Zeta Petroleum Limited

Report and Financial Statements

Period Ended 31 December 2006

ZETA PETROLEUM LIMITED

REPORT AND FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

Page:

GENERAL INFORMATION

Directors

J A Rutland (Chairman)
C C G Lewis (Chief Executive)
S P West
T W Osborne

Company Secretary

S P West

Registered Office

1 Berkeley Street
London
W1J 8DJ
United Kingdom

Company Number

5560854

Auditor

Ernst & Young LLP
1 More London Place
London
SE1 2AF
United Kingdom

REPORT OF THE DIRECTORS FOR THE PERIOD ENDED 31 DECEMBER 2006

The directors present their report together with the audited financial statements for the sixteen month period from incorporation to 31 December 2006.

Results and Dividends

The consolidated income statement is set out on page 7 and shows a loss for the period amounting to £1,562,000. The directors do not recommend the payment of a dividend.

Principal Activities and Review of Operations

The principal activities of the Group are oil and gas exploration, development and production.

The Company was incorporated and commenced business on 12 September 2005 and has its head office in London.

The Company acquired a 70% interest in eight onshore licences in northern Turkey in November 2005. These licences are collectively referred to as the Bartin and Sakarya licence areas and cover an area of approximately 3,800km^2.

During 2006 the Company raised £3,811,145 (net of expenses) through the issue of new ordinary shares to fund the work programme in Turkey and to develop new venture opportunities.

The Company re-entered an existing well on the Bartin licences in June/July 2006 at a cost of £766,255 and reprocessed existing seismic on the Bartin licences during the year at a cost of £89,845. In addition, geological and geophysical works were performed on the Sakarya licences during 2006 at a cost of £7,820.

In September 2006 the Company entered into an agreement with a third party whereby the Company has the right to acquire an interest of up to 50% in a partitioned area of the EIV-03 Zegujani licence in south west Romania. The cash cost to the Company of entering into this agreement was £76,620.

The subsidiary undertakings principally affecting the profits or net assets of the Group are listed in Note 12 to the consolidated financial statements.

Principal Risks and Uncertainties

As an exploration company in the oil and gas industry the Company operates in an inherently risky sector and faces a large number of risks including:

Discovery Risk:	Risk that no economically producible oil or gas will be discovered or found to be present in the Company's licence areas.
Capital Intensive Business:	The drilling of wells to discover whether there is oil or gas is a highly capital intensive business and will require the Company to raise the capital in the future.
Natural Gas Price:	The Company's asset value and the economic viability of its exploration projects depend on the price of natural gas and the Company's ability to raise funds in the future is likely to be sensitive to the price of natural gas.
Environmental Regulations:	The Company's operations are subject to the environmental risks inherent in the oil and gas industry.

Post Balance Sheet Events

Post balance sheet events are disclosed in Note 23 to the consolidated financial statements.

REPORT OF THE DIRECTORS FOR THE PERIOD ENDED 31 DECEMBER 2006

Share Capital

Details of the Company's authorised and issued share capital as at 31 December 2006 and of shares issued during the period are set out in Note 16 to the consolidated financial statements.

Policy and Practice on Payment of Creditors

It is the Company's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers, providing that all trading terms and conditions have been complied with.

Directors and Directors' Interests

The directors who held office at 31 December 2006 had the following interests in the ordinary shares of the Company according to the register of directors' interests:

	Class of share	Interest at end of year
C C G Lewis (appointed 12 September 2005)	Ordinary	553,200
S P West (appointed 12 September 2005)[1]	Ordinary	412,000
T W Osborne (appointed 31 March 2006)	Ordinary	-
J A Rutland (appointed 25 May 2006)	Ordinary	2,306

[1] S P West's interest is indirect as all the shares are owned by Cresthaven Investments Limited, a company in which S P West has an indirect beneficial interest.

According to the register of directors' interests, no rights to subscribe for shares in or debentures of Group companies were granted to any of the directors or their immediate families, or exercised by them, during the financial period except as indicated below:

	Number of options granted and balance at end of year	Exercise price £	Date from which exercisable	Expiry date
C C G Lewis	100,000	2.8736	50% - 29 March 2007 50% - 29 September 2007	29 March 2016
S P West	100,000	2.8736	50% - 29 March 2007 50% - 29 September 2007	29 March 2016
J A Rutland	27,840	2.8736	50% - 13 June 2007 50% - 13 December 2007	13 June 2016

Substantial Shareholders

The following parties had interests of greater than 3% of the issued share capital of the Company at 31 December 2006:

Substantial shareholder	Number of shares	% of issued ordinary share capital
GM Investment & Co Limited	699,952	28.86
C C G Lewis	553,200	22.80
Cresthaven Investments Limited[2]	412,000	16.99
S Pagel	348,000	14.35
WCI Overseas Oil & Gas LLC	191,400	7.89
AM2 (Bermuda) Limited	104,400	4.30

[2] Cresthaven Investments Limited is a company in which S P West has an indirect beneficial interest.

REPORT OF THE DIRECTORS FOR THE PERIOD ENDED 31 DECEMBER 2006

Statement of Directors' Responsibilities

The directors are responsible for preparing the consolidated and company financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards as adopted by the European Union.

The directors are required to prepare consolidated and company financial statements for each financial year which present fairly the financial position of the Group and Company, and the financial performance and cash flows of the Group and Company for the period. In preparing those financial statements the directors are required to:

- select suitable accounting policies in accordance with IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors* and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's and/or Company's financial position and performance; and
- state that the Group and Company have complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the consolidated and company financial statements comply with the Companies Act 1985 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Statement as to Disclosure of Information to Auditors

The directors who were members of the board at the time of approving the directors' report are listed on page 1. Having made inquiries of fellow directors and of the Company's auditors, each of these directors confirm that:

- to the best of each director's knowledge and belief, there is no information relevant to the preparation of their report of which the Company's auditors are unaware; and
- each director has taken all the steps a director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Company's auditors are aware of that information.

Political and Charitable Contributions

The Group made no political contributions or donations to United Kingdom charities during the period.

Auditors

Ernst and Young LLP were appointed auditors to the Company on 8 December 2006 and a resolution reappointing Ernst & Young LLP as auditors was passed at the Company's first annual general meeting on 22 March 2007.

By order of the Board

S P West
Director
11 May 2007

1 Berkeley Street
London W1J 8DJ
United Kingdom

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF ZETA PETROLEUM LIMITED

We have audited the financial statements of Zeta Petroleum Limited for the period ended 31 December 2006 which comprise the Consolidated Income Statement, the Consolidated and Company Balance Sheets, the Consolidated and Company Cash Flow Statements, the Consolidated and Company Statements of Changes in Equity and the related notes 1 to 23. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the consolidated and Company financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities on page 4.

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

We report to you our opinion as to whether the consolidated and Company financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether the information given in the directors' report is consistent with the financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies within it. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF ZETA PETROLEUM LIMITED

Opinion

In our opinion:

- the consolidated and Company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's and the Company's affairs as at 31 December 2006 and of the loss of the Group for the period then ended;
- the consolidated and Company financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the directors' report is consistent with the financial statements.

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
London
11 May 2007

CONSOLIDATED INCOME STATEMENT
FOR THE PERIOD ENDED 31 DECEMBER 2006

	Note	*12 September 2005 to 31 December 2006* Group £'000
Continuing operations		
Revenue	2	**1**
Gross profit		**1**
Exploration and evaluation expenses		**(877)**
Administrative expenses		**(786)**
Operating loss		**(1,662)**
Interest income		**100**
Loss for the period attributable to the equity holders		**(1,562)**
Loss per ordinary share – basic	9	93.15p

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE PERIOD ENDED 31 DECEMBER 2006

	12 September 2005 to 31 December 2006				
	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Retained Losses £'000	Total £'000
As at 12 September 2005	-	-	-	-	-
Issue of share capital	2	4,195	-	-	4,197
Transaction costs of issue of shares	-	(285)	-	-	(285)
Issue of share options	-	-	337	-	337
Loss for the period	-	-	-	(1,562)	(1,562)
At 31 December 2006	2	3,910	337	(1,562)	2,687

COMPANY STATEMENT OF CHANGES IN EQUITY
FOR THE PERIOD ENDED 31 DECEMBER 2006

	12 September 2005 to 31 December 2006				
	Issued Capital £'000	Share Premium £'000	Share Options Reserve £'000	Retained Losses £'000	Total £'000
As at 12 September 2005	-	-	-	-	-
Issue of share capital	2	4,195	-	-	4,197
Transaction costs of issue of shares	-	(285)	-	-	(285)
Issue of share options	-	-	337	-	337
Loss for the period	-	-	-	(1,532)	(1,532)
At 31 December 2006	2	3,910	337	(1,532)	2,717

CONSOLIDATED AND COMPANY BALANCE SHEETS AS AT 31 DECEMBER 2006

	Note	Group £'000	Company £'000
ASSETS			
Non-current assets			
Intangible assets	10	**85**	**10**
Property, plant & equipment	11	**8**	**4**
Investment in subsidiary	12	**-**	**1**
Other receivables		**-**	**129**
		93	**144**
Current assets			
Trade and other receivables	14	**63**	**46**
Prepayments and accrued income		**81**	**80**
Cash and cash equivalents	13	**2,478**	**2,473**
		2,622	**2,599**
Total assets		**2,715**	**2,743**
EQUITY AND LIABILITIES			
Equity attributable to equity holders			
Issued capital	16	**2**	**2**
Share premium	17	**3,910**	**3,910**
Share options reserve	18	**337**	**337**
Retained losses	19	**(1,562)**	**(1,532)**
Total equity		**2,687**	**2,717**
Current liabilities			
Trade and other payables	15	**28**	**26**
Total liabilities		**28**	**26**
Total equity and liabilities		**2,715**	**2,743**

Stephen West, Finance Director
11 May 2007

CONSOLIDATED AND COMPANY CASH FLOW STATEMENTS
FOR THE PERIOD ENDED 31 DECEMBER 2006

	12 September 2005 to 31 December 2006	
	Group	**Company**
	£'000	**£'000**
Operating activities		
Loss before tax from continuing operations	**(1,562)**	**(1,532)**
Adjustments to reconcile loss to net cash outflow from operating activities		
Non-cash:		
Depreciation	**5**	**5**
Amortisation	**15**	**13**
Share based payments	**337**	**337**
Write-off of exploration and evaluation costs	**877**	**864**
Interest income	**(100)**	**(100)**
Working capital adjustments:		
Increase in trade and other receivables	**(63)**	**(46)**
Increase in prepayments and accrued income	**(81)**	**(80)**
Increase in trade and other payables	**28**	**26**
Net cash outflow from operating activities	**(544)**	**(513)**
Investing activities		
Purchase of property, plant and equipment	**(13)**	**(9)**
Purchase of intangible assets	**(100)**	**(23)**
Exploration and evaluation costs	**(877)**	**(864)**
Purchase of shares in subsidiary	**-**	**(1)**
Interest received	**100**	**100**
Loans to subsidiary	**-**	**(129)**
Net cash used in investing activities	**(890)**	**(926)**
Financing activities		
Proceeds from issue of shares	**4,197**	**4,197**
Transaction costs for issue of shares	**(285)**	**(285)**
Net cash inflow from financing activities	**3,912**	**3,912**
Net increase in cash and cash equivalents	**2,478**	**2,473**
Cash and cash equivalents at 12 September 2005	**-**	**-**
Cash and cash equivalents at 31 December 2006	**2,478**	**2,473**

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

1. Accounting policies

1.1 Authorisation of financial statements and statement of compliance with IFRSs

Zeta Petroleum Limited ("Zeta" or the "Company"), the ultimate parent of the Group, is a private company incorporated in England. The registered office and principal place of business is 1 Berkeley Street, London, W1J 8DJ. The principal activities of Zeta and its subsidiaries (the Group) are oil and gas exploration, development and production.

The Group's consolidated financial statements for the period ended 31 December 2006 were authorised for issue by the board of directors on 11 May 2007 and the balance sheets were signed on the Board's behalf by S P West.

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. The principal accounting policies adopted by the Group are set out below.

1.2 Basis of preparation

The consolidated financial statements of Zeta have been prepared on a historical cost basis. The consolidated financial statements are presented in British pounds and all values are rounded to the nearest thousand (£000) except when otherwise indicated.

Zeta Petroleum Ltd was incorporated on 12 September 2005. The consolidated financial statements cover the period from 12 September 2005 to 31 December 2006.

1.3 Basis of consolidation

The consolidated financial statements comprise the financial statements of Zeta and its subsidiaries as at 31 December 2006. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

All intra-group balances, transactions, income and expenses and profits and losses resulting from intra-group transactions that are recognised in assets, are eliminated in full.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

Zeta has used the exemption granted under s230(1)(b) of the Companies Act 1985 that allows for the non-disclosure of the Income Statement of the parent company. The loss attributable to Zeta for the period ended 31 December 2006 was £1,532,000.

1.4 Joint ventures

The Group has a number of contractual arrangements with other parties which represent joint ventures.

A joint venture is a contractual arrangement whereby the Group and the other parties undertake an economic activity that is subject to joint control.

Where a Group company undertakes its activities under joint venture arrangements, the Group's share of jointly and directly controlled assets and any liabilities incurred jointly with other ventures are recognised and classified according to their nature. The Group's share of joint venture expenses are recognised when it is probable that the economic benefits associated with the transactions will flow from the Group and their amounts can be measured reliably.

1.5 Foreign currencies

The consolidated financial statements are presented in British pounds, which is the Company's functional and presentational currency. Each entity in the Group translates foreign currency transactions into its functional currency at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange prevailing at the Balance Sheet date. Exchange differences arising are taken to the Income Statement.

The functional currency of the foreign subsidiary Zeta Petroleum (Romania) SRL is Romanian New Leu (RON). Zeta translates the subsidiary accounts into the presentational currency using the closing rate method for assets and liabilities, which are translated into British pounds at the rate of exchange prevailing at the Balance Sheet date, and the weighted average exchange rate for the period for Income Statement accounts. Exchange differences arising on the translation of net assets of the subsidiary are taken to reserves.

1.6 Intangible Assets

Oil and gas exploration assets
Zeta follows the successful efforts based accounting policy for oil and gas assets. The successful efforts method means that only costs which relate directly to the discovery and development of specific oil and gas reserves are capitalised.

Costs incurred prior to obtaining the legal rights to explore an area are expensed immediately to the Income Statement.

Expenditure incurred on the acquisition of a licence interest is initially capitalised on a licence by licence basis and amortised on a straight-line basis over the estimated period of exploration and, in the event that no future activity is planned, the remaining balance of licence acquisition costs is written off. Should a discovery be made, the amortisation would be suspended and the remaining costs aggregated with exploration expenditure on a field by field basis as properties awaiting approval for development. When development is approved, the relevant expenditure is transferred to tangible assets.

Exploration expenditure incurred in the process of determining exploration targets is capitalised initially within exploration assets and subsequently allocated to drilling activities. Exploration drilling costs are initially capitalised on a well by well basis until the success or otherwise of the well has been established. The success or failure of each exploration effort is judged on a well by well basis. Drilling costs are written off on completion of a well unless the results indicate that hydrocarbon reserves exist and there is a reasonable prospect that these reserves are commercial.

Following appraisal of successful exploration wells, if commercial reserves are established and technical feasibility for extraction demonstrated, then the related capitalised exploration costs are transferred into a single field cost centre within development/producing assets after testing for impairment. Where results of exploration drilling indicate the presence of hydrocarbons which are ultimately not considered commercially viable, all related costs are written off to the Income Statement.

All costs incurred after the technical feasibility and commercial viability of producing hydrocarbons has been demonstrated are capitalised within development/producing assets on a field by field basis.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

Subsequent expenditure is capitalised only where it either enhances the economic benefits of the development/producing assets or replaces part of the existing development/producing asset. Any costs remaining associated with the part replaced are expensed.

Software costs
Software costs are carried within intangible assets at cost, less any accumulated amortisation and accumulated impairment losses.

Amortisation is charged so as to write off the cost over the estimated useful lives (1 to 3 years) using the straight-line method.

1.7 Property, plant and equipment

Property, plant and equipment are carried at cost, less any accumulated depreciation and accumulated impairment losses. Cost includes purchase price and construction costs for qualifying assets and borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets commences when the assets are ready for their intended use.

Depreciation is charged so as to write off the cost, less estimated residual value, over their estimated useful lives using the straight-line method, for the following classes of assets: computer equipment (3 years) and other equipment (1 to 5 years).

The estimated useful lives of property, plant and equipment and their residual values are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the Income Statement for the relevant period.

1.8 Impairment of intangible assets and property, plant and equipment

At each balance sheet date, the Group reviews the carrying amounts of its intangible assets and property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. Individual assets are grouped together as a cash-generating unit for impairment assessment purposes at the lowest level of their identifiable cash flows, where these are largely independent of the cash flows of the other Group assets. In the case of exploration assets this will normally be at a field by field level.

If any such indication of impairment exists the Group makes an estimate of the recoverable amount of the asset or cash generating unit. The recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an individual asset or a cash-generating unit exceeds its recoverable amount, the asset/cash-generating unit is considered impaired and is written down to its recoverable amount. In accessing the value in use, the estimated future cash flows are adjusted for the risks specific to the asset/cash-generating unit and are discounted to their present value at a rate that reflects the current market indicators.

Where an impairment loss subsequently reverses, the carrying amount of the asset/cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset/cash-generating unit in prior years. A reversal of an impairment loss is recognised as income immediately.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

1.9 Impairment of financial assets

The Group assesses at each balance sheet date whether a financial asset is impaired and will recognise the impairment loss immediately through the income statement.

1.10 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and current balances with banks and similar institutions, which are readily convertible to known amounts of cash. Cash equivalents are short-term with an original maturity of less than 3 months, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

1.11 Trade and other receivables

Trade receivables are recognised and carried at the lower of their original invoiced value and recoverable amount. Other debtors are recognised and measured at nominal value.

1.12 Share-based payments

Share options

The Group issues equity-settled share-based payments to the directors and senior management ("Employee Share Options") and to its corporate finance advisers for assistance in raising private equity ("Non-employee Share Options"). Equity-settled share-based payments are measured at fair value at the date of grant for Employee Share Options and the date of service for Non-employee Share Options. The fair value determined at the grant date or service date, as applicable, of the equity-settled share-based payments is expensed, with a corresponding credit to equity, on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest. At each subsequent balance sheet date the Group calculates the estimated cumulative charge for each award having regard to any change in the number of options that are expected to vest and the expired portion of the vesting period. The change in this cumulative charge since the last balance sheet date is expensed with a corresponding credit being made to equity. Once an option vests, no further adjustment is made to the aggregate amount expensed. The fair value is calculated using the Black Scholes method. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability exercise restrictions and behavioural considerations. The market price used in the model is the issue price of Company shares at the last placement of shares immediately preceding the calculation date. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitation of the calculations used.

1.13 Taxation

Income tax expense represents the sum of the current tax payable and deferred tax.

The current tax payable is based on taxable profit for the period. Taxable profit differs from net profit as reported in the income statement because it excludes items of income and expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax base used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered. Any such reduction shall be reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised based on tax rates and laws substantively enacted by the balance sheet date. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there exists a legal and enforceable right to offset and they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

1.14 Investments and other financial assets

Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, and available for sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the entity first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit and loss.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments held for trading are recognised in profit and loss.

Financial assets may be designated at initial recognition as at fair value through profit or loss if the following criteria are met: (i) the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis; or (ii) the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management strategy; or (iii) the financial asset contains an embedded derivative that would need to be separately recorded. As at 31 December 2006, no financial assets have been designated as at fair value through profit and loss.

Held-to-maturity investments
Held-to-maturity investments are non-derivative financial assets which carry fixed or determinable payments and fixed maturities and which the Group has the positive intention and ability to hold to maturity. After initial measurement held to maturity investments are measured at amortised cost. This cost is computed as the amount initially recognised minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognised amount and the maturity amount, less allowance for impairment. This calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. Gains and losses are recognised in the income statement when the investments are derecognised or impaired, as well as through the amortisation process. As at 31 December 2006, the Company had no held-to-maturity investments.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are subsequently carried at amortised cost using the effective interest method less any allowance for impairment. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial investments
Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial measurement, available for sale financial assets are measured at fair value with unrealised gains or losses being recognised directly in equity in the net unrealised gains reserve. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognised in the income statement. Interest earned or paid on the investments is reported as interest income or expense using the effective interest rate. Dividends earned on investments are recognised in the income statement as 'Dividends received' when the right of payment has been established. As at 31 December 2006, the Company had no available-for-sale financial investments.

Fair value
The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models.

1.15 Revenue recognition

Sales of oil and gas products are recognised when the significant risks and rewards of ownership have passed to the buyer and it can be reliably measured. Other services are recognised when the services have been performed. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, VAT and other sales taxes or duty.

Interest income is recognised as the interest accrues, by reference to the net carrying amount at the effective interest rate applicable.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

1.16 Trade payables

Trade payables are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method.

1.17 Share issue expenses and share premium account

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

2. Revenue

Revenue received is entirely attributable to other services provided by the Company to the joint venture operations in Turkey.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

3. Segment information

For the purposes of segmental information the primary segment reporting format is determined to be the business segment. The Group has one class of business, the exploration, development and production of oil and gas. No further disclosure is required in relation to primary segment reporting in this note as all the relevant disclosure is already detailed throughout the Group financial statements.

Secondary segment information is reported geographically. The Group's geographical segments are United Kingdom, Turkey and Romania.

Group revenue for the period ended 31 December 2006 is entirely attributable to the United Kingdom geographical segment.

The following tables present expenditure and certain asset information regarding the Group's geographical segments for the period ended 31 December 2006:

Segment assets	**Group £'000**
United Kingdom	**2,586**
Turkey	**27**
Romania	**102**
	2,715

Capital expenditure	***12 September 2005 to 31 December 2006*** **Group £'000**
United Kingdom	**32**
Turkey	**864**
Romania	**94**
	990

4. Operating loss

Operating loss is stated after charging:

	12 September 2005 to 31 December 2006 **Group £'000**	**Company £'000**
Amortisation (note 10)	**15**	**13**
Depreciation (note 11)	**5**	**5**
Net foreign exchange differences	**10**	**9**

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

5. Auditors' remuneration

	12 September 2005 to 31 December 2006 Group £'000	Company £'000
Audit of the financial statements	**15**	**15**
Other fees to auditors:		
- Taxation services	**1**	**-**
	16	**15**

6. Employment costs

	12 September 2005 to 31 December 2006 Group £'000	Company £'000
Wages and salaries	**127**	**127**
Social security costs	**14**	**14**
Share based payments	**272**	**272**
	413	**413**

The weighted average number of employees (including executive directors) during the period was:

	Group	Company
Management	**2**	**2**

7. Remuneration of Directors

Group and Company:	*12 September 2005 to 31 December 2006* Total £'000
Basic salary and fees	**127**
Share based payments	**255**
	382

Details of interests in share options for each director are set out in the Directors Report on page 3.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

8. Taxation

The tax charge for the period is £nil. The tax charge is calculated as follows:

	12 September 2005 to 31 December 2006 Group £'000
Accounting loss before tax	**(1,562)**
Tax at domestic rate of corporation tax of 30%	**(469)**
Disallowed expenses and non-taxable income	**6**
Share options issued	**101**
Non-qualifying depreciation and amortisation	**7**
Effect of lower tax rates in Romania	**2**
Unrecognised tax losses	**353**
	-

The Directors do not consider it appropriate to provide for any deferred tax asset to reflect the potential benefit arising from temporary differences at 31 December 2006. At 31 December 2006 there were unprovided deferred tax assets in respect of tax losses carried forward of approximately £352,532.

9. Loss per share

Basic loss per share is calculated on the loss for the period attributable to equity holders of the parent of £1,562,000 and divided by the weighted average of 1,677,102 ordinary shares.

As the exercise of options would be anti-dilutive no diluted earnings per share figure has been provided.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

10. Intangible assets

	Licence Acquisition Costs £'000	Exploration and Evaluation £'000	Software Costs £'000	Total £'000
GROUP				
Cost:				
As at 12 September 2005	-	-	-	-
Additions	77	877	23	977
Unsuccessful exploration and evaluation	-	(877)	-	(877)
At 31 December 2006	77	-	23	100
Amortisation:				
As at 12 September 2005	-	-	-	-
Provided in the period (see note 4)	(2)	-	(13)	(15)
At 31 December 2006	(2)	-	(13)	(15)
Net book value at 12 September 2005	-	-	-	-
Net book value at 31 December 2006	75	-	10	85
COMPANY				
Cost:				
As at 12 September 2005		-	-	-
Additions		864	23	887
Unsuccessful exploration and evaluation		(864)	-	(864)
At 31 December 2006		-	23	23
Amortisation:				
As at 12 September 2005		-	-	-
Provided in the period (see note 4)		-	(13)	(13)
At 31 December 2006		-	(13)	(13)
Net book value at 12 September 2005		-	-	-
Net book value at 31 December 2006		-	10	10

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

11. Property, plant and equipment

	Group £'000	Company £'000
Cost:		
As at 12 September 2005	-	-
Additions	13	9
At 31 December 2006	13	9
Depreciation:		
As at 12 September 2005	-	-
Provided in the period (see note 4)	(5)	(5)
At 31 December 2006	(5)	(5)
Net book value at 12 September 2005	-	-
Net book value at 31 December 2006	8	4

12. Investment in subsidiary

	Company £'000
Additions and as at 31 December 2006	1

The Company's only subsidiary is Zeta Petroleum (Romania) SRL, a Romanian incorporated company in which the Company holds 100% of the entire issued capital. The principal activity of Zeta Petroleum (Romania) SRL is exploration and production and the company operates in Romania.

13. Cash and cash equivalents

	Group £'000	Company £'000
Cash at bank and in hand	18	13
Short-term deposits	2,460	2,460
As at 31 December 2006	2,478	2,473

Cash at bank earns interest at floating rates based on a discount to US$ / GBP LIBOR. Short-term deposits are made for varying periods of between one day and one month depending on the future cash requirements of the Group, and earn interest at the respective short-term deposit rates. The fair value of cash and cash equivalents is £2,478,377.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

14. Trade and other receivables

	Group £'000	Company £'000
Trade receivables	1	1
Other receivables	62	45
As at 31 December 2006	63	46

15. Trade and other payables

	Group £'000	Company £'000
Trade payables	5	3
Other taxes and social security costs	8	8
Accruals	15	15
As at 31 December 2006	28	26

16. Share capital

	Group Number of £0.001 Ordinary	Company Number of £0.001 Ordinary
Authorised ordinary shares		
As at 31 December 2006	3,000,000	3,000,000

	Group £'000	Company £'000	Group Number of £0.001 Ordinary	Company Number of £0.001 Ordinary
Allotted, issued and fully paid ordinary shares				
Issued in period for cash	2	2	2,425,398	2,425,398
As at 31 December 2006	2	2	2,425,398	2,425,398

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

16. Share capital *continued*

On the date of incorporation the Company had an authorised capital of 1,000 £1 ordinary shares and issued capital of 2 £1 ordinary shares.

On 2 March 2006 a unanimous resolution was passed by the members of the Company to subdivide each existing ordinary share of £1 that had been issued and credited as fully paid into 1,000 ordinary shares of £0.001 each. In addition, it was resolved on this date to increase the authorised capital of the Company from £1,000 to £3,000 by the creation of 2,000,000 ordinary shares of £0.001 each ranking pari passu for all purposes with the existing ordinary shares of £0.001 in the capital of the Company.

The following shares were allotted during the period:

(i) 600 £1 ordinary shares on 10 October 2005 at a price of £1 per share;

(ii) 219 £1 ordinary shares on 11 October 2005 at a price of £457 per share;

(iii) 179 £1 ordinary shares on 1 March 2006 at a price of £1 per share;

(iv) 1,049,457 £0.001 ordinary shares on 28 March 2006 at a price of £2.8736 per share;

(v) 375,941 £0.001 ordinary shares on 25 May 2006 at a price of £2.8736 per share.

17. Share premium

	Group £'000	Company £'000
Arising on shares issued for cash	**4,195**	**4,195**
Transaction costs for issue of shares	**(285)**	**(285)**
As at 31 December 2006	**3,910**	**3,910**

18. Share options reserve

	Group £'000	Company £'000
Charge for the period and as at 31 December 2006	**337**	**337**

The balance in the share options reserve relates to the fair value of the share options that have been expensed through the income statement in accordance with IFRS 2. During the period, 242,840 share options were granted to directors and senior management (none of which were exercisable as at 31 December 2006) and 73,429 share options were granted to the Company's corporate finance advisers (all of which were exercisable as at 31 December 2006).

The weighted average fair value of options granted during the period was £1.61 and the exercise price for options outstanding as at 31 December 2006 ranged from £2.87 to £3.32.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

19. Retained earnings

	Group £'000	Company £'000
Loss for the period and as at 31 December 2006	**(1,562)**	**(1,532)**

20. Financial instruments

The Group's principal financial instruments comprise cash and cash equivalents, and short-term deposits. The main purpose of these financial instruments is to finance the Group's operations. The Group has other financial instruments which mainly comprise trade payables which arise directly from its operations.

Exposure to currency and interest rate risks arise in the normal course of the Group's business.

Interest rate risk
The Group and Company earn interest from bank deposits at floating rates.

The interest rate profile of the financial assets of the Group and Company as at 31 December 2006 is as follows (excluding short-term assets and liabilities, non-interest bearing):

Floating rate – within one year	Group £'000	Company £'000
Cash and cash equivalents	**2,478**	**2,473**

Floating rate financial assets comprise cash deposits placed on money markets at call and cash at bank.

Foreign currency risk
The Group operates internationally and has monetary assets and liabilities in currencies other than the functional currency of the operating company involved. These exposures, which are immaterial as at 31 December 2006, give rise to the net currency gains and losses recognised in the profit and loss account.

The Group does not use foreign exchange contracts to hedge its currency risk.

Fair values of financial assets and financial liabilities
All financial assets and liabilities are shown in the balance sheet at their nominal amount, which approximates to the underlying fair value.

The following methods and assumptions are used in estimating the fair values of financial instruments reflected in this note:

(a) Financial assets – the fair value of a financial asset is the amount at which the financial asset could be exchanged in an arm's length transaction. Where available, market values have been used; and

(b) Trade and other receivables/payables – all trade and other receivables and payables have a remaining life of less than one year. The nominal amount is deemed to reflect the fair value.

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED 31 DECEMBER 2006

21. Related party transactions

On 10 October 2005 Mr S West loaned an amount of £21,000 (unsecured and interest free) to the Company. This amount was repaid in full by the Company on 4 November 2005.

On 10 March 2006 Mr S West loaned an amount of £10,000 (unsecured and interest free) to the Company. This amount was repaid in full by the Company on 29 March 2006.

22. Capital commitments

In accordance with an agreement between the Group and a third party in Romania, the Group is committed to drilling an appraisal well in Romania in 2007. The Group estimates that the minimum cost of drilling this well will be £510,440.

23. Post balance sheet events

On 15 January 2007 the Group acquired a 100% interest in the Bobocu licence in Romania through a liquidation auction. The total price paid by the Group was RON 3,405,000 (£672,660) which includes VAT of RON 543,655 (£107,400). The VAT amount is expected to be recovered during 2007. A concession agreement was signed with the Romanian National Agency for Minerals and Resources on 27 March 2007. The concession agreement is now passing through the ministerial approval process, which is expected to take up to 12 months.

On 31 March 2007 the Group entered into a farm-out agreement with a third party ("Farmee") whereby, subject to certain conditions, the Farmee is committed to invest up to US$4.5 million in the Bartin licences in Turkey and in return the Group has agreed to transfer 50.5% of its 70% interest in the Bartin licences to the Farmee. In accordance with the terms of the farm-out agreement, the Group has a 19.5% effective interest in the Bartin licences as at the date of this report.