Kerr-McGee Resources (U.K.) Limited

Annual report and financial statements
for the year ended 31 December 2001

Registered number: 3295116

Directors' report

For the year ended 31 December 2001

The directors present their annual report on the affairs of Kerr-McGee Resources (U.K.) Limited ("the Company"), for the year ended 31 December 2001, together with the financial statements and auditors' report thereon.

Principal activity and review of the business

The Company is engaged in petroleum exploration, development and production activities in the United Kingdom sector of the continental shelf.

The Company's principal areas of operation are:

Andrew field (KM 6.6%) block 16/27a: Gross average daily production was 42,600 barrels of oil and 41 million cubic feet of gas in 2001.

Wytch Farm area (KM 7.4%) blocks 98/6a and 98/7a: Gross daily production averaged 60,600 barrels of oil in 2001.

Results and dividends

The Company reported a loss after taxation for the year of $4,856,000 (2000 - $40,697,000 profit). The profit and loss account had a deficit balance of $1,077,000 at 31 December 2001 (2000 - $3,779,000 surplus). The directors do not propose a dividend.

Directors and their interests

The following have served as directors of the Company during the year:

K.W. Crouch	
F. Sharratt	
J.M. Rauh	
L.R. Corbett	
A.T. Curran	
C.L. Koontz	(Appointed 23 July 2002)
C.A. Meloy	(Appointed 28 May 2002)
P. Oldham	(Resigned 28 May 2002)
D.R. Phillips	(Resigned 28 May 2002)
D.M. Shaffer	(Resigned 29 March 2002)

No directors had any beneficial interest in the shares of the Company during the year or in the prior year.

Directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

Auditors

Arthur Andersen will not be reappointed as auditors for the ensuing year. The directors will place a resolution before the annual general meeting to appoint Ernst & Young as auditors.

55 Grosvenor Street
London
W1K 3HY

By order of the Board,

Craig L. Koontz

Craig L. Koontz
Director

July 31, 2002

Independent auditors' report

To the Shareholder of Kerr-McGee Resources (U.K.) Limited:

We have audited the financial statements of Kerr-McGee Resources (U.K.) Limited for the year ended 31 December 2001 which comprise the Profit and loss account, Balance sheet and the related notes numbered 1 to 17. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards are set out in the Statement of directors' responsibilities. Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

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

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company as at 31 December 2001 and of the Company's loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Arthur Andersen

Arthur Andersen
Chartered Accountants and Registered Auditors

180 Strand
London
WC2R 1BL

July 31, 2002

Profit and loss account

For the year ended 31 December 2001

	Notes	2001 $'000	2000 $'000
Turnover	2	93,103	141,000
Cost of sales			
Operating expenses		(17,726)	(19,956)
Depreciation, depletion and amortisation	7	(26,716)	(25,725)
Asset impairment	7	(24,270)	-
Royalty expense		(4,540)	(5,962)
		(73,252)	(51,643)
Gross profit		19,851	89,357
Exploration expenses		(949)	(1,581)
Other operating income and expenses, net		(3,559)	9,575
Loss on foreign currency exchange		(13,915)	(25,471)
Operating profit		1,428	71,880
Profit on sale of fixed assets		5,778	-
Interest receivable		17	-
Interest payable and similar charges	4	(1,156)	(1,013)
Profit on ordinary activities before taxation	3	6,067	70,867
Tax provision on profit on ordinary activities	5	(10,923)	(30,170)
(Loss) profit on ordinary activities for the year	14	(4,856)	40,697

There are no recognised gains or losses in either year other than the (loss)/profit for that year.

The accompanying notes are an integral part of these statements.

Balance sheet

As at 31 December 2001

	Notes	2001 $'000	2000 $'000
Fixed assets			
Intangible assets	7	6,920	9,430
Tangible assets	7	97,929	133,071
Investments in subsidiary undertakings	6	162	162
Loans to subsidiary undertakings		398	398
		105,409	143,061
Current assets			
Stock	8	950	985
Debtors	9	300,058	313,380
Cash at bank and in hand		-	320
		301,008	314,685
Creditors: Amounts falling due within one year	10	(6,911)	(28,003)
Net current assets		294,097	286,682
Total assets less current liabilities		399,506	429,743
Creditors: Amounts falling due after more than one year	11	(7)	(8)
Provisions for liabilities and charges	12	(7,323)	(32,703)
Net assets		392,176	397,032
Total equity shareholder's funds			
Called-up equity share capital	13	395,418	395,418
Translation reserve	14	(2,165)	(2,165)
Profit and loss account	14	(1,077)	3,779
	15	392,176	397,032

Approved by the Board on July 31, 2002 and signed on its behalf by:

Craig L. Koontz

Craig L Koontz
Director

The accompanying notes are an integral part of this balance sheet.

1 Accounting policies

A summary of the principal accounting policies, all of which have been applied consistently throughout the year and the preceding year, is set out below.

The financial statements are prepared under the historical cost convention and are in accordance with applicable accounting and reporting standards.

a) Turnover

Turnover includes crude oil, natural gas and natural gas liquids revenues on the basis of the Company's entitlement to deliveries of natural gas and production of crude oil and natural gas liquids, and is before deduction of royalties. Liftings in excess of entitlement are classified as deferred revenues. Where entitlement exceeds liftings the excess is classified as receivables.

b) Fixed assets

The Company follows the policy of capitalising costs associated with the acquisition of non-producing licences and costs associated with successful wells. Licence costs are initially capitalised as intangible fixed assets pending evaluation.

Acquisition costs of undeveloped licences are amortised over the estimated holding period of the licences.

Costs of exploration and appraisal drilling relating to properties are initially capitalised as intangible fixed assets, pending evaluation. Where proved reserves are determined, the associated costs are transferred from intangible to tangible fixed assets. Subsequent field development costs, including developmental dry holes, are classified as tangible fixed assets. Where discoveries are deemed uncommercial, the associated capitalised costs are charged to exploration expense. Costs capitalised in respect of individual unsuccessful exploration wells are charged to exploration expense as they are shown to be dry. Geological and geophysical costs are charged directly to exploration expense as they are incurred.

Maintenance and repairs are expensed as incurred, except that costs of replacements or renewals which improve or extend the lives of existing properties are capitalised.

The recoverability of capitalised costs, including estimates of future capital expenditures to the extent that they can be foreseen, is examined on a field-by-field basis in relation to future production from current economically viable reserves, which are defined as proved and probable reserves, and provisions are made for impairment if the carrying value exceeds the discounted cash flows. Prior years' impairment losses are reversed when there is an indication that the impairment loss recognised no longer exists or has decreased. The reversal is recorded in the profit and loss account.

c) Depreciation, depletion and amortisation

The Company amortises its investment in producing properties on a field-by-field basis using a physical unit-of-production method based upon the relationship of the current year's production to the estimated remaining proved reserves. Other property and equipment is depreciated over its estimated life using the straight-line method.

1 Accounting policies (continued)

d) Decommissioning provision

In accordance with the provisions of Financial Reporting Standard ("FRS") 12, the Company provides a reserve for the present value of this estimated cost at present-day prices of dismantling and removing oil and gas production and related facilities. An asset is recognised as the offset to this discounted provision and is depreciated by the unit-of-production method.

e) Effect of changing estimates

The effect of changes in estimated costs or other factors affecting unit-of-production calculations for depreciation are dealt with prospectively over the estimated remaining reserves.

f) Foreign currency

The Company's functional reporting currency is the U.S. Dollar. Transactions denominated in other currencies are converted to dollars and recorded using the rate of exchange at the end of the previous month. Amounts due from or to other parties denominated in other currencies are translated at the rates of exchange in effect at the balance sheet date. Translation gains and losses are reflected in the profit and loss account.

The year end exchange rate used was $1.4378 to £1 GBP (2000: $1.4935 to £1 GBP). The average transaction rate during the year was $1.4434 to £1 GBP (2000: $1.5215 to £1 GBP).

g) Investments in subsidiary undertakings

Investments are shown at cost, less provision for impairment.

h) Corporation tax

UK corporation tax is provided at amounts expected to be paid using the anticipated tax rates.

Deferred tax is provided using the liability method on all timing differences and arises principally as a result of tax allowances for deferred exploration and development costs exceeding the depreciation, depletion and amortisation provided in the accounts.

The future tax benefit of unutilised losses is recognised to the extent that there is a credit balance in the deferred taxation account.

1 Accounting policies (continued)

i) Petroleum revenue tax (PRT)

The total PRT charge for the year is computed on the life-of-field basis whereby the total PRT expense estimated to arise over the life of each field is expensed on a unit-of-sales method. The benefit of allowances for non-field expenditure is recognised as such expenditure is incurred up to the level of PRT otherwise arising. Any difference between the life-of-field PRT expense and the current PRT charge for the period is recorded as deferred PRT.

j) Royalties

Under the terms of certain of its production licences, the Company is obliged to pay royalties to the United Kingdom government at specified rates of the value of oil and gas won and saved during the year less certain allowances. Royalties are accounted for in the period for which they are payable.

k) Interest in joint ventures

The Company's interests in upstream oil and gas joint ventures are accounted for as joint arrangements that are not entities under FRS 9 such that the Company accounts directly for its share of transactions conducted through these joint arrangements.

l) Cash flow statement

Under the provisions of FRS 1 (revised) the Company has not prepared a cash flow statement because it is a wholly owned subsidiary of a parent undertaking whose consolidated financial statements, which include the accounts of the Company, are publicly available.

m) Group accounts

The Company is not required to prepare group accounts as its parent company, Kerr-McGee (G.B.) PLC, consolidates the accounts of this Company and its subsidiary.

2 Turnover

All turnover and operating profit originated from sales of hydrocarbons and all sales were within the United Kingdom and Europe. All of the Company's operations take place, and all of its oil and gas assets are held in the United Kingdom and in one business segment, the production and sale of hydrocarbons.

3 Profit on ordinary activities before taxation

Auditors' remuneration was borne by Kerr-McGee North Sea (U.K.) Limited, a subsidiary of parent company, Kerr-McGee (G.B.) PLC.

The Company had no employees in 2001 and 2000. Staff costs are borne by Kerr-McGee North Sea (U.K.) Limited.

The only directors that receive remuneration for their services are those that are also directors of the parent company, Kerr-McGee (G.B.) PLC. The emoluments of these directors are disclosed therein.

4 Interest payable and similar charges

	2001 $'000	2000 $'000
Bank loans and overdrafts	-	174
Amortisation of discount on Euro-commercial paper	49	49
Unwinding of discount on decommissioning provisions	940	790
Other interest payable	167	-
	1,156	1,013

5 Tax provision on profit on ordinary activities

	2001 $'000	2000 $'000
Corporation tax at 30%		
- current	3,938	12,770
- deferred	2,480	12,133
Additional deferred corporation tax due to increase in tax rate (note 12)	968	-
Deferred corporation tax on impairment	(6,629)	-
Petroleum revenue tax at 50%		
- current	10,755	23,362
- deferred	3,277	(10,880)
Foreign exchange gain on deferred tax liability	(3,866)	(7,215)
	10,923	30,170

The charges for deferred corporation tax and deferred petroleum revenue tax above exclude foreign exchange gains and losses in the year on the related balance sheet amounts. The foreign exchange gain presented separately above represents a gain of $3,723,000 (2000 - $7,572,000 gain) on the deferred corporation tax provision and a gain of $143,000 (2000 - $357,000 loss) on the deferred petroleum revenue tax provision.

6 Investments in subsidiary undertakings

The Company holds all of the issued share capital of Kerr-McGee York Limited, a subsidiary undertaking registered in England and Wales and engaged in exploration and production of oil and gas.

7 Fixed assets

	Beginning of year $'000	Additions $'000	Disposals $'000	Dry hole $'000	Depreciation, depletion and amortisation charge $'000	End of year $'000
Cost						
Intangible assets (unevaluated)						
- licences	10,057	-	(2,713)	-	-	7,344
- exploratory and appraisal drilling	2,157	27	-	160	-	2,344
	12,214	27	(2,713)	160	-	9,688
Tangible assets (evaluated)						
- production facilities	246,891	12,386	-	-	-	259,277
- decommissioning asset	10,890	1,450	-	-	-	12,340
	257,781	13,836	-	-	-	271,617
Accumulated depreciation, depletion and amortisation						
Intangible assets						
- licences	(2,784)	-	2,024	-	(2,008)	(2,768)
Tangible assets						
- production facilities	(120,310)	-	-	-	(47,538) [1]	(167,848)
- decommissioning asset	(4,400)	-	-	-	(1,440)	(5,840)
	(124,710)	-	-	-	(48,978)	(173,688)
Net book value						
Intangible assets	9,430	27	(689)	160	(2,008)	6,920
Tangible assets	133,071	13,836	-	-	(48,978)	97,929
	142,501	13,863	(689)	160	(50,986)	104,849

(1) Amount includes asset impairments of $24,270,000.

7 Fixed assets (continued)

The cost of tangible fixed assets includes cumulative interest capitalised of $1,024,000 (2000 - $1,024,000). Associated accumulated depreciation is $388,000 (2000 - $318,000).

Total pre-production costs incurred during the period were $13,522,000 (2000 - $8,429,000). This includes $1,109,000 of exploration and appraisal costs immediately charged to expense (2000 - $675,000).

8 Stocks

Stocks held at 31 December 2001 and 2000 relate entirely to materials and supplies.

9 Debtors

	2001 $'000	2000 $'000
Trade debtors	4,729	10,948
Amounts owed by other group undertakings	293,616	285,409
Corporation tax recoverable	502	-
VAT	124	1,109
Prepayments and deferred charges	1,087	15,914
	300,058	313,380

During the year the UK Group's procedures for invoicing joint venture expenditures were changed such that all amounts are invoiced, received and then internally reallocated, by Kerr-McGee (G.B.) PLC. Debtors at 31 December 2001 reflect these arrangements.

10 Creditors: amounts falling due within one year

	2001 $'000	2000 $'000
Trade creditors	207	6,292
Royalties payable	2,168	3,084
Amounts owed to other group undertakings	382	731
Corporation tax payable	-	11,647
Petroleum revenue tax payable	2,763	3,747
Accruals and deferred income	1,391	2,502
	6,911	28,003

The 2000 trade creditor balance above includes accruals of $1,001,000. In 2001 accruals are separately disclosed.

10 Creditors: amounts falling due within one year (continued)

During the year the UK Group's procedures for processing and payment of all invoiced expenditures were changed such that all amounts are processed, paid and then internally reallocated, through Kerr-McGee North Sea (U.K.) Limited. Creditors at 31 December 2001 reflect these arrangements.

11 Creditors: amounts falling due after more than one year

	2001 $'000	2000 $'000
Deferred income	7	8

The deferred income represents amounts received relating to customers take-or-pay obligations under long-term contracts for the supply of natural gas by the Company.

12 Provisions for liabilities and charges

	2001 $'000	2000 $'000
Decommissioning costs	14,480	12,090
Deferred corporation tax	(2,756)	28,148
Deferred petroleum revenue tax	(4,401)	(7,535)
	7,323	32,703

	Deferred corporation tax $'000	Deferred PRT $'000	Decommissioning costs $'000	Total $'000
At 1 January 2001	28,148	(7,535)	12,090	32,703
Increase in provision in year	-	-	1,450	1,450
Unwinding of discount	-	-	940	940
(Release) charge to the profit and loss account	(6,904)	3,134	-	(3,770)
Transfers	(24,000)	-	-	(24,000)
At 31 December 2001	(2,756)	(4,401)	14,480	7,323

The Company's share of the net present value of the total costs of decommissioning related to the fields in which it held an interest at 31 December 2001 is estimated at $14,480,000 at current prices inflated at 2%. This has been discounted at 6%. It has also been assumed that all site restoration costs will be fully allowable for tax purposes.

12 Provisions for liabilities and charges (continued)

Deferred corporation tax is attributable to:

	2001 $'000	2000 $'000
Excess of tax allowances over book depreciation of fixed assets	(1,325)	27,568
Provision for site restoration	(5,792)	(3,628)
Deferred petroleum revenue tax	1,761	2,261
Decommissioning asset	2,600	1,947
	(2,756)	28,148

During 2000 a Licence was transferred from the Company to Kerr-McGee Oil (U.K.) PLC, a subsidiary of parent company Kerr-McGee (G.B.) PLC. The deferred corporation tax transfer represents the deferred corporation tax on this Licence.

In April 2002, as part of the Budget announcements for the 2002/03 fiscal year, the Chancellor of the Exchequer proposed to increase tax on North Sea Oil profits from 30% to 40%. The impact of this change on deferred taxation has been reflected in the balances as at 31 December 2001.

13 Called-up equity share capital

	2001 $'000	2000 $'000
Authorised:		
395,000,000 ordinary shares of £1 each	656,451	656,451
100,000,000 cumulative redeemable preference shares of £1 each	166,190	166,190
	822,641	822,641
Allotted, called-up and fully paid:		
239,508,383 (2000 – 239,508,383) ordinary shares of £1 each	395,418	395,418

14 Reserves

	Translation Reserve $'000	Profit and Loss account $'000
Balance at 31 December 2000	(2,165)	3,779
Retained loss for year	-	(4,856)
Balance at 31 December 2001	(2,165)	(1,077)

15 Reconciliation of movements in total equity shareholder's funds

	2001 $'000	2000 $'000
(Loss) profit for the financial year	(4,856)	40,697
Opening equity shareholder's funds	397,032	356,335
Closing equity shareholder's funds	392,176	397,032

16 Capital commitments

Authorised future capital expenditures are estimated at $5,176,000 (2000 - $6,876,000).

17 Ultimate parent company

The Company is a wholly owned subsidiary undertaking of Kerr-McGee (G.B.) PLC. The smallest group for which consolidated accounts are prepared and the Company is a member, is that headed by Kerr-McGee (G.B.) PLC.

Kerr-McGee (G.B.) PLC's ultimate parent company is Kerr-McGee Corporation. The consolidated accounts of Kerr-McGee Corporation are available to the public and may be obtained from Kerr-McGee Corporation at Kerr-McGee Center, Oklahoma City, Oklahoma 73125, USA.

As a wholly owned subsidiary undertaking of Kerr-McGee Corporation, the Company has taken advantage of the exemption in FRS 8, "Related party disclosures," from disclosing transactions with other members of the group headed by Kerr-McGee Corporation.

Supplementary information – 31 December 2001 (unaudited)

Net proved oil and gas reserves quantities

Oil and gas reserves

The Company's share of proved oil (millions of barrels) and gas (billions of cubic feet) reserves is shown below:

	2001		2000	
	Oil	Gas	Oil	Gas
Proved reserves, beginning of year				
- developed	19.4	15.2	22.7	16.9
- undeveloped	2.5	1.2	18.4	3.5
	21.9	16.4	41.1	20.4
Changes during the year				
- transfers to subsidiary undertakings	-	-	(15.0)	(2.5)
- extensions, discoveries and other additions	0.1	-	-	-
- revisions	0.2	0.7	0.7	-
- production	(3.5)	(1.5)	(4.9)	(1.5)
	(3.2)	(0.8)	(19.2)	(4.0)
Proved reserves, end of year				
- developed	17.0	14.9	19.4	15.2
- undeveloped	1.7	0.7	2.5	1.2
	18.7	15.6	21.9	16.4
Equivalent barrels of oil (6 thousand cubic feet equals 1 barrel):	21.3		24.6	

The estimates of proved reserves have been prepared by the Company's geologists and engineers. Such estimates include reserves on certain properties that are partially undeveloped and reserves that will be obtained in the future by secondary recovery operations now in operation or for which successful testing has been demonstrated.