

LAKES OIL N.L.

A.B.N. 62 004 247 214

AND CONTROLLED ENTITIES

**FINANCIAL REPORT
FOR THE HALF-YEAR ENDED
31 DECEMBER 2005**

This half-year financial report is to be read in conjunction with the financial report for the year ended 30 June 2005

**LAKES OIL N.L. AND CONTROLLED ENTITIES
FINANCIAL REPORT FOR THE HALF-YEAR ENDED
31 DECEMBER 2005**

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LAKES OIL N.L. AND CONTROLLED ENTITIES DIRECTORS' REPORT

The Directors present their report together with the condensed financial report of the consolidated entity consisting of Lakes Oil N.L. and the entities it controlled, for the half-year ended 31 December 2005 and independent review report thereon. This financial report has been prepared in accordance with Australian Equivalents of International Financial Reporting Standards.

DIRECTORS NAMES

The directors in office since the start of the financial period to the date of this report are:-

Robert J. Annells
Peter C. Dunn
Peter B. Lawrence

REVIEW OF OPERATIONS

The consolidated loss of the group for the half-year after providing for income tax was \$1,653,142.

During the half year, vigorous drilling programs occurred in several permits in both onshore and offshore locations, which included drilling of wells in:

- PEP 157 onshore Gippsland Basin
- PEP 155 (Marlo Block) onshore Gippsland Basin
- PEP 163 onshore Otway Basin and
- VIC/P47 (Gilbert Block) offshore Gippsland Basin

Onshore Gippsland Basin

□ PEP 155 Western Block – Onshore, Victoria (Lakes Oil Group, Operator: 100% interest)

A review of new centrifuge technology for the separation of water from oil continued in relation to the Hunters Lane well, in the Lakes Entrance Oil Field.

□ PEP 155 Marlo Block (Eastern portion) – Onshore, Victoria (Lakes Oil Group, Operator: 46% interest)

Drilling activity in the Eastern Block of PEP 155 included a shallow stratigraphic well, Patrobus-1, drilled in the Marlo area to test for the possibility of up-dip migration of hydrocarbons from offshore Gippsland fields. No visible signs of hydrocarbons were encountered during drilling. Post-drilling analysis of Patrobus core data indicated that residual hydrocarbons were present in very small amounts in potential reservoir rocks that were intersected.

In early January 2005, a second shallow well, Banjo-1A was spudded some 5 kilometres to the west of Patrobus-1. The well reached a total depth of 282 metres after intersecting Palaeozoic basement. No visible signs of hydrocarbons were encountered. Post-drilling analysis is continuing for the two stratigraphic holes.

□ PEP 156 – Onshore, Victoria (Lakes Oil Group, Operator: 100% interest)

Geological studies were conducted in the Bairnsdale/Lakes Entrance area and around Loch Sport. This permit expired on 16 February 2006.

LAKES OIL N.L. AND CONTROLLED ENTITIES DIRECTORS' REPORT (continued)

Onshore Gippsland Basin (continued)

- **PEP 157 – Onshore, Victoria**
(Lakes Oil Group, Operator: 100% interest of overall permit. Roma Petroleum NL has a 5% over-riding royalty)

Trifon Block (Lakes Oil Group, Operator: 50% interest; Jarden Corporation Australia Pty Ltd 50% interest)

Wombat Block (Lakes Oil Group, Operator: 92.5% interest; Private interests 7.5% interest)

The Boundary Creek – 2 well was drilled in October as a deep exploration well and reached a total depth of 2,341 metres. The well was drilled on the Longford Dome to test for tight gas sands in the Strzelecki Group. Continuous gas readings were recorded throughout the Strzelecki Group. The well was cased to about 1,100 metres and suspended for future fracture stimulation at a later date. Advanced logging and post-drilling evaluation programs will provide Lakes Oil with a fuller understanding of the nature of the tight gas reservoirs and extracted hydrocarbons encountered in this well which will also have broader application throughout the Gippsland Basin.

Ongoing field testing was conducted on Wombat – 2, Wombat – 3 Trifon – 2 and North Seaspray – 3 wells, which allowed gas flow tests to be performed and fresh gas samples to be collected and analysed.

The pre-feasibility study of the Wombat and Trifon tight gas fields commissioned by Landmark Consulting in USA continued in this period. The completion date has been extended due to staff shortage with the contractor. Results are expected to be available in the first quarter of 2006.

- **PEP 158 – Onshore, Victoria**
(Lakes Oil Group, Operator: 100% interest of overall permit. Roma Petroleum NL has a 5% over-riding royalty)

The focus was on re-mapping the western portion of the Gippsland Basin using new technologies to re-evaluate existing data that will assist in identifying new leads.

- **PEP 166 – Onshore, Victoria**
(Lakes Oil Group, 50% interest; Operator: Lakes Oil jointly with Ausam Resources Limited)

Several leads and prospects on the subsurface top of Strzelecki Group have been identified including leads at the Hazelwood and Loy Yang domes. The company is to drill Loy Yang – 2 well on the Loy Yang dome situated beneath the Loy Yang B Power Station in the first quarter of 2006. Lakes Oil intends to sole-risk this project without joint venture participation from Ausam Resources. Lakes Oil will fund the drilling and post-drilling fracture stimulation. In return, Lakes Oil will hold a 75% interest in the defined "Loy yang" Block in PEP 166 and Ausam will retain a 25% interest in the Block. In the remainder of the permit, Lakes Oil and Ausam will continue to each hold a 50% interest.

Offshore Gippsland Basin Victoria

- **VIC/P47 (Gilbert Block) – Offshore, Victoria**
(Lakes Oil Group, 26% interest; Operator: Bass Strait Oil Co)

During October 2005, Lakes Oil participated in the drilling of Gilbert – 1 well in the Gilbert Block. This well was drilled to a total depth of 810 metres using the "Ocean Patriot" semi submersible drilling rig to test the Gurand and Latrobe Formations plays and to investigate the underlying Strzelecki Group reservoirs. While elevated gas readings and strong fluorescence were encountered in several zones in the well, further evaluation still needs to be conducted to fully assess the nature of these shows.

- **VIC/P40(V) – Offshore, Victoria**
(Lakes Oil Group, Operator: 39.2% interest)

Further interpretation of the Falcon airborne gravity survey continued together with available geological and seismic data from nearby offshore areas.

LAKES OIL N.L. AND CONTROLLED ENTITIES DIRECTORS' REPORT (continued)

Onshore Otway Basin Victoria

- **PEP 163 – Onshore, Victoria**
(Lakes Oil Group, Operator: 50% interest; Jupiter Energy (Victoria) Pty Ltd 50% interest)

Bellarine – 1 well was drilled in PEP 163 during July 2005 to test an up-dip closure in the Eumeralla Formation (equivalent to the Strzelecki Group), southeast of Hindaugh Creek – 1 which was drilled in 1969 and encountered gas shows in the formation. The well reached a total depth of 2,139 metres without reaching the Pretty Hill sands secondary target. Intermittent gas readings were encountered throughout much of the Eumeralla Formation. Subsequent evaluation has indicated the presence of gas in natural fractures making Bellarine – 1 a potential candidate for future fracture stimulation.

Work has also continued in the onshore Otway Basin permits, where a number of leads have been identified from regional geological and seismic studies. Regional surface geochemical surveys were conducted in both permits in the June quarter that identified several soil gas anomalies that may warrant further investigation.

- **PEP 164 – Onshore, Victoria**
(Lakes Oil Group, Operator: 100% interest)

Work has continued in the onshore Otway Basin permits, where a number of leads have been identified from regional geological and seismic studies. Regional surface geochemical surveys were conducted in both permits in the June quarter that identified several soil gas anomalies that may warrant further investigation.

- **PEP 152 – Onshore, Victoria**
(Lakes Oil Group, 15.59% interest; Operator: Essential Petroleum Resources)

The tenure of PEP 152 in the onshore Otway Basin, Victoria expired in November 2005 and the company and its joint venture partner do not plan to re-apply for this permit.

Onshore Otway Basin South Australia

- **PEL 57 – Onshore, South Australia**
(Lakes Oil Group, Operator: 90% interest)

Regional interpretation work continued in PEL 57. Planning and preparation for regional geochemical surveys in this permit was conducted.

- **PEL 66 – Onshore, South Australia**
(Lakes Oil Group, Operator: 90% interest)

Regional interpretation work continued in PEL 62. Planning and preparation for regional geochemical surveys in this permit was conducted.

Eromanga Basin Queensland

- **ATP 560P – Mclvor Block – Onshore, Queensland**
(Lakes Oil Group, 90% interest; Operator: Victoria Petroleum N.L.)

There was no activity undertaken on this permit during the half year.

- **ATP 560P – Ueleven Block – Onshore, Queensland**
(Lakes Oil Group, 25% interest; Operator: Icon Oil N.L.)

There was no activity undertaken on this permit during the half year.

**LAKES OIL N.L. AND CONTROLLED ENTITIES
DIRECTORS' REPORT (continued)**

Onshore USA – San Joaquin Basin California

- ❑ **Eagle Prospect – Onshore, California, USA**
(Lakes Oil Group, 15% interest; Operator: Victoria Petroleum Inc.)

In California, Lakes Oil is participating in the drilling of the Eagle North – 1 well, which was spudded in January 2006. This well is an appraisal well on the Eagle Oil Pool, discovered in 1986 by the Mary Bellocchi – 1 well in which Lakes Oil also participated. The well is programmed to drill to 4,200 metres from a vertical hole and upon reaching the target oil-bearing Gatchel Sandstone, it will be horizontally drilled for 300 metres. In the event of a successful horizontal well completion, the well will be completed for oil production. If successful, estimated flow rates of up to 1,000 barrels of oil per day is anticipated.

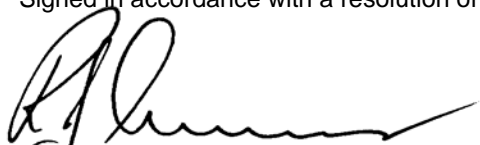
- ❑ **Kingfisher Prospect – Onshore, California, USA**
(Lakes Oil Group, 10% interest; Operator: Victoria Petroleum Inc.)

There was no activity undertaken on this permit during the half year.

AUDITORS' DECLARATION

A copy of the auditors' independence declaration in relation to the review for the half-year is provided with this report.

Signed in accordance with a resolution of the directors:


.....
Robert J. Annells

Dated this 1st day of March 2006

**AUDITOR'S INDEPENDENCE DECLARATION
To the Directors of Lakes Oil N.L.**

In relation to the independent review for the six months to 31 December 2005, to the best of my knowledge and belief there have been:

- (i) No contraventions of the auditor independence requirements of the Corporations Act 2001
- (ii) No contraventions of any applicable code of professional conduct.



PITCHER PARTNERS



M W PRINGLE
Partner

1 March 2006

**LAKES OIL N.L. AND CONTROLLED ENTITIES
CONDENSED CONSOLIDATED INCOME STATEMENT
FOR THE HALF YEAR ENDED 31 DECEMBER 2005**

	Half-year	
	2005	2004
	\$	\$
Revenue		
Other income	668,931	887,163
	<hr/>	<hr/>
Employee benefits expenses	(431,129)	(275,493)
Depreciation and amortisation expenses	(30,740)	(19,871)
Finance costs	(2,682)	(3,547)
Exploration expenditure written off	(976,098)	(89)
Accounting and audit expenses	(40,102)	(64,374)
Marketing and promotion expenses	(103,234)	(63,956)
Rent and occupancy expenses	(99,137)	(75,160)
Consulting expenses	(256,730)	(263,248)
Administrative expenses	(382,221)	(243,839)
Total expenses	<hr/> (2,322,073) <hr/>	<hr/> (1,009,577) <hr/>
(Loss) before income tax	(1,653,142)	(122,414)
Income tax expense	-	-
	<hr/>	<hr/>
(Loss) from continuing operations	(1,653,142)	(122,414)
	<hr/>	<hr/>
(Loss) for the half-year	(1,653,142)	(122,414)
(Loss) attributable to the members of the parent	(1,653,142)	(122,414)
	<hr/>	<hr/>
Basic loss per share (cents per share)	(0.12)	(0.0001)
Diluted loss per share (cents per share)	(0.12)	(0.0001)

The accompanying notes form part of these financial statements.

**LAKES OIL N.L. AND CONTROLLED ENTITIES
CONDENSED CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2005**

	31 Dec 2005 \$	30 June 2005 \$
CURRENT ASSETS		
Cash and cash equivalents	2,194,444	3,594,733
Trade receivables	886,617	818,553
Other financial assets	230,982	-
Other current assets	44,715	295,067
	<u>3,356,758</u>	<u>4,708,353</u>
Financial assets at fair value through profit or loss	2,375,471	1,570,683
TOTAL CURRENT ASSETS	<u>5,732,229</u>	<u>6,279,036</u>
NON-CURRENT ASSETS		
Property, plant and equipment	491,627	187,152
Deferred exploration, evaluation and development	31,869,453	27,747,800
TOTAL NON-CURRENT ASSETS	<u>32,361,080</u>	<u>27,934,952</u>
TOTAL ASSETS	<u>38,093,309</u>	<u>34,213,988</u>
CURRENT LIABILITIES		
Trade and other payables	2,328,305	2,071,157
Short-term provisions	69,299	40,141
TOTAL CURRENT LIABILITIES	<u>2,397,604</u>	<u>2,111,298</u>
NON-CURRENT LIABILITIES		
Long-term provisions	22,325	37,501
TOTAL NON-CURRENT LIABILITIES	<u>22,325</u>	<u>37,501</u>
TOTAL LIABILITIES	<u>2,419,929</u>	<u>2,148,799</u>
NET ASSETS	<u>35,673,380</u>	<u>32,065,189</u>
EQUITY		
Share capital	59,560,792	54,369,463
Other reserves	1,176,518	1,106,512
Accumulated losses	(25,063,930)	(23,410,786)
TOTAL EQUITY	<u>35,673,380</u>	<u>32,065,189</u>

The accompanying notes form part of these financial statements.

**LAKES OIL N.L. AND CONTROLLED ENTITIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE HALF YEAR ENDED 31 DECEMBER 2005**

	Half-year	
	2005	2004
	\$	\$
TOTAL EQUITY AT THE BEGINNING OF THE HALF-YEAR	32,065,189	25,777,224
Employee share options	70,006	28,543
Net income recognised directly in equity	70,006	28,543
(Loss) for the year	(1,653,142)	(122,414)
Total recognised income and expense for the period	(1,583,136)	(93,871)
Attributable to:		
Members of the parent	(1,583,136)	(93,871)
	(1,583,136)	(93,871)
Transactions with equity holders in their capacity as equity holders:		
Contributions	5,191,327	2,948,250
	5,191,327	2,948,250
TOTAL EQUITY AT THE END OF THE HALF-YEAR	35,673,380	28,631,603

The accompanying notes form part of these financial statements.

**LAKES OIL N.L. AND CONTROLLED ENTITIES
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE HALF YEAR ENDED 31 DECEMBER 2005**

	Half-year	
	2005	2004
	\$	\$
CASH FLOW FROM OPERATING ACTIVITIES		
Management fees received	-	290,827
Payments to suppliers and employees	(1,680,748)	(2,030,254)
Payment for exploration and evaluation cost	(4,211,994)	(4,452,665)
Interest received	80,618	57,074
Net cash used in operating activities	(5,812,124)	(6,135,018)
CASH FLOW FROM INVESTING ACTIVITIES		
Proceeds from sale of listed securities	31,423	428,636
Proceeds from matured security deposits	106,166	25,000
Payment for property, plant and equipment	(361,810)	(145,204)
Payment for bonds and deposits	(108,982)	(100,000)
Payment for purchase of listed securities	(270,000)	(785,000)
Net cash used in investing activities	(603,203)	(576,568)
CASH FLOW FROM FINANCING ACTIVITIES		
Proceeds from issues of ordinary shares	5,549,235	3,035,000
Payment of share issue costs	(341,378)	(180,412)
Net advances (to)/from non-related parties	(192,819)	-
Net cash provided by financing activities	5,015,038	2,854,588
Net (decrease) in cash and cash equivalents	(1,400,289)	(3,856,998)
Cash and cash equivalents at beginning of half-year	3,594,733	3,998,277
Cash and cash equivalents at end of the half-year	2,194,444	141,279

The accompanying notes form part of these financial statements.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005

NOTE 1: BASIS OF PREPARATION OF THE HALF-YEAR FINANCIAL REPORT

This general purpose half-year financial report has been prepared in accordance with Accounting Standard AASB 134 'Interim Financial Reporting' and the *Corporation Act 2001*.

This half-year financial report does not include all the notes of the type usually included in an annual financial report. It is recommended that this financial report be read in conjunction with the financial report for the year ended 30 June 2005 and any public announcements made by Lakes Oil N.L. during the half-year in accordance with any continuous disclosure obligations arising under the Corporations Act 2001.

(a) Basis of preparation of the half-year financial report

This is the first financial report of Lakes Oil N.L. prepared in accordance with Australian Equivalents of International Financial Reporting Standards (AIFRS). The financial reports of Lakes Oil N.L. were prepared in accordance with the previous Australian Generally Accepted Accounting Principles (AGAAP) until 30 June 2005. There are certain differences between accounting policies under AIFRS and AGAAP and where applicable the comparative figures have been restated to reflect these adjustments. A summary of the significant accounting policies under AIFRS is provided below. Reconciliations of equity and operating profit/loss between AGAAP and AIFRS are provided under notes 7 to 10.

The financial report has been prepared under the historical cost convention, as modified by revaluations to fair value for certain classes of assets as described in the accounting policies.

Summary of the significant accounting policies under AIFRS:

(b) Principles of Consolidation

The consolidated financial statements are those of the consolidated entity, comprising the financial statements of the parent entity and of all entities, which Lakes Oil N.L. controlled from time to time during the half-year and at balance date.

The financial statements of subsidiaries are prepared for the same reporting period as the parent entity, using consistently applied accounting policies. Adjustments are made to bring into line any dissimilar accounting policies, which may exist. All inter-company balances and transactions, including any unrealised profits or losses have been eliminated on consolidation.

(c) Revenue Recognition

Interest revenue is recognised on a proportional basis taking into account the interest rates applicable to the financial assets.

All revenue is stated net of the amount of goods and services tax (GST).

(d) Cash and cash equivalents

Cash and cash equivalents include cash on hand and at banks, and deposits held at call with financial institutions.

(e) Property, plant and equipment

Cost and valuation

Freehold land is measured at fair value. At each balance date the carrying value of each asset is reviewed to ensure that it does not differ materially from the asset's fair value at reporting date. Where necessary, the asset is re-valued to reflect its fair value. Changes in the carrying amounts arising on revaluation of land are credited to other reserves in shareholders' equity after bringing to account any capital gains tax that would arise on disposal of that asset.

All other classes of property, plant and equipment are measured at cost.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

(e) Property, plant and equipment (continued)

The carrying amount of plant and equipment is reviewed annually by directors to ensure it is not in excess of the recoverable amount from those assets. Refer to note 1(h).

Depreciation

Land is not depreciated. The depreciable amounts of all other fixed assets are depreciated on a diminishing value basis over their estimated useful lives commencing from the time the asset is held ready for use. Leasehold improvements are depreciated over the shorter of either the unexpired period of the lease or the estimated useful lives of the improvements.

The useful lives for each class of assets are:

	2005	2004
Plant and equipment:	7 years	7 years
Motor vehicles	5 years	5 years
Technical equipment	3 – 10 years	3 – 10 years
Computer equipment	3 years	3 years
Office equipment	8 years	8 years

(f) Leases

Leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership.

Operating Leases

Lease payments for operating leases, where substantially all of the risks and benefits remain with the lessor, are charged as expenses in the period in which they are incurred.

Finance Leases

The group has no finance leases.

(g) Exploration and evaluation costs

Costs arising from exploration activities are carried forward provided such costs are expected to be recouped through successful development or sale, or exploration activities have not reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves. AASB 6 "Exploration for and Evaluation of Mineral Resources" requires that the company perform impairment tests on those assets when facts and circumstances suggest that the carrying amount may be impaired. However, the directors believe the impairment testing has been aligned with the factors that must currently be satisfied for capitalisation of exploration and evaluation costs. Consequently, the standard provides similar outcomes for exploration and evaluation costs to the Company's present accounting policy, with no change to profit or loss from AGAAP to AIFRS.

Grants and subsidies are offset against costs as incurred.

Costs carried forward in respect of an area of interest that is abandoned are written off in the year in which the decision to abandon is made.

Amortisation

Costs on production areas are amortised over the life of the area if interest to which such costs relate on the production output basis. The entity does not currently have any production areas.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

(g) Exploration and evaluation costs (continued)

Restoration costs

Restoration costs that are expected to be incurred are provided for as part of the cost of the exploration, evaluation, development, construction or production phases that give rise to the need for restoration. Accordingly, these costs are recognised gradually over the life of the facility as these phases occur. The costs include obligations relating to reclamation, waste site closure, platform removal and other costs associated with the restoration of the site. These estimates of the restoration obligations are based on anticipated technology and legal requirements and future costs that have been discounted to their present value. Any changes in the estimates are adjusted on a retrospective basis. In determining the restoration obligations, the entity has assumed no significant changes will occur in the relevant Federal and State legislation in relation to restoration of such wells in the future.

(h) Impairment of assets

Assets with an indefinite useful life are not amortised but are tested annually for impairment in accordance with AASB 136. Assets subject to annual depreciation or amortisation are reviewed for impairment whenever events or circumstances arise that indicate that the carrying amount of the asset may be impaired. An impairment loss is recognised where the carrying amount of the asset exceeds its recoverable amount. The recoverable amount of an asset is defined as the higher of its fair value less costs to sell and value in use.

(i) Taxes

Income tax losses

Future income tax benefits arising from tax losses of the parent entity and its controlled entities are not recognised at reporting date as realisation of the benefit is not regarded as probable. The future income tax benefit will only be obtained if: (a) Future assessable income is derived of an amount sufficient to enable the benefit to be realised; (b) the conditions for deductibility imposed by tax legislation continue to be complied with; and (c) no changes in tax legislation adversely affect the consolidated entity in realising the benefit.

Tax Consolidation

The parent entity and its controlled entities have formed an income tax consolidated group under the tax consolidation legislation. The parent entity is responsible for recognising the current and deferred tax assets and liabilities for the tax consolidated group. The tax consolidated group has also entered a tax sharing agreement whereby each company in the group contributes to the income tax payable in proportion to their contribution to the net profit before tax of the tax consolidated group.

(j) Employee Benefits

Liabilities arising in respect of wages and salaries, annual leave, and any other employee benefits expected to be settled within twelve months of the reporting date are measured at their nominal amounts based on remuneration rates which are expected to be paid when the liability is settled. All other employee benefit liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to the reporting date.

Share-based payments

There is no formal share option plan. However, from time to time share options are granted to directors, employees and consultants on a discretionary basis. The bonus element over the exercise price for the grant of shares and options is recognised as an expense in the Income Statement in the period(s) when the benefit is earned.

The total amount to be expensed over the vesting period is determined by reference to the fair value of the options at grant date. Under the transitional arrangements for first-time adoption of AIFRS, no expense has been recognised for the options granted before 7 November 2002 and/or vested before 1 January 2005.

For options granted after 7 November 2002 and vesting after 1 January 2005 the fair value of options at grant date is determined using a Black-Scholes option pricing model, and is recognised as an employee expense over the period during which the employees become entitled to the option.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

(k) Financial Instruments

Classification

The group classifies its financial instruments in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and re-evaluates the designation at each reporting date.

Financial assets at fair value through profit or loss

Investments in listed securities are carried at fair value through profit and loss. They are measured at their fair value at each reporting date and any increment or decrement in fair value from the prior period is recognised in the profit and loss of the current period. Fair value of listed investments are based on current bid prices.

Held-to-Maturity Investments

Fixed term investments intended to be held to maturity are classified as held-to-maturity investments. These are measured at amortised cost using the effective interest rate method.

Loans and Receivables

Loan and receivables are measured at fair value at inception and subsequently at amortised cost using the effective interest rate method.

Financial Liabilities

Financial liabilities include trade payables, other creditors and loans from third parties including inter-company balances and loans from or other amounts due to director-related entities.

(l) Foreign Currencies

Transactions and Balances

Transactions in foreign currencies of entities within the consolidated entity are translated into functional currency at the rate of exchange ruling at the date of the transaction.

(m) Comparatives

In accordance with the first-time adoption of AIFRS, comparative information has been reclassified, where appropriate, through retrospective application of AIFRS to the previous year results, so as to achieve consistency with current year disclosures.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

NOTE 2: SUBSEQUENT EVENTS

During December 2005 Lakes Oil N.L. offered a Share Purchase Plan inviting existing shareholders to apply for ordinary fully paid shares. On 6 January 2006, 80,287,047 shares were allotted at 1.8 cents per share raising \$1,445,166.85.

On 10 January 2006 Lakes Oil N.L. issued to staff and consultants a total of 6,000,000 options to apply for ordinary fully paid shares at 3 cents per share at any time before 17 November 2009.

On 19 January 2006 Lakes Oil N.L. announced a placement of 50,000,000 shares at 2 cents raising \$1,000,000.

On 16 February 2006, the tenure of Petroleum Exploration Permit (PEP) 156 expired. Petro Tech Pty Ltd held a 100% interest in the area and the group carries an amount of \$397,589 attributable to this permit in capitalised exploration expenditure. This amount will now be written off before financial year end.

NOTE 3: SIGNIFICANT ITEMS

	Half-year	
	2005	2004
	\$	\$
Exploration Expenditure written off	976,098	89
	<u>976,098</u>	<u>89</u>

In November 2005 the lease over permit PEP 152 onshore Gippsland in Victoria expired. Consequently, Lakes Oil Group ceased to have an interest and have written off the exploration expenditure previously capitalised. The joint venture partners will not re-apply for the permit.

NOTE 4: DIVIDENDS

No dividends have been paid for provided for during the half-year.

NOTE 5: SEGMENT INFORMATION

The economic entity operates in the oil and gas exploration industry, predominantly in Australia.

NOTE 6: CONTINGENT LIABILITIES

There have been no changes in contingent liabilities since 30 June 2005.

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

NOTE 7: FIRST-TIME ADOPTION OF AIFRS – RECONCILIATION OF EQUITY REPORTED UNDER AGAAP TO EQUITY UNDER AIFRS

(a) At the date of transition to AIFRS – 1 July 2004

	AGAAP \$	Adjustment \$	AIFRS \$
CURRENT ASSETS			
Cash and cash equivalents	3,998,277		3,998,277
Trade receivables	444,755		444,755
Other current assets	331,541		331,541
TOTAL CURRENT ASSETS	4,774,573		4,774,573
NON-CURRENT ASSETS			
Other financial assets	886,764	921,969	1,808,733
Property, plant and equipment	67,031		67,031
Deferred exploration, evaluation and development	20,356,294	(211,461)	20,144,833
TOTAL NON-CURRENT ASSETS	21,310,089		22,020,597
TOTAL ASSETS	26,084,662		26,795,170
CURRENT LIABILITIES			
Trade and other payables	943,355		943,355
Short-term provisions	63,315		63,315
TOTAL CURRENT LIABILITIES	1,006,670		1,006,670
NON-CURRENT LIABILITIES			
Long-term provisions	11,276		11,276
TOTAL NON-CURRENT LIABILITIES	11,276		11,276
TOTAL LIABILITIES	1,017,946		1,017,946
NET ASSETS	25,066,716		25,777,224
EQUITY			
Share capital	46,233,855		46,233,855
Other reserves	-	25,089	25,089
Accumulated losses	(21,167,139)	685,419	(20,481,720)
TOTAL EQUITY	25,066,716		25,777,224

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

(b) At the date of the last half-year reporting period under AGAAP - 31 December 2004

	AGAAP \$	Adjustment \$	AIFRS \$
CURRENT ASSETS			
Cash and cash equivalents	141,279		141,279
Trade receivables	1,658,319		1,658,319
Other current assets	228,091		228,091
TOTAL CURRENT ASSETS	<u>2,027,689</u>		<u>2,027,689</u>
NON-CURRENT ASSETS			
Other financial assets	1,544,552	1,027,995	2,572,547
Property, plant and equipment	191,980		191,980
Deferred exploration and evaluation	24,413,297	(211,550)	24,201,747
TOTAL NON-CURRENT ASSETS	<u>26,149,829</u>		<u>26,966,274</u>
TOTAL ASSETS	<u>28,177,518</u>		<u>28,993,963</u>
CURRENT LIABILITIES			
Trade and other payables	284,217		284,217
Short-term provisions	64,621		64,621
TOTAL CURRENT LIABILITIES	<u>348,838</u>		<u>348,838</u>
NON-CURRENT LIABILITIES			
Deferred tax liabilities			
Long-term provisions	13,522		13,522
TOTAL NON-CURRENT LIABILITIES	<u>13,522</u>		<u>13,522</u>
TOTAL LIABILITIES	<u>362,360</u>		<u>362,360</u>
NET ASSETS	<u>27,815,158</u>		<u>28,631,603</u>
EQUITY			
Share capital	49,182,105		49,182,105
Other reserves	-	53,632	53,632
Accumulated losses	(21,366,947)	762,813	(20,604,134)
TOTAL EQUITY	<u>27,815,158</u>		<u>28,631,603</u>

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

(c) At the date of the last annual reporting period under AGAAP – 30 June 2005

	AGAAP \$	Adjustment \$	AIFRS \$
CURRENT ASSETS			
Cash and cash equivalents	3,594,733		3,594,733
Trade receivables	818,553		818,553
Other current assets	295,067		295,067
TOTAL CURRENT ASSETS	4,708,353		4,708,353
NON-CURRENT ASSETS			
Other financial assets	1,423,630	147,053	1,570,683
Property, plant and equipment	187,152		187,152
Deferred exploration and evaluation	27,959,350	(211,550)	27,747,800
TOTAL NON-CURRENT ASSETS	29,570,132		29,505,635
TOTAL ASSETS	34,278,485		34,213,988
CURRENT LIABILITIES			
Trade and other payables	2,071,157		2,071,157
Short-term provisions	40,141		40,141
TOTAL CURRENT LIABILITIES	2,111,298		2,111,298
NON-CURRENT LIABILITIES			
Long-term provisions	37,501		37,501
TOTAL NON-CURRENT LIABILITIES	37,501		37,501
TOTAL LIABILITIES	2,148,799		2,148,799
NET ASSETS	32,129,686		32,065,189
EQUITY			
Share capital	54,369,463		54,369,463
Other reserves	969,000	137,512	1,106,512
Retained earnings	(23,208,777)	(202,009)	(23,410,786)
TOTAL EQUITY	32,129,686		32,065,189

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

NOTE 8: FIRST-TIME ADOPTION OF AIFRS – RECONCILIATION OF PROFIT REPORTED UNDER AGAAP TO PROFIT UNDER AIFRS

(a) Reconciliation of profit for the half-year ended 31 December 2004

	AGAAP \$	Adjustment \$	AIFRS \$
Revenue			
Other income	781,137	106,026	887,163
	<u>781,137</u>		<u>887,163</u>
Employee benefits expense	(246,950)	(28,543)	(275,493)
Depreciation and amortisation expenses	(19,871)		(19,871)
Finance costs	(3,547)		(3,547)
Other expenses	(710,577)	(89)	(710,666)
	<u>(199,808)</u>		<u>(122,414)</u>
Loss before income tax	(199,808)		(122,414)
Income tax expense	-		-
	<u>(199,808)</u>		<u>(122,414)</u>
Loss for the half year	(199,808)		(122,414)
Loss attributable to the members of the parent	(199,808)		(122,414)

(b) Reconciliation of profit for the year ended 30 June 2005

	AGAAP \$	Adjustment \$	AIFRS \$
Revenue			
Other income	1,034,277		1,034,277
	<u>1,034,277</u>		<u>1,034,277</u>
Employee benefits expense	(538,237)	(112,423)	(650,660)
Depreciation and amortisation expenses	(53,916)		(53,916)
Finance costs	(7,066)		(7,066)
Other expenses	(2,476,696)	(774,997)	(3,251,693)
	<u>(2,041,638)</u>		<u>(2,929,058)</u>
Loss before income tax	(2,041,638)		(2,929,058)
Income tax expense	-		-
	<u>(2,041,638)</u>		<u>(2,929,058)</u>
Loss for the half year	(2,041,638)		(2,929,058)
Loss attributable to the members of the parent	(2,041,638)		(2,929,058)

LAKES OIL N.L. AND CONTROLLED ENTITIES

Notes to the financial statements

31 December 2005 (continued)

NOTE 9: FIRST-TIME ADOPTION OF AIFRS – RECONCILIATION OF CASH FLOW STATEMENT FOR THE YEAR ENDED 30 JUNE 2005 AS REPORTED UNDER AGAAP TO CASH FLOWS UNDER AIFRS

The adoption of AIFRS has not resulted in any material adjustments to the cash flow statement.

NOTE 10: FIRST-TIME ADOPTION OF AIFRS – EXPLANATION OF CHANGES IN ACCOUNTING POLICY ARISING ON FIRST-TIME ADOPTION OF AIFRS

(a) Share based payments

Under AASB 2 Share based Payments, the company is required to determine the fair value of equity settled transactions and recognise an expense in the Income Statement.

On first-time adoption of AIFRS retained earnings at 1 July 2004 and reported results for the half-year to 31 December 2004 have been adjusted for all share-based payments granted after 7 November 2002, which did not vest prior to 1 January 2005.

(b) Impairment of assets

Under AIFRS the “recoverable amount” test under the previous AGAAP is replaced by “impairment testing” whereby the recoverable amount is determined as the higher of fair value less costs to sell and value in use. Value in use incorporates the use of discounted cash flows.

(c) Exploration and evaluation expenditure

On first time adoption of AIFRS the entity has performed the impairment test on any carried amounts that may be impaired. Any amounts deemed impaired have been written off against retained earnings.

(d) Income taxes

Under AIFRS a balance sheet approach is required where temporary differences are identified for each asset and liability rather than accounting for the effect of timing and permanent differences between taxable and accounting profit.

Tax losses have not been recognised because they do not satisfy the criteria for the “probable recovery” test.

(e) Financial instruments

The entity previously measured all investments at fair value and recognised gains and losses in the asset revaluation reserve. On first-time adoption of AIFRS investments that are listed on a recognised securities exchange have been designated as fair value through profit and loss and therefore the balance in the revaluation reserve relating to these investments has been transferred to retained earnings.

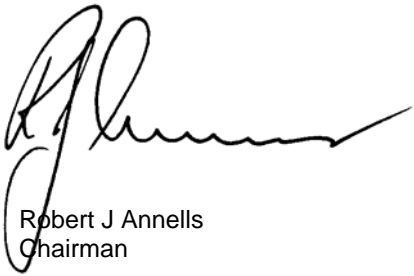
LAKES OIL N.L. AND CONTROLLED ENTITIES DIRECTORS DECLARATION

The directors declare that the financial statements and notes set out on pages 8 to 21 in accordance with the *Corporations Act 2001*:

- (a) Comply with Accounting Standard AASB 134 "Interim Financial Reporting" and the *Corporations Regulations 2001*, and
- (b) Give a true and fair view of the financial position of the consolidated entity as at 31 December 2005 and of its performance as represented by the results of its operations and its cash flows, for the half-year ended on that date.

In the directors' opinion there are reasonable grounds to believe that Lakes Oil N.L. will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors



Robert J Annells
Chairman

Melbourne
1 March 2006

**INDEPENDENT REVIEW REPORT
TO THE MEMBERS OF LAKES OIL N.L.**

Scope

We have reviewed the condensed consolidated financial report of Lakes Oil N.L for the half-year ended 31 December 2005 as set out on pages 8 to 22. The directors are responsible for the financial report. We have performed an independent review of the financial report in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that the financial report is not presented fairly in accordance with Accounting Standard AASB 134 'Interim Financial Reporting' and other mandatory professional reporting requirements in Australia and statutory requirements, so as to present a view which is consistent with our understanding of the entity's financial position, and performance as represented by the results of its operations and cash flows, and in order for the entity to lodge the financial report with the Australian Securities and Investments Commission.

Our review has been conducted in accordance with Australian Auditing Standards applicable to review engagements. A review is limited primarily to inquiries of company personnel and analytical procedures applied to the financial data. These procedures do not provide all the evidence that would be required in an audit, thus the level of assurance is less than given in an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

Statement

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Lakes Oil N.L. is not in accordance with:

- (a) the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the consolidated entity's financial position as at 31 December 2005 and of its performance for the half-year ended on that date; and
 - (ii) complying with Accounting Standard AASB 134 'Interim Financial Reporting' and the *Corporations Regulations 2001*; and
- (b) other mandatory professional reporting requirements in Australia.



PITCHER PARTNERS



**M W PRINGLE
Partner
Melbourne**

1 March 2006