Prospectus

InterOil Exploration and Production ASA

(a public limited liability company organized under the laws of Norway)

Registration number 988 247 006.

Listing of the Company's shares on Oslo Børs

This Prospectus does not constitute an offer to buy, subscribe or sell the securities described herein. This Prospectus serves as a listing prospectus as required by applicable laws and no securities are being offered or sold pursuant to this Prospectus.

Manager

Pareto Securities ASA

17 July 2006

IMPORTANT NOTICE[1]

This Prospectus has been issued by InterOil Exploration and Production ASA ("InterOil" or "the Company") in connection with the Listing of InterOil's shares on Oslo Børs, as further described herein.

This Prospectus has been prepared to comply with the Norwegian Securities Trading Act chapter 5 and related secondary legislation, including the EC Commission Regulation EC/809/2004. The Prospectus has been prepared solely in the English language. Oslo Børs has approved this Prospectus in accordance with the Norwegian Securities Trading Act sections 5-3 and 5-7.

Except for the approval by Oslo Børs, no action has been taken to permit the distribution of this Prospectus in any jurisdiction where action would be required for distribution. Accordingly, this Prospectus may not be used for the purpose of an offer of, or solicitation for, any securities in any jurisdiction or in any circumstances in which such offer or solicitation would be unlawful or unauthorized.

The information contained herein is only updated as of the date hereof and subject to change, completion or amendment without notice. In accordance with section 5-15 of the Norwegian Securities Trading Act, any new factor, significant error or inaccuracy that might have an effect on the assessment of the New Shares and/or the New Shares and emerges between the time of publication of the Prospectus and the Listing of the New Shares, will be included in a supplement to the Prospectus. Such supplement must be approved by Oslo Børs. Neither the publication nor distribution of this Prospectus nor any sale made hereunder shall under any circumstances create any implication that the information herein is correct as of any date subsequent to the date of the Prospectus.

This Prospectus does not constitute an offer to sell, or a solicitation of an offer to buy, any of the Shares or any other securities issued by the Company.

This Prospectus has not been approved or recommended by any United States federal or state securities commission or regulatory authority nor have such entities confirmed its accuracy or adequacy. Any representation to the contrary is a criminal offence.

THE SECURITIES DESCRIBED IN THIS PROSPECTUS HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "**US SECURITIES ACT**") AND MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S OF THE U.S. SECURITIES ACT) UNLESS AN EXEMPTION FROM REGISTRATION IS AVAILABLE PURSUANT TO THE US SECURITIES ACT.

In relation to the United Kingdom, this Prospectus is only directed at, and may only be distributed to, persons who fall within the meaning of Article 19 (Investment Professionals) and 49 (High Net Worth Companies, Unincorporated Associations etc.) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (as amended) or who are persons to whom the document may otherwise be lawfully distributed. This Prospectus may only be distributed in circumstances which do not result in an offer to the public in the United Kingdom within the meaning of Public Offers of Securities Regulations 1995 (as amended). The distribution (which term shall include any form of communication) of this Prospectus may be restricted pursuant to section 21 (Restrictions on Financial Promotion) of the Financial Services and Markets Act 2000 (as amended).

All inquiries relating to this Prospectus should be directed to the Manager.

In the ordinary course of their respective businesses, the Manager and certain of their affiliates have engaged, and may in the future engage, in investment banking and commercial banking transactions with the Company.

Any dispute that might arise regarding this Prospectus is subject to Norwegian law and the exclusive jurisdictions of the Norwegian courts.

[1] Capitalized terms used in this section and not defined herein shall have the meaning ascribed to them in the Section headed "Definitions and Glossary".

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This Prospectus has been prepared in the English language only.

1 Summary

The following summary should be read in conjunction with, and is qualified in its entirety, by the more detailed information and the Appendices appearing elsewhere in this Prospectus.

In case a claim relating to the information contained in the Prospectus is brought before a court, the plaintiff Investor might have to bear the cost of translating the Prospectus before legal proceedings are initiated. Civil liability attaches to those persons who have tabled the summary including any translation thereof, and applied for its notification, but only if the summary is misleading, inaccurate or inconsistent when read together with the other parts of the Prospectus.

1.1 Description of InterOil

1.1.1 Introduction

InterOil was founded in May 2005. In September, 2005, InterOil acquired all the assets of Mercantile International Petroleum Inc, and became the operator and producer of oil and gas in Peru and Colombia. Subsequently InterOil has implemented an investment program in both countries, significantly increased production and established a core of professionals in Norway and Switzerland to manage and run this operation. The local management in Peru and Colombia has continued following InterOil's acquisition.

1.1.2 History

The Company was established on 2 May 2005 as a Norwegian Private Limited Company ("AS"). It was transformed to a Norwegian Public Limited Company ("ASA") on 14 November 2005. The Company is registered in the Register of Business Enterprises with org. no: 988247006. The Company's registered office is Strandveien 50, 1366 Lysaker.

InterOil is an upstream oil exploration and production company focused on South America and Africa. The Company currently has oil exploration activities in Peru and Colombia, and is in the process of establishing operations in West Africa.

The Company's activities in Peru and Colombia are the result of the acquisition of certain subsidiaries previously owned by the oil exploration company Mercantile International Petroleum Inc. ("**MIPI**"). In 2004 MIPI was looking to sell its oil exploration activities in Peru and Colombia. Negotiations for the acquisition of MIPI's operations and assets in Peru and Colombia started in September 2004, and on 9 June 2005 InterOil entered into a sales and purchase agreement with MIPI. The closing of the acquisition took place on 27 September 2005.

The assets in Peru and Colombia were originally negotiated by InterOil Exploration SA, a Swiss company wholly owned by the Company. The assets were later transferred to another 100% subsidiary of InterOil, InterOil Exploration and Production Latin America AS.

1.1.3 Business description

The Company's operations are currently located in Peru and Colombia. In addition, the Company is currently in the process of establishing operations in West Africa, and has been offered participation in two exploration licenses in Angola.

1.1.3.1 Peru

In Peru InterOil's activities and assets consist of three companies and two producing assets, located in the Talara area in the north-west of Peru. The licenses Block III & IV are located close to Talara, where the Peruvian part of the Group has its operational office. Most oil related services can be found in this town, as well as Piura, located 100km to the south of Talara.

The operating companies include:

- Mercantile Peru Oil & Gas S.A. – License holder of Block III
- Compania Petrolera Rio Bravo S.A. – License holder of Block IV
- Manitoba Services S.A. – Service company

Talara has a large refinery, operated by Perupetro S.A., the Peruvian state oil company. The oil produced by the Company is piped to this refinery.

InterOil's net production from these operations before royalties at the end of April 2006 was approximately 2,400 bbl/d, which is an increase of approximately 800 bbl/d since the beginning of the year. Additional investments will be done in 2006 in order to further increase the production.

1.1.3.2 Colombia

In Colombia, InterOil's activities and assets is held by a Colombian branch of a BVI registered company, Mercantile Colombia Oil and Gas Inc. (the only activity of the company is the operation of the Colombian branch), Mercantile Colombia Oil and Gas Inc. have seven contract areas which cover a total area of 258 km^2. All contract areas are located in the Rio Magdalena basin.

The Company's main office is in Bogota and its operations are carried out 100km south-west of Bogota in the Upper Magdalena Valley. This is an area which has limited facilities. The Company's oil is piped locally into tankers and trucked to the south to Hocols storage facility, which is situated 200 km to the south of the Company's operations.

The Company is the operator of all contract areas with the Colombian state-owned oil company Ecopetrol as partner. Ecopetrol has the right to a 30%-50% equity interest in all areas, and has exercised this in all contracts except one. Mercantile Colombia has a staff of approximately 42.

InterOil's net production from all areas in Colombia before royalties at end of April was approx. 1,000 bbl/d, an increase of approximately 250 bbl/d since the beginning of the year. InterOil will invest approx. USD 8 million in Colombia in 2006 in order to increase the production, but so far the effect of these investments has not been as successful as in Peru.

Below is an overview of the fields:

- Toqui-Toqui field (located within Puli C Block)
- Rio Opia contract (located within Puli C Block)
- Ambrosia contract (located within Puli C Block)
- Mana contract (located within Puli C Block)
- Armero contract
- Paraiso contract
- Puli B Block

1.1.3.3 West Africa

In addition to the Company's activities in Peru and Colombia, the Company is currently in the process of establishing operations in West Africa. The objective is to acquire one producing asset in this region within 2006.

During the 1Q of 2006, InterOil applied for two blocks offshore Angola. On 9 May 2006, the Company was offered participation in exploration licenses for Block 5 & 6 offshore Angola. The possible participation will be evaluated during 2006.

1.1.4 Vision and Strategy

The objective of InterOil is to develop the Company as an exploration and production oil & gas company active primarily in West Africa and South America.

InterOil will seek to achieve this through:

- initial growth from the purchase of one or more junior oil & gas producers
- developing organically the assets within these companies
- acquire one or more producing assets
- participate in offshore and onshore exploration with the ultimate goal of achieving a balance of the Company's portfolio between exploration, appraisal, developing and producing assets.

1.1.5 Board of Directors, Senior Management and Employees

Board of Directors

The Company's Board of Directors, will from the time of the Listing, consist of 5 members: Mårten Rød (Chairman), Gian Angelo Perrucci, Robert Blair Thomas, Berit Kjøll and Patricia Guerra.

For further information please see Section 9.4.1 below.

Management

The Group executive management comprise: Nils Trulsvik (CEO), Tom Wolden (COO), Jon Wiggen (CFO), Rene Graf (CTO), Christian Nygaard (Director Development), and Pascal Berthou (General Manager, Africa). For further information please see Section 9.4.3 below.

Employees

As of the date of this Prospectus, InterOil and it's subsidiaries employ 134 persons.

For further information please see Section 9.10 below.

1.1.6 Advisors and Auditors

Manager

Pareto Securities ASA has been retained as the Manager for the Listing.

Legal counsel

The Company's legal counsel is Wiersholm, Mellbye & Bech, advokatfirma AS.

Auditor

The Company's auditor is PricewaterhouseCoopers AS, Oslo, Norway.

For further information, please see Section 6.10.

1.1.7 Major shareholders and related party transactions

Major shareholders

As of 17 July 2006 the five largest shareholders in the Company were:

1	Eksportconsult AS	5,225,000	24.6%
2	Caberian Investment Inc.	4,600,000	21.7%
3	Credit Suisse Securities	1,870,600	8.8%
4	Bear Sterns Securities Corp.	1,618,800	7.6%
5	Force Capital Partners AS	800,000	3.8%

For further information please see Section 10.6.

Related party transactions

Eksportconsult AS has a management agreement with InterOil relating to the business development in the Company. Eksportconsult AS is owned by the Chairman of the board, Mårten Rød, and his immediate family.

For further information please see Section 6.6.

1.2 Selected financial information

The following table sets out certain selected financial information of the Company for period from 2 May 2005 (inception) to 31 December 2005 and the first quarter ending 31 March 2006 and 2005.

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and correspond with the interpretation of the International Standards Board. The consolidated financial statement is presented in USD and is rounded up to thousands (1,000). The consolidated financial statements have been prepared under the historical cost convention, except for financial assets at fair value through profit or loss.

1.2.1 Consolidated income statement

Amounts in USD 1 000	For the three months period ended 31 March 2006	For the period from 2 May 2005 (inception) to 31 December 2005
	(Unaudited)	
Sales	8 641	7 991
Cost of goods sold	-3 438	-3 240
Gross profit	**5 203**	**4 751**
Tariffs and transportation	-133	-204
Exploration cost expensed	123	-783
Administrative expense	-1 905	-1 501
Other income	105	181
Other operating expenses	-8	-143
Profit from operating activities	**3 385**	**2 301**
Finance costs – net	-1 340	-1 522
Profit before income tax	**2 045**	**780**
Income tax expense	-1 438	-503
Net profit	**607**	**276**
Earnings per share for profit attributable to the equity holders of the Company during the period (expressed in USD per share)		
– basic	0.03	0.04
– diluted	0.03	0.04

1.2.2 Condensed consolidated Balance sheet

Amounts in USD 1 000	As of 31 March 2006	As of 31 December 2005
	(Unaudited)	
ASSETS		
Total non-current assets	101 489	98 600
Total current assets	20 531	26 259
TOTAL ASSETS	**122 021**	**124 859**
EQUITY		
Share capital and share premium	43 574	43 574
Other reserves	3 096	3 096
Retained earnings	883	276
Total equity	**47 553**	**46 946**
LIABILITIES		
Total non-current liabilities	57 906	57 105
Total current liabilities	16 562	20 807
Total liabilities	**74 468**	**77 913**
TOTAL EQUITY AND LIABILITIES	**122 021**	**124 859**

1.2.3 Capitalization and indebteness

As of 31 March 2006, the Company had cash, cash equivalents and marketable securities of NOK 15.2 million.

The Company believes that its current capital resources together with the proceeds from the Bond Issue, will be sufficient to fulfil commitments referred to under the section 6.5 "Investments" and 6.8 "Property, Plants and Equipment".

InterOil has a total of NOK 68 million in debt consisting of USD 42 million in long-term debt, USD 20 million in a Senior Unsecured Bond Loan and subordinated interest bearing debt amounting to USD 6 million to Maxi Assets Inc. (Panama) relating to the acquisition of the assets in Peru and Colombia.

The Company has an equity ratio of 33%.

1.3 The Listing and admission to trading

The board of Oslo Børs approved InterOil's application for listing of the Shares at its meeting held on 22 June 2006. Barring unforeseen circumstances, the first day of trading for the Shares is expected to be on or about 19 July 2006. The Shares are expected to trade in round lots of 200 Shares with the ticker-symbol "IOX".

1.4 Summary of Risk Factors

A number of risk factors may adversely affect the Company. Below is a brief summary of some of the most relevant risk factors described in Section 2 "Risk factors". The risks described in section 2 are not exhaustive, and other risks not discussed herein may also adversely affect the Company. Prospective investors should consider carefully the information contained in this Prospectus and make an independent evaluation before making any investment decision.

1.4.1 Financial risk

Financial risk comprises foreign exchange risk, credit risk, liquidity risk, cash flow and interest rate risk.

Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and the investment of excess liquidity. Currently, the Company uses no derivative financial instruments to hedge the above mentioned risk exposures.

Currently, the Group is selling its oil In Peru to Petroperu, a state owned company and in Colombia, to Hocol, a subsidiary of a French enterprise. The credit risk for these customers is considered to be low.

Prudent liquidity risk management implies maintaining sufficient cash and available for sale financial assets and develop operations according to budget. InterOil has in 2005 generated positive cash flows from operations.

The Group has obtained financing with fixed interest rates which exposes the Group to fair value changes. There are no other financing agreements and the Group has not entered into any interest rate swaps

1.4.2 Operational risk

The business of exploration and production of oil and gas involves a certain degree of risk. Few prospects that are explored are ultimately developed into producing oil and gas fields. Significant expenditure is required to establish the extent of oil and gas reserves through seismic and other surveys and drilling and there can be no certainty that oil and gas reserves will be found.

1.4.3 Political risk

Changes in the legislative and fiscal framework governing the activities of the companies engaged within the oil and gas sector may have a material impact on exploration and development activity or directly affect the Company's operations. In particular, changes in political regimes will constitute a material risk factor for the Company's operations in foreign countries.

1.4.4 Market risk

The marketability of any oil and gas discovered will be affected by numerous factors beyond the control of InterOil. The oil and gas industry is highly competitive. There is strong competition for the discovery and acquisition of properties considered to have commercial potential. InterOil competes with other exploration and production companies, many of which have great financial resources.

InterOils' production and prospective production comes from its interests in a small number of oil and gas fields in South America. Whilst the production has been stable and existed for a long time, InterOil will remain dependent on

a production from this area in the near future. Operational problems in any one field could have a materially adverse affect on InterOil.

The profitability and cash flow of InterOils' operations will be dependent upon the market price of oil and gas. This is known to fluctuate. If the price of oil and gas products should drop significantly, the economic prospects of the projects in which InterOil has an interest would be significantly reduced.

The actual cost estimate provided for abandonment and restitution cost could differ in amount and timing and the regulations governing abandonment may be different in the future. Such differences could have some impact on InterOil's business.

1.5 Additional Information

1.5.1 Share Capital and shareholder matters

InterOil is a Norwegian public limited liability company with registration number 988 247 006.

The Company's registered share capital prior to the Listing is NOK 1,062,250 consisting of 21,245,000 Shares each with a nominal value of NOK 0.05, fully paid and issued in accordance with Norwegian law.

All issued Shares in the Company are vested with equal shareholder rights in all respects. There is only one class of shares issued and all Shares are freely transferable.

See Section 10 "Share Capital and Shareholder Matters" for a further description of the Company's share capital.

The Shares are registered with VPS under the International Securities Identification Number (ISIN) NO 001 0284318. The registrar for the Shares is DnB NOR Bank, Verdipapirservice.

1.5.2 Articles of Association

The articles of association of InterOil are included as Appendix 1 to this Prospectus.

The Company's purpose according to its articles is the exploration, development, production, purchase and sale of oil and natural gas deposits and production licences, as well as any activities related thereto, cf. article 3. The Company has one class of shares. The Board of Directors consists of 6 members.

1.5.3 Documents on display

The following documents (or copies thereof) may be inspected at www.interoil.no:

i. the articles of associations of the Company;
ii. first quarter report for 2006,
iii. historical financial information including auditor's report for the financial years ending 31 December 2005,
iv. historical financial information for Mercantile International Petroleum Inc. for 2004 and 2003,
v. stock exchange notices, including quarterly reports, distributed by the Company through Oslo Børs' information system at www.newsweb.no.

1.5.4 Third party statements

The information in this Prospectus that has been sourced from third parties has been accurately reproduced and, as far as the Company is aware and able to ascertain from the information published by that third party, no facts have been omitted that would render the reproduced information inaccurate or misleading.

2 Risk Factors

Prospective investors should carefully consider the following risk factors, in addition to the other information presented in this Prospectus, before making an investment decision. The risks discussed below are not the only ones that may affect the Company's business or the value of the Company's securities. Additional risks not presently known to the Company or that the Company currently considers immaterial, may also impair the Company's business operations and prospects. If any of the following risks occur, potential investors could lose the entire value of their investment in the Company's securities.

The Group's activities are exposed to certain financial risks: market risk, credit risk, liquidity risk and interest risk. The Group's overall risk management plan focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. Risk management is carried out by the Chief Financial Officer.

2.1 Financial risk

2.1.1 Foreign exchange risk

The Group operates internationally and is, to some extent, exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the following currencies; USD, PEN and COP. All revenues are invoiced to the customers in USD, while operating expenses are mostly denominated in USD, NOK, PEN and COP. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and the investment of excess liquidity. Currently, the Company uses no derivative financial instruments to hedge the above mentioned risk exposures.

2.1.2 Credit risk

Currently, the Group is selling all of its oil to Petroperu, and Hocol, a French enterprise. The credit risk for these customers is considered to be low.

2.1.3 Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and available for sale financial assets and develop operations according to budget. InterOil has in 2005 generated positive cash flows from operations. In 2005, the Group performed a share issue with net proceeds of USD 43,558 million and should be able to raise additional funds if the liquidity status requires additional funding. Cash positions are monitored regularly to ensure that cash positions are kept an acceptable level to ensure reasonable coverage for the Groups commitments and other planned investments.

2.1.4 Cash flow and fair value interest rate risk

The Group has obtained financing with fixed interest rate which exposes the Group to fair value changes. There are no other financing agreements and the Group has not entered into any interest rate swaps.

2.1.5 The Company's Share Prices may experience volatility

An investment in the Company's shares is associated with a significant element of risk. The Company operates in a market featuring open and fierce competition and a number of factors outside the Company's control may affect the performance of the Company. The market price of the Shares could fluctuate significantly in response to quarterly variations in operating results, adverse business developments, changes in financial estimates by securities analysts and / or changes to the regulatory environment in which the Company operates. The price of the Shares will also be subject to fluctuations in line with general movements in the capital markets and the liquidity in the secondary market as well as specific movements for oil service companies.

2.1.6 Investment and Trading Risks in General

All investments in securities are exposed to risk of loss of capital. Investment in oil exploration and production as contemplated by the Company involves significant economic risks. Although the Company's investment and management strategy is expected to provide some protection from the risk of loss inherent in the ownership of such assets, there can be no assurance that these strategies will completely protect against this risk or that the Company's investment objectives will be achieved.

2.2 Operational risk

2.2.1 General

The business of exploration and production of oil and gas involves a certain degree of risk. Few prospects that are explored are ultimately developed into producing oil and gas fields. Significant expenditure is required to establish the extent of oil and gas reserves through seismic and other surveys and drilling and there can be no certainty that oil and gas reserves will be found.

The exploration and development of oil and gas assets may be curtailed, delayed or cancelled by unusual or unexpected geological formation pressures, oceanographic conditions, hazardous weather conditions or other factors. There are numerous risks inherent in drilling and operating wells, many of which are beyond the Company's control. InterOil's operations may be curtailed, delayed or cancelled as a result of environmental hazards, industrial accidents, occupational and health hazards, technical failures, shortage or delays in the delivery of rigs and/or other equipment, labor disputes and compliance with governmental requirements. Drilling may involve unprofitable efforts, not only with respect to dry wells, but also with respect to wells which, though yielding some petroleum, are not sufficiently productive to justify commercial development or cover operating and other costs. Completion of a well does not assure a profit on the investment or recovery of drilling, completion and operating costs.

The reserves data included in this document are estimates. The nature of reserve quantification studies means that there can be no guarantee that estimates of quantities and quality of oil and gas disclosed will be available for extraction. Therefore, actual production, revenues, cash flows, royalties and development and operating expenditures may vary from these estimates. Such variances may be material.

2.2.2 Political Risk

Changes in the legislative and fiscal framework governing the activities of the companies engaged within the oil and gas sector may have a material impact on exploration and development activity or directly affect the Company's operations. In particular, changes in political regimes will constitute a material risk factor for the Company's operations in foreign countries. Below is a short overview of the political and economical risks presents in the countries where the Company operates.

Peru

Peru's economy reflects its varied geography - an arid coastal region, the Andes further inland, and tropical lands bordering Colombia and Brazil. Abundant mineral resources are found in the mountainous areas, and Peru's coastal waters provide excellent fishing grounds. However, overdependence on minerals and metals subjects the economy to fluctuations in world prices, and a lack of infrastructure deters trade and investment.

The oil and gas industry is, under the new fiscal regulations that were introduced last year, quite favorable in Peru, which can be seen from the latest allocation of licenses.

Columbia

Colombia's economy has been on a recovery trend during the past two years despite a serious armed conflict. The economy continues to improve thanks to austere government budgets, focused efforts to reduce public debt levels, an export-oriented growth strategy, and an improved security situation in the country.

InterOil's subsidiary MCOG, has operated in Colombia since 1994. Neither the expatriates nor the local staff have ever been threaten or harmed. The Company has an office in Bogota and its operation is 100 km SW in the Upper Magdalen a valley. InterOil transports oil daily by trucks over 200 km each way. There has never been an incident nor any disruption in this transportation. The oil is stored in tankers (onshore) and transported by pipeline over 200km to the NW. There have not been any incidents with this pipeline for the last 5 years.

Angola

Angola's economy has undergone a period of rapid transformation in recent years, moving from the disarray caused by a quarter century of war to being the fastest growing economies in Africa and in the world. Growth is almost entirely driven by rising oil production which surpassed 1.2 million barrels per day in late-2005. Control of the oil industry is consolidated in Sonangol, a conglomerate which is owned by the Angolan government. The economy grew 18% in 2005; growth is expected to reach 26% in 2006 and stay above 10% for the rest of the decade. The security brought about by the 2002 peace settlement has led to the resettlement of 4 million displaced persons, thus resulting in large-scale increases in agriculture production. With revenues booming from oil exports, the government has started to implement ambitious development programs in building roads and other basic infrastructure for the nation.

The president has announced the government's intention to hold elections in 2006. These elections would be the first since 1992 and would serve to elect both a new president and a new National Assembly.

The management and members of the Board have 20 years long relationship to Angola and Sonangol. The said board members and management have actively been involved in Angola and seen the development first hand. The oil industry has, because of well established regulatory system for oil and gas activity (PSA's) been active in the country before and after independence. The activity increased significantly in the mid 90's by the discovery of large offshore oil deposits in very deep water. Angola is today considered prime area for most oil and gas companies, although the entry ticket and the cost of establishing an operation in Angola is considered high.

2.2.3 Environmental risks

All phases of the oil business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and state and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. The discharge of oil, natural gas or other pollutants into the air, soil or water may give rise to liabilities to foreign governments and third parties and may require the Company to incur costs to remedy such discharge. No assurance can be given that environmental laws will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect the Company's financial condition, results of operations or prospects.

2.2.4 Dependence on key executives and personnel

InterOil's development and prospects are dependent upon the continued services and performance of its senior management and other key personnel. The loss of the services of any of the senior management or key personnel may have an adverse impact on InterOil.

2.3 Market risks

The marketability of any oil and gas discovered will be affected by numerous factors beyond the control of InterOil. These factors include market fluctuations, proximity and capacity of oil and gas pipelines and processing equipment, availability of transportation capacity and government regulations including regulations relating to taxation, royalties, productions levels, imports and exports and the environment, the effect of which cannot be accurately predicted.

2.3.1 Current Operating Conditions

Oil and gas commodity prices are currently high and therefore driving up the cost of oilfield goods and services worldwide and in the countries in which InterOil operates. The impact of this on InterOil's business could be a delay in activity because of, for example a lack of available drilling rigs as well as increased costs.

2.3.2 Competition

The oil and gas industry is highly competitive. There is strong competition for the discovery and acquisition of properties considered to have commercial potential. InterOil competes with other exploration and production companies, many of which have great financial resources. Joint selling of oil or gas may have serious repercussions for the sellers, including fines, invalidity of contracts and refund claims, provided such sales can be held to have affected the competitive situation in the market.

2.3.3 Oil and gas assets

InterOils' production and prospective production comes from its interests in a small number of oil and gas fields in South America. Whilst the production has been stable and existed for a long time, InterOil will remain dependent on a production from this area in the near future. Operational problems in any one field could have a materially adverse affect on InterOil. Further, the oil and gas fields from which InterOil receive its current production, are substantially under plateau production levels, and production is, in the absence of production-enhancing work, declining over time. InterOils' production originates from mature fields and licenses granted several decades ago. As such, commercial production life may exceed the period of the current license period. While in all precedent situations in

both Peru and Colombia, these licenses have been extended to allow production to continue with the same owners, there is no guarantee that this will continue to be the case. The average remaining license period is 12 years before renewal.

2.3.4 Commodity prices

The profitability and cash flow of InterOils' operations will be dependent upon the market price of oil and gas. This is known to fluctuate. Oil and gas prices are affected by numerous factors beyond InterOils' control, including economic and political conditions, levels of supply and demand, the policies of the Organisation of Petroleum Exporting Countries (Opec), currency exchange rates and the availability of alternate fuel sources. If the price of oil and gas products should drop significantly, the economic prospects of the projects in which InterOil has an interest would be significantly reduced.

2.3.5 Abandonment risk

The actual cost estimate provided for abandonment and restitution cost could differ in amount and timing and the regulations governing abandonment may be different in the future. Such differences could have an adverse impact on InterOils' business.

2.4 Forward-looking statements and future developments

This Prospectus contains forward-looking statements and information relating to the Company and its business and industry. All statements other than statements of historical facts included in this Prospectus are forward-looking statements. Words such as believe, intend, expect, anticipate, project, estimate, predict and similar expressions are intended to identify forward-looking statements. The statements are based on the Company's assumptions and beliefs in light of the information currently available.

These assumptions involve risks and uncertainties which may cause actual results, performance or achievements to be materially different form actual results or achievements expressed or implied by such forward-looking statements.

3 Responsibility Statements

3.1 Statement from the Board of Directors of InterOil Exploration and Production ASA

The Board of Directors of the Company confirms that, after having taken all reasonable care to ensure that such is the case, the information contained in the Prospectus is, to the best of their knowledge, in accordance with the facts and contains no omission likely to affect its import.

Market developments and future prospects described herein have been assessed according to the best of our knowledge and should be read in conjunction with the "Risk Factors" disclosed in Section 2 of this Prospectus.

Oslo, 17 July 2006

The Board of Directors of InterOil Exploration and Production ASA

Mårten Rød (Chairman) Gian Angelo Perrucci Robert Blair Thomas

3.2 Statement from the Manager

Pareto Securities ASA has, as sole Manager in connection with the application for Listing, at the request of, and with the co-operation of, the Board of Directors and management of InterOil, prepared this Prospectus. The assistance with regard to the preparation of the Prospectus has been based on: (i) publicly available information, (ii) discussions with the Board of Directors and management of InterOil who have also reviewed the Prospectus and verified the accuracy and completeness thereof in a separate statement to the Manager, (iii) financial due diligence conducted by the Independent Financial Advisor to the Manager, and (iv) a limited legal due diligence investigation conducted by the legal advisors (including legal counsel in Peru and Colombia) to the Manager.

Based upon such information, the Manager has endeavoured to assist InterOil to provide as accurate and complete presentation of the Company that is possible. Thommessen Krefting Greve Lund AS Advokatfirma has coordinated and performed a limited legal due diligence of InterOil and its subsidiaries on behalf of the Manager. In addition, Ernst & Young AS has performed a limited financial due diligence of InterOil.

On the basis of the above, the Manager can not accept any legal or financial liability for the completeness or accuracy of this Prospectus.

As of 17 July 2006, Pareto Securities ASA and its employees hold 90,300 Shares in InterOil.

Oslo, 17 July 2006

Pareto Securities ASA

3.3 Statement from the legal advisor to the Company

Wiersholm Mellbye & Bech AS has acted as Norwegian legal advisor to the Company in connection with the Listing of the Company's Shares on Oslo Børs.

We have reviewed the information regarding Norwegian legal matters contained in chapter 13 (Tax Issues) of this Prospectus. On the basis of the information presented to us, it is our view that the said chapters give a fair and balanced description of the Norwegian legal matters described therein.

Our statement is limited to the above and does not extend to the content of other chapters of the Prospectus or to any descriptions of commercial, financial, accounting or technical matters contained in the Prospectus. Our statement is limited to matters of Norwegian law.

Oslo, 17 July 2006

Wiersholm, Mellbye & Bech, advokatfirma AS

4 Key Information

4.1 Purpose of Listing

The contemplated Listing of the Shares on Oslo Børs is an important element of the Company's strategy. Through a Listing, the Company will be able to provide a regulated marketplace for the trading of its Shares. Moreover, the Listing will facilitate the use of the capital markets in order to raise further equity, and will increase the attractiveness of the Shares as consideration in possible future acquisitions and/or mergers.

4.2 Working capital statement

In InterOil's opinion, the working capital is sufficient to support its present requirements.

4.3 Capitalisation and indebtedness

The following table shows the Company's capitalisation as of 31 December 2005 and 31 March 2006, being the last disclosed financial statements of the Company.

(USD 1,000)	**31 March 2006**	**31 December 2005**
Share capital	157	157
Share premium reserve	43,417	43,417
Other reserves	3,096	3,096
Retained earnings	883	276
Shareholders' equity	**47,553**	**46,946**
Total current debt:		
Guaranteed	-	-
Secured	-	-
Unguaranteed/unsecured	16,562	20,807
Total non-current debt		
Guaranteed	-	-
Secured	35,507	35,135
Unguaranteed/unsecured	22,399	21,971
Total indebteness	**74,468**	**77,913**
Total capitalisation	**122,021**	**124,859**
Cash	7,189	8,437
Cash equivalents	-	-
Trading securities	8,016	10,901
Liquidity	**15,205**	**19,338**
Current bank debt	-	-
Current portion of non current debt	-	-
Other current financial debt	6,000	6,000
Current financial indebtedness	**6,000**	**6,000**
Non current bank loans	35,507	35,135
Bonds issued	-	-
Other non current loans	**35,507**	**35,135**
Non current financial indebtedness	**35,507**	**35,135**
Net financial indebtedness	**26,302**	**21,797**

The table above should be read in conjunction with the Company's consolidated financial statements and the related notes thereto.

There has been no material changes since the date of InterOil's last published information, except for the issuance of the Senior Unsecured Bond Loan described under section 6.7.3 below.

4.4 Third party statements

The information in this Prospectus that has been sourced from third parties has been accurately reproduced and, as far as the Company is aware and able to ascertain from the information published by that third party, no facts have been omitted that would render the reproduced information inaccurate or misleading.

5 The Listing

5.1 Purpose of and background for the Listing

The Listing is an important element of the Company's strategy. Through the Listing, InterOil will be able to access a regulated marketplace for the trading of the Shares. Moreover, the Listing will provide the Company with improved access to the capital markets for the purpose of raising further equity, if and when required. The Listing is further expected to increase the attractiveness of the Shares as consideration in possible further acquisitions of and/or mergers with other companies.

5.2 Admission to trading and dealing arrangements

On 23 May 2006, the Company submitted an application to Oslo Børs for the Listing. The Listing comprises all of the outstanding Shares in the Company, being 21,245,000 Shares each with a par value of NOK 0.05 per Share.

The Board of Directors of Oslo Børs approved the Listing in a board meeting held on 22 June 2006. The Shares will be listed on the SMB list and are expected to trade in round lots ("børspost") of 200 Shares under the ticker symbol "IOX". It was a condition to the Listing that the Company publishes a listing prospectus approved by Oslo Børs and that the Company obtained additional funding in the amount of USD 20 million before Listing. Both of these requirements have been met.

Since 6 October 2005, the Shares have been publicly traded on the Norwegian OTC market under the ticker INOX.

5.3 Lock-up agreement

The Manager has entered into lock-up agreements with the Company's main shareholders Eksportconsult AS and Force Capital Partners with respect to all shares held by said companies. Under the lock-up agreement, the main shareholders will agree not to offer, sell, contract or otherwise dispose of shares in the Company for a period of 8 months following the first day of trading of the shares on Oslo Børs, without the prior written consent of the Manager.

5.4 VPS registration

The Company's Shares are registered in the VPS under the securities number ISIN NO 001 0284318. The registrar is DnB NOR Bank ASA.

5.5 Manager

The Manager of the Listing is Pareto Securities ASA.

The Manager address is Pareto Securities ASA, P. O. Box 1411Vika, N-0115 Oslo Norway.

5.6 Expected costs related to the Listing

Transaction costs and all other directly attributable costs in connection with the Listing will be borne by the Company. The total costs related to the Listing are expected to amount to approximately NOK 2 million (exclusive of VAT).

6 Selected Financial Information

6.1 Consolidated financial statements

Annual reports including audited historical financial information and audit reports in respect of 2005 may be found at the Company's website www.interoil.no and information published after 23 May 2006 at www.newsweb.no under the ticker "IOX". The financial statements have been audited by InterOil's statutory auditor, PricewaterhouseCoopers AS, see Section 6.2.3 for further information.

The Company's annual report for 2005 is enclosed as Appendix 2 and the Company's unaudited condensed consolidated interim financial information for the first quarter 2006 is enclosed as Appendix 3.

6.1.1 Basis for preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and correspond with the interpretation of the International Standards Board. The consolidated financial statement is presented in USD and is rounded up to thousands (1,000). The consolidated financial statements have been prepared under the historical cost convention, except for financial assets at fair value through profit or loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4 to the consolidated financial statements as of 31 December 2005 (see Appendix 2).

The Group has implemented IFRS 6, Exploration for and Evaluation of Mineral Resources. The standard requires the use of successful effort method of accounting which has been implemented by the Group. IFRS 6 also requires the Group to disclose certain information which has been implemented in the disclosure to the consolidated financial statements.

On 27 September 2005, InterOil acquired 100% of the shares of Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I. (subsidiaries in Peru and Colombia), all oil companies operating in Latin America. The subsidiaries are fully consolidated from the date on which control is transferred to the Group.

The unaudited pro forma income statement shown in chapter 6.2 for the year ended 31 December 2005 illustrates the effect of the acquisition as if the acquisition occurred on 1 January 2005. The unaudited pro forma statements and thefinancial information were prepared in accordance with IFRS.

The Group's activities in Peru and Colombia are the result of the acquisition of assets previously owned by the oil exploration company Mercantile International Petroleum Inc. ("MIPI"). MIPI owned the shares of Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I. MIPI prepared consolidated financial statements in 2003 and 2004 in accordance with Canadian GAAP, see enclosed appendix 5 and 6 to the prospectus.

The main difference in accounting policies is that MIPI in 2003 and 2004 used full costing while InterOil in 2005 used successful efforts costing in the annual accounts and proforma income statements in accordance with IFRS. The principal difference between full costing and successful efforts costing concerns costs that cannot be directly related to the discovery of specific oil reserves. Under full cost those costs are carried forward to future periods as costs of oil reserves generally, under successful efforts costing those costs are charged to expense.

MIPI's holding costs are included in the 2003 and 2004 financial statements. Finance cost in 2003 and 2004 is based on MIPI's financing of the subsidiaries who is not comparable with InterOils finance costs after the acquisition of the companies in 2005.

The historical financial statements for 2003, 2004 and 2005 are not comparable, and these financial statements should be read in conjunction with the accounting policies described in the financial statements for each year.

6.1.2 Accounting policies

The principal accounting policies applied in preparation of these consolidated financial statements are set out below. These policies have been consistently applied to the periods presented.

Consolidation

Subsidiaries

Subsidiaries are all entities over which the Group that has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases. All subsidiaries have been incepted by the parent company.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. Any excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill if applicable.

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

Consolidated subsidiaries

Consolidated subsidiaries are specified in note 26 to the consolidated financial statements as of 31 December 2005 (see Appendix II).

Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in USD, which is the functional currency for the parent company and all subsidiaries and the presentation currency for the Group.

b) Transactions and balances

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

Exploration and production rights asset

Oil and natural gas exploration and evaluation expenditures are accounted for using the successful efforts method of accounting. Costs are accumulated on a field-by-field basis. Geological and geophysical costs are expensed as incurred. Costs directly associated with an exploration well, and exploration and property leasehold acquisition costs, are capitalised until the determination of reserves is evaluated. If the commercial discovery has not been achieved, these costs are charged to expense.

Capitalisation is made within property, plant and equipment according to the nature of the expenditure.

Once commercial reserves are found, exploration and evaluation assets are tested for impairment and transferred to development tangible and intangible assets. No depreciation and/or amortisation is charged during the exploration and evaluation phase.

Development assets

Expenditure on the construction, installation or completion of infrastructure facilities such as production equipment, pipelines and the drilling of commercially proven development wells is capitalised within tangible assets. When development is completed on a specific field, it is transferred to production assets. No depreciation and/or amortisation is charged during the development phase.

Oil production assets

Oil and gas properties are aggregated exploration, production rights assets and development expenditures associated with the production of proved reserves. Furthermore, the oil production assets include property leasehold acquisition costs directly attributable to production assets.

Depreciation and amortization

Oil assets that are purchased are depreciated and amortised using the unit-of-production method based on proved reserves. Exploration and development assets transferred to production assets are depreciated and amortised using the unit of production method based on proved developed reserves, which are oil mineral reserves estimated to be recovered from existing facilities using current operating methods.

Impairment – production right, exploration and development assets

Production right, exploration and development assets are tested for impairment when reclassified to development assets or whenever facts and circumstances indicate impairment. An impairment loss is recognised for the amount by which the assets' carrying amount exceeds their recoverable amount. The recoverable amount is the higher of the assets' fair value less costs to sell and their value in use. For the purposes of assessing impairment, the assets subject to testing are grouped with existing cash-generating units (CGUs) of production fields that are located in the same geographical region.

Impairment – oil production assets

Oil production assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The 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, the proved oil and gas properties subject to testing are grouped with existing cash-generating units (CGUs) of production fields that are located in the same geographical region.

Other property, plant and equipment

All other property, plant and equipment is stated at historical cost less depreciation. Historical cost include expenditures that is directly attributable to the acquisition of the items. Depreciation is calculated using the straight-line method to allocate their cost to their values over their estimated useful lives. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

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

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

Financial assets at fair value through profit or loss

A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Changes in fair value of such derivatives are recognised within operating income (loss) in the income statement.

Trade receivables

Trade receivables are recognised initially at fair value less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

Inventories

Inventories are valued using the First-In-First-Out principle. Inventory cost includes raw material, freight, and direct production expenses together with a portion of indirect expenses.

Cash and cash equivalents
Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less. All cash and cash equivalents not available to the Group at the balance sheet date is classified as restricted as specified in note 17 to the consolidated financial statements as of 31 December 2005 (see Appendix 2).

Share capital
Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Borrowings
Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method. The fair value of the liability portion of a convertible bond is determined using a market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortized cost basis until extinguished on conversion or maturity of the bonds. The remainder of the proceeds is allocated to the equity element of the financing agreement, i.e. the warrants. The equity element is recognized and included in shareholders' equity, net of income tax effects. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Deferred income tax
Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting, nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

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

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Provisions

General:
A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of past event and it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

Abandonment and decommissioning liabilities:
In accordance with the terms of the license concessions for licenses where the Group has ownership interest, the local authorities may instruct the license holders to partly or completely remove the facilities at the end of production or when the concession period expires. Upon initial recognition of a liability, the company calculates and records the net present value related to future abandonment and decommissioning. The same amount is capitalised as part of the cost price of the asset and depreciated using the unit of production method. The change in the time value of the liability related to the abandonment and decommissioning is charged to expense as other expenses and increases the future liability related to the abandonment and decommissioning. Any change in the estimate related to expenditures associated with abandonment and decommissioning liabilities are accounted for prospectively (remaining production) based on the unit of production method.

Revenue recognition
Sales revenue related to sale of oil is recognised when the ownership rights are transferred to the customer at the time of delivery based on contractual terms in the sales agreements. Royalty payments are excluded from total sales reported by the Group.

Leases
Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

Earnings per share
Basic earnings per share are calculated by dividing the net profit for the period attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

For the purpose of calculating diluted earnings per share, the net profit attributable to ordinary shareholders and the weighted average number of shares outstanding are adjusted for the effects of all dilutive potential ordinary shares from exercise of stock options. Stock options are deemed to have been converted into ordinary shares on the date when the options were granted. When net profit is negative, the dilutive instruments described above will have an anti dilutive effect when calculating dilutive earnings per share.

6.1.3 Consolidated income statements

Amounts in USD 1 000 unless otherwise stated	**For the three months period ended 31 March 2006**	**For the period from 2 May 2005 (inception) to 31 December 2005**
	(Unaudited)	
Sales	8,641	7,991
Cost of goods sold	-3,438	-3,240
Gross profit	**5,203**	**4,751**
Tariffs and transportation	-133	-204
Exploration cost expensed	123	-783
Administrative expense	-1,905	-1,501
Other income	105	181
Other operating expenses	-8	-143
Profit from operating activities	**3,385**	**2,301**
Finance costs – net	-1,340	-1,522
Profit before income tax	**2,045**	**780**
Income tax expense	-1,438	-503
Net profit	**607**	**276**
Earnings per share for profit attributable to the equity holders of the Company during the period (expressed in USD per share)		
– basic	0.03	0.04
– diluted	0.03	0.04

6.1.4 Consolidated balance sheet

Amounts in USD 1 000	As of 31 March 2006	As of 31 December 2005
	(Unaudited)	
ASSETS		
Non-current assets		
Property, plant and equipment	100,799	97,911
Deferred income tax assets	689	689
Total non-current assets	**101,489**	**98,600**
Current assets		
Inventories	617	493
Trade and other receivables	4,709	6,428
Financial assets at fair value of profit or loss	8,016	10,901
Cash and cash equivalents	7,189	8,437
Total current assets	**20,531**	**26,259**
TOTAL ASSETS	**122,021**	**124,859**
EQUITY		
Share capital and share premium	43,574	43,574
Other reserves	3,096	3,096
Retained earnings	883	276
Total equity	**47,553**	**46,946**
LIABILITIES		
Non-current liabilities		
Interest-bearing loan	35,507	35,135
Deferred income tax liabilities	21,445	21,042
Provisions for other liabilities and charges	954	929
Total non-current liabilities	**57,906**	**57,105**
Current liabilities		
Trade and other payables	8,993	12,902
Income tax liabilities	1,405	1,166
Subordinated loan, related parties	6,000	6,000
Current interest-bearing liabilities	64	639
Provisions for other liabilities and charges	100	100
Total current liabilities	**16,562**	**20,807**
Total liabilities	**74,468**	**77,913**
TOTAL EQUITY AND LIABILITIES	**122,021**	**124,859**

6.1.5 Consolidated cash-flow statement

Amounts in USD 1 000	For the three months period ended 31 March (Unaudited)	For the period from 2 May 2005 (inception) to 31
Cash generated from operations		
Profit for the period	607	276
Income tax expense	1,438	503
Depreciation and amortization	2,341	1,800
Interest received from financial assets at fair value through profit or loss	-105	-181
Amortization of debt issuance cost and equity component	260	260
Interest expense	1,206	1,206
Changes in assets & liabilities		
Inventories	-124	63
Trade and other receivables	1,719	613
Trade and other payables	-846	2,702
Other provision for other liabilities	25	147
Interest paid	-1,269	-230
Taxes paid	-796	-799
Net cash generated from operating activities	**4,455**	**6,360**
Cash flows from investing activities		
Acquisition of subsidiaries, net of cash acquired and selling credit	-	-65,580
Purchases of property, plant and equipment (PPE)	-5,230	-3,604
Other financial assets at fair value through profit or loss	2,989	-10,720
Net cash used in investing activities	**-2,240**	**-79,904**
Cash flows from financing activities		
Proceeds from issuance of ordinary shares (excluding tax effect)	-	42,996
Proceeds from issuance of interest-bearing loan inclusive equity	112	39,175
Repayment of interest bearing debt	-575	-190
Repayment of selling credit	-3,000	
Net cash used in financing activities	**-3,463**	**81,981**
Net increase in cash and cash equivalents	**-1,248**	**8,437**
Cash and cash equivalents at beginning of the period	**8,437**	**0**
Cash and cash equivalents at end of the period	**7,189**	**8,437**

6.1.6 Financial key figures

	For the three months period ended 31 March 2006	For the period from May 2 (inception) to 31 December 2005
All amounts in USD		
Dividends per share (USD)	-	-
Book equity per share (end of period) (USD)	2.24	2.21
Earnings per share (weighted average) (USD)	0.03	0.04
Equity ratio (%) end of period	39.0%	37.6%
Net operating margin before depreciation	66.3%	51.3%
Return on equity	1.3%	0.6%
Number of employees	134	130

6.1.7 Consolidated interim statement of changes in equity

The table below shows the consolidated interim statement of changes in equity for the period from 2 May 2005 (inception) to 31 March 2006.

Amounts in USD 1 000	Share capital and share premium	Other reserves	Retained earnings	Total equity
Inception on 2 May 2005	16	-	-	16
Issue of share capital, net of share issuance cost 15 September 2005	63	-	-	63
Issue of share capital, net of share issuance cost 30 September 2005, net of tax	43 495	-	-	43 495
Equity component interest bearing debt, net of tax	-	3 096	-	-
Net profit for the period	-	-	276	276
Balance at 31 December 2005	**43 574**	**3 096**	**276**	**46 946**
Net profit for the period (unaudited)	-	-	607	607
Balance at 31 March 2006 (unaudited)	**43 574**	**3 172**	**883**	**47 553**

6.2 Pro forma financial statements

6.2.1 Basis for preparation

On 27 September 2005, InterOil acquired 100% of the shares of Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I. (subsidiaries in Peru and Colombia), all oil companies operating in Latin America. The following unaudited pro forma income statement data for the year ended 31 December 2005 illustrates the effect of the acquisition as though the acquisition had occurred on 1 January 2005.

The unaudited pro forma combined financial information was prepared in accordance with IFRS. The information and table presented below should be read in conjunction with the audited consolidated financial statements of the Company as included elsewhere in this prospectus. The unaudited pro forma financial information has been prepared on the basis of assumptions and adjustments explained below. The pro forma information does not necessarily show the results that would have actually been obtained if the acquisition had been executed on 1 January 2005 and has been prepared for illustrative purposes only. Because of its nature, the pro forma financial information addresses a hypothetical situation and, therefore, does not represent the company's actual financial position or results.

The pro forma financial information below has been prepared on the basis of the following assumptions:

- Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I. were acquired on 27 September 2005, but have been included in the pro forma financial information as though the acquisition had occurred on 1 January 2005.
- The cost price for the acquisition was USD 77 490. For the purpose of presenting the pro forma financial information, the same cost price has been used as of 1 January 2005 which means that the fair value of the companies described above have been kept constant throughout the pro forma period.
- Excess value for the acquired business has been fully allocated to property, plant and equipment as of 1 January 2005 which is consistent with the allocation made on 27 September 2005.
- The column named Subsidiaries in Peru and Colombia as presented in the table below for the pro forma period from 1 January 2005 to the acquisition date is based on the acquired companies historical financial information conformed into the Company's IFRS accounting policies including the use of successful efforts method.
- For the companies included in the InterOil consolidated financial statements as of 31 December 2005 other than the Subsidiaries in Peru and Colombia, pro forma consolidated income statement data have been based on historical transactions only, i.e. no adjustments have been made.

The following table shows the adjustments that have been made to the income statement data for the year ended 31 December 2005 to prepare the pro forma income statements data included elsewhere in this prospectus.

6.2.2 Income Statement Data

	Consolidated income statement for the period from 2 May (inception) to 31 December 2005	Subsidiaries in Peru and Colombia for the pro forma period from 1 January to the acquisition date	Pro forma Adjustments	Pro forma consolidated income statement data
Amounts in USD 1,000	**(Audited)**	**(Audited)**	**(Unaudited)**	**(Unaudited)**
Sales	7,991	21,271	-	29,262
Cost of goods sold	-3,240	-6,381	(i) -2,802	-12,423
Gross profit	**4,751**	**14,890**	**-2,802**	**16,839**
Tariffs and transportation	-204	-650	-	-854
Exploration cost expensed	-783	-248	-	-1,031
Administrative expense	-1,501	-1,396	-	-2,897
Other income	181	10	-	191
Other operating expenses	-143	-378	-	-521
Profit from operating activities	**2,301**	**12,228**	**-2,802**	**11,727**
Finance costs – net	- 1,522	-212	(ii) -3,584	-5,318
Profit before income tax	**780**	**12,016**	**-6,386**	**6,409**
Income tax expense	-503	-3,599	(iii) 908	-3,194
Net profit	**276**	**8,417**	**-5,478**	**3,215**

The pro forma financial information below has been prepared on the basis of the following adjustments:

(i) InterOil is using the unit-of-production method to calculate depreciation and amortization. In order to calculate depreciation and amortization during the pro forma period, production volumes in the pro forma period have been added to proven reserves for the individual fields at the beginning of the pro forma period. Deprecation and amortization for oil related assets have been calculated based on actual

production during the year ended 2005. Depreciation and amortization is based on the allocated excess value for the purchase allocation only. Please see assumptions described above for further information.

(ii) Finance costs have been calculated assuming that the TCW Loan (referred to in Section 6.7.1 below) incurred to finance the acquisition, had been issued on 1 January 2005. It has also been assumed that the effective interest rate on the TCW Loan for the year ending 2005 is the same as for the period presented in the consolidated financial statements.

(iii) Tax effects on pro forma adjustments have been calculated using the nominal tax rates in the applicable countries. The company has not made any deferred tax adjustments regarding the financial expense adjustments described above since it has been assumed that the finance expense would result in tax losses carry forwards that would not qualify for being capitalised as deferred tax assets.

6.2.3 Auditors statement

The following statement has been received from the Company's auditor, PricewaterhouseCoopers AS:

"We have examined the pro forma adjustments reflecting the transaction described in chapter 6.2 in the prospectus and the application of these adjustments to the historical financial information in preparation of unaudited pro forma consolidated income statement data for the year ended 31 December 2005.

The unaudited pro forma consolidated income statement data for the year ended 31 December 2005 is prepared on the basis of audited consolidated financial statements for InterOil Exploration and Production ASA and subsidiaries. It is our responsibility to provide the opinion required by the Norwegian Securities Trading Act and accompanying regulation. We are not responsible for expressing any other opinion on the pro forma consolidated income statement date or on any of its constituent elements.

We conducted our examination in accordance with the Norwegian Auditing standard RS 800 "The Auditor's report on special purpose audit engagements". Our work consisted primarily of comparing the unadjusted financial information with the source documents, obtaining evidence supporting the adjustments and discussing the pro forma financial information with the management of the Company. We believe that our examination provides a reasonable basis for our opinion.

The objective of the pro forma financial information is to present what the most significant effects on the historical financial information might have been, had the transaction occurred at an earlier date. However, the pro forma financial information is not necessarily indicative of the financial position and the result of the operations that would have been attained, had the above mentioned transaction actually occurred earlier. The pro forma financial information is not intended to provide, nor does it provide, all information and additional information required to express InterOil Exploration and Production ASA's consolidated financial position and result in compliance with International Financial Reporting Standards (IFRS) as adopted by EU.

Based on our examination, in our opinion the unaudited pro forma financial information has been properly compiled on the basis stated and that basis is consistent with the accounting policies of the issuer.

Oslo, 26 May 2006

PricewaterhouseCoopers AS

Fredrik Melle

State Authorised Public Accountant (Norway)"

6.3 Segment Information

The groups only business segment to date has been the production and sale of oil. The Group's oil activity today is based in Colombia and Peru. In Norway and Switzerland it has been some holding activities, and the Group has expansion plan in West Africa.

6.3.1 Income statement information

For the three months ended 31 March 2006 (Unaudited)

Amounts in USD 1 000	Colombia	Peru	Total report. segm.	Unalloc./ elimin.	Group
Sales	3,235	5,406	8,641	-	**8,641**
Cost of goods sold	-1,450	-1,988	-3,438	-	**-3,438**
Gross profit	**1,785**	**3,418**	**5,203**	**-**	**5,203**
Tariffs and transportation	-133	-	-133	-	**-133**
Exploration cost expensed	123	-	123	-	**123**
Administrative expense	-150	-400	-550	-1,355	**-1,905**
Other income	-	-	-	105	**105**
Other operating expenses		-8	-8	-	**-8**
Profit from operating activities	**1,624**	**3,010**	**4,635**	**- 1,250**	**3,385**
Finance costs – net	-33	21	-12	-1,328	**-1,340**
Profit before income tax	**1,591**	**3,031**	**4,623**	**-2,578**	**2,045**
Income tax expense	-595	-874	-1,469	31	**-1,438**
Net profit	**997**	**2,157**	**3,154**	**-2,547**	**607**

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	Colombia	Peru	Total report. Segm.	Unalloc./ elimin.	Group
Sales	3,346	4,645	7,991	-	**7,991**
Cost of goods sold	-1,505	-1,735	-3,240	-	**-3,240**
Gross profit	**1,841**	**2,910**	**4,751**	**-**	**4,751**
Tariffs and transportation	-204	-	-204	-	**-204**
Exploration cost expensed	-783	-	-783	-	**-783**
Administrative expense	-155	-469	-625	-876	**-1,501**
Other income	-	-	-	181	**181**
Other operating expenses	-15	-28	-43	-100	**-143**
Profit from operating activities	**684**	**2,412**	**3,096**	**-795**	**2,301**
Finance costs – net	-55	18	-37	-1,485	**-1,522**
Profit before income tax	**629**	**2,431**	**3,060**	**-2,280**	**780**
Income tax expense	-262	-817	-1,079	575	**-503**
Net profit	**367**	**1,614**	**1,981**	**-1,705**	**276**

6.3.2 Balance sheet information

As of 31 December 2005

	Colombia	Peru	Total report. segm.	Unalloc./ elimin.	Group
Property, plant and equipment	34,779	63,072	97,851	60	**97,911**
Other assets	3,923	9,214	13,137	13,811	**26,948**
Total segment assets	**38,702**	**72,285**	**110,988**	**13,871**	**124,859**
Total segment liabilities	**11,517**	**19,989**	**31,506**	**46,407**	**77,913**

6.3.3 Other segment information (Unaudited)

Production and sales for the three months ended 31 March 2006

	Colombia	Peru	Total
Sale in barrels – net			
Sale of oil, barrels	61,000	91,129	152,129
Total sale in barrels – net	**61,000**	**91,129**	**152,129**
Production in barrels – net			
Working interest, barrels	81,373	164,048	245,421
Royalty	12,265	72,919	85,184
Total production in barrels – net of royalty	**69,108**	**91,129**	**160,237**

Production and sales for the period from 1 October 2005 to 31 December 2005

	Colombia	Peru	Total
Sale in barrels – net			
Sale of oil, barrels	69,000	85,684	154,684
Total sale in barrels – net	**69,000**	**85,684**	**154,684**
Production in barrels – net			
Working interest, barrels	71,955	149,412	221,367
Royalty	13,390	63,728	77,118
Total production in barrels – net of royalty	**58,565**	**85,684**	**144,249**

6.4 Capital resources

Since its incorporation, the Company has raised approximately USD 87 million before share and debt issuance cost through issuing new Shares and incurring the TCW Loan referred to below, and these funds have financed the Company's commitments and liabilities.

As of 31 March 2006, the Company had cash, cash equivalents and marketable securities of NOK 15.2 million.

The Company believes that its current capital resources together with the proceeds from the Bond Issue, will be sufficient to fulfil commitments referred to under the section 6.5 “Investments” and 6.8 “Property, Plants and Equipment”. The adequacy of available funds will depend on many factors, including the further growth of the business, capital expenditures, market development, competition and potential acquisitions. Accordingly, the Company may require additional funds and seek to raise such funds through issuing new equity or debt.

6.5 Investments

On 27 September 2005, the Group acquired 100% of the shares capital of Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I. all oil companies operating in Latin America. The consideration for all outstanding shares, including direct acquisition costs, amounted to USD 77.5 million.

Capitalized expenditures in 2005 after the acquisition of subsidiaries amounted to USD 3.6 million and capitalised expenditures in the first quarter of 2006 were 5.2 million.

6.6 Related party transactions

Eksportconsult AS has a management agreement with InterOil relating to the business development in the Company. Eksportconsult AS is paid USD 20,000 (excl. VAT) per month for these services which primarily include to seek out new business opportunities for the Company worldwide. Eksportconsult AS is required to work at least 20 man-days per month. Eksportconsult AS is owned by the Chairman of the Board of Directors, Mårten Rød, and his immediate relatives. The management agreement between Eksportconsult AS and the Company has been approved by the Company's Board of Directors. The agreement may be terminated by either party with three months prior notice.

Caberian Investment Limited has previously had a management agreement with InterOil relating to business development in the Company. Caberian Investment Limited was paid USD 10,000 (excl. VAT) per month for the services of Gian Angelo Perrucci which primarily included development of the Company's activities in Africa, of which Mr. Perrucci has important knowledge and experience. The management agreement between Caberian Investment Limited and the Company is per this date terminated.

The Company is of the opinion that the management agreement described above is relatively common internationally, and the fees paid are at the low end of the international consultancy market. The Company's fees for consultants used in the international market are today between USD 1,500 – 2,500 per day, depending on experience. InterOil is paying Eksportconsult USD 1,000 per day as defined in the contract described above.

The Company has previously been party to a management agreement with Force Capital Partners AS under which the services of Nils Trulsvik as CEO were provided to the Company.

InterOil has purchased office furniture and equipment from Eksportconsult AS.

The above agreements have been concluded at estimated market terms.

The Company is not party to any other transactions with any related party as defined in the Stock Exchange Regulation § 2-3 other than internal agreements with subsidiaries entered into in the ordinary course of business and on an arm's length basis.

Please see note 5 to the consolidated financial statements as of 31 December 2005 for further information (Appendix 2).

6.7 Debt obligations

6.7.1 TCW Loan – USD 42 million

In September of 2005 the Company borrowed an interest-bearing loan in the original principal amount of USD 42 million from certain investment funds managed by TCW Asset Management Company ("**TCW**"). The Company is in the process of assigning this loan (the "**TCW Loan**") to its wholly-owned subsidiary, InterOil Exploration and Production Latin America AS ("**InterOil Latin America**") meaning that the rights and obligations, including the covenants, will be applicable to InterOil Latin America and its subsidiaries. The TCW Loan has been fully drawn, and has a final maturity date occurring in October, 2012. The TCW Loan bears interest at a fixed interest rate of 9%, or 11% if the loan is in default. Interest and principal are payable quarterly on the TCW Loan, but principal payments do not begin until October, 2008. Principal payments must be made in an amount equal to the greater of a minimum scheduled amount and an amount derived from a formula, based on available net cash flow after the payment of operating expenses and debt service. In some cases, all available net cash flow is dedicated for application to the loan's principal repayment. The TCW Loan may be prepaid at any time upon advance notice, so long as such prepayment is accompanied by a specified prepayment fee. The TCW Loan is secured by a pledge by the Company of all stock owned by the Company in InterOil Latin America, as well as the stock and assets of certain other direct and indirect subsidiaries of InterOil Latin America, including a pledge of all cash flow earned in the operations of InterOil Latin America and its direct and indirect subsidiaries. The agreements documenting the TCW Loan contain a series of affirmative and negative covenants, representations and warranties, customary for loans of this type. The key financial covenants are:

- The collateral coverage ratio shall be at least 150%, calculated as the quotient of the net present value of the future net revenues expected to accrue to the interests of the expected production from the specified operations during the remaining expected lives of such operations plus positive working capital and cash reserves over the sum of the outstanding obligations under the notes plus any past due payments owing for thirty days or more under the TCW Loan plus the absolute value of the working capital (if negative).

- The Company shall maintain a current ration of at least 1.0:1.0, based on current assets to current liabilities determined on a consolidated basis under GAAP.
- Restrictions on incurring or making payments of debt, unless approved by TCW.
- No mergers or creation of subsidiaries unless approved by TCW.
- Requirements with respect to working capital balance, at least USD 8,000,000.
- Limitations to the issuance of capital stock. The Company is not allowed to issue any voting or non-voting shares to any party unless approved by TCW, and if such approval has been granted the issued shares shall be pledged to the collateral agent. We have been informed that this covenant has been waived.

If the covenants are not performed or maintained as true and correct, this may lead to a default and the right of the TCW Loan lenders to foreclose on the pledged assets, thereby denying the Company access to the cash flow it would otherwise receive from the operations of InterOil Latin America and its direct and indirect subsidiaries. There are other events of default specified in the TCW Loan documents, as well. Following the assignment of the TCW Loan, the covenants in the TCW Loan documents will apply principally to InterOil Latin America and its subsidiaries and not the Company.

In order to induce the TCW Loan lenders to advance the TCW Loan to the Company, the Company granted the TCW Lenders an assignable Overriding Royalty Interest (the "**TCW Royalty**") in respect of its operations, which only becomes effective if the Company does not undertake an IPO by a prescribed date. The TCW Loan lenders have also been granted warrants (together, the "**TCW Warrant**"), entitling them to purchase stock in the Company. These subscription rights are further described in section 10.3.

6.7.2 Maxi Assets Inc. – USD 6 million

The Company has a subordinated interest bearing debt amounting to USD 6 million to Maxi Assets Inc. (Panama) relating to the acquisition of the assets in Peru and Colombia. The interest rate is Libor + 2%. The loan agreement does not include any covenants.

6.7.3 Senior Unsecured Bond Loan – USD 20 million

On 11 July 2006 the Company issued a senior unsecured bond loan with a total loan amount of USD 20 million. The bond loan has term of 5 years and will expire on 11 July 2011. The coupon is a fixed rate of 9.00 per cent per annum on the basis of a 360 day year consisting of 12 months of 30 days, with interest in respect of any part of an uncompleted such month being determined on the basis of a 30 day month less the remaining number of calendar days in the month.

The Bonds have a nominal value of USD 1,000.

The Bonds rank at least *pari passu* with all other senior obligations of the Issuer other than obligations which are mandatory preferred by law. The Bonds shall rank ahead of subordinated capital. The Bonds are not be secured by any mortgage, pledge or other security.

6.8 Property, plants and equipment

	Production rights assets	Exploration assets	Develop. Assets	Oil production assets	Other	Total
Period ended 31 December 2005						
Opening net book amount	-	-	-	-	-	-
Acquisitions of subsidiaries	2,607			91,917	1,582	96,107
Additions		2 770	1,541		76	4,311
Transfers		-1 987		1,987		0
Exploration cost expensed		-783				-783
Depreciation charge				-1,773	-27	-1,800
Closing net book amount	**2,607**	**0**	**1,541**	**92,131**	**1,631**	**97,911**
At 31 December 2005						
Cost or valuation	2,607	0	1,541	93,904	1,658	99,711
Accumulated depreciation	-	-	-	-1,773	-27	-1,800
Net book amount	**2,607**	**0**	**1,541**	**92,131**	**1,631**	**97,911**

The following assets have been pledged for the benefit of the lenders of the TCW Loan as security for the TCW Loan, the TCW Warrant and the TCW Royalty (see note 20 to the 2005 consolidated financial statements):

- All the stock of InterOil Latin America AS owned by the Company
- Certain bank accounts and money market funds owned by InterOil Latin America, into which the cash proceeds of its operations are deposited (and which cash proceeds are also pledged for the benefit of the lenders of the TCW Loan).
- All shares of stock owned by InterOil Latin in each of its operating subsidiaries undertaking oil and gas exploration and production in Peru and Colombia
- Certain assets owned by the operating subsidiaries of InterOil Latin America.
- The Maxi Assets loan and the Senior Unsecured Bonds, both referred to above, are each unsecured.

6.9 Significant change in the Company's financial or trading position

The Company is not aware of any significant changes in the financial or trading position of the InterOil Group which have occurred since the end of 31.12.2005.

6.10 Statutory Auditor

The Company's auditor is PricewaterhouseCoopers AS ("PwC"), org. no. 987 009 713, with its address Karenslyst Allè 12, 0278 Oslo, Norway. PwC has been the company's auditor since November 2005. PwC is a member of The Norwegian Institute of Public Accountants. PwC has audited the financial statements presented in this Prospectus.

The Company has not received any comments or remarks in the auditor's statements for these years. PwC is also auditor for the Company's subsidiaries in Peru and Colombia.

The Company was incorporated as a shelf company in May 2005, with BDO Revico Sandvika DA, Hamangskogen 60, 1338 Sandvika, Norway, org. no. 984 098 243, as its auditor. BDO Revico Sandvika DA was later replaced by Kjelstrup & Wiggen AS, Drammensveien 6, 0255 Oslo, org. no. 983 953 328. None of them has audited any of the financial statements presented in this Prospectus.

7 Description of InterOil

7.1 Overview

InterOil is an upstream oil exploration and production company focused on South America and Africa. The Company currently has oil exploration activities in Peru and Colombia and is in the process of establishing operations in West Africa. Please refer to Section 7.4.3 below for further details.

The Company was established on 2 May 2005 as a Norwegian Private Limited Company ("AS"). It was transformed to a Norwegian Public Limited Company ("ASA") on 14 November 2005. The Company is registered in the Register of Business Enterprises with org. no: 988 247 006. The Company's registered office is Strandveien 50, 1366 Lysaker, tel: (+47) 6751 86 50.

The Company's shares are currently not listed on any stock exchange, but the shares are registered on the OTC-list managed by the Norwegian Securities Dealers Association under the ticker "INOX".

7.2 History

The Company's activities in Peru and Colombia are the result of the acquisition of several companies purchased from the oil and gas company Mercantile International Petroleum Inc. ("**MIPI**"). MIPI was listed in Canada in the mid 90-ies, but experienced financial difficulties in 2001/2002 and started a process for sale of its oil exploration activities in Peru and Colombia in late 2004. Negotiations for the acquisition of MIPI's operating companies in Peru and Colombia started in September 2004, and were made effective on 27 September 2005. On the 9 of June 2005 InterOil entered into a Sales and Purchase Agreement with MIPI.

InterOil raised a total of USD 87 million dollars through a USD 45 million equity issue and the TCW Loan (in the amount of USD 42 million prior to the acquisition of the assets on 27 September 2005. Net proceeds from these transactions after share issuance costs and debt issuance costs were USD 83 million.

During 2006, the oil production from the Company's subsidiaries has increased substantially from approximately 2,400 bbl/d to approximately 3,400 bbl/d as per mid-April 2006. The assets in Peru produce approximately 2,400 bbl/d, while the Colombian assets produce approximately 1,000 bbl/d.

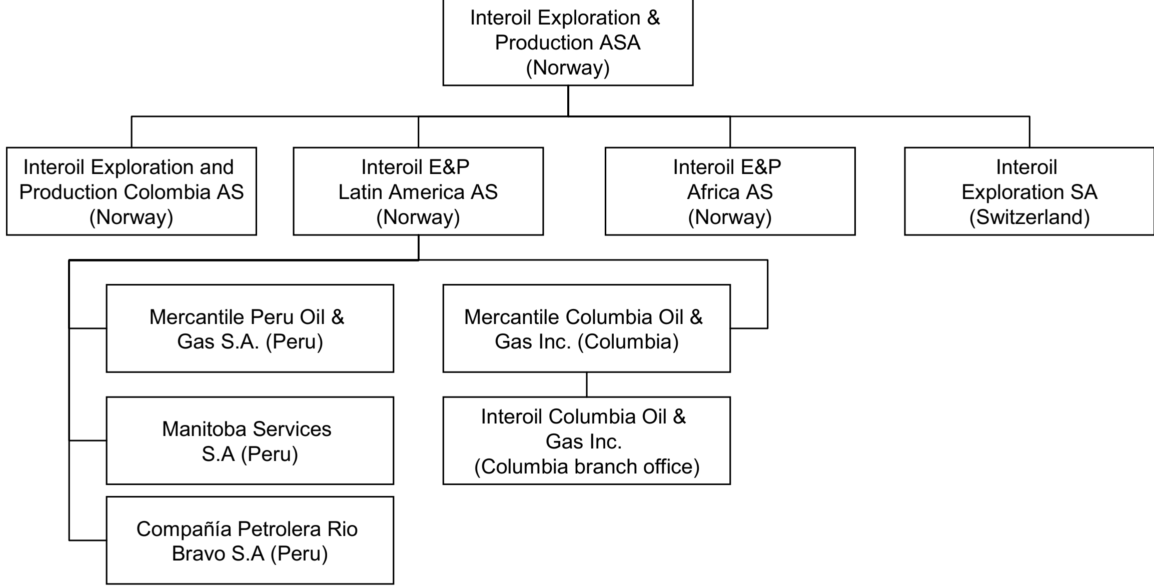
7.3 The Company's strategy and objectives

The vision of InterOil is to develop the Company as an exploration and production oil & gas company in the energy sector in West Africa and South America through.

- Developing InterOil as an exploration and production oil & gas company active primarily in West Africa and South America.
- Purchasing one or more junior oil & gas producers
- Developing organically the assets within its current and future subsidiaries
- Acquiring one or more producing assets
- Participating in offshore and onshore exploration with the ultimate goal of achieving a balance of the Company's portfolio among exploration, appraisal, developing and producing assets.

7.4 Corporate structure

InterOil currently owns operating companies in Peru and Colombia, indirectly held through InterOil Exploration & Production Latin America, a 100% owned subsidiary of the Company. As set out below, the Company has also established a 100 % owned subsidiary, InterOil Exploration & Production Africa AS, which will be the holding company of its activities in Africa.



7.5 Company's business and activities

The Company's current activities are located in Peru and Colombia. In addition the Company is currently in the process of establishing operations in West Africa.

7.5.1 Peru

In Peru InterOil's activities and assets are comprised of three companies and three main producing areas, of which assets are located in the Talara basin. InterOil's net production from these assets before royalties at the end of April 2006, was approx. 2,400 bbl/d, which is an increase of approx. 800 bbl/d since the beginning of the year. Additional investments will be done in 2006 in order to further increase the production. The effect of the investments so far this year has been very successful. Below is a short description of the operating companies:

Mercantile Peru Oil & Gas S.A. – License holder of Block III

InterOil has a working interest in Block III of 100%. Block III covers an area of 356 km^2 and production from the block started as early as 1916. MIPI started operating the block in 1995. The gross daily production as of end April 2006 is approx. 900 bbl/d, while the peak production of approx. 4,800 bbl/d was obtained in 1964. As of today approx. 455 wells have been drilled on the block, of which 3 has been drilled after InterOil acquired MIPI. Current production is from 186 wells. Several new wells will be drilled in 2006.

Compania Petrolera Rio Bravo S.A. – License holder of Block IV

InterOil's working interest in Block IV is 100%. Block IV covers an area of 307 km^2 and production from the block started in 1951. MIPI started operating the block in 1997. The gross daily production today is as of end April 2006 approx. 1,400 bbl/d, while the peak production of approx. 5,000 bbl/d was obtained in 1960. As of today approx. 358 wells have been drilled on the block, of which 4 has been drilled after InterOil acquired Compania Petrolera Rio Bravo S.A. Current production is from 203 wells. Several new wells will be drilled in 2006.

Manitoba Services S.A. – Service company

Manitoba Services SA is a service company, located in Talara, which provides well services to each of the other production companies.

The current number of total employees in the three Peruvian companies is 86.

Reserves

According to Gaffney, Cline & Associates, InterOil's net proven oil reserves in Peru as of 31 March 2006 was 10.7 million bbls and 6.0 million bbls net of royalties, while InterOil's net proven + probable oil reserves in Peru as of 31 March 2006 were 13.1 million bbls and 7.4 million bbls net of royalties.

7.5.2 Colombia

In Colombia, InterOil's activities and assets are held by a Colombian branch of a BVI registered company, Mercantile Colombia Oil and Gas Inc. Mercantile Colombia Oil and Gas Inc. has seven contract areas which cover a total area of 258 km^2. All contract areas are located in the Rio Magdalena basin. The Company is operator for all contract areas with the Colombian State owned oil company Ecopetrol as partner. Ecopetrol has the right to a 30%-50% equity interest in all areas, and has exercised this in all contracts except one. Mercantile Colombia has a staff of approximately 42 and has a head office in Bogota.

InterOil's net production from all areas before royalties is as of end April approx.1,000 bbl/d, which is an increase of approx. 250 bbl/d since the beginning of the year. InterOil will invest a total of US$ 8 million in Colombia in 2006 in order to increase the production, but so far the effect of these investments has not been as successful as in Peru.

Toqui-Toqui field (located within Puli C Block)

The Toqui-Toqui field is the main producing asset with a gross daily production of approx. 1,100 bbl/d. The field started production in 1987. As of today 36 wells have been drilled on the field, of which three has been drilled after InterOil acquired MIPI. 80 km^2 of 3D seismic covering most of the Puli C Block will be acquired this summer and will cover part of Ambrosia, Rio Opia and Mana Block. InterOil's working interest in Toqui-Toqui is 50%.

Rio Opia contract (located within Puli C Block)

The gross daily production from the Rio Opia contract is approximately 60 bbl/d. The first successful well in the area was drilled in the spring of 2004. The production development has been disappointing and no further wells will be drilled until the new 3D seismic has been interpreted. InterOil's working interest in the Rio Opia contract is 70%.

Ambrosia contract (located within Puli C Block)

The gross daily production from the Ambrosia contract is approx. 150 bbl/d. Five successful wells were drilled in the area in 2003/2004. The production development has been disappointing and no further wells will be drilled until the new 3D seismic has been interpreted. InterOil's working interest in the Ambrosia contract is 70%.

Mana contract (located within Puli C Block)

One well was drilled early 2004 and was defined as a discovery. However, the ability to produce from the reservoir has proven difficult. The well is today not on production. One dry exploration well was drilled in the Mana contract area in 2005. No further wells will be drilled until the new 3D seismic has been interpreted. InterOil's working interest in the Mana contract is 70%.

Armero contract

The gross daily production from the Armero contract is approx. 100 bbl/d. Seven successful wells were drilled in the area in the period 1987-1991. The production from these wells, however, did not start until 1999 due to lack of infrastructure. The production development has been disappointing and no further wells will be drilled until new geological and geophysical work has been conducted. InterOil's working interest in the Armero Rio contract is 50%.

Paraiso contract

No wells have so far been drilled in the Paraiso contract area. The first exploration well is planned for fall 2006, but might be postponed until 2007. InterOil's working interest in the Paraiso contract is 100%.

Puli B Block

The gross daily production from the Puli B Block is approx. 260 bbl/d. One successful well was drilled on the block in 1992, while a new well has been drilled recently. The production from the first well, however, did not start until 1998 due to lack of infrastructure. The last well is very promising and new wells will probably be drilled during 2006. InterOil's working interest in the Puli B Block is 50%. Pacific Stratus Energy, a Canadian Company has a 50% interest in future next wells, as well as well no. 7, drilled in 2006, which they also operated.

New areas

One new evaluation contract was awarded in 2005. The area is in northern Colombia, Lower Magdalena Valley. Geological and geophysical work is ongoing with an aim of either making a formal bid for the block or relinquishing. InterOil's working interests in the new areas are 100%.

Reserves

According to Gaffney, Cline & Associates, InterOil's net proven oil reserves in Colombia as of 31 March 2006 were 3.4 million bbls and 2.8 million bbls net of royalty, while InterOil's net proven + probable oil reserves in Colombia as of 31 March 2006 were 5.3 million bbls and 4.4 million bbls net of royalties.

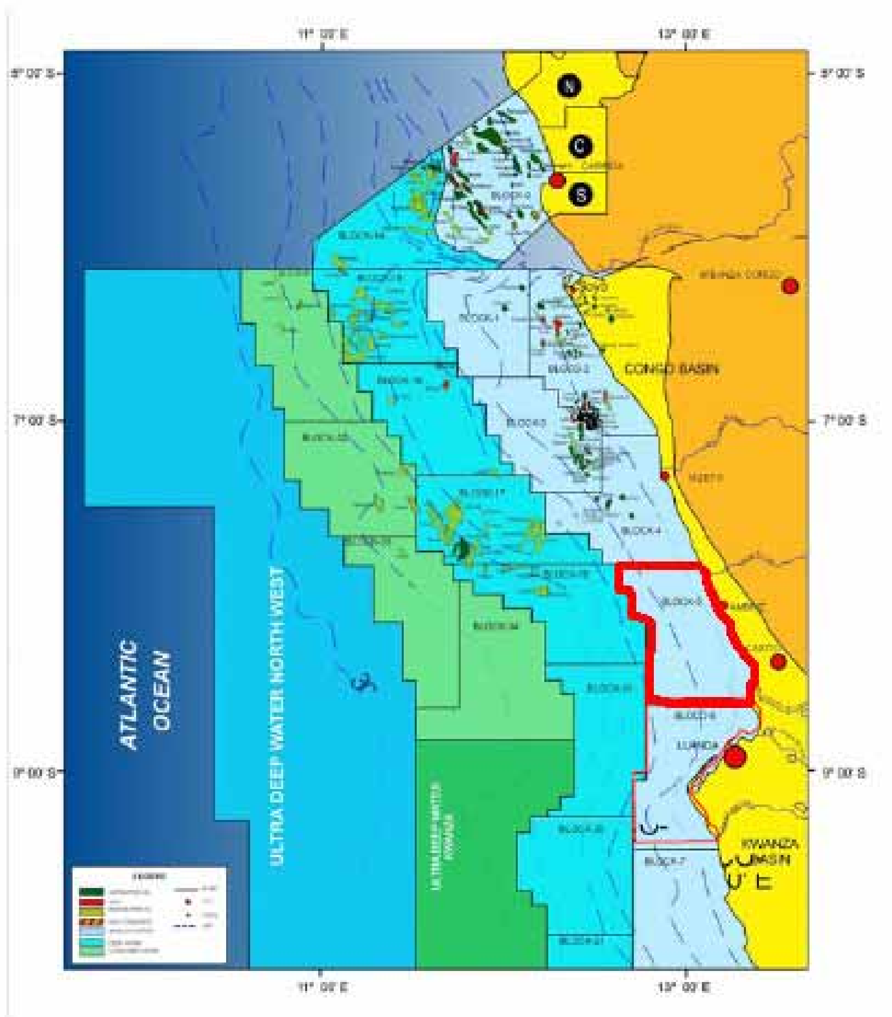
7.5.3 West Africa

In addition to the Company's activities in Peru and Colombia, the Company is currently in the process of establishing operations in West Africa.

Angola

InterOil was offered to participate in exploration licenses for two blocks offshore Angola on 9 May 2006. This offer was a result of a license round presented by the government of Angola in January 2006. InterOil made an application for these blocks, and in competition with the general oil and gas industry, successfully was offered to participate in the following blocks:

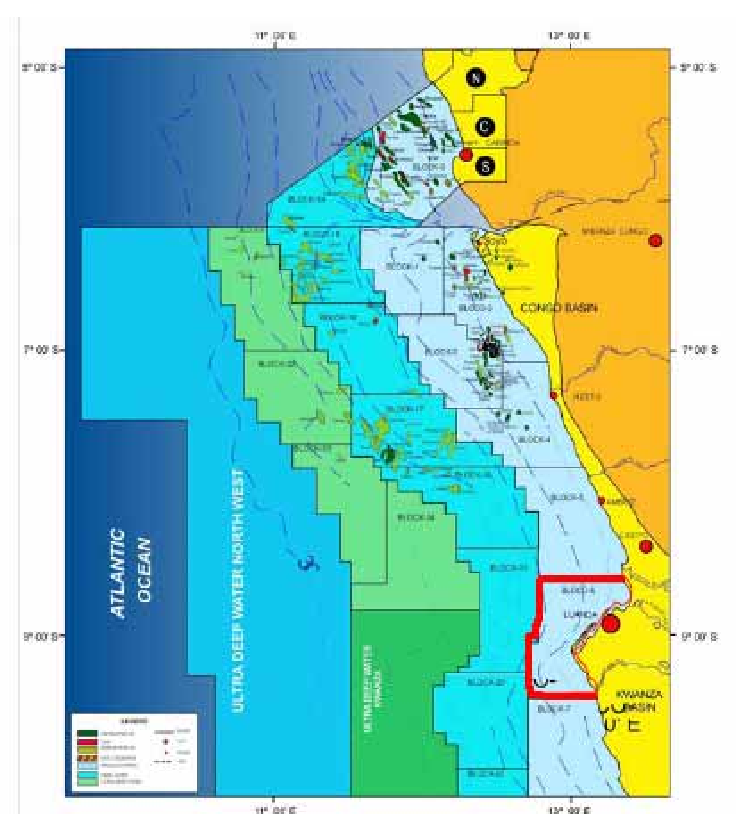
Block 5:



Block 5 has an area of 5708km^2. InterOil's proposed participation is 40% with Vaalco Energy Inc (Operator) and Sonangol (the state owned oil company in Angola) as partners. Below is an overview of the main terms of the licence for block 5:

InterOil's participating interest	40%
Signature bonus (for 100% of the block) [2]	• US$ 21 million (non-recoverable) • US$ 4 million as contribution for social projects (non recoverable)
Initial Exploration Period:	• Term: 4 years (Effective Date pending amendments to PSA & Concession Decree) • Work Commitments: o 1,000 Km^2 3D seismic o 2 Exploration Wells
Second Exploration Period:	• Term: 3 year • Work Commitments: o 2 Exploration Wells o 600km^2 3D seismic
Production period:	20 years with possible extension
Contract type: PSA	• Partners o Vaalco Energy Inc (Operator, 40%). o Sonangol P&P (20%) • Maximum InterOil Exposure estimated to (4 years): o US$ 29 million

Block 6:



[2] The signature bonus is not payable by Sonangol, and it thus divided pro rata among the other participants in accordance with their share in the license; i.e. Vaalco and the Company each has to bear 50% of the signature bonus.

Block 6 covers an area of 4,930km². InterOil's proposed participation is 20%, with Petrobras as Operator. Below is an overview of the details of the Block:

InterOil's participating interest	20%
Signature bonus (for 100% of the block) [3]	• US$ 50 million (non-recoverable) • US$ 12.5 million as contribution for social projects (non-recoverable)
Initial Exploration Period:	• Term: 4 years (Effective Date pending amendments to PSA & Concession Decree) • Work Commitments: o 1,200 Km^2 3D seismic o 2 Exploration Wells
Second Exploration Period:	• Term: 3 year • Work Commitments: o 2 Exploration Wells o 800km² 3D seismic
Production period:	20 years with possible extension
Contract type: PSA	• Partners o Petrobras (Operator, 40%). o Sonangol P&P (20%) o Initial Oil and Gas SA (10%) o Falcon Oil (10%) • Maximum InterOil Exposure estimated to (4 years): o US$ 21 million

[3] See footnote 2 above: The signature bonus is not payable by Sonangol, and it thus divided pro rata among the other participants in accordance with their share in the license.

8 Market Information

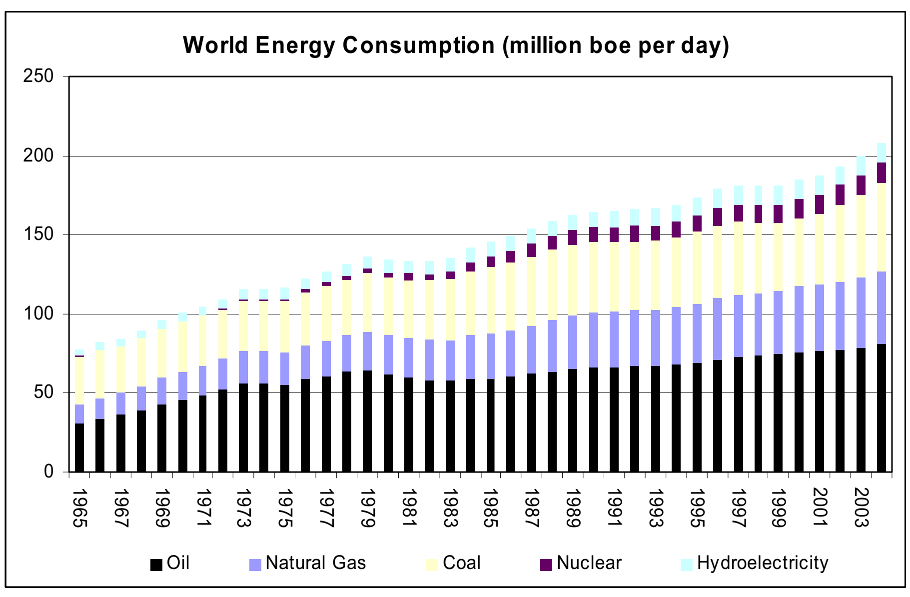
8.1 Industry overview

The world's energy consumption has increased constantly during recent years. The trend shows that there still is a growth in consumption of oil, together with natural gas and coal while the use of nuclear energy and hydroelectric energy has stagnated. The oil market is an integral part of the world economy, where demand moves in line with the general economy. The International Monetary Fund (IMF) estimates world economic growth at 4.3% in 2005 and 4.4% in 2006. Demand for oil is estimated by the International Energy Agency (IEA) to grow by 1.8 Mbd in 2006 up from 83.4 Mbd, compared to 2005.

OPEC is an international organisation of eleven countries, which are heavily reliant on oil revenues as their main source of income. Membership is open to any country which is a substantial net exporter of oil and shares the ideals of the organisation. The current members are Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, the United Arab Emirates and Venezuela.

Twice a year, or more frequently if required, the Oil and Energy Ministers of the OPEC countries meet to decide on the Organisation's output level and consider whether any action to adjust output is necessary in the light of recent and anticipated oil market developments. OPEC has currently suspended their price band target oil price of USD 22–28 for the OPEC oil basket. The price for Brent blend equalled around USD 2-3 above the OPEC basket price before the suspension. As oil prices have increased further, it has become evident that OPEC at the moment does not have enough production capacity to meet the growth in world demand. The organisation is planning to increase its capacity in the coming years, mainly from Saudi-Arabia, to attempt to regain control over prices.

World's energy consumption



Source: BP

As a consequence of a solid global economy and a strong increase in oil demand, the general international offshore oil and gas market showed a healthy development from 1995 until 1997. The financial crisis in Asia and the oil price collapse in 1998/99 led to a weak market in the period from 1998 to 2000. As energy prices increased, this contributed to an improvement during 2001, but the upturn was short as the weakening in global economy negatively influenced the rate of new investments in new oil and gas fields, whereas the market for offshore services and modifications were only modesty affected due to the continuous upgrading and production support. This development continued into 2002 and 2003, but during the end of 2003 and 2004, demand for oil showed a significant improvement. The latest IEA report shows a 2004 demand growth of 3.2% compared to 2.2% in 2003, and demand and prices in the offshore modification and services markets provide a favourable market outlook for 2005 and into 2006 after record high oil price boosted investments in the industry.

Despite strong oil prices from late 1999, oil companies have until recently been reluctant to increase exploration and production spending accordingly. Until mid 2003, the high prices were more a result of OPEC's success in controlling the supply side rather than growing demand. However, since then the situation has changed and oil demand has shown a strong year-to-year growth. Since there is currently only about 1% excess production capacity worldwide, increased exploration and production activity is expected. Exploration and production spending worldwide were up some 10% in 2004 and estimated to grow by 5-6% in 2005 (Salomon Smith Barney's

exploration and production spending survey from January 2005). This is also reflected in a rush for new drilling rigs in 2005, which have become more difficult to contract.

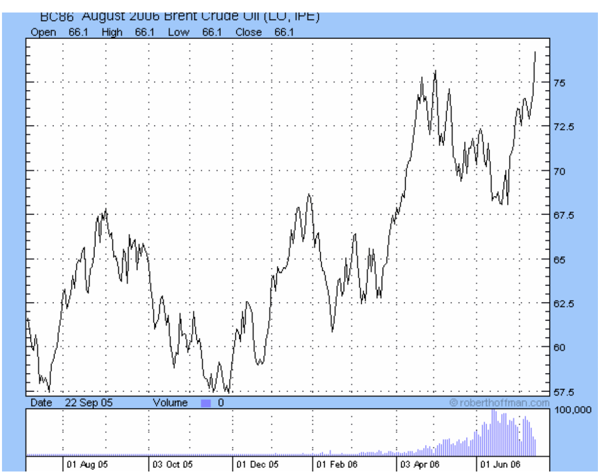
8.2 The oil price

Although higher prices have slowed world petroleum consumption growth, expected growth remains strong at 1.6 million barrels per day (bbl/d) in 2006 and 1.8 million bbl/d in 2007. The oil price as of today is at record highs in nominal terms but not in real terms.

For the year, crude oil was expected to average $67.25 a barrel, $9.25 higher than predicted just six months ago. Crude oil for August delivery closed down 5 cents at $75.14 a barrel in trading on the New York Mercantile Exchange.

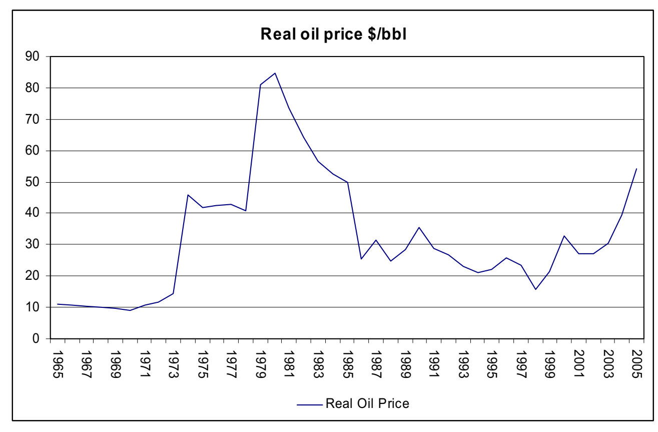
As can be seen from the second graph below, it is still under the level in the early eighties after the Iranian Revolution when the price peaked at USD 84.6/Bbl in 2005 dollars.

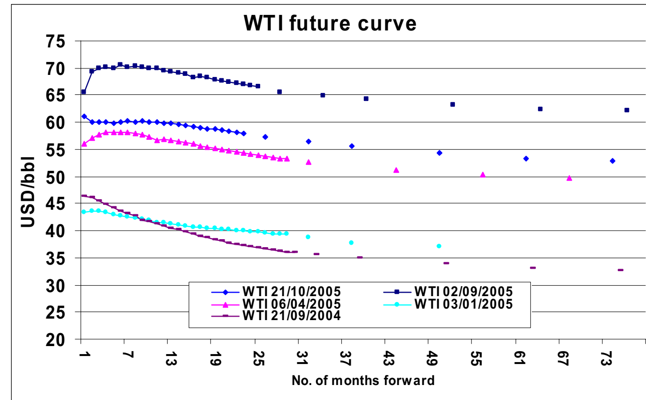
The Brent Crude Oil Price development



Source: Datastream

Real and future Oil Price





Source: BP, Pareto Research, Bloomberg

8.3 The demand for oil

World demand for oil normally moves along the lines of the world's GDP growth. The table below shows the estimates from IEA as of October 2005.

Global Oil Demand

	Global demand[1]	Change from same quarter last year mill. boe/day	%
1Q04	82.1	2.3	2.8
2Q04	80.9	4.1	5.3
3Q04	81.7	2.9	3.7
4Q04	83.8	2.5	3.0
2004	82.1	2.9	3.7
1Q05	83.8	1.7	2.1
2Q05	81.9	1.0	1.2
3Q05	82.4	0.7	0.9
4Q05(e)	85.5	1.7	2.0
2005(e)	83.4	1.3	1.5
1Q06(e)	85.4	1.5	1.8
2Q06(e)	83.4	1.5	1.8
3Q06(e)	84.7	2.3	2.8
4Q06(e)	87.2	1.7	2.0
2006(e)	85.2	1.7	2.1

[1)] Million barrels of oil equivalents per day

Source: IEA

The use of oil with respect to the total energy consumption has also increased, but it must be noted that the market is dynamic and that means that the demand for oil is inversely linked to the price. Longer periods of high oil prices can therefore lead to increased use of alternative energy sources at the cost of oil demand.

8.3.1 Drivers affecting the oil price

- Changes in supply and demand for oil and gas
- OPEC regulations
- Weather conditions
- Regulations from domestic / foreign authorities
- The price of substitutes
- Political conditions
- Economic conditions

8.4 Oil market balance

Oil market balance

	2002	2003	2004	2005(e)	2006(e)
OECD Demand	48.0	48.6	49.5	49.8	50.3
Non-OECD Demand	29.7	30.6	32.7	33.6	34.8
Total Demand	77.7	79.2	82.2	83.4	85.1
NON-OPEC supply	48.1	49.0	50.1	50.3	51.6
OPEC Supply	28.8	30.7	33.0		
Total Supply	76.9	79.7	83.1		

Source: IEA

8.5 Overview of the Peruvian market and oil industry

Peru's economy reflects its varied geography - an arid coastal region, the Andes further inland, and tropical lands bordering Colombia and Brazil. Abundant mineral resources are found in the mountainous areas, and Peru's coastal waters provide excellent fishing grounds. However, overdependence on minerals and metals subjects the economy to fluctuations in world prices, and a lack of infrastructure deters trade and investment.

The oil and gas industry is, under the new fiscal regulations that were introduced last year, quite favorable in Peru, which can be seen from the latest allocation of licenses.

The largest oil producer in Peru is Argentina-based Pluspetrol, which controls over one-half of the country's entire crude oil production. Other major producers include Occidental Petroleum, Petrobras, and Petro-Tech Peruana. Peru mostly privatized the former state-owned oil company, Petroperu, in 1993. Still, Petroperu continues to control the country's only crude oil pipeline, most of the refineries, and a majority of the retail oil products market.

8.6 Overview of the Colombian market and oil industry

Colombia's economy has been on a recovery trend during the past two years despite a serious armed conflict. The economy continues to improve thanks to austere government budgets, focused efforts to reduce public debt levels, an export-oriented growth strategy, and an improved security situation in the country.

The government's economic policy and democratic security strategy have engendered a growing sense of confidence in the economy, particularly within the business sector. Coffee prices have recovered from previous lows as the Colombian coffee industry pursues greater market shares in developed countries such as the United States.

InterOil's subsidiary MCOG, has operated in Colombia since 1994. Neither the expatriates nor the local staff have ever been threaten or harmed. The Company has an office in Bogota and its operation is 100 km SW in the Upper Magdalen a valley. InterOil transports oil daily by trucks over 200 km each way. There has never been an incident nor any disruption in this transportation. The oil is stored in tankers (onshore) and transported by pipeline over 200km to the NW. There have not been any incidents with this pipeline for the last 5 years.

In an effort to increase transparency and spur exploration, the Colombian government spun off regulatory responsibilities from Ecopetrol, Colombia's state-owned oil company, and created the National Hydrocarbons Agency (ANH). The ANH now administers Colombia's competitive process, allowing Ecopetrol to compete side by side with foreign firms for subsequent hydrocarbon contracts.

Under the new model, oil companies may assume up to 100 percent of investment and risk activities in all exploration and production contracts. Oil companies may also obtain the right to exploit such regions for 30 years or until field depletion, as well as extend previous association contracts. This system is based on providing new incentives to investors, who will benefit from higher returns on their investments. These measures have attracted significant foreign investment.

The biggest catch during 2004 was ExxonMobil, which along with Petrobras, took advantage of the new business climate to undertake an ambitious project to explore 4.4 million hectares in Colombian Caribbean waters. Other big companies like ChevronTexaco and Occidental Petroleum have extended natural gas and oil contracts. The Harken Energy Corporation, Repsol-YPF of Spain, Hocol and several smaller companies have signed either exploration contracts or viability agreements that will likely lead to exploration. Under the new form of contracting, ANH had signed 39 exploration contracts during 2004 (only 20 were projected), continuing a trend from 2003, when 21 companies signed contracts.

8.7 Overview of the Angolan market and oil industry

Angola's economy has undergone a period of rapid transformation in recent years, moving from the disarray caused by a quarter century of war to being the fastest growing economy in Africa and one of the fastest in the world. Growth is almost entirely driven by rising oil production which surpassed 1.2 million barrels per day in late-2005. Control of the oil industry is consolidated in Sonangol, a conglomerate which is owned by the Angolan government. The economy grew 18% in 2005; growth is expected to reach 26% in 2006 and stay above 10% for the rest of the decade. The security brought about by the 2002 peace settlement has led to the resettlement of 4 million displaced persons, thus resulting in large-scale increases in agriculture production. With revenues booming from oil exports, the government has started to implement ambitious development programs in building roads and other basic infrastructure for the nation.

The president has announced the government's intention to hold elections in 2006. These elections would be the first since 1992 and would serve to elect both a new president and a new National Assembly. The management and members of the Board have a long relationship to Angola and Sonangol. Over the last 20 years, many of the Board members and management have actively been involved in Angola and seen the development first hand. The oil industry has, because of well established regulatory system for oil and gas activity (PSA's) been active in the country before and after independence. The activity increased significantly in the mid 90's by the discovery of large offshore oil deposits in very deep water. Angola is today considered prime area for most oil and gas companies, although the entry ticket and the cost of establishing an operation in Angola is considered high.

In an effort to increase transparency, Sonangol has now adopted a very open approach to licensing and the recent licensing round has been an excellent example of the openness now adopted by many West Africa Countries. The legal framework and all the economic terms are well presented and openly disclosed at time of invitation to bid. The bidding process has an element of bonus payment and social contribution which is openly presented to the industry. A committee then reviews the bids and makes all the bid information available.

ExxonMobil, ChevronTexaco, Total, BPAmoco, ENI, Norsk Hydro, Deveon Energy, Marathon, Statoil are some of the largest competitors in Angola. However, there are many small independents like Svenska, ROC Oil, Vaalco and a large number of small private national companies that have become active in the last few years. Force Petroleum, Sumoil, to name a few.

9 Organization, Board and Management

9.1 Organization

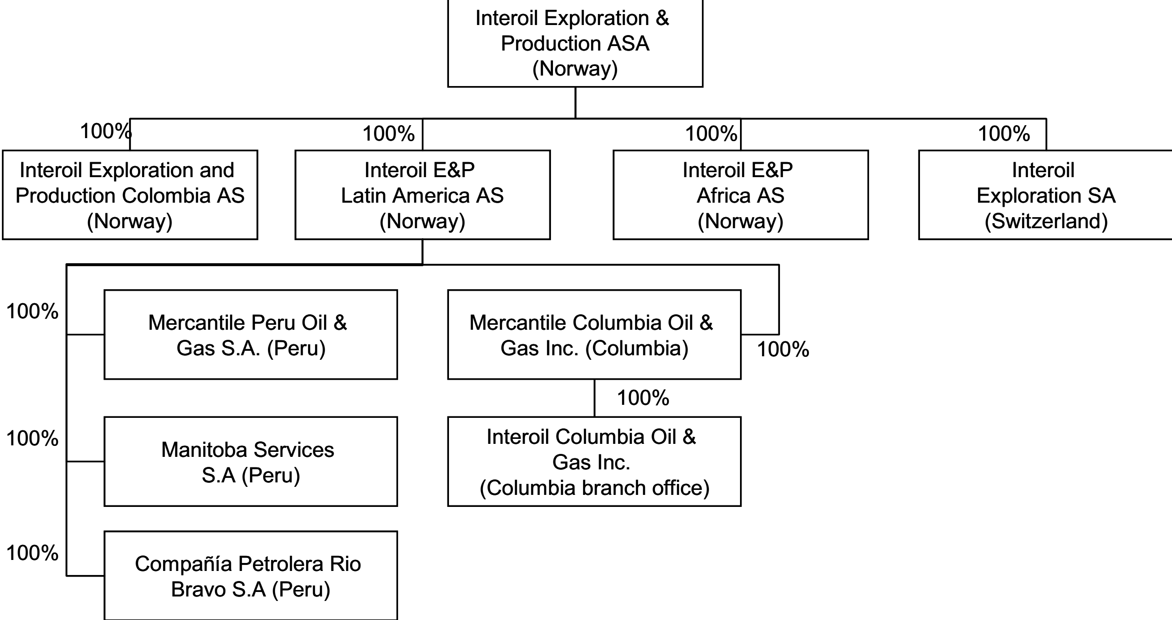
The Company was established on 2 May 2005 as a Norwegian Private Limited Company ("AS"). It was converted to a Norwegian Public Limited Company ("ASA") on 14 November 2005. The Company is registered in the Register of Business Enterprises with org. no: 988 247 006. The Company's registered office is Strandveien 50, 1366 Lysaker.

The Company's shares are currently not listed on any stock exchange but the shares are registered on the OTC-list managed by the Norwegian Securities Dealers Association, and are traded under ticker "INOX".

9.2 Company structure

InterOil currently owns operating companies in Peru and Colombia, indirectly held through InterOil Latin America, a 100% owned subsidiary of the Company. As set out below, the Company has also established a 100 % owned subsidiary InterOil Exploration and Production Africa AS, which will be the holding company of its activities in Africa.

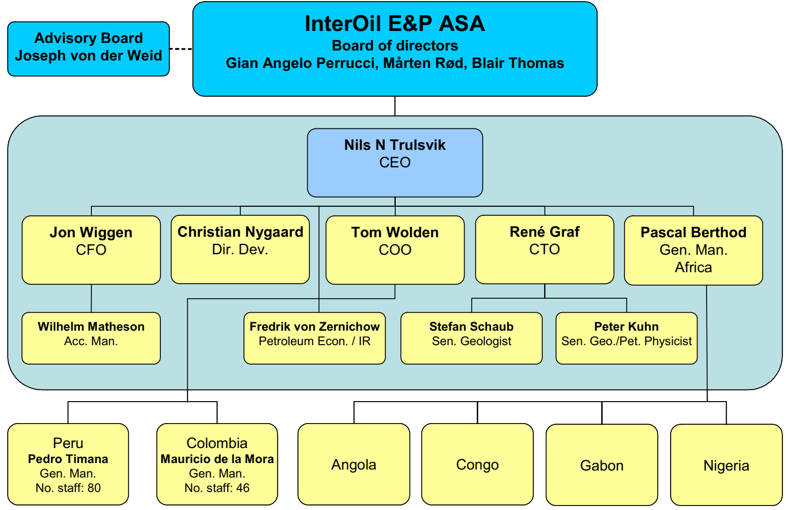
The figure below is an overview of the corporate structure of InterOil.



InterOil Exploration & Production ASA is the holding company in the group and is responsible for group financing and group reporting. In addition, the holding company is responsible for the IR function. The operating activities are conducted by the subsidiaries as illustrated above.

9.3 Organizational structure

The figure below is an overview of the organizational structure of InterOil.



9.4 Management and board of directors

The following table sets forth information with respect to members of the board of directors and the Group executive officers.

Name	Age	Position	Shares	Options
Directors				
Mårten Rød [1]	57	Chairman of the Board	5,225,000	0
Gian Angelo Perrucci[2]	62	Member of the Board	625,000	0
Robert Blair Thomas	43	Member of the Board	0	0
Berit Kjøll	50	Member of the Board	0	0
Patricia Guerra	46	Member of the Board	0	0
Group Executive Officers				
Nils Trulsvik[3]	57	CEO	800,000	0
Jon Wiggen	55	CFO	0	0
Rene Graf	58	CTO	0	0
Tom Wolden	50	COO	0	0
Christian Nygaard	53	Development Director	0	0
Pascal Berthou	49	General Manager, Africa	0	0

[1] Shares owned through the wholly owned subsidiary Eksportconsult. Eksportconsult AS also holds a forward contract to purchase 150,000 shares in the Company.
[2] In addition, Mr. Perucci owns 10% of Caberian Investment Inc, who in turn owns 4,600,000 shares in InterOil and holds a forward contract to purchase 150,000 shares in the Company.
[3] Owned through his wholly owned company Force Capital Partners AS.

9.4.1 Description of the Board of Directors

In accordance with Norwegian law, the board of directors is responsible for administering the Company's affairs and for ensuring that the Company's operations are organized in a satisfactory manner.

The composition of the Board of Directors is in accordance with the recommendations in Norwegian Code of Practice for Corporate Governance dated 8 December 2005. As long as the warrants initially issued to TCW are outstanding, TCW shall have the right to appoint one member of the Board of Directors of the Company. Four of the board members are independent of the Company's main shareholders, while three of the board members are independent of the Company's executive management and material business contacts.

Berit Kjøll and Patricia Guerra have been elected as board members with effect from the first day of listing on Oslo Børs.

Ms. Kjøll, Mr. Perucci and Mrs._Guerra are considered independent of the Company's management according to the Code of Practice.

The nomination committee will, according to the Articles of Association, nominate the members to be elected for the Board of Directors by the general meeting each year.

Mårten Rød (57) -Chairman of the Board, c/o InterOil, Strandveien 50, 1366 Lysaker, Norway**.**

Mr. Mårten Rød has long experience as entrepreneur and from the oil and gas industry both upstream and downstream. He worked 11 years for Arco in the North Sea, and founded Northern Energy UK in 1998, an oil company with production in Texas and Oklahoma. He was president in InterOil Norway from 1995, which participated in various oil and mineral projects in West-Africa. Mr. Rød is a Norwegian citizen with residence in Asker, Norway..

Gian Angelo Perrucci (62), Board member, c/o Nicrest Limited, 14 Grosvenor Crescent, London SWIX 7EE, UK.

Mr. Gian Angelo Perrucci is an Italian entrepreneur. He previously built up a major shipping company in USA and Europe. During the last 15 years, he has developed a major logistics operation in West Africa including supply bases, engineering and production yards, and offshore support vessels. Mr. Perrucci is an Italian citizen with residence in London, UK. Mr. Perucci has been on the board of directors since 18 October, 2005.

Robert Blair Thomas (43), Board member, c/o The TCW Group, Inc., 865 South Figueroa Street Los Angeles, California 90017, USA.

Robert Blair Thomas is a Group Managing Director of Trust Company of the West and the Chief Executive of TCW's Energy & Infrastructure Group. Prior to joining TCW, he was a senior investment officer in the Inter-American Development Bank and an attorney at the law firm of Brown & Wood in New York. He also served as a legislative advisor on energy and budget policy in the first Bush White House. Mr. Thomas is a member of the Board of Directors of TCW Asset Management Company and several private energy companies in the U.S., UK, Norway and the Dominican Republic. Mr. Thomas is an American citizen with residence in Los Angeles, California, USA. Mr. Thomas has been on the board of InterOil since 18 October, 2005 and is appointed by TCW in accordance with their right to appoint a board member in accordance with the agreement for the warrants described above.

Berit Kjøll (50), Board member, c/o Telenor ASA, Snarøyveien 30 1331 Fornebu, Norway.

Berit Kjøll has broad experience from managing businesses in Norway. Mrs. Kjøll is today COO in Telenor and responsible for Consumer Market – Norway with 13 billion NOK turnover. She has previously held the positions as CEO of Steen&Strøm ASA, Flytoget AS, Tusenfryd ASA and Kilroy Travels. Mrs. Kjøll is member of the board of directors of SAS AB, DnB NOR ASA and Tusenfryd ASA. She holds positions of trust in Den Norske Turistforening and Skiforeningen. Ms. Kjøll is a Norwegian citizen and resides in Oslo, Norway. Ms. Kjøll was elected to the board on 12 June 2006.

Patricia Guerra (46), Board member, c/o Meyer Lustenberger Attorney at Law, Forchstrasse 452, P.O. Box 1432, 8032 Zürich, Switzerland.

Patricia Guerra is born in Equador. She is a partner in the Swiss law firm Meyer Lustenberger. Her main areas of practice are corporate law and M&A, international estate planning and inheritance law and charitable organizations. Mrs. Guerra has previously been working with Mayer, Brown and Platt, Chicago, USA as an attorney and with König and Meyer, Zürich as an attorney. Mrs. Guerra is member of the Board of Directors of several Swiss companies, including subsidiaries of large international groups active in the areas of shipping and the glass industry, as well as companies in the reinsurance and medical technology business. Ms. Guerra has been on the board since 12 June 2006. Ms. Guerra is a Swiss citizen and resides in Zürich, Switzerland.

9.4.2 Independency of the Board of Directors

The object of the Board of Directors of InterOil is to manage the shareholders' assets in the best possible manner and treat all shareholders of the Company equally. In electing board members emphasis is therefore placed on having independent members and members who represent different ownership interests. The Company intends to comply with the Corporate Governance Code with respect to the board's independency. According to the Corporate Governance Code minimum 50% of the board members shall be independent from the executive management and material business contacts. At least two board members shall be independent from the major shareholders. Following the implementation of the election of Mrs. Patricia Guerra and Mrs. Berit Kjøll as new board members from the time of listing, it is the Company's opinion that the Board of Directors is in compliance with the Corporate Governance Code. One board member is regarded as not being independent from the major shareholders. Two board members might be considered as not being independent of the executive management and material business contacts according to the Corporate Governance Code.

The Chairman of the Board, Mårten Rød, is through the company Eksportconsult AS, which he owns together with immediate family, one of the principal shareholders of the Company. Accordingly Mr. Rød is not considered independent from the major shareholders. Eksportconsult AS has a management agreement with InterOil which has been described under section 9.6 below. The management agreement might imply that Mr. Rød is not regarded as independent from the executive management and material business contacts. The agreement may be terminated by either party with three months prior notice. The agreement has been approved by the Board which has regarded this agreement as being of high value for the Company.

Robert Blair Thomas represents TCW in the Board of Directors. Due to InterOil's interest-bearing debt to TCW, the Company does not consider Mr. Blair Thomas being independent from the executive management and material business contacts.

It is the Company's opinion that the board members Mr. Gian Angelo Perrucci, Mrs. Patricia Guerra and Mrs. Berit Kjøll are independent from the major shareholders as well as the executive management and material business contacts. The Company would like to address the fact that the Company previously has had a management agreement with Caberian Investment Limited, a company which is 10 % owned by Mr. Perrucci, under which the services of Mr. Perrucci related to development of the Company's business in West Africa was provided to the Company. The management agreement wit Caberian Investment Limited has been terminated. If so desired by the Company will have the possibility to call on Mr. Perrucci's services from time to time with respect to specific projects.

9.4.3 Description of the Group executive management

The Group executive management is responsible for the daily management and the operations of the Company.

Nils N. Trulsvik (born 1948) – Managing Director.

Mr. Nils Trulsvik is a petroleum explorationist with extensive experience throughout the world. He worked seven years with Saga Petroleum with assignments in the North Sea, Mediterranean, Africa, South and North America. In 1981 he co-founded Nopec, where he worked for 13 years with assignments in Northwest Europe, Africa and the Far East. From 1987 until 1993 he was Managing Director. He was part of the management team in Fountain Oil from 1994 – 1998. He has been working with various oil and gas projects the last 8 years. Mr. Trulsvik is a Norwegian citizen with residence in Oslo, Norway.

Jon Wiggen, (born 1950), Chief Financial Officer (CFO).

Mr. Wiggen is a state authorized auditor and has over 30 years experience in various businesses including several publicly listed companies. He was CFO for the Brynestad Group of companies for several years, and consulting and audit partner with Deloitte for a number of years. Mr. Wiggen is a Norwegian citizen with residence in Oslo, Norway.

Tom Wolden, (born 1955), Chief Operational Officer (COO).

Mr. Wolden is a petroleum geologist with extensive experience in all facets of promotion, exploration, evaluation and production of hydrocarbons in technical performance and management. 22 years of experience in the oil business centred on offshore NW Europe, Africa, Russia, SE Asia, Middle East and Norway. He has also held assignments outside Norway, including UK and Seychelles. The experience is gathered through work in Saga Petroleum, Nopec and for the last 10 years in PGS Exploration. Mr. Wolden is a Norwegian citizen and resides in Nærsnes, Norway.

Rene Graf (born 1947), Chief Technical Officer (CTO).

Mr. Graf has long international experience covering all aspects of exploration with focus on geophysical field operations, processing and interpretation, both 2-D and 3-D, land and marine. This experience has been acquired during a period of almost 20 years working for Shell International in The Netherlands, France, Malaysia and Colombia. Mr. Graf is a Swiss citizen with residence in Zürich, Switzerland.

Pascal Berthou (born 1957) General Manager, Africa.

Mr. Berthou has over 25 years experience in the oil and gas industry in engineering, fabrication and installation offshore/onshore. Extensive international experience of contract management. Especially trained in offshore revamping and hook-up modification of life platform, piping and structural fabrication and installation. Qualified in pipe-laying, fabrication and installation of major structure: jackets and topside facilities, modules etc. for the last ten years, intensive involvement in EPIC contract, responsibility for all aspect of projects: management, contract, QA/QC and Safety, engineering and method, commissioning and start up. Mr. Berthou is a French citizen and resides in Le Prieure, France.

Christian Nygaard (born 1953) Business Development Director, Oslo

Mr. Nygaard has over 25 years work experience from among others PGS Production, Technip, Spars International Inc & Aker Maritime, Aker Oil & Gas Technology, Norwegian Contractors and Det norske Veritas. Mr. Nygaard holds a Bachelor of Science, Business Administration from the University of San Francisco, US and Post Diploma Degree, Naval Architecture, from Sunderland Polytechnic, UK. Mr. Nygaard is a Norwegian citizen and resides in Oslo, Norway.

9.4.4 Nomination committee

The annual general meeting of the Company held on 12 June 2006 resolved to establish a nomination committee. At the extraordinary general meeting held on 29 June 2006 the following members were elected to the committee:

Aage Thoen (51), c/o Aage Thoen Ltd AS, Haakon VII's gate 1, 0161 Oslo, Norway.

Mr. Thoen has 25 years of management experience from Norwegian and foreign private and listed companies within banking, international financing, offshore and shipping. He is a member of the board of Privatbanken ASA, Star Reefers Inc, DSND ASA, Ivarans Rederi AS and he is chairman and owner of the investment company Aage Thoen Ltd AS. Mr. Thoen holds an MBA and BSBA from USA and he is a Norwegian citizen with resident in Stabekk, Norway.

Rolf Johan Ringdal (51), c/o Bugge, Arentz-Hansen & Rasmussen Advokatfirma, Stranden 1, PB 1525 Vika, 0117 Oslo, Norway**.**

Mr. Ringdal is a partner in the law firm Ba-Hr, where he has been employed since 1982. He holds a cand.jur. from the University of Oslo in 1982. Mr. Ringdal is a Norwegian citizen, and resides in Oslo, Norway.

9.5 General

During the last five years preceding the date of this document, no member of the Board of Director or the senior management (except for Mr. Thomas as described in section 9.6 below) has:

- any convictions in relation to indictable offences or convictions in relation to fraudulent offences;
- received any official public incrimination and/or sanctions by any statutory or regulatory authorities (including designated professional bodies) or ever been disqualified by a court from acting as a member of the administrative, management or supervisory bodies of a company or from acting in the management or conduct of the affairs of any company; or
- been declared bankrupt or been associated with any bankruptcy, receivership or liquidiation in his capacity as a founder, director or senior manager of a company.

Over the five years preceding the date of this document, the members of the Board and the senior management hold or have held the following directorships (apart from their directorships of the Company) and/or partnerships:

Name	Current directorships/partnerships	Previous directorships/partnerships
Board of directors		
Mårten Rød	Chairman of the Board InterOil,	Member of the Board Eksportconsult AS
Gian Angelo Perrucci	Member of the Board InterOil, member of the board of Orlean Invest	-
Robert Blair Thomas	Member of the Board InterOil, CDX Gas, Electricidad del Este, TCW Asset Management Company, Viking Petroleum and CH4 Energy	-
Berit Kjøll	Member of the Board InterOil, SAS AB, DNB Nor ASA and Tusenfryd ASA	Member of the Board Gassco AS (2001-2002
Patricia Guerra	Member of the Board InterOil, Gearbulk AG, Baar / Switzerland, Vitro Group Switzerland, Corinphila Auktionen AG, Zurich / Switzerland, Renewave Medical Systems SA, Nyon / Switzerland, U.S. Robotics Schweiz GmbH, Baar / Switzerland	Member of the board SDC (Suisse) SA, Vallorbe / Switzerland, CPP Clinical Plastic Products Ltd, La Chaux-de-Fonds / Switzerland, V.I.M. SA, Luxembourg

Management	Current directorships/partnerships	Previous directorships/partnerships
Nils Trulsvik	CEO InterOil, member of the Board TM Bridge Group AS, Force Petroleum, Scan Geophysical AS, Tersus Energy Ltd., CanArgo Energy Corp Inc and Force Capital Partners AS.	Force Petroleum
Jon Wiggen	CFO InterOil, member of the Board Kjelstrup & Wiggen AS, Kjelstrup & Wiggen ANS, Nexia Norge DA, Ole Fladersgt 10 AS, H Wergelandsgt 4 – Hotel Skagerak AS, Thin Film Electronics ASA.	Partner in Kjelstrup & Wiggen AS
Rene Graf	CTO InterOil	-
Tom Wolden	COO InterOil	-
Christian Nygaard	Development Director InterOil	Member of the Board Technip R&D (2000-2004)
Pascal Berthou	General Manager, Africa (InterOil)	Member of the board Titan Engineering Nigeria (2000-2003) and Suffix Energie Solutions (2004-2005)

9.6 Conflict of interests etc.

None of the Company's board members (other than Mr. Thomas) or members of the senior management have been associated with any bankruptcies, receiverships or liquidations for the last five years. Mr. Thomas, as a representative of TCW, was a nominal board member of an English company which incurred loans from certain TCW investment funds; the company appointed a receiver for its properties after encountering economic difficulties. None of the board members have been the subject of any official public incrimination and / or sanctions by statutory or regulatory authorities (including designated professional bodies), or been disqualified by a court from acting as a member of the administrative, management, or supervisory bodies of an issuer or from acting in the management or conduct of the affairs of any issuer, or convicted of any fraudulent offences, for the last five years.

Eksportconsult AS has a management agreement with InterOil relating to the business development in the Company. Eksportconsult AS is paid USD 20,000 (excl. VAT) per month for these services which primarily include to seek out new business opportunities for the Company worldwide. Mårten Rød's executive tasks under the management agreement are primarily related to assisting the Company in establishing contacts with respect to new business opportunities for the Company. Such services have been of relevance to the Company's operations in Peru and Colombia and of particular importance with respect to the establishing of business in Angola. The services of Mårten Rød under the management agreement are considered to be of high value to future business development in the Company.

The management agreement might imply a possibility that Mårten Rød is not considered independent of the Company's management according to the Code of Practice.

See a detailed description under section 6.6 "Related party transactions".

Caberian Investment Limited has previously had a consulting agreement with InterOil related to development of the Company's business in West Africa. If so desired by the Company, it will have the possibility to call on Mr.Perucci's services from time to time with respect to specific projects.

To the Company's knowledge there are currently no potential conflicts of interests between any duties of the Company or its subsidiaries and private interest or other duties of the Board of Directors of senior management.

9.7 Compensation to the board of directors and executive management

9.7.1 Remuneration and salary

The remuneration of the directors of the Board shall be determined on a yearly basis by the Company in its annual general meeting. The directors may also be reimbursed for, inter alia, travelling, hotel and other expenses incurred by them in attending meetings of the directors or in connection with the business of the Company. A director who has been given a special assignment, besides his normal duties as a director of the Board, in relation to the business

of the Company may be paid such extra remuneration as the directors may determine. No members of the Board have any contractual entitlement to benefits upon termination of their directorships.

At the Company's ordinary general meeting on 12 May 2006, the total annual remuneration to the Board for 2005, and for 2006 up to the ordinary general meeting, was set to NOK 740,000, consisting of NOK 320,000 to the chairman of the Board and NOK 210,000 for the other board members.

The CEO, Mr. Nils Trulsvik, has a compensation of NOK 2.9 million per year. In addition, he receives car allowance and the company covers the costs of mobile- and home telephone as well as the costs of newspapers and pension-, group life- , travel- and holiday insurance. The CEO has no other compensation.

The CFO, Jon Wiggen has a compensation of NOK 1.8 million per year. Jon Wiggen has performed his services as CFO through an agreement between the Company and Kjelstrup & Wiggen, where he has been a partner up to August 2006, from which point of time he will be employed directly by the Company. In addition the Company covers the costs of pension- group life, as well as various other minor benefits.

No members of the executive management have any contractual entitlement to benefits upon termination of employment.

The total amount of remuneration for the senior management in the financial year 2005 was NOK 2.6 million.

9.7.2 Pension plans

The Company has a pension plan which came into effect on 1 July 2006. The plan gives the employee a pension of 66% of his/her last year salary, limited to 12G, and assuming 30 year employment.

The total amount set aside or accrued to provide pension to the senior management in the financial year 2005 was 0.

9.7.3 Share incentive program

On 12 June 2006, the general meeting of the Company adopted an incentive program for employees, comprising an option program. At the same general meeting the board was granted an authorisation to issue shares to option holders exercising their options, see section 10.2 for a further description of the authorisation.

No payment is to be made for these options, and upon exercise of the options the Company may elect to fulfil its obligations by way of issuance of new shares, sale of existing shares, or by making an alternative cash bonus payment equal to the number of shares multiplied by the difference between the market value of each share and the agreed price according the option agreement. The agreed price to be paid per share at the exercise of the option is proposed to be market price at the time of issuance of the option. The total number of shares comprised by the share option program shall never exceed five percent of the, at the time of entering into of an option agreement, issued number of shares in the Company.

The right to acquire shares on the basis of the option agreement may be exercised from the signing of the share option agreement and for a period of 12 months thereafter. The option holder may, at his own discretion, choose to exercise all or parts of the options awarded upon each exercise. However, each exercise may not relate to less than one third of the options awarded in the option agreement entered into between the employee and the Company.

With the current face value of NOK 0.05 the Board is authorised to issue up to 1,500,000 new shares in the Company in connection with the option program, equal to approx 7% of the existing share capital.

The board has not yet granted any options under the program.

9.8 Related party transactions

Please see Section 6.6 for further information.

9.9 Material contracts

The Company's activities in Peru and Colombia are the result of the acquisition of several companies purchased from the oil and gas company Mercantile International Petroleum Inc. ("MIPI"). MIPI was listed in Canada in the mid 90-ies, but experienced financial difficulties in 2001/2002 and started a process for sale of its oil exploration activities in Peru and Colombia in late 2004. Negotiations for the acquisition of MIPI's operating companies in Peru and Colombia started in September 2004, and were made effective on 27 September 2005. On the 9 of June 2005 InterOil entered into a Sales and Purchase Agreement with MIPI.

InterOil raised a total of USD 87 million dollars through a USD 45 million equity issue and the TCW Loan (in the amount of USD 42 million prior to the acquisition of the assets on 27 September 2005. Net proceeds from these transactions after share issuance costs and debt issuance costs were USD 83 million.

9.10 Employees

As of the date of the Prospectus, InterOil has 8 employees inclusive of the management referred to in section 9.4.2 above. The InterOil Group employs a total of 134 people world-wide.

Historically, the number of employees has developed as follows:

Country	**2005**	**2004**	**2003**
Peru	86	66	55
Columbia	42	26	21
Norway	5	0	0
Total	**134**	**92**	**76**

9.11 Corporate Governance

With the exemption of the matters described in section 9.4.1 above, the Company is in compliance with, and is dedicated to observing high standards of corporate governance, based on the principles set forth in the Norwegian Code of Practice for Corporate Governance, as published on 8 December 2005. The Company will annually produce a report as to corporate governance, which will be included in its annual report.

10 Share Capital and Shareholder Matters

10.1 Share capital

The issued share capital of Company is NOK 1,062,250 consisting of 21,245,000 Shares fully paid, with a par value of NOK 0.05 per Share and issued in accordance with Norwegian law. The Shares are equal in all respects, and each Share carries one vote at the Company's general meeting. There has been no change in the Company's share capital since 31 December 2005.

10.2 Outstanding authorizations

At the ordinary general meeting on 12 June 2006 the Board of Directors was granted an authorisation to increase the share capital with up to NOK 500,000, valid until 30 June 2007 (or the annual general meeting in 2007, whichever comes first). With the current face value of NOK 0.05 the Board is authorised to issue up to 10,000,000 new shares in the Company, equal to approx 47.1% of the existing share capital. The existing shareholders' pre-emptive rights may be waived. The authorisation may be used for one or more issue of new shares. The authorisation can only be used for share issues against cash deposit. At the same ordinary general meeting the board was authorised to increase the share capital by up to NOK 75,000 by the issuance of up to 1,500,000 shares. The authorization shall only be used in connection with the issuance of shares under the option program adopted by the Company. The existing shareholders' pre-emptive rights may be waived. The authorisation may be used for one or more issue of new shares. Both authorisations are conditional on the share capital increases in total under the authorisations not exceeding NOK 500,000. The authorisations were registered in the Norwegian Register of Business Enterprises on 16 June 2006. For technical reasons the Norwegian Register of Business Enterprises registered the authorisations as one single authorisation giving the right to increase the share capital by up to NOK 500,000.

The authorisations have not been used at the date of this Prospectus

10.3 Warrants

Pursuant to the TCW Warrant, the Company has issued subscription rights to the lenders under the TCW Loan. In total, the subscription rights carry the right to subscribe for the number of ordinary shares that can be purchased for USD 5,040,000 based on the price per share established as part of a future initial public offering.

The subscription price for these shares is the NOK equivalent to USD 0.01 (but not below the par value of the shares). Any shares purchased pursuant to the TCW Warrant must be held at least until the six month anniversary of any Company IPO.

In the event that there has not been an initial public offering within 24 months from 21 September 2005 the lenders shall have a springing royalty of 1.5 % on all of the Company's petroleum production which springing royalty shall be retroactive for such 24 month period. Any amounts payable to the lenders pursuant to such retroactive springing royalty shall not be reduced or otherwise affected by any operating, transportation, compression, marketing or capital costs of the Company.

At an extraordinary general meeting on 29 June 2006 it was resolved to issue 2,720,000 warrants to subscribers in the 9% Senior Unsecured Bond Loan free of payment. Each warrant gives the holder the right to demand the issue of one Share with a nominal value of NOK 0.05. The holders of the warrants have the right to demand that shares are issued at a subscription price of NOK 46.00 at any time prior to 29 June 2011. The warrants were registered in the Norwegian Register of Business Enterprises on 11 July 2006 and are registered in the VPS with ISIN code: ISIN NO 001 0325657. An application for listing of the warrants on Oslo Stock Exchange may be submitted to Oslo Stock Exchange at a later stage.

Except for the warrants as described above, the Company has no outstanding convertible bonds, options or other rights to subscribe for shares in the Company. However, the Company has introduced a share option program for key employees, see section 9.7.3 above.

10.4 Historical Development of share capital

The table below shows the historical development of share capital and the number of outstanding shares in Company:

Date	Type of change	Change in share capital (NOK)	Nominal value per share (NOK)	Total share capital	Number of shares
2005	Private Placement	500,000	0.05	500,000	10,000,000
Sept 2005	Private Placement	562,250	0.05	1,062,250	21,245,000

10.5 Share price development

Since 6 October 2005, the Shares have been publicly traded on the OTC market in Norway under the ticker INOX. The share price performance is shown in the graph below.

The tables below set forth price and trading volume for the Shares, as reported on the OTC, during the periods indicated. The closing price of the Shares as reported on the OTC on 17 July 2006 was NOK 33.00.

Traded price and volumes InterOil

NOK | Volume

Volume — Closing Price

Source: Norwegian Securities Dealers Association

10.6 Ownership structure

As of 17 July 2006, InterOil had a total of 155 registered shareholders, of whom 124 were Norwegian and 31 were foreign shareholders. There are no limits restricting foreign ownership of the Company's Shares. The Shares carry equal rights in all respects. Each Share has the right to one vote at general meetings.

The table below shows the 20 largest shareholders in the Company as registered by the VPS on 17 July 2006:

	Shareholder	Number of Shares	%
1	Eksportconsult AS [1]	5,225,000	24.6%
2	Caberian Investment Inc. [2]	4,600,000	21.7%
3	Credit Suisse Securities (nominee)	1,870,600	8.8%
4	Bear Stearns Securities Corp. (nominee)	1,618,800	7.6%
5	Force Capital Partners AS [3]	800,000	3.8%
6	Gian Angelo Perrucci	625,000	2.9%
7	Muslik AS	518,450	2.4%
8	Norinvest Ltd.	500,000	2.4%
9	Awilco Invest AS	450,000	2.1%
10	KLP Liv Norge	400,000	1.9%
11	Bank of New York (nominee)	319,200	1.5%
12	Aweco Invest AS	300,000	1.4%
13	Toluma AS	300,000	1.4%
14	SIS Segaintersettle (nominee)	264,500	1.2%
15	Storebrand Livsforsikring P980	231,720	1.1%
16	Skandinaviska Enskilda Banken (nominee)	202,800	1.0%
17	Consafe Invest AB	202,000	1.0%
18	Banque Invik SA Luxembourg	200,000	0.9%
19	KLP Aksjenorge	120,000	0.6%
20	Follum Invest AS	100,000	0.5%
	Total 20 largest shareholders	**18,848,070**	**88.7%**
	Other shareholders	2,396,930	11.3%
	Total shareholding	**21,245,000**	**100.00%**

[1] Owned by Mårten Rød and his immediate family
[2] 10% owned by Gian Angelo Perrucci.
[3] Owned by Nils Trulsvik

The following table sets out the shareholdings of the Company's officers and directors and any shareholders that hold more than 5% or approximately 5% of the outstanding shares of the Company as of the date of this Prospectus.

Name of beneficial owner[1]	Number of Shares	%
Eksportconsult AS [1]	5,225,000	24.6%
Caberian Investment Inc. [2]	4,600,000	21.7%
Credit Suisse Securities (nominee)	1,870,600	8.8%
Bear Stearns Securities Corp. (nominee)	1,618,800	7.6%

[1] Owned by Mårten Rød and his immediate family
[2] 10% owned by Gian Angelo Perrucci.

To the knowledge of the Company, the Company is not for purposes of Norwegian law, directly or indirectly, controlled by another corporation or by any foreign government.

As of the date of this Prospectus, the total number of Shares held indirectly beneficially by directors and executive officers of the Company as a group, was 6,650,000. As of the date of this Prospectus, to the knowledge of the Company, there are no arrangements or agreements, which may at a subsequent date result in a change of control in the Company.

There are no limitations restricting foreign ownership of the Company's Shares. The Shares are equal in all respects. Each Share will have the right to one vote at the general meetings. There are no restrictions on the Company's Shares.

10.7 Shareholder Policy

InterOil will inform Oslo Børs, the Company's shareholders and the market in general on an ongoing basis of the Company's development, activities and special events, ensuring that as far as possible the pricing of the Company's Shares reflects the underlying values and expectations of future profits. Such information will, among other things, take the form of annual reports, quarterly reports, stock exchange bulletins, press releases and investor presentations when appropriate.

10.8 Dividend Policy

Company will strive to follow a dividend policy favourable to shareholders. This will be achieved by sound business development and continuous growth. The Company aims to give shareholders a competitive return on capital relative to the underlying risk. InterOil's existing dividend policy is to retain earnings in order to maintain a sound equity ratio a liquidity reserve and secure funding of product development projects. Due to this the Company does not anticipate to pay cash dividend on a regular basis in the foreseeable future. The payment of future dividends will, among other things, depend on the Company's earnings, financial condition, investment requirements and rate of growth.

10.9 Shareholder agreements

The Company is not aware of any agreements related to shares in the Company.

10.10 Articles of Association

The articles of association of InterOil are included as Appendix 1 to this Prospectus.

The Company's purpose according to its articles is activities such as exploration, development, production, purchase and sale of oil and natural gas deposits and production licences, as well as any activities related thereto, including investments in equal and similar enterprises, cf. article 3. The Company has one class of shares. The Board of Directors consist of up to seven members.

The articles of association do not provide for any rights, preferences and restrictions attaching to the Shares and do not lay down more significant conditions necessary to change the rights of shareholders than required under Norwegian law. The rights, preferences and restrictions attaching to the Shares are set out in the Public Limited Companies Act.

All Shares entitles the holder to one vote at the annual or special shareholders meeting. A shareholder may be present in person or by proxy.

The articles of association do not lay down more significant conditions necessary to change the rights of shareholders than required by the Public Limited Companies Act. Under the Public Limited Companies Act, general meetings must be convened by written notice to all shareholders whose address is known. The notice must be sent at the latest two weeks before the date of the general meeting. The notice must set forth the time and date of the meeting and specify the agenda of the meeting. It must also name the person appointed by the Board of Directors to open the meeting. All shareholders who are registered in the register of shareholders maintained by the VPS, or have otherwise reported and proved an acquisition of Shares, are entitled to admission provided pre-registration has been received by the Company four days prior to the general meeting.

The articles of association do not contain any provisions as to the manner in which general meetings of the Company are called or as to the conditions of admission to general meetings.

There are no provisions in the articles of association which would have an effect of delaying, deferring or preventing a change of control of the Company, or which require disclosure of ownership above any thresholds. However, please see Section 10.13 for a description of the requirements under the Securities Trading Act for the disclosure of transactions which cause certain thresholds to be passed.

The articles of association do not impose more stringent conditions for changing the capital of the Company than required by law.

10.11 Mandatory bid rules

Norwegian law requires any person, or associated persons that acquire more than 40% of the voting rights of a Norwegian company listed on Oslo Børs to make an unconditional general offer to acquire the whole of the outstanding share capital of that company. The offer must be made within four weeks of the transaction which triggers the obligation to make the offer. The offer is subject to approval by Oslo Børs before submission of the offer to the shareholders. The offer must be in cash or contain a cash alternative at least equivalent to any other consideration offered. The offering price per share must be at least as high as the highest price paid by the offeror in the six-month period prior to the date the 40 per cent threshold was exceeded, but at least equal to the market price when the 40% threshold was exceeded if it is clear that that market price was higher than the highest price in the preceding six months. A shareholder who fails to make the required offer must, within four weeks, dispose of sufficient shares to bring his shareholding below 40 per cent. Otherwise, Oslo Børs may cause the shares exceeding the 40 per cent limit to be sold by public auction. A shareholder who fails to make such bid within the statutory time limit cannot, as long as the mandatory bid requirement remains in force, vote for his shares or exercise any rights of

share ownership, unless a majority of the remaining shareholders approve. However, such shareholder retains the right to receive dividends and preferential rights in the event of a share capital increase. In addition, Oslo Børs may impose a daily fine upon a shareholder who fails to make the required offer.

10.12 Compulsory acquisition rules

A shareholder who, directly or via subsidiaries, acquires shares representing more than 90 per cent of the total number of issued shares as well as more than 90 per cent of the total voting rights of a company has the right (and each remaining minority shareholder of that company would have the right to require the majority shareholder) to effect a compulsory acquisition of any shares not already owned by the majority shareholder. A compulsory acquisition results in the majority shareholder becoming the owner of the shares of the minority shareholders with immediate effect.

A majority shareholder who effects a compulsory acquisition is required to offer the minority shareholders a specific price per share and to pay the consideration offered to a separate bank account for the benefit of the minority shareholders. The determination of the offer price is at the discretion of the majority shareholder. Should any minority shareholder not accept the offered price, such minority shareholder may, within a specified period of not less than two months, request that the price be set by the Norwegian courts. The cost of such court procedure would normally be charged to the account of the majority shareholder, and the courts would have full discretion in determining the consideration due to the minority shareholder as a result of the compulsory acquisition.

10.13 Disclosure of Acquisitions and Disposals

Under the Securities Trading Act, a person, entity or group acting in concert that acquires or disposes of shares, options for shares or other rights to shares resulting in its beneficial ownership, directly or indirectly, in the aggregate, reaching, exceeding or falling below the respective thresholds of 1/20, 1/10, 1/5, 1/3, 1/2, 2/3 or 9/10 of the share capital has an obligation to notify Oslo Børs immediately.

11 Legal Matters

11.1 General

Except from the description below in 11.2, the Company and the Group has no knowledge of any other legal or arbitration proceedings pending or threatened towards the Company.

11.2 Legal and arbitration proceedings

The Company and its subsidiary will from time to time be involved in disputes in the ordinary course of its business activities. The Company has not been involved in any governmental, legal or arbitration proceedings during the last twelve months and is not aware of any ongoing or threatened governmental, legal or arbitration proceedings that may be expected to have a material negative impact on the InterOil Group, except for a process with the previous CEO of MIPI; Rudolph Berends as described below.

Mr. Rudolph Berends instituted legal proceedings in November 2005 in London claiming loss and damages in the size of minimum EUR 2,700,899 relating to an allegedly invalid termination by the Company of a Management Services Agreement with Berends. InterOil is of the opinion that no contract was ever entered into. These matters are always complex and hence a provision to cover a final settlement amounting to USD 100 000 has been set aside in the financial statements as of 31 December 2005.

12 Tax Issues

Set out below is a summary of certain Norwegian tax considerations relevant to the purchase, holding and disposal of shares by shareholders that are residents of Norway for Norwegian tax purposes ("resident shareholders") and shareholders that are not resident in Norway for such purposes ("non-resident shareholders").

The summary is based on Norwegian laws, rules and regulations applicable at the date of this Prospectus, and does not address foreign tax laws. Norwegian laws, rules and regulations are subject to change, possibly on a retroactive basis. The summary is of a general nature and does not purport to be a comprehensive description of all the tax considerations that may be relevant to the Investors. Investors who wish to clarify their own tax situation should consult with and rely upon their own tax advisers. Investors resident in jurisdictions other than Norway should consult with and rely upon local tax advisors as regards the tax position in the country of residence.

12.1 Resident shareholders

This section summarizes Norwegian tax rules relevant to shareholders that are residents of Norway for Norwegian tax purposes.

12.1.1 Taxation of dividends

Resident *corporate shareholders* (i.e. limited liability companies and similar entities) are exempt from tax on dividends received on shares in Norwegian limited liability companies and similar entities.

Dividends distributed to resident *individual shareholders* are taxable as general income at a flat rate of 28% to the extent the dividends exceed a calculated tax-free allowance. The allowance is calculated separately for each share as the tax purchase price of the share (adjusted for any RISK-amounts up to 1 January 2006) multiplied with a determined risk-free interest rate, which will be based on the effective rate after tax of interest on treasury bills (Norwegian: *statskasseveksler*) with three months maturity. The part of the allowance one year exceeding the dividend distributed on the share the same year ("unused allowance") will be added to the tax purchase price of the share and be included in the basis for calculating the allowance the next year, and may also be carried forward and set off against future dividends received on, and against gains upon the realization of, the same share.

12.1.2 Taxation of capital gains upon the realization of shares

Resident *corporate shareholders* are exempt from tax on capital gains upon the realization of shares in Norwegian limited liability companies and similar entities. Losses upon the realization and costs incurred in connection with the acquisition and realization of such shares are not deductible for tax purposes.

Resident individual shareholders are subject to taxation in Norway on capital gains upon the realization of shares, and have a corresponding right to deduct losses which arise upon such realization. The tax liability applies irrespective of time of ownership and the number of shares realized. Gains are taxable as, and losses may be deducted from, general income in the year of realization. The tax rate for general income is currently 28%.

The taxable gain / deductible loss is calculated per share as the consideration received by the realization less the tax purchase price of the share (adjusted for any RISK-amounts up to 1 January 2006). Any unused allowance on a share (see above) may be set off against gains upon the realization of the same share, but this may not lead to or increase a deductible loss, i.e. any unused allowance exceeding the capital gain upon the realization of a share will be annulled.

If shares acquired at different times are realized, the shareholder must apply a "first-in first-out" (FIFO) principle when calculating the gain or loss, i.e. the shares that were first acquired will be deemed as first sold.

Costs incurred in connection with the acquisition and realization of shares may be deducted from the resident individual shareholders' general income in the year of realization.

12.1.3 Net Wealth Tax

Resident corporate shareholders are exempt from Norwegian net wealth tax.

For other resident shareholders, shares will form part of their capital and be subject to net wealth taxation by the state and the local municipality. With effect as from the income year 2006, listed shares are valued at 80% of their quoted value on 1 January in the assessment year. The maximum combined state and municipal rate of the wealth tax is 1.1%.

12.2 Non-resident shareholders

This Section summarizes Norwegian tax rules relevant to non-resident shareholders. Non-resident shareholders' tax liabilities in their home country or other countries will depend on tax rules applicable in the relevant country.

12.2.1 Taxation of dividends

Dividends paid by Norwegian limited liability companies and similar entities to non-resident shareholders, both corporate and individual, are subject to withholding tax in Norway at a flat rate of 25%, unless otherwise provided for in an applicable income tax treaty or the recipient is covered by the specific regulations for shareholders resident within the EEA (see below). Norway has entered into income tax treaties with more than 80 countries, and in most of the treaties the withholding tax rate is reduced to 15%. The shareholder's home country will normally give credit for the Norwegian withholding tax imposed on the dividends.

Non-resident *corporate shareholders* who are tax resident within the EEA are exempt from Norwegian withholding tax on dividends distributed from Norwegian limited liability companies and similar entities, provided that the shareholder is the beneficial owner of the dividends.

Non-resident *individual shareholders* who are tax resident within the EEA are subject to Norwegian withholding tax on dividends received from Norwegian companies at the regular rate or at a reduced rate determined in an applicable tax treaty. However, such shareholders may apply individually to the tax authorities for a refund of an amount corresponding to the calculated tax-free allowance on each individual share (see above). In contrast to resident individual shareholders, the authorities have stated that non-resident individual shareholders resident within the EEA may not carry forward any unused allowance.

In accordance with the present administrative system in Norway, a distributing company will normally deduct withholding tax at the applicable reduced rate when dividends are paid directly to an eligible non-resident shareholder based on information registered with the VPS (the Norwegian Central Securities Depository) as to the tax residence of the non-resident shareholder. Dividends paid to non-resident shareholders in respect of nominee registered shares are not eligible for reduced treaty-rate withholding at the time of payment unless the nominee, by agreeing to provide certain information regarding beneficial owners, has obtained approval for reduced treaty-rate withholding from the Central Office for Foreign Tax Affairs (Sentralskattekontoret for utenlandssaker).

Non-resident shareholders who have suffered a higher withholding tax than set out by an applicable tax treaty may apply to the Norwegian tax authorities for a refund of the excess withholding tax deducted.

Non-resident shareholders should consult their own advisers regarding the availability of treaty benefits in respect of dividend payments including the ability to effectively claim refunds of over-withheld amounts.

12.2.2 Taxation of capital gains upon the realization of shares

Capital gains upon the realization of shares in Norwegian companies by non-resident *corporate shareholders* are not subject to taxation in Norway.

For non-resident *individual shareholders*, capital gains upon the realization of shares will be subject to taxation in Norway if the shareholding is effectively connected with a business which the shareholder takes part in or carries out in Norway.

If a non-resident individual shareholder has been a resident of Norway for tax purposes and has realized shares less than five calendar years after termination of the tax residency in Norway, the latent capital gain on the shares at the time of such termination will be subject to taxation in Norway, provided that such latent capital gain on the shareholder's total shareholding exceeds the tax-free allowance.

12.2.3 Net Wealth Tax

Non-resident shareholders are not liable to pay net wealth tax in Norway on shares in Norwegian companies unless the shareholder is an individual and the shareholding is effectively connected with a business which the shareholder takes part in or carries out in Norway.

12.3 Resident and non-resident shareholders

12.3.1 Duties on the transfer of shares

No stamp or similar duties are currently imposed in Norway on the transfer or issuance of shares in Norwegian companies.

12.3.2 Inheritance tax

When shares are transferred either through inheritance or as a gift, such transfer may give rise to inheritance or gift tax in Norway if the decedent, at the time of death, or the donor, at the time of the gift, is a resident or citizen of Norway, or if the shares are effectively connected with a business carried out through a permanent establishment in Norway. However, in the case of inheritance tax, if the decedent was a citizen but not a resident of Norway, Norwegian inheritance tax will not be levied if inheritance tax or a similar tax is levied by the decedent's country of residence.

In the case of listed shares, the basis for the tax calculation is the market value of the shares.

13 Definitions and Glossary

The following definitions and glossary apply in this Prospectus unless dictated otherwise by the context, including the foregoing pages of this Prospectus.

13.1 Definitions

Board:...	The Board of Directors of InterOil Exploration and Production ASA.
Company:....................................	InterOil Exploration and Production ASA or when the context so requires, the InterOil Group.
IFRS:...	International Financing Reporting Standards, issued by the International Financial Reporting Interpretations Committee (IFRIC) (formerly, the "Standing Interpretations Committee" (SIC)).
Group or InterOil Group:	InterOil Exploration and Production ASA together with its subsidiaries.
InterOil:......................................	InterOil Exploration and Production ASA or when the context so requires, the Company Group.
Listing:	The Listing of the Company's shares on Oslo Børs.
Manager:	Pareto Securities ASA.
MIPI:	Mercantile International Petroleum Inc.
NOK:...	Norwegian Kroner, the lawful currency of the Kingdom of Norway.
Norwegian Public Limited Companies Act:...........................	The Norwegian Public Limited Companies Act of 13 June 1997 no. 45 ("Allmennaksjeloven").
Norwegian Securities Trading Act:..	The Securities Trading Act of 19 June 1997 no. 79 ("Verdipapirhandelloven").
Norwegian Stock Exchange Regulations:	The Stock Exchange Regulations of 17 January 1994 no. 30, last amended by Regulation of 9 December 2005 nr. 1427 ("Børsforskriften").
Oslo Børs:	Oslo Børs ASA (translated "the Oslo Stock Exchange").
Prospectus:	This Prospectus dated 17 July 2006 prepared in connection with the Listing of the Company's shares on Oslo Børs.
Share(s):	"Shares" means common shares in the capital of InterOil and "Share" means any one of them.
TCW:	Trust Company of the West Asset Management Company.
TCW Loan:	The 9% secured loan of USD 42 million, granted by TCW, with maturity in October 2012.
TNOK:	NOK 1,000.
USD:	United States Dollars.
VPS:	Verdipapirsentralen (Norwegian Central Securities Depository), which organizes the Norwegian paperless securities registration system.

13.2 Glossary of Terms

Term	Definition
Acre:..	4047 square meters.
Barrel:	159 litres, a measuring unit for volume.
Bbl:...	Barrels of oil.
Bboe:..	Billion barrels of oil equivalent.
Boe:..	Barrel of oil equivalent, a measuring unit for oil and natural gas.
Boepd:..	Barrels of oil equivalent per day.
BOPD:..	Barrels of oil per day.
E&P:...	Exploration and Production.
Ft:...	Feet (1 feet = 0.3048 metres).
GAAP:	Generally Accepted Accounting Principles.
IEA:..	International Energy Agency.
IFRS:..	International Financial Reporting Standards and International Accounting Standards.
KBbl:..	Thousand Barrels per day.
MOU:...	Memoranda of Understanding.
OPEC:	Organisation of Petroleum Exporting Countries.
Probable Reserves:	As approved by the Society of Petroleum Engineers (SPE) and the World Petroleum Congress (WPC) in March 1997, probable reserves are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable. In this context, when probabilistic methods are used, there should be at least a 50% probability that the quantities actually recovered will equal or exceed the sum of estimated proved plus probable reserves.
Prospective Resources:	As approved by the Society of Petroleum Engineers (SPE), the World Petroleum Congress "(WPC)" and the American Association of Petroleum Geologists (AAPG), prospective resources are those quantities of petroleum, which are estimated, on a given date, to be potentially recoverable from undiscovered accumulations.
Proven Reserves:	As approved by the Society of Petroleum Engineers (SPE) and the World Petroleum Congress (WPC) in March 1997, proved reserves are those quantities of petroleum which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods and government regulations. If deterministic methods are used, the term reasonable certainty is intended to express a high decree of confidence that the quantities will be recovered. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate.
PSA:...	Production Sharing Agreement.
WTI:...	West Texas Intermediate crude.
2P:..	Proven and Probable reserves.

14 Appendices and documents on display

14.1 Appendices

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Appendix 2: Annual Report for 2005..A 2

Appendix 3: Condensed Consolidated Interim Financial Information for the first quarter 2006............................A 32

Appendix 4: Auditors statement on review of pro forma adjustments...A 35

Appendix 5: Annual Report 2004 for Mercantile International Petroleum Inc...A 36

Appendix 6: Annual Report 2003 for Mercantile International Petroleum Inc...A 44

14.2 Documents on display

Copies of the following documents will during the life of this Prospectus be available for inspection at any time during normal business hours on any business day free of charge at the registered office of the Company and may also be inspected at www.interoil.no:

i. the articles of associations of the Company;

ii. first quarter report for 2006,

iii. historical financial information including auditor's report for the financial years ending 31 December 2005,

iv. historical financial information for Mercantile International Petroleum Inc. for 2004 and 2003,

v. stock exchange notices, including quarterly reports, distributed by the Company through Oslo Børs' information system at www.newsweb.no.

Appendix 1: Articles of Association[4]

ARTICLES OF ASSOCIATION
FOR
INTEROIL EXPLORATION AND PRODUCTION ASA

(as per extraordinary general meeting on 29 June 2006)

§ 1

The Company's name is InterOil Exploration and Production ASA. The Company is a public limited company.

§ 2

The Company's business office is in the municipality of Bærum.

§ 3

The Company's business activity shall comprise activities such as exploration, development, production, purchase and sale of oil and natural gas deposits and production licences, as well as any activities related thereto, including investments in equal and similar enterprises.

§ 4

The Company's share capital is NOK 1,062,250 divided into 21,245,000 shares each of a nominal value of NOK 0.05. The shares shall be registered in the Securities Registry ("Verdipapirsentralen").

§ 5

The Company's board shall consist of a minimum of one and a maximum of seven directors. The Chairman of the Board shall have the signing authority of the Company.

§ 6

Shareholders or their representatives wishing to attend and vote at the General Meeting must inform the Company of this four days prior to the General Meeting.

§ 7

The Company shall have a Nomination Committee, elected by the General Meeting. The Nomination Committee shall make recommendations to the General Meeting regarding the election of members to the Board of Directors. The Chairman of the Board of Directors shall, without having any voting right, be summoned to at least one meeting with the Nomination Committee before the Committee gives its final recommendation.

The Nomination Committee shall consist of two members who shall be shareholders or representatives of shareholders, and who shall be independent of the Board of Directors and the operational management. The members of the Nomination Committee shall be elected for periods of two years.

§ 8

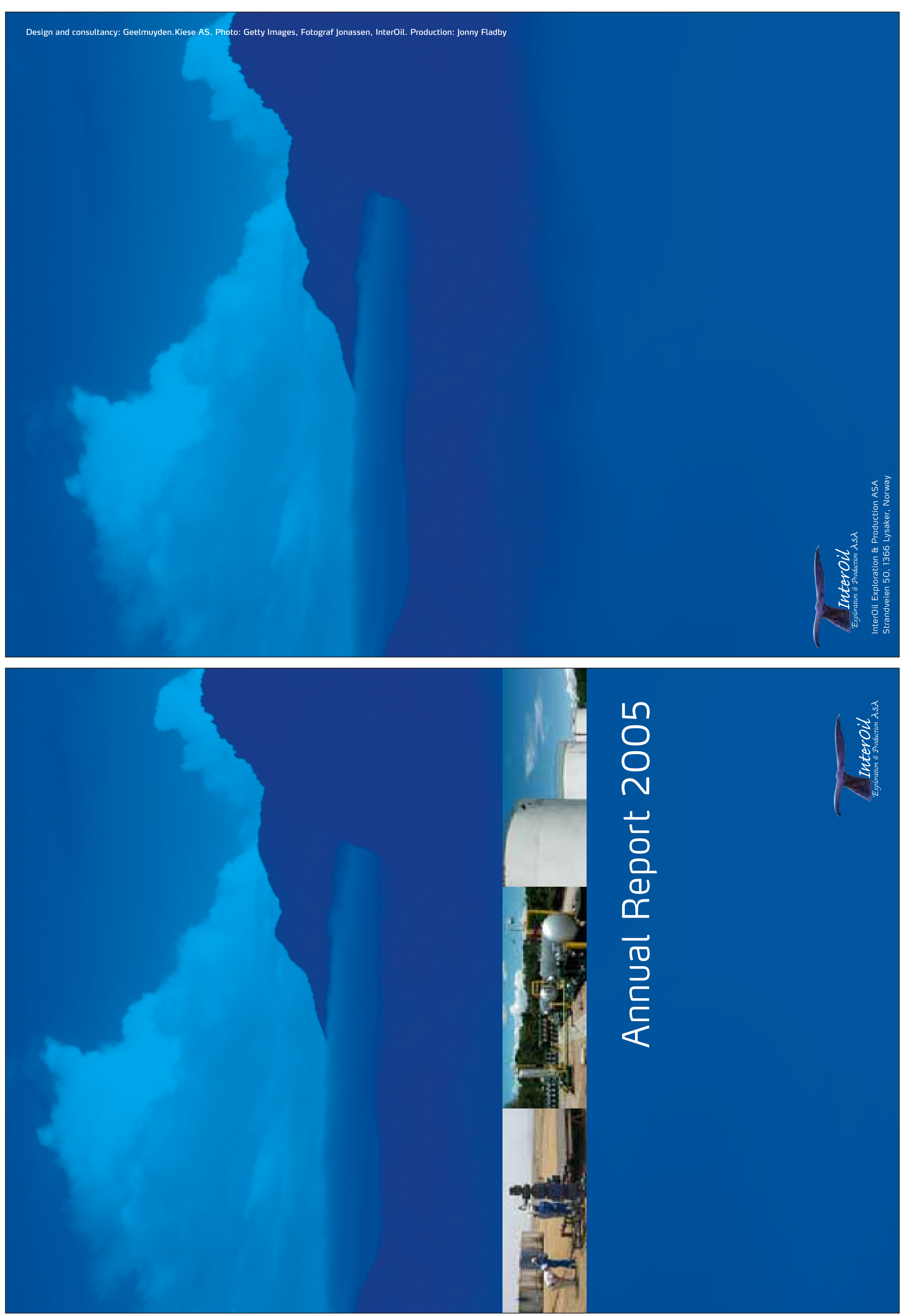
The annual general meeting shall discuss and resolve the following matters:

1. Approval of the annual accounts and the annual report, including distribution of dividend.
2. Any other matters which according to law or the Articles of Association fall within the scope of the general meeting.

*****

[4] Unofficial translation from Norwegian

Appendix 2: Annual Report for 2005



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Mårten Rød
Chairman

Chairman's Remarks

INTEROIL'S MAIN LONG-TERM ambition is to be a strong participant in the oil and gas sector in West Africa.

As we speak, we have just been successful and offered a large participation in what we believe to be two very interesting shallow water offshore blocks in Angola.

The major shareholders have spent more than 25 years in the Western part of this continent, and built strong relations after decades of commitment and proven success.

Part of our team, however, also worked a long time in Latin America. The acquisition and restructuring of several producing oilfields in Peru and Colombia, was therefore an important first step in our strategy.

InterOil now qualifies as an oil and gas producer with more than 50 years of history. Our management has implemented with great success, a value added program. We shall continue to grow through selective investments in this part of the world.

Peru and Colombia have in addition contributed, allowing InterOil to get up to speed on all elements of operational challenges, and employ a team of top professionals anxious to participate and build a new company from scratch.

All employees in Norway and Switzerland, Peru and Colombia, have taken full responsibility and risen to the task.

We are now in an excellent position to take on larger commitments, well set for future growth, and ready to focus on new challenges.

Thank you team!

Best regards

Mårten Rød
Chairman

Board/ Management

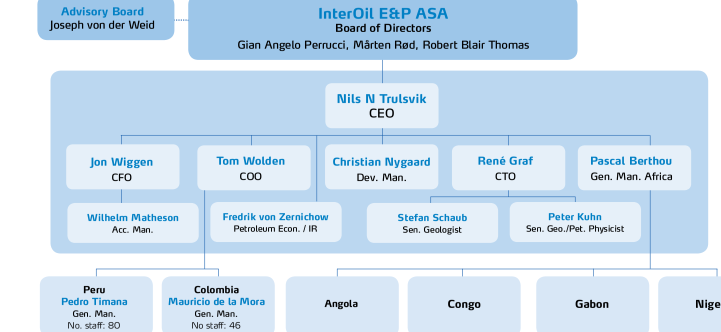
Mårten Rød, born 1948, has long experience as entrepreneur and from the oil and gas industry, both from upstream and downstream business. He worked 11 years for Arco in the North Sea, founded Northern Energy UK in 1998, an oil company with production in Texas and Oklahoma. From 1995 he was President of InterOil Norway, which participated in various oil and mineral projects in West-Africa.

Robert Blair Thomas, born 1963, is Group Managing Director for Energy & Infrastructure at Trust Company of the West (TCW). He was a Senior investment Officer involved in structuring and negotiating private sector non-recourse project finance transactions related to infrastructure and natural resource development in Global Energy and Infrastructure.

Gian Angelo Perrucci, born 1943, is an Italian entrepreneur. He previously built up a major shipping company in USA and Europe. During the last 15 years, he has developed a substantial major logistics operation in West Africa including supply bases, engineering and production yards, as well as offshore support vessels.

Joseph von der Weid, born 1934, has long experience from executive positions for Shell in South America. Mr. Weid has been E&P Manager in Shell Argentina, General Manager in Shell Peru (1981-86), President and CEO in Shell Colombia (1986-88) and President in Shell Argentina (1988-91).

Nils N. Trulsvik, born 1948, is a petroleum explorationist with extensive experience throughout the world. Mr. Trulsvik worked seven years with Saga Petroleum on assignments in the North Sea, Mediterranean, Africa, South and North America. He co-founded Nopec in 1981, working for 13 years in Northwest Europe, Africa and the Far East, and as Managing Director from 1987 until 1993. During the last 10 years, Mr Trulsvik has been working with various oil and gas projects.



René Graf, born 1947, has long international experience, covering all aspects of exploration with focus on geophysical field operations, processing and interpretation, both 2-D and 3-D, land and marine seismic. This experience has been acquired during a period of almost 20 years working for Shell International in The Netherlands, France, Malaysia and Colombia.

Jon Wiggen, born 1950, is a state authorized auditor and has over 30 years experience in various businesses including several publicly listed companies. He was CFO for Brynestad Group of companies for several years.

Tom Wolden, born 1955, is a petroleum geologist with 22 years of experience in the oil business focused on offshore in NW Europe, Africa, Russia, SE Asia, Middle East and Norway. Mr. Wolden has been working for Saga Petroleum, Nopec and PGS and he was business area manager in the Middle East and Mediterranean for PGS Exploration AS for the last 6 years.

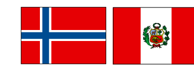
Christian Nygaard, born 1952, has more than 25 years of international experience in oil related industries. Mr. Nygaard was Vice President of sales and business development for PGS Production, Technip, Spars International Inc. and Aker Maritime.

Pascal Berthou, born 1956, has been working as General Manager for different oil and gas projects in Angola, Congo, Nigeria and Gabon for the last 20 years.

Peru

Official name:	Republica del Peru
Population:	27.9 mill.
Area:	1 285 186 km2
Political:	Republic
Capital:	Lima
Language:	Spanish
Religion:	Roman Catholic
Currency:	Sol
GDP (PPP):	169.5 billion $ (2005)
GDP per capita:	6,100 $ (2005)
Major exports:	Copper, gold and fishmeal
Oil prod:	120,000 bbl/d
Oil cons:	157,000 bbl/d
Oil proved res:	370 million bbl

Sources: CIA World Fact Book
Economist Country Briefing



InterOil in Peru (2005)

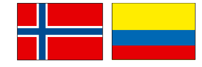
Number of employees:	80
Total number of wells:	approx. 800
Area:	164,000 acres (663 km2)
Annual production:	623,000 bbl
Average daily production:	1,706 bbl
OPEX:	3,074,000 USD

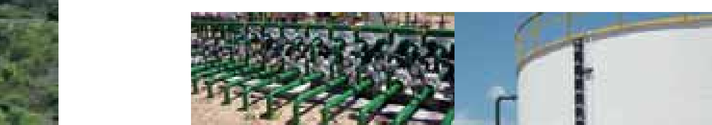
Due to increased political and economic stability, Peru is rapidly attracting new foreign investments in the energy sector. Recent policy reforms in the oil sector make Peruvian contract terms, alongside Colombian, among the best in Latin America. InterOil takes its responsibility in Latin America seriously and monitors the political and social situation in the region closely. We are grateful for the recent positive developments in Peru and Colombia, and it is encouraging to be part of a traditional, yet rapidly expanding oil industry in a promising environment.

In Peru InterOil's activities and assets consist of three companies and two producing areas. InterOil is licenced to operate on two Peruvian blocks, Block III and Block IV. Block III is licensed to and operated by Mercantile Peru Oil and Gas S.A, whereas Compania Petrolera Rio Brava S.A does the same for Block IV. InterOil is located in the Talara Area of northwestern Peru. Block III and IV are located close to Talara, where also the InterOil main office is located. Talara houses most of the region's petroleum industry. The industry has been involved in this part of Peru for more than 50 years. Several other oil companies are active in the region, e.g. Petrobras Pluspetrol, Occidental Petroleum, Petro-Tech Peruana and the state owned Petroperu.

By the end of April 2006 InterOil had completed 7 out of 11 wells planned in 2006. All wells are producers. As a result of this, production increased from 1 600 bopd in September 2005, to 2 400 bopd by the end of April 2006. The completions of 4 remaining wells are expected to increase production further.

According to Gaffney, Cline and Associates (independent reservoir engineers), InterOil's net proven oil reserves in Peru as of December 31 2005 were 8.3 million bbls and 4.8 million bbls net of royalties. InterOils net proven and probable oil reserves in Peru as of December 31 2005 were 10.4 million bbls and 6.0 million bbls net of royalties.





Colombia

Official name:	Republica de Colombia
Population:	46.0 million
Area:	1 138 910 km2
Form of government:	Republic
Capital:	Bogotá
Language:	Spanish
Religion:	Roman Catholic
Currency:	Colombian Pesos
GDP (PPP):	303.7 billion $ (2005)
GDP per capita:	7,100 $ (2005)
Major exports:	Petroleum and petroleum products coal, coffee
Oil prod:	512,400 bbl/d
Oil cons:	270,000 bbl/d
Oil proved res:	1.492 billion bbl

Sources: CIA World Fact Book
Economist Country Briefing

InterOil in Colombia (2005)

Number of employees:	46
Wells in production:	42
Area:	62, 945 acres (258 km2)
Annual production:	305,000 bbl
Average daily production:	836 bbl
OPEX:	2,303,000 USD

Increasingly favourable economic and political conditions and recent oil policy reforms, make Colombia one of Latin America's most sought after markets in the petroleum sector.

In general terms, Latin America is under-explored with large oil and natural gas reserves. This is particularly true for Colombia, where estimates show that only 11% of Colombia's total sedimentary area has been licensed.

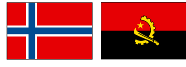
In Colombia, InterOil's assets and activities are operated through Mercantile Colombia Oil and Gas Inc., and cover a total area of 258 km2. All contract areas are located in the Rio Magdalena Basin. InterOil's main office is located in Bogotá and has its operations in the upper Magdalena Valley, 100 km south-west of Bogotá. The oil is piped locally into storage tanks and transported by truck 200 km south to Hocol´s storage facility.

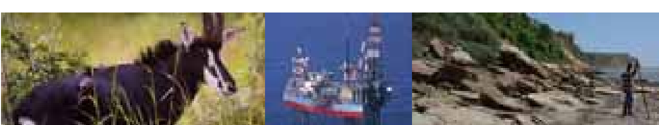
By April 2006 InterOil has drilled 6 out of 8 planned wells in 2006. Oil was encountered in all but one well. InterOil, as the new owner, has changed the drilling program and proposed to Ecopetrol a new 3-D seismic in order to better evaluate the prospective oil reservoirs. We trust the change will result in higher yield and additional production.

One new technical assistance contract was awarded in 2005 concerning an area in the lower Magdalena Valley, Northern Colombia. Geological and geophysical work is ongoing with the aim to either make a formal bid for the block or relinquish.

According to Gaffney, Cline and Associates InterOil's proven oil reserves in Colombia as of December 31 2005 were 3.5 million bbls and 2.9 million bbls net of royalties. InterOil's net proven and probable oil reserves in Colombia as of December 31 2005 were 5.6 million bbls and 4.7 bbls net of royalties.

Angola





Official name:	Republic of Angola
Area:	1 246 700 sq.km
Population:	13.5 million
Form of government:	Republic
Capital:	Luanda
Language:	Portuguese (official), Ovimbundu, Kimbundu in addition to various Bantu dialects
Religion:	Roman Catholic, other Christian denominations, some Islam, local religions
Currency:	Kwanza
GDP (PPP):	45.93 billion $ (2005)
GDP per capita:	3,200 $ (2005)
Main industries:	Oil, gas, diamonds
Oil production:	1.6 mill bbl/d (2005)
Oil consumption:	46,000 bbl/d (2003)
Oil proved res:	25 billion bbl (2005)

Sources: CIA World Fact Book
Economist Country Briefing

InterOil in Angola

Area	Block 6 (4930 km²)
Partners	Petrobras (Operator, 40%) InterOil Exploration & Production (20%) Sonangol (20%) Initial Oil & Gas SA (10%) Falcon Oil (10%)
Area	Block 5 (5708 km²)
Partners	Vaalco Energy (Operator, 40%) InterOil Exploration & Production (40%) Sonangol (20%)

In addition to its activities in Colombia and Peru, InterOil is in the process of establishing operations in West-Africa. Angola's economy has undergone a period of rapid transformation in recent years, moving from a quarter century of war to being the fastest growing economy in Africa and one of the fastest in the world. Growth is almost entirely driven by rising oil production which surpassed 1.2 million barrels per day in late 2005. In Angola the historical hit track record on drilling is 50%.

The republic of Angola includes three of the major salt basins on Africa's Atlantic margin. The three major basins are the Congo Basin in the North, Kwanza/ Benguela Basin in the centre and the Namibe Basin to the South.

In May 2006 InterOil was offered to participate in two licences in Block 5 & 6 in Angola's Kwanza Basin. InterOil will receive 40% in Block 5, where Vaalco is the operator and 20% in Block 6 where Petrobas is the operator.

Block 5 was first licensed to Total in the 1970s. The area was further developed by Conoco and Sonangol throughout the 1980s and 1990s. The continued presence of oil in five wells indicates that oil is generated in the area.

Block 6 was also first licensed to Total. After being further developed by Conoco and Sonangol, it will now be operated by Petrobas. The discovery of heavy oil in two wells gives rise to optimism, as the operator has extensive experience in the development of such fields.

Board of Directors' Report

VISION AND STRATEGY InterOil Exploration and Production ASA ("InterOil") was founded during the summer of 2005.

Our vision is to develop InterOil as a major player in the energy sector in West Africa and South America. Our goal will be achieved by defining objectives, and the first stepping stone is already in place. The Company has a clear focus on this task, since organic growth within existing assets in Peru and Colombia is achievable, both in terms of production and cash flow.

In 2006, we shall grow by acquiring additional producing assets, as well as participating in offshore and onshore exploration with the ultimate aim to achieve a balance between the Company's portfolio of exploration, appraisal, developing and producing properties.

INTEROIL'S BUSINESS

InterOil acquired the Peruvian and Colombian assets in the end of September, 2005. The Founders recognized the opportunity, changed management, restructured the operation and created a basis for future growth. After reviewing the operations and securing the required approvals, we started a program in both countries with the aim to increase production.

Total production per month in South America is now up from approximately 2 600 barrels per day ("bopd") in 2005 to 3 400 bopd in May 2006. The production for (Q4) 2005 was 221 367 barrels of oil. The production is sold to Hocol (Colombia) and PetroPeru. These sales are made at market price.

Last month, we were offered participation in two blocks in the last round of concessions in Angola; 40% in our first priority (Block 5), and 20% in our second priority (block 6).

We believe this region will be increasingly important and focused upon by the world oil industry over the next decades. InterOil is now well positioned to participate further.

FINANCIAL OVERVIEW

(Consolidated Financial Statements)
The operating revenue and gross profit during last quarter 2005 (Q4) was USD 8.0 million and USD 4.8 million respectively. Operating expenses and other income were net USD 2.5 million. Financial cost for the period was USD 1.5 million, of which the amortisation and interest expense to Trust Company of the West ("TCW") related to the acquisition loan, equalled USD 1.2 million. Profit for the year was USD 0.3 million after a tax charge of USD 0.5 million.

The result for Q4 must be considered in light of that extraordinary expenses were incurred in order to finance the acquisition, and the implementation of new control routines for Peru and Colombia. It also includes acquisition costs for evaluating new business opportunities both in Peru and Columbia as well as in West Africa. A cost of USD 0.8 million to cover exploration expenses due to drilling a dry well in Colombia, is included.

Capitalized expenditures for the period was USD 3.6 million, and USD 65.6 million relates to the purchase of the oil assets in Peru and Colombia as shown in Note 29.

InterOil's total assets as of December 31 2005 were USD 124.9 million and total cash and cash equivalents were USD 8.4 million. In addition, InterOil had USD 10.9 million in Money Market Fund. The equity ratio of the group was 37.6 %.

In accordance with Norwegian Accounting Law, InterOil confirms that its accounts have been prepared on a going concern basis.

PARENT COMPANY ACCOUNTS AND ALLOCATION OF PROFIT

The profit and loss account for the period for the parent company, InterOil Exploration and Production ASA, showed a net loss of USD 1.6 million. The board of directors propose to transfer this loss, in full, to the share premium reserve. The parent company's equity totalled USD 45.1 million as of December 31 2005. The parent company has no distributable reserves as of year-end 2005.

FINANCIAL RISK

InterOil's revenues are invoiced to the customers in USD, while operating expenses are charged in USD, NOK, PEN and COP. InterOil uses no derivative financial instruments to hedge the currency risk exposure.

The profitability and cash flow of InterOil's operations will be dependent upon the market price of crude oil, which has shown a tendency to fluctuate. If the price of oil and gas products should drop significantly, the economics of our projects would be reduced. However, in order to demonstrate a prudent approach, our budget forecasted oil price is USD 40 per barrel during the second half of 2006, which we believe to be on the safe side.

ORGANISATION

InterOil has its main office at Lysaker, Norway. There are a total of 134 employees in the Group. We also employ consultants to supplement peak work loads.

Our core area of expertise reflects an upstream oil and gas company. This includes geology, geophysics, reservoir, production and development engineers. Since we are operators in both Peru and Colombia, we also have drilling and completion engineers, as well as field workers that maintain and service our production equipment.

HEALTH, SAFETY AND ENVIRONMENT

InterOil carries out its operations to the best health, safety and environment (HSE) practices. The activities in Peru and Colombia can pollute the environment. There were no major accidents or any environmental claims during the year. InterOil's activities satisfied all statutory environmental requirements.

There is a policy of equal pay for equal work. This means that men and women in the same job shall receive equal pay provided all other factors are equal. The Board is currently of the opinion that it is not necessary to implement any further equal opportunity measures.

CORPORATE GOVERNANCE

The Company has adopted the recommended corporate guidelines under the Norwegian Code of Practice for Corporate Governance (the "Corporate Governance Code"). At this stage we do not know of any aspects of non-compliance with the Corporate Governance Code.

OUTLOOK

Production was 245 421 barrels in Q1 2006, up from 221 367 in Q4 2005. Additional increase resulting from the successful drilling in Peru, will have full effect in Q2 2006.

Drilling will continue, mainly in Peru during Q2 2006. In Colombia, drilling of two new wells are planned; one in Toqui Toqui (June 2006), and one in Puli B (August 2006). Additional activities for Q2 2006 consist of workovers mainly in Toqui Toqui in order to optimize production.

A 80km² 3D seismic survey will be undertaken in order to establish a better detail of the subsurface in our most productive area in Colombia, and to ensure a greater drilling success in the future. The survey will be completed and fully analysed by Q4 2006.

The possibility to participate in two offshore blocks in Angola is significant for InterOil, both in terms of risk and reward. Oil was earlier discovered (mid 1980s) in both of the blocks, but there still needs to be major work done in terms of seismic, evaluation and drilling before declared commercial.

InterOil is currently reviewing several West African exploration, developing and producing assets with the aim to obtain a balanced portfolio.

The board of directors has a positive outlook for 2006 and expects growth and profitability during this year. The Board is confident that cash flow from existing operations, combined with new equity and/or loans, will provide sufficient liquidity in order to cover the planned investment program.

London, 15 May 2006
The Board of Interoil Exploration & Production ASA

Mårten Rød
Chairman of Board

Gian Angelo Perruci
Member of the Board

Blair Thomas
Member of the Board

Nils Trulsvik
Chief Executive Officer

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InterOil

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INTEROIL EXPLORATION AND PRODUCTION ASA
CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2005

CONSOLIDATED INCOME STATEMENT

Amounts in USD 1 000 unless otherwise stated

For the period from 2 May 2005 (inception) to 31 December 2005	**Note**	**2005**
Sales	7	7 991
Cost of goods sold	8	-3 240
Gross profit		4 751
Tariffs and transportation		-204
Exploration cost expensed		-783
Administrative expense	9	-1 501
Other income	16	181
Other operating expenses	10	-143
Profit from operating activities		**2 301**
Finance costs – net	11	-1 522
Profit before income tax		**780**
Income tax expense	12	-503
Net profit		**276**
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in USD per share)		
– basic	25	0.04
– diluted	25	0.04

CONSOLIDATED BALANCE SHEET

Amounts in USD 1 000

As of 31 December	Note	2005
ASSETS		
Non-current assets		
Property, plant and equipment	13	97 911
Deferred income tax assets	12	689
Total non-current assets		**98 600**
Current assets		
Inventories	15	493
Trade and other receivables	14	6 428
Financial assets at fair value through profit or loss	16	10 901
Cash and cash equivalents	17	8 437
Total current assets		**26 259**
TOTAL ASSETS		**124 859**
EQUITY		
Share capital and share premium	18	43 574
Other reserves	19	3 096
Retained earnings		276
Total equity		**46 946**
LIABILITIES		
Non-current liabilities		
Interest-bearing loan	20, 21	35 135
Deferred income tax liabilities	12	21 042
Provisions for other liabilities and charges	22	929
Total non-current liabilities		**57 105**

As of 31 December	Note	2005
Current liabilities		
Trade and other payables	24	12 902
Income tax liabilities	12	1 166
Subordinated loan, related parties	20	6 000
Current interest-bearing liabilities	20,21	639
Provisions for other liabilities and charges	22	100
Total current liabilities		**20 807**
Total liabilities		**77 913**
TOTAL EQUITY AND LIABILITIES		**124 859**

London, 15 May 2006
The Board of InterOil Exploration & Production ASA

Mårten Rød
Chairman of Board

Gian Angelo Perruci
Member of the Board

Blair Thomas
Member of the Board

Nils Trulsvik
Chief Executive Officer

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Amounts in USD 1 000

For the period from 2 May 2005 (inception) to 31 December 2005	Note	Share capital and share premium	Other reserves	Retained earnings	Total equity
Inception on 2 May 2005	18	16	–	–	16
Issue of share capital, net of share issuance cost 15 September 2005	18	63	–	–	63
Issue of share capital, net of share issuance cost 30 September 2005, net of tax	18	43 495	–	–	43 495
Equity component interest bearing debt, net of tax	19	–	3 096	–	–
Net profit for the period				276	276
Balance at 31 December 2005		**43 574**	**3 096**	**276**	**46 946**

CONSOLIDATED CASH FLOW STATEMENT

Amounts in USD 1 000

For the period from 2 May 2005 (inception) to 31 December 2005	Note	2005
Cash generated from operations		
Profit for the period		**276**
Income tax expense		503
Depreciation and amortization	13	1 800
Interest received from financial assets at fair value through profit or loss	16	-181
Amortization of debt issuance cost and equity component	21	260
Interest expense	11	1 206
Changes in assets & liabilities		
Inventories		63
Trade and other receivables		613
Trade and other payables		2 702
Other provision for other liabilities		147
Interest paid		-230
Taxes paid		-799
Net cash generated from operating activities		**6 360**
Cash flows from investing activities		
Acquisition of subsidiaries, net of cash acquired and selling credit	29	-65 580
Purchases of property, plant and equipment (PPE)	13	-3 604
Other financial assets at fair value through profit or loss	16	-10 720
Net cash used in investing activities		**-79 904**
Cash flows from financing activities		
Proceeds from issuance of ordinary shares (excluding tax effect)	18	42 996
Proceeds from issuance of interest-bearing loan inclusive equity component	21	39 175
Repayment of interest bearing debt		-190
Net cash used in financing activities		**81 981**
Net increase in cash and cash equivalents		8 437
Cash and cash equivalents at beginning of the period		0
Cash and cash equivalents at end of the year	**17**	**8 437**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. Corporate information

InterOil Exploration and Production ASA ("the Company") and its subsidiaries (together 'the Group' or InterOil) is an upstream oil exploration and production company focused on South America and Africa. InterOil currently has oil exploration activities in Peru and Colombia, while it is in process of establishing operations in West Africa.

The Company was established on 2 May 2005 as a Norwegian Private Limited Company ("AS"). It was converted to a Norwegian Public Limited Company ("ASA") on 14 November 2005. The Company is registered in the Register of Business Enterprises with org. no: 988247006. The Company's registered office is Strandveien 50, 1366 Lysaker.

The Group activities in Peru and Colombia is the result of the acquisition of assets previously owned by the oil exploration company Mercantile International Petroleum Inc. ("MIPI"). In 2004 MIPI was looking to sell its oil exploration activities in Peru and Colombia. Negotiations for the acquisition of MIPI's operations and assets in Peru and Colombia started in September 2004, and were made effective on 27 September 2005. On the 9 of June 2005 InterOil Exploration SA entered into a Sales and Purchase Agreement ("SPA") with MIPI.

The assets in Peru and Colombia were originally acquired by InterOil Exploration SA, a Swiss company which acted on behalf of the Company. Eventually the assets were transferred to another 100% subsidiary (InterOil Exploration and Production Latin America AS) of the Company.

These consolidated financial statements have been approved for issue by the Board of Directors on 15 May 2006.

2. Summary of significant accounting policies

The principal accounting policies applied in preparation of these consolidated financial statements are set out below.

2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and correspond with the interpretation of the International Standards Board. The consolidated financial statement is presented in USD and is rounded up to thousands (1 000). The consolidated financial statements have been prepared under the historical cost convention, except for financial assets at fair value through profit or loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

The Group has implemented IFRS 6, Exploration for and Evaluation of Mineral Resources. The standard requires the use of successful effort method of accounting which has been implemented by the Group. IFRS 6 also requires the Group to disclose certain information which has been implemented in the disclosure to the consolidated financial statements.

Standards, interpretations and amendments to published standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2006 or later periods but which the Group has not early adopted, as follows:

IAS 39 (Amendment), Cash Flow Hedge Accounting of Forecast Intragroup Transactions (effective from 1 January 2006)

The amendment allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the consolidated financial statements, provided that: (a) the transaction is denominated in a currency other than the functional currency of the entity

entering into that transaction; and (b) the foreign currency risk will affect consolidated profit or loss. This amendment is not relevant to the Group's operations, as the Group has not entered into any intragroup transactions that would qualify as a hedged item in the consolidated financial statements as of December 31, 2005 and 2004.

IAS 39 (Amendment), The Fair Value Option (effective from 1 January 2006)
This amendment changes the definition of financial instruments classified at fair value through profit or loss and restricts the ability to designate financial instruments as part of this category. The Group believes that this amendment is not applicable, as the Group has not entered into any such financial instruments.

IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts (effective from 1 January 2006)
This amendment requires issued financial guarantees, other than those previously asserted by the entity to be insurance contracts, to be initially recognised at their fair value, and subsequently measured at the higher of (a) the unamortised balance of the related fees received and deferred, and (b) the expenditure required to settle the commitment at the balance sheet date. Management has considered this amendment to IAS 39 and IFRS 4 (Amendment) and has concluded that the amendments are not currently relevant to the Group.

IFRS 7, Financial Instruments: Disclosures, and a complementary Amendment to IAS 1, Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007)
IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including sensitivity analysis to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. It is applicable to all entities that report under IFRS. The amendment to IAS 1 introduces disclosures about the level of an entity's capital and how it manages capital. The Group assessed the impact of IFRS 7 and the amendment to IAS 1 and concluded that the main additional disclosures will be the sensitivity analysis to market risk and the capital disclosures required by the amendment of IAS 1. The Group will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006)
IFRIC 4 requires the determination of whether an arrangement contains a lease to be based on the substance of the arrangement. It requires an assessment of whether: (a) fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset); and (b) the arrangement conveys a right to use the asset. Management has assessed the impact of IFRIC 4 on the Group's operations and concluded that it is currently not relevant.

IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006).
The Group believes that this amendment is not currently applicable.

2.2 Consolidation

Subsidiaries
Subsidiaries are all entities over which the Group that has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases. All subsidiaries have been incepted by the parent company.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. Any excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill if applicable.

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

Consolidated subsidiaries
Consolidated subsidiaries are specified in note 26.

2.3 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

2.4 Foreign currency translation

(a) Functional and presentation currency
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in USD, which is the functional currency for the parent company and all subsidiaries and the presentation currency for the Group.

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

2.5 Exploration and production rights assets

Oil exploration expenditures are accounted for using the successful efforts method of accounting. Costs are accumulated on a field-by-field basis. Geological and geophysical costs are expensed as incurred. Costs directly associated with an exploration well, and exploration and property leasehold acquisition costs, are capitalised until the determination of reserves is evaluated. If the commercial discovery has not been achieved, these costs are charged to expense.

Capitalisation is made within property, plant and equipment according to the nature of the expenditure.

Once commercial reserves are found, exploration and production rights assets are tested for impairment and transferred to development assets. No depreciation and/or amortisation is charged during the developement phase.

2.6 Development assets

Expenditure on the construction, installation or completion of infrastructure facilities such as production equipment, pipelines and the drilling of commercially proven development wells is capitalised within tangible assets. When development is completed on a specific field, it is transferred to production assets. No depreciation and/or amortisation is charged during the exploration phase.

2.7 Oil production assets

Oil production assets are aggregated exploration, production rights assets and development expenditures associated with the production of proved reserves. Furthermore, the oil production assets include property leasehold acquisition costs directly attributable to production assets.

2.8 Depreciation and amortisation

Oil assets that are purchased are depreciated and amortised using the unit-of-production method based on proved reserves. Exploration and development assets transferred to production assets are depreciated and amortised using the unit of production method based on proved developed reserves, which are oil mineral reserves estimated to be recovered from existing facilities using current operating methods.

2.9 Impairment – production right, exploration and development assets

Production right, exploration and development assets are tested for impairment when reclassified to development assets or whenever facts and circumstances indicate impairment. An impairment loss is recognised for the amount by which the assets' carrying amount exceeds their recoverable amount. The recoverable amount is the higher of the assets' fair value less costs to sell and their value in use. For the purposes of assessing impairment, the assets subject to testing are grouped with existing cash-generating units (CGUs) of production fields that are located in the same geographical region.

2.10 Impairment – oil production assets

Oil production assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The 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, the proved oil and gas properties subject to testing are grouped with existing cash-generating units (CGUs) of production fields that are located in the same geographical region.

2.11 Other property, plant and equipment

All other property, plant and equipment is stated at historical cost less depreciation. Historical cost include expenditures that is directly attributable to the acquisition of the items. Depreciation is calculated using the straight-line method to allocate their cost to their values over their estimated useful lives. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

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

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

2.12 Financial assets at fair value through profit or loss

A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Changes in fair value of such derivatives are recognised within operating income (loss) in the income statement.

2.13 Trade receivables

Trade receivables are recognised initially at fair value less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due, according to the original terms of receivables.

2.14 Inventories

Inventories are valued using the First-In-First-Out principle. Inventory cost includes raw material, freight, and direct production expenses together with a portion of indirect expenses.

2.15 Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less. All cash and cash equivalents not available to the Group at the balance sheet date is classified as restricted as specified in note 17.

2.16 Share capital

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

2.17 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method. The fair value of the liability portion of the loan with detachable equity instrument (i.e., warrants) is determined using a market interest rate for an equivalent loan without warrants. This amount is recorded as a liability on an amortized cost basis. The remainder of the proceeds is allocated to the equity element of the financing agreement, i.e. the warrants. The equity element is recognized and included in shareholders' equity, net of any income tax effects. Borrowings are classified as current liabilities, unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

2.18 Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting, nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

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

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

2.19 Provisions

General:

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of past event and it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

Abandonment and decommissioning liabilities:

In accordance with the terms of the license concessions for licenses where the Group has ownership interest, the local

authorities may instruct the license holders to partly or completely remove the facilities at the end of production or when the concession period expires. Upon initial recognition of a liability, the company calculates and records the net present value related to future abandonment and decommissioning. The same amount is capitalised as part of the cost price of the asset and depreciated using the unit of production method. The change in the time value of the liability related to the abandonment and decommissioning is charged to expense as other expenses and increases the future liability related to the abandonment and decommissioning. Any change in the estimate related to expenditures associated with abandonment and decommissioning liabilities are accounted for prospectively (remaining production) based on the unit of production method.

2.20 Revenue recognition

Sales revenue related to sale of oil is recognised when the ownership rights are transferred to the customer at the time of delivery based on contractual terms in the sales agreements, i.e. when deliveries are made at a sales transfer point. Royalty payments are excluded from total sales reported by the Group.

2.21 Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

2.22 Earnings per share

Basic earnings per share are calculated by dividing the net profit for the period attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

For the purpose of calculating diluted earnings per share, the net profit attributable to ordinary shareholders and the weighted average number of shares outstanding are adjusted for the effects of all dilutive potential ordinary shares from exercise of stock options. Stock options are deemed to have been converted into ordinary shares on the date when the options were granted. When net profit is negative, the dilutive instruments described above will have an anti dilutive effect when calculating dilutive earnings per share.

3. Financial risk management

The Group's activities are exposed to certain financial risks: market risk, credit risk, liquidity risk and interest risk. The Group's overall risk management plan focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. Risk management is carried out by the Chief Financial Officer.

(a) Market risk

Foreign exchange risk; The Group operates internationally and is, to some extent, exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the following currencies; USD, PEN and COP. All revenues are invoiced to the customers in USD, while operating expenses are mostly denominated in USD, NOK, PEN and COP. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and the investment of excess liquidity. Currently, the Company uses no derivative financial instruments to hedge the above mentioned risk exposures.

Price risk; The Group is exposed to changes in oil prices. Currently, the Company uses no derivate financial instruments to hedge the risk related to volatility in oil prices.

(b) Credit risk

Currently, the Group is selling all of its oil to the local state-owned oil companies. The credit risk for these customers is considered to be low.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash, and available for sale financial assets and develop operations according to budget. InterOil has in 2005 generated positive cash flows from operations. In 2005, the Group performed a share issuance with net proceeds of USD 43.6 million and should be able to raise additional funds if the liquidity status requires additional funding. Cash positions are monitored regularly to ensure that cash positions are kept at an acceptable level to ensure reasonable coverage for the Groups commitments and other planned investments.

(d) Cash flow and fair value interest rate risk

The Group has obtained financing with fixed interest rate which expose the Group to fair value changes. There are no other financing agreements and the Group has not entered into any interest rate swaps.

4. Critical accounting estimates and judgments

Estimates and judgements are continually evaluated, and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

(a) Income taxes
The Group is subject to income taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for income taxes.

Judgment is required in determining the Group's provision for deferred tax assets and liabilities. The Group recognises deferred tax assets if it is probable that sufficient taxable income will be available in the future against which the temporary differences and unused tax losses can be utilised. Management has considered future taxable income in assessing whether deferred income tax assets should be recognised. The carrying amount of deferred income tax assets and deferred income tax liabilities is USD 0.7 million and USD 21.0 million, respectively, at 31 December 2005. See note 11.

(b) Impairment of exploration and other oil related assets
The Group tests whether exploration assets and oil related assets has suffered any impairment, in accordance with the accounting policy stated in note 2.9 and 2.10. The recoverable amounts of cash generating units have been determined based on value-in-use calculations. These calculations require the use of estimates. Current oil price does not indicate impairment, and the Group has not recognised any impairment at 31 December 2005.

(c) Abandonment and decommissioning liabilities
The Groups future cost for environmental clean up depends on a number of uncertain factors, such as the extent and type of remediation required. Due to uncertainties inherent in the estimation process, it is possible that such estimates could be revised. The carrying amount of provisions for environmental issues at 31 December 2005 is USD 405 000. See note 22.

5. Related-party disclosure

The company's directors and management team are considered related parties.

Shareholders
Shares in InterOil Exploration and Production ASA directly and indirectly owned by related parties at 31 December 2005 (note 18):

Name	Shares in %	Position
Nils Trulsvik	3.8%	Chief Executive Officer
Gian Angelo Perrucci	5.1%	Member of the board
Mårten Rød	24.6%	Chairman of the board of directors

Gian Angelo Perrucci owns 2.9% directly and 2.2% indirectly through a 10% ownership in Caberian Investment Inc.

Amounts in USD 1 000 unless otherwise stated

Maxi Assets – Sales credit
The founders of InterOil, Gian Angelo Perrucci, Mårten Rød and Nils N. Trulsvik negotiated an exclusive agreement between the major shareholders of MIPI and a group of investors under the leadership of InterOil Ltd (BVI).

InterOil Exploration AS was formed in 2005 in order to acquire all the shares in the Peruvian and Colombian companies owned by Mercantile International Petroleum Inc (MIPI). The total cost price of the shares of MPOG, MCOG, RBSA, and Manitoba Services S.A was USD 78 million. Later the price was reduced to USD 77 million due to a USD 1 million dividend paid to MIPI before closing of the SPA.

InterOil Ltd (BVI) had negotiated the purchase of the shares in MIPI and later assigned this option to Maxi Assets Ltd in March 2005. Maxi Assets had formed a consortium and committed the required funding and guarantees to complete the acquisition. InterOil Exploration SA was established in May 2005 with the purpose to purchase the rights from Maxi Assets and finalise the agreement with MIPI.

At the closing in September, the USD 23 million was considered a sales credit, and on 31 December 2005, the outstanding part of the sales credit was USD 9 million. USD 3 million was repaid early January 2006, while the remaining USD 6 million, in accordance with an agreement established between the parties and TCW, is payable at the planned IPO. From 1 January 2006, the interest rate is Libor + 2 %.

Management contracts
InterOil has entered into management contracts with separate companies owned by the three main shareholders Nils Trulsvik, Gian Angelo Perrucci and Mårten Rød, who performs all their management services etc. through these companies.

Fees to Force Capital AS, owned by CEO Nils Trulsvik, have been charged as an expense with USD 75, for the period after the acquisition of InterOil, from which he took on the responsibility as CEO. His advisory services prior to acquisition, involving valuations, due diligence, negotiations etc, has been capitalized with USD 125.

Fees to Caberian Investment, owned 10% by Gian Angelo Perrucci, have been charged as an expense with USD 30.

Chief Financial Officer ("CFO")
The CFO Jon Wiggen is a partner in the audit firm Kjelstrup & Wiggen AS. In 2005 Kjelstrup & Wiggen AS has been paid USD 123 for CFO and controlling services.

Remuneration to the Board of Directors
The Board of Directors has not been compensated in 2005.

Eksportconsult AS – various
Fees to Eksportconsult, owned by the Chaiman of the Board, Mårten Rød, have been charged as an expense with USD 60.

Furthermore Eksportconsult was involved in negotiating an exclusive agreement between the major shareholders of MIPI and a group of investors under the leadership of Maxi Assets Ltd from which Eksportconsult was entitled to 17% of the defined upside.

Furniture and fixture for fully equipped office premises, formerly rented out to external tenants, have been billed from Eksportconsult to InterOil at estimated market value of USD 37.

The lease agreement of the premises at the Headquarters of InterOil ASA has been transported to InterOil from Eksportconsult with effect from 1 October 2005, without compensation. The lease period expired at the end of 2005, and has been prolonged with the owner Vital for 5 years at an annual lease amounting to USD 85 inclusive of parking space etc. This represents a cost pr sq meter office premises of USD 251 (not in thousands). As of 1 February 2006 InterOil leased additional premises for a five years period at an annual lease of USD 48, representing USD 285 per sq. meter (not in thousands): This cost covers some investments in the locations according to InterOils specifications, paid by the owner.

30 % of the salary to a part time secretary has been charged to Eksportconsult, based on estimated time worked for Eksportconsult.

Net receivable from Eksportconsult at 31 December 2005 is USD 105, which has been repaid in the beginning of 2006.

6. Segment information

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within particular economic environments that are subject to risks and returns that are different from those of segments operating in other economic environments.

Primary reporting format - business segments:
According to the Group's internal financial reporting systems, business segments are the primary basis for segmentation. Based on IAS 14, the Company considers that the entire Group's operations constitute a single business segment which is oil exploration and oil production activities.

Secondary reporting format - geographical segments:
Secondary segments consist of geographic markets. The risk and returns of the Group are influenced both by the geographical location of its operations and also by the location of its markets. InterOil's definition of geographical segments is based on the location of its markets and customers. Transactions within the different segments are eliminated. The parent company is located in Norway, while the Groups oil activities is currently based in Colombia and Peru.

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	Colombia	Peru	Total report. segm.	Unalloc./ elimin.	Group
Sales	3 346	4 645	7 991	-	7 991
Cost of goods sold	-1 505	-1 731	-3 286	-	-3 286
Gross profit	**1 841**	**2 914**	**4 705**	**-**	**4 751**
Tariffs and transportation	-204	-	-204	-	-204
Exploration cost expensed	-783	-	-783	-	-783
Administrative expense	-155	-469	-625	-876	-1 501
Other income	-	-	-	181	181
Other operating expenses	-15	-28	-43	- 100	-143
Profit from operating activities	**684**	**2 412**	**3 096**	**- 795**	**2 301**
Finance costs – net	-55	18	-37	-1 485	-1 522
Profit before income tax	**629**	**2 431**	**3 060**	**-2 280**	**780**
Income tax expense	-262	-817	-1 079	575	-503
Net profit	**367**	**1 614**	**1 981**	**-1 705**	**276**
Balance sheet information					
Property, plant and equipment	34 779	63 072	97 851	60	97 911
Other assets	3 923	9 214	13 137	13 811	26 948
Total segment assets	**38 702**	**72 285**	**110 988**	**13 871**	**124 859**
Total segment liabilities	**11 517**	**19 989**	**31 506**	**46 407**	**77 913**
Capital expenditures, during the year	**2 001**	**1 541**	**3 542**	**62**	**3 604**
Other segment information					
Lifting cost	704	579	1 283	-	1 283
Amortisation and depreciation – cost of goods sold	713	1 060	1 773	-	1 773

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

7. Sales and royalty agreements

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Sale of oil	
Sale of oil – before royalty	12 576
Royalty	-4 588
Sale of oil – net, barrels	7 988
Sale of services	3
Total sales	**7 991**

Sale in barrels – see note 30

Royalty:
The royalty payments are excluded from total sales reported by the Group.

Royalty agreements in Peru:
The royalty payment in percentage of gross oil price in accordance with royalty agreement with Perupetro in Peru is dependent on oil price according to a sliding scale below:

Royalty for Total Production, Value of Crude Basket
Oil

Price	<=$27.0	$30.0	$35.0	$45.0	$55.0	$65.0	$75.0	$85.0
Royalty	13.0%	20.2%	31.1%	38.0%	42.5%	45.5%	47.8%	49.5%

Royalty agreements in Colombia:
The royalty payment in percentage of gross oil price in accordance with royalty agreement with Ecopetrol in Colombia varies between 8 – 20%, depending on contract.

8. Cost of goods sold

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Cost of goods sold	
Lifting costs	1 237
Depreciation and amortisation	1 773
Changes in inventory	230
Total cost of goods sold	**3 240**
Lifting costs, specifications:	
Field production costs	401
Insurance	47
Production costs external consultants	91
Well services and workovers	325
Repairs and maintenance of installations/equipment	358
Other production costs	15
Total lifting costs	1 237

9. Administrative expenses

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Administrative expenses	
Employee benefit expense	226
Depreciation	25
General and administration expenses	1 250
Total administrative expenses	**1 501**

Employee benefit expense directly attributable to production and exploration are reclassified to lifting cost and capital expenditure in the income statement.

Employee benefit expense, specifications:	
Salaries and wages employees	375
Social expenses	52
Other payroll related expenses	30
Pensions	37
Total employee benefit expense	495
Reclassified to lifting cost	-248
Reclassified to capital expenditure	-21
Employee benefit expense – Administrative expenses	**226**

10. Other operating Expenses

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Other operating expenses	
Abandonment provisions, impairments	15
Provisions legal claim (note 18)	100
Other operating expenses	28
Total other operating expenses	**143**

11. Finance costs – net

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Financial income	
Interest income	93
Financial income	**93**
Financial expenses	
Interest expenses	1 206
Amortisaton of debt issue cost and equity component of issued interest-bearing loan	260
Other financial expenses	149
Financial expenses	**1 615**
Finance costs – net	**-1 522**

12. Taxes

For the period from 2 May 2005 (inception) to 31 December 2005
Amounts in USD 1 000

Income tax expense	
Current tax	605
Deferred tax	-102
Income tax expense	**503**

Income taxes

Profit before income tax	**780**
Expected income tax according to nominal tax rate (28%/30%/38.5%)	330
Adjustment of deferred tax assets not recorded	33
Expenses not deductible for tax purposes	163
Other items	-22
Total income taxes	**503**
Effective income tax rate	65%

Nominal tax rate in Norway, Peru and Colombia is respectively 28%, 30% and 38.5%.

Deferred income tax
Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

As at 31 December	**2005**
Deferred tax assets:	
– Deferred tax asset to be recovered after more than 12 months	1 403
– Deferred tax asset to be recovered within 12 months	684
	2 087
Deferred tax liabilities:	
– Deferred tax liability to be recovered after more than 12 months	-21 784
– Deferred tax liability to be recovered within 12 months	-656
	-22 440
	-20 353

The gross movement on the deferred income tax account for the period from 2 May 2005 (inception) to 31 December 2005 is as follows:

At inception	–
Acquisition of subsidiaries	19 828
Income statement charge	102
Tax charged to equity	-627
At 31 December 2005	**-20 353**

The movement in deferred tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred tax liabilities:	Accelerated tax depreciation	Borrowings	Other	Total
At inception	**–**	**–**	**–**	**–**
Acquisition of subsidiaries	-20 866	–	–	-20 866
Charged/(Credited) to the income statement	-412	42	–	-370
Charged to equity	–	-1 204	–	-1 204
At 31 December 2005	**-21 278**	**-1 162**	**–**	**-22 440**

Deferred tax assets:	Provisions of assets	Tax losses	Other	Total
At inception	**–**	**–**	**–**	**–**
Acquisition of subsidiaries	450	267	321	1 038
(Credited)/charged to the income statement	-245	276	441	472
Charged to equity	–	577	–	577
At 31 December 2005	**205**	**1 120**	**762**	**2 087**
Net deferred income tax liability at 31 December 2005				**-20 353**

Deferred tax asset of USD 19 related to tax loss carried forward has not been recognized as the recognition criteria in IAS 12 have not been met. InterOil Exploration and Production Africa AS has a history of recent losses. As of 31 December 2005 there is not convincing evidence that sufficient taxable profit will be available against which the unused tax losses could be utilized.

13. Property, plant and equipment

	Production rights assets	Exploration assets	Develop. Assets	Oil production assets	Other	Total
Period ended 31 December 2005						
At inception	**–**	**–**	**–**	**–**	**–**	**–**
Acquisitions of subsidiaries	2 607	–	–	91 917	1 582	96 107
Additions	–	2 770	1 541	–	76	4 311
Transfers	–	-1 987	–	1 987	–	0
Exploration cost expensed	–	-783	–	–	–	-783
Depreciation charge	–	–	–	-1 773	-27	-1 800
Closing net book amount	**2 607**	**0**	**1 541**	**92 131**	**1 631**	**97 911**
At 31 December 2005						
Cost or valuation	2 607	0	1 541	93 904	1 658	99 711
Accumulated depreciation	–	–	–	-1 773	-27	-1 800
Net book amount	**2 607**	**0**	**1 541**	**92 131**	**1 631**	**97 911**

The following assets have been pledged as security for the interest-bearing loan (see Note 20)

Assets owned by InterOil Exploration and Production AS:
Shares in InterOil Exploration and Production Latin America AS and bank accounts and money market fund in Deutsche Bank amouting to USD 16.2 million.

Assets owned by InterOil Exploration and Production Latin America AS
Shares in the operating companies in Colombia and Peru.

Assets owned by MCOG SA, MPOG SA and RBSA:
All assets including financial assets at fair value through profit or loss (money market fund) amounting to USD 10.9 million.

14. Trade and other receivables

Period ended 31 December Amounts in USD 1 000	2005
Trade receivables	3 096
Less: provision for impairment of receivables	-59
Trade receivables – net	3 037
Joint operations accounts	252
Prepayments	23
VAT receivable	152
Mercantile International Petroleum Inc.	2 000
Other short-term receivables	965
Total trade and other receivables	**6 428**

The carrying amount of trade and other receivables approximate their fair value.

15. Inventories

Period ended 31 December Amounts in USD 1 000	2005
Crude oil	493
Total inventories	**493**

16. Financial assets at fair value through profit or loss / Other Income

Period ended 31 December Amounts in USD 1 000	2005
Money Market Fund:	
Opening balance	-
Addition, JPM USD Liquidity Premier	10 720
Interest	181
Total financial assets at fair value through profit or loss	**10 901**
Interest income – recognised in the income statement as other income	**181**

According to the loan agreement with TCW money market fund of USD 10 901 is restricted for payment of interest, instalment to TCW, repayment of USD 3 000 in selling credit, working capital and capital expenditure in Peru and Colombia.

17. Cash and cash equivalents

Period ended 31 December	
Amounts in USD 1 000	**2005**
Bank deposits denominated in USD	6 433
Bank deposits denominated in NOK	394
Bank deposits denominated in Colombian Pesos	1 417
Bank deposits denominated in Peruvian Soles	45
Cash and cash equivalents, restricted	158
Total cash and cash equivalents	**8 437**

According to the loan agreement with TCW bank deposits of USD 1 072 is restricted for payment of interest, instalment to TCW, working capital and capital expenditure in Peru and Colombia.

The effective interest rates at the balance sheet date were as follows:

	2005			
	US$	**NOK**	**Colombian Pesos**	**Peruvian Soles**
Bank deposits	1.8%	2.0%	0.0%	2.7%

18. Paid in Capital

Amounts in USD 1 000	**Number of Shares (1 000)**	**Ordinary shares**	**Share premium**	**Total**
Inception on 2 May 2005	2 000	16	–	16
Issue of share capital, net of share issuance cost 15 September 2005, net of tax	8 000	63	–	63
Issue of share capital, net of share issuance cost 30 September 2005, net of tax	11 245	88	43 407	43 495
Currency translation differences	–	-10	10	–
At 31 December 2005	**21 245**	**157**	**43 417**	**43 574**

The total number of issued shares is 21 245 thousands shares with a par value of NOK 0.05 per share. All issued shares are fully paid. The total number of authorised shares consists of the following; 1) the 21 245 thousands issued shares mentioned above; 2) the number of shares that will be issued because of the subscription rights included in the TCW loan agreement (note 21) and as explained below;

The company has issued 10 000 subscription rights to TCW. In total, the subscription rights gives TCW the right to subscribe for the number of ordinary shares that can be purchased for USD 5 040 divided on the price per share set in the Initial Public Offering (IPO). The subscription price for new shares is the highest of the price in NOK equivalent to USD 0.01 and the par value of the shares.

Top 20 shareholders & consolidated nominee accounts
AS of 31 December 2005

Company	**Shares held**	**% of total shares**
Eksportconsult AS [1]	5 225 000	24.6%
Caberian Investment Inc. [2]	4 600 000	21.7%
Credit Suisse Securities	1 875 000	8.8%
Pareto Securities AS (market making)	1 000 000	4.7%
Goldman Sachs	1 000 000	4.7%
Bear Sterans Securies Corp.	820 000	3.9%
Force Capital Partners AS [3]	800 000	3.8%
UBS AG, London Branch client account	685 000	3.2%
Gian Angelo Perrucci (registered on Caberian Investment Inc. in VPS)	625 000	2.9%
UBS AG, London Branc Equities	565 000	2.7%
Norinvest Ltd.	500 000	2.4%
KLP Forsikring	400 000	1.9%
Storebrand Livforsikring	392 420	1.8%
Morgan Stanley and Co. Intl. Limited	380 000	1.8%
Consafe Invest AB	375 000	1.8%
Pactum AS	375 000	1.8%
Pecunia Forvaltning	220 000	1.0%
Banque Invik SA Luxembourg	200 000	0.9%
Bank of New York	180 000	0.8%
Muslik AS	144 000	0.7%
Total 20 largest shareholders	20 361 420	95.8%
Other	883 580	4.2%
Total	**21 245 000**	**100.0%**

1) Owned by Mårten Rød
2) Owned by Gian Angelo Perrucci (10%)
3) Owned by Nils Trulsvik

19. Other reserves

Period ended 31 December		
Amounts in USD 1 000	**Subscription rights**	**Total**
At inception date	–	-
Equity component interest-bearing loan (note 20, 21)	4 300	4 300
Tax on equity component	-1 204	-1 204
At 31 December 2005	**3 096**	**3 096**

20. Interest-bearing liabilities/subordinated loan

Period ended 31 December Amounts in USD 1 000	**2005**
Non-current	
Loan, The American Investment Bank, Trust Company of the West ("TCW")	35 135
Total non-current interest-bearing liabilities	**35 135**
Current	
Subordinated loan to Maxi Assets (note 5 related party)	6 000
Liabilities to financial institutions	639
Total current interest-bearing liabilities/subordinated loans	**6 639**
Total interest-bearing liabilities/subordinated loans	**41 774**

Terms of the non-current interest-bearing liabilities:

	Currency	Amount	Effective interest rate	Maturity
Loans from the American Investment Bank, TCW	USD	35 135	14.4%	2012
Total non-current interest-bearing liabilities		**35 135**		

The effective interest rate at the balance sheet date for subordinated loan was 6.5%.

Fair value of the liabilities cannot be measured reliably, since the loan is not quoted in a market. Further information about the loan from TCW is set out in note 21.

The maturity of interest-bearing liabilities is as follows:

Amounts in USD 1 000	**2005**
0-12 months	6 639
Between 1 and 2 years	–
Between 2 and 5 years	17 545
Over 5 years	17 590
Total interest-bearing liabilities	**41 774**

The Group's interest-bearing liabilities are denominated in the following currencies:

Period ended 31 December Amounts in USD 1 000	**2005**
USD	41 135
Colombian Pesos	639
Total interest-bearing liabilities	**41 774**

21. Loan with subscription rights

Period ended 31 December Amounts in USD 1 000	**2005**
Face value of loan from TCW	42 000
Borrowing cost	-2 825
Equity component	-4 300
Liability component on initial recognition at 27 September 2005	34 875
Amortisation of debt issue cost and liability component of issued interest bearing loan	260
Liability component at 31 December 2005 (note 20)	**35 135**

The Company has an interest-bearing loan amounting to USD 42 million to TCW. The nominal interest rate is 9% per year, quarterly payment, and 3 years grace on repayment of the principal. The down payment of the principal is on quarterly basis, starting October 2008, with final repayment October 2012.

The facility has a covenant structure with focus on the measurement of specific key figures, such as collateral coverage ratio and current ratio. In additions limitations are set for addional borrowings, sale and purchase of companies/assets, issuance of share capital and other negative covenants. The Company is not in breach with the covenants of the loan agreement and expects future compliance with these.

The company has issued 10 000 subscription rights to TCW. In total, the subscription rights gives TCW the right to subscribe for the number of ordinary shares that can be purchased for USD 5 040 divided on the price per share set in the Initial Public Offering (IPO). The subscription price for new shares is the highest of the price in NOK equivalent to USD 0.01 and the par value of the shares. The subscription rights may be exercised at the last day of the initial public offering prior to the listing on Oslo Stock Exchange only. Shares subscribed for in accordance with the subscription rights may not in any way be disposed of before six months after closing of the initial public offering. The residual value of the subscription rights were USD 4 300 on initial recognition at 27 September 2005. It is assumed that the subscription rights will be exercised in September 2007.

Except for the subscription rights described above, the Company has no outstanding convertible bonds, options or other rights to subscribe for shares in the Company.
In the event that there has not been an initial public offering within 21 September 2007, TCW shall have a springing royalty of 1.5% on all of the Groups petroleum production which springing royalty shall be retroactive for the two year period from 21 September 2005 to 21 September 2007.

22. Provisions for other liabilities and charges

Period ended 31 December Amounts in USD 1 000	**2005**
Non-current	
Asset retirement obligations	405
Other long term obligations	524
Total non-current provisions for other liabilities and charges	**929**
Current	
Legal claims (note 23)	100
Total current provisions for other liabilities and charges	**100**
Total provisions for other liabilities and charges	**1 029**

Amounts in USD 1 000	Asset retirem. oblig.	Other long term oblig.	Legal claims	Total
Inception on 2 May 2005	–	–	–	–
Acquisition of subsidiaries	390	523	–	913
Charged to consolidated income statement:				
- Additional provisions	15	–	100	115
Used during the period	–	–	–	–
Balance at 31 December 2005	**405**	**523**	**100**	**1 029**

Other long term obligation is provision in connection with employees in Colombia based on local statutory requirements.

23. Commitments and contingencies

Drilling commitment
The Group is obliged, through its licence contracts in Peru and Colombia, to carry through the following drilling program for the period subsequent to 31 December 2005

As of 31 December 2005:

Amounts in USD 1 000	2006	After	Total
Colombia			
- Seismic	303	1 300	1 603
- Well drilling	750	1 650	2 400
- Other	103	195	298
Total Colombia	**1 156**	**3 0458**	**4 201**
Peru			
- Seismic	0	0	0
- Well drilling	4 765	5 849	10 614
- Other	0	0	0
Total Peru	**4 765**	**5 849**	**10 614**
Total	**5 921**	**8 894**	**14 815**

The group leases offices and machinery under non-cancellable operating lease agreements. The future aggregate minimum lease payments under non-cancellable operating leases are USD 240.

Lawsuits
InterOil has been informed that the former CEO Rudolph Berends is in the process of filing a lawsuit for wrongful dismissal. InterOil will claim that no contract was ever consummated. These matters are always complex and hence a provision to cover a final settlement amounting to USD 100 has been set aside.

There is also a lawsuit filed by Mr. Enrique Davila de Heredia, former General Manager against the Colombia Branch office for USD 130. This labour claim was originated by the Branch's decision to terminate Mr. Davila de Heredia's contract in August 2002.

The Branch's legal advisors and management consider that the Court will issue a verdict favourable for the Branch, and therefore no provision has been recorded for such purposes.

No additional significant litigation was reported by the Branch's legal advisors.

24. Trade and other payables

Period ended 31 December

Amounts in USD 1 000	2005
Trade creditors	3 705
Public duties payable	715
Debt to employees and shareholders	195
Other accrued expenses	4 788
Maxi Assets – selling credit (note 5 – related party)	3 000
Mercantile International Petroleum Inc. – selling credit	500
Total trade and other payables	**12 902**

The carrying amount of trade and other payable is considered to approximate their fair value.

25. Earnings per share

Basic
Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year.

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	
Profit attributable to equity holders of the Company	276
Weighted average number of ordinary shares in issue (thousands)	6 467
Basic earnings per share (USD per share)	**0.04**

Diluted
Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The subscription rights is assumed to have been converted into ordinary shares (see note 21)

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	
Profit attributable to equity holders of the Company	276
Weighted average number of ordinary shares in issue (thousands)	6 467
Adjustment for subscription rights – shares to fair value of USD 5 040	310
Weighted average number of ordinary shares for diluted earnings per share (thousands)	6 777
Diluted earnings per share (USD per share)	**0.04**

26. List of consolidated subsidiaries

InterOil Exploration and Production ASA has 100% (direct and indirect) shareholding and voting rights in the following subsidiaries:

Company	Registered business address	Direct and indirect shareholding and voting rights
InterOil Exploration SA	Switzerland	100%
InterOil Exploration and Production Latin America AS	Norway	100%
InterOil Exploration and Production Africa AS	Norway	100%
InterOil Exploration and Production Colombia AS	Norway	100%
Mercantile Peru Oil and Gas S.A (MPOG)	Peru	100%
Compania Petrolera Rio Bravo S.A (RBSA)	Peru	100%
Manitoba Services S.A	Peru	100%
Mercantile Colombia Oil and Gas B.V.I (MCOG)	Colombia	100%

27. Subsequent events

Blocks in Angola

As of 28 April 2006, InterOil was offered participation in two offshore blocks in Angola.

Block 5 – 40 % participation
Block 6 – 20 % participation

Block 5 - Block 5 implies a signature bonus on InterOil's 40 % share amounting to USD 10.5 million. Social projects participation amount to approximately USD 2 million. Acquiring seismic and drilling 2 exploration wells amount to approximately USD 25 million.

Block 6 implies a signature bonus on InterOil's 20 % share amounting to USD 12.5 million. Social projects participation amount to approximately USD 3.25 million. Acquiring seismic and drilling 2 exploration wells amount to approximately USD 14 million.

Total investment in phase one inclusive of 3D seismic and two exploration wells are expected to amount to USD 81 million (inclusive of signature bonus) over a 4 year period

28. External audit remuneration

PricewaterhouseCoopers ("PwC") is the Group's principal auditor. The following table shows total audit and non-audit fees.

Amounts in USD 1 000

2005	Audit fee	Assurance services	Tax Services	Other non-audit services	Total
PwC Norway	15	-	-	-	15
PwC Abroad	33	-	-	30	63
Total PwC	**48**	**-**	**-**	**30**	**78**

29. Business combinations

Amounts in USD 1 000

On 27 September 2005, the Group acquired 100% of the shares capital of Mercantile Peru Oil and Gas S.A, Compania Petrolera Rio Bravo S.A, Manitoba Services and Mercantile Colombia Oil and Gas B.V.I., all oil companies operating in Latin America. The consideration for all outstanding shares, including direct acquisition costs, amounted to USD 77 490.

The acquired businesses contributed revenues of USD 7 991 and net profit of USD 1 981 to the group for the period ended 31 December 2005.

If the acquisition had occurred on 1 January 2005, Group revenue would have been USD 29 262, and net income would have been USD 3 215. These amounts have been calculated using the Group's accounting policies and by adjusting the results of the acquired business to reflect the additional depreciation and amortisation that would have been charged assuming the fair value adjustment to property, plant and equipment had applied on 1 January 2005, together with the consequential tax effects. In addition, these amounts have been calculated by adjusting the financial expense that would have been charged assuming that the TCW loan and the Maxi Asset loan had been issued on 1 January 2005. Assets acquired and liabilities assumed have been recognized at estimated fair value.

Purchase considerations

Amounts in USD 1 000	2005
Cash paid	77 000
Direct cost relating to acquisition	490
Total purchase consideration	**77 490**
Fair value of net assets acquired	77 490
Goodwill	**0**

The assets and liabilities arising from the acquisition are as follows:

Amounts in USD 1 000	Fair value	Acquiree's carrying amount
Deferred income tax assets	560	560
Property, plant and equipment	96 107	43 447
Inventories	556	556
Trade and other receivables	7 041	7 041
Cash and cash equivalents	2 411	2 411
Deferred income tax liabilities	-20 387	-3 519
Provisions for other liabilities and charges	-883	-883
Trade and other payables	-5 726	-5 726
Income taxes payable	-1 359	-1 359
Current interest-bearing liabilities	-829	-829
Net assets	**77 490**	**41 699**

Purchase consideration settled in cash	77 490
Cash in subsidiary acquired	-2 410
Selling credit as of 31 December 2005 (note 20 og 24)	-9 500
Cash outflow on acquisition	**65 580**

30. Oil and gas reserves (unaudited)

InterOil reserve classification uses the SPE/WPC definitions estimating Proven and Probable reserves. The reserves have been audited by an independent third party, Gaffney, Cline and Associates. The reserves have, for the sake of clarity, been reported before and after royalty. Royalty in Peru is dependent on oil price so hence the net of royalty number is only correct at date of report (31 December 2005).

Continuity of Proved Reserves by Segment – Working interest

Crude oil and gas equivalents (boe)	Colombia	Peru	Total
Proved reserves at 30 September 2005	3 613	8 503	12 116
4 th quarter 2005 production	-72	-149	-221
Proved reserves at 31 December 2005	**3 541**	**8 354**	**11 895**

Continuity of Proved and Probable Reserves by Segment – Working interest

Crude oil and gas equivalents (boe)	Colombia	Peru	Total
Proved and probable reserves at 30 September 2005	5 671	10 583	16 254
4 th quarter 2005 production	-72	-149	-221
Proved and probable reserves at 31 December 2005	**5 599**	**10 434**	**16 033**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

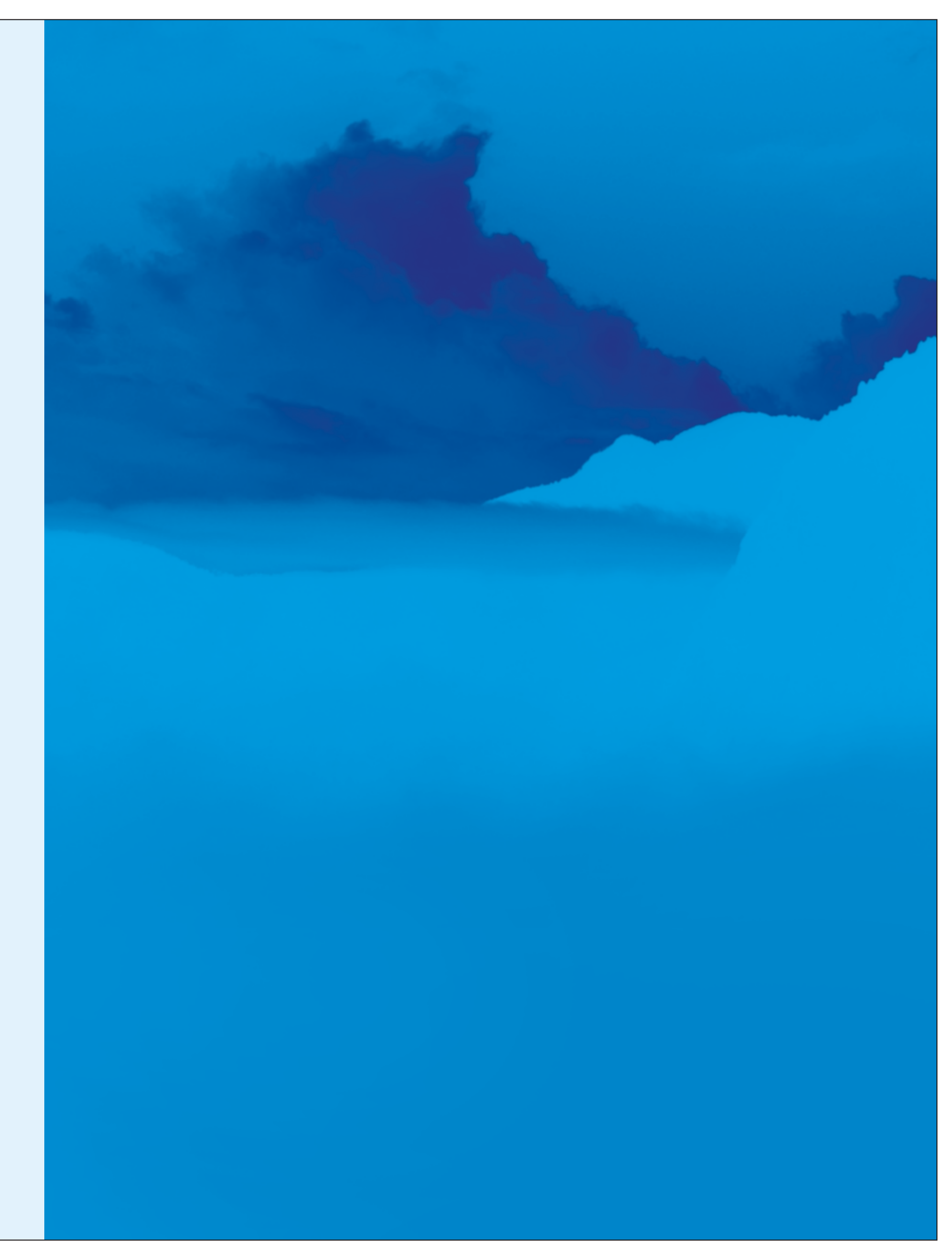
Continuity of Proved Reserves by Segment – Net interest after Royalty

Crude oil and gas equivalents (boe)	Colombia	Peru	Total
Proved reserves at 30 September 2005	2 992	4 875	7 867
4 th quarter 2005 production	-59	-85	-144
Proved reserves at 31 December 2005	**2 933**	**4 790**	**7 723**

Continuity of Proved and Probable Reserves by Segment – Net interest after Royalty

Crude oil and gas equivalents (boe)	Colombia	Peru	Total
Proved and probable reserves at 30 September 2005	4 740	6 064	10 804
4 th quarter 2005 production	-59	-85	-144
Proved and probable reserves at 31 December 2005	**4 681**	**5 979**	**10 660**

Production and sales for the period from 1 October 2005 to 31 December 2005	Colombia	Peru	Total
Sale in barrels – net			
Sale of oil, barrels	69 000	85 684	154 684
Total sale in barrels – net	**69 000**	**85 684**	**154 684**
Production in barrels – net			
Working interest, barrels	71 955	149 412	221 367
Royalty	13 390	63 728	77 118
Total production in barrels – net of royalty	**58 565**	**85 684**	**144 249**



INTEROIL EXPLORATION AND PRODUCTION ASA
FINANCIAL STATEMENTS

31 DECEMBER 2005

INCOME STATEMENT

Amounts in USD 1 000

For the period from 2 May 2005 (inception) to 31 December 2005	Note	2005
Administrative expense	2	-787
Other operating expenses	15	-100
Other income		181
Profit/(loss) from operating activities		**-706**
Finance costs – net	3	-1 484
Loss before income tax		**-2 190**
Income tax	4	613
Net loss		**-1 578**

BALANCE SHEET

Amounts in USD 1 000

As of 31 December	Note	2005
ASSETS		
Non-current assets		
Property, plant and equipment	5	60
Investments in subsidiaries	14	77 130
Intercompany receivables		644
Total non-current assets		**77 834**
Current assets		
Trade and other receivables	6	358
Financial assets at fair value through profit or loss	7	10 901
Cash and cash equivalents	8	2 387
Total current assets		**13 646**
TOTAL ASSETS		**91 480**
EQUITY		
Share capital and share premium	9	43 574
Other reserves	10	3 096
Accumulated deficit		-1 578
Total equity		**45 092**
LIABILITIES		
Non-current liabilities		
Interest-bearing loan	11, 12	35 135
Deferred income tax liabilities	4	14
Total non-current liabilities		**35 149**

As of 31 December	Note	2005
Current liabilities		
Trade and other payables	13	5 012
Intercompany payables		128
Subordinated loan, related parties	11	6 000
Provisions for other liabilities and charges	15	100
Total current liabilities		**11 240**
Total liabilities		**46 247**
TOTAL EQUITY AND LIABILITIES		**91 480**

London, 15 May 2006
The Board of InterOil Exploration & Production ASA

Mårten Rød
Chairman of Board

Gian Angelo Perruci
Member of the Board

Blair Thomas
Member of the Board

Nils Trulsvik
Chief Executive Officer

STATEMENT OF CHANGES IN EQUITY

Amounts in USD 1 000

For the period from 2 May 2005 (inception) to 31 December 2005	Note	Share capital and share premium	Other reserves	Accumulated deficit	Total equity
Inception on 2 May 2005	9	16	–	–	16
Issue of share capital, net of share issuance cost 15 September 2005	9	63	–	–	63
Issue of share capital, net of share issu-ance cost 30 September 2005, net of tax tax effect	9	43 495	–	–	43 495
Equity component interest bearing debt, net of tax	10	–	3 096	–	3 096
Net loss for the period		–	–	- 1 578	- 1 578
Balance at 31 December 2005		**43 574**	**3 096**	**- 1 578**	**45 092**

CASH FLOW STATEMENT

Amounts in USD 1 000

For the period from 2 May 2005 (inception) to 31 December 2005	Note	2005
Cash generated from operations		
Net loss for the period		**- 1 578**
Income tax	4	-613
Depreciation and amortization	5	2
Interest received from financial assets at fair value through profit or loss	7	-181
Amortization of debt issuance cost and equity component	12	260
Interest expense	3	1 161
Changes in assets & liabilities		
Trade and other receivables		-358
Trade and other payables		535
Other provision for other liabilities		100
Interest paid		-185
Net cash generated from operating activities		**-857**
Cash flows from investing activities		
Acquisition of subsidiaries, net of selling credit		-67 631
Purchases of property, plant and equipment (PPE)	5	-62
Other financial assets at fair value through profit or loss	7	-10 720
Net cash used in investing activities		**-78 412**
Cash flows from financing activities		
Proceeds from issuance of ordinary shares (excluded tax effect)	9	42 996
Proceeds from issuance of interest-bearing loan inclusive equity component	12	39 175
Repayments of inter-company borrowings		-516
Net cash used in financing activities		**81 655**
Net increase in cash and cash equivalents		2 387
Cash and cash equivalents at beginning of the period		0
Cash and cash equivalents at end of the year	**8**	**2 387**

NOTES TO INTEROIL EXPLORATION AND PRODUCTION ASA FINANCIAL STATEMENTS

1. Summary of significant accounting policies

When preparing the financial statements for InterOil Exploration and Production ASA, the company has taken advantage of the opportunity to apply a simplified version of IFRS as specified by the EU and adopted in the Norwegian Accounting Act. This means that the IFRS valuation rules are observed, while keeping to the Norwegian Accounting Act and Norwegian generally accepted accounting principles for presentation of the notes. The company's accounting policies are specified in note 2 (Consolidated financial statements). These financial statements is presented in USD, which is the company's functional currency, and rounded up to thousands (1 000).

Shares in subsidiaries are recorded in accordance with the cost method in the parent company accounts. The investments are reviewed for impairment annually or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

2. Administrative expenses

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	2005
Salaries and social expenses *	7
Depreciation	2
Professional fees	528
General administration expenses	250
Total administrative expense	**787**
Salaries and social expenses, specification:	
Salaries and wages employees	6
Social expenses	1
Salaries and social expenses	**7**

The average number of employees during the period is 1.
The fees to the auditor PricewaterhouseCoopers AS for audit service is USD 15 for the parent company.
Remuneration to CEO and Board of Directors, see note 5 (consolidated financial statements).

3. Finance costs – net

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	2005
Financial income	
Interest income	57
Exchange rate gain	7
Interest income, inter-company loan	1 203
Financial income	**1 267**
Financial expenses	
Interest expenses	1 161
Amortisation of debt issue cost and equity component of issued interest bearing loan	260
Other intercompany financial cost	1 203
Other financial expenses	128
Financial expenses	**2 752**
Finance costs – net	**-1 484**

4. Taxes

For the period from 2 May 2005 (inception) to 31 December 2005

Amounts in USD 1 000	2005
Income tax	
Taxes payable	-
Deferred tax	613
Income tax	**613**
Income taxes	
Loss before income tax	-2 190
Expected income tax according to nominal tax rate (28%)	-613
Expenses not deductible for tax purposes	1
Total income taxes	**-612**
Effective income tax rate	**28%**

Period ended 31 December
Deferred income tax

Deferred tax assets:	
– Deferred tax asset to be recovered after more than 12 months	1 120
– Deferred tax asset to be recovered within 12 months	28
	1 148
Deferred tax liabilities:	
– Deferred tax liability to be recovered after more than 12 months	-997
– Deferred tax liability to be recovered within 12 months	-165
	-1 162
Net deferred tax liabilities	**- 14**

The gross movement on the deferred income tax account is as follows:	**2005**
At inception	–
Income statement charge	613
Tax charged to equity – Equity component TCW loan	-1 204
Tax charged to equity – Tax on share issue cost	577
At 31 December 2005	**- 14**

Deferred tax liabilities:	**Accelerated Tax depreciation**	**Borrowings**	**Other**	**Total**
At inception		–	–	–
Charged/(Credited) to the income statement		42	–	42
Charged to equity		-1 204	–	-1 204
At 31 December 2005		**-1 162**	**-**	**-1 162**

Deferred tax assets:

	Claims	**Tax losses**	**Other**	**Total**
At inception	–	–	–	–
Charged/(credited) to the income statement	28	543	–	571
Charged to equity		577		577
At 31 December 2005	**28**	**1 120**	**-**	**1 148**
Net deferred income tax liabilities at 31 December 2005	**-**	**-**	**-**	**-14**

5. Property, plant and equipment

Period ended 31 December 2005

Amounts in USD 1 000	Office machines and furniture	Total
Opening net book amount	-	-
Additions	62	62
Depreciation charge	-2	-2
Closing net book amount	**60**	**60**
At 31 December 2005		
Cost	62	62
Accumulated depreciation	-2	-2
Net book amount	**60**	**60**

6. Trade and other receivables

Period ended 31 December

Amounts in USD 1 000	2005
VAT receivable	152
Other short-term receivables	206
Total trade and other receivables	**358**

The carrying amount of trade and other receivables approximate their fair value.

7. Financial assets at fair value through profit or loss / Other Income

Period ended 31 December

Amounts in USD 1 000	2005
Money Market Fund:	
Opening balance	-
Addition, JPM USD Liquidity Premier	10 720
Interest	181
Total financial assets at fair value through profit or loss	**10 901**
Interest income – recognised in the income statement as other income	181

8. Cash and cash equivalents

Period ended 31 December

Amounts in USD 1 000	2005
Bank deposits denominated in USD	1 989
Bank deposits denominated in NOK	394
Cash and cash equivalents, restricted	2
Total cash and cash equivalents	**2 387**

The effective interest rates at the balance sheet date were as follows:

	2005	
	US$	**NOK**
Bank deposits	1.8%	2.0%

9. Paid in Capital

Amounts in USD 1 000	Number of Shares (1 000)	Ordinary shares	Share premium	Total
Inception on 2 May 2005	2 000	16	–	16
Issue of share capital, net of share issuance cost 15 September 2005, net of tax	8 000	63	–	63
Issue of share capital, net of share issuance cost 30 September 2005, net of tax	11 245	88	43 407	43 495
Currency translation differences	–	-10	10	–
At 31 December 2005	**21 245**	**157**	**43 417**	**43 574**

The total number of issued shares is 21 245 thousands shares with a par value of NOK 0.05 per share. All issued shares are fully paid. The total number of authorised shares consists of the following; 1) the 21 245 thousands issued shares mentioned above; 2) the number of shares that will be issued because of the subscription rights included in the TCW loan agreement (note 21) and as explained below;

The company has issued 10 000 subscription rights to TCW. In total, the subscription rights gives TCW the right to subscribe for the number of ordinary shares that can be purchased for USD 5 040 divided on the price per share set in the Initial Public Offering (IPO). The subscription price for new shares is the highest of the price in NOK equivalent to USD 0.01 and the par value of the shares.

Shareholders as of 31 December 2005 – see Group note 18.

10. Other reserves

Period ended 31 December Amounts in USD 1 000	Subscription rights	Total
At inception date	–	–
Equity component interest-bearing loan (note 11, 12)	4 300	4 300
Tax on equity component	-1 204	-1 204
At 31 December 2005	**3 096**	**3 096**

11. Interest-bearing liabilities/subordinated loan

Amounts in USD 1 000 **Period ended 31 December**	**2005**
Non-current	
Loan, The American Investment Bank, Trust Company of the West ("TCW")	35 135
Total non-current interest-bearing liabilities	**35 135**
Current	
Subordinated loan to Maxi Assets see note 5 (consolidated financial statements)	6 000
Total current interest-bearing liabilities/subordinated loans	**6 000**
Total interest-bearing liabilities/subordinated loans	**41 135**

Terms of the non-current interest-bearing liabilities:

	Currency	Amount	Effective interest rate	Maturity
Loans from the American Investment Bank, TCW	USD	35 135	14.4%	2012
Total non-current interest-bearing liabilities		**35 135**		

The effective interest rate at the balance sheet date for subordinated loan was 6.5%.

Fair value of the liabilities cannot be measured reliably, since the loan is not quoted in a market. Further information about the loan from TCW is set out in note 12.

The maturity of interest-bearing liabilities is as follows:

Amounts in USD 1 000	**2005**
0-12 months	639
Between 1 and 2 years	–
Between 2 and 5 years	17 545
Over 5 years	17 590
Total interest-bearing liabilities	**41 135**

The company's interest bearing liabilities are denominated in USD.

12. Loan with subscription rights

Period ended 31 December Amounts in USD 1 000	**2005**
Face value of loan from TCW	42 000
Borrowing cost	-2 825
Equity component	-4 300
Liability component on initial recognition at 27 September 2005	**34 875**
Amortisation of debt issue cost and liability component of issued interest bearing loan	260
Liability component at 31 December 2005 (note 11)	**35 135**

The Company has an interest-bearing loan amounting to USD 42 million to TCW. The nominal interest rate is 9% per year, quarterly payment, and 3 years grace on repayment of the principal. The down payment of the principal is on quarterly basis, starting October 2008, with final repayment October 2012.

The facility has a covenant structure with focus on the measurement of specific key figures, such as collateral coverage ratio and current ratio. In additions limitations are set for addional borrowings, sale and purchase of companies/assets, issuance of share capital and other negative covenants. The Company is not in breach with the covenants of the loan agreement and expects future compliance with these.

The company has issued 10 000 subscription rights to TCW. In total, the subscription rights gives TCW the right to subscribe for the number of ordinary shares that can be purchased for USD 5 040 divided on the price per share set in the Initial Public Offering (IPO). The subscription price for new shares is the highest of the price in NOK equivalent to USD 0.01 and the par value of the shares. The subscription rights may be exercised at the last day of the initial public offering prior to the listing on Oslo Stock Exchange only. Shares subscribed for in accordance with the subscription rights may not in any way be disposed of before six months after closing of the initial public offering. The residual value of the subscription rights were USD 4 300 on initial recognition at 27 September 2005. It is assumed that the subscription rights will be exercised in September 2007. Except for the subscription rights described above, the Company has no outstanding convertible bonds, options or other rights to subscribe for shares in the Company.

In the event that there has not been an initial public offering within 21 September 2007, TCW shall have a springing royalty of 1.5% on all of the Groups petroleum production which springing royalty shall be retroactive for the two year period from 21 September 2005 to 21 September 2007.

NOTES TO INTEROIL EXPLORATION AND PRODUCTION ASA FINANCIAL STATEMENTS

13. Trade and other payables

Period ended 31 December

Amounts in USD 1 000	**2005**
Trade creditors	422
Public duties payable	9
Mercantile International Petroleum Inc. – selling credit	500
Maxi Assets – selling credit, Note 5 (consolidated financial statements)	3 000
Other accrued expenses	1 080
Total trade and other payables	**5 012**

The carrying amount of trade and other payable is considered to approximate their fair value.

14. Subsidiaries

Period ended 31 December 2005

Amounts in USD 1 000	Registered business address	Book value	Interest held
InterOil SA	Switzerland	78	100%
InterOil Exploration and Production Latin-America AS	Norway	77 017	100%
InterOil Exploration and Production Africa AS	Norway	18	100%
InterOil Exploration and Production Colombia AS	Norway	18	100%
Total book value		**77 130**	

15. Provisions for other liabilities and charges

Amounts in USD 1 000

Period ended 31 December 2005	Legal claims	Total
At incorporation date	-	-
Charged to income statement:		
-Additional provisions	100	100
Used during the year	-	-
At 31 December 2005	**100**	**100**

See note 23 (consolidated financial statements).

AUDITOR'S REPORT FOR 2005

To the Annual Shareholders' Meeting of InterOil Exploration and Production ASA

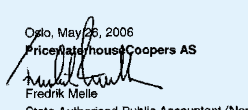
We have audited the annual financial statements of InterOil Exploration and Production ASA as of December 31, 2005, showing a loss of USD 1 578 000 for the parent company and a profit of USD 276 000 for the group. We have also audited the information in the directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the loss. The annual financial statements comprise the financial statements of the parent company and the group. The financial statement of the parent company comprise the balance sheet, the statements of income and cash flows, the statement of changes in equity and the accompanying notes. The financial statement of the group comprise the balance sheet, the statement of income and cash flows, the statement of changes in equity and the accompanying notes. Simplified IFRS according to the Norwegian accounting act § 3-9 have been applied in the preparation of the financial statements of the parent company. IFRSs as adopted by the EU have been applied in the preparation of the financial statements of the group. These financial statements are the responsibility of the Company's Board of Directors and Managing Director. Our responsibility is to express an opinion on these financial statements and on other information according to the requirements of the Norwegian Act on Auditing and Auditors.

We conducted our audit in accordance with the laws, regulations and auditing standards and practices generally accepted in Norway, including standards on auditing adopted by The Norwegian Institute of Public Accountants. These auditing standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. To the extent required by law and auditing standards an audit also comprises a review of the management of the Company's financial affairs and its accounting and internal control systems. We believe that our audit provides a reasonable basis for our opinion.

In our opinion,

- the financial statements of the parent company have been prepared in accordance with the law and regulations and give a true and fair view of the financial position of the Company as of December 31, 2005, and the results of its operations and its cash flows and the changes in equity for the period then ended, in accordance with simplified IFRS according to the Norwegian accounting act § 3-9
- the financial statements of the group have been prepared in accordance with the law and regulations and give a true and fair view of the financial position of the Group as of December 31, 2005, and the results of its operations and its cash flows and the changes in equity for the period then ended, in accordance with IFRS as adopted by the EU
- the company's management has fulfilled its duty to produce a proper and clearly set out registration and documentation of accounting information in accordance with the law and good bookkeeping practice in Norway
- the information in the directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the loss are consistent with the financial statements and comply with the law and regulations

Oslo, May 26, 2006
PricewaterhouseCoopers AS



Fredrik Melle
State Authorised Public Accountant (Norway)

Contact

InterOil Exploration & Production ASA
Strandveien 50
1366 Lysaker
Norway
+47 67 51 86 50

Appendix 3: Condensed Consolidated Interim Financial Information for the first quarter 2006

InterOil

Exploration & Production ASA

Report for the first quarter 2006

8 June, 2006

First quarter 2006

Interoil Exploration and Production ("the Company") acquired the producing assets in South America September 27, 2005. The Company was established on 2 May 2005. Based on this, a material portion of the transactions recorded for the period from 2 May 2004 (inception) to 31 December 2005 is recorded in the 4th quarter 2005. Based on this, the financial information for the above mentioned period has been referred to as Q4 2005 in this report.

Interoil total revenue for Q1 2006 was USD 8.6 million. The Group result before tax was USD 2.0 million.

Key Figures

Figures in USD millions	For the three months ended 31 March 2006 ("Q1 2006")	For the period fom 2 May 2005 (inception) to 31 December 2005 ("Q4 2005")
Operating revenue	8.6	8.0
Production, before royalties(bbls)	245 421	221 367
Production, net of royalties (bbls)	160 237	144 249
EBITDA	5.6	3.9
Profit before tax	2.0	0.8
Capitalized Expenditures	5.2	3.6

Operations

The operating revenue for Q1 2006 was USD 8.6 million and profit before tax was USD 2.0 million. As for Q4 2005, the result for Q1 2006 must be considered in light of the fact that a lot of expenses were incurred in implementing the acquisition, and pursuing business opportunities both in Peru and Columbia as well as in West Africa. The effort in West Africa has carried fruits, as we have been offered shares in two interesting blocks in Angola.

Production and sales

The production after royalties for Q1 2006 was 160 237 barrels of oil, up from 144 249 barrels for Q4 2005. The production is sold every two weeks to Hocol (Colombia) and PetroPeru, whereas there are some minor differences between sales and production figures for the same period. In Q1 2006 the sale was 152 129 barrels, while the production was 160 237 barrels. In Q4 2005 the sale was 154 684 barrels, while production was 144 249 barrels. The sale is made at market price for that specific quality of oil.

Financial Items and tax
Net financial costs for the first quarter of 2006 were USD 1.3 million of which the interest to "Trust Company of the West" (TCW) related to acquisition loan was USD 1.2 million.

Net profit for the first quarter of 2006 was USD 0.6 million after income tax expense of USD 1.4 million.

Investments
Investments/Capitalized expenditures in the first quarter of 2006 was USD 5.2 million. For details, see operational highlights below.

Balance Sheet and Liquidity
Interoils total assets as at 31. March 2006 was USD 122,0 million and total cash and cash equivalents was USD 7.2 million. Additionally USD 8.0 million was invested in Money market funds. The equity ratio of the group was 39.0%.

Cash flow
Operating activities generated a cash flow of USD 4.5 million during the first quarter of 2006.

Operational Highlights

Interoil acquired the Peruvian and Colombian assets end September, 2005. After reviewing the operations and securing the required approvals, Interoil began an investment program in both countries with the aim of increasing production. The summary below gives an update of achievements so far:

All production figures are Working Interest (WI) gross of royalty

Peru

In Peru we have by the end of April 2006 drilled 7 out of 11 planned well program in 2006. All wells have discovered oil and we are very enthusiastic regarding the results of the ongoing drilling program. As a result, the production has increased from 1 700 barrels per day ("bopd") by the end of September 2005 to
2 400 bopd by the end of April 2006. The area of focus for our development drilling is in the southern part of Block III, where we have a relatively large area not extensively drilled previously, and the northern part of Block IV, where we have discovered a fault block not previously depleted. This area in Block IV is of particular interest since production from these wells has been as high as 320 bopd, which is substantially higher than expected. We are therefore giving priority to this area in our next wells to be drilled over the next months. We believe that these new wells have a potential to increase the production above the current level.

Colombia

In Colombia we have by the end of April drilled 6 out of 8 wells planned in 2006. All wells except one encountered oil. We have drilled one well in the Mana license which was dry and another well in Ambrosia which encountered oil but had limited flow rates. After the two less successful wells, Interoil as the new owner changed the drilling program focusing on drilling in the producing areas of the concessions. This shift has been a success and the wells on Toqui Toqui, our main producing field, have yielded significant additional production.

The well drilled in the license to the east, in Puli B, jointly with our license partner Pacific Stratus, was a very successful well, producing 220 bopd, where we have 50% interest. We have also performed well stimulation /fracking which have given positive results. All in all, the production increase in Colombia from October to April has been from 740 bopd to 1 100 bopd by the end of April 2006.

Currently we are producing 2 300 - 2 500 bopd in Peru and 1 100 bopd in Colombia.

Reserves as of 31 March 2006:

Interoil reserve classification uses the SPE/WPC definitions estimating Proven and Probable reserves. The reserves have been audited by an independent third party, Gaffney Cline. The reserves have, for the sake of clarity, been reported before and after royalty. Royalty in Peru is dependent on oil price so hence the net of royalty number is only correct at date of report (31 March 2006). The reserves in Peru have increased by 2.7 million barrels since 31 December 2006. The increase can be traced back to successful drilling made in Q1 2006 which has caused higher production than expected. As these reserves figures were presented immediately upon presentation of this report, the income statement presented has not been affected through reduction of depreciation and amortization following the new reserves.

Peru

RESERVE CATEGORY Working Interest (WI) *in mmbbls*	BLOCK III	BLOCK IV	PERU TOTAL
Proven	5.8	4.9	10.7
Probable	1.0	1.4	2.4
Proven +Probable	6.8	6.3	13.1

RESERVE CATEGORY Net of Royalty *in mmbbls*	BLOCK III	BLOCK IV	PERU TOTAL
Proven	3.2	2.8	6.0
Probable	0.6	0.8	1.4
Proven +Probable	3.8	3.6	7.4

Colombia

RESERVE CATEGORY Working Interest (WI) *in mmbbls*	COL TOTAL
Proven	3.4
Probable	1.9
Proven +Probable	5.3

RESERVE CATEGORY Net of Royalty *in mmbbls*	COL: TOTAL
Proven	2.8
Probable	1.6
Proven +Probable	4.4

Summary of Reserves (WI) million bbls - Peru and Colombia

Proved ***14.1***
Proven +Probable ***18.4***

Outlook

Production was at 245 421 barrels for Q1. The main increase from the successful drilling in Peru will be reflected in Q2. Drilling will continue, mainly in Peru in Q2, and a new drilling campaign of six wells has been decided in addition to the 11 wells already planned for with the aim of further increasing production. In Colombia, another well is planned for Toqui Toqui in June, and another well in Puli B for August. Activities for Q2 consist of workovers in mainly Toqui Toqui in order to optimize production.

Angola

In addition to its activities in Colombia and Peru, InterOil is in the process of establishing operations in West-Africa. Angola's economy has undergone a period of rapid transformation in recent years, moving from a quarter century of war to being the fastest growing economy in Africa and one of the fastest in the world. Growth is almost entirely driven by rising oil production which surpassed 1.2 million barrels per day in late 2005. In Angola the historical success rate for drilling of exploration wells is is 50%.

The republic of Angola includes three of the major salt basins on Africa's Atlantic margin. The three major basins are the Congo Basin in the North, Kwanza/ Benguela Basin in the centre and the Namibe Basin to the South. In May 2006 InterOil was offered to participate in two licences in Block 5 & 6 in Angola's Kwanza Basin. InterOil will receive 40% in Block 5, where Vaalco is the operator and 20% in Block 6 where Petrobras is the operator.

Block 5 was first licensed to Total in the 1970s. The area was further developed by Conoco and Sonangol throughout the 1980s and 1990s. The continued presence of oil in five wells indicates that oil is generated in the area.

Block 6 was also first licensed to Total. After being further developed by Conoco and Sonangol, it will now be operated by Petrobras. The discovery of heavy oil in two wells gives rise to optimism, as the operator has extensive experience in the development of such fields. We are very enthusiastic when it comes to the development of the two licenses and we consider the awards a breakthrough for our ambitions to build a substantial position in West Africa.

Lysaker, 8 June 2006

The Board of Directors of
Interoil Exploration and Production ASA

***

Appendix 4: Auditors statement on review of pro forma adjustments

PricewaterhouseCoopers AS
N-0245 Oslo
Telephone +47 02316
Telefax +47 23 16 10 00

To the Shareholders of Interoil Exploration and Production ASA

Independent Auditor's Statement on Review of Pro Forma Adjustments

We have examined the pro forma adjustments reflecting the transaction described in chapter 6.2 in the prospectus and the application of these adjustments to the historical financial information in preparation of unaudited pro forma consolidated income statement data for the year ended 31 December 2005.

The unaudited pro forma consolidated income statement data for the year ended 31 December 2005 is prepared on the basis of audited consolidated financial statements for Interoil Exploration and Production ASA and subsidiaries. It is our responsibility to provide the opinion required by the Norwegian Securities Trading Act and accompanying regulation. We are not responsible for expressing any other opinion on the pro forma consolidated income statement date or on any of its constituent elements.

We conducted our examination in accordance with the Norwegian Auditing standard RS 800 "The Auditor's report on special purpose audit engagements". Our work consisted primarily of comparing the unadjusted financial information with the source documents, obtaining evidence supporting the adjustments and discussing the pro forma financial information with the management of the Company. We believe that our examination provides a reasonable basis for our opinion.

The objective of the pro forma financial information is to present what the most significant effects on the historical financial information might have been, had the transaction occurred at an earlier date. However, the pro forma financial information is not necessarily indicative of the financial position and the result of the operations that would have been attained, had the above mentioned transaction actually occurred earlier. The pro forma financial information is not intended to provide, nor does it provide, all information and additional information required to express Interoil Exploration and Production ASA's consolidated financial position and result in compliance with International Financial Reporting Standards (IFRS) as adopted by EU.

Based on our examination, in our opinion the unaudited pro forma financial information has been properly compiled on the basis stated and that basis is consistent with the accounting policies of the issuer.

Oslo, 26 May 2006
PricewaterhouseCoopers AS

Fredrik Melle
State Authorised Public Accountant (Norway)

Kontorer: Arendal Bergen Drammen Fredrikstad Førde Hamar Kristiansand Mo i Rana Molde Måløy Narvik Oslo Stavanger Stryn Tromsø Trondheim Tønsberg Ålesund
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www.pwc.no

Appendix 5: Annual Report 2004 for Mercantile International Petroleum Inc.

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
Providence House
East Hill Street
P.O. Box N-3910
Nassau, The Bahamas
Website: www.pwc.com
E-mail: pwcbs@bs.pwc.com
Telephone (242) 302-5300
Facsimile (242) 302-5350

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Mercantile International Petroleum Inc.

We have audited the accompanying consolidated balance sheets of Mercantile International Petroleum Inc. and its subsidiaries (the Company) as of 31 December 2004 and 2003 and the related consolidated statements of operations, changes in shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Canada. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as of 31 December 2004 and 2003, and the results of its consolidated operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in Canada.

PricewaterhouseCoopers

Chartered Accountants
5 May 2005

MERCANTILE INTERNATIONAL PETROLEUM INC.

CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 2004

Mercantile International Petroleum Inc.
Consolidated Balance Sheet
As of 31 December 2004 and 2003
(Expressed in United States dollars)

ASSETS	2004 $	2003 $
Current Assets		
Cash (Note 4)	4,183,014	3,835,328
Trade accounts receivable	1,184,538	659,366
Recoverable expenses (Note 8)	882,691	725,660
Sundry receivables	126,841	28,565
Inventory	114,253	122,426
Prepaid expenses and other current assets	1,318,031	575,468
	7,809,368	5,946,813
Property, Plant and Equipment (Note 5)	51,126,832	42,875,902
Total Assets	58,936,200	48,822,715
LIABILITIES		
Current Liabilities		
Accounts payable		
Bank loan (Note 4)	1,112,461	-
Trade accounts payable	3,302,896	696,238
Other payables and accruals	3,208,216	2,072,614
	7,623,573	2,768,852
Long-term Liabilities		
Deferred tax (Note 6)	4,164,308	3,105,982
Site restoration	830,439	743,193
	4,994,747	3,849,175
SHAREHOLDERS' EQUITY		
Share capital (Note 7)	25,431,674	25,431,674
Contributed surplus	15,497,114	15,497,114
Retained earnings	5,389,092	1,275,900
	46,317,880	42,204,688
Total Liabilities and Shareholders' Equity	58,936,200	48,822,715

SIGNED ON BEHALF OF THE BOARD:

Director

5 May 2005
Date

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Operations
For the years ended 31 December 2004 and 2003
(Expressed in United States dollars)

	2004 $	2003 $
REVENUE		
Oil and gas, net of royalties	17,039,871	11,734,782
Interest and other income	73,618	213,683
Total revenue	**17,113,489**	**11,948,465**
EXPENSES		
Oil and gas operating expenses	4,278,916	4,303,938
General and administrative		
Corporate	1,361,851	1,201,857
Peru	548,319	454,317
Colombia	369,580	697,025
Interest and bank charges	314,824	102,794
Site restoration provision	87,246	53,115
Depletion, depreciation and amortization	4,556,127	5,226,901
Total expenses	**11,516,863**	**12,039,947**
Net income/(loss) before income tax	**5,596,626**	**(91,482)**
Income tax:		
Current	(425,108)	(582,424)
Deferred	(1,058,326)	1,949,806
Net income for the year	**4,113,192**	**1,275,900**
Basic income per share after tax (Note 7)	**0.11**	**0.03**

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Changes in Shareholders' Equity
For the Years Ended 31 December 2004 and 2003
(Expressed in United States dollars)

	Share Capital	Contributed Surplus	Retained earnings	Total
	$	$	$	$
Balance as of 1 January 2003	25,431,674	79,228,326	(63, 731,212)	40,928,788
Transfer of retained deficit as of 30 June 2003 to contributed surplus approved by directors meeting on 1 July 2003 (Note 7)	-	(63,731,212)	63,731,212	-
Net income	-	-	1,275,900	1,275,900
Balance as of 31 December 2003	**25,431,674**	**15,497,114**	**1,275,900**	**42,204,688**
Balance as of 1 January 2004	25,431,674	15,497,114	1,275,900	42,204,688
Net income	-	-	4,113,192	4,113,192
Balance as of 31 December 2004	**25,431,674**	**15,497,114**	**5,389,092**	**46,317,880**

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Cash Flows
For the years ended 31 December 2004 and 2003
(Expressed in United States dollars)

	2004	2003
	$	$
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income for the year	4,113,192	1,275,900
Adjustments for non-cash items:		
Depletion, depreciation and amortization	4,556,127	5,226,901
Site restoration provision	87,246	53,115
Deferred taxes	1,058,326	(1,949,806)
(Increase)/decrease in trade and sundry receivables	(623,448)	691,607
(Increase)/decrease in recoverable expenses	(157,031)	322,726
Decrease/(increase) in inventory	8,173	(14,452)
Increase in prepaid expenses and other current assets	(742,563)	(54,204)
Increase/(decrease) in accounts payable and accruals	3,742,265	(1,808,103)
Net cash from operating activities	**12,042,287**	**3,743,684**
CASH FLOWS FROM INVESTING ACTIVITIES		
Expenditure for property, plant and equipment	(12,807,062)	(1,202,354)
Net cash used in investing activities	**(12,807,062)**	**(1,202,354)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Bank loan	1,112,461	(300,000)
Net cash from/(used in) financing activities	**1,112,461**	**(300,000)**
Net increase in cash and cash equivalents	347,686	2,241,330
Cash and cash equivalents, beginning of year	3,835,328	1,593,998
Cash and cash equivalents, end of year	**4,183,014**	**3,835,328**

The accompanying notes are integral part of these financial statements.

1. **Incorporation and Activities**

Mercantile International Petroleum Inc. (the Company) is incorporated in the Cayman Islands. The registered office of the Company is at West Wind Building, P.O. Box 2075, Grand Cayman, Cayman Islands. The Company is the successor to an amalgamation of Mercantile International Petroleum B.V.I. Inc. and Severn Mines Limited pursuant to a scheme of arrangement and amalgamation dated April 1996. The Company is involved in oil and gas acquisition, exploration and development and presently holds certain oil and gas interests through wholly owned subsidiaries in Peru (Mercantile Peru Oil and Gas S.A. and Compañía Petrolera Río Bravo S.A.) and Colombia (Mercantile Colombia Oil and Gas Inc.). The Company has two other wholly-owned subsidiaries: Mercantile South-East Asia Petroleum Inc. (MSEA) which is inactive and Mercantile Admin. (Bahamas) Inc. (MABI).

Its current activities are the result of the following interests and acquisitions:

Peru

Mercantile Peru Oil and Gas S.A. (MPOG), a wholly owned subsidiary of the Company, has a 100% working interest in a licensed contract for Block III in the Talara Basin. All oil produced from the license area is sold to Petróleos del Peru S.A. Block III currently produces approximately 1202 BOPD from 159 wells (2003: 645 BOPD from 152 wells). A program for enhancement of the oil production from existing and shut-in wells is presently under consideration.

Compañía Petrolera Río Bravo S.A. (Río Bravo), wholly-owned subsidiaries of the Company, have a 100% working interest in a licensed contract for the Block IV in the Talara Basin. All oil produced from the license area is also sold to Petroleos del Peru S.A. Block IV currently produces approximately 898 BOPD from 197 wells (2003: 586 BOPD from 150 wells).

Colombia

Mercantile Colombia Oil and Gas Inc. (MCOG), a wholly owned subsidiary of the Company, has ownership interests in five association contracts located in the Magdalena River Valley of Colombia.

MCOG currently produces 1450 BOPD from 36 wells (2003: 805 BOPD from 33 wells) in the Toqui, Puli, Rio Opia, Ambrosia, Mana and Armero fields.

2. **Summary of Significant Accounting Policies**

The Company's consolidated financial statements are prepared under the historical cost convention and conform in all material respects to accounting principles generally accepted in Canada. Significant accounting policies adopted are as follows:

(a) Use of estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. **Summary of Significant Accounting Policies (Continued)**

(b) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries in Peru, Colombia, and The Bahamas. All material intercompany items have been eliminated in consolidation. A substantial part of the Company's operations is carried out through joint venture, partnership or similar arrangements. The financial statements reflect only the Company's proportionate interest in such arrangements.

(c) Oil and gas operations

(i) Capitalized Costs – The Company follows the full cost method of accounting whereby all costs associated with the exploration for and development of crude oil and natural gas reserves are capitalized in cost centers on a country by country basis and charges against income as set out below. Such costs include land acquisition, lease rentals on non-producing properties, drilling, geological and geophysical, and facilities. Proceeds on disposition of oil and gas properties and production equipment are credited against accumulated costs. However, when such a disposal would change the rate of depletion and depreciation by more than 20%, a gain or loss is recorded.

(ii) Depletion and Depreciation - Capitalized costs of properties having proved reserves, including a provision for future costs to develop such reserves, are amortized through depletion and depreciation charges using the unit of production method based on estimated proved crude oil and natural gas reserves, as determined by independent reservoir engineers. For purposes of these calculations, production of crude oil and natural gas reserves are converted to a common unit of measure on the basis of their approximate relative energy content. Costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion until it is determined whether or not proved reserves are attributable to the properties or impairment occurs. Other fixed assets are depreciated on a straight-line basis over 3 to 10 years.

(iii) Ceiling Test – The net carrying value of the Company's oil and gas properties and production equipment in cost centers is limited to an estimated recoverable amount. This amount is calculated as the aggregate future net revenues from proved reserves plus the cost of unproved properties, net of impairment allowances, less future expenditures required to develop and produce those reserves. Future net revenues are calculated using prices in effect at the Company's year-end without escalation or discounting. The net carrying value of all cost centers, less accumulated provisions for future site restoration costs and deferred income taxes, is further limited to the total estimated recoverable amount of all cost centers, less future general and administrative costs, financing costs and income taxes. The oil prices used in performing the ceiling test as of 31 December 2004 were $22 and $25 (2003: $25 and $25) for Peru and Colombia, respectively. The prices used for benchmark are Forties, Oman and Suez Blend, and WTI for Peru and Columbia, respectively.

2. Summary of Significant Accounting Policies (Continued)

(c) Oil and gas operations (Continued)

(iv) Site restoration – Future estimated site restoration costs for property, plant and equipment, net of expected recoveries, are accrued and charged against income over the life of the estimated proved crude oil and natural gas reserves using the unit of production method. Site restoration expenditures incurred are charged to the accumulated provision for future site restoration.

(d) Inventory

Crude oil inventory is valued at the lower of either its cost or net realizable value.

(e) Revenue recognition

Oil and gas revenue is recognized when deliveries are made at a sales transfer point.

(f) Foreign currency translation

The Company regards the United States dollar as its functional currency and substantially all transactions are conducted in United States dollars. Monetary assets and liabilities denominated in currencies other than the Unites States dollar have been translated into United States dollars at the applicable exchange rates at the balance sheet date and non-monetary items are translated at historic rates. Foreign currency transaction and income and expense items have been translated at the average exchange rates for the year except for depreciation and depletion, which are translated at historic rates. Gains and losses arising from translation are taken directly to the income statement (interest and bank charges), except for those relating to monetary items having a fixed or ascertainable life extending beyond one year, which are deferred and amortized over the remaining life of the monetary items.

(g) Taxes

The subsidiaries located in Peru and Colombia make full provision for corporate taxes deferred as the result of claiming depreciation, exploration, development and other costs for corporate tax purposes, which differ from the related amounts charged to earnings. The Company is incorporated in the Cayman Islands and MABI is domiciled in The Bahamas. Both countries are no tax jurisdictions and accordingly there is no liability in respect of income tax, corporate tax or capital gains tax.

(h) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with banks, including amounts restricted to satisfy work commitments and guarantees (see note 10).

3. Taxation

The Company through its subsidiaries in Peru and Colombia has accumulated taxation losses as of 31 December 2004 in the amounts of $4,947,959 and $1,772,085, respectively. These taxation losses are available for offset against any future profits of the respective subsidiary within four or five years of the year in which the loss was incurred. There are no accumulated taxation losses available for offset against future profits with respect to Rio Bravo, PAIPC and MSLA. There are deferred taxes assets within the Peruvian subsidiaries as of 31 December 2004 (see note 6).

4. Cash

Cash balances as of 31 December comprise:

	2004 $	2003 $
Unrestricted funds	4,183,014	3,685,328
Restricted funds	-	150,000
	4,183,014	**3,835,328**

Restricted Funds in 2004 and 2003 represent cash to secure bank performance bonds related to projects in Peru and Colombia or guarantees and commitments as defined at note 10.

The bank loan was acquired in March 2004 and was renewed in October in order to finance the Company's investments in projects.

5. Property, Plant and Equipment, Net

Property, plant and equipment, net comprise:

	2004 $	2003 $
Cost	108,446,961	95,666,906
Accumulated depletion, depreciation and amortization	(57,320,129)	(52,791,004)
	51,126,832	**42,875,902**

The cost balances above include oil and gas assets for Peru of $50,787,787 (2003: $47,039,319) and Colombia of $56,629,051 (2003: $46,936,501). The figure for Peru represents cost of acquisition of Blocks III and IV, beginning in 1994 and capital expenditures. The figure for Colombia represents historical investment by American International Petroleum Corporation of Colombia, acquired by the Company in February 1997, plus additions by MCOG since that date.

6. Deferred Tax

The deferred tax is recorded under the liability method, on the basis of the temporary differences between the assets and liabilities for tax purposes and those for financial purposes, by applying the tax rate currently in force.

	2004 $	2003 $
Balance as at 1 January	3,105,982	5,055,788
Transfer to Consolidated Statement of Operations	1,058,326	(1,949,806)
Balance as at 31 December	**4,164,308**	**3,105,982**

During 2003, Peru had recognized the tax benefit of $450,032 of the tax, losses used in the year 2003. In addition, based on the projection of its future results, Peru has recognized the tax benefit of the tax loss carry-forward for $1,350,097 which it estimates will be utilized with taxable income to be obtained until 2006.

7. Share Capital

The authorized capital of the Company is 250,000,000 (2003: 250,000,000) shares at a par value of Cdn$1.00 (2003: Cdn$1.00) each.

As of 31 December 2001, the Company had 42,521,442 issued and outstanding common shares with share capital and contributed surplus totaling $45,190,867.

Restructuring

On 28 June 2002, the Company restructured its US$40,000,000 11.5% senior unsecured debentures due 11 May 2002. The restructuring was done under a Plan of Arrangement under the Companies Law of the Cayman Islands, which was implemented effective as of 28 June 2002. Under the Plan, the Company's outstanding common shares were consolidated on a 10 for 1 basis into 4,252,144 consolidated common shares; 33,631,000 consolidated common shares and 43,604,000 new B Warrants of the Company were issued to the debenture holders in full satisfaction of all principal and accrued interest owing on the debentures; the Company's existing 12,000,000 warrants, expiring 11 May 2002, were exchanged for 1,200,000 new A warrants; 710,000 new A warrants were issued to the shareholders of the Company; and 773,000 consolidated common shares and 1,285,000 new B Warrants were issued to the Company's non-executive chairman, Jeffrey Waterous, (2% of total shares), to settle amounts owing to him for past services and to purchase his 4% working interest in Block III Talara, Peru.

All consolidated common shares and A Warrants issued under the Plan are held in escrow for up to 24 months after listing of the consolidated common shares on a recognized stock exchange (or such longer period, if any, imposed by the applicable exchange). The A Warrants entitle holders to purchase consolidated common shares at a price of US$1.20 per share and expire five (5) years after their first exercise date, which is the earlier of i) the second anniversary of the implementation of the Plan; and ii) the Company's common shares first trading at $2.40 per share or more for at least twenty (20) out of thirty (30) consecutive trading days. The B Warrants entitle holders to purchase consolidated common shares at a price of US$2.40 per share and expire three (3) years after the shares are first listed for trading on a recognized stock exchange, provided that after listing, the shares trade at $2.40 per share or more for at least twenty (20) out of thirty (30) consecutive trading days, and only one-third of the warrants may be exercised in each of such three years.

As part of the restructuring, a new stock option plan was approved, pursuant to which 10% of the fully diluted pro forma shares of the Company, representing up to 4,500,000 common shares (post restructuring) and 4,985,000 B Warrants were set aside for issuance to officers, directors and senior employees of the Company and its subsidiaries.

Following the restructuring, the issued and outstanding common shares are as follows:

	Number of common shares	Share Capital $	Contributed Surplus $
After consolidation on 10 to 1 basis	4,252,144	2,797,463	42,393,404
Shares issued to debenture holders in settlement of outstanding principal and interest	33,631,000	22,125,658	36,018,785
Shares issued to Non-Executive Chairman	773,000	508,553	816,137
	38,656,144	**24,431,674**	**79,228,326**

7. Share Capital (Continued)

	Number of common shares	Share Capital $	Contributed Surplus $
Transfer of retained deficit as of 30 June 2003 to contributed surplus approved by directors meeting on 1 July 2003	-	-	(63,731,212)
As of 31 December 2003	**38,656,144**	**25,431,674**	**15,497,114**

The Articles of the Company prescribe a par value per share. Shares to the founders were issued at par and then reduced to reflect the actual cash value contributed.

Following the restructuring, the following options and warrants are outstanding as of 31 December 2004 and 2003:

Date of grant	Number of common shares issued on exercise of options and warrants	Exercise price
28 June 2002	1,910,000 A Warrants	1.20
28 June 2002	44,889,000 B Warrants	2.40

Basic loss per share is calculated using the weighted average method. Fully diluted loss per share is not calculated as the effect of potential conversions of warrants and options in existence as of 31 December 2004 and 2003 would be anti-dilutive in nature.

8. Recoverable charges

These amounts relate to the portion of cost overruns incurred in oil wells in Colombia that are to be borne by Empresa Colombiana de Petroleos (Ecopetrol). These amounts are to be reimbursed during 2005.

9. Financial Instruments and Risk Management

The fair value of cash, investments, accounts receivable and all current liabilities approximate their carrying value due to the relatively short term nature of these instruments. The maximum credit risk exposure of all financial assets is therefore limited to the carrying value of those assets. A substantial portion of the Company's accounts receivable are with Ecopetrol.

The Company's activities expose it to a variety of financial risks. The Company's risk management program tries to minimize the potential adverse effects on its financial performance.

i) Foreign exchange risk - The Company operates mainly in United States dollars and for this reason it is not exposed to foreign exchange risk.

ii) Interest rate risk - Income and operational cash flows of the Company are independent of changes in market interest rates. The Company has no significant assets and liabilities that bear interest.

iii) Credit risk - The majority of all crude oil is sold to government agencies in Colombia and Peru, with the remaining oil being sold on terms of less than 30 days to independent distributors.

iv) Liquidity risk - Prudent liquidity risk management implies maintaining sufficient cash and the available funds to meet current obligations.

10. Commitments

The Company is committed to various minimum work programs under agreements in the countries in which they operate.

Peru

Minimum work programs commitment are:

Mercantile Peru Oil & Gas S.A.

Over the three year period as from 2 August 2004 (date of the third amendment), the Company should develop the following program that comprises of three stages and where the Company should develop the following works with the following investments:

	Investment US$
First stage (12 months)	
Drilling of 3 development wells	1,620,000
Re-conditioning of 6 wells	180,000
Rehabilitation of 10 wells temporarily abandoned	400,000
Drilling of water wells	50,000
Second stage (12 months)	
Drilling of 3 development wells	1,620,000
Re-conditioning of 5 wells	150,000
Rehabilitation of 3 wells temporarily abandoned	120,000
Recording of 80Km of 2D seismic	500,000
Drilling of water wells	50,000
Thirst stage (12 months)	
Drilling of 4 development wells	2,160,000
Re-conditioning of 2 wells	60,000
Rehabilitation of 2 wells temporarily abandoned	80,000
Recording of 80Km of 12 seismic	500,000
Drilling of water wells	50,000
Total investments	**7,540,000**

Additional work program

The additional work program will have a two year term calculated as from the date of completion of the minimum work program. This program comprises two stages and the development of the following works and investments:

10. Commitments (Continued)

Peru (Continued)

	Investment US$
First stage (12 months)	
Drilling of 3 development wells	1,620,000
Re-conditioning of 3 wells	90,000
Rehabilitation of 6 wells temporarily abandoned	240,000
Second stage (12 months)	
Drilling of 3 development wells	1,620,000
Re-conditioning of 2 wells	60,000
Rehabilitation of 4 wells temporarily abandoned	160,000
Total investments	**3,790,000**

Minimum work programs commitment are:

Compañia Petrolera Rio Bravo S.A.

Over the three year period as from 2 August 2004 (date of the third amendment), the Company should develop the following program that comprises of three stages and where the Company should develop the following works with the following investments:

	Investment US$
First stage (12 months)	
Drilling of 3 development wells	1,365,000
Re-conditioning of 7 wells	490,000
Rehabilitation of 9 wells temporarily abandoned	630,000
Drilling of water wells	30,000
Second stage (12 months)	
Drilling of 3 development wells	1,365,000
Re-conditioning of 4 wells	280,000
Rehabilitation of 10 wells temporarily abandoned	700,000
Recording of 80Km of 2D seismic	460,000
Drilling of water wells	40,000
Thirst stage (12 months)	
Drilling of 2 development wells	910,000
Re-conditioning of 6 wells	420,000
Rehabilitation of 5 wells temporarily abandoned	350,000
Recording of 80Km of 2D seismic	460,000
Total investments	**7,500,000**

Additional work program

The additional work program will have a two year term calculated as from the date of completion of the minimum work program. This program comprises two stages and the development of the following works and investments:

10. Commitments (Continued)

Peru (Continued)

	Investment US$
First stage (12 months)	
Drilling of 3 development wells	1,370,000
Re-conditioning of 3 wells	280,000
Rehabilitation of 6 wells temporarily abandoned	420,000
Second stage (12 months)	
Drilling of 3 development wells	910,000
Re-conditioning of 2 wells	280,000
Rehabilitation of 7 wells temporarily abandoned	490,000
Total investments	**3,750,000**

Columbia

No commitments for Colombia.

11. Contingencies

There are two litigations against the Company, brought by its former employees with a potential maximum exposure of $205,000. Legal counsel has advised that the Company has meritorious defenses against these claims and accordingly no provision has been made in these financial statements.

Peru

At the end of each quarter, the Company is obliged to present a guarantee to Perupetro S.A. for an amount equivalent to the difference between:

(a) Investments and expenses incurred by the Company in connection with performed activities or executed in accordance with the terms of the programs.

(b) The difference between the accumulated royalties as from the date of the third amendment up to the end of the current quarter, applying the royalties percentages in force before the date of the said amendment and the accumulated royalties for the same period, applying the new royalty percentage.

This guarantee will only be applicable if the difference between (a) and (b) above is less than zero.

At 31 December 2003, the Company received a demand from a prior worker who claims the payment of social contributions for US$60,000. Company's Management, based on its legal advisor's opinion, considers that this demand will not proceed and the final result will be favorable to the Company.

11. Contingencies (Continued)

Columbia

In ruling of July and October 2002, the Cundinamarca Administrative court agreed with the appeal of the Branch rejecting the National Tax Administration's claim of additional tax for 1996.

In March 2003, the ruling was appealed by the National Tax Administration to the State Council and the last actions made in this process were the presentation of conclusive allegations in June 2003, by the parties involved. As from 23 June 2003, the process is in its final phase. Management and its tax advisors believed that the Branch will prevail and thus have made no provision.

Appendix 6: Annual Report 2003 for Mercantile International Petroleum Inc.

Mercantile International Petroleum Inc.
Annual Report 2003

P.O. Box 2075 G.T.
West Wind Building
70 Harbour Drive
George Town, Grand Cayman

Mercantile International Petroleum Inc.

MERCANTILE INTERNATIONAL PETROLEUM, INC.

C/o Maricorp Services Ltd., 4th floor, West Wind Building, 70 Harbour Drive, George Town – Grand Cayman
Tel.: (305) 577 0133   Fax: (305) 358 3498

May 8th, 2004

Dear Shareholders:

The year 2003 was a transition year. The financial state of the Company turned around from nearly bankrupt 2 years ago to a healthy profitable Company. All debts were paid off and the existing production in Perú and Colombia were kept at the same level which basically means that the natural production decline of about 15% was replaced by additional oil production. The Company also hired new senior people in Colombia resulting in a strong technical team.

The year 2004 is a year where Mercantile is investing heavily in exploration wells and work-overs in Perú and Colombia. All incurred costs will be self-financed by the Company.

In Colombia the Company signed two new Exploration contracts, Gaviotas and the Maná Blocks. The first two Exploration wells drilled during the period of February through April, called Río Opia-1 and Ambrosía-1, were oil discoveries. The third Exploration well, Maná-1, will be drilled later this year.

Río Opia-1, located south of Toqui-Toqui field, encountered a new producing formation, called the Monserrate, which is of Cretaceous age. The well flows naturally between 200 - 400 bopd with an API of 31° and is presently on a 6 months testing program as required by law. It is too early to say what the flow capacity of the well will be. Mercantile is planning to stimulate the well by fracturing in order to increase the production further. A second development well is planned for later this year.

Ambrosía-1, located north-west of the Toqui-Toqui field, encountered hydrocarbons in the Doima /Chicoral formation. The well flows naturally between 180-250 bopd with an API of 25°. The well will be put on a 6 month long term production test similar to the Río Opia-1 well. The attractiveness of this discovery is the shallow depth (3000 ft) of the producing horizon. The costs of drilling the Development wells will be around $450,000 resulting in very profitable investments. The Company plans to drill this year four development wells over the Ambrosía structure.

The target in Colombia for this year is to double the production.

1

In Perú, the Government passed the new Royalty law and Perupetro´s Board of Directors approved Mercantile´s new Royalty/Investment program. It is anticipated that the Supreme Decree will be issued in about 2 months. Under the new law, the Royalty rate will be cut in half and could go as low as 13% depending on the price of oil. In exchange for the decrease in the Royalty rate, the Company is committed to spend $22.5 million over 5 years. Two Exploration wells are planned in Perú for this year. The new Royalty law will create an attractive business opportunity to develop the remaining reserves in Perú.

To summarize, Mercantile is investing heavily in 2004 in Exploration and Development with the aim to increase the production and the cash flows. I would like to stress that there are risks involved in Mercantile´s aggressive investment strategy with the greatest unknown being "Mother Earth".

The Company is progressing towards a Public Listing and is working with several advisors in the U.K. in preparation for the IPO on the AIM market. The Company is also looking for another country to invest in, thereby diversifying the portfolio. Finally, Mercantile is evaluating merger opportunities in order to enhance shareholder value.

Please feel free to contact me at: mercantileceo@aol.com, if you have any questions or comments.

Mercantile´s website is: www.mercantile.com.pe.

Yours very truly,

Rudolph Berends
Chief Executive Officer
Mercantile International Petroleum

Mercantile International Petroleum Inc.

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Mercantile International Petroleum Inc.

MERCANTILE INTERNATIONAL PETROLUEM INC.

BUSINESS PLAN FOR 2004

The Company has remained focused and true to its primary goal of developing and adding value for the Shareholder. Over the past two years the Company has taken a complete review of the practices and procedures and modified those that did not add value and incorporated new ones that have born fruit.

The past two years have been very difficult for the Company with the substantial legal judgements and debts incurred and the repayment of same. As of January 1, 2004 the Company has paid off these debts and obligations and is poised for growth and expansion.

We have a number of opportunities now available that previously were not. In Colombia we have drilled two wells with very promising results in areas that are very attractive economically and provide for many more offset drilling locations. In Peru, on November 21, 2003, the Peruvian Congress signed into law a new Royalty Program with the focus to revitalize the economy of Northwestern Peru and at the same time provide the impetus for the Contractor to invest in their fields. The new program offers substantially reduced royalties, less than half of what was being paid before, as an incentive to invest in the Contractor's respective blocks.

The Company is looking forward to 2004 and what it has to offer. The focus of our efforts can be summarized as follows:

1) Develop existing low cost reserves potential by reviewing and targeting bypassed zones not previously perforated and deepening existing wells thereby taking advantage of existing infrastructure.
2) Realize the potential offered by the new royalty program in Peru. The Company has committed to spend upwards of $20 million dollars, self financed, to reap the benefits for the Shareholder.
3) Grow Colombia by developing newly discovered oil reserves in the Rio Opia and Ambrosia Blocks. Recent production tests have resulted in a favorable appraisal of newly discovered reserves in each of the Blocks. While the exact size of the hydrocarbon structures is unknown, it appears that up to 10 additional wells in each structure could be drilled.
4) Develop a "third-leg" opening new business in a Country of choice. The Company sees the addition of a third area or Country as a means to reducing Shareholder risk and at the same time opening new doors to growth.
5) Evaluate potential merger opportunities. A merger would increase the size of the Company immediately and position the Company in a new country with immediate production and staffing. Economies of scale previously unavailable to us, such as

Mercantile International Petroleum Inc.

purchasing arrangements with the resulting cost reductions, could be implemented due to larger volumes. Lines of credit would also be available to the Company as the perceived risk to the lending institutions would be lower.

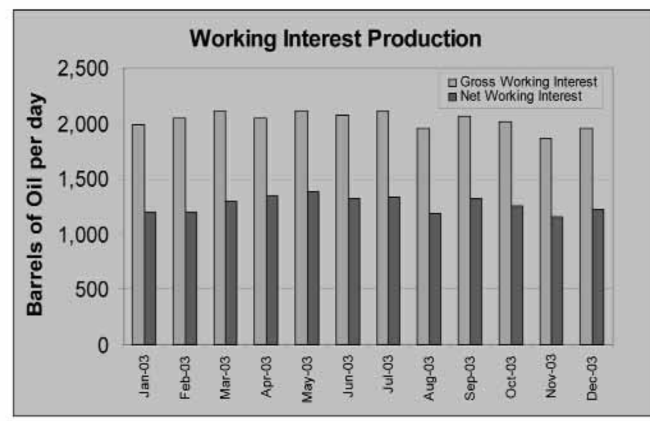
6) Continue IPO process with the Initial Placement Offering taking place late 2004. It is the intent of the Company and the desire of the Shareholder that the Company "go" public empowering the Shareholder with the liquidity they so desire.
7) Identify growth opportunities in the core countries of Colombia and Peru. Taking advantage of the existing infrastructure and experienced staff is one positive method of growing the Company. With the newly discovered fields in Colombia and the reduced royalty rate in Peru the Company is poised for growth.
8) Continue to incorporate techniques to reduce operating costs, improve operating practices and bring value to the Shareholder. This has been a focused effort the Company on all fronts. Incorporating experience from the various offices has resulted in substantial reductions in operating costs and at the same time maintaining or increasing production at no additional cost.

OPERATIONAL REVIEW

2003 Key Achievements:

- Reduced operating costs in Peru from $6.50/bbl to $5.72/bbl. Maintained costs in Colombia;
- Reduced overall per barrel General and Administrative costs by 4% and 17% in Colombia and Peru, respectively, now $1.94 vs. $2.02 for Colombia and $1.05 vs. $1.26 for Peru (excluding extraordinary items—office move);
- Combined LOE and G&A costs were reduced in Peru and only marginally higher in Columbia: $6.30 vs. $6.02 in Colombia and $6.77 vs. $7.76 in Peru;
- Increased production in both Colombia and Peru, with annual production now up 4% and 5% respectively from the year previously;
- Acquisition of two new blocks in association with Ecopetrol: Mana (November 2003) and Gaviotas (December 2003);
- Moved and consolidated offices in Peru reducing G&A by some $70k to $100k per year;
- MCOG "took back operatorship" of the Puli field from a third party contractor saving up to $15,000 monthly; and,

- Re-negotiated the crude price contract with ECP to obtain better pricing.



Operating Expenses

	12 months Dec. 31, 2003	12 months Dec. 31, 2002	12 months Dec. 31, 2001
Peru	$ 5.72 / bbl	$ 6.50 / bbl	$ 8.50 / bbl
Colombia	$ 4.36 / bbl	$ 4.00 / bbl	$ 4.12 / bbl
General & Administrative			
Peru	$ 1.05 / bbl	$ 1.26 / bbl	$ 1.59 / bbl
Colombia	$ 1.94 / bbl	$ 2.02 / bbl	$ 2.18 / bbl
Combined			
Peru	$ 6.77 / bbl	$ 7.76 / bbl	$10.09 / bbl
Colombia	$ 6.30 / bbl	$ 6.02 / bbl	$ 6.30 / bbl

Includes extraordinary items such as office relocation but excludes provisional items.

Looking Ahead to 2004:

- Drilled two discoveries in Colombia in the first quarter of this year, Rio Opia-1 and Ambrosia-1;
- It is anticipated the Company will sign the Reduced Royalty Fiscal terms in Peru by mid-year;
- Mercantile Peru will work over 11 wells, rehabilitate 11 wells and drill 4 wells;
- Mercantile Colombia will drill up to 6 additional wells in Colombia this year;
- Anticipate production will increase from 1100 bpd at the start of the year to over 1600 bpd by year-end in Peru (gross);
- Anticipate production will increase from 1500 bpd at the start of the year to over 2500 bpd by year-end in Colombia (gross);
- Drilling of several development wells to the Doima formation in Ambrosia and one well to the deeper formation, the newly discovered K4 formation, in the Rio Opia block;
- Future testing of a potential gas zone discovered in the Ambrosia well;
- Performing a general fracture study on the Toqui-Toqui field to increase production; and,
- Analyzing shooting density in old wells to increase flow area and drain more oil on the Toqui-Toqui and Peruvian fields.

COLOMBIAN OPERATIONS

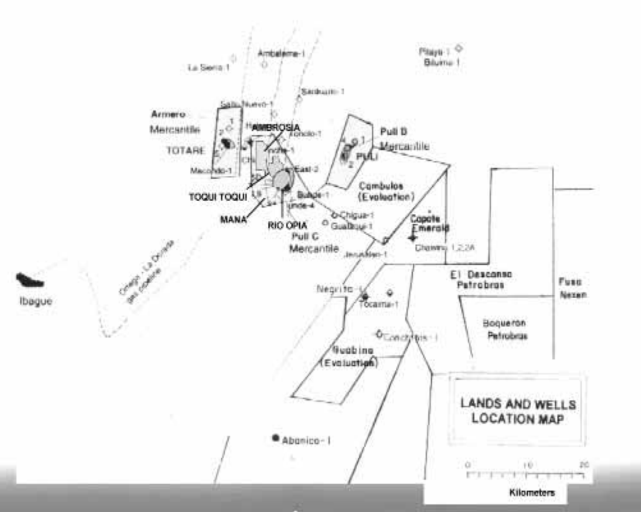
In February 1997, Mercantile acquired the Colombian subsidiary of American International Petroleum Corporation ("AIPC"). The Colombian company continued to operate under the name American International Petroleum Corporation of Colombia until September of 2000, when the name of the company was changed to Mercantile Colombia Oil and Gas Inc. ("MCOG").

MCOG is a wholly owned subsidiary of Mercantile. In May 1998, MCOG purchased from Petroleos del Norte, the 10% working interest, which it held in the Puli Association Contract. This increased MCOG's total working interest in this contract to 50%, with the remainder being held by Colombian state owned oil company, Ecopetrol. This contract was legalized on 27 April 1998 with the signature of Ecopetrol's president.

During December 2003, MCOG produced a gross daily average of 807 BOPD WI from 32 wells (2002: 715 BOPD from 32 wells) in the Toqui, Armero and Puli fields.

Three new contracts were signed (Río Opia, Ambrosía, Mana) during 2002 and 2003 with ECOPETROL S.A to explore and exploit hydrocarbons in the Puli "C" Block.

MCOG has ownership interests in seven association contracts located in the Magdalena River Valley of Colombia, as follows Puli B, Puli C, Armero, Rio Opia, Ambriosia, Mana and Gaviotas:



Mercantile International Petroleum Inc.

Summary:

Total Block Area:	62,945 acres	
Basin:	Middle Magdalena Valley.	
Contract Areas:	6	
Wells:	38	
Gross Production (Dec 2003):	Toqui-Toqui	940 bopd
	TT-34	37 bopd
	Totare	100 bopd
	Puli	200 bopd
	Total	1277 bopd
WI Production:		807 bopd
Royalty:	20% for above fields (8% on Rio Opia & Ambrosia)	

Reserves

	Net Reserves Mstb
Proved Developed Producing	1,029.55
Proved Developed Not Producing	260.69
Proved Undeveloped	2,216.00
Sum of the above	3,506.24
Total as a Project	3,576.38

Crude price: $25.00 per barrel.

EXPENSES

The following table shows the comparison of the production expenses and G&A for the years 2000 through 2003:

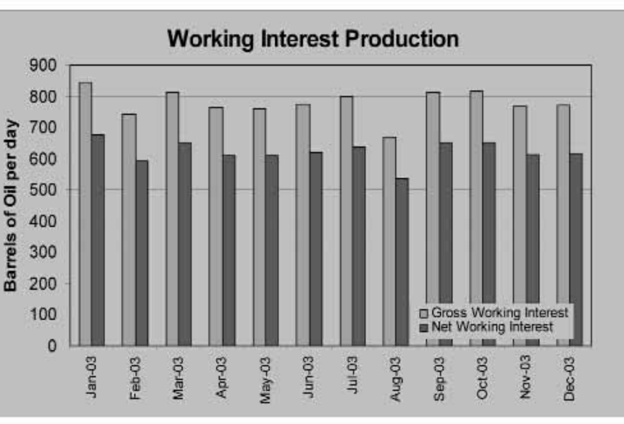
	2003	2002	2001	2000
Gross Production	456,659	452,222	494,561	530,741
Working Interest Production	279,749	282,176	307,125	333,375
L.O.E.	1,221,164	1,129,044	1,265,555	1,635,666
L.O.E. Per Barrel	4.36	4.00	4.12	4.91
G&A	544,727	570,858	670,915	704,000
G&A per Barrel	1.94	2.02	2.18	2.11
Sale Price at well head	24.06	19.35	19.52	21.68
Minimum Income Taxes	261,354	327,009	187,797	375,600

The expenses shown here do not include provisions.

Mercantile International Petroleum Inc.

LOCATION, STAFF AT OPERATION BASE

The administrative offices, located in Bogotá, are staffed by 8 people. The Toqui Toqui field is located 40 km. from Ibagué and the field's operations team is comprised of 10 people, conducting day-to-day production operations and oil dispatches. There are two operators and a watchman in the Totare field and one operator in Velasquez.



SIGNIFICANTS EVENTS

- Two exploration wells were successfully drilled, RO-1 and Amb-1, during the first quarter 2004;
- Currently the RO-1 well is being evaluated with a 6 months long term test;
- RO-1 is flowing naturally 200-400 bopd, an artificial lift system will be installed; and,
- MCOG "took back operatorship" of the Puli field from a third party contractor saving up to $15,000 monthly.

Mercantile International Petroleum Inc.

FUTURE POTENTIAL AND PLANNED ACTIVITIES

In Toqui Toqui Field

- In discussion with Gas del Tolima to sell all the Toqui Toqui gas production of approximately 1 million scf per day;
- Carrying out a study on the Chicoral formation to identify wells for fracturing operations under the risk/reward scheme with the contractors;
- Planning to implement a study evaluating the impact of increasing shot density in old wells; and,
- Redesign the scrubber system to avoid carry over of liquids into the plant pit.

In Ambrosia Field

- Future testing of a potential gas zone discovered in the Ambrosia well;
- Drilling of four shallow wells during the third quarter 2004 to a depth of 3,500 feet; and,
- Long Term Test for Amb-1.

In Río Opia Field

- Drilling one well to the newly discovered K-4 formation 6,000 feet; and,
- Long Term Test for RO-1.

In Mana Field

- Drilling one well to 4,000 feet.

PERUVIAN OPERATIONS

Mercantile currently licenses and operates two blocks located in the Talara Basin in northern Peru.

• BLOCK III
Block III is operated by a wholly owned subsidiary named Mercantile Peru Oil & Gas S.A. ("MPOG"). The interest was purchased from a private company in December 1994 and was subject to a Service Contract until December 19th, 1995. On that date MPOG became the official operator and negotiated a License Agreement with Perupetro, the Peruvian government licensing authority:

Expiration Date	July 2013
Area, acres	88,000
Current Production, bpd	572
Producing Wells	140

• BLOCK IV
This block is operated by a wholly owned subsidiary named Compania Petrolera Rio Bravo S.A. ("Rio Bravo"). The interest was purchased from AIPC in February 1997 and from a private company in November 1997. Rio Bravo became the operator under a License Agreement with Perupetro:

Expiration Date	July 2013
Area, acres	76,000
Current Production, bpd	533
Producing Wells	155

Block III

	Proven Reserves						
	Developed Production (MBbls)	Developed Not Producing (MBbls)	Un Developed (MBbls)	Total Proven (MBbls)	Probable (MBbls)	Possible (MBbls)	Total (MBbls)
GROSS	713.7	1,830.70	1,537.70	4,082.20	1,319.50	1,356.60	6,758.20
NET After Royalty	372.7	1,435.30	1,205.60	3,013.60	1,034.50	1,063.60	5,111.60

Crude price: $22.00 per barrel.

Mercantile International Petroleum Inc.

Block IV

	Proven Reserves						
	Developed Production (MBbls)	Developed Not Producing (MBbls)	Un Developed (MBbls)	Total Proven (MBbls)	Probable (MBbls)	Possible (MBbls)	Total (MBbls)
GROSS	816.8	895	1,849.90	3,561.80	1,224.90	1,178.30	5,965.00
NET After Royalty	437.1	732.1	1,513.30	2,682.50	1,001.90	963.8	4,648.30

Crude price: $22.00 per barrel.

LOCATION, STAFF AT OPERATION BASE
To avoid the duplication of management services and to minimize overhead, both MPOG and Rio Bravo have a signed joint Service Agreement, which allows a sharing of these costs. Mercantile now has only one office in Peru (shared with Rio Bravo) as a result of the merging of the administrative office, formerly in Lima with the field office in Talara. This will result in savings between $75,000 and $100,000 per year. Indirect savings are related to the reduced hotel and transportation costs that were previously incurred as a result of having two offices. Furthermore, the office in Talara moved as well to larger premises sufficient to handle the combined offices, with a yard for parking trucks and the Company's heavy equipment and all for a lower monthly rental rate.

The Talara office, midway between the two operational blocks, is where the field office is located. From this location day-to-day field operations, performance enhancing studies, geology and reservoir engineering are performed. There are 55 staff members comprised of management, engineers, accountants, operators and mechanics that maintain the operations and oversea the lifting operations and crude oil deliveries to the marketplace.

SIGNIFICANT EVENTS

Mercantile has held numerous discussions with the Government of Peru to further reduce the oil royalty. These discussions continued through 2003 until the Congress signed Ley 28109 "Ley Para La Promoción De La Inversión En La Explotación De Recursos Y Reservas Marginales De Hidrocarburos A Nivel Nacional" (Law For The Promotion Of Investment In The Exploitation Of Hydrocarbon Resources And Marginal Reserves). Mercantile Peru and Rio Bravo submitted an investment plan that has been approved by the Board of Directors of Perupetro and now is awaiting approval by the President and the issuance of a Supreme Decree (July, 2004). With this new law, the Company's onerous royalty payments (currently more than 55%) will be cut in half and could go as low as 13% depending on the price of oil. The Company plans to invest more than $22.5 million over the next 5 years in a combined drilling, rehabilitation and work over campaign;

- An extensive geological study was conducted on Blocks III and IV during 2003. This study has formed the basis for the work related to the New Royalty Law that we will undertake starting in late May;
- Reduced operating costs in Peru from $6.50/bbl to $5.02/bbl. Two years ago operating costs were $8.50 per barrel
- Reduced overall per barrel General and Administrative costs by 23% in Peru, now $0.97 vs. $1.26 per barrel for Peru (excluding extraordinary items—office move); and,
- Increase total annual production in 2003 over the year 2002. This was the result of a new stimulation program and working over 15 wells (Block III eight workover/rehabilitations and Block IV seven workovers).

FUTURE POTENTIAL AND PLANNED ACTIVITIES

As a result of the signing into law, Ley 28109, the Company plans to invest more than $22.5 million over the next 5 years in a combined drilling, rehabilitation and work over campaign. Mercantile Peru and Rio Bravo will undertake starting in late May, the work over of 11 wells, the rehabilitation of 11 wells and drill 4 wells;

- The Company is currently reviewing changing the fiscalization point (custody transfer point) with the focus to save some $200,000 instead of replacing pipelines and paying higher tariffs; and,
- The Company is continuing its ongoing program of repairing and restoring equipment that was previously abandoned with the result that operational costs have decreased now that the Company is doing the work itself instead of paying a local vendor.

Working Interest Production

Barrels of Oil per day (0 – 1,600); Jan-03 to Dec-03; □ Gross Working Interest ■ Net Working Interest

MANAGEMENT DISCUSSION AND ANALYSIS

Mercantile Internation Petroleum Inc.
Management Discussion and Analysis

	2003	2002	2001	2000
Revenue				
Oil and Gas net of royalties	11,734,782	9,401,502	9,450,018	10,715,087
Other Income	213,683	176,971	1,159,141	767,110
	11,948,465	9,578,473	10,609,159	11,482,197
Expenses				
Production	4,303,938	3,928,995	4,923,016	3,963,427
Operating profit	7,644,527	5,649,478	5,686,143	7,518,770
General and Administrative				
Corporate	1,201,857	843,615	499,522	512,280
Peru	454,317	576,493	854,654	970,476
Colombia	697,025	570,858	670,915	671,985
Total G & A	2,353,199	1,990,966	2,025,091	2,154,741
Taxes	-1,367,382	492,823	-41,343	500,169
Provisions	0	828,542	421,358	1,578,642
Interest & Banks Charges	102,794	123,381	248,485	134,815
Interest on long terms loans	0	1,661,110	4,600,000	4,600,000
Depletion and depreciation	5,226,901	4,925,670	4,882,595	6,723,209
Site Restoration provision	53,115	68,524	90,052	124,514
Loss in sales of assets			39,904	337
Amortization of deferred charges				1,235,000
Total Expenses	10,672,565	14,020,011	17,189,158	21,014,854
Net Profit (loss) for the year	**1,275,900**	-4,441,538	-6,579,999	-9,532,657

REVENUE PRODUCTION:

Oil and gas revenues for 2003 were $11,734,782 with $6,348,242 from Perú and $5,386,540 arising from Colombia. This compared to oil and gas revenues in 2002 of $9,401,502 with Peruvian operations accounting for $4,980,308 and Colombian operations accounting for $4,421,194, representing an increase of 24.8%.

The production in 2003 was 736,904 (Perú 457,155 barrels and Colombia 279,749 barrels) compared to 2002 production of 713,255 barrels (Perú 431,079 barrels at Colombia 282,176 barrels), an increase of approximately 3%.

OPERATING EXPENSE

Operating expense for 2003 decreased to $3,836,194 (Peru $2,615,030 and Colombia $1,221,164), compared to $3,928,996 for 2002 (Peru $2,799,952 and Colombia $1,129,044), an overall decrease of approximately 2%.

Operating expenses on a per barrel basis were as follows:

	12 months Dec. 31, 2003	**12 months Dec. 31, 2002**
Peru	$ 5.72 / bbl	$ 6.50 / bbl
Colombia	$4.36 / bbl	$ 4.00 / bbl

GENERAL AND ADMINISTRATIVE EXPENSES

General and Administrative expenses ("G&A") in 2003 increased 18% to $2,353,199 compared to $1,990,966.

Corporate G&A accounted for $1,201,857, while Peruvian and Colombian G&A was $454,317 and $697,025, respectively.

TAXATION

Through its subsidiaries the company has accumulated taxation losses in Perú of $6,731,885 and $4,749,984 in Colombia. These losses are available for offset against future profits of the respective subsidiary within four or five years of the year in which the loss was incurred.

LIQUIDITY AND CAPITAL RESOURCES

The Company paid off all remaining outstanding debt to Carbopetrol and AIPC.

OUTLOOK

Mercantile enters 2004 with a significant drilling campaign in Colombia and Perú.

The first two explorations wells in Colombia, Río Opia-1 and Ambrosía-1 are oil discoveries and presently Mercantile is carrying out a six months long term testing program as required by the Ministry of Energy.

One more exploration well is planned in Colombia for 2004, called Maná-1. Mercantile Colombia is also planning to drill 4 to 5 development wells in the Río Opia and Ambrosia block. It is the intention to double the production in Colombia in 2004.

Mercantile Perú production went slightly down during the first months of 2004. The reason is that the Company was waiting for the approval of Perupetro to lower the Royalty by more than half. In April, Perupetro's Board of Directors approved the Royalty reduction and Mercantile is now awaiting for a Supreme Decree which is expected to be issued in about 2 months. The new Royalty decree stipulates that Mercantile invest $22.5 million over the next five years. This new law will greatly increase the profitability of Perú.

Mercantile is pursuing an IPO in the United Kingdom, planned for later this year and is also in discussion with several merger candidates.

MERCANTILE INTERNATIONAL PETROLEUM INC.

CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 2003

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
P.O. Box N-1910
Providence House
East Hill Street
Nassau, The Bahamas
Telephone (242) 302 5300
Facsimile (242) 302 5350

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Mercantile International Petroleum Inc.

We have audited the accompanying consolidated balance sheets of Mercantile International Petroleum Inc. and its subsidiaries (the "Company") as of 31 December 2003 and 2002 and the related consolidated statements of operations, changes in shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Canada. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as of 31 December 2003 and 2002, and the results of its consolidated operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in Canada.

PricewaterhouseCoopers

Chartered Accountants
20 April 2004

Mercantile International Petroleum Inc.
Consolidated Balance Sheet
As of 31 December 2003 and 2002
(Expressed in United States dollars)

	2003	2002
ASSETS		
Current Assets		
Cash (Note 4)	3,835,328	1,593,998
Trade accounts receivable	659,366	1,217,234
Recoverable expenses (Note 10)	725,660	1,048,386
Sundry receivables	28,565	162,304
Inventory	122,426	107,974
Prepaid expenses and other current assets	575,468	521,264
	5,946,813	4,651,160
Property, Plant and Equipment (Note 5)	**42,875,902**	**46,900,449**
Total Assets	**48,822,715**	**51,551,609**
LIABILITIES		
Current Liabilities		
Trade accounts payable	696,238	2,371,487
Debentures (Note 7)	-	300,000
Other payables and accruals	2,072,614	2,205,468
	2,768,852	**4,876,955**
Long Term Liabilities		
Deferred tax (Note 8)	3,105,982	5,055,788
Site restoration	743,193	690,078
	3,849,175	**5,745,866**
SHAREHOLDERS' EQUITY		
Share capital (Note 9)	25,431,674	25,431,674
Contributed surplus	15,497,114	79,228,326
Retained Earnings/(deficit)	1,275,900	(63,731,212)
	42,204,688	**40,928,788**
Total Liabilities and Shareholders' Equity	**48,822,715**	**51,551,609**

SIGNED ON BEHALF OF THE BOARD:

Director

29 April 2004
Date

Director

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Operations
For the years ended 31 December 2003 and 2002
(Expressed in United States dollars)

	2003 $	2002 $
REVENUE		
Oil and gas, net of royalties	11,734,782	9,401,502
Interest and other income	213,683	176,971
Total revenue	**11,948,465**	**9,578,473**
EXPENSES		
Oil and gas operating expenses	4,303,938	3,928,995
General and administrative		
Corporate	1,201,857	843,615
Peru	454,317	576,493
Colombia	697,025	570,858
Interest and bank charges	102,794	123,381
Provision for adverse legal judgment (Note 15)	-	154,295
Site restoration provision	53,115	68,524
Retainer settlement (Note14)	-	373,223
Interest on debentures	-	1,661,110
Amortization of deferred charges (Note 6)	-	301,024
Depletion, depreciation and amortization	5,226,901	4,925,670
Total expenses	**12,039,947**	**13,527,188**
Net income/(loss) before income tax	**(91,482)**	**(3,948,715)**
Income tax:		
Current	(582,424)	(503,970)
Deferred	1,949,806	11,147
Net income/(loss) for the year	**1,275,900**	**(4,441,538)**
Basic income/(loss) per share after tax (Note 9)	**0.03**	**(0.21)**

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Changes in Shareholders' Equity
For the Years Ended 31 December 2003 and 2002
(Expressed in United States dollars)

	Share Capital $	Contributed Surplus $	Retained earnings $	Total $
Balance as of 1 January 2002	30,372,459	14,818,408	(59,289,674)	(14,098,807)
Consolidation of shares on 10 for 1 basis	(27,574,996)	27,574,996	-	-
Conversion of principal and interest on debentures into equity	22,125,658	36,018,785	-	58,144,443
Issue of shares in settlement of amounts owing to Non-Executive Chairman	508,553	816,137	-	1,324,690
Net loss	-	-	(4,441,538)	(4,441,538)
Balance as of 31 December 2002	**25,431,674**	**79,228,326**	**(63, 731,212)**	**40,928,788**
Balance as of 1 January 2003	25,431,674	79,228,326	(63, 731,212)	40,928,788
Transfer of retained deficit as of 30 June 2003 to contributed surplus approved by directors meeting on 1 July 2003 (Note 9)	-	(63,731,212)	63,731,212	-
Net income	-	-	1,275,900	1,275,900
Balance as of 31 December 2003	**25,431,674**	**15,497,114**	**1,275,900**	**42,204,688**

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Consolidated Statement of Cash Flows
For the years ended 31 December 2003 and 2002
(Expressed in United States dollars)

	2003 $	2002 $
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income/(loss) for the year	1,275,900	(4,441,538)
Adjustments for non-cash items:		
Depletion, depreciation and amortization	5,226,901	4,925,670
Amortization of deferred charges	-	301,024
Site restoration provision	53,115	68,524
Interest on debentures	-	1,661,110
Retainer settlement	-	373,223
Deferred taxes	(1,949,806)	(11,147)
Decrease in trade and sundry receivables	691,607	579,771
Decrease/(Increase) in recoverable expenses	322,726	(1,048,386)
Increase in inventory	(14,452)	(14,707)
(Increase)/Decrease in prepaid expenses and other current assets	(54,204)	38,602
Decrease in long-term receivable	-	155,727
(Decrease)/Increase in accounts payable and accruals	(1,808,103)	2,318,014
Decrease in purchase consideration payable	-	(65,976)
Decrease in provision	-	(800,000)
Net cash from operating activities	**3,743,684**	**4,039,911**
CASH FLOWS FROM INVESTING ACTIVITIES		
Expenditure for property, plant and equipment	(1,202,354)	(2,529,103)
Net cash used in investing activities	**(1,202,354)**	**(2,529,103)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of debentures	(300,000)	(1,200,000)
Net cash used in financing activities	**(300,000)**	**(1,200,000)**
Net increase in cash and cash equivalents	2,241,330	310,808
Cash and cash equivalents, beginning of year	1,593,998	1,283,190
Cash and cash equivalents, end of year	**3,835,328**	**1,593,998**

The accompanying notes are integral part of these financial statements.

Mercantile International Petroleum Inc.
Notes to the Consolidated Financial Statements
31 December 2003 and 2002

1. Incorporation and Activities

Mercantile International Petroleum Inc. (the Company) is incorporated in the Cayman Islands. The registered office of the Company is at West Wind Building, P.O. Box 2075, Grand Cayman, Cayman Islands. The Company is the successor to an amalgamation of Mercantile International Petroleum B.V.I. Inc. and Severn Mines Limited pursuant to a scheme of arrangement and amalgamation dated April 1996. The Company is involved in oil and gas acquisition, exploration and development and presently holds certain oil and gas interests through wholly owned subsidiaries in Peru (Mercantile Peru Oil and Gas S.A., Pan American International Petroleum Corporation and Compañia Petrolera Río Bravo S.A.) and Colombia (Mercantile Colombia Oil and Gas Inc.). The Company has two other wholly-owned subsidiaries: Mercantile South-East Asia Petroleum Inc. (MSEA) which is inactive and Mercantile Admin. (Bahamas) Inc. (MABI).

Its current activities are the result of the following interests and acquisitions:

Peru

Mercantile Peru Oil and Gas S.A. (MPOG), a wholly owned subsidiary of the Company, has a 100% working interest in a licensed contract for Block III in the Talara Basin. All oil produced from the license area is sold to Petróleos del Peru S.A. Block III currently produces approximately 645 BOPD from 152 wells (2002: 629 BOPD from 165 wells). A program for enhancement of the oil production from existing and shut-in wells is presently under consideration.

Pan American International Petroleum Corporation (PAIPC) and Compañia Petrolera Río Bravo S.A. (Río Bravo), wholly-owned subsidiaries of the Company, have a 100% working interest in a licensed contract for the Block IV in the Talara Basin. All oil produced from the license area is also sold to Petroleos del Peru S.A. Block IV currently produces approximately 586 BOPD from 155 wells (2002: 552 BOPD from 150 wells).

Colombia

Mercantile Colombia Oil and Gas Inc. (MCOG), a wholly owned subsidiary of the Company, has ownership interests in five association contracts located in the Magdalena River Valley of Colombia.

MCOG currently produces 805 BOPD from 33 wells (2002: 771 BOPD from 31 wells) in the Toqui, Puli and Armero fields.

2. Summary of Significant Accounting Policies

The Company's consolidated financial statements are prepared under the historical cost convention and conform in all material respects to accounting principles generally accepted in Canada. Significant accounting policies adopted are as follows:

2. Summary of Significant Accounting Policies (Continued)

(a) Use of estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(b) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries in Peru, Colombia, and The Bahamas. All material intercompany items have been eliminated in consolidation. A substantial part of the Company's operations is carried out through joint venture, partnership or similar arrangements. The financial statements reflect only the Company's proportionate interest in such arrangements.

(c) Oil and gas operations

(i) Capitalized Costs – The Company follows the full cost method of accounting whereby all costs associated with the exploration for and development of crude oil and natural gas reserves are capitalized in cost centers on a country by country basis and charges against income as set out below. Such costs include land acquisition, lease rentals on non-producing properties, drilling, geological and geophysical, and facilities. Proceeds on disposition of oil and gas properties and production equipment are credited against accumulated costs. However, when such a disposal would change the rate of depletion and depreciation by more than 20%, a gain or loss is recorded.

(ii) Depletion and Depreciation - Capitalized costs of properties having proved reserves, including a provision for future costs to develop such reserves, are amortized through depletion and depreciation charges using the unit of production method based on estimated proved crude oil and natural gas reserves, as determined by independent reservoir engineers. For purposes of these calculations, production of crude oil and natural gas reserves are converted to a common unit of measure on the basis of their approximate relative energy content. Costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion until it is determined whether or not proved reserves are attributable to the properties or impairment occurs. Other fixed assets are depreciated on a straight-line basis over 3 to 10 years.

(iii) Ceiling Test – The net carrying value of the Company's oil and gas properties and production equipment in cost centers is limited to an estimated recoverable amount. This amount is calculated as the aggregate future net revenues from proved reserves plus the cost of unproved properties, net of impairment allowances, less future expenditures required to develop and produce those reserves. Future net revenues are calculated using prices in effect at the Company's year-end without escalation or discounting. The net carrying value of all cost centers, less accumulated provisions for future site restoration costs and deferred income taxes, is further limited to the total estimated recoverable amount of all cost centers, less future general and administrative costs, financing costs and income taxes. The oil prices used in performing the ceiling test as of 31 December 2003 were $25 and $25 (2002: $22 and $29) for Peru and Colombia, respectively. The prices used for benchmark are Forties, Oman and Suez Blend, and WTI for Peru and Columbia, respectively.

2. Summary of Significant Accounting Policies (Continued)

(c) Oil and gas operations (Continued)

(iv) Site restoration – Future estimated site restoration costs for property, plant and equipment, net of expected recoveries, are accrued and charged against income over the life of the estimated proved crude oil and natural gas reserves using the unit of production method. Site restoration expenditures incurred are charged to the accumulated provision for future site restoration.

(d) Inventory

Crude oil inventory is valued at the lower of either its cost or net realizable value.

(e) Revenue recognition

Oil and gas revenue is recognized when deliveries are made at a sales transfer point.

(f) Foreign currency translation

The Company regards the United States dollar as its functional currency and substantially all transactions are conducted in United States dollars. Monetary assets and liabilities denominated in currencies other than the Unites States dollar have been translated into United States dollars at the applicable exchange rates at the balance sheet date and non-monetary items are translated at historic rates. Foreign currency transaction and income and expense items have been translated at the average exchange rates for the year except for depreciation and depletion, which are translated at historic rates. Gains and losses arising from translation are taken directly to the income statement (interest and bank charges), except for those relating to monetary items having a fixed or ascertainable life extending beyond one year, which are deferred and amortized over the remaining life of the monetary items.

(g) Taxes

The subsidiaries located in Peru and Colombia make full provision for corporate taxes deferred as the result of claiming depreciation, exploration, development and other costs for corporate tax purposes, which differ from the related amounts charged to earnings. The Company is incorporated in the Cayman Islands and MABI is domiciled in The Bahamas. Both countries are no tax jurisdictions and accordingly there is no liability in respect of income tax, corporate tax or capital gains tax.

(h) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with banks, including amounts restricted to satisfy work commitments and guarantees (see note 12).

3. Taxation

The Company through its subsidiaries in Peru and Colombia has accumulated taxation losses as of 31 December 2003 in the amounts of $6,731,885 and $4,749,984, respectively. These taxation losses are available for offset against any future profits of the respective subsidiary within four or five years of the year in which the loss was incurred. There are no accumulated taxation losses available for offset against future profits with respect to Rio Bravo, PAIPC and MSEA. There are deferred taxes assets within the Peruvian subsidiaries as of 31 December 2003 (see note 8).

4. Cash

Cash balances as of 31 December comprise:

	2003 $	2002 $
Unrestricted funds	3,685,328	1,443,998
Restricted funds	150,000	150,000
	3,835,328	**1,593,998**

Restricted Funds in 2003 and 2002 represent cash to secure bank performance bonds related to projects in Peru and Colombia or guarantees and commitments as defined at note 12.

5. Property, Plant and Equipment, Net

Property, plant and equipment, net comprise:

	2003 $	2002 $
Cost	95,666,906	94,796,732
Accumulated depletion, depreciation and amortization	(52,791,004)	(47,896,283)
	42,875,902	**46,900,449**

The cost balances above include oil and gas assets for Peru of $47,039,319 (2002: $46,936,501) and Colombia of $46,936,501 (2002: $46,972,116). The figure for Peru represents cost of acquisition of Blocks III and IV, beginning in 1994 and capital expenditures. The figure for Colombia represents historical investment by American International Petroleum Corporation of Colombia, acquired by the Company in February 1997, plus additions by MCOG since that date.

6. Deferred Charges

In 2002, $301,024 was fully written-off, due to the uncertainty of the project to which they related. The amounts related to the Gas Generating Project in Peru.

7. Debentures

Subsidiary company debentures were repaid in full during the year.

8. Deferred Tax

The deferred tax is recorded under the liability method, on the basis of the temporary differences between the assets and liabilities for tax purposes and those for financial purposes, by applying the tax rate currently in force.

	2003 $	2002 $
Balance as at 1 January	5,055,788	5,066,935
Transfer to Statement of Operations	(1,949,806)	(11,147)
Balance as at 31 December	**3,105,982**	**5,055,788**

During the year, Peru has recognised the tax benefit of $450,032 of the tax, losses used in the year 2003. In addition, based on the projection of its future results, Peru has recognised the tax benefit of the tax loss carry-forward for $1,350,097 which it estimates will be utilized with taxable income to be obtained until 2006.

9. Share Capital

The authorized capital of the Company is 250,000,000 (2002: 250,000,000) shares at a par value of Cdn$1.00 (2002: Cdn$1.00) each.

As of 31 December 2001 the Company had 42,521,442 issued and outstanding common shares with share capital and contributed surplus totaling $45,190,867.

Restructuring

On 28 June 2002, the Company restructured its US$ 40,000,000 11.5% senior unsecured debentures due 11 May 2002. The restructuring was done under a Plan of Arrangement under the Companies Law of the Cayman Islands, which was implemented effective as of 28 June 2002. Under the Plan, the Company's outstanding common shares were consolidated on a 10 for 1 basis into 4,252,144 consolidated common shares; 33,631,000 consolidated common shares and 43,604,000 new B Warrants of the Company were issued to the debenture holders in full satisfaction of all principal and accrued interest owing on the debentures; the Company's existing 12,000,000 warrants, expiring 11 May 2002, were exchanged for 1,200,000 new A warrants; 710,000 new A warrants were issued to the shareholders of the Company; and 773,000 consolidated common shares and 1,285,000 new B Warrants were issued to the Company's non-executive chairman, Jeffrey Waterous, (2% of total shares), to settle amounts owing to him for past services and to purchase his 4% working interest in Block III Talara, Peru.

9. Share Capital (Continued)

All consolidated common shares and A Warrants issued under the Plan are held in escrow for up to 24 months after listing of the consolidated common shares on a recognized stock exchange (or such longer period, if any, imposed by the applicable exchange). The A Warrants entitle holders to purchase consolidated common shares at a price of US$1.20 per share and expire five (5) years after their first exercise date, which is the earlier of i) the second anniversary of the implementation of the Plan; and ii) the Company's common shares first trading at $2.40 per share or more for at least twenty (20) out of thirty (30) consecutive trading days. The B Warrants entitle holders to purchase consolidated common shares at a price of US$2.40 per share and expire three (3) years after the shares are first listed for trading on a recognized stock exchange, provided that after listing, the shares trade at $2.40 per share or more for at least twenty (20) out of thirty (30) consecutive trading days, and only one-third of the warrants may be exercised in each of such three years.

As part of the restructuring, a new stock option plan was approved, pursuant to which 10% of the fully diluted pro forma shares of the Company, representing up to 4,500,000 common shares (post restructuring) and 4,985,000 B Warrants were set aside for issuance to officers, directors and senior employees of the Company and its subsidiaries.

Following the restructuring, the issued and outstanding common shares are as follows:

	Number of common shares	Share Capital $	Contributed Surplus $
After consolidation on 10 to 1 basis	4,252,144	2,797,463	42,393,404
Shares issued to debenture holders in settlement of outstanding principal and interest	33,631,000	22,125,658	36,018,785
Shares issued to Non-Executive Chairman	773,000	508,553	816,137
	38,656,144	**25,431,674**	**79,228,326**
Transfer of retained deficit as of 30 June 2003 to contributed surplus approved by directors meeting on 1 July 2003	-	-	(63,731,212)
As of 31 December 2003	**38,656,144**	**25,431,674**	**15,497,114**

9. Share Capital (Continued)

The Articles of the Company prescribe a par value per share. Shares to the founders were issued at par and then reduced to reflect the actual cash value contributed.

Following the restructuring, the following options and warrants are outstanding as of 31 December 2003:

Date of grant	Number of common shares issued on exercise of options and warrants	Exercise price
28 June 2002	1,910,000 A Warrants	1.20
28 June 2002	44,889,000 B Warrants	2.40

Basic loss per share is calculated using the weighted average method. Fully diluted loss per share is not calculated as the effect of potential conversions of warrants and options in existence as of 31 December 2003 and 2002 would be anti-dilutive in nature.

10. Recoverable charges

These amounts relate to the portion of cost overruns incurred in oil wells in Colombia that are to be borne by Empresa Colombiana de Petroleos (Ecopetrol).). These amounts are to be reimbursed during 2004.

11. Financial Instruments and Risk Management

The fair value of cash, investments, accounts receivable and all current liabilities approximate their carrying value due to the relatively short term nature of these instruments. The maximum credit risk exposure of all financial assets is therefore limited to the carrying value of those assets. A substantial portion of the Company's accounts receivable are with Ecopetrol.

The Company's activities expose it to a variety of financial risks. The Company's risk management program tries to minimize the potential adverse effects on its financial performance.

i) Foreign exchange risk - The Company operates mainly in United States dollars and for this reason it is not exposed to foreign exchange risk.

ii) Interest rate risk - Income and operational cash flows of the Company are independent of changes in market interest rates. The Company has no significant assets and liabilities that bear interest.

iii) Credit risk - The majority of all crude oil is sold to government agencies in Colombia and Peru, with the remaining oil being sold on terms of less than 30 days to independent distributors.

iv) Liquidity risk - Prudent liquidity risk management implies maintaining sufficient cash and the available funds to meet current obligations.

12. Guarantees and Commitments

In June 2001 MPOG, Rio Bravo and PAIPC operators and owners of a Peruvian license interest in Block III and Block IV, signed a modified license agreement which Perupetro, the Peru licensing authority, agreed to reduce the oil royalty applicable to a portion of the oil production being produced from the respective blocks.

In the case of MPOG (Block III) the Company has committed to a work program over a period of two years within the calendar years of 2002 and 2003, consisting of well rehabilitation, work-over and drilling at an estimated cost of $4,300,000 in exchange for a reduced oil royalty on the resulting incremental production volumes sold over an agreed base production profile during the license life ending in July 2013. Oil royalty will range from 15% to 27% depending on oil price. The agreement is supported by financial guarantees provided by the Company to ensure completion by June 2003. Work was completed in 2003 except for the drilling of an exploration well.

In the case of Rio Bravo and PAIPC (Block IV) the companies have committed to a work program over a period of two years within the calendar years 2002 and 2003 consisting of well rehabilitation, work-over, drilling and seismic acquisition at an estimated cost of $3,800,000 in exchange for a reduced oil royalty on the resulting incremental production volumes sold over an agreed base production profile during the license life ending March 2013. Oil royalty will range from 15% to 27% depending on oil price. The agreement is supported by financial guarantees provided by the Company to ensure completion by June 2003. Work was completed in 2003 except for the drilling of an exploration well.

13. Contingencies

Certain employees following their dismissal from the group companies retained legal counsel and asserted claims for constructive dismissal and other employment benefits totaling approximately $190,000. The Company's legal counsel is of the view that these claims are without merit and so the Company has not provided for any liability.

14. Related Party Transactions

Under the restructuring described in Note 9, 773,000 consolidated common shares and 1,285,000 B Warrants were issued by the Company on June 28, 2002 to its non-executive Chairman, Jeffrey Waterous, to settle all amounts owing to him for past services under his retainer agreements and to purchase his 4% working interest in Block III Talara, Peru. The number and value of shares issued was based on the net asset of the Company after the restructuring. In addition Mr. Waterous consented to the cancellation of options held by him to purchase 1,828,570 common shares of the Company (pre-consolidation), which were to expire in 2005 and 2007.

15. Provision for Adverse Legal Judgment

During the year 2000 an Arbitration Tribunal under the regulations of the Colombian Chamber of Commerce rendered a judgement in the Arbitration procedure set up by Carbones y Petroleos Colombianos S.A. (Carbopetrol) vs. MCOG. Carbopetrol was seeking termination of an Overriding Royalty contract, which was executed on 22 August 1996 by means of Public Deed No. 2355. The judgement awarded Carbopetrol direct and indirect damages of $1,578,642.

MCOG had filed a Nullity Recourse action against the judgement before the Tribunal of Judicial District of Bogotá (Colombia). In November 2001 the Judicial Tribunal rendered a further adverse judgement against MCOG and as a result the final award to Carbopetrol amounted to $2,000,000. A settlement was reached with Carbopetrol paying $1,200,000 in December 2001 and the remaining $800,000 to be paid in 24 monthly payments. Interest on the outstanding balance accrues at 10% per year and is payable monthly. This balance was repaid in full in 2003.

Mercantile International Petroleum Inc.

CORPORATE PROFILE

Mercantile International Petroleum Inc. is an oil and gas company engaged in the exploration and exploitation of existing oil fields in Latin America.

The Company was incorporated in November 1994 and is registered in the Cayman Islands.

The Company has a staff of approximately 74 personnel, including 18 in Colombia, 55 in Peru, and 2 at the corporate level.

Mercantile International Petroleum Inc.

CORPORATE INFORMATION
(As of May 1st, 2003)

DIRECTORS

Jeffrey M.Waterous
Non-Executive Chairman

Rudolph Berends
Chief Executive Officer

Roger Nelson
Secretary

AUDITORS

PricewaterhouseCoopers
Providence House
Nassau, Bahamas

LEGAL COUNSEL

Nelson & Co
Georgetown, Grand Cayman

TRANSFER AGENT

CIBC Mellon Trust Company
200 Queens Quay East, Unit 6
Toronto, Ontario M5A 4K9
Canada

OFFICERS

Rudolph Berends
Chief Executive Officer

Kevin P. McCoy, P.E.
VP International Operations

Colombia
Rudolph Berends
Acting General Manager

Jose Francisco Chalela
Chairman

Peru
Pedro Timana
General Manager

Jose Ludowieg Echecopar
Chairman

Mercantile International Petroleum Inc.

ABBREVIATIONS

bbls	barrels
Bcf	billion cubic feet
Bcfe	billion cubic feet equivalent
Boe	barrel of oil equivalent
Btu	British thermal unit
GJ	gigajoule
km	kilometer(s)
kW	kilowatt
kWh	kilowatt hour
m	meter(s)
Mbbls	thousand barrels
Mcf	thousand cubic feet
Mcfe	thousand cubic feet equivalent
Mstb	thousand barrels of stock tank oil
MM	million
MMbbls	million barrels
MMboe	million barrels of oil equivalent
MMBtu	million British thermal units
MMcf	million cubic feet
MMcfe	million cubic feet equivalent
MMstb	million barrels of stock tank oil
NGLs	natural gas liquids

InterOil Exploration and Production ASA

Strandveien 50

1366 Lysaker

Norway

Tel: +47 67 51 86 50

Fax: +47 67 51 86 60

www.interoil.no

Pareto Securities ASA

Pareto Securities ASA

Dronning Maudsgate 3

P.O. Box 1411 Vika

0105 Oslo

Norway

Tel: +47 22 87 87 00

Fax: +47 22 87 87 10

www.pareto.no

www.kursiv.no