in the future, financial results and net assets will be reduced during the financial period in which this determination is made.

In addition, exploration and evaluation expenditure is carried forward on the basis that exploration and evaluation activities in the areas of interest have not at the end of the reporting period reached a stage that permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active and significant operations in, or in relation to, the areas of interest are continuing. To the extent it is determined in the future this capitalised expenditure should be written off, financial results and net assets will be reduced during the financial period in which this determination is made.

Information on the reasonable existence or otherwise of economically recoverable reserves is progressively gained through geological analysis and interpretation, drilling activity and prospect evaluation during a normal exploration permit term. A reasonable assessment of the existence or otherwise of economically recoverable reserves can generally only be made, therefore, at the conclusion of those exploration and evaluation activities.

(b) Share-based Payments

The Group measures the cost of share-based payment transactions with Directors and employees by reference to the fair value of the options at the date they were granted. Fair value is ascertained using the Black-Scholes option pricing model taking into account the terms and conditions upon which the options were granted. The accounting estimates and assumptions relating to share-based payments would have no impact on the carrying amounts of assets and liabilities within the next reporting period but may impact expense and equity.

(c) Income Tax

The Group is subject to income taxes in Australia and jurisdictions where it has foreign operations. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Group estimates its tax liabilities based on the Group's understanding of the tax law. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred tax balances in the financial period in which such determination is made.

The Group has not recognised deferred tax assets in respect of tax losses and temporary tax differences as the future utilisation of these losses and temporary tax differences is not considered probable at this point in time. Assessing the future utilisation of tax losses and temporary tax differences requires the Group to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws. To the extent that future utilisation of these tax losses and temporary tax differences becomes probable, this could result in significant changes to deferred tax assets recognised, which would in turn impact future financial results.

Note 3. Financial Risk Management

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and interest rate risk); credit risk and liquidity risk. The Group's overall financial risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Group. The Group uses different methods to measure the different types of financial risk to which it is exposed. These methods include sensitivity analysis in the case of foreign exchange and interest rates.

The overall financial risk management strategy of the Group is governed by the Board of Directors and is primarily focused on ensuring that the Group is able to finance its business plans, while minimising potential adverse effects on financial performance. The Board of Directors provides written principles for overall financial risk management, as well as written policies covering specific areas, such as mitigating foreign exchange, interest rate and credit risks, use of derivative financial instruments and investment of excess cash. Financial risk management is carried out by the Company's finance function under policies approved by the Board of Directors. The finance function identifies, evaluates and if necessary hedges financial risks in close cooperation with the Executive Chairman. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and Group activities.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised in respect of each class of financial asset and financial liability are disclosed in Note 1.

The Group's financial instruments consist of cash and cash equivalents, receivables, security deposits, trade and other payables.

The Group had no off-statement of financial position financial assets or financial liabilities at either 30 June 2011 or 30 June 2010.

The totals for each category of financial instruments in the consolidated statement of financial position are as follows:

		Consolidated	
	Note	**2011** **$**	2010 $
Financial assets			
Cash and cash equivalents	10	**266,839,144**	87,122,836
Receivables	11	**4,003,566**	4,873,578
Security deposits	13	**67,360,580**	16,639,562
Total financial assets		**338,203,290**	108,635,976
Financial liabilities			
Trade and other payables (refer note (a) below)		**3,809,100**	13,672,624
Total financial liabilities		**3,809,100**	13,672,624

Note:

(a) Trade and other payables above exclude amounts relating to leave liabilities, which are not considered a financial instrument. The reconciliation to the amount in the consolidated statement of financial position is as follows:

	Note	2011 $	2010 $
Trade and other payables	18	**4,306,586**	13,912,243
Less: Leave liabilities		**(497,486)**	(239,619)
		3,809,100	13,672,624

Note 3. Financial Risk Management (continued)

(a) Market Risk

(i) Foreign Exchange Risk

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Foreign exchange risk arises when future commercial transactions and recognised financial assets and financial liabilities are denominated in a currency that is not the Company's functional currency.

The Group operates internationally and is exposed to foreign exchange risk arising from currency exposures to predominately United States dollar expenditures and cash and deposits held in United States dollars. The Group manages foreign exchange risk at the corporate level by monitoring forecast cash flows in currencies other than Australian dollars and ensuring that adequate United States dollar cash balances are maintained.

United States dollars are bought on the spot market in excess of immediate requirements. Where currencies are purchased in advance of requirements, these balances do not usually exceed three months' requirements.

Regular sensitivity analysis is conducted to evaluate the potential impact of unfavourable exchange rates on the Group's future financial position. The results of this evaluation are used to determine the most appropriate risk mitigation tool to be used. The Group will hedge when it is deemed the most appropriate risk mitigation tool to be used.

Foreign currency hedging transactions were not entered into during the financial year or previous financial year.

An analysis of the Group's exposure to foreign exchange risk for financial instruments, expressed in Australian dollars, at the end of the financial year is set out below:

	2011				2010			
Consolidated	**AUD $**	**USD $**	**REAL $**	**Total $**	AUD $	USD $	REAL $	Total $
Financial assets								
Cash and cash equivalents	**192,445,470**	**73,556,394**	**837,280**	**266,839,144**	63,389,400	22,987,761	745,675	87,122,836
Receivables	**1,722,844**	**2,280,722**	**-**	**4,003,566**	735,344	4,138,234	-	4,873,578
Security deposits	**359,509**	**10,027,347**	**56,973,724**	**67,360,580**	93,727	4,810,814	11,735,021	16,639,562
Total financial assets	**194,527,823**	**85,864,463**	**57,811,004**	**338,203,290**	64,218,471	31,936,809	12,480,696	108,635,976
Financial liabilities								
Trade and other payables	**1,393,545**	**1,420,761**	**994,794**	**3,809,100**	1,175,245	12,127,933	369,446	13,672,624
Total financial liabilities	**1,393,545**	**1,420,761**	**994,794**	**3,809,100**	1,175,245	12,127,933	369,446	13,672,624

Foreign Exchange Sensitivity Analysis

The following table details the Group's sensitivity to a 10.0% increase or decrease in the Australian dollar against the United States dollar, with all other variables held constant. The sensitivity analysis includes only outstanding foreign currency denominated amounts at the end of the financial year and adjusts their translation for a 10.0% change in the relevant foreign exchange rate.

The sensitivity analysis is not fully representative of the inherent foreign exchange risk, as the financial year end exposure does not necessarily reflect the exposure during the course of a financial year. These sensitivities should not be used to forecast the future effect of movements in United States dollar exchange rates on future cash flows.

	Consolidated 2011 $	2010 $
Change in profit (loss)		
- Improvement in AUD to USD by 10.0%	(7,479,610)	(2,737,438)
- Decline in AUD to USD by 10.0%	9,141,745	3,345,757
Change in financial assets		
- Improvement in AUD to USD by 10.0%	(7,807,288)	(4,037,382)
- Decline in AUD to USD by 10.0%	9,542,240	4,934,578
Change in financial liabilities		
- Improvement in AUD to USD by 10.0%	129,160	1,102,539
- Decline in AUD to USD by 10.0%	(157,862)	(1,347,548)
Change in foreign currency translation reserve		
- Improvement in AUD to USD by 10.0%	198,518	197,405
- Decline in AUD to USD by 10.0%	(242,633)	(241,273)

(ii) Interest Rate Risk

Interest rate risk is the risk that the fair value of future cash flows of financial assets and financial liabilities will fluctuate because of changes in market interest rates. Interest rate risk is managed on a Group basis at the corporate level.

As at 30 June 2011 and 30 June 2010, there was no borrowing outstanding and there was no interest rate hedging in place.

The Group's interest rate risk arises from relevant financial assets, primarily cash and cash equivalents deposited at variable rates of interest and security deposits held in Brazil. Surplus cash is invested in short term bank deposits due to uncertainty of the timing of major cash outflows. Whilst some of the invested cash is in United States dollars, the primary exposure is to Australian interest rates.

An analysis of the Group's exposure to interest rate risk for financial assets and financial liabilities at the end of the financial year is set out below:

			Consolidated			
2011	**Weighted Average Interest Rate % P.A.**	**Floating Interest Rate $**	**Fixed Interest Rate $**	**Non-interest Bearing $**	**Fair Value $**	**Carrying Amount $**
Financial assets						
Cash and cash equivalents	4.3	80,585,111	184,939,247	1,314,786	266,839,144	266,839,144
Receivables	-	-	-	4,003,566	4,003,566	4,003,566
Security deposits	9.4	44,959,458	22,384,825	16,297	67,360,580	67,360,580
Total financial assets		125,544,569	207,324,072	5,334,649	338,203,290	338,203,290
Financial liabilities						
Trade and other payables	-	-	-	3,809,100	3,809,100	3,809,100
Total financial liabilities		-	-	3,809,100	3,809,100	3,809,100

Note 3. Financial Risk Management (continued)

2010	Weighted Average Interest Rate % P.A.	Floating Interest Rate $	Fixed Interest Rate $	Non-interest Bearing $	Fair Value $	Carrying Amount $
	Consolidated					
Financial assets						
Cash and cash equivalents	4.0	24,894,805	61,171,587	1,056,444	87,122,836	87,122,836
Receivables	-	-	-	4,873,578	4,873,578	4,873,578
Security deposits	8.2	4,100	16,635,462	-	16,639,562	16,639,562
Total financial assets		24,898,905	77,807,049	5,930,022	108,635,976	108,635,976
Financial liabilities						
Trade and other payables	-	-	-	13,672,624	13,672,624	13,672,624
Total financial liabilities		-	-	13,672,624	13,672,624	13,672,624

Interest Rate Sensitivity Analysis

The following table details the Group's sensitivity to a 1.0% p.a. increase or decrease in interest rates, with all other variables held constant. The sensitivity analysis is based on the balance of floating interest rate amounts held at the end of the financial year.

The sensitivity analysis is not fully representative of the inherent interest rate risk, as the financial year end exposure does not necessarily reflect the exposure during the course of a financial year. These sensitivities should not be used to forecast the future effect of movements in interest rates on future cash flows.

	Consolidated 2011 $	2010 $
Change in profit (loss)		
- Increase of interest rate by 1.0% p.a.	**1,255,446**	248,989
- Decrease of interest rate by 1.0% p.a.	**(536,744)**	(55,377)
Change in financial assets		
- Increase of interest rate by 1.0% p.a.	**1,255,446**	248,989
- Decrease of interest rate by 1.0% p.a.	**(536,744)**	(55,377)

(b) Credit Risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. Credit risk arises from cash and cash equivalents and security deposits held with banks, financial institutions and joint venture operators, as well as credit exposures to customers, including outstanding receivables.

Credit risk is managed on a Group basis at the corporate level. Management monitors credit risk on an ongoing basis within the Group.

To minimise credit risk, the Group has adopted a policy of only dealing with recognised and creditworthy third parties. The Group does not have any material credit risk exposure to any single debtor or group of debtors entered into by the Group. Receivable balances are monitored on an ongoing basis with the result being the Group's exposure to bad debts is minimised. The Group does not hold collateral, nor does it securitise its receivables.

The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history.

Cash and cash equivalents and security deposit counterparties are limited to high credit quality banks and financial institutions. For banks and financial institutions, only independently rated counterparties with a minimum rating of 'AA-' are accepted. Where commercially practical, the Group seeks to limit the amount of credit exposure to any one bank or financial institution. Cash and cash equivalents and security deposits are spread amongst a number of AA and AAA rated banks and financial institutions to minimise the risk of default of counterparties.

The maximum exposure to credit risk at the end of the financial year is the carrying amount of the financial assets as disclosed in the consolidated statement of financial position and notes to the financial statements.

As at 30 June 2011, there were $Nil (30 June 2010: $Nil) financial assets past due.

(c) Liquidity Risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities.

At the end of the financial year, the Group held cash and cash equivalents at call of $81,899,897 (30 June 2010: $25,951,249) that are expected to readily generate cash inflows for managing liquidity risk.

The Group manages liquidity risk by ensuring that there are sufficient funds available to meet financial obligations on a day-to-day basis and to meet unexpected liquidity needs in the normal course of business. Emphasis is placed on ensuring there is sufficient funding in place to meet the ongoing requirements of the Group's exploration and evaluation activities.

The following mechanisms are utilised:

- preparing and maintaining rolling forecast cash flows in relation to operational, investing and financing activities;
- maintaining a reputable credit profile;
- managing credit risk related to financial assets;
- investing surplus cash only in high credit quality banks and financial institutions; and
- comparing the maturity profile of financial liabilities with the realisation profile of financial assets.

An analysis of the Group's financial liability maturities at the end of the financial year is set out below:

	Consolidated					
2011	**Less than 6 Months $**	**6-12 Months $**	**Between 1 and 2 Years $**	**Between 2 and 5 Years $**	**Over 5 Years $**	**Total $**
Financial liabilities						
Trade and other payables	**3,809,100**	**-**	**-**	**-**	**-**	**3,809,100**
Total financial liabilities	**3,809,100**	**-**	**-**	**-**	**-**	**3,809,100**
2010	**$**	**$**	**$**	**$**	**$**	**$**
Financial liabilities						
Trade and other payables	13,672,624	-	-	-	-	13,672,624
Total financial liabilities	13,672,624	-	-	-	-	13,672,624

(d) Fair Value Estimation

For disclosure purposes only, the fair values of financial assets and financial liabilities as at 30 June 2011 are presented in the table under Note 3(a)(ii) and can be compared to their carrying values as presented in the consolidated statement of financial position. Fair values are those amounts at which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair values estimated for disclosure purposes are based on information that is subject to judgement, where changes in assumptions may have a material impact on the amounts estimated.

Note 3. Financial Risk Management (continued)

(d) Fair Value Estimation (continued)

The following summarises the significant methods and assumptions used in estimating fair values of financial assets and financial liabilities for disclosure purposes:

Cash and Cash Equivalents

The carrying amount is fair value due to the liquid nature of these assets.

Receivables

The carrying amounts of receivables are assumed to approximate their fair values due to their short term nature.

Security Deposits

The carrying amounts of security deposits are assumed to represent their fair values based on their likely realisability profile.

Trade and Other Payables

Due to the short term nature of these financial liabilities, their carrying amounts are assumed to represent their fair values.

	Note	Consolidated 2011 $	Consolidated 2010 $
Note 4. Revenue			
Interest income from unrelated entities		**14,225,048**	6,459,623
Total revenue		**14,225,048**	6,459,623
Sundry income		**-**	914
Total other income		**-**	914
Note 5. Expenses			
Loss before income tax includes the following specific expenses:			
Depreciation and amortisation expense:			
- depreciation of plant and equipment	15	**335,347**	246,223
- amortisation of computer software	16	**195,898**	169,444
Total depreciation and amortisation expense		**531,245**	415,667
Exploration and evaluation expenditure expensed or written off:			
- exploration and evaluation expenditure expensed		**780,662**	136,812
- exploration and evaluation expenditure written off	17	**3,881,892**	-
Total exploration and evaluation expenditure expensed or written off		**4,662,554**	136,812
Finance costs:			
- bank charges		**447,592**	244,275
- interest expense to unrelated entities		**8,698**	-
Total finance costs		**456,290**	244,275
Share-based payments expense	27(d)	**5,069,475**	5,289,047
Rental expense on operating leases – minimum lease payments		**668,041**	228,395
Net loss on disposal of plant and equipment		**82,945**	-

	Consolidated 2011 $	2010 $
Note 6. Income Tax		
(a) Income Tax Recognised in the Consolidated Statement of Comprehensive Income		
Tax expense comprises:		
Current income tax	-	228,822
Deferred income tax	-	-
Total income tax expense	-	228,822

The prima facie tax on loss before income tax is reconciled to income tax expense as follows:

	2011 $	2010 $
Prima facie tax payable on loss before income tax, calculated at the Australian tax rate of 30% (2010: 30%)	(6,991,474)	(4,399,505)
Add (subtract) tax effect of:		
Share-based payments expense	1,520,843	1,586,714
Other non-deductible items	2,422,961	732,205
Prior financial year's income tax expense on foreign operations	-	228,822
Tax losses and temporary tax differences not recognised	3,047,670	3,126,480
Other items	-	(1,045,894)
Total income tax expense	-	228,822

(b) Unrecognised Deferred Tax Assets

A deferred tax asset has not been recognised in the consolidated statement of financial position as the benefits of this will only be realised if the conditions for deductibility set out in Note 1(f) occur:

	2011 $	2010 $
- Unrecognised temporary tax differences relating to deferred tax assets	5,500,782	480,814
- Tax losses:		
- Australian operating losses at a rate of 30%	8,150,065	7,025,051
- Brazilian operating losses at a rate of 34%	334,002	-
Potential tax benefit	13,984,849	7,505,865

(c) Current Tax Liability

	2011 $	2010 $
Income tax payable	-	(235,727)
Total current tax liability	-	(235,727)

(d) Deferred Tax Liabilities

	2011 $	2010 $
Temporary tax differences relating to deferred tax liabilities	(67,609,198)	(57,200,549)
Offset by deferred tax assets relating to operating losses	67,609,198	57,200,549
Total deferred tax liabilities	-	-

	Consolidated 2011 $	Consolidated 2010 $

Note 7. Remuneration of External Auditors

Remuneration received or due and receivable by the external auditor of Karoon Gas Australia Ltd for:

(a) PricewaterhouseCoopers Australia

(i) Audit and other assurance services

	2011 $	2010 $
Audit and review of financial statements	**195,320**	109,029
Non-audit services (due diligence services for Brazilian initial public offering)	**135,600**	-
Total remuneration for audit and other assurance services	**330,920**	109,029

(ii) Other services

	2011 $	2010 $
Benchmarking services	**10,000**	-
Total remuneration of PricewaterhouseCoopers Australia	**340,920**	109,029

(b) Related practices of PricewaterhouseCoopers Australia

(i) Audit and other assurance services

	2011 $	2010 $
Audit and review of financial statements	**37,186**	35,199
Non-audit services (due diligence services for Brazilian initial public offering)	**449,657**	-
Total remuneration for audit and other assurance services of related practices	**486,843**	35,199
Total remuneration of external auditors	**827,763**	144,228

Note 8. Dividends

There were no ordinary dividends declared or paid during the financial year by the Group (2010: $Nil).

Dividend franking account

	2011 $	2010 $
Balance of franking account at end of financial year	-	-

Note 9. Earnings Per Share

	2011	2010
Loss for financial year used to calculate basic and diluted loss per ordinary share:	**(23,304,914)**	(14,893,839)
(a) Basic loss per ordinary share	**(0.1119)**	(0.0842)
(b) Diluted loss per ordinary share*	**(0.1119)**	(0.0842)

* Diluted loss per ordinary share equates to basic loss per ordinary share because a loss per ordinary share is not considered dilutive for the purposes of calculating earnings per share pursuant to *AASB 133 'Earnings per Share'*.

	2011	2010
Weighted average number of ordinary shares on issue during the financial year used in calculating basic loss per ordinary share:	**208,328,055**	176,786,841
Weighted average number of potential ordinary shares:	**1,188,898**	2,991,254
Weighted average number of ordinary shares and potential ordinary shares used in calculating diluted loss per ordinary share (excluding anti-dilutive options outstanding):	**209,516,898**	179,778,095
Weighted average number of anti-dilutive options:	**2,829,263**	1,124,139

Potential ordinary shares

Options over unissued ordinary shares of the Company outstanding at the end of the financial year are considered to be potential ordinary shares and have been included in the determination of diluted loss per ordinary share to the extent to which they are dilutive. The options have not been included in the determination of basic loss per ordinary share.

	Consolidated	
	2011	2010
	$	$

Note 10. Cash and Cash Equivalents

Cash at banks and on hand	**81,899,897**	25,951,249
Short term bank deposits	**184,939,247**	61,171,587
Total cash and cash equivalents	**266,839,144**	87,122,836

(a) Cash at Banks and on Hand

Cash at banks and on hand includes share of joint venture operation cash balances. Refer to Note 23 for further details.

(b) Short Term Bank Deposits

Short term bank deposits are made for varying periods of between one day and 180 days, depending on the immediate cash requirements of the Group, and earn interest at the respective short term bank deposit rates.

(c) Financial Risk Management

Information concerning the Group's exposure to financial risks on cash and cash equivalents is set out in Note 3.

Note 11. Receivables

	Consolidated	
	2011	2010
	$	$
Current		
Other receivables	**4,003,566**	4,873,578
Total current receivables	**4,003,566**	4,873,578

(a) Financial Risk Management

Information concerning the Group's exposure to financial risks on receivables is set out in Note 3.

Note 12. Inventories

Current		
Casing and other drilling inventory, at cost	**279,892**	360,081
Total current inventories	**279,892**	360,081

Note 13. Security Deposits

Current		
Karoon Petróleo & Gas SA (refer Note (a) below)	**37,870,543**	11,723,326
Karoon Gas Australia Ltd (refer Note (b) below)	**3,400,231**	-
Karoon Gas Australia Ltd, KEI (Peru Z38) Pty Ltd, Sucursal del Peru (refer Note (c) below)	**30,969**	40,107
Karoon Gas Australia Ltd (refer Note (d) below)	**-**	293,324
Karoon Gas Pty Ltd (refer Note (e) below)	**-**	35,115
Total current security deposits	**41,301,743**	12,091,872
Non-current		
Karoon Petróleo & Gas SA (refer Note (a) below)	**18,941,299**	-
Karoon Gas Australia Ltd (refer Note (b) below)	**6,611,416**	4,517,490
Karoon Gas Australia Ltd, Karoon Petróleo & Gas SA (refer Note (c) below)	**506,122**	30,200
Total non-current security deposits	**26,058,837**	4,547,690

Note 13. Security Deposits (continued)

(a) Performance Bonds

The Group has provided Agencia Nacional do Petróleo (the Brazilian Petroleum Agency) letters of credit and insurance bonds (refer Note 24) to carry out minimum work programs in relation to the Group's exploration permits in the Santos Basin, Brazil (Santos Basin Blocks 1037, 1101, 1102, 1165 and 1166). The letters of credit are fully funded by way of payment of a security deposit, which will be released once the work programs are met. The insurance bonds have been part funded to 50% of the value of the total bonds provided to Agencia Nacional do Petróleo by establishment of an escrow account. The funds deposited in escrow are invested on term deposit and quarterly interest earned is released from escrow after the end of each quarter. The principal funds held in escrow will be released as work is undertaken to satisfy the work programs.

(b) Performance Guarantees

Performance guarantees (via letters of credit) were provided to Peru Petro SA for Block Z-38 and Block 144 by the Group (refer Note 24) for second and third period work commitments (30 June 2010: for first and second period work commitments). The letters of credit are fully funded by way of payment of a security deposit, which will be released once the work commitments are met.

(c) Bank Guarantees

Cash deposits are held as security against bank guarantee facilities for bank guarantees (refer Note 24) given to lessors for the Group's compliance with its obligations in respect of operating lease rental agreements for office premises at Melbourne, Mount Martha, Peru and Brazil.

(d) Performance Guarantee

In the previous financial year, a performance guarantee (via a letter of credit) was provided to a third party supplier by the Group for exploration work undertaken in Peru (refer Note 24). The letter of credit was fully funded by way of payment of a security deposit, and was released once the Group's obligation under the contract was satisfied.

(e) Bond

Cash was held in the previous financial year as a security deposit for the relinquished exploration licence EL4537.

(f) Financial Risk Management

Information concerning the Group's exposure to financial risks on security deposits is set out in Note 3.

	Consolidated	
	2011	2010
	$	$
Note 14. Other Assets		
Current		
Prepayments	**3,525,878**	710,376
Total current other assets	**3,525,878**	710,376

(a) Included in current prepayments are deposits of $2,093,163 on long lead materials inventory items for the anticipated Santos Basin Block exploration drilling program.

Non-current		
Prepayments	**1,102,759**	-
Total non-current other assets	**1,102,759**	-

	Note	Consolidated 2011 $	2010 $

Note 15. Plant and Equipment

	Note	2011 $	2010 $
Plant and equipment			
At cost		**3,284,993**	1,591,884
Accumulated depreciation		**(1,068,461)**	(984,332)
Total plant and equipment, at net book value		**2,216,532**	607,552

Reconciliation

The reconciliation of the carrying amount for plant and equipment is set out below:

	Note	2011 $	2010 $
Balance at beginning of financial year		**607,552**	618,562
Additions	22	**2,058,646**	235,213
Disposals		**(114,319)**	-
Depreciation expense	5	**(335,347)**	(246,223)
Net carrying amount at end of financial year		**2,216,532**	607,552

Note 16. Intangible Assets

	Note	2011 $	2010 $
Computer software			
At cost		**1,144,552**	825,904
Accumulated amortisation		**(664,511)**	(470,982)
Total intangibles, at net book value		**480,041**	354,922

Reconciliation

The reconciliation of the carrying amounts for computer software is set out below:

	Note	2011 $	2010 $
Balance at beginning of financial year		**354,922**	240,689
Additions	22	**321,017**	283,677
Amortisation expense	5	**(195,898)**	(169,444)
Net carrying amount at end of financial year		**480,041**	354,922

Note 17. Exploration and Evaluation Expenditure Carried Forward

	Note	2011 $	2010 $
Deferred geological, geophysical, drilling and other exploration and evaluation expenditure, including directly attributable general administrative costs		**276,465,002**	265,243,372

Reconciliation

The reconciliation of exploration and evaluation expenditure carried forward is set out below:

	Note	2011 $	2010 $
Balance at beginning of financial year		**265,243,372**	100,235,662
Additions	22	**22,242,534**	165,145,066
Net foreign currency difference on translation of financial statements of foreign subsidiaries		**(7,139,012)**	(137,356)
Exploration and evaluation expenditure written off (refer Note (a) below)	5	**(3,881,892)**	-
Total exploration and evaluation expenditure carried forward (refer Note (b) below)		**276,465,002**	265,243,372

Note 17. Exploration and Evaluation Expenditure Carried Forward (continued)

		Consolidated	
		2011	2010
	Note	**$**	$
Tangible		**-**	-
Intangible		**276,465,002**	265,243,372
Total exploration and evaluation expenditure carried forward		**276,465,002**	265,243,372

(a) Exploration and evaluation expenditure written off during the financial year related to the AC/P8 exploration permit, following a decision by the Board of Directors to surrender the permit in good standing having satisfied all firm commitments.

(b) Exploration and evaluation expenditure carried forward relates to areas of interest in the exploration and evaluation phase for exploration permits WA-314-P, WA-315-P, WA-398-P, Block 1037, Block 1101, Block 1102, Block 1165, Block 1166, Block Z-38 and Block 144 (30 June 2010: WA-314-P, WA-315-P, WA-398-P, Block 1037, Block 1101, Block 1102, Block 1165, Block 1166, Block Z-38, Block 144 and AC/P8).

The expenditure is carried forward on the basis that exploration and evaluation activities in the areas of interest have not reached a stage that permits reasonable assessment of the existence or otherwise of economically recoverable reserves and active and significant activity in, or in relation, to the areas is continuing. The future recoverability of the carrying amount of capitalised exploration and evaluation expenditure is dependent on successful development and commercial exploitation or, alternatively, the sale of the respective areas of interest.

		Consolidated	
		2011	2010
	Note	**$**	$

Note 18. Trade and Other Payables

Current (unsecured)			
Trade payables		**1,149,991**	477,260
Sundry payables and accrued expenditure		**3,156,595**	13,434,983
Total current trade and other payables		**4,306,586**	13,912,243

(a) Financial Risk Management

Information concerning the Group's exposure to financial risks on trade and other payables is set out in Note 3.

Note 19. Provisions

Non-current			
Provision for long service leave		**99,484**	60,738
Total non-current provisions		**99,484**	60,738

(a) Provision for Long Service Leave

A provision was recognised for employee entitlements relating to long service leave. The measurement and recognition criteria relating to long service leave entitlements are as described in Note 1(q).

	Consolidated 2011 Number	Consolidated 2010 Number	Consolidated 2011 $	Consolidated 2010 $

Note 20. Issued Capital and Reserves within Equity

(a) Share Capital

	2011 Number	2010 Number	2011 $	2010 $
Ordinary shares, fully paid	**221,420,769**	177,546,198	**664,894,335**	381,147,212

Ordinary shares have no par value and the Company does not have a limited amount of authorised capital.

Voting rights of shareholders are governed by the Company's Constitution. In summary, on a show of hands every holder of ordinary shares present at a meeting in person or by proxy is entitled to one vote, and upon a poll each such attending shareholder is entitled to one vote for every fully paid ordinary share held.

Ordinary shares participate in dividends as declared from time to time and the proceeds on winding up of the Company in proportion to the number of fully paid ordinary shares held.

(b) Movement in Ordinary Shares

Date	Details	Note	Number of Ordinary Shares	Issue Price Per Ordinary Share	$
1 July 2009	Opening balance in previous financial year		171,301,831		347,331,271
2 July 2009	Exercise of ESOP options	(i)	30,000	$2.95	88,500
7 July 2009	Exercise of ESOP options	(i)	50,000	$4.00	200,000
14 July 2009	Exercise of ESOP options	(i)	100,000	$2.95	295,000
14 July 2009	Exercise of ESOP options	(i)	100,000	$4.00	400,000
17 July 2009	Exercise of ESOP options	(i)	100,000	$2.95	295,000
21 July 2009	Exercise of ESOP options	(i)	100,000	$4.00	400,000
21 July 2009	Exercise of ESOP options	(i)	130,000	$2.95	383,500
22 July 2009	Exercise of ESOP options	(i)	30,000	$4.00	120,000
24 July 2009	Share purchase plan	(ii)	3,514,367	$6.70	23,546,259
27 July 2009	Exercise of ESOP options	(i)	200,000	$4.00	800,000
27 July 2009	Exercise of ESOP options	(i)	100,000	$5.00	500,000
30 July 2009	Exercise of ESOP options	(i)	10,000	$4.00	40,000
10 August 2009	Exercise of other share options	(i)	1,250,000	$4.00	5,000,000
28 October 2009	Exercise of ESOP options	(i)	100,000	$4.00	400,000
16 February 2010	Exercise of ESOP options	(i)	20,000	$2.95	59,000
16 February 2010	Exercise of ESOP options	(i)	42,500	$4.00	170,000
11 March 2010	Exercise of ESOP options	(i)	50,000	$4.00	200,000
16 March 2010	Exercise of ESOP options	(i)	60,000	$2.95	177,000
18 March 2010	Exercise of ESOP options	(i)	85,000	$4.00	340,000
23 March 2010	Exercise of ESOP options	(i)	165,000	$4.00	660,000
26 March 2010	Exercise of ESOP options	(i)	7,500	$4.00	30,000
	Less: Transaction costs arising on ordinary shares issued during previous financial year				(288,318)

Note 20. Issued Capital and Reserves Within Equity (continued)

Date	Details	Note	Number of Ordinary Shares	Issue Price Per Ordinary Share	$
30 June 2010	Balance at end of previous financial year		177,546,198		381,147,212
22 September 2010	Share placement	(ii)	**26,631,929**	**$7.00**	**186,423,503**
23 September 2010	Exercise of ESOP options	(i)	**50,000**	**$5.00**	**250,000**
23 September 2010	Exercise of other share options	(i)	**200,000**	**$2.95**	**590,000**
30 September 2010	Exercise of ESOP options	(i)	**60,000**	**$2.95**	**177,000**
30 September 2010	Exercise of ESOP options	(i)	**50,000**	**$5.00**	**250,000**
30 September 2010	Exercise of other share options	(i)	**520,000**	**$2.95**	**1,534,000**
1 October 2010	Exercise of other share options	(i)	**280,000**	**$2.95**	**826,000**
12 October 2010	Exercise of ESOP options	(i)	**25,000**	**$5.00**	**125,000**
12 October 2010	Exercise of ESOP options	(i)	**145,000**	**$2.95**	**427,750**
14 October 2010	Exercise of ESOP options	(i)	**5,000**	**$5.00**	**25,000**
27 October 2010	Exercise of ESOP options	(i)	**75,000**	**$4.00**	**300,000**
27 October 2010	Share purchase plan	(ii)	**11,692,642**	**$7.00**	**81,848,494**
28 October 2010	Exercise of ESOP options	(i)	**15,000**	**$4.00**	**60,000**
9 February 2011	Exercise of ESOP options	(i)	**200,000**	**$5.00**	**1,000,000**
11 February 2011	Exercise of ESOP options	(i)	**25,000**	**$5.00**	**125,000**
14 February 2011	Exercise of ESOP options	(i)	**100,000**	**$5.00**	**500,000**
16 February 2011	Exercise of ESOP options	(i)	**5,000**	**$5.00**	**25,000**
23 February 2011	Exercise of ESOP options	(i)	**20,000**	**$5.00**	**100,000**
25 February 2011	Exercise of other share options	(i)	**1,500,000**	**$5.00**	**7,500,000**
25 February 2011	Exercise of other share options	(i)	**1,500,000**	**$4.50**	**6,750,000**
25 February 2011	Exercise of ESOP options	(i)	**30,000**	**$5.00**	**150,000**
28 February 2011	Exercise of ESOP options	(i)	**50,000**	**$5.00**	**250,000**
4 March 2011	Exercise of ESOP options	(i)	**25,000**	**$5.00**	**125,000**
9 March 2011	Exercise of ESOP options	(i)	**20,000**	**$5.00**	**100,000**
16 March 2011	Exercise of ESOP options	(i)	**10,000**	**$5.00**	**50,000**
22 March 2011	Exercise of ESOP options	(i)	**225,000**	**$5.00**	**1,125,000**
25 March 2011	Exercise of ESOP options	(i)	**40,000**	**$5.00**	**200,000**
11 April 2011	Exercise of ESOP options	(i)	**65,000**	**$5.00**	**325,000**
2 May 2011	Exercise of ESOP options	(i)	**60,000**	**$5.00**	**300,000**
2 May 2011	Exercise of other share options	(i)	**250,000**	**$4.00**	**1,000,000**
	Less: Transaction costs arising on ordinary shares issued during financial year				**(8,714,624)**
30 June 2011	Balance at end of financial year		**221,420,769**		**664,894,335**

(i) Employee Share Option Plan ('ESOP') and Other Share Options

Information relating to the Company's ESOP and other share options, including details of options granted, exercised, cancelled, forfeited and expired during the financial year and options outstanding at the end of the financial year, is set out in Note 27.

(ii) Share Placement and Share Purchase Plan

The purpose of the share placement to sophisticated and professional investors during September 2010 and the share purchase plan during October 2010 was to provide the Group with a strong cash position for its continued exploration and appraisal program in the Browse Basin, exploration in Brazil and Peru and general working capital.

The purpose of the share purchase plan during July 2009 was to provide the Group with a strong cash position for its continued exploration and appraisal program in the Browse Basin, along with exploration programs in Peru and Brazil.

(c) Capital Management

The Board of Directors controls the capital of the Company in order to ensure that the Group can fund its operations and continue as a going concern. The aim is to maintain a capital structure that ensures the lowest cost of capital to the Company.

The Executive Chairman manages the Company's capital by monitoring future rolling cash flows and adjusting its capital structure, as required, in consultation with the Board of Directors to meet Group business objectives.

There were no externally imposed capital management restrictions on the Group during the financial year.

(d) Reserves within Equity

(i) Share-based Payments Reserve

The share-based payment reserve is used to recognise the grant date fair value of share-based payments to Directors, other key management personnel and employees as part of their remuneration, as described in Note 1(p).

(ii) Foreign Currency Translation Reserve

The foreign currency translation reserve is used to recognise exchange differences arising from the translation of financial statements of foreign subsidiaries, as described in Note 1(e). The relevant amounts included in the foreign currency translation reserve will be recognised in the consolidated statement of comprehensive income when each relevant investment in foreign subsidiary is disposed.

Note 21. Subsidiaries

The financial statements incorporate the assets, liabilities and results of the following subsidiaries in accordance with the accounting policy described in Note 1(b):

Name	Country of Incorporation or Registration	Business Activities Carried on in	Percentage of Equity and Voting Interests Held 2011 %	2010 %
Parent Company:				
Karoon Gas Australia Ltd	Australia	Australia		
Unlisted subsidiaries of Karoon Gas Australia Ltd:				
Eastern Pacific Coal Pty Ltd	Australia	Australia	**100.0**	100.0
Karoon Energy International Ltd	Australia	Australia	**100.0**	100.0
Karoon Gas (Browse Basin) Pty Ltd	Australia	Australia	**100.0**	100.0
Karoon Gas Pty Ltd	Australia	Australia	**100.0**	100.0
Karoon Gas (FPSO) Pty Ltd	Australia	Australia	**100.0**	-
Unlisted subsidiaries of Karoon Energy International Ltd:				
KEI (Brazil Santos) Pty Ltd	Australia	Australia	**100.0**	100.0
KEI (Peru 112) Pty Ltd	Australia	Australia	**100.0**	100.0
KEI (Peru Z38) Pty Ltd	Australia	Australia	**100.0**	100.0
Jointly owned unlisted subsidiary of Karoon Energy International Ltd and KEI (Brazil Santos) Pty Ltd:				
Karoon Petróleo & Gas SA	Brazil	Brazil	**100.0**	100.0
Branch of KEI (Peru 112) Pty Ltd:				
KEI (Peru 112) Pty Ltd, Sucursal del Peru	Peru	Peru	**100.0**	100.0
Branch of KEI (Peru Z38) Pty Ltd:				
KEI (Peru Z38) Pty Ltd, Sucursal del Peru	Peru	Peru	**100.0**	100.0

Karoon Petróleo & Gas Ltda changed its name to Karoon Petróleo & Gas SA during the financial year.

Karoon Gas (FPSO) Pty Ltd was incorporated as a proprietary company limited by shares on 13 January 2011.

Note 22. Segment Information

(a) Description of Segments

The Group has identified its operating segments based on the internal reports that are reviewed and used by the Executive Chairman and Executive Director/Exploration Director (identified as the 'chief operating decision maker') in assessing performance and in determining the allocation of resources.

The operating segments identified are based on the Group's equity interest in each individual exploration permit. Discrete financial information (including expenditure on exploration and evaluation assets) is provided to the chief operating decision maker on a regular basis. In certain circumstances, individual exploration permits are aggregated into a single operating segment where the economic characteristics and long term planning and operational considerations of the individual exploration permits are such that they are considered interdependent.

The Group has identified three operating segments:

(i) Australia exploration – the Group is currently involved in the exploration and evaluation of hydrocarbons in three offshore permit areas within the Browse Basin, Australia: WA-314-P, WA-315-P, WA-398-P; and one offshore permit area within the Bonaparte Basin, Australia: AC/P8;

(ii) Brazil exploration – the Group is currently involved in the exploration and evaluation of hydrocarbons in five offshore blocks within the Santos Basin, Brazil: Block 1037, Block 1101, Block 1102, Block 1165 and Block 1166; and

(iii) Peru exploration – the Group is currently involved in the exploration and evaluation of hydrocarbons in two blocks in Peru: Block 144 (onshore) and Block Z-38 (offshore).

'All other segments' include amounts of a corporate nature not specifically attributable to an operating segment.

The following items and associated assets and liabilities are not allocated to operating segments as they are not considered part of the core operations of any segment but are reviewed by the chief operating decision maker on a regular basis:

- interest income;
- net foreign currency gains (losses);
- finance costs;
- net employee benefits expense (including non-cash share-based payments expense of $5,069,475 (2010: $5,289,047));
- administration and other operating expenses (including Brazilian initial public offering expenses of $5,673,914 (2010: $407,317));
- depreciation and amortisation expense;
- property costs; and
- income tax expense.

Employee benefits expenses and other operating expenses, that are associated with the exploration and evaluation activities and specifically relate to an area of interest, are allocated to the area of interest and are capitalised as exploration and evaluation assets.

Segment revenues and results do not include transfers between segments as intercompany balances are eliminated on consolidation.

The amounts provided to the chief operating decision maker with respect to total assets are measured in a manner consistent with that of the financial statements. Reportable segment assets are equal to consolidated total assets.

Note 22. Segment Information (continued)

(b) Operating Segments

Segment Performance	Australia $	Brazil $	Peru $	All Other Segments $	Consolidated $
Revenue for financial year ended 30 June 2011					
Segment revenue	**-**	**-**	**-**	**-**	**-**
Interest income from unrelated entities	**-**	**-**	**-**	**14,225,048**	**14,225,048**
Total revenue					**14,225,048**
Result for financial year ended 30 June 2011					
Segment result	**(4,448,680)**	**(32,449)**	**(18,277)**	**(163,148)**	**(4,662,554)**
Interest income from unrelated entities	**-**	**-**	**-**	**14,225,048**	**14,225,048**
Net foreign currency losses	**-**	**-**	**-**	**(10,440,658)**	**(10,440,658)**
Finance costs	**-**	**-**	**-**	**(456,290)**	**(456,290)**
Employee benefits expense (net)	**-**	**-**	**-**	**(8,529,761)**	**(8,529,761)**
Administration and other operating expenses	**-**	**-**	**-**	**(12,133,822)**	**(12,133,822)**
Depreciation and amortisation expense	**-**	**-**	**-**	**(531,245)**	**(531,245)**
Property costs	**-**	**-**	**-**	**(775,632)**	**(775,632)**
Loss before income tax					**(23,304,914)**
Income tax expense					**-**
Loss for financial year					**(23,304,914)**
Revenue for financial year ended 30 June 2010					
Segment revenue	-	-	-	-	-
Interest income from unrelated entities	-	-	-	6,459,623	6,459,623
Total revenue					6,459,623
Result for financial year ended 30 June 2010					
Segment result	(70,705)	(12,207)	(3,001)	(49,985)	(135,898)
Interest income from unrelated entities	-	-	-	6,459,623	6,459,623
Net foreign currency losses	-	-	-	(8,514,337)	(8,514,337)
Finance costs	-	-	-	(244,275)	(244,275)
Employee benefits expense (net)	-	-	-	(6,719,729)	(6,719,729)
Administration and other operating expenses	-	-	-	(4,820,088)	(4,820,088)
Depreciation and amortisation expense	-	-	-	(415,667)	(415,667)
Property costs	-	-	-	(274,646)	(274,646)
Loss before income tax					(14,665,017)
Income tax expense					(228,822)
Loss for previous financial year					(14,893,839

Segment Assets	Australia $	Brazil $	Peru $	All Other Segments $	Consolidated $
As at 30 June 2011					
Segment asset information					
Cash and cash equivalents	**343,869**	**848,356**	**85,553**	**265,561,366**	**266,839,144**
Exploration and evaluation expenditure carried forward	**195,034,904**	**58,519,082**	**22,911,016**	**-**	**276,465,002**
Security deposits	**-**	**56,811,842**	**10,011,647**	**537,091**	**67,360,580**
Inventories	**279,892**	**-**	**-**	**-**	**279,892**
Other	**188,091**	**4,150,819**	**2,263,013**	**4,726,853**	**11,328,776**
Segment assets	**195,846,756**	**120,330,099**	**35,271,229**	**270,825,310**	**622,273,394**
As at 30 June 2010					
Segment asset information					
Cash and cash equivalents	10,230,163	1,965,638	223,434	74,703,601	87,122,836
Exploration and evaluation expenditure carried forward	190,077,406	52,024,240	23,141,726	-	265,243,372
Security deposits	35,115	11,723,326	4,810,814	70,307	16,639,562
Inventories	360,081	-	-	-	360,081
Other	1,339,515	28,487	3,343,996	1,834,430	6,546,428
Segment assets	202,042,280	65,741,691	31,519,970	76,608,338	375,912,279

(c) Other Segment Information

Additions to non-current assets, other than financial assets (refer Note 3), during the reporting periods were:

Segment Assets	Australia $	Brazil $	Peru $	All Other Segments $	Consolidated $
Financial year ended 30 June 2011					
Plant and equipment	**-**	**-**	**-**	**2,058,646**	**2,058,646**
Intangible assets	**-**	**-**	**-**	**321,017**	**321,017**
Exploration and evaluation expenditure carried forward	**8,839,390**	**9,595,443**	**3,807,701**	**-**	**22,242,534**
Other assets (prepayments)	**-**	**1,102,759**	**-**	**-**	**1,102,759**
Financial year ended 30 June 2010					
Plant and equipment	-	-	-	235,213	235,213
Intangible assets	-	-	-	283,677	283,677
Exploration and evaluation expenditure carried forward	128,212,334	20,525,118	16,407,614	-	165,145,066

Note 23. Joint Venture Operations

The Group had an interest in the following joint venture operations as at 30 June 2011 as follows:

Exploration Permit	Unincorporated Interest 2011 %	Unincorporated Interest 2010 %	Principal Activities	Operator of Joint Venture Operation
WA-314-P	**90.00^**	40.00	Exploration and evaluation	ConocoPhillips
WA-315-P	**40.00**	40.00	Exploration and evaluation	ConocoPhillips
WA-398-P	**40.00**	40.00	Exploration and evaluation	ConocoPhillips
AC/P8	**66.67**	66.67	Exploration and evaluation	Karoon Energy International Ltd
Block Z-38	**75.00#**	75.00#	Exploration and evaluation	KEI (Peru Z38) Pty Ltd, Sucursal del Peru

^ The Group's 90% equity interest is subject to regulatory approval.
# The Group's 75% Block equity interest is subject to completion of farm-in obligations.

Note 23. Joint Venture Operations (continued)

The following amounts represented the Group's share of assets and liabilities employed in joint venture operations. The amounts are included in the financial statements, in accordance with the accounting policy described in Note 1(s), under the following classifications:

	Consolidated	
	2011 **$**	2010 $
Cash and cash equivalents	**343,869**	10,217,259
Other receivables	**118,278**	872,986
Inventories	**279,892**	360,081
Total current assets	**742,039**	11,450,326
Exploration and evaluation expenditure carried forward	**216,828,377**	212,525,349
Total non-current assets	**216,828,377**	212,525,349
Trade payables	**-**	19,130
Sundry payables and accrued expenditure	**200,796**	10,651,597
Total current liabilities	**200,796**	10,670,727
Share of net assets employed in joint venture operations	**217,369,620**	213,304,948

The future recoverability of the carrying amount of capitalised exploration and evaluation expenditure is dependent on successful development and commercial exploitation or, alternatively, the sale of the respective areas of interest.

Contingent liabilities in respect of joint venture operations are set out in Note 24. Exploration expenditure commitments and capital commitments in respect of joint venture operations are set out in Note 25.

Parent Company guarantees have been provided to ConocoPhillips guaranteeing Karoon Gas (Browse Basin) Pty Ltd's performance under the joint venture operating agreements covering the three Browse Basin permit interests. In addition, a deed of cross charge has been entered into with ConocoPhillips by Karoon Gas (Browse Basin) Pty Ltd covering its three Browse Basin permit interests.

Note 24. Contingent Liabilities and Contingent Assets

(a) Contingent Liabilities

The Group had contingent liabilities as at 30 June 2011 that may become payable in respect of:

	Consolidated	
	2011 **$**	2010 $
(i) The Group has provided Agencia Nacional do Petróleo (the Brazilian Petroleum Agency) letters of credit and insurance bonds to carry out minimum work programs in relation to the Group's exploration permits in the Santos Basin, Brazil. The Directors are of the opinion that the work programs will be satisfied. The letters of credit are fully funded by way of payment of security deposit (refer Note 13), which will be released once the work programs are met. The insurance bonds have been part funded to 50% of the value of the total bonds provided to Agencia Nacional do Petróleo by establishment of an escrow account. The principal funds held in escrow will be released as work is undertaken to satisfy the work programs.	**56,811,842**	11,723,326
(ii) Performance guarantees (via letters of credit) were provided to Peru Petro SA for Block Z-38 and Block 144 by the Group for second and third period work commitments (2010: first and second period work commitments). The Directors are of the opinion that the work commitments will be satisfied for both Blocks. The letters of credit are fully funded by way of payment of security deposit (refer Note 13), which will be released once the work commitments are met.	**10,011,647**	4,517,490

	Consolidated	
	2011	2010
	$	$
(iii) Bank guarantees were provided in respect of operating lease rental agreements for the Group. These guarantees may give rise to liabilities in the Group if obligations are not met under these guarantees. The bank guarantees given to lessors are fully funded by way of payment of security deposit (refer Note 13).	**537,091**	70,307
(iv) In the previous financial year, a performance guarantee (via a letter of credit) was provided to a third party supplier by the Group for exploration work undertaken in Peru. The letter of credit was fully funded by way of payment of a security deposit (refer Note 13), and was released once the Group's obligation under the contract was satisfied.	**-**	293,324
(v) On 23 August 2010, Karoon Petróleo & Gas SA, a wholly owned subsidiary of the Company, executed a farm-in agreement with Petróleo Brasileiro SA ('Petrobras') to acquire a 20% interest in both Block S-M-1352 and Block S-M-1354 located in the offshore Santos Basin, Brazil.	**39,429,646**	-

Under the farm-in agreement and subject to obtaining regulatory approvals from Agencia Nacional do Petróleo (the Brazilian Petroleum Agency), Karoon Petróleo & Gas SA. will earn a 20% equity interest by funding a proportion of the costs of drilling two exploration wells. Karoon Petróleo & Gas SA will then pay its equity share of continued work and reimburse Petrobras for sunk costs.

The two well drilling program included drilling of the Quasi Prospect in Block S-M-1354, which was subsequently plugged and abandoned during September 2010. The second well, the Maruja-1 exploration well, in Block S-M 1352 commenced drilling during September 2010 and was suspended following a completion of a production test during January 2011. Block S-M 1354 expired during November 2010 and was formally relinquished by Petrobras during January 2011. The farm-in area of S-M 1352 has been reduced to an area retained around the Maruja discovery. This reduction also includes the partial relinquishment of S-M 1352.

Continued work during the financial year also included the drilling of a third well, the Maruja-2 appraisal well, which was completed and abandoned during March 2011.

Under the farm-in agreement with Petrobras, the Group's share of the costs incurred on both Blocks as at 30 June 2011 was $39,429,646, which is payable upon obtaining regulatory approvals.

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(vi) Joint venture operations

In accordance with normal industry practice, the Group has entered into joint venture operations with other parties for the purpose of exploring and evaluating its permit interests. If a participant to a joint venture operation defaults and does not contribute its share of joint venture operation obligations, then the remaining joint venture participants are jointly and severally liable to meet the obligations of the defaulting participant. In this event, the interest in the exploration permit held by the defaulting participant may be redistributed to the remaining joint venture participants.

In the event of a default, a contingent liability exists in respect of expenditure commitments due to be met by the Group in respect of the defaulting joint venture participant.

No material losses are anticipated in respect of any of the above contingent liabilities.

(b) Contingent Assets

The Group had no contingent assets as at 30 June 2011 (30 June 2010: $Nil).

	Consolidated 2011 $	2010 $

Note 25. Commitments

(a) Capital Expenditure Commitments

	2011 $	2010 $
Contracts for capital expenditure in relation to assets not provided for in the financial statements and payable:		
Drilling operations (non-joint venture operations)		
Not later than one year	**12,965,882**	-
Total capital expenditure commitments	**12,965,882**	-

(b) Operating Lease Rental Commitments

	2011 $	2010 $
Non-cancellable operating lease rentals not provided for in the financial statements and payable:		
Not later than one year	**855,745**	294,144
Later than one year but not later than five years	**2,829,030**	443,945
Later than five years	**192,762**	-
Total operating lease rental commitments	**3,877,537**	738,089

The Group has an office lease for Office 6 & 7, 34-38 Lochiel Avenue, Mount Martha with a primary three year term that expires on 31 January 2013. Rent is payable monthly in advance. Annually from the commencement date, the rent is adjusted by reference to the consumer price index. There is an option to extend for one further term of three years, except that a market review of rent will be triggered on renewal.

The Group has an office lease for Level 25, 367 Collins Street, Melbourne with a primary six year term that expires on 30 November 2016 and a 4% p.a. rental increase. Rent is payable monthly in advance. There is no option for renewal at the end of the term.

The Group also has an office lease at Level 10, 406 Collins Street, Melbourne with a five year term that expires on 31 May 2012 and a 4% p.a. rental increase. Rent is payable monthly in advance.

The Group has two office leases in Brazil. One at Rua Visconde de Pirajá, 303 – 9º Andar – Salas 904/912, Ipanema, Rio de Janeiro with a primary four year term that expires on 30 April 2015. Rent is payable monthly in advance. There is an option to extend for a further term, which is negotiable at the end of the lease. The second office lease is at Av Afonso Delambert Neto, 619 sala 5 Lagoa da Conceição, Florianópolis with a primary four year term that expires on 30 April 2015. Rent is payable monthly in advance. The lease can be renewed for no more than 12 months. A market review of rent is triggered at the end of the lease term.

The Group has an office lease at Antequera 777, 101, Sam Isidro, Peru with a primary term that expires on 31 July 2013. Rent is payable monthly in advance. There is an option to extend for a further term of twelve months, on essentially the same terms and conditions, except that a market review of rent will be triggered on renewal.

(c) Exploration Expenditure Commitments

Some subsidiaries within the Group have commitments for exploration expenditure arising from obligations to government, to perform minimum exploration and evaluation work and expend minimum amounts of money pursuant to the award of exploration permits WA-314-P, WA-315-P, WA-398-P, Block 1037, Block 1101, Block 1102, Block 1165, Block 1166, Block Z-38, Block 144 and AC/P8 (30 June 2010: WA-314-P, WA-315-P, WA-398-P, Block 1037, Block 1101, Block 1102, Block 1165, Block 1166, Block Z-38, Block 144 and AC/P8) not provided for in the financial statements and payable. Included in exploration expenditure commitments are $90,965,044 (30 June 2010: $175,918,961) of commitments that relate to the non-guaranteed work commitments:

	Consolidated 2011 $	2010 $
Not later than one year	**155,694,566**	40,061,235
Later than one year but not later than five years	**265,895,674**	215,123,116
Total exploration expenditure commitments	**421,590,240**	255,184,351
The above commitments include exploration expenditure commitments relating to joint venture operations:		
Not later than one year	**155,694,566**	40,061,235
Later than one year but not later than five years	**146,836,168**	156,618,029
Total joint venture operation exploration expenditure commitments	**302,530,734**	196,679,264

Estimates for future exploration expenditure commitments to government are based on estimated well and seismic costs, which will change as actual drilling locations and seismic surveys are organised, and are determined in current dollars on an undiscounted basis. The exploration and evaluation obligations may vary significantly as a result of renegotiations with relevant parties.

The commitments may also be reduced by the Group entering into farm-out agreements, which are typical of the normal operating activities of the Group.

Where exploration and evaluation expenditure included in this category relates to an existing contract for expenditure, the amount will be included in both categories (a) and (c) above.

Note 26. Notes to the Consolidated Statement of Cash Flows

Reconciliation of Loss for Financial Year to Net Cash Flows Used in Operating Activities

	Consolidated 2011 $	2010 $
Loss for financial year	**(23,304,914)**	(14,893,839)
Add (subtract):		
Depreciation of plant and equipment and amortisation of computer software	**531,245**	415,667
Net foreign currency losses	**9,675,904**	8,393,323
Non-cash employee benefits expense: share-based payments expense	**5,069,475**	5,289,047
Items classified as investing/financing activities:		
Exploration and evaluation expenditure written off	**3,881,892**	-
Net foreign currency losses	**764,754**	121,005
Net loss on disposal of plant and equipment	**82,945**	-
Change in operating assets and liabilities		
(Increase) decrease in assets:		
Receivables – current	**(959,099)**	93,443
Security deposits	**(2,855,838)**	(1,182,800)
Other assets	**466,076**	(411,374)
Increase (decrease) in liabilities:		
Trade and other payables – current	**826,430**	173,457
Provisions	**38,746**	(33,217)
Income tax liability	**(220,227)**	228,822
Net cash flows used in operating activities	**(6,002,611)**	(1,806,466)

Note 27. Share-based Payments

The share-based payments plan is described below. There has been no cancellation to the plan during the financial year. Amendments to the plan and its continuing operation were approved by shareholders at the 2009 Annual General Meeting.

(a) Employee Share Option Plan

The Group had an ESOP, which has been operating since the listing of the Company on the ASX. ESOP options expire up to four years after they are granted. The exercise price of ESOP options, issued during the financial year, is based on the volume weighted average price at which the Company's ordinary shares are traded on the ASX during the 180 trading days before the ESOP options are offered. ESOP options may be exercised after the date the option was granted. If there is a change of control in the Company, all unexercised ESOP options will become immediately exercisable. Options granted under the ESOP carry no dividend or voting rights. When exercisable, each ESOP option is convertible into one ordinary share of the Company.

The following summary reconciles the outstanding ESOP options over unissued ordinary shares in the Company at the beginning and end of the financial year:

	Consolidated		Consolidated	
	2011 Number	**2011 Weighted Average Exercise Price**	2010 Number	2010 Weighted Average Exercise Price
Balance at beginning of financial year	**3,830,000**	**$9.27**	3,010,000	$4.36
Granted during financial year	**1,445,000**	**$9.77**	2,330,000	$12.08
Exercised during financial year	**(1,300,000)**	**$4.61**	(1,480,000)	$3.76
Cancelled during financial year	**(200,000)**	**$10.64**	(30,000)	$6.84
Forfeited during financial year	**-**	**-**	-	-
Expired during financial year	**-**	**-**	-	-
Balance at end of financial year	**3,775,000**	**$11.00**	3,830,000	$9.27
Exercisable at end of financial year	**830,000**	**$11.81**	2,030,000	$7.30

The weighted average fair value of ESOP options granted during the financial year was $1.99 (2010: $3.31).

The weighted average share price when the ESOP options were exercised during the financial year was $7.66 (2010: $9.38).

ESOP options outstanding as at 30 June 2011 had a range of exercise prices from $6.84 to $14.07 (30 June 2010: $2.95 to $14.07) with a weighted average remaining contractual life of 956 days (30 June 2010: 866 days).

Details of ESOP options outstanding at the end of the financial year are:

Grant Date	Expiry Date	Exercise Price Per Option	Number
29 June 2009	30 October 2011	$6.84	**200,000**
23 November 2009	12 November 2013	$14.07	**530,000**
9 December 2009	18 November 2013	$11.50	**1,600,000**
25 March 2010	18 November 2013	$11.50	**100,000**
3 September 2010	31 October 2014	$9.77	**945,000**
12 January 2011	31 October 2014	$9.77	**300,000**
18 November 2010	18 November 2014	$9.77	**100,000**
Total ESOP options			**3,775,000**

(b) Other Share Options

The Group had granted other share options over unissued ordinary shares in the Company during the financial year to Directors. The exercise price of other share options is based on the weighted average price at which the Company's ordinary shares are traded on the ASX during the 180 trading days before the options are offered. Other share options may be exercised after the date the option was granted. If there is a change of control of the Company, all unexercised other share options will become immediately exercisable. Other share options granted carry no dividend or voting rights. When exercisable, each other share option is convertible into one ordinary share of the Company.

Options issued to Directors are approved on a case-by-case basis by shareholders at relevant general meetings.

The following summary reconciles the outstanding other share options over unissued ordinary shares in the Company at the beginning and end of the financial year:

	Consolidated		Consolidated	
	2011 Number	**2011 Weighted Average Exercise Price**	2010 Number	2010 Weighted Average Exercise Price
Balance at beginning of financial year	**5,250,000**	**$6.15**	5,500,000	$4.22
Granted during financial year	**500,000**	**$9.48**	1,000,000	$14.07
Exercised during financial year	**(4,250,000)**	**$4.28**	(1,250,000)	$4.00
Forfeited during financial year	**-**	**-**	-	-
Expired during financial year	**-**	**-**	-	-
Balance at end of financial year	**1,500,000**	**$12.54**	5,250,000	$6.15
Exercisable at end of financial year	**-**	**-**	4,250,000	$4.28

The weighted average fair value of other share options granted during the financial year was $2.75 (2010: $2.40).

The weighted average share price when other share options were exercised during the financial year was $7.17 (2010: $10.60).

Other share options outstanding as at 30 June 2011 had a range of exercise prices from $9.48 to $14.07 (30 June 2010: $2.95 to $14.07) with a weighted average remaining contractual life of 990 days (30 June 2010: 446 days).

Details of other share options outstanding at the end of the financial year are:

Grant Date	Expiry Date	Exercise Price Per Option	Number
23 November 2009	12 November 2013	$14.07	**1,000,000**
18 November 2010	18 November 2014	$9.48	**500,000**
Total other share options			**1,500,000**

Note 27. Share-based Payments (continued)

(c) Fair Value of Options

The fair value of each option during the financial year was estimated on grant date using the Black-Scholes option pricing model. The Black-Scholes option pricing model takes into account the exercise price, the term of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

The Group applied the following assumptions and inputs in estimating the weighted average fair value:

	2011	2010
Weighted average exercise price	**$9.70**	$12.98
Weighted average life of options	**1,481 days**	1,408 days
Weighted average share price	**$7.13**	$8.21
Expected share price volatility	**42%**	55%
Risk free interest rate	**5.21%**	5.44%
Weighted average option value	**$2.19**	$2.90

Historical volatility was the basis for determining expected share price volatility as it is assumed that this is indicative of future trends, which may not eventuate.

(d) Share-based Payments Expense

Total expenses arising from share-based payment transactions recognised during the financial year, included as part of employee benefits expense in the consolidated statement of comprehensive income, was $5,069,475 (2010: $5,289,047).

Note 28. Remuneration of Key Management Personnel

Directors and other key management personnel at any time during the financial year were as follows:

Name	**Position**
Directors	
Mr Robert Hosking	Executive Chairman
Mr Mark Smith	Executive Director and Exploration Director
Mr Geoff Atkins	Independent Non-Executive Director
Mr Clark Davey	Independent Non-Executive Director
Mr Stephen Power	Non-Executive Director
Other key management personnel	
Mr Scott Hosking	Company Secretary and Chief Financial Officer (Group)
Mr Tim Hosking	Chief Executive Officer South America
Mr Lino Barro	Engineering Manager
Mr Edward Munks	Chief Operating Officer

All of the above persons were also Directors or other key management personnel during the previous financial year, except for Mr Clark Davey and Mr Edward Munks.

(a) Directors and Other Key Management Personnel Remuneration

Directors and other key management personnel remuneration was summarised as follows:

	Consolidated	
	2011	2010
	$	$
Short term employee benefits	**2,044,994**	2,096,999
Post-employment benefits	**170,533**	150,680
Long term employee benefits (non-cash)	**25,648**	-
Share-based payments expense (non-cash)	**2,044,402**	3,203,299
Total key management personnel remuneration	**4,285,577**	5,450,978

Detailed remuneration disclosures are provided in Sections A-D of the audited Remuneration Report on pages 22 to 29.

(b) Employee Share Option Plan and Other Share Options

Information relating to the Company's ESOP and other share options, including details of options granted, exercised, cancelled, forfeited and expired during the financial year and options over unissued ordinary shares in the Company outstanding at the end of the financial year to Directors, other key management personnel and others, is set out in Note 27.

(c) Options Over Unissued Ordinary Shares in the Company

During the financial year 900,000 (2010: 2,230,000) options over unissued ordinary shares in the Company were issued to Directors and other key management personnel.

The movement of options over unissued ordinary shares in the Company held by Directors and other key management personnel, including their personally-related entities, during the financial year and previous financial year was as follows:

	Balance as at 1 July 2010	Granted as Remuneration	Options Exercised	Net Change Other	Balance as at 30 June 2011	Total Vested as at 30 June 2011	Total Exercisable as at 30 June 2011	Total Unexercisable as at 30 June 2011
Executive Directors								
Mr Robert Hosking	1,750,000	-	(1,750,000)	-	-	-	-	-
Mr Mark Smith	1,500,000	-	(1,500,000)	-	-	-	-	-
Non-Executive Directors								
Mr Geoff Atkins	1,000,000	-	(500,000)	-	**500,000**	-	-	**500,000**
Mr Clark Davey *(appointed 1 October 2010)*	-	500,000	-	-	**500,000**	-	-	**500,000**
Mr Stephen Power	1,000,000	-	(500,000)	-	**500,000**	-	-	**500,000**
Other key management personnel								
Mr Scott Hosking	500,000	100,000	(200,000)	-	**400,000**	**400,000**	**400,000**	-
Mr Tim Hosking	230,000	-	-	-	**230,000**	**230,000**	**230,000**	-
Mr Lino Barro	400,000	100,000	(100,000)	-	**400,000**	-	-	**400,000**
Mr Edward Munks *(appointed 1 January 2011)*	30,000	200,000	(30,000)	-	**200,000**	-	-	**200,000**
Total key management personnel	6,410,000	900,000	(4,580,000)	-	**2,730,000**	**630,000**	**630,000**	**2,100,000**

Note 28. Remuneration of Key Management Personnel

	Balance as at 1 July 2009	Granted as Remuneration	Options Exercised	Net Change Other	Balance as at 30 June 2010	Total Vested as at 30 June 2010	Total Exercisable as at 30 June 2010	Total Unexercisable as at 30 June 2010
Executive Directors								
Mr Robert Hosking	2,250,000	-	(500,000)	-	1,750,000	1,750,000	1,750,000	-
Mr Mark Smith	2,250,000	-	(750,000)	-	1,500,000	1,500,000	1,500,000	-
Non-Executive Directors								
Mr Geoff Atkins	500,000	500,000	-	-	1,000,000	500,000	500,000	500,000
Mr Stephen Power	500,000	500,000	-	-	1,000,000	500,000	500,000	500,000
Other key management personnel								
Mr Scott Hosking	300,000	300,000	(100,000)	-	500,000	500,000	500,000	-
Mr Tim Hosking	300,000	230,000	(300,000)	-	230,000	230,000	230,000	-
Mr Lino Barro	300,000	300,000	(200,000)	-	400,000	100,000	100,000	300,000
Mr David Ormerod	350,000	100,000	(150,000)	-	300,000	200,000	200,000	100,000
Mr Jorg Bein	300,000	300,000	(200,000)	-	400,000	100,000	100,000	300,000
Total key management personnel	7,050,000	2,230,000	(2,200,000)	-	7,080,000	5,380,000	5,380,000	1,700,000

(d) Shareholdings

The number of ordinary shares held by Directors and other key management personnel, including their personally-related entities, as at 30 June 2011 and 30 June 2010 was as follows:

	Balance as at 1 July 2010	Received as Remuneration	Options Exercised	Ordinary Shares Purchased	Ordinary Shares Sold	Other	Balance as at 30 June 2011
Executive Directors							
Mr Robert Hosking	12,102,320	-	1,750,000	22,142	(1,350,000)	-	**12,524,462**
Mr Mark Smith	2,572,037	-	1,500,000	-	(1,070,000)	-	**3,002,037**
Non-Executive Directors							
Mr Geoff Atkins	417,500	-	500,000	284,284	(505,000)	-	**696,784**
Mr Clark Davey *(appointed 1 October 2010)*	10,746	-	-	2,398	-	-	**13,144**
Mr Stephen Power	300,000	-	500,000	2,142	(200,000)	-	**602,142**
Other key management personnel							
Mr Scott Hosking	167,350	-	200,000	147,328	(245,000)	-	**269,678**
Mr Tim Hosking	279,913	-	-	2,142	(40,000)	-	**242,055**
Mr Lino Barro	-	-	100,000	-	(100,000)	-	**-**
Mr Edward Munks *(appointed 1 January 2011)*	119,913	-	30,000	4,284	-	-	**154,197**
Total key management personnel	15,969,779	-	4,580,000	464,720	(3,510,000)	-	**17,504,499**

	Balance as at 1 July 2009	Received as Remuneration	Options Exercised	Ordinary Shares Purchased	Ordinary Shares Sold	Other	Balance as at 30 June 2010
Executive Directors							
Mr Robert Hosking	12,388,820	-	500,000	-	(811,500)	25,000	12,102,320
Mr Mark Smith	2,405,000	-	750,000	-	(600,000)	17,037	2,572,037
Non-Executive Directors							
Mr Geoff Atkins	427,500	-	-	-	(10,000)	-	417,500
Mr Stephen Power	300,000	-	-	-	-	-	300,000
Other key management personnel							
Mr Scott Hosking	160,979	-	100,000	124,840	(218,469)	-	167,350
Mr Tim Hosking	149,943	-	300,000	38,070	(208,100)	-	279,913
Mr Lino Barro	-	-	200,000	-	(200,000)	-	-
Mr David Ormerod	25,000	-	150,000	-	(175,000)	-	-
Mr Jorg Bein	12,000	-	200,000	1,492	(210,746)	-	2,746
Total key management personnel	15,869,242	-	2,200,000	164,402	(2,433,815)	42,037	15,841,866

(e) Loans to Directors and Other Key Management Personnel

There were no loans to Directors or other key management personnel during the financial year or previous financial year.

(f) Other Transactions with Directors and Other Key Management Personnel

Refer to Note 29 for other transactions with Directors and other key management personnel during the financial year.

Note 29. Related Party Transactions

Transactions between related parties are on normal commercial terms and conditions no more favourable than those available to other parties, unless otherwise stated.

(a) Parent Company

The ultimate Parent Company within the Group is Karoon Gas Australia Ltd.

(b) Subsidiaries

Interests in subsidiaries are set out in Note 21.

During the financial year, the Group provided accounting, administrative and technical services to subsidiaries at cost. This allocation was based on costs recharged on a relevant time allocation of employees and consultants and associated office charges.

Other transactions that occurred were advancement of intercompany loans at Nil% interest rate (2010: Nil%) and no fixed term for repayment as it was used for funding the intercompany operations and therefore will not be repaid within twelve months. Loans are unsecured and are repayable in cash.

The above transactions are eliminated on consolidation.

Parent Company guarantees provided to third parties guaranteeing a subsidiary's performance under joint venture operating agreements are set out in Note 23.

(c) Directors and Other Key Management Personnel

Disclosures relating to Directors and other key management personnel are set out in the Directors' Report and Note 28.

Apart from the details disclosed in this note, no Director or other key management personnel has entered into a material contract with the Group since the end of the previous financial year and there were no material contracts involving Directors' or other key management personnel interests subsisting as at 30 June 2011 other than as stated in the Directors' Report (Remuneration Report, Section C).

Note 29. Related Party Transactions (continued)

(d) Superannuation Contributions

During the financial year, the Group contributed to accumulation type benefit funds administered by external fund managers or an employee's self-managed superannuation fund. The funds cover all Australian domiciled employees and Directors of the Company. The current contribution rate is 9.0% p.a. (2010: 9.0% p.a.) of employee cash remuneration. Contributions to superannuation funds, on behalf of Directors and employees, during the financial year by the Group amounted to $306,565 (2010: $284,771).

(e) Other Related Party Transactions Within the Group

During the financial year, Mr Stephen Power, a Director, had an interest in Napier Legal Pty Ltd which provided legal services to the Group. The value of transactions during the financial year in the Group was $593,034 (2010: $376,960).

During the financial year and the previous financial year, Mr Mark Smith, a Director, had an interest in IERS (Australia) Pty Ltd, which has an ongoing agreement with the Group to provide geophysical fault seal analysis software. This contract had been negotiated at commercial terms and does not include monetary compensation. Instead, the Group provides testing and ongoing development of the geophysical fault seal analysis software in return for its use.

	Company	
	2011	2010
	$	$

Note 30. Parent Company Financial Information

(a) Summary Financial Information

The individual financial statements for Karoon Gas Australia Ltd show the following aggregate amounts:

	2011 $	2010 $
Statement of financial position		
Current assets	**270,071,493**	75,836,959
Non-current assets	**348,672,866**	283,387,194
Total assets	**618,744,359**	359,224,153
Current liabilities	**765,990**	750,024
Non-current liabilities	**99,486**	60,738
Total liabilities	**865,476**	810,762
Net assets	**617,878,883**	358,413,391
Equity		
Issued capital	**664,894,335**	381,147,212
Accumulated losses	**(65,364,034)**	(36,012,928)
Share-based payments reserve	**18,348,582**	13,279,107
Total equity	**617,878,883**	358,413,391
Loss for financial year	**(29,351,106)**	(14,267,261)
Total comprehensive loss for financial year	**(29,351,106)**	(14,267,261)

	Consolidated	
	2011	2010
	$	$
(b) Contingent Liabilities of Parent Company		
(i) Bank guarantees were provided in respect of operating lease rental agreements at Melbourne and Mount Martha for the Company and a subsidiary. These guarantees may give rise to liabilities in the Parent Company if obligations are not met under these guarantees. The bank guarantees given to lessors are fully funded by way of payment of security deposit (refer Note 13).	**359,509**	70,307
(ii) Performance guarantees (via letters of credit) were provided to Peru Petro SA for Block Z-38 and Block 144 by the Company for second and third period work commitments (2010: first and second period work commitments). The Directors are of the opinion that the work commitments will be satisfied under both Blocks. The letters of credit are fully funded by way of payment of security deposit (refer Note 13), which will be released once the work commitments are met.	**10,011,647**	4,517,490
(iii) In the previous financial year, a performance guarantee (via a letter of credit) was provided to a third party supplier by the Parent Company for exploration work undertaken in Peru. The letter of credit was fully funded by way of payment of a security deposit (refer Note 13), and was released once the obligation under the contract was satisfied.	**-**	293,324
(iv) The Company's present intention is to provide the necessary financial support for all Australian incorporated subsidiaries, whilst they remain wholly owned subsidiaries, as is necessary for each company to pay all debts as and when they become due.		

(c) Guarantees Entered into by Parent Company

Parent Company guarantees provided to third parties guaranteeing a subsidiary's performance under joint venture operating agreements are set out in Note 23.

A bank guarantee provided by the Parent Company to a third party, guaranteeing a subsidiary's performance under an operating lease rental agreement, is set out in Note 24.

Note 31. Subsequent Events

Since 30 June 2011, the following material events have occurred:

(a) Santos Basin Drilling Program

On 24 August 2011, Karoon Petróleo & Gas Ltda, a wholly owned subsidiary of the Company, executed drilling agreements with Dolphin Drilling Ltd for the Blackford Dolphin semi-submersible drilling rig.

The drilling contract covers the use of the Blackford Dolphin rig for the drilling of three exploration wells in the Group's five wholly owned blocks in the Santos Basin, expected to commence in the first half of calendar year 2012.

(b) Browse Basin Drilling Program

On 8 September 2011, ConocoPhillips, as the Operator of the jointly held WA-314-P, WA-315-P and WA-398-P Browse Basin permits, signed a drilling contract with Sedco Forex International Inc. for the 'Transocean Legend' semi-submersible drilling rig. The drilling rig will be used to complete the planned phase-2 Browse Basin exploration drilling program in the WA-314-P, WA-315-P and WA-398-P Browse Basin permits.

The contract comprises five firm wells (fulfilling permit Government work commitments) with options for three additional wells. Drilling is expected to commence during the fourth quarter of calendar year 2011.

The Annual Report was authorised for issue by the Board of Directors on 13 September 2011. The Board of Directors has the power to amend and reissue the financial statements and notes.

DIRECTORS' DECLARATION

In the Directors' opinion:

(a) the financial statements and notes, set out on pages 33 to 80, are in accordance with the *Corporations Act 2001*, including:

  (i) complying with relevant Australian Accounting Standards and the *Corporations Regulations 2001*; and

  (ii) giving a true and fair view of the Group's financial position as at 30 June 2011 and of its performance for the financial year ended on that date; and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Note 1(a) confirms that the financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

The Directors have been given the declarations by the Executive Chairman and Chief Financial Officer required by Section 295A of the *Corporations Act 2001*.

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

On behalf of the Directors:

Mr Robert Hosking
Executive Chairman

13 September 2011
Melbourne

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Independent Auditor's Report to the Members of Karoon Gas Australia Ltd

Report on the Financial Report

We have audited the accompanying financial report of Karoon Gas Australia Ltd ('the Company'), which comprises the consolidated statement of financial position as at 30 June 2011, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and consolidated statement of cash flows for the financial year ended on that date, a summary of significant accounting policies, other explanatory notes and the Directors' Declaration for the Group. The Group comprises the Company and the subsidiaries it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The Directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the Directors also state, in accordance with Accounting Standard *AASB 101 Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the financial report.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

Auditor's Opinion

In our opinion:

(a) the financial report of Karoon Gas Australia Ltd is in accordance with the *Corporations Act 2001*, including:

  (i) giving a true and fair view of the Group's financial position as at 30 June 2011 and of their performance for the year ended on that date; and

  (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*; and

(b) the financial report and notes also complies with International Financial Reporting Standards as disclosed in Note 1.

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 22 to 29 of the Directors' Report for the year ended 30 June 2011. The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with Section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion, the Remuneration Report of Karoon Gas Australia Ltd for the financial year ended 30 June 2011, complies with Section 300A of the *Corporations Act 2001*.

Matters Relating to the Electronic Presentation of the Audited Financial Report

This auditor's report relates to the Financial Report and Remuneration Report of the Company for the year ended 30 June 2011 included on the Company's website. The Company's directors are responsible for the integrity of the Company's website. We have not been engaged to report on the integrity of this website. The auditor's report refers only to the Financial Report and Remuneration Report named above. It does not provide an opinion on any other information which may have been hyperlinked to/from the Financial Report or the Remuneration Report. If users of this report are concerned with the inherent risks arising from electronic data communications they are advised to refer to the hard copy of the audited Financial Report and Remuneration Report to confirm the information included in the audited financial report and remuneration report presented on this web site.

PricewaterhouseCoopers

Charles Christie
Partner

Melbourne
13 September 2011

STATEMENT OF CORPORATE GOVERNANCE

The second edition of the revised ASX Corporate Governance Council Principles and Recommendations published during August 2007 (revised Corporate Governance Council Principles) established the framework for how the Board of Directors oversees the Company and performs its functions on behalf of shareholders. The Company's objective is to achieve best practice in corporate governance and the Company's Directors, senior management and employees are committed to achieving this objective.

This statement summarises the Company's key corporate governance principles and practices.

Role of the Board of Directors

The roles and responsibilities of the Board of Directors are to oversee and direct the senior management of the Company by:

- defining and monitoring the strategic direction of the Company;
- defining policies and procedures to ensure the Company operates within the legal, ethical and social requirements of its environment;
- establishing control and accountability systems within the Group's operations to conform to the legal requirements and the expectations of shareholders and other stakeholders;
- defining and monitoring the management of an effective risk assessment strategy;
- securing funds to develop the Company's assets;
- driving Company performance;
- from time to time, reviewing and monitoring management and Company performance;
- appointing and appraising the Executive Chairman and any other Executive Director;
- ensuring there are adequate plans and procedures for succession planning;
- reviewing and approving the remuneration of the Executive Chairman, any other Executive Director and senior management;
- approving and monitoring the progress of major capital expenditure, capital management, acquisitions and divestitures; and
- approving and monitoring financial and other reporting.

The Company's Board Charter can be found on the Company's website at www.karoongas.com.au.

Composition of the Board of Directors

The Board of Directors is constituted by five Directors. The skills, experience and expertise relevant to the position of each Director who is in office at the date of the Annual Report and their term of office are detailed in the Directors' Report.

The Non-Executive Directors of the Company are Mr Geoff Atkins, Mr Clark Davey and Mr Stephen Power. Mr Geoff Atkins and Mr Clark Davey are Independent Directors. The Company considers Mr Stephen Power to be a Non-Independent Director, due to Napier Legal Pty Ltd, a law firm in which Mr Power has an interest, providing legal services to the Company. These services are provided by Napier Legal Pty Ltd on normal commercial terms and conditions and at market rates.

Recommendation 2.1 of the revised Corporate Governance Council Principles provides that a majority of the Board of Directors should be Independent Directors. The Company does not currently comply with this Recommendation. The composition of the Board is reviewed on an ongoing basis having regard to the growth of the Company's business, with a view to appointing a majority of Independent Directors.

When determining the independent status of a Director, the revised Corporate Governance Principles state that the Board should consider whether the Director:

- is a substantial shareholder of the Company or an officer of, or otherwise associated directly with, a substantial shareholder of the Company;
- is employed, or has previously been employed in an executive capacity by the Company or another Group member, and there has not been a period of at least three years between ceasing such employment and serving on the Board;
- has within the last three years been a principal of a material professional adviser or a material consultant to the Company or another Group member, or an employee materially associated with the service provided; and
- is a material supplier or customer of the Company or other Group member, or an officer of or otherwise associated directly or indirectly with a material supplier or customer who has a material contractual relationship with the Company or another Group member other than as a Director.

Recommendation 2.2 of the revised Corporate Governance Council Principles provides that the Chairman should be an Independent Director. Also, Recommendation 2.3 of the revised Corporate Governance Council Principles provides that the roles of the Chairman and the Chief Executive Officer should not be exercised by the same individual. The Company's Chairman also acts as its Chief Executive Officer and was also its founding Director and is one of the Company's largest shareholders. Given the stage of the Company's growth, the Board of Directors considers it acceptable for the Chairman to be an Executive Director and not independent.

Meeting Schedule

The Board of Directors meets at least every two months with additional committee meetings, if and when required, to discuss specific matters.

Advice to Directors

Subject to the approval of the Board of Directors, an individual Director may engage an independent professional adviser at the expense of the Company in appropriate circumstances.

Board Committees

The Board of Directors may establish appropriate committees to assist in its roles and responsibilities at appropriate points in the Company's growth.

The Board of Directors has established an Audit Committee, a Remuneration Committee and a Nomination Committee.

Audit Committee

The role of the Audit Committee is to advise on the establishment and maintenance of a framework of internal control and the appropriate ethical standards for the financial management of the Group. The Company has formally adopted an Audit Committee Charter. A copy of the Audit Committee Charter can be found on the Company's website at www.karoongas.com.au.

The Audit Committee also reviews the quality and reliability of financial information prepared for use by the Board of Directors in determining policies or for inclusion in financial statements.

The Audit Committee consists of:

Mr Geoff Atkins (Chairman)

Mr Clark Davey

Mr Stephen Power

The record of attendance for each of the members of the Audit Committee is set out in the Directors' Report of the Annual Report.

Recommendation 4.2 of the revised Corporate Governance Council Principles recommends that the Audit Committee be structured so that it:

- consists only of Non-Executive Directors;
- consists of a majority of Independent Directors;
- is chaired by an Independent Chairman, who is not Chairman of the Board of Directors; and
- has at least three members.

The recommendation is to ensure that the Audit Committee is of sufficient size, independence and technical expertise to discharge its mandate effectively. The Company has fully complied with Recommendation 4.2. The Audit Committee met four times during the financial year.

The responsibilities of the Audit Committee include:

- reviewing the integrity of the Company's financial reporting and overseeing the independence of external auditors;
- liaising with external auditors and ensuring that the annual statutory audits and half year auditor reviews are conducted in an effective manner;
- reviewing internal controls and recommending improvements;
- reviewing the half year financial report prior to lodgement of this document with the ASX, and any significant adjustments required as a result of the review;
- reviewing the draft annual financial report and the independent auditor's report and making the necessary recommendations to the Board of Directors for approval of the annual financial report;
- reviewing treasury recommendations and making necessary recommendations to the Board of Directors for approval; and
- reviewing and reporting on any special reviews deemed necessary by the Board of Directors.

The Audit Committee reports to the Board of Directors after each Committee Meeting and minutes of meetings are provided to all Directors.

Nomination Committee

The role of the Nomination Committee is to provide for a formal and transparent process for the selection, appointment and re-appointment of Directors. The Company has formally adopted a Nomination Committee Charter. A copy of the Nomination Committee Charter can be found on the Company's website at www.karoongas.com.au.

The Nomination Committee consists of:

Mr Clark Davey (Chairman)

Mr Geoff Atkins

Mr Robert Hosking

Recommendation 2.4 of the revised Corporate Governance Council Principles recommends that the Nomination Committee be structured so that it:

- consists of a majority of Independent Directors;
- is chaired by an Independent Chairman, who is not Chairman of the Board of Directors; and
- has at least three members.

The Company fully complies with Recommendation 2.4. However, the Nomination Committee was established after the end of the financial year. Prior to the Nomination Committee being formally established, the Board of Directors considered that the same efficiencies that may be derived from a Nomination Committee with respect to a larger Board may not, in the current circumstances, be derived from a formal Nomination Committee structure. However, the Board of Directors had processes in place which addressed the issues that would otherwise be considered by a Nomination Committee.

The Company's Constitution provides that, at each Annual General Meeting of the shareholders, one third of the Directors (excluding the Managing Director) must resign, with Directors resigning by rotation based on the date of their appointment. Directors resigning by rotation may offer themselves for re-election. This procedure ensures that no Director can serve for more than three years without being re-elected.

Mr Clark Davey was appointed during the financial year. The Board of Directors has adopted a Selection and Appointment of Directors Policy which can be found on the Company's website.

Remuneration Committee

The Remuneration Committee is responsible for the review of and recommendation to the Board of Directors on:

- the Company's recruitment, retention and termination policies and procedures for senior executives;
- senior executives' remuneration and incentives;
- superannuation arrangements; and
- the remuneration framework for Directors.

The Company's remuneration policy is designed to ensure that:

- remuneration is kept competitive in order to attract and retain talented and motivated employees and Directors to Karoon;
- there is a clear relationship between performance, responsibility and remuneration; and
- a performance evaluation process is created to monitor the Board of Directors and senior executives.

The Remuneration Committee consists of:

Mr Geoff Atkins (Chairman)

Mr Clark Davey

Mr Stephen Power

The record of attendance for each of the members of the Remuneration Committee is set out in the Directors' Report of the Annual Report.

Recommendation 8.2 of the revised Corporate Governance Council Principles recommends that the Remuneration Committee be structured so that it:

- consists of a majority of Independent Directors;
- is chaired by an Independent Director; and
- has at least three members.

The Company fully complies with Recommendation 8.2.

A copy of the Remuneration Committee Charter can be found on the Company's website at www.karoongas.com.au.

Remuneration Policy

As an overall policy, the Company will remunerate in such a way that it motivates Directors and employees to pursue the long term growth and success of the Company within an appropriate control framework that demonstrates a clear relationship between key executive performance and remuneration. The Remuneration Committee is responsible for executive remuneration and making recommendations to the Board of Directors.

Executive remuneration is set by the Board of Directors and may contain salary, bonuses and ESOP options.

Non-Executive Directors are remunerated by way of Directors' fees in the form of cash and superannuation contribution at market levels, as well as non-performance related share option incentives.

The aggregate Directors' fee pool to Non-Executive Directors is set and may not be increased without prior approval of the shareholders at a general meeting.

Options over unissued ordinary shares of the Company issued to Directors are approved on a case-by-case basis by shareholders at relevant general meetings.

The Company has a policy restricting recipients of ESOP and other share options from:

- dealing at any time in financial products such as options, warrants, futures or other financial products issued over the Company's securities by third parties such as banks and other institutions. An exception may apply where the Company's securities form a component of a listed portfolio or index product; or
- entering into transactions in products associated with the Company's securities which operate to limit the economic risk of their security holding in the Company over unvested entitlements (including hedging arrangements).

These restrictions are set out in the Company's Share Trading Policy which can be found on the Company's website at www.karoongas.com.au.

The Company has not established any schemes for retirement benefits, other than superannuation, for Non-Executive Directors.

Further information on the remuneration of the Directors and other key management personnel can be found in the Remuneration Report section of the Directors' Report.

Performance Review

Recommendation 2.5 of the revised Corporate Governance Council Principles provides that companies should disclose the process for evaluating the performance of the Board of Directors, its committees and individual Directors.

During the financial year, performance evaluation of the Executive Directors was undertaken in accordance with the Board Performance Review Policy and submitted to the Remuneration Committee. Non-Executive Directors did not receive a formal evaluation. Due to the nature and stage of the Company's operations and its evolution, the Board of Directors was of the view that a formal performance review of the Non-Executive Directors was not necessary.

The Board Performance Review Policy for senior executives and the Board of Directors is available on the Company's website at www.karoongas.com.au.

Management Performance Review

Recommendation 1.2 of the revised Corporate Governance Council Principles provides that the performance of senior executives should be reviewed regularly against appropriate measures.

Performance evaluation for senior executives has taken place during the financial year.

Role of the Company Secretary

All Directors have access to the Company Secretary and the appointment and removal of the Company Secretary is a matter for decision by the Board of Directors as a whole.

The Company Secretary is accountable to the Board of Directors, through the Chairman, on all corporate governance matters.

The Company Secretary supports the effectiveness of the Board of Directors by monitoring compliance with Board policy and procedures and coordinating the completion and despatch of the Board papers.

External Auditors

Recommendation 4.4 of the revised Corporate Governance Council Principles provides that the Company should make publicly available information on procedures for the selection and appointment of the external auditor and the rotation of external audit engagement partners.

The Company appointed the current external auditors, PricewaterhouseCoopers, during the financial year ended 30 June 2009.

The Company has prepared a Selection and Appointment of External Auditor Policy, whereby the Company reviews every three years and assesses performance and potentially rotates the external auditor. The External Auditor Selection Policy is available on the Company's website at www.karoongas.com.au

Ethical Standards, Compliance with Obligations and Responsible Decision Making

The Directors, officers, employees and consultants are required to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of the Group. The Company also strives to comply with legal and other obligations to stakeholders.

Recommendation 3.1 of the revised Corporate Governance Council Principles provides that the Company should establish a code of conduct. The Company has developed a Code of Conduct for the Board of Directors, senior management and employees of the Company. The Company's Code of Conduct can be found on the Company's website at www.karoongas.com.au. The Code includes:

- the practices necessary to maintain confidence in the Company's integrity;
- the practices necessary to take into account their legal obligations and the reasonable expectations of stakeholders; and
- the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

Diversity

The Board recognises the importance of diversity and has adopted a Diversity Policy in accordance with Recommendation 3.2 of the revised Corporate Governance Council Principles. The Company proposes to introduce appropriate measures to ensure the policy is implemented properly. The Company's Diversity Policy can be found on the Company's website at www.karoongas.com.au.

Fair Dealings and Related Party Transactions

A Director, or entities in which a Director has a significant interest and/or influence, who enters into a transaction with the Company must make full disclosure of all material elements of the transaction to the Chairman, or, if the Director involved is the Chairman, to the Board of Directors.

In addition, contracts with Directors, or entities in which Directors have a significant interest and/or influence, must be approved by the Audit Committee in advance of committing the Company to:

- contracts for the supply of goods and/or services which extend beyond one year, or where the total value of goods and/or services supplied under the contract will, in any one year, exceed $25,000;
- all agreements to lease and/or leases of property; and
- all agreements for acquisition or disposal of property, except by way of public auction.

Any Director who is a member of the Audit Committee and who has a significant interest and/or influence in relation to a contract to be approved by the Audit Committee must absent themselves from the meeting and not participate in any vote to approve such contract.

Policy and Procedure for Share Trading

Directors, officers, employees and consultants are prohibited from dealing in securities of the Company if they are in possession of information concerning the Company which, if made public, a reasonable person would expect to have a material impact on the price or value of the Company's securities ('insider information').

Directors, officers, key management personnel and other designated persons are prohibited from dealing in securities of the Company during any embargo period declared by the Chairman or Company Secretary. Embargo periods include the period of two weeks prior to the release of the Company's half year results and final results to the ASX and the period from the close of trading 10 days before the Company's Annual General Meeting.

These restrictions in dealing in securities of the Company are subject to discretion exercised by the Chairman in exceptional circumstances.

Prior to dealing in securities of the Company, Directors, officers, key management personnel and other designated persons must:

- seek written clearance from the Chairman or Company Secretary of the proposed dealing to ensure that there is not any imminent ASX announcement that contains price sensitive information; and
- confirm to the Chairman or Company Secretary that he or she is not aware of any insider information that has not been released to the ASX.

Directors, officers, key management personnel and other designated persons must advise the Company Secretary of any dealing in securities of the Company within two days of such dealing.

The Company's Share Trading Policy can be found on the Company's website at www.karoongas.com.au.

Environment

The Company has a Health, Safety and Environment Policy and is committed to conducting all its activities in an environmentally responsible manner.

The Company's Health, Safety and Environment Policy can be found on the Company's website at www.karoongas.com.au.

Disclosure of Information

The Company aims to provide honest and open disclosure of information in dealing with stakeholders, subject to appropriate commercial considerations associated with competitive and sensitive information.

The Company has developed a Continuous Disclosure Policy to ensure compliance by the Company with the Corporations Act 2001 and the ASX Listing Rule obligations in relation to disclosure of information to the market and to ensure accountability at a senior management level for that compliance.

The Company's Continuous Disclosure Policy can be found at www.karoongas.com.au.

The Role of Shareholders

The Board of Directors aims to ensure that all shareholders are informed of all major developments affecting the Company's state of affairs in accordance with its legal obligations. Information is communicated to shareholders as follows:

- the Annual Report is distributed to any shareholders who request a copy. The Board of Directors ensures that the Annual Report includes relevant information about the operations of the Group during the relevant financial year, changes in the state of affairs of the Group and other disclosures required by the *Corporations Act 2001*;
- the half year financial report, prepared in accordance with the requirements of the *Corporations Act 2001*, is subject to an external auditor's review. The half year financial report is sent to any shareholder who requests a copy;
- proposed major changes in the Company which may impact on share ownership rights are submitted to a vote of shareholders; and
- the Company posts all reports, ASX and media releases and copies of significant presentations on the Company's website at www.karoongas.com.au.

In addition, news announcements and other information are sent by email to all persons who have requested their details be added to the Company's electronic mailing list. If requested, the Company, where appropriate, will provide general information by email, facsimile or post.

The Company will ensure that the Annual General Meeting is held in a manner that enables as many shareholders as possible to attend and encourages effective participation by shareholders at the Annual General Meeting.

The Company will arrange to have its external auditor attend the Company's Annual General Meeting and be available to answer shareholder questions concerning the conduct of the audit, preparation and content of the Independent Auditor's Report.

The Chairman of the Annual General Meeting will allow a reasonable opportunity for shareholders to ask questions about the Company's performance and operations and also ask questions of the external auditor concerning the conduct of the audit, preparation and content of the Independent Auditor's Report.

Risk Assessment and Management

Recommendation 7.1 of the revised Corporate Governance Council Principles provides that companies should establish policies for the oversight and management of material business risks and disclose a summary of those policies. The Board of Directors has overall responsibility for monitoring compliance and oversight of these policies along with ensuring that they are efficient and effective.

Currently, as part of the Group's strategy to implement an integrated framework of control, the Board of Directors continually identifies and monitors the key business and financial risks that could jeopardise the Group achieving its objectives. The Board of Directors has and continues to develop appropriate controls to effectively manage those risks. A summary of the Company's policies for the oversight and management of material business risks follows:

- financial controls are set in place by the use of an authority matrix, general purchasing principles and approvals procedures. All expenditure is closely monitored by the Audit Committee on behalf of the Board of Directors and reported on a quarterly basis. The Chairman of the Audit Committee also works closely with the Company's finance personnel prior to Board meetings in order to understand financial risks and report such risks to the Board of Directors. Management accounts are prepared regularly for the Board of Directors to ensure information congruence between management and the Board of Directors;
- the Company offsets the risk of operational failures using appropriate insurance, with covers for third party liability, well control, day-to-day office and business insurance and operator's extra expense;
- the Company protects its employees through the adoption of a Health, Safety and Environment Policy and travel insurance for periods where employees are travelling on business, along with membership to emergency assistance and management for an employee overseas; and
- operational reporting is submitted to the Board of Directors at every Board meeting to ensure decisions are made in an efficient and effective manner. Reports include reviews of current assets, potential acquisitions and general operational issues and/or opportunities.

Management Accountability

In compliance with Recommendation 7.3, the Board of Directors encourages senior management level accountability for the Company's Annual Report by requiring the Executive Chairman and Chief Financial Officer to state in writing to the Board of Directors that:

- the Company's Annual Report presents a true and fair view, in all material respects, of the Company's financial condition and operational results and is in accordance with relevant Australian Accounting Standards; and
- the Annual Report is compiled in accordance with best practice and is properly monitored using the Audit Committee and the external auditors to ensure a sound system of risk management and control.

Recommendation 7.2 of the revised Corporate Governance Council Principles provides that the Board of Directors should require management to design and implement the risk management and internal control system to manage the Company's material business risks and report to it on whether those risks are being managed effectively. Throughout the financial year, the Company has reviewed and where required improved risk management and internal compliance and control systems following reports from senior management. The Company will continue to review and improve its risk management systems in conjunction with senior management over the coming financial period.

ADDITIONAL SECURITIES EXCHANGE INFORMATION

Additional information required by ASX Listing Rules and not disclosed elsewhere in the Annual Report is set out below. The information was applicable for the Company as at 5 September 2011.

Distribution of Shareholding

The number of shareholders ranked by size of holding is set out below:

Size of Holding	Number of Holders	Number of Ordinary Shares on Issue
Less than 1,000	3,267	1,560,853
1,001 to 5,000	4,292	11,531,147
5,001 to 10,000	1,210	8,816,347
10,001 to 100,000	1,169	29,059,518
More than 100,000	129	170,452,904
Total	10,067	221,420,769

There were 854 shareholders holding less than a marketable parcel of ordinary shares to the value of $500.

Substantial Shareholders

The number of ordinary shares held by substantial shareholders and their associates (who held 5% or more of total fully paid ordinary shares on issue), as disclosed in substantial holder notices given to the Company, is set out below:

	Fully Paid Ordinary Shares	
Shareholder	**Number Held**	**% of Issued Ordinary Shares**
Wellington Management Group, LLP and its related bodies corporate	28,374,885	12.81
Talbot Group Holdings Pty Ltd	26,714,728	12.07
Mr Robert Hosking	12,524,462	5.66
Total	67,614,075	30.54

Twenty Largest Shareholders

The names of the twenty largest shareholders of the Company's ordinary shares are listed below:

		Fully Paid Ordinary Shares	
Shareholder		**Number Held**	**% of Issued Ordinary Shares**
1	HSBC Custody Nominees (Australia) Limited	40,455,549	18.27
2	JP Morgan Nominees Australia Limited	20,454,723	9.24
3	Talbot Group Holdings Pty Ltd <Talbot Equities A/C>	15,317,043	6.92
4	Talbot Group Investments Pty Ltd	11,000,313	4.97
5	JP Morgan Nominees Australia Limited <Cash Income A/C>	10,316,985	4.66
6	Ropat Nominees Pty Ltd	9,210,022	4.16
7	Citicorp Nominees Pty Limited	8,936,643	4.04
8	National Nominees Limited	7,159,527	3.23
9	HSBC Custody Nominees (Australia) Limited-GSCO ECA	4,017,520	1.81
10	HSBC Custody Nominees (Australia) Limited - A/C 2	3,435,611	1.55
11	UBS Wealth Management Australia Nominees Pty Ltd	2,589,708	1.17
12	Mr Robert Hosking	2,250,000	1.02
13	Woodross Nominees Pty Ltd	1,782,156	0.80
14	Mr Mark Smith	1,500,000	0.68
15	HSBC Custody Nominees (Australia) Limited <3 A/C>	1,330,547	0.60
16	IERS (Australia) Pty Ltd <Smith Family Investment A/C>	1,271,500	0.57
17	AMP Life Limited	1,154,347	0.52
18	Mrs Mara Spong	1,127,888	0.51
19	Bond Street Custodians Ltd <Macquarie Smaller Co's A/C>	972,000	0.44
20	Rose Burton Pty Ltd	796,692	0.36
Total		145,078,774	65.52

Unlisted Equity Securities: Options

The following options over unissued ordinary shares of the Company were unquoted:

	Number of Holders	Number of Unlisted Options on Issue
Options issued pursuant to Company's ESOP	37	3,775,000
Other share options issued	3	1,500,000
Total	40	5,275,000

Voting Rights

(a) Ordinary Shares, Fully Paid

Voting rights of shareholders are governed by the Company's Constitution. In summary, on a show of hands every holder of ordinary shares present at a meeting in person or by proxy is entitled to one vote, and upon a poll each such attending shareholder is entitled to one vote for every fully paid ordinary share held.

(b) Unlisted Options

No voting rights.

Other Information

The Company was incorporated as a public company on 11 November 2003.

The Company was admitted to the ASX official list during June 2004 and quotation of its ordinary shares commenced on 8 June 2004.

The register of securities is held at Computershare Investor Services Pty Limited, Yarra Falls, 452 Johnston Street, Abbotsford VIC 3067 Australia. Investor enquiries can be made via telephone on 1300 850 505 (within Australia).

Schedule of Interests

Exploration Permit	Basin	% Interest Held
AC/P8	Bonaparte, Australia	66.67
WA-314-P	Browse, Australia	90.00*^
WA-315-P	Browse, Australia	40.00*
WA-398-P	Browse, Australia	40.00
Block 1037	Santos, Brazil	100.00
Block 1101	Santos, Brazil	100.00
Block 1102	Santos, Brazil	100.00
Block 1165	Santos, Brazil	100.00
Block 1166	Santos, Brazil	100.00
Block 1352	Santos, Brazil	20.00†
Block 144	Maranon, Peru	100.00
Block Z-38	Tumbes, Peru	75.00#

* 1.5% ORR for first five years of production, going to 2% thereafter.
† The Group's 20.00% Block equity interest is subject to satisfying farm-in obligations and obtaining regulatory approvals in Brazil, including from the Brazilian Petroleum Agency.
^ The Group's 90.00% equity interest is subject to regulatory approval.
# The Group's 75.00% Block equity interest is subject to completion of farm-in obligations.

GLOSSARY OF TERMS

Term	Definition
2D seismic	Two-dimensional seismic.
3D seismic	Three-dimensional seismic.
$ or cents	Units of Australian currency.
AASB	Australian Accounting Standards Board.
ANP	Agencia Nacional do Petróleo.
API	American Petroleum Institute's inverted scale for denoting the 'lightness' or 'heaviness' of crude oils and other liquidhydrocarbons.
appraisal well	A well drilled to confirm the size or quality of a hydrocarbon discovery.
associated gas	Natural gas found in association with oil, dissolved either in the oil or as a cap of free gas above the oil.
ASX	Australian Securities Exchange or ASX Limited (ACN 008 624 691).
ATO	Australian Taxation Office.
AUD	Australian currency.
barrel or bbl	Barrel of oil, inclusive of condensate. A quantity of 42 United States gallons; equivalent to approximately 159 litres.
basin	An ancient natural depression on the Earth's surface in which sediments, eroded from higher surrounding ground levels, accumulated and were preserved.
BCF	Billion cubic feet (1,000,000,000 cubic feet); equivalent to approximately 28.3 million cubic metres.
block	A licence or concession area. It may be almost any size or shape, although usually part of a grid pattern.
boe	Barrel of oil equivalent. The factor used to convert gas to oil equivalent is based upon an approximate energy value of 6,000 standard cubic feet per barrel and not price equivalence at the time.
BTU	British Thermal Unit. The unit of measurement of the quantity of heat required to raise the temperature of one pound of water by one degree fahrenheit, equivalent to 1055.056 joules.
Company or Parent Company	Karoon Gas Australia Ltd.
condensate	Hydrocarbons which are predominantly pentane and heavier compounds which are in a gas phase in the reservoir and which separate out from natural gas at the well head and condense to liquid at lower pressures and temperatures.
ConocoPhillips	ConocoPhillips (Browse Basin) Pty Ltd.
contingent resources	Quantities of hydrocarbons which are estimated, on a given date, to be potentially recoverable from known accumulations, but which are not yet currently considered to be commercially recoverable for lack of market or suitable price.
CSEM	Controlled Source Electro Magnetic (survey).
DSEWPaC	Department of Sustainability, Environment, Water, Population and Communities.
Director	A Director of Karoon Gas Australia Ltd.
DHI	Direct hydrocarbon indicator
discovery well	The first successful well on a new prospect.
DST	Drill stem test.
economically recoverable reserves	The estimated quantity of hydrocarbons in an area of interest that can be expected to be profitably extracted, processed and sold under current and foreseeable economic conditions.
EDT	Eastern Daylight Time, being the time in Melbourne, Victoria.

Term	Definition
EIA	Environmental Impact Assessment. A report on the study of the effect of proposed works on the local people and environment.
ESOP	The Karoon Gas Australia Employee Share Option Plan.
exploration	The process of identifying, discovering and testing prospective hydrocarbon regions and structures, mainly by interpreting regional and specific geochemical, geological, geophysical survey data and drilling.
farm-in and farm-out	A commercial agreement in which an incoming joint venture participant (the 'farmee') earns an interest in an exploration permit by funding a proportion of exploration and evaluation expenditures, while the participant owning the interest in the exploration permit (the 'farmor') pays a reduced contribution. The interest received by a farmee is a farm-in while the interest transferred by the farmor is a farm-out.
FBT	Fringe Benefits Tax in Australia.
FID	Final Investment Decision.
field	An area consisting of a single reservoir or multiple reservoirs all grouped on or related to the same individual geological structural feature or stratigraphic condition. The field name refers to the surface area although it may refer to both the surface and underground productive formation.
financial year	Financial year ended 30 June 2011.
GST	Goods and Services Tax in Australia.
hydrocarbon	A compound of the elements hydrogen and carbon, in either liquid or gaseous form. Natural gas and petroleum are mixtures of hydrocarbons.
IASB	International Accounting Standards Board.
Karoon or Group	Karoon Gas Australia Ltd and its subsidiaries.
lead	A potential hydrocarbon target which has been identified but requires further evaluation before it is drill ready, at which point it becomes a prospect.
LNG	Liquefied natural gas.
LPG	Liquid petroleum gas.
m	Metres.
market capitalisation	The product of a company's share price multiplied by the total number of ordinary shares issued by the company.
migration	Hydrocarbons are often found in formations other than those in which their organic source was deposited. This movement often covers considerable distances and is known as migration.
mm	Million.
mmbbls	Millions of barrels (1,000,000 barrels).
mmscf/d	Millions of standard cubic feet per day; equivalent to 28,317 cubic metres per day.
MMtpa	Million tonnes per annum. A common measurement of LNG facility production capacity.
Monte Carlo simulation	Where there is uncertainty in the variables used in the calculation of economically recoverable reserves, the ranges of possible values of each variable can be incorporated in a Monte Carlo simulation calculation to produce a range of probabilistic outcomes that reflect that uncertainty. The 'mean' is the expected outcome. The P10 (probability greater than 10%) is often used as the maximum case, the P50 (probability of 50%) the mid case and the P90 (probability greater than 90%) the minimum case.
mRT	Metres rotary table.
MAZ	Multi Azimuth Seismic Processing
NGER Act	*National Greenhouse and Energy Reporting Act 2007.*

Term	Definition
Operator	One joint venture participant that has been appointed to carry out all operations on behalf of all the joint venture participants.
ordinary shares	The ordinary shares in the capital of Karoon Gas Australia Ltd.
ORR	Over-riding royalty.
p.a.	Per annum.
permit	A hydrocarbon tenement, lease, licence, concession or Block.
Petrobras	Petróleo Brasileiro SA.
play	A trend within a prospective basin that has common geologic elements containing one or more fields, prospects or leads with common characteristics.
previous financial year	Financial year ended 30 June 2010.
prospect	A geological or geophysical anomaly that has been surveyed and defined, usually by seismic data, to the degree that its configuration is fairly well established, and on which further exploration such as drilling can be recommended.
prospectivity	Referring to the likelihood of finding commercial hydrocarbons.
prospective resource	The term used to describe undiscovered volumes in an exploration prospect yet to be drilled.
psia	Pounds per square inch absolute.
REAL	Brazilian currency.
recoverable gas	An estimated measure of the total amount of gas which could be brought to surface from a given reservoir. In a good quality reservoir this is usually in the order of 70-80% of the estimated gas-in-place.
reserves	Quantities of economically recoverable hydrocarbons estimated to be present within a trap.
reservoir	A porous and permeable rock formation to store and transmit fluids such as hydrocarbons and water.
rig	The equipment needed for drilling a well. It includes the onshore and offshore vehicles, mobile platforms or vessel on which the equipment is stored.
risk	Prospect risk or geologic risk is the assessed chance that the drilling of the prospect will be successful in finding significant volumes of hydrocarbons. The risk is calculated by multiplying the chance of success of each of the petroleum system elements involved in the prospect.
seismic survey	A type of geophysical survey where the travel times of artificially created seismic waves are measured as they are reflected in a near vertical plane back to the surface from subsurface boundaries. This data is typically used to determine the depths and form of stratigraphic units and in making subsurface structural contour maps and ultimately in delineating prospective structures.
spud	To start drilling a new well.
Talisman	Talisman Oil & Gas (Australia) Pty Limited.
TCF	Trillion cubic feet (1,000,000,000,000 cubic feet).
unrisked	A risk value has not been applied to an estimate of hydrocarbon volume either in place or recoverable.
USD	United States dollars.
WAZ	Wide Azimuth Seismic Data

CORPORATE DIRECTORY

Board of Directors

Mr Robert Hosking – Executive Chairman
Mr Mark Smith – Executive Director
Mr Geoff Atkins – Independent Non-Executive Director
Mr Clark Davey – Independent Non-Executive Director
Mr Stephen Power – Non-Executive Director

Company Secretary

Mr Scott Hosking

Audit Committee Members

Mr Geoff Atkins (Chairman of Committee)
Mr Clark Davey
Mr Stephen Power

Nomination Committee Members

Mr Clark Davey (Chairman of Committee)
Mr Geoff Atkins
Mr Robert Hosking

Remuneration Committee Members

Mr Geoff Atkins (Chairman of Committee)
Mr Clark Davey
Mr Stephen Power

Registered Office and Head Office

Office 7A, 34-38 Lochiel Avenue
Mount Martha VIC 3934
Australia

ACN 107 001 338
ABN 53 107 001 338
Telephone +61 3 5974 1044
Facsimile +61 3 5974 1644
Website www.karoongas.com.au
Email info@karoongas.com.au

External Auditor

PricewaterhouseCoopers Australia
Freshwater Place
2 Southbank Boulevard
Southbank VIC 3006
Australia

Telephone +61 3 8603 1000
Facsimile +61 3 8603 1999

Share Registrar

Computershare Investor Services Pty Limited
Yarra Falls
452 Johnston Street
Abbotsford VIC 3067
Australia

Telephone 1300 850 505 (within Australia)
+61 3 9415 5000 (outside Australia)
Facsimile +61 3 9473 2500
Website www.computershare.com

Securities Exchange Listing

The Company's ordinary shares are listed on the ASX.
The home exchange is Melbourne VIC.
ASX code KAR

Notice of Annual General Meeting

The Annual General Meeting of Karoon Gas Australia Ltd will be held at:

River Rooms 2 and 3 at the Crown Towers
Level 1, 8 Whiteman Street
Southbank VIC 3006

Time 11.00am EDT (registration opens at 10.00am EDT)
Date Wednesday 26 October 2011

Karoon
Gas Australia Ltd