

ANNUAL REPORT 2005 FOR THE SDFI AND PETORO



Contents

2	Key figures for the SDFI
3	Highlights of 2005
4	Kjell Pedersen: Boldness and innovative thinking
8	Directors’ report 2005
24	Health, safety and the environment
27	Management team for Petoro AS
30	Carbon dioxide injection: double dividends
34	Carbon dioxide injection: important for improving the recovery factor
36	Improving governance boosts value creation
40	Corporate governance
43	SDFI appropriation accounts
44	SDFI capital accounts
45	SDFI income statement
46	SDFI balance sheet at 31 December 2005
47	SDFI cash flow statement
48	SDFI notes
67	Audit letter from the Office of the Auditor General
70	Petoro AS income statement
71	Petoro AS Balance sheet
72	Petoro AS Cash flow statement
73	Petoro AS Notes
79	Auditor’s report

Front cover: Detail of *Interior of the Gare Saint Lazare*, Claude Monet, 1877. See also page 32.

One of our values in Petoro is boldness and innovative thinking, a theme we touch on in this annual report – including the way we have chosen to illustrate it. We challenged art historian Lau Albrektsen to select and provide brief descriptions of artworks or architectural gems which represent transitions or paradigm shifts in European comprehension, thought and expression over 20 generations.

Our interest lies in the actual change, in the processes which get us to see, understand and do things differently. And innovative thinking is by no means confined to broad trends in world art. We have more than enough practical themes and issues in the Norwegian petroleum industry which need to be approached in new ways.

If the illustrations in this report succeed in arousing a little curiosity, encouraging reflection and perhaps even stimulating innovative thinking, we will have achieved our aim.

Development of space and perspective in the Renaissance – page 6



Emergence of glass and iron in architecture during the 19th century – page 22



Impressionism/Expressionism: the birth of modern painting – page 28



Vitalism/Cubism in the early 20th century – page 38

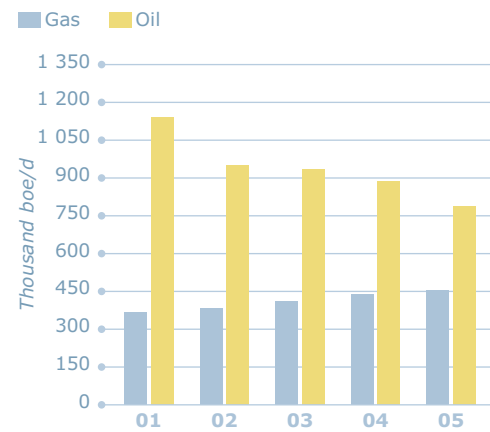


Painting as an autonomous mode of expression – page 68

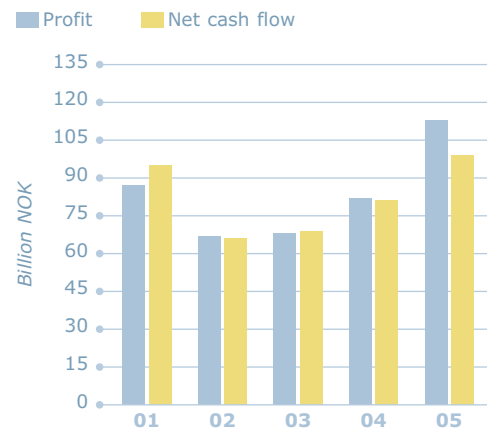


Key figures for the SDFI*

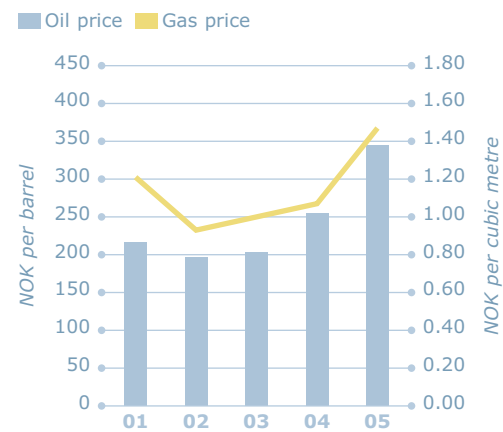
Production



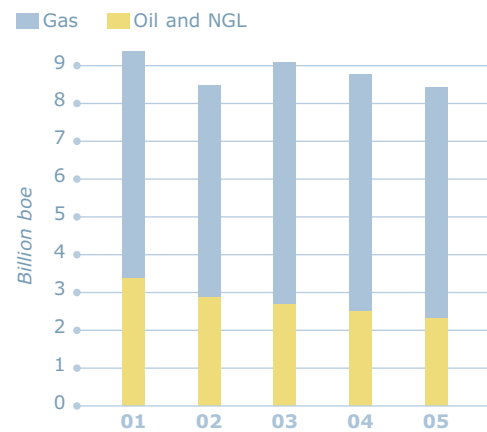
Profit and cash flow



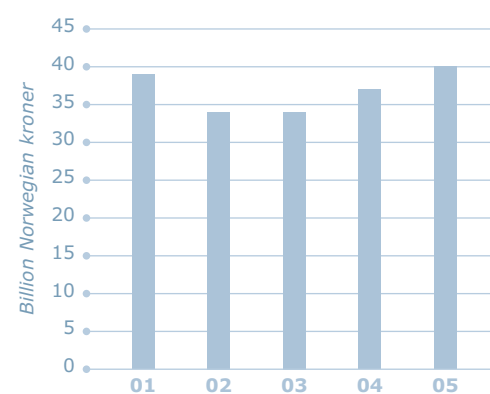
Oil and gas prices



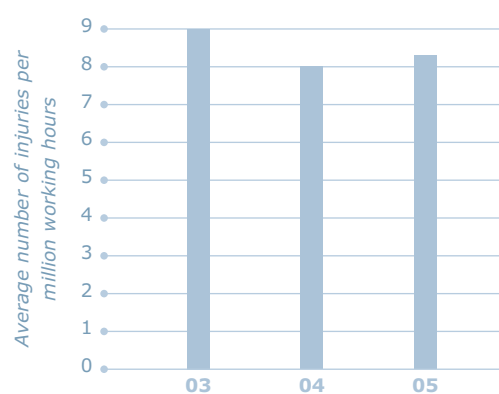
Remaining reserves



Costs



Personal injuries



* The figures for 2001 have been adjusted for the sale of 15 per cent of the SDFI portfolio's assets to Statoil at 1 June 2001. Similarly, the 2002 figures have been adjusted for the sale of 6.5 per cent of the SDFI portfolio to other companies in that year.

Highlights of 2005

- Net profit of NOK 113 billion – best financial result for the SDFI in Petoro's history.
- One large discovery and several smaller ones.
- Four new developments sanctioned by the licences: Ringhorne East, Tordis improved oil recovery, Oseberg Delta and the Tampen Link pipeline.
- Two new fields on stream: Kristin and Urd.
- New reserves: 177 million barrels of oil equivalent added to the portfolio.
- Oil production reduced substantially, partly offset by higher gas sales.
- New cost rise and delay on Snøhvit, delay in drilling and production start-up on Kristin.
- Four people died on installations within Petoro's area of activity.
- Petoro secured acceptance in 2005 for many of its proposals on governance and increased influence for the partners in production licences on the NCS. New agreements are being developed by the Norwegian Oil Industry Association (OLF).
- Petoro was commissioned by the government just before Christmas to lead work on identifying oil fields which could use carbon dioxide injection as a method for improving profitable offshore recovery. The results of this work will be incorporated in a report due to be submitted to the government on 1 June 2006 on the possible creation of a carbon value chain.

Financial data

(NOK million)	2005	2004	2003	2002	2001
Operating revenue	152 683	120 807	101 699	103 709	125 562
Operating profit	113 069	83 653	68 621	70 366	86 318
Net profit	113 172	82 343	68 154	67 417	86 688
Cash flow from operational activities	122 181	98 820	85 045	82 078	108 344
Cash flow used for investing activities	19 661	16 492	14 465	13 140	16 513
Net cash flow	99 175	81 401	69 005	66 082	94 548

Operational data

Production – oil and NGL (1 000 b/d)	788	886	933	949	1 140
Production – dry gas (scm/d)	73	70	65	61	58
Production – oil, NGL and dry gas (1 000 boe/d)	1 244	1 324	1 341	1 333	1 508
Remaining reserves (million boe)	8 422	8 773	9 095	8 478	9 369
Reserve replacement ratio* (three-year average in %)	96	88	84	25	N/A
Reserves added* (million boe)	177	88	1 104	95	95
Oil price (USD/bbl)	53.03	37.57	28.76	24.20	24.02
Oil price (NOK/bbl)	344	254	203	196	216
Gas price (NOK/scm)	1.47	1.07	1.00	0.93	1.21

* Excluding changes to the portfolio from the addition/disposal of interests in production licences.

Boldness and innovative thinking

“Boldness and innovative thinking” is one of the values on which we in Petoro base our business. It has occasionally presented us with some difficult questions. How can you be bold in Norway’s oil industry? Where does the boundary go between boldness and foolhardiness? Are we able to think innovatively? How can we make a contribution?

An easy option is to look for the answers in the commitment to the far north. Developments in the Barents Sea and the northern and outermost parts of the Norwegian Sea demand courage, strength and drive – qualities I associate with being bold.

Activities in such regions demand a high level of expertise and a strong commitment in a number of areas – the highest safety and environmental standards, technology, financial endurance, concern for the community and foreign policy flexibility.

Petoro was already positioned in the far north before the 19th licensing round. With the SDFI receiving interests in five of six new licences awarded in the Barents Sea in the spring of 2006, we have also become a substantial player in this part of the NCS. Like others both inside and outside the oil industry, we are looking forward with great expectations to what the Norwegian and Barents Seas will bring in the years to come.

At the same time, we also need to be bold and innovative with the bird in our hand. The mature areas of the NCS are where the industry extracts the massive wealth which daily lubricates Norway’s economy and gives Norwegians good jobs, welfare benefits and commercial opportunities which would otherwise be no more than a dream.

I am accordingly very gratified with the results you can read more about in this annual report. We can present a profit of no less than NOK 113 billion for the SDFI in 2005 – an almost inconceivably large sum.

But since we can have more than one thought in our heads at a time, I would also express my concern over the fact that both current cash flow and future dreams are diverting attention from today’s reality and the immediate challenges faced in the mature sector of the NCS:

- offshore production is declining, and we are not exploring enough for more oil and gas
- unit costs are rising, so that the infrastructure needed for profitable development of future discoveries could be shut down prematurely
- too few young Norwegians are securing the expertise they need to replace those of us who run the business today
- large quantities of oil and gas could remain below ground if we fail to develop and/or adopt new technology in time.



Kjell Pedersen
President and CEO

I do not want to be a prophet of doom, particularly with today’s oil prices. On the contrary, my point is that even while we are working determinedly to catch the two birds sitting in the bush, we have huge opportunities for value creation in the mature part of the NCS. That view is based on our big remaining reserves, the extensive infrastructure we have already installed, and the expertise we have built up in this industry.

But things do not just happen. If we continue to work in the way which has previously been successful for us, even moderate estimates of production development on the NCS could be difficult to attain. At Petoro, we want to be a driver in ensuring that our industry takes the right steps and adapts in time. If we do, I am convinced that it will be possible to achieve – and perhaps even exceed – the most optimistic production curves for our mature areas. If we also succeed in catching those birds in the bush, a high level of daily production from the NCS can be viewed in a very long perspective.

That makes it all the more gratifying to see that a growing number of operators and other licensees on the NCS want to adopt the new opportunities provided by technology to operate installations in a smarter and more integrated way between sea and land. But this calls for us to be prepared to change the way we work and make better use of our expertise. We must also ask some questions about the way we manage, measure and monitor our operations, so that we are always ahead of the game.

As an example of boldness and innovative thinking, I would venture to highlight the way our strategic focus on improved recovery in Petoro has led us into a role as a driving force in converting carbon dioxide from a waste problem to an instrument of value creation. The government stated in the autumn of 2005 that it could contribute to establishing a value chain for this gas. And, at the government’s request, we are working in the spring of 2006 with Gassco to study the technical and financial basis for such a chain. At the time of writing, no conclusions have been drawn from this complex and highly interesting assignment.

The fact that Statoil and Shell have jointly announced similar plans for a value chain embracing a gas-fired power station at Tjeldbergodden and carbon injection on Draugen, and later on Heidrun, indicates the momentum that this issue has acquired.

We have opted to illustrate this annual report with paintings and architecture which represent paradigm shifts in European history. Without pressing the comparison too far, I believe it could also be valuable for our industry to reflect over the basis for such changes in mindset. What was it that prompted Michelangelo, Monet and Munch to break with accepted perceptions of the world and the way it should be understood and presented?

Or, for that matter, what characterises the people who rejected received wisdom by insisting on the presence of oil beneath the North Sea? What prompted somebody to decide to develop huge concrete platforms for 300 metres of water? And what drove those who pushed through, against strong opposition, the decision to produce the thin oil zones in the Troll field?

They had thought innovatively and boldly.

And we have to do that again.

Kjell Pedersen
President and CEO

Giotto – development of space and perspective in the Renaissance (AD 1400-1600)

Medieval society was dominated by the Church and its world-view.

People were primarily meant to cultivate their relationship with God in order to be fully prepared for a new life after death. They saw themselves as part of a system, where everyone – regardless of their social rank – played a role predetermined by God.

During the High Middle Ages, the Church and the feudal system faced competition from an expanding and more self-conscious urban bourgeoisie, which eventually transferred the economic centre of gravity to the towns. The emergence of cities and a money economy, partly as a result of the Crusades and specialisation in commodity production, changed the way people thought about themselves. They moved from an objective perception of self, in which their role in life was thought to be fixed by the deity, to a subjective view where one observed the world from one's own perspective and regarded changing/improving one's lot as not only possible but also the main purpose of life.

This development was swift in Italy, partly because of its role in the great Crusades. The need to take ship for the Holy Land encouraged the growth of wealthy ports such as Venice, Genoa and Pisa. To find a prototype for their new position, they looked back to the Italian past – the Roman Empire and the humanism of Classical Antiquity, which represented precisely a view of humanity suited to modern people at the end of the Middle Ages. That sparked the Renaissance – the "rebirth".

Its primary impact on painting was that artists no longer wished to present an ideal, God-ruled world, but a realistic one in which they were personally present and could act from their own standpoint. That created a need to depict space. With his linear perspective, Giotto was the first and clearest artist to systematise this desire in the "proto-Renaissance" of the early 14th century.



GIOTTO: *The Annunciation to Anna*, 1303-06. Fresco, Scrovegni Chapel, Padua.

Directors’ report 2005

As manager of the State’s Direct Financial Interest (SDFI) on the Norwegian continental shelf, Petoro’s object is to create the highest possible financial value from this portfolio. Net income for the portfolio in 2005 came to NOK 113.2 billion, an increase of NOK 30.8 billion from the year before. Total operating revenue was NOK 152.7 billion, compared with NOK 120.8 billion in 2004. Cash flow amounted to NOK 99.2 billion as against NOK 81.4 billion the year before. The board is very satisfied with the financial results for the year¹.

The increase in net profit primarily reflects higher oil and gas prices. Overall oil and gas sales for the year were lower than expected, at 1 257 million barrels of oil equivalent (boe) per day compared with 1 329 million boe per day in 2004. Production challenges on Snorre and Åsgard were important reasons for the reduction in sales. The general maturation of the portfolio, with a number of fields off plateau, also represents an important reason for the decline in production of oil and natural gas liquids (NGL). In addition, drilling delays – partly caused by rig strikes in 2004 – had significant consequences in 2005. A steady expansion in gas sales made a positive contribution, and is expected to compensate for declining oil output in coming years.

Income before financial items came to NOK 113.1 billion. A net financial income of NOK 0.1 billion reflected net realised and unrealised currency losses related to a slight weakening of the NOK exchange rate against the USD, which was partly offset by higher interest costs relating to future removal liabilities.

Total operating revenue was NOK 152.7 billion as against NOK 120.8 billion in 2004. This increase reflects higher oil and gas prices.

Revenue for the year from dry gas sales totalled NOK 45.2 billion as against NOK 32.1 billion in 2004. The volume of equity gas sold was 26.5 billion standard cubic metres (scm) or 456 000 boe per day as against 438 000 in 2004. Several fields increased their gas production from 2004, with Troll Gas accounting for the biggest rise together with a full production year on Kvitebjørn. Troll accounted for 47 per cent of total gas revenues. The average gas price for the year was NOK 1.47 per scm as against NOK 1.07 in 2004. Gas revenues increased by NOK 13.1 billion from 2004.

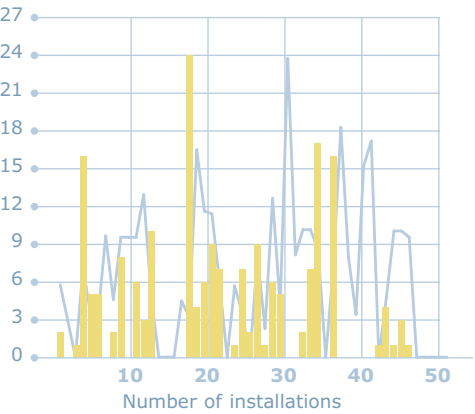
Total revenue for 2005 from oil and NGL was NOK 96.5 billion, compared with NOK 80.9 billion the year before. The sales volume was 292 million barrels or a daily average of 801 000 barrels. Production of oil and NGL fell by 11 per cent from 2004, reflecting declining output from a growing number of mature fields as well as drilling delays. Snorre experienced substantial challenges in 2005 relating to gas injection capacity and shut-in production wells. Oil output from Troll has gone off plateau, and declined by 22 per cent from 2004. Good well capacity on Kvitebjørn meant that revenues from this field’s first full production year were higher than expected. The oil price for the year averaged NOK 344 per barrel in 2005, up by 35 per cent from NOK 254 the year before. The oil price in US dollars was 53.03 per barrel, an increase of 41 per cent from 2004. Oil and NGL revenue for the portfolio increased by NOK 15.5 billion from 2004.

¹ All figures in NGAAP.

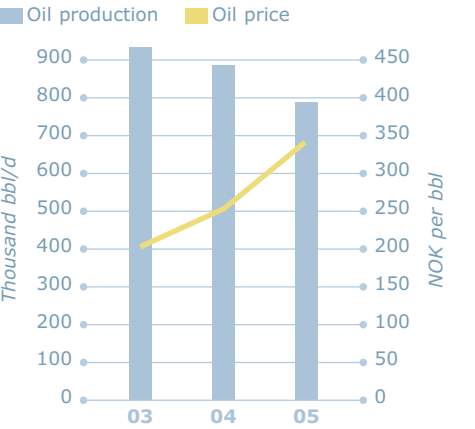
Serious incidents and personal injuries per installation in 2005

Personal injuries per million working hours

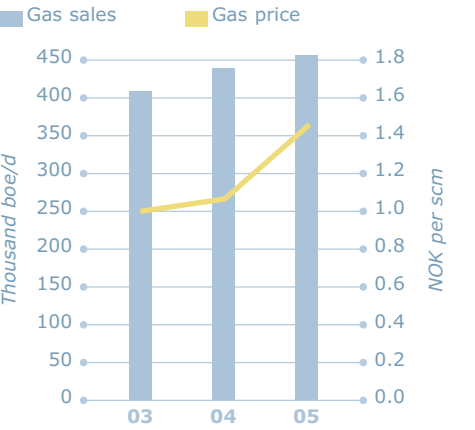
Serious incidents



Oil production/price



Gas sales/price



Total investment in 2005 was NOK 21.3 billion as against NOK 17.8 billion the year before. The largest investments related to Ormen Lange, Langeled, Snøhvit, Troll Oil and Gassled.

Exploration-related costs amounted to NOK 942 million in 2005, of which NOK 400 million was capitalised as investment and the remainder recorded as exploration expenses in the income statement. Correspondingly, exploration expenses totalled NOK 624 million in 2005. A total of 10 wells were drilled during the year compared with four in 2004. The board is concerned to see a further increase in exploration activity during 2006 in the hunt for additional reserves.

At 31 December, the portfolio's expected oil, NGL and gas reserves comprised 8.4 billion boe – a decrease of 349 million boe from the year before. Petoro classifies the portfolio's expected reserves in accordance with categories 1-3 in the Norwegian Petroleum Directorate's classification system. Resources which have not been sufficiently matured and where the licensees have not submitted their plan for development and operation (PDO) to the authorities are accordingly excluded. The gross addition of expected reserves in 2005 came to 177 million boe, mainly through improved recovery from mature fields, while production was 454 million boe. The net reserve replacement rate for 2005 was thereby 38 per cent, compared with 33 per cent in 2004. An average rate of 96 per cent has been achieved by the portfolio over the past three years.

The book value of assets totalled NOK 164 billion at 31 December 2005. These assets primarily comprise operating facilities relating to field installations, pipelines and land-based plants, as well as current debtors.

Equity at 31 December amounted to NOK 135 billion. Long-term liabilities totalled NOK 19.2 billion, of which NOK 18.5 billion related to future removal liabilities. These liabilities are calculated in accordance with an established industry standard based on existing technology. Great uncertainty exists over the removal estimate and the timing of removals. Current liabilities, primarily provision for costs incurred but not paid, were NOK 9.8 billion at 31 December.

Petoro served at 31 December 2005 as the licensee for interests in 100 production licences and 12 joint ventures covering pipelines and terminals. The company also manages the

government's commercial interests in Mongstad Terminal DA, Etanor DA and Vestprosess DA as well as the shares in Norsea Gas AS and Norpipe Oil AS. It has the same rights and obligations as other licensees, and manages the SDFI on a commercial basis. Petoro has divided the portfolio's production licences into geographic areas. Further details of operations in these areas during 2005 are provided below.

TROLL AREA

Average daily production from the Troll area in 2005 was in line with targets. Oil output from Troll has gone off plateau. Combined with delays in the Troll Oil drilling programme, this meant that production was lower than in 2004. Petoro gives weight to maintaining a high level of drilling in Troll Oil in order to meet the licensees' ambition of increasing the field's commercially-recoverable oil reserves. Three drilling rigs were on charter during 2005.

Gas output from Troll in 2005 was in line with expectations, and the field produced overall close to its production permit for the year.

Troll Oil and Troll Gas are ranked as best field in efficiency terms by benchmarkings of production costs on the NCS. Petoro has also pressed for the implementation of technology which can further improve the field's recovery factor and reduce its costs.

The company is working to realise good development solutions for Camilla/Belinda and Gjølå which will provide high flexibility in the Sogn area. The licensees are working towards the completion of a PDO for these discoveries in the second half of 2006.

Kvitebjørn delivered a higher gas and condensate output than expected in its first full operating year. Roughly 70 per cent of its proven reserves can be recovered with existing wells and the drilling programme will continue until the third quarter of 2006. The joint venture will give priority during 2006 to the work of tying in Valemon and other resources in the area. Estimated reserves in Kvitebjørn have been increased by 50 per cent, from 465 million boe to 700 million. This means

an increase of 70 million boe in the SDFI's reserves and contributes to reserve growth in 2006.

OSEBERG AREA/GRANE

Oil production from the Oseberg area accorded with expectations in 2005, but overall output was nevertheless higher because of increased gas flow from Tune. Grane reached plateau production as planned towards the end of 2005.

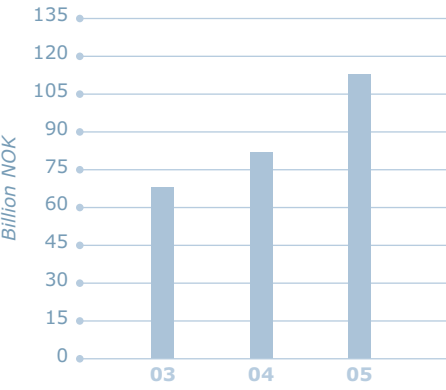
Production and maintenance costs for the area have been stable for a number of years. Grane has substantial costs relating to the purchase of gas for injection to improve oil recovery. This gas injection strategy has proved successful and contributes to increased production and a higher recovery factor. Most of the purchased gas is expected to be recovered in a later phase.

The joint venture submitted a PDO for Oseberg Delta to the authorities in July 2005. These plans involve a sub-sea development of the Delta structure in the Oseberg area, with facilities at the Oseberg field centre utilised for processing and export. Production is expected to begin in 2007, and will total some 14 000 boe per day at plateau. A PDO for Ringhorne East was also submitted to the authorities in October 2005. This development involves drilling four production wells from the existing Ringhorne installation and processing on the Balder vessel. The project is expected to come on stream in 2006.

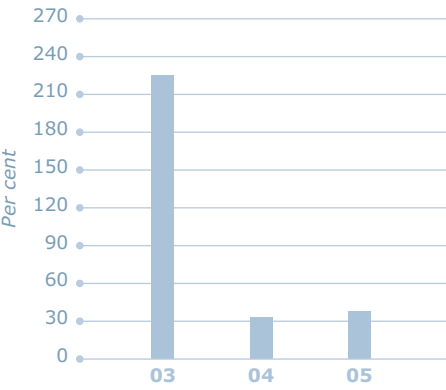
TAMPEN AREA

Production from the Tampen area was substantially below target in 2005. The principal reason was the shutdown of Snorre for much of the first quarter, and significant well problems on this field during the year. Problems with sand control and delays in the drilling programme mean that the annual level of production from this field has also been reduced for coming years. A step-by-step increase in output during 2005 nevertheless restored the field to a normal level of production towards the end of the year. Reduced production from Visund and Gullfaks were other reasons why the oil target for 2005 was not reached. An extended turnaround on Visund and technical problems on Gullfaks were the

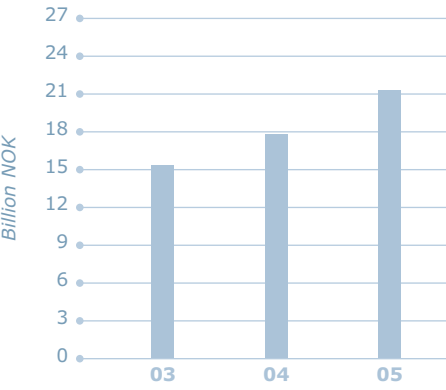
Profit



Reserve replacement ratio



Investment



most important reasons for the failure to reach production targets on these fields. The start of test production in February from Gimle, previously known as Topas, partly offset these reductions.

Improving production efficiency had high priority in 2005, both through future use of smart (integrated) operation and other improvements to production and maintenance. Experience was exchanged between Gullfaks and Oseberg in order to take advantage of best practice on both fields.

The PDO for low-pressure production and subsea separation on Tordis was approved by the authorities in December 2005. Low-pressure operation is due to begin in October 2006, with subsea separation starting a year later. This project will boost oil production from Tordis by about 15 per cent.

NORWEGIAN SEA

Overall production from the Norwegian Sea was substantially below the 2005 target. The main reasons were delays to drilling and well work on Åsgard, Norne and Draugen as well as shut-downs caused by cracking in flowlines on Åsgard. Crack formation in two of this field’s flowlines were discovered during a routine inspection, and work to prevent further propagation began in November 2005. The relevant flowlines will be shut down until temporary repairs have been completed in the summer of 2006. Full repair or possible new installation of the flowlines is planned for 2007.

The Kristin gas and condensate field began production on 3 November 2005, a month behind schedule. Faults in the installation’s lifeboats were a significant reason for the delayed start-up. High reservoir pressure and temperature as well as implementation of the drilling programme have been demanding challenges for the project. The level of well output and the use of new downhole solutions have partly offset the consequences of delays in the drilling programme. Plans call for production to reach plateau in the summer of 2006, and estimated reserves are in line with the calculations in the PDO.

Production began from the Urd field in the Norne area on 8 November 2005, a month behind schedule. Reserves in this field are 70 million barrels of oil plus a small volume of gas. Production from Urd will help to ensure good utilisation of the Norne production ship and infrastructure in the area.

Petoro is working for a reduction in unit costs in order to extend the producing life of fields. Åsgard, Heidrun and Norne have shown a positive trend, and the development of new drilling technology has increased recoverable reserves on Heidrun and Norne. A number of measures have been identified on Draugen for reducing production costs over the next three years.

Activity in the Ormen Lange project was high during 2005. Securing the personnel required for planned operations has been a major challenge. Offshore work in the project passed important milestones with the installation of templates and the start to drilling. Planned activities were executed in the Langeled project for laying the southern pipeline leg from Sleipner to Easington and modification of the Sleipner riser platform. Measures were adopted to ensure the progress of construction work on the landfall terminal in the UK. Both projects are on schedule, with start-up of Ormen Lange planned on 1 October 2007 and Langeled due to become operational a year earlier. However, 2006 will be a critical period for all sub-projects, with the execution of a great many offshore operations, well drilling and a high level of activity at Nyhamna throughout the year.

BARENTS SEA

The Snøhvit development is organised in sub-projects for the field and the land-based plant. The field development part was largely completed during 2005 in line with the original plans and budget. Wells required for starting production have been completed, and subsea installations – including the pipeline – are in place. Remaining work in 2006 involves the drilling of three wells on the Albatross reservoir, covering pipelines and readying for operation. The land-based plant at Melkøya posed a special challenge for the Snøhvit project team in 2005. All sub-deliveries, modules and barges were shipped from the various construction sites and hook-up is under way. This work has proved considerably more demanding than expected, leading to substantial cost increases and delays. The operator announced in September 2005 that costs would rise by an additional NOK 7 billion, of which the SDFI’s share is NOK 2.1 billion, and that a start to production would be postponed for a further six months to 1 June 2007. This delay also

poses challenges for existing sales contracts, which specify that deliveries to customers begin in October 2006. The board remains concerned about the many challenges facing the execution of this project.

PRODUCTION LICENCES IN THE EXPLORATION PHASE

The board is disappointed that, despite the high level of activity on the NCS in 2005, exploration operations were below expectations. Only half the planned exploration wells were drilled. Challenges relating to rig accessibility and increased demand for drilling and well work on producing fields resulted in delays to and postponements of planned exploration programmes. A total of 10 wells were drilled during the year, six more than in 2004 when the extensive rig strike meant that large parts of the work had to be postponed.

An important oil discovery in the Brent formation on Troll B is expected to increase reserves in this field by about 30 million barrels of oil. Work also began on an appraisal well for this discovery, which will be completed in 2006. Gas was also proven in the Peon prospect north of Troll. Further investigation and testing in 2006 will clarify whether this discovery is commercial.

Three exploration wells were completed in the Norwegian Sea during 2005. Two resulted in discoveries, in Onyx South West and the Stetind structure respectively. The first of these is expected to be commercial, with appraisal planned in 2006. Further evaluation and drilling are needed on Stetind before any conclusion on commerciality can be reached. An appraisal well drilled on the Sklinna structure failed to prove mobile hydrocarbons. Several planned wells close to Norne and Heidrun were postponed until 2006 because of a shortage of rigs.

Four exploration wells were drilled in the Oseberg area during 2005, with three discoveries made in Oseberg South. Two of these were in the same well. Recoverable reserves are expected to be in the order of 10-30 million barrels of oil, and one of the discoveries will be brought on stream as early as the autumn of 2006. Two exploration wells were also completed in the Idun and Barry-Powell prospects close to Brage and Tune respectively. Both yielded disappointing results.



ANDREA DEL CASTAGNO:
The Last Supper, 1447.
Mural, S Apollonia, Florence.



DOMENICO GHIRLANDAIO:
The Last Supper, 1480.
Mural, Ognissanti, Florence.



LEONARDO DA VINCI:
The Last Supper, 1495-97.
Mural, S Maria delle Grazie, Milan.

After some setbacks caused by the Black Death in the mid 14th century, the Renaissance achieved its definitive breakthrough around 1400. The new tool provided for painters by central perspective meant they were no longer content to produce paintings as peepholes into another world. Walls are also decorated with murals to create the illusion of the real room continuing into the painted space. Three examples of such works in monastery refectories (dining rooms) are illustrated above. The monks could thereby see their own table extend into the artist's depiction of the original Last Supper. In the two older murals, the main concern of the artist is to make the illusion of continuity as great as possible, so no action is taking place. Da Vinci, on the other hand, has chosen to illustrate the dramatic moment when Christ reveals that one of those present will betray him, causing a violent reaction among the apostles.

One exploration well in the Tampen area was completed in 2005, yielding a discovery in the M prospect which is estimated to contain some 10 million barrels of oil.

No exploration wells were drilled in production licences with SDFI participation in the Barents Sea during 2005, but preparations are being made to drill the Tornerose prospect in 2006.

PIPELINES AND LAND-BASED PLANTS

As the largest partner in pipelines and land-based plants, Petoro has worked to ensure that Gassled's improvement programme to reduce operating costs and enhance regularity is implemented as planned. The approved improvement programme for Kårstø aims to trim some NOK 500 million from operating costs by 2009.

Appropriate management tools have been established for coordinating a number of sub-projects at Kårstø relating to safety, regularity and capacity. An expansion of this plant was completed in the autumn of 2005 at the same time as Kristin came on stream. The project was executed on time and to budget, but the facilities have suffered start-up problems which are now being dealt with.

A project to expand export capacity has been initiated at the Kollsnes plant, with completion planned for the autumn of 2006.

Construction of a new pipeline from Statfjord via existing transport systems to the UK was approved by the authorities in 2005. This work is on schedule, with start-up planned in 2007. The object is to transport gas from Statfjord and other fields, mainly in the Tampen area, for sale in the UK.

MARKETS AND SALES

All oil and NGL produced from the portfolio is sold to Statoil, which is also responsible for marketing the SDFI's gas. Petoro's responsibility for supervising Statoil's sales of the government's petroleum is targeted on achieving the highest possible overall value for the petroleum belonging to both Statoil and the government, and to ensure an equitable division of total value creation. Petoro focuses in this work on Statoil's marketing and sales strategy and risks, issues of great significance in value terms, matters of principle and questions relating to incentives, as well as ensuring that the SDFI receives the correct share of revenue and costs.

Natural gas belonging to Statoil and the government is sold as a single portfolio. The bulk of this gas is committed under long-term contracts, with contractual opportunities for price revisions. Substantial work on gas sales during 2005 related to negotiations on such revisions, most of which were completed during the year. Petoro has monitored on-going gas sales to ensure that all available supplies are sold and to help overcome challenges relating to delivery delays

arising from the delayed start-up of Snøhvit. The company has also been concerned with sales to Statoil's own installations, and carried out checks to ensure that the SDFI receives its rightful share of costs and revenues from gas sales.

Statoil concluded new contracts on long-term gas sales in Norway, the UK and continental Europe during 2005. Annual deliveries of roughly 300 million scm over 10 years were agreed with Statkraft, while Scottish Power undertook to buy roughly 500 million scm per year. Both contracts run from 1 October 2007. Germany's Verbundnetz Gas (VNG) extended an existing sales contract by six years, involving additional deliveries totalling 12 billion scm until 2022 from the combined portfolio.

Where oil and NGL sales is concerned, Petoro focused attention during 2005 on oil sales from fields where Statoil is not a licensee and sales to Statoil's own or affiliated installations. A review of sales costs was also carried out, and checks were made to ensure that the SDFI receives its rightful share of revenues.

HEALTH, SAFETY AND THE ENVIRONMENT (HSE)
With four fatal accidents in activities involving the SDFI, 2005 was a very disappointing year from a safety perspective. Two deaths were suffered in connection with the Ormen Lange and Kristin fields. A contractor was killed while working on the construction of a gas store in the UK, and a person died in an accident on a ship at Mongstad. Such incidents occur despite the purposeful efforts being made by the industry to avoid harm to people and the environment. This underlines the need for good management models and work to change attitudes. In that context, the company would highlight Statoil's safe behaviour programme as a good example of enhancing the awareness of each person working in this industry.

In accordance its management system, Petoro works systematically to improve HSE results in the portfolio's licences. As part of this supervision, bilateral management meetings are held regularly with the largest operators. Petoro again participated during 2005 in several HSE management inspections on selected fields and

installations where a negative trend in HSE results had been observed.

The goal of reducing total personal injuries in 2005 was not met. This indicator remained at the same level as the year before. Petoro supports the work done by the operators and the industry to reduce the number of personal injuries and serious incidents on the NCS. The inquiry report after the serious gas leak on Snorre in 2004 identified a number of measures. During 2005, the operator worked systematically to close identified gaps and has kept the joint venture informed about the progress of this work. An industry seminar was held the operator in February 2006 to share the experience gained from Snorre.

The zero discharge plans adopted by the industry in 2003 were due to be implemented during 2005. At 31 December, however, a number of fields had still failed to carry out the measures in full. Petoro will continue its work in the joint ventures to meet the environmental requirements for reduced discharges of oil in produced water.

Three undesirable incidents were registered in 2005, including a personal injury to a contractor employee working in Petoro's premises. None of the company's own personnel suffered injury. Sickness absence was again low, with short-term (one-three days) absences of 0.2 per cent and long-term (more than three days) of 2.4 per cent. Total sickness absence was 2.6 per cent compared with 1.8 per cent in 2004. The company's inclusive workplace agreement with the national insurance service embraces an action plan for keeping sickness absence at a continued low level. Petoro again implemented measures in 2005 to influence the personal attitudes of its personnel towards HSE and their commitment in this area. Further development of the HSE culture during the year included a focus on diet, training and health through lectures and campaigns, as well as safety information at the year's regular HSE day for employees and their families.

STRATEGIC PRIORITIES IN 2005

Petoro again prioritised the use of its resources during 2005 for the execution of strategic projects. Project

themes are determined on the basis of potential for value creation, risk considerations and time criticality. These projects form part of the company's operationalisation of selected strategies.

COORDINATION AND FIELD DEVELOPMENT IN CORE AREAS

Reduced costs through operational improvements

Substantial value can be created for the company's portfolio through efficient operation on the NCS. Today's high oil prices mean a high level of activity, and measures to improve cost efficiency are demanding. Petoro appreciates the distinction between expenditure on measures which increase oil and gas volumes and high costs incurred in operations. The company's flagship issue accordingly relates to unit costs, which reflect the efficiency of value creation in the portfolio. Cost-effective operation is crucial for extending the producing life of fields, while also providing the basis for long-term development of the NCS. In the work of securing continuous operational improvements, Petoro is concerned to ensure a transfer of best practice between fields. It sees significant gains in this context from a sharing of experience from the most cost-effective installations on the NCS with those which have the greatest improvement potential. In 2005, the cost project also benchmarked operating costs on the NCS against a global portfolio. The intention was to analyse the reasons for the big differential in unit production costs between the NCS and the Gulf of Mexico, and to garner experience which can be applied to change processes on the portfolio's own fields.

Implementing good corporate governance in the licences has been a priority for Petoro in 2005. Over the year, it pursued this issue mainly in the company arena and will work purposefully in 2006 to implement best practice in the production licences where it has interests. This work has been an integrated part of processes in the industry to revise and harmonise the agreements which regulate rights and duties between licensees on the NCS. The board considers it very important that the industry obtains a future system of licence management based on more efficient models which set clear directions and ambitions and ensure good collaboration between licensees.

Troll Phase 3 development

The company is the licensee for a 56 per cent holding in Troll, and gave priority in 2005 to work in the licence on assessing alternative strategies for optimising long-term value creation from the whole Troll area. Through the Troll future development project, the joint venture is assessing options for the next development phase on the field. That includes the construction of infrastructure. This work is very demanding, and depends crucially on the collective success of the licensees in taking account of optimum gas offtake while safeguarding the opportunities which could be provided by technological advances for improved oil recovery.

REDUCING UNIT COSTS THROUGH EARLY APPLICATION OF TECHNOLOGY

Smart operation

Petoro has pressed since 2004 for more extensive use of modern information technology by the industry for transferring real-time drilling data, production optimisation, reservoir management, operation and maintenance. This involves extensive changes to the pattern of collaboration between installations on land and offshore. Changed work processes permit better utilisation of expertise and will contribute to greater cost efficiency and improved recovery factors.

A third round-table conference was staged by Petoro for specially-invited senior executives from operators and suppliers to exchange insights and experience relating to the value creation potential and efficiency of restructuring processes. To ensure effective transfer of experience between fields on the NCS, the company undertook a comparative survey of the extent to which smart operation solutions have been adopted. The results were presented to the operator concerned. Most of the companies have now accepted the value creation potential, but Petoro still wants to see speedier implementation of solutions on several of the portfolio's fields.

Light well intervention

The recovery factor is lower on fields developed with subsea wells than on those with platform wells. This partly reflects high intervention costs from the use of expensive drilling rigs. Petoro accordingly pressed in

The Room of the Married Couple is a wholly profane representational space for the Duke of Mantua. He is depicted on all four walls together with his family in various scenes of daily life in the ducal palace. Here, the spatial illusion is taken to its logical conclusion in that the real room is described as covered by a canopy supported on pillars, and extending on all sides into the painted surfaces – even to an illusory opening in the ceiling.



ANDREA MATEGNA: *The Room of the Married Couple, 1473-74. Mural, Ducal Palace, Mantua.*

2005 for well intervention solutions which permit the use of simpler vessels. Today's very tight rig market makes it important to avoid the use of conventional units for this work.

An important milestone for the project was passed when Statoil, on behalf of a number of licences, secured long-term charters for two modern well intervention ships. Petoro will continue its efforts during 2006 to secure mobile rigs and possibly heavier well intervention vessels for the NCS.

REALISING THE POTENTIAL IN THE GAS CHAIN

Infrastructure – future opportunities and challenges

The ownership of most Norwegian gas pipelines and land-based transport and processing facilities is coordinated in Gassled, where Petoro manages the largest owner position. The company pursued a project in 2005 relating to the gas infrastructure, including identification of areas and issues where special follow-up will be required to realise the value which formed the basis for creating Gassled. Petoro will work for good capacity utilisation, timely phasing-in of new infrastructure and cost-effective operation of Gassled.

Gas chain development in the Norwegian Sea

Petoro worked in 2005 on gas infrastructure solutions for the Halten/Nordland area. The licensees have been concerned to identify the optimum regional solution for gas evacuation from Skarv. Alternative solutions have been studied, and the company is now very satisfied with the preference being given to utilising capacity in the Åsgard Transport system rather than constructing a new pipeline.

LONG-TERM ACCESS TO RESERVES

Achieving increased access to reserves from the portfolio's production licences is crucial for delaying the effect of declining oil output. High recovery factors and optimum production from the installations are crucial for retrieving as much as possible of the resources on the NCS. In this context, the company is working systematically to ensure that the licences establish clear exploration strategies and ambitious targets for improved oil recovery (IOR) measures. Increased drilling activity will be a priority area in 2006.

Exploration relating to areas which will have spare capacity in the near future is very important for securing long-term, efficient utilisation of existing fields and infrastructure. To ensure further development of the portfolio's core areas, the company will continue to seek the realisation of coordination gains between licences.

Petoro does not submit applications in licensing rounds. SDFI participation in new licences is reserved by the government on the basis of the licensing policy in force at any given time. Petoro became a licensee during 2005 in a total of eight new licences allocated as part of the awards in pre-defined areas.

Carbon dioxide injection

Petoro continued its work in several arenas during 2005 to investigate the potential for carbon dioxide injection as a method for improving oil recovery and thereby for increasing the

Bente Rathe
(Chair)

Jørgen Lund
(Deputy chair)

Ingelise Arntsen
(Director)

Nils-Henrik M von der Fehr
(Director)



value of the portfolio. This commitment included both technical and commercial assessments of relevant fields. During the budget process for the licences, Petoro proposed that specific studies be launched in four of them – Gullfaks, Oseberg East, Brage and Veslefrikk. It eventually secured agreement for such work on Oseberg East and Brage.

WORKING ENVIRONMENT AND PERSONNEL

Petoro is a knowledge company, and its personnel have a high level of education and expertise. The substantial activity in the industry places heavy pressure on access to resources, and the whole sector is finding recruitment of the necessary expertise to be a demanding business. Petoro’s ability to safeguard the government’s interests in an effective way depends on being able to attract, retain and develop skilled employees in competition with new and existing players on the NCS. Petoro implemented the company’s expertise strategy in 2005 through challenging assignments, active transfer of experience between employees, rotation between departments and disciplines, participation in multidisciplinary projects, courses and conferences. Purposeful development of personnel will remain a priority area in the time to come.

Petoro again conducted a workplace climate survey among all its staff in 2005. Such polls are an important instrument and basis for measures to secure continuous improvement in the working environment. The board is satisfied that the survey provides good feedback from the organisation in important areas. It is particularly gratifying to see that the company’s values and goals are well entrenched with the workforce.

The company is concerned to treat men and woman equally, and facilities equal opportunities for both

genders. This is given particular priority through recruitment and development opportunities and by laying the basis for flexible arrangements on working hours. Respondents to the 2005 climate survey again broadly agreed that both genders are treated equally.

The proportion of females in the company’s board and management is 43 and 22 per cent respectively. Women account for 32 per cent of total employees. Seven women personnel have participated over the past three years in the Female Future project run by the Confederation of Norwegian Business and Industry (NHO). Under this national commitment, NHO members are invited to help strengthen the proportion of women in the management of Norwegian companies and on their boards.

Collaboration with Petoro’s working environment committee and works council again functioned very well in 2005. This work lays an important basis for a good climate of in-house cooperation.

CORPORATE GOVERNANCE

Good corporate governance is characterised by a responsible interaction between owner, board and management in a long-term value creation perspective. The company’s values base and ethical guidelines provide important inputs for corporate governance. Petoro seeks the continuous development of a corporate culture characterised by opportunity-oriented attitudes and a sound internal control system. Maintaining a high level of trust in the company is crucial if Petoro is to deliver lasting value to owner, employees and society as a whole. The company’s management models are based on long-term value creation, focused on the risks posed by its business and targets for cost efficiency. Information from

Petoro will be credible, timely and consistent. The board gives weight to continued development of the management of the company’s operations through dynamic processes between owner, board and management in accordance with sound principles for good corporate governance. Corporate governance is described in more detail in a separate section of this annual report.

Jan M Wennesland retired from the board on 29 April 2005. Olav K Christiansen also retired as a director at the company’s general meeting in June 2005. Two new shareholder representatives were elected to the board – Per-Christian Endsjø and Nils-Henrik M von der Fehr. No other changes occurred among the shareholder- or worker-elected directors.

As licensee for the largest portfolio on the NCS, the company works purposefully to achieve efficiency gains, cost reductions and improved recovery of petroleum. To ensure efficient resource utilisation with an organisation totalling 60 employees, Petoro sets priorities for its work in and between the various joint ventures. These priorities are based on the relative value of each joint venture, its strategic significance, time criticality and Petoro’s opportunities to exert influence. For joint ventures which are not prioritised, business managers have been engaged by Petoro to exercise daily administrative supervision.

Developments in national and international accounting terminology have resulted in a number of companies in the oil and gas industry converting to the International Financial Reporting Standards (IFRS). Other important companies are due to convert by the end of 2007. Reporting in accordance with the IFRS is intended to provide improved information about businesses. Petoro will carry out the necessary work in 2006 to permit the portfolio’s accounts to be presented in accordance with the new accounting terminology from 2007. This transition is not expected to involve significant changes from today’s reporting. Regardless of any such change, the accounts of the portfolio will also be presented in accordance with the cash basis used by the government.

RISK

To discharge its overall responsibility for supervision and control of the business, the board is concerned to ensure that the company’s management models are effective and purposeful and that great attention is paid to the risks facing the company. As part of a continuous improvement effort in this area, Petoro carried out a special project in 2005 on implementing unified, systematic risk management. As an integrated part of the company’s business processes and internal control system, such management involves a process of maturation where planned cultural development plays a crucial role. Unified risk management handles the assessment of conditions and incidents which could prevent the business from attaining specified targets and implementing chosen strategies. Risk management will again be a priority area in 2006.

The portfolio’s oil and NGL is sold to Statoil at market-based prices. Its gas is sold by Statoil and revenue from the sale of gas to customers reflects its market value. The business is exposed to fluctuations in oil and gas prices and exchange rates in the global market for oil and gas sales. Such changes will have an effect on revenues, operating costs and investments over shorter or longer periods.

Given that the SDFI forms part of the government’s overall risk management, its strategy is to make only limited use of financial instruments (derivatives). The use of derivatives to counter fluctuations in results caused by changes in raw material prices is undertaken by Statoil through its responsibility for marketing and sale of the government’s petroleum.

The bulk of the SDFI’s revenue derives from sales of oil and gas, which are denominated in US dollars, euros or pounds sterling. In line with the government’s currency strategy, Petoro does not currency-hedge the portfolio’s future sales of petroleum. The SDFI’s receivables are exposed to exchange rate fluctuations. However, these are regarded as limited in relation to the overall value of the balance sheet.



ANDREA POZZO:
Glorification of St Ignatius, 1691-94.
Church ceiling, S Ignazio, Rome.

During the Baroque period, the Jesuits in particular made use of spatial illusion in churches so that the observer could contemplate the splendours of Heaven. Here, the church’s ceiling opens out with a fantastic illusion of endless space reaching Heavenwards. Typically, Pozzo was actually a mathematician.

Per-Christian Endsjø
(Director)

John Magne Hvidsten
(Worker director)

Elen Carlson
(Worker director)



Since it has no long-term interest-bearing debt, the SDFI is not financially exposed to interest rate changes.

The portfolio's sales are made to a limited number of opposite parties, with all oil and NGL sold to Statoil. Financial instruments relating to gas sales are purchased from counterparties with sound credit ratings. For that reason, credit risk in current transactions is regarded as insignificant.

The SDFI generates a significant positive cash flow from its operations. In-house guidelines on managing the flow of liquidity have been established.

Further information on the risks facing the business is provided in note 15.

PROSPECTS

The portfolio's oil production is expected to decline in coming years, but gas output will increase. While European gas production is decreasing, demand is rising. This offers increased opportunities for Norwegian gas sales in the years to come.

Oil prices during 2005 reached a peak in September of just over USD 65 per barrel for Dated Brent. They declined somewhat towards the end of the year, and Dated Brent was priced at USD 58.2 per barrel on 31 December. The most important reasons for high oil prices in 2005 were market concerns over supply problems and the fact that the US south coast was hit on several occasions by bad weather which reduced oil and natural gas production. Oil output from the North Sea was also lower than expected. The fall in North Sea and US production meant that non-Opec output was unchanged from 2004, even though countries in the former Soviet Union and several African nations substantially increased their production. The latest figures from the International Energy Agency (IEA) show that Chinese demand rose in 2005 by about 200 000 barrels per day. Demand in China is expected to expand by about 400 000 barrels per day in 2006. Global economic growth is also forecast to remain strong, and the IEA predicts that world demand for oil will rise by 1.8 million barrels per day in 2006.

As with oil, gas prices were high in 2005 because they are indexed against oil products in most long-term European gas contracts. In addition, the gas price in the UK – traditionally a commodity market – was very high at times.

According to figures from the IEA, gas consumption in Europe increased by 3.9 per cent in the first nine months of 2005 compared with the same period of 2004. Demand in the European market is expected to grow by just under two per cent annually from 2003-20, driven primarily by rising consumption of gas to generate electricity. At the same time, import requirements in Europe are growing as production in the continent falls. That has increased the focus on security of supply, and recent challenges relating to deliveries from Russia have made this issue even more relevant. With Langeled scheduled to become operational in the fourth quarter of 2006 and Ormen Lange due on stream in 2007, the SDFI is well positioned to participate in this growth. In addition, it is a partner in the Tampen Link pipeline which will to run from Norway to the UK via the British Flags system. This facility is due to become operational in late 2007.

The trading pattern for liquefied natural gas has meant a gradual globalisation of gas markets which were earlier very regional in character. Trading with LNG is currently based on a combination of long-term contracts and spot sales. New LNG projects, with associated transport and receiving terminals in the USA and Europe, are being pursued at a rapid pace. The SDFI is positioned in the LNG chain through its interest in Snøhvit. Its share of the Snøhvit gas has been sold to the Spanish and US markets.

The market expects oil prices to remain at relatively high during 2006, a little above the 2005 level. Good growth in the world economy and a supply position without the capacity to handle major production problems are both factors which point to high oil prices in the time to come. The market expects gas prices in the UK to be higher than in 2005. Long-term gas contracts indexed against oil products are also likely to see price rises in 2006 as a result of the high oil price over the past year.

SHARE CAPITAL AND SHAREHOLDER

The company's share capital at 31 December 2005 was NOK 10 million, divided between 10 000 shares. All the shares are owned by the Ministry of Petroleum and Energy on behalf of the Norwegian government. Petoro's business office is in Stavanger.

NET INCOME AND ALLOCATIONS

Administration of the portfolio by Petoro is subject to the accounting regulations for the government. The company maintains separate accounts for all transactions relating to the participatory interests, so that revenue and expenses for the portfolio are kept apart from operation of the company. Cash flows from the portfolio are transferred to the central government's own accounts with the Bank of Norway. The company prepares separate annual accounts for the SDFI, with an overview of the participatory interests managed by Petoro and associated resource accounting. Accounts for the portfolio are presented both on the cash basis used by the government and in accordance with the Norwegian Accounting Act and Norwegian generally-accepted accounting principles (NGAAP). All amounts cited in this report are based on NGAAP.

The company's operating expenses are covered by annual appropriations over the central government budget. Operating revenue for the year was NOK 177.9 million, comprising a net operating contribution of NOK 174.3 million from the government plus NOK 6 million in other revenue and deferred earnings less a net NOK 2.4 million in capitalised investment.

The government contribution for 2005 was NOK 217.9 million compared with NOK 203 million the year before. This sum includes VAT, so that disposable revenue was NOK 174.3 million as against NOK 163.7 million in 2004.

Operating expenses of NOK 177.9 million for the year, compared with NOK 166.7 million in 2004, related primarily to payroll expenses, administration expenses and the purchase of external services which include ICT and accounting. The purchase of leading-edge expertise relating to supervision of production licences in the SDFI portfolio accounts for a substantial proportion of the company's operating expenses.

Net financial revenue for 2005 was NOK 1 million, relating to interest on the company's surplus liquidity. This figure was on a par with 2004.

Profit after financial items came to NOK 0.9 million. The board proposes that this profit be allocated to other equity. The company's non-restricted equity totalled NOK 5.7 million.

Petoro's operating revenue takes the form of a contribution from the government, which is directly liable for the commitments accepted by the company under contract or in other forms. In accordance with section 3, subsections 3 and 2a of the Norwegian Accounting Act, the board confirms that the annual accounts for the portfolio and the company give a fair picture of the assets and liabilities, financial position and results of the business, and that the annual accounts have been prepared under the assumption that the company is a going concern.

Stavanger, 23 February 2006

Bente Rathe
Chair

Jørgen Lund
Deputy chair

Ingelise Arntsen
Director

Per-Christian Endsjø
Director

Nils-Henrik M von der Fehr
Director

John Magne Hvidsten
Worker director

Elen Carlson
Worker director

Kjell Pedersen
President and CEO

Emergence of glass and iron in architecture during the 19th century

Social and philosophic changes were not the only inspiration for artistic and architectonic developments. Scientific breakthroughs and new technological opportunities have also influenced aesthetic perceptions.

The expansion in manufacturing units during the Industrial Revolution created opportunities and capacity to use cast iron on a large scale for practical structures such as bridges. This is the world's oldest iron bridge, which was naturally built in Britain. The weight of the material in relation to its elasticity and load-bearing capacity made it very suitable for such purposes.

People were more reserved in adopting iron as a construction material for buildings. It was used as the load-bearing framework for theatres, factories and so forth in both Britain and France, but primarily for fireproofing. The iron components were concealed, being regarded as aesthetically uninteresting.

ABRAHAM DARBY:
Coalbrookdale Bridge, 1777-81, Shropshire, UK.



Four fatalities in 2005

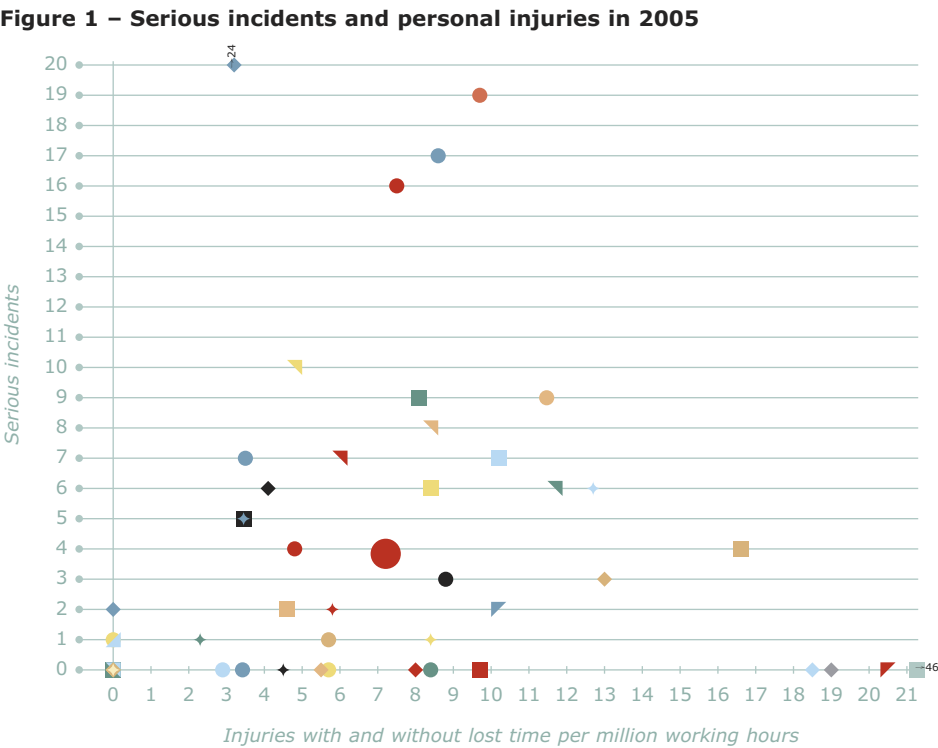
Four people lost their lives in accidents on or associated with installations where Petoro managed interests in 2005. These fatalities coloured the safety picture for the year. On the environmental side, oil discharges rose sharply, primarily as a result of large acute spill on Norne. Emissions of carbon dioxide and nitrogen oxides showed little change, while releases of volatile organic compounds (VOC) continued their downward trend.

The four deaths mean that 2005 will stand in any event as a poor year for Petoro in purely safety terms. Two of them occurred in connection with field developments – one during fabrication of the topsides for the Kristin platform at Stord and the other at the land-based terminal for Ormen Lange at Nyhamna in western Norway. A third was suffered during construction of the Aldbrough gas store in the UK, and a member of the crew on *Sally Knudsen* died in October while the vessel was berthed at Mongstad.

An average of 8.3 personal injuries were recorded per million working hours in 2005 at facilities in which the SDFI has interests. This means that Petoro’s goal of reducing this frequency from 2004 was not achieved. The average number of serious incidents was 3.6 per installation, just inside the target for a reduction.

Attention still needs to be sharply focused on safety, good management models and work to shape attitudes as an instrument for improvement. Petoro applies its own management system, which sets requirements for systematic work in the licences to improve HSE results. This includes regular bilateral management meetings with the largest operators. During 2005, Petoro participated in a number of management inspections on selected fields and installations where results had moved in a negative direction.

Each point on the graph presents an installation, and its placement indicates how this facility performed for personal injuries per million working hours and serious incidents in 2005. The large point represents the average for all the installations in the portfolio.



HENRI LABROUSTE:
Sainte-Geneviève Library, Paris, 1838-50.

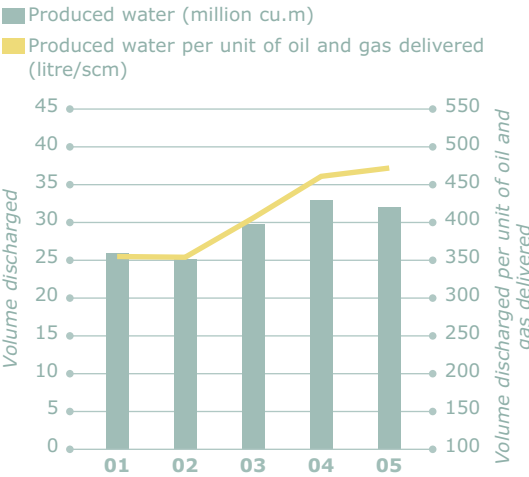
This building was the first large structure with glass and iron as its main elements, permitting a light and airy reading room. However, the internal iron frame has been clad in a stone box exterior of more traditional character. Typically, the interior ironwork has been cast in a form which apes the classical columns of stone architecture.



Three undesirable incidents were registered at Petoro’s offices in Stavanger during 2005, including a personal injury to a contractor employee working in the company’s premises. None of Petoro’s own personnel suffered injury.

Implementing zero discharges
Plans to achieve zero environmentally-harmful discharges, adopted by the industry in 2003, were due to be implemented during 2005. At 31 December, however, a number of fields had still failed to complete the necessary measures. Petoro will continue its work to meet the environmental requirements for reduced oil discharges. The main source of such discharges are oil residues in the produced water from the reservoir.

Figure 2 – Discharges of produced water and the volume of produced water per scm of oil and gas delivered



The graphs on discharges/emissions embrace all the fields and joint ventures managed by Petoro, and show the SDFI’s share of total discharges/emissions.

Formation water production and discharges to the sea have been growing in recent years, reflecting a rising water cut on many oil fields which are now in their mature phase. The curve for the portfolio’s discharges dipped slightly in 2005, owing to a significant increase in the quantity of produced water being pumped back below ground on fields in which Petoro manages large interests. However, the decline in discharges of produced water was smaller than the fall in oil and gas production, as figure 2 shows.

This year’s report has adopted a new standardised method for determining the quantity of dispersed oil in discharged formation water. The method gives rather lower discharges than the IS freon method used before. The graphs will accordingly differ slightly from those published in earlier Petoro annual reports.

Figure 3 – Discharges of oil to the sea

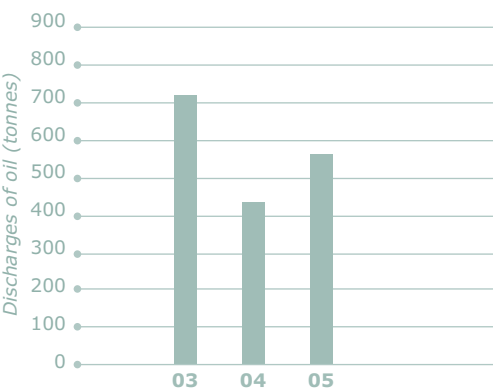


Figure 3 shows that total oil discharges from the portfolio increased by about 30 per cent from 2004 to 2005. The dominant contributor to this development was a large acute spill in 2005 on the Norne field, where Petoro is the licensee for a substantial interest. This also means that the total quantity of oil discharged to the sea increased more strongly for the portfolio from 2004 to 2005 than for the NCS as a whole.

Figure 4 – Carbon dioxide emissions

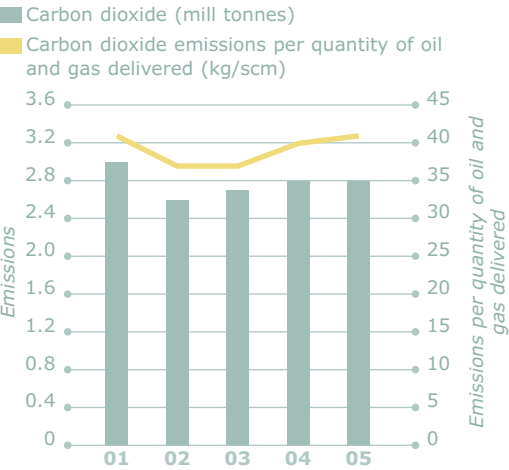


Figure 5 – Emissions of nitrogen oxides

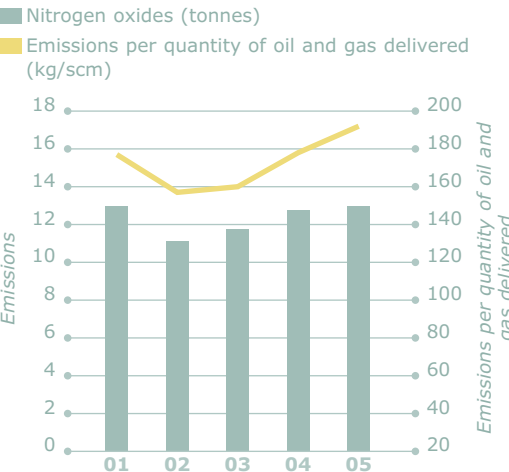
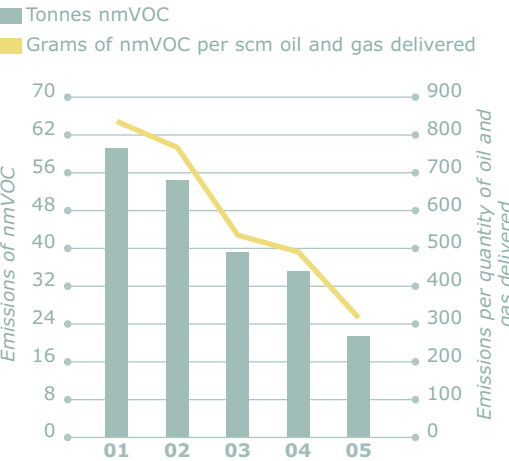


Figure 6 – Emissions of nmVOC



Emissions of carbon dioxide showed a marginal decline from 2004, compared with a marginal rise for the NCS as a whole. Figure 4 shows the emissions per quantity of oil and gas delivered in oil equivalent (oe).

Emissions of nitrogen oxides also changed only marginally from 2004, as indicated by figure 5. A slightly rising trend in 2004 and a slight decline in 2005 reflect increased production drilling from mobile units. Such rigs use diesel engines which emit significantly larger quantities of nitrogen oxides per kilowatt-hour than on fixed production installations where such emissions largely hail from gas turbines. However, the increase for the portfolio was smaller than for the NCS as a whole. That was because the biggest change in emissions from mobile units was experienced on fields where the SDFI has limited or no interests.

Emissions of non-methane VOC (nmVOC) displayed a marked decline from 2004 in terms of both the total emitted and emissions per quantity of oil and gas delivered. This trend has been under way since 2000, and primarily reflects the adoption of measures to reduce emissions from shuttle tankers and offshore storage facilities.



JOHN PAXTON:
Crystal Palace, London,
1851.

The Crystal Palace was constructed in central London to house the Great Exhibition of 1851. As the first structure wholly in iron and glass, it was built entirely from prefabricated sections in order to simplify disassembly and second-hand use. After the exhibition, it was moved to Sydenham in south London.

Management team for Petoro AS

Nina Lie,
chief financial officer



Olav Boye Sivertsen,
legal affairs



Roy Ruså,
technology and IT

Grete Willumsen,
human resources



Sveinung Sletten,
external affairs

Dag Omre,
commercial

Laurits Haga,
marketing and sales



Tor Rasmus Skjærpe,
licence management

Kjell Pedersen,
president and CEO



▲ FERDINAND DUTERT: Palace of
Machines, Paris, 1886-89.

► GUSTAVE EIFFEL: The Eiffel
Tower under construction.
Contemporary drawing, 1887-89.



The Palace of Machines was the main exhibition hall for the World Exposition of 1889, while the Eiffel Tower was constructed for the same event to demonstrate how high one could build in iron. The design of the latter was accordingly more functional than aesthetic, representing the form needed to reach a maximum height. Dutert and Eiffel belonged to a new generation of architects who had not studied art, like their predecessors, but were engineers by training.

Impressionism/Expressionism: the birth of modern painting



When photography arrived in the 1840s, it was initially perceived as a useful corrective for painters to see reality with “new eyes” and free themselves from old-fashioned painting conventions. But photographs quickly became a competitor and took over much of the lucrative portrait market, for instance.

A group of innovative painters staged an exhibition in Paris in 1874 where their leader, Monet, exhibited *Impression: Sunrise*. The title of this painting, which depicts a morning scene in the port of Le Havre, prompted a reviewer to dub the whole group “the Impressionists”.

Monet’s idea was that visible reality actually consists only of light and colours – which the photography of the day was unable to depict. As a result, the ripples in the foreground are seen more clearly than the big cranes and quays in the distance because we are looking down at the sea surface with the harbour installations backlit. The sun will soon rise higher in the sky, changing the visual conditions completely.

CLAUDE MONET:

Impression: Sunrise, 1874. Oil on canvas,
Musée Marmottán, Paris.

Double dividends

By Nina Morgan

Improved oil recovery (IOR) using carbon dioxide sounds in theory like an answer to the oil industry's prayers, offering benefits to both it and the environment. But although there are no serious technical barriers to implementation, this method has not been applied so far in Europe. So what does the future hold for using carbon dioxide to improve recovery? A recent European Commission report examined the issues.

Affordable and plentiful energy underpins European lifestyles and is an essential ingredient in economic prosperity. Yet the world is confronted at the start of the 21st century with the challenge of moving to a truly sustainable energy system – one that ensures we have access to the energy we need with minimal environmental damage.

Any technique which offers the potential for improved recovery from existing assets and consequent enhanced security of European energy supply, while reducing emissions of carbon dioxide – the dominant anthropogenic gas associated with global warming – has therefore got to be a good thing.

So carbon dioxide would seem an obvious choice. But although the use of carbon injection for IOR is being examined by a number of oil companies in Europe, and no technical barriers to its implementation appear to exist, it has not been used so far in Europe despite being commercialised elsewhere.

Why?

Economic factors such as the relatively high price of carbon dioxide, high capital and operating costs, particularly offshore, and the oil pricing regime of the past few years, are a major reason, according to *Enhanced oil recovery using carbon dioxide in the European energy system*. This report was published by the European Commission in December 2005 and prepared by the Directorate General Joint Research Centre at the Institute for Energy in the Dutch town of Petten.

But a detailed economic analysis for the report suggests that, at today's oil prices and if financial incentives are offered, a number of carbon injection projects for IOR could become viable in the North Sea. The

authors argue that this method would offer several advantages in Europe. It could enhance recovery from North Sea fields reaching the end of their productive lives, for instance, thus helping to improve the security of European energy supply while at the same time offering environmental benefits through carbon sequestration.

How does it work?

The fundamental principle involved in using carbon dioxide to improve recovery is simple. Supplies captured from power stations or other anthropogenic sources are injected into oil fields which have nearly reached the end of their producing lives to help recover some of the remaining oil. This generates an income which helps the overall economics of the process. When the field finally shuts down, the carbon dioxide would remain in the geological formations. Such storage is currently considered the best carbon sequestration option. In some cases, therefore, additional revenue could be earned through carbon emission credits or other forms of financial support.

From an environmental engineering viewpoint, sequestering carbon dioxide in oil and gas fields makes a lot of sense because it provides some assurance that any injected carbon would be stored for long enough to constitute a reasonable option for combating climate change. Geological carbon storage has been practised, albeit on a small scale, since the 1980s. The Sleipner project, where one million tonnes of carbon dioxide per year – equivalent to emissions from a 140-MW power station – are injected and stored in a saline aquifer in the North Sea, is currently the only commercial application of geological carbon storage. But the idea is catching on. Carbon injection into a gas field has begun recently at In Salah in Algeria, and a similar

project is being implemented on the Snøhvit gas field in the Barents Sea.

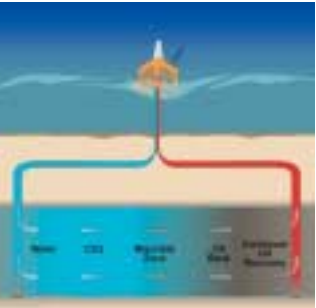
In a production engineering perspective, carbon injection appears to be a useful “tertiary” method for improving recovery. The primary method is normal pressure reduction, while secondary techniques involve water or gas injection. Injecting carbon dioxide into a reservoir mobilises oil not extracted by primary or secondary methods. In a North Sea context, the most interesting effect is that the carbon dioxide mixes with the crude, causes the volume of the oil to swell and reduces surface tension effects.

This improves the flowability of the oil and thereby boosts production. A tertiary recovery process of this kind, which is based on the miscibility of the carbon dioxide in the oil, is already regarded as a commercial technology and is used in some onshore fields in North America.

Immiscible displacement, in contrast, has not yet been commercialised and is not an option currently being looked at in the North Sea. This article will accordingly give no further consideration to that alternative.

Data from onshore applications in the USA show that carbon injection can increase oil recovery by nine to 18 per cent beyond what is achievable using conventional recovery methods. However, the exact increase depends on the injection method used and the characteristics of each oil reservoir and its crude oil. When deciding on the feasibility and economics of carbon injection for IOR, account must accordingly be taken of the individual characteristics of each reservoir as well as field location.

Given that well spacing is also wider offshore because of cost, economics and operating conditions are more challenging in such projects. Nevertheless, although preliminary reservoir modelling indicates that probable oil recovery rates in the North Sea will be lower than in the USA, the calculations suggest that the additional production should still be significant.



Water injection is a secondary production technique which works primarily by providing pressure support in the reservoir. Carbon dioxide has the additional effect that it mixes with the oil and makes it flow more easily through the reservoir. This figure shows than water and carbon injection can be combined. Illustration: Hydro

Potential costs and benefits

This estimate is based on data from 81 active oilfields in the UK, Norwegian and Danish sectors of the North Sea with reserves of more than 73 million barrels. By estimating the maximum potential for additional oil recovery from carbon injection in each field, the EU report’s authors suggest that an average of 4.2 billion barrels could be recovered from Norwegian fields. By comparison, the average potential additional recovery is put at 2.7 billion barrels for the UK and 400 million barrels in the Danish sector. It can be mentioned that the Norwegian Petroleum Directorate has estimated a technical potential of around two billion barrels from some 20 fields on the NCS.

The economics of carbon injection on 15 North Sea oil fields which are more than 80 per cent depleted were also considered by the report. This assessment took account of various oil recovery factors, price scenarios and carbon trading prices. The analysis assumed that the carbon dioxide would be sourced from existing land-based coal-fired power stations and would be transported to each field in a dedicated pipeline.

The authors concluded that, under favourable oil recovery factors (nine to 18 per cent of extra recovery, a 10 per cent discount rate and ignoring taxes and inflation) and a low price scenario of USD 25 per barrel for oil and EUR 15 per tonne of carbon stored through emission trading, carbon dioxide injection could be economically viable in nine of the 15 fields.

This economic analysis suggests that, if financial incentives for carbon storage were available, carbon injection projects in the North Sea would be financially viable. The authors calculate, for example, that such

In order to explore his Impressionist theories, Monet found it natural to work in series where he painted the same scene at different times of the day and under varying weather conditions. This was intended to show that “reality” is a relative concept, which depends entirely on colour and light. Painting became a kind of research project. The *Gare St Lazare* is one of Monet’s first series, which typically enough depicts the hectic life of a railway station – the very heart of a city’s communication system and itself a symbol of modern life. The smoke billowing from the new locomotive speed demons was also very suitable as a subject for the Impressionists.

CLAUDE MONET:
Interior of the Gare Saint Lazare, 1877.
Oil on canvas, Musée d’Orsay, Paris.



CLAUDE MONET:
Gare Saint Lazare, 1877,
Fogg Art Museum,
Cambridge.



CLAUDE MONET:
The Rome Platform (Gare Saint Lazare). 1877,
Musée Marmottán.



injection would be profitable in a price scenario of USD 35 per barrel for oil and EUR 25 per tonne for carbon stored through emission trading in all the fields studied. With Brent crude selling in the range of USD 50-60 per barrel for a long period, the economics must be even more favourable. Under optimal conditions, carbon injection projects in the North Sea could potentially yield up to 180 million barrels of oil annually while simultaneously storing up to 60 million tonnes of carbon dioxide.

What’s stopping us?

Nevertheless, in contrast to the USA, carbon injection for IOR is not yet taking off in Europe. One reason is differences in development solutions between land-based and offshore fields.

Another factor, the report suggests, is the cost of obtaining carbon dioxide in Europe. In the USA and Canada, large amounts of carbon dioxide are captured for IOR use from six chemical and gas treatment plants, and is also present in some cases in underground natural reservoirs near the injection sites. As a result, supplies are often available in large quantities at low cost. By contrast, large combustion plants such as power stations located on land are the main potential source of carbon dioxide for IOR in European offshore oil fields.

This poses some additional challenges and adds to the cost. Before it could be used, for example, the carbon dioxide would have to be separated from the flue gases. But large-scale carbon separation and capture from power stations has yet to be demonstrated commercially. The carbon dioxide would then have to be transported to the injection sites, and because the majority of European oil fields are located offshore and at a significant distance from land-based power stations, a carbon transport infrastructure would need to be developed.

While these challenges could be overcome in technical terms, the expense of carbon capture, transport and injection would add significantly to oil production costs. This has tended to make the economics of carbon injection on European fields seem prohibitive under the oil-pricing regime of the past few years, especially in light of the high operating and capital expenses associated with offshore projects.

A further economic drawback is uncertainty about eligibility for financial support. Because environmental concerns over the permanence and safety of underground carbon storage are prompting questions about injection for this purpose, it is uncertain whether carbon storage associated with injection for IOR would qualify for financial incentives via mechanisms such as emission trading.

Times are changing

However, the European energy scene is changing – and so could the prospects for introducing carbon injection. On the environmental side, the urgent need to curb carbon emissions in compliance with the Kyoto commitments and beyond means that political attitudes are changing. As a result, capture and storage technologies are among the major carbon mitigation options being considered (see, for example, www.co2captureproject.org).

Although the direct impact of carbon injection on reducing greenhouse gas emissions would apply mainly to carbon sources in those countries, mainly around the North Sea, closest to the oil fields, this IOR approach would help all EU members by supporting the Lisbon strategy. Aiming to make the EU the most dynamic and competitive knowledge-based economy in the world by 2010, this strategy offers new incentives and opportunities for developing advanced energy conversion technologies based on the decarbonisation of fossil fuels. In addition, the knowledge gained through implementing carbon injection projects in the North Sea could be applied to other geological storage projects for the gas elsewhere in Europe.

From an economic perspective, even though the roughly five billion tonnes of carbon storage capacity in North Sea fields is a drop in the ocean compared with the four billion tonnes of greenhouse gases emitted annually in the EU, the European Union allowance (EUA) emission trading scheme is likely to provide some financial incentive to implement carbon injection for IOR. In addition, higher oil prices may now justify investment in oil recovery projects previously deemed uneconomic. All in all, this suggests that carbon injection could well be an economically viable option in the North Sea.

And the time to start taking action is now, the report urges. With many important oil fields in the North Sea reaching the end of their producing lives, oil companies are currently considering their options for abandonment. Once the oil recovery infrastructure is dismantled completely, it will be too late. And this would be an important opportunity lost, the report authors argue.

Petoro asked freelance science writer Nina Morgan to produce this article on the basis of information in the EUR 21895 report on *Enhanced oil recovery using carbon dioxide in the European energy system*, compiled by E Tzimas, A Georgakaki, C Garcia Cortes and S D Peteves of the DG JRC Institute for Energy at Petten in the Netherlands. This report does not necessarily represent the views of the European Commission.

Based in the UK, Dr Morgan (nina@morgan@lineone.net) has a PhD in earth sciences and worked in oil exploration for seven years before turning to science writing in 1986.

Petoro found the EU report of interest in relation to its own work on identifying candidate oil fields for carbon injection on the Norwegian continental shelf. However, the EU report does not necessarily reflect the views of Petoro.

Carbon dioxide injection: important for improving the recovery factor

It is hard to find injection media other than carbon dioxide which could be made available in sufficient quantities during the final stages of a field’s producing life to reach Norway’s official oil recovery target, says Jan Rosnes. He is project manager for Petoro’s assessment of fields which could be candidates for carbon injection to raise the average recovery factor from today’s 46 per cent to the Norwegian Petroleum Directorate’s goal of 55 per cent.

A dedicated project team is at work in Petoro during the spring of 2006 to identify fields where injecting carbon dioxide could yield the best value creation. Being pursued on behalf of the Ministry of Petroleum and Energy, this job forms part of a broader project looking at opportunities for creating a carbon value chain. That work is being coordinated by Gassco, which is due to submit a report to the government on 1 June.

Mr Rosnes is normally Petoro’s asset manager for the Oseberg/Grane area, but has been seconded to head the carbon project. He notes that Petoro has worked since its foundation in 2001-02 to improve recovery from the mature areas of the NCS. As the former manager of the company’s commitment in the Tampen area, he was heavily involved in 2003-04 with the issue of carbon injection on Gullfaks.

“We worked together with the two other licensees, Statoil and Hydro, to improve recovery from this important Norwegian field,” he recalls. “At our initiative, the water injection programme was amended and the results were so good that they actually ‘consumed’ part of the potential for later carbon injection. This was one reason why we concluded, after a couple of extra rounds in the spring of 2004, that a carbon project on Gullfaks was not sufficiently profitable.”

Nor did the Norwegian Petroleum Directorate, in a report published in the spring of 2005, find it economic to adopt carbon injection unless oil prices came close to USD 30 per barrel. But Mr Rosnes notes that three significant factors have subsequently changed. The oil companies have upgraded their long-term oil price expectations from about USD 20 per barrel to roughly USD 30, the cost of European Union allowances (EUAs) for carbon emissions has settled at a higher-than-

expected level of EUR 20-25 per tonne, and technology developments are reducing carbon capture costs.

Mr Rosnes also finds it positive that the question of using carbon dioxide on the NCS no longer stands or falls with Gullfaks. “Both the seven fields we’ve identified and the collaboration announced between Statoil and Shell on a carbon value chain for injection in Draugen and Heidrun show that a number of projects are relevant,” he says, and envisages that the first step could be carbon injection in one large field or in several smaller ones. The number of fields and their size will depend to a great extent on the availability of carbon dioxide and its price.

Producing an oil field typically involves three phases, explains Arve Mamre, the reservoir specialist in Petoro’s carbon dioxide team. Primary recovery is achieved by drilling wells and producing oil through pressure reduction. Secondary recovery involves pressure support by pumping water or gas into the reservoir. And tertiary recovery could mean pumping down carbon dioxide which – under specific conditions – blends with the crude and makes it flow more easily through the reservoir. More oil can thereby be recovered. Carbon injection can improve recovery on some fields, but not all.

This technique is well known from US fields, Mr Mamre notes. American experience can be adapted to fields on the NCS to yield a substantial potential for value creation. Carbon injection has been studied in detail on Gullfaks, and the expected improvement in oil recovery amounts to well over 100 million barrels.

Mr Rosnes finds it difficult at the moment to envisage injection media other than carbon dioxide which would



The carbon dioxide team. From left: Svein Helland, Arve Mamre, Sonja Ytreland and Jan Rosnes.

be available in the quantities needed to meet the NPD’s target of a 55 per cent recovery factor for the NCS.

“I wouldn’t exclude the possibility that alternative methods for tertiary recovery, such as the use of surfactants (detergents) or other chemicals, could be simpler and perhaps more economic for smaller fields when viewed in isolation. But if we’re going to raise the average NCS recovery factor from today’s 46 per cent to 55 per cent, my view for now is that we’ve got to use carbon dioxide to get worthwhile volumes.”

On Petoro’s work, he says that about 40 fields were subject to a simplified review before seven were selected for more detailed examination. These are Draugen in the Norwegian Sea, Gullfaks, Sygna, Oseberg East and Brage in the northern North Sea, Volve in the Sleipner area and Gyda at the southernmost end of the NCS. Petoro’s final recommendation is likely to involve a further reduction in candidates for the first step towards a carbon project.

Criteria for selecting a field are reserves in place, the expected recovery factor and the effect that carbon injection is likely to have on this factor. That in turn will influence the earnings potential.

However, cost is another important consideration. Sonja Ytreland in the carbon team is looking at processing

facilities and such factors as the materials used in wells, pipelines and plants. “By comparing earnings potential with costs, we get an indication of the ability of each field to pay for carbon injection” she says. “That’ll be crucial in the selection process.”

The location of a field in relation to possible carbon dioxide sources will also be important. Before Gassco submits its report, Petoro’s choice of potential fields will be compared with the list of possible carbon sources being drawn up by the Gassnova company.

Asked whether he sees perspectives for carbon injection beyond an initial limited project, Mr Rosnes says that he thinks a possible first step will make this an interesting value creation opportunity for several fields in the same area.

“And if we’re first going to talk about perspectives, it’s also possible to look at the high carbon dioxide content in many Norwegian Sea gas fields and discoveries. We could separate this substance out and use it for injection in nearby oil developments. That would increase the value of both gas discoveries – which can dispose of unwanted carbon dioxide – and oil fields.”

But he admits that this is speculation, and that it is challenging enough for the moment to achieve profitability for an initial carbon value chain on the NCS.

Gauguin exhibited initially together with the Impressionists. But he painted *The Vision After the Sermon (Jacob Wrestling with the Angel)* with big, strong, almost monochrome blocks of paint in a “synthetic” style. This painting depicts how deeply-religious Breton women in a churchyard experience the story of Jacob’s fight with the angel through their inner eye, immediately after hearing about it in a sermon. In other words, it does not present visible reality, but a spiritual inner one. We get not an *impression* but an *expression*.

PAUL GAUGUIN: *The Vision After the Sermon (Jacob Wrestling with the Angel)*, 1888. Oil on canvas. National Gallery of Scotland, Edinburgh.



Improving governance boosts value creation

The revenue flow from the 10-15 largest fields on the NCS bears comparison with earnings by the biggest companies in mainland Norway. Stronger governance by owners in production licences on the NCS will help to enhance value creation.

One goal for governance in production licences is to get licensees to pull in the same direction. A key element in this context is to define collective long-term ambitions for enhancing production and cost efficiency, says Nina Lie, Petoro’s chief financial officer. She is backed by Jan Rosnes, the company’s asset manager for the Oseberg area.

“It’s 40 years since the first licensing round on the Norwegian continental shelf, and we’ve naturally enough ended up today with a patchwork of different agreements which regulate the exercise of ownership in the licences,” she notes.

Work on strengthening governance in the licences was stepped up after the Ministry of Petroleum and Energy asked the oil companies to propose an improved structure for joint operating agreements. Ms Lie, who has played a key role in this work within the Norwegian Oil Industry Association (OLF), says that it will harmonise agreements between all the licences. This in itself will make their work more efficient.

Joint venture benefits

“A licence is legally-speaking a joint venture, a form of ownership with many advantages which we must utilise better in the future management of resources on the NCS,” she observes. “This mode of organisation involves sharing risk and power in a long-term operational venture. To ensure efficient collaboration in the venture, it is crucial that the joint operating agreement contributes in a clear way to an appropriate division of roles whereby the operator handles the day-to-day management and the licensees take all significant decisions jointly.”

“Governance models which place the emphasis on framing strategies as well as performance and risk management will lead to a focus on management of measures and non-conformances by the joint venture.

The operator, for its part, must be given the necessary opportunity to work undisturbed as long as it stays on target. We’ve emphasised standardisation, simplification and firming up the licence’s reporting requirements. That requires the joint venture to shift its attention towards short- and long-term measures which can yield greater volume and cost efficiency. In that way, this work could contribute to increased value creation from the NCS.”

Another benefit of the joint venture as a form of ownership is its suitability for utilising the diversity of expertise possessed by Norwegian and foreign oil companies. Ms Lie believes that this overall expertise can be further exploited if the owners jointly strengthen the licence’s decision-making processes for ensuring efficient collaboration in a project’s early phase.

Openness and cooperation

“My experience from working in licences is that the partners are often involved too late in important decision-making processes,” Mr Rosnes says. “When major investment projects are involved, it’s crucial that the licensees who share the risk and profits collectively retain overall control. We have a potential for improvement here.”

Both he and Ms Lie believe that Petoro’s entry as a big new licensee has made a significant contribution to putting the issue of better governance on the agenda. “In that respect, it’s very important that the Storting (parliament) opted to give us an active partner role rather than creating a pure financial administrator/investor,” says Ms Lie. “This has also given us real ownership power in relation to the way decisions are taken and joint ventures managed.”

The division of costs between operator and partners in the licences has been a central issue in drawing up the new agreements. Ms Lie notes that the NCS faces



Far left: Jan Rosnes, asset manager
Left: Nina Lie, chief financial officer

declining production and rising unit costs. Given that background, clear rules and transparency are also important when charging costs.

She emphasises that implementing the new joint operating agreement is intended to encourage a governance characterised by openness and cooperation between the licensees. “That’ll allow us to make better use of the overall expertise in the industry in order to meet our collective challenges.”

Mr Rosnes notes that the concept of “corporate governance” in companies has existed since the mid-1970s. But it has become increasingly relevant in recent years, not least as a result of major international business scandals – and also through incidents relating to governance of operations on the NCS. A case in point is the public attention which has been given to delays and cost overruns in the Snøhvit project.

Stronger involvement by owners

“Big efforts have been made from many quarters to strengthen owner involvement in and improve governance in limited companies,” Mr Rosnes notes. “But we’ve also seen growing interest in better governance of the joint ventures which operate the major oil and gas fields on the NCS”.

On the positive side, the asset manager highlights one example of joint venture governance which he regards as both bold and innovative. When the Gullfaks licensees were collectively awarded the Norwegian Petroleum Directorate’s prize for improved oil recovery, the jury praised the good governance of the venture by the licensees.

“Through our broad portfolio, we’ve been able to observe that many of the big fields are managed and controlled in different ways, and that a significant improvement potential is offered through learning and the development of best practice,” Mr Rosnes notes. “Unified and efficient corporate governance models are intended to secure and develop value for the owners – and that also applies to licensees on the NCS.”

Mr Rosnes has written a more extensive article on offshore governance, based on Petoro’s model for best practice. He points here to the way the framework for management and control is intended to create a good interaction between all the interests in a production licence and to provide a foundation for the way the joint venture plans, supervises and manages activities in line with its strategy. In this article, which has been posted (in Norwegian only) to Petoro’s website at www.petoro.no, Mr Rosnes describes the principles for corporate governance and how they can be implemented in joint ventures on the NCS through a future governance model.

In the painting below, Munch has gone even further than Gauguin in removing himself from visible reality in that he expresses a condition of the soul – angst – by describing a sound. A scream shapes the figure’s head as a kind of (sound) wave, which spreads out into space. This creates a striking Expressionist image of something which takes place in the artist’s soul under given circumstances. “I want to describe what can’t be photographed, Heaven and Hell,” Munch wrote.

EDVARD MUNCH:
The Scream, 1893.
Oil on canvas,
Nasjonalgalleriet, Oslo.



Schmidt-Rottluff was a key figure in the Die Brücke group, which emerged in Dresden in 1905. Their Expressionism took the form of paintings which sought to achieve the most intense expression possible through crude forms and brutal colours. The subject accordingly played almost no role, the expression was everything.

KARL SCHMIDT-ROTTLUFF:
Portrait of Rosa Schpire, 1911.
Oil on canvas, Die Brücke Museum, Berlin.



Vitalism/Cubism in the early 20th century



A great enthusiasm for the future arose at the beginning of the 20th century, inspired in part by the rapid development of both science and technology. Inventions such as film, cars and aircraft meant that artists had to reassess their own medium, and find a stylistic language and expression which seemed meaningful and modern in relation to the furious pace of progress they experienced around them.

EDVARD MUNCH:
Bathing Boys, 1904. Oil on canvas.
Munch Museum, Oslo.

The belief that the new century marked the transition to a fundamentally new society and reality found initial form through a vitalised classicism, in which the artist hailed the sound and strong, with men bathing in sunshine and health. In typical fashion, Munch – who was inspired by Darwin – gives the swimmers the shape of frogs and octopi, which he explains as the refraction of light through the water.

Corporate governance

Good corporate governance is characterised by a responsible interaction between a company’s owners, board and management in a long-term value creation perspective.

Corporate governance in Petoro builds on its overall goal, which is to create the highest possible financial value from the State’s Direct Financial Interest (SDFI) on the NCS. By observing the principles for good corporate governance, the company aims to secure the trust of its owner, employees, the oil industry and other stakeholders as well as the community at large.

Petoro is a limited company wholly owned by the Norwegian state. Its operations are subject to the Act on Limited Companies and the Petroleum Act, and to the government’s financial regulations – including the rules on appropriations and accounting. The Ministry of Petroleum and Energy’s instruction for financial management of the SDFI and the annual Letter of Award are among the company’s topmost governing documents. Petoro presents separate accounts for the SDFI portfolio’s transactions. Cash flows generated from the portfolio are transferred to the government’s own accounts with the Bank of Norway. The company’s operating expenses are covered by annual appropriations over the central government budget.

The company is the licensee for 100 production licences and 12 joint ventures for pipelines and terminals. Petoro has the same rights and obligations as the other licensees.

Petoro gives weight to transparency and communication in-house and externally, in part through its website and through the publication of quarterly and annual results.

The company has clear guidelines on business ethics, and requires that all its employees confirm annually that they have studied and accepted these. Rules on commercial ethics also form part of the company’s standard contracts with its suppliers.

Petoro is responsible for monitoring Statoil’s marketing and sale of the government’s petroleum. Since the government is the majority shareholder in Statoil and the sole owner of Petoro, it pursues a common ownership strategy through the marketing and sales instruction adopted by Statoil’s general meeting. Petoro’s board and members of the company’s management are included on Statoil’s register of primary insiders with the Oslo Stock Exchange. In-house guidelines have also been established for insider trading in shares, together with a special system for approving external directorships held by employees.

Governing bodies

The Ministry of Petroleum and Energy, in the person of the minister, represents the government as sole owner and serves as the company’s general meeting and highest authority. The annual general meeting is held before the end of June each year. The Petroleum Act lays down guidelines on issues to be considered by the company’s general meeting. The general meeting elects the board of directors, with the exception of the worker directors, and determines its remuneration. The general meeting elects the company’s external auditor. Remuneration for directors and company employees does not include bonus schemes.

Bente Rathe is chair of the company, with Jørgen Lund as the deputy chair. The other directors elected by the company’s general meeting are Ingelise Arntsen, Per-Christian Endsjø and Nils-Henrik M von der Fehr. The worker directors are Elen Carlson and John Magne Hvidsten. Directors normally serve for two-year terms. They have no commercial agreements or other financial relations with the company other than the agreements on directors’ fees and contracts of employment for the worker directors. No member of the company’s management sits on the board. The board is responsible for the overall management and supervision of Petoro, which includes ensuring an acceptable organi-



PABLO PICASSO:
The Two Brothers, 1906.
Oil on canvas, Kunstmuseum, Basle.

sation of the business. The board determines the company’s goals, strategy and budgets, and is also responsible for the quarterly accounts for the limited company and the portfolio. It must ensure that overall management and control systems are tailored to the scope of the business and its risk picture. An annual evaluation related to the management of the company’s risk picture is carried out by the board, along with an annual self-assessment of its own work and its cooperation with the company’s management. The board appoints the president and CEO, and determines his remuneration. Petoro’s rules of procedure for the board provide an important basis for the board’s management of the business. It specifies the division of authority and provides guidelines about which issues must be submitted to the directors by the president and CEO.

Petoro’s management team comprises the president and CEO, Kjell Pedersen, as well as vice presidents Grete Willumsen, Roy Ruså, Sveinung Sletten, Olav Boye Sivertsen, Laurits Haga, Dag Omre, Tor Rasmus Skjærpe and Nina Lie. Day-to-day management of the company’s operations is the responsibility of the president and CEO, who reports monthly to the board on the company’s financial progress and position. He also reports regularly on the status of the business and other conditions of substantial strategic or financial significance for the company’s operations.

Details of the actual remuneration paid to directors and to the president and CEO are provided in the notes to the Petoro accounts.

Auditing and internal control

The Auditor General is the external auditor for the SDFI portfolio and submits an annual auditor’s report to the company’s board. Petoro’s internal audit is a control body which supports the company’s board and management in discharging their responsibility to exercise control pursuant to statutory requirements. The internal auditor reports to the vice president finance and works in accordance with instructions determined by the board. To ensure an independent and objective internal audit, the internal auditor can report directly as and when required to the president and CEO or the board. The annual plan for internal auditing is adopted by the board, which also receives reports on its implementation, and is based on assessments of the company’s activities for the coming year and risk assessments made by the company’s organisation, management team and board.

Deloitte has been engaged to conduct an internal financial audit of the portfolio’s accounts, and submits an annual auditor’s report in accordance with Norwegian auditing standards. Erga Revisjon AS is the external auditor for Petoro AS.

Petoro’s internal control function is intended to ensure that the company operates in accordance with the established governance model, and that the business is subject to satisfactory management and control.

Financial statements 2005

SDFI appropriation accounts

Expenses and revenue	Note	NOK
Removal		0
Pro and contra settlements (payments)		686 004
Investment	2	20 701 299 004
Total expenses		20 701 985 008
Pro and contra settlements (receipts)		(1 083 252)
Operating revenue	3, 4	(144 181 514 144)
Operating expenses	5	24 289 045 688
Exploration and field development expenses		978 364 291
Depreciation	2	12 914 083 658
Interest	6	6 670 289 165
Operating income		(99 329 731 341)
Depreciation	2	(12 914 083 658)
Transfer from Govt Petroleum Insurance Fund	9	(887 568 860)
Interest on fixed capital	6	(6 646 122 298)
Interest on intermediate accounts	6	(24 166 867)
Total revenue		(119 802 756 278)
Cash flow (net revenue from the SDFI)		(99 100 771 270)

SDFI capital accounts

Items	Note	NOK	NOK	NOK
Open account government 31 Dec 05				(737 453 442)
Real investments before write-down		128 906 035 780		
Write-down	2, 9	(28 146 071)		
Account for real investments	2, 8	128 877 889 709	128 877 889 709	
Total			128 140 436 268	
Open account government 1 Jan 05		663 236 167		
Total expenses	20 701 985 008			
Total revenue	(119 802 756 278)			
Cash flow	(99 100 771 270)	(99 100 771 270)		
Net transfer to the government		99 174 988 545		
Open account government at 31 Dec 05		737 453 442	737 453 442	
Fixed capital 1 Jan 05		(121 118 820 435)		
Investments for the year		(20 701 299 004)		
Depreciation for the year		12 914 083 658		
Write-down	2, 9	28 146 071		
Fixed capital 31 Dec 05	2, 8	(128 877 889 709)	(128 877 889 709)	
Total			(128 140 436 268)	

Stavanger, 23 February 2006


Bente Rathe
Chair


Jørgen Lund
Deputy chair


Ingelise Arntsen
Director


Per-Christian Endsjø
Director


Nils-Henrik M. von der Fehr
Director


John Magne Hvidsten
Worker director


Elen Carlson
Worker director


Kjell Pedersen
President and CEO

SDFI income statement

All figures in NOK million	Note	2005	2004	2003*
OPERATING REVENUE				
Operating revenue	3, 4, 9, 10	152 683	120 807	101 699
Total operating revenue		152 683	120 807	101 699
OPERATING EXPENSES				
Exploration expenses		543	473	440
Depreciation and amortisation	2, 12	14 051	15 656	15 081
Other operating expenses	5, 9, 10, 11	25 020	21 025	17 557
Total operating expenses		39 614	37 154	33 078
Operating income		113 069	83 653	68 621
FINANCIAL ITEMS				
Financial income		3 056	3 542	1 608
Financial expenses		2 953	4 852	2 075
Net financial items	7	103	(1 310)	(467)
Net income for the year		113 172	82 343	68 154

*Figures for 2003 have been revised to reflect the change of principles for abandonment and removal (note 12).

GUSTAV VIGELAND:
Man With Woman in His Arms, 1905 and 1915.
Vigelandsmuseet, Oslo.

These two variants of the same subject show how
a development has occurred over a decade, with
the bodies exuding more vitalist potency.



SDFI balance sheet at 31 December 2005

All figures in NOK million	Note	2005	2004	2003*
Intangible fixed assets		1 241	999	1 005
Tangible fixed assets		140 990	130 869	127 231
Other fixed assets		7	10	14
Fixed assets	2	142 238	131 878	128 249
Stocks		505	469	360
Trade debtors	10, 11	20 693	11 607	10 627
Bank deposits		76	75	113
Current assets		21 274	12 151	11 101
Total assets		163 512	144 029	139 350
Equity at 1 January		120 530	119 427	120 289
Paid from/(to) government during the year		(99 175)	(81 401)	(69 005)
Net income		113 172	82 343	68 154
Conversion differences**		27	161	(11)
Equity	18	134 554	120 530	119 427
Long-term removal liabilities	12	18 538	14 930	13 320
Other long-term liabilities	13	648	1 001	618
Long-term liabilities		19 186	15 931	13 938
Trade creditors		1 966	1 679	1 793
Other current liabilities	10, 14	7 805	5 889	4 193
Current liabilities		9 771	7 568	5 986
Total equity and liabilities		163 512	144 029	139 350

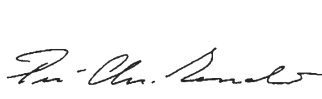
*Figures for 2003 have been revised to reflect the change of principles for abandonment and removal (note 12).
**Relating to conversion difference and settlements after the 2001 asset sale.

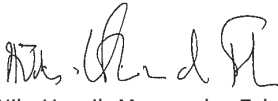
Stavanger, 23 February 2006

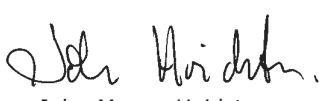

Bente Rathe
Chair

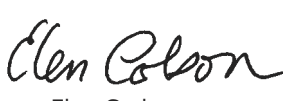

Jørgen Lund
Deputy chair

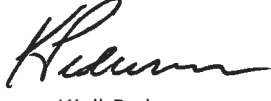

Ingelise Arntsen
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Director


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Worker director


Elen Carlson
Worker director


Kjell Pedersen
President and CEO

SDFI cash flow statement

All figures in NOK million	2005	2004	2003
CASH FLOW FROM OPERATING ACTIVITIES			
Cash receipts from operations	146 839	120 956	101 888
Cash disbursements to operations	(25 407)	(21 123)	(16 664)
Net financial outflow	749	(1 013)	(179)
Net cash flow from operational activities	122 181	98 820	85 045
CASH FLOW FROM INVESTMENT ACTIVITIES			
Investments	(19 661)	(16 492)	(14 465)
Cash flow from investment activities	(19 661)	(16 492)	(14 465)
CASH FLOW FROM FINANCING ACTIVITIES			
Change in current liabilities	(2 990)	(1 374)	(465)
Change in long-term liabilities	(353)	383	(922)
Net transfer to the government	(99 175)	(81 401)	(69 005)
Pro and contra from government sale	0	25	(112)
Cash flow from financing activities	(102 518)	(82 367)	(70 503)
Increase in bank deposits of land-based partnerships	1	(39)	76



JENS FERDINAND WILLUMSEN:
A Female Mountaineer, 1912. Statens Museum for Kunst, Copenhagen.

This lady in walking dress is apparently in Norway’s Jotunheimen range. Through their shape and size, the mountains represent something of the most potent in nature and were sufficiently “natural” for a Danish painter. But this is not a tourist poster. It depicts the commitment and vitalist attitude of the woman. She is not out for a stroll, she is conquering the mountain.

SDFI notes



PABLO PICASSO:
Les Demoiselle d'Avignon, 1907. Oil on canvas, Museum of Modern Art, New York.

Picasso considered it unsatisfactory to use references to the past, such as Classicism. He questioned the whole three-dimensional form which had dominated European painting since the Renaissance. As a kind of parallel to developments in such sciences as physics and chemistry, he explored a new concept for space, time and the relationships between the three-dimensional and the two-dimensional canvas. This gave rise to Cubism, and its first great work was this painting. A number of later “isms” are based precisely on Cubism’s artistic idiom.

ACCOUNTING PRINCIPLES

General

Petoro’s object is to be responsible for and manage the direct financial interest related to the SDFI portfolio and related operations. The company’s overall goal is to maximise the total value of the portfolio on a commercial basis. Petoro served at 31 December 2005 as the licensee for interests in 100 production licences and 12 joint ventures covering pipelines and terminals. The company also manages the government’s commercial interests in Mongstad Terminal DA, Etanor DA and Vestprosess DA as well as the shares in Norsea Gas AS and Norpipe Oil AS. It has the same rights and obligations as other licensees, and manages the SDFI on the NCS on a commercial basis. Petoro maintains separate accounts for all the transactions relating to its licence shares, so that revenue and costs relating to the SDFI portfolio are separated from the operation of the company. Cash flows from the portfolio are transferred to the central government’s own accounts with the Bank of Norway. Petoro prepares separate annual accounts for the SDFI, with an overview of the participatory interests managed by the company and associated resource accounting. Administration of the portfolio by Petoro is subject to the accounting regulations for the government. Accounts for the portfolio are presented both on the cash basis used by the government and in accordance with the Norwegian Accounting Act and Norwegian generally-accepted accounting principles (NGAAP).

Accounting principles (NGAAP)

The SDFI’s interests in limited companies and partnerships with shared liability (land-based partnerships) relating to the production of petroleum are included under the respective items in the income statement and balance sheet in accordance with the proportionate consolidation method for the SDFI’s share of income, expenses, assets and liabilities. In addition, revenue and expenses from production licences with net profit agreements (relates to licences awarded in the second licensing round) are recorded as other income using the net method for each licence.

GENERAL RULE FOR VALUATION AND CLASSIFICATION OF ASSETS AND LIABILITIES

Assets intended for permanent ownership or use in the business are classified as fixed assets. Other assets are classified as current assets. Debtors due within one year are classified as current assets. Classification of current and long-term liabilities is based on the same criteria.

Tangible fixed assets and investments are recorded in accordance with the Norwegian Accounting Act and NGAAP. Fixed assets are carried at historical cost with a deduction for planned depreciation. Should the fair value of a fixed asset be lower than the book value, and this decline is not expected to be temporary, the asset has been written down to its fair value. Expenses for major alterations and renewals which significantly increase the economic life of fixed assets are also capitalised. Replacements of fixed assets are expensed. Fixed assets under construction are carried at historical cost. Should the fair value be lower than the book value, the asset under construction will be written down to its fair value. The SDFI does not take up loans, and incurs no interest expenses associated with financing development projects.

The SDFI’s installations in operation can be broken down into the following categories:

- field installations and facilities, including production wells, which include oil and gas production installations and in-field transport systems
- pipelines used by more than one field, riser platforms and land-based plants
- machinery, fixtures and fittings, etc.

Current assets are assets not classified as fixed. They are valued at the lower of historic cost and fair value. Current liabilities are valued at their face value. Creditors due within one year are classified as current assets. The first year’s instalment on long-term debt is classified as a current liability.

FOREIGN CURRENCIES

Monetary items in foreign currencies are valued at the exchange rate prevailing on the balance sheet date. Unrealised currency losses and realised currency gains and losses are recorded as financial income or expenses.

STOCKS

The principle for valuing stocks accords with the general valuation principle for current assets. The lower of cost or net realisable value rule is applied for valuing stocks of spare parts and operating materials.

Spare parts of insignificant value for use in connection with the operation of oil or gas fields are expensed at the time of acquisition. Materials for drilling wells are capitalised and expensed as a well cost as and when used. Petoro accepts the assessments made by operators regarding which materials should be capitalised and which expensed.

Equipment purchases for development projects are capitalised as part of the project investment, while purchases of significant spare parts are capitalised and expensed as and when used in operations.

DEBTORS

Trade debtors and other debtors are carried at face value less a provision for expected loss. This provision is based on an individual assessment of each debtor.

BANK DEPOSITS

Cash flows from oil and gas sales are transferred directly to the SDFI’s accounts with the Bank of Norway. The SDFI’s bank account with DnB Nor forms part of the government’s group overdraft facility. This means that these accounts are balanced on a daily basis. Capitalised bank deposits accordingly include the SDFI’s share of bank deposits in partnerships with shared liability (land-based partnerships) in which the SDFI has an interest.

TAXES

The SDFI is exempt from income tax and royalty in Norway. The SDFI is registered for VAT in Norway. Virtually all the SDFI’s sales of oil and gas products from its activity take place outside the geographic area to which Norway’s VAT legislation applies (the continental shelf and abroad). The SDFI invoices these sales to the buyer free of tax. At the same time, the SDFI can deduct possible VAT incurred on invoiced costs which are relevant to its activity.

FINANCIAL INSTRUMENTS

Since the SDFI is included in the government’s overall risk management, only limited use is made of financial instruments.

Such instruments are valued at their market value on the balance sheet date. Unrealised losses relating to financial instruments are recorded as expenses. Unrealised gains are recorded as income if all the criteria are fulfilled: the instrument is classified as a current asset, is part of a trading portfolio and traded on an exchange or in a regulated market, and has adequate liquidity and a fragmented ownership structure.

The valuation rules for fixed assets are applied to financial instruments not classified as current assets.

ACCOUNTING TREATMENT OF EXPLORATION AND DEVELOPMENT COSTS

Petoro employs the successful-effort method to record exploration and evaluation costs for oil and gas operations in the SDFI accounts. Exploration-related expenses are capitalised in anticipation of the drilling results. Should discoveries of oil and gas prove commercial, the expenses are classified as fixed assets in the balance sheet.

All expenses relating to wells, field installations and production facilities are capitalised. Expenses incurred by the operator’s project organisation for fields under development and development expenses incurred after approval of the plan for development and operation are also capitalised.

Costs for dry wells, non-commercial discoveries and operational preparations are expensed on a continuous basis. The same applies to the procurement of spare parts in the production phase and expenses relating to repairs and maintenance. All costs relating to operator charges for research and development are expensed.

DEPRECIATION

Ordinary depreciation of oil and gas production facilities is calculated for each field and field-dedicated transport system using the unit of production method. This means that the acquisition cost is depreciated in line with the relationship between volume sold during the period and reserves at the beginning of the period. Investments in wells are depreciated in line with the reserves made available by the wells drilled.

Petoro determines the reserve base for depreciation purposes on the basis of estimates for proven reserves. As the best estimate for such reserves, the company applies the reported P90 estimates from the operators. The reserve base for depreciation of oil fields in 2005 totals 67.5 per cent of expected remaining oil reserves, while the corresponding figure for gas fields is 87.4 per cent.

The portfolio’s expected reserves are classified by Petoro in accordance with category 1 in the NPD’s classification system. The reserve base accordingly excludes reserves which are not sufficiently matured. The reserve estimate is revised annually. Possible changes are given a prospective effect.

Ordinary depreciation for land-based plants and transport systems as well as riser platforms used by several fields is calculated on a straight-line basis over the remaining licence period at 31 December 2005. Intangible fixed assets and other tangible fixed assets are depreciated on a straight-line basis over their expected economic lifetime.

REVENUE RECOGNITION

The Norwegian government pursues a common ownership strategy to maximise the combined value of its shareholding in Statoil and its own oil and gas interests through the SDFI. This finds expression in the marketing and sales instruction, which has the overall aim of achieving the highest possible combined value for the oil and gas belonging to both Statoil and the government. Under the terms specified by the instruction for selling the government’s oil, NGL, condensate and natural gas, all oil and NGL from the SDFI is sold to Statoil, and all gas is sold by Statoil. Petoro’s responsibility is to monitor Statoil’s sale of the government’s petroleum in order to secure the highest possible combined value for the oil and gas belonging to both Statoil and the government, and to secure an equitable division of the total value creation.

The SDFI recognises the revenue from its sold share of oil and gas when the products are delivered to the customer. Revenue from ownership in pipelines and land-based production plants is recognised when the services are rendered.

Gas swap and borrowing agreements where settlement takes the form of returning volumes are accrued using the sales method. This means that the borrower records the sale as revenue on delivery to the buyer. At the same time, a provision is made for the expected future cost of producing and possibly transporting the gas to be returned. When lending gas, the lower of production expense and estimated net present value of the future sales price is capitalised as a pre-paid expense. Location swaps are concluded to solve transport problems by making gas available at a particular location and save transport costs or to make a gain by exploiting spare capacity in the transport system. From 2005, the SDFI’s share of location swaps related to the purchase or sale of third-party gas is recorded net as operating revenue. Liabilities arising because too much crude oil has been lifted in relation to the SDFI’s share of the production partnership are valued at production cost, while receivables due from the



CARLO CARRA:
The Red Rider, 1914.
Oil on canvas, private
owner, Milan.



GIACOMO BALLA:
*Abstract Speed - The Car Has
Passed*, 1913. Oil on canvas,
Tate Gallery, London.

The Italian Futurists published their manifesto in Paris in 1909. Futurism embraced all art forms and implicitly also ideas about a future vitalistic/nationalistic society. Within painting, the invention of film – the living picture – led to the introduction of the “fourth dimension” of time. Ideas from the Renaissance about the unity of time and place were abandoned in favour of showing the subject in motion over time by repeating its contours across the canvas.

other partners in the production partnerships are valued at the lower of production cost and fair value. No significant difference exists between SDFI volumes sold and the SDFI’s share of production.

PURCHASES AND SALES BETWEEN FIELDS AND/OR TRANSPORT SYSTEMS

Internal expenses and revenues relating to purchases and sales between fields and/or transport systems in which the SDFI is both owner and shipper are eliminated, so that only costs paid to third parties appear as net transport costs.

TRANSFER OF PROPRIETARY RIGHTS BETWEEN LICENCES

Reference is made to Proposition no 1 (2004-2005) to the Storting, section on other authorities (IX) under the Ministry of Petroleum and Energy, concerning the transfer of proprietary rights from a group of proprietors which includes Petoro as manager of the SDFI to another group of proprietors. The transfer of proprietary rights from the licence which has paid an investment to the licence in which the investment has been made normally takes place at the date of transfer. The paying licence then retains the right of use to the capital equipment.

ABANDONMENT AND REMOVAL EXPENSES

Under the terms of a licence, the authorities can require the licensees to remove offshore installations when their production life comes to an end. In accordance with Norwegian accounting standard 13 on uncertain liabilities and contingent assets, and in line with general developments in the industry, Petoro has decided to implement the capitalisation method from 1 January 2004. This means that the fair value of the removal liability is recorded during the period in which the liability arises. A corresponding amount is capitalised as part of the asset’s acquisition cost and depreciated together with this. Changes to the estimated removal costs are capitalised as part of the asset’s acquisition cost and depreciated over its remaining economic life. Calculated interest – the effect of the date of removal having moved one year closer – is recorded as a financial expense.

CONTINGENT LIABILITIES

Probable and quantifiable losses are expensed.

NOTE 1 – TRANSFER OF ASSETS

The government’s portfolio has been subject to minor adjustments during 2005 in connection with the unitisation of fields in the Oseberg area, with an effective date of 1 July 2005. Under the agreement, the licensees in production licence 079 will make a one-off payment to the licensees in production licence 190 for the right to recover petroleum from Delta Extension. The SDFI has interests in both licences.

In connection with the start-up of new installations at Kårstø, the equity interest in Gassled and the terminals in continental Europe changed from 38.293 per cent to 38.627 per cent with effect from 1 October 2005. In accordance with the provisions of Proposition no 41 (1994-1995) to the Storting, the SDFI acquired five per cent of Norpipe Oil AS at 15 October 2005.

The SDFI was awarded interests in eight new licences in connection with the awards in predefined areas for 2005. These interests were formally awarded by the King in Council on 6 January 2006.

A review of the calculations used to determine cash payments for transferred assets relating to government sales in 2001 (15 per cent to Statoil) and in 2002 (6.5 per cent to other oil companies) continued in 2005. Outstanding issues relating to the 2001 asset sale were resolved during 2005, with an impact of NOK 48 million on the income statement related to earlier tariff charges for removal of Tommeliten. An insurance issue related to the 2002 asset sale was resolved with accounting effect in 2005. A dispute over the valuation of stocks related to the sale of the SDFI’s interest in a production licence in 2002 was settled in December 2005. Both amounts are insignificant. They are recorded in accounting terms in 2005, but the cash effect will first be reflected in the 2006 accounts. Some issues relating to the asset sales are still outstanding.

NOTE 2 – SPECIFICATION OF FIXED ASSETS

	Historical cost at 1 Jan 05	Addition 2005	Amorti- sation 2005	Dis- posal* 2005	Transfers 2005	Accumulated depreciation 1 Jan 05	Depre- ciation 2005	Book value at 31 Dec 05
All figures in NOK mill								
Fields under development								
Kristin	2 836	1 005			(3 840)			
Urd	298	514			(812)			
Ormen Lange	1 904	4 062						5 965
Ringhorne East		7						7
Skinfaks	59				(59)			
Snøhvit	6 784	3 193						9 978
Sub-total	11 882	8 780			(4 712)			15 950
Fields in operation								
Brage	1 992			(4)		(1 868)	(61)	59
Draugen	9 146	390				(7 001)	(566)	1 969
Ekofisk II	2 242	320				(875)	(165)	1 522
Frøy	2 456			(15)		(2 439)		2
Grane	4 553	286				(384)	(588)	3 867
Gullfaks	26 311	1 148			76	(21 922)	(981)	4 631
Heidrun	24 970	644				(14 053)	(1 485)	10 076
Heimdal	2 037			(21)		(1 988)	(11)	18
Huldra	2 183	98				(1 733)	(228)	320
Jotun	323			(16)		(262)	(9)	36
Kristin					3 840		(49)	3 791
Kvitebjørn	3 074	279				(17)	(537)	2 798
Njord	658	40				(475)	(80)	143
Norne	8 488	802				(5 806)	(683)	2 801
Oseberg South	4 359	650				(1 523)	(527)	2 959
Oseberg Unit	17 956	972			79	(15 309)	(275)	3 424
Oseberg East	2 334	208				(1 462)	(142)	938
Skirne	721	53				(70)	(196)	508
Snorre	14 794	485				(8 659)	(639)	5 981
Statfjord North	1 753	17				(1 357)	(85)	328
Statfjord East	1 504	92				(1 253)	(61)	281
Sygna	600	7				(456)	(28)	123
Tordis	2 386	45				(1 992)	(97)	342
Troll Gas	22 629	932				(4 527)	(684)	18 350
Troll Oil	33 101	2 583				(25 707)	(1 834)	8 143
Urd					812		(17)	795
Tune	1 379	150				(534)	(877)	117
Varg	1 054	182				(822)	(127)	286
Veslefrikk	4 478	185				(3 351)	(238)	1 074
Vigdis	2 856	72				(2 041)	(199)	688
Visund	4 537	470			10	(1 738)	(111)	3 168
Åsgard	19 966	501				(5 721)	(1 186)	13 560
Sub-total	224 836	11 611		(55)	4 818	(135 345)	(12 766)	93 099

	Historical cost at 1 Jan 05	Addition 2005	Amorti- sation 2005	Dis- posal* 2005	Transfers 2005	Accumulated depreciation 1 Jan 05	Depre- ciation 2005	Book value at 31 Dec 05
All figures in NOK mill								
Pipelines and terminals								
Dunkerque Terminal	178	0				(45)	(6)	129
Etanor	926	57				(122)	(43)	818
Gassled	38 426	966				(14 045)	(1 032)	24 316
Haltenpipe	1 145					(405)	(57)	683
Langeled	1 262	2 319						3 582
Mongstad Terminal	104	7				(37)	(12)	62
Oseberg Transport System	2 622	25				(2 142)	(38)	467
Ormen Lange Eiendom DA		37						37
Troll Oil Pipeline I and II	914	1				(698)	(48)	169
Vestprosess	854	6				(107)	(41)	713
Frostpipe	234	6				(228)		11
Tampen Link		20						20
Zeepipe Terminal	198	1				(96)	(4)	98
Sub-total	46 864	3 447				(17 925)	(1 282)	31 105
Capitalised exploration expenses	557	601	(216)		(106)			836
Total tangible assets	284 139	24 439	(216)	(55)		0 (153 270)	(14 047)	140 990
Intangible assets	1 002	242				(2)	0	1 241
Other fixed assets	184					(174)	(3)	7
Total fixed assets (NGAAP)	285 325	24 681	(216)	(55)		0 (153 446)	(14 051)	142 238
Conversion to cash basis	(21 007)	(3 980)	188	55		10 247	1 137	(13 360)
Total fixed assets on cash basis	264 318	20 701	(28)			(143 200)	(12 914)	128 878

*When net addition investments and change in removal liability are negative, they are shown as a disposal.

Intangible assets of NOK 1 241 million relate mainly to:

- Capacity rights for regasification of LNG at the Cove Point terminal in the USA with an associated agreement on the sale of LNG from Snøhvit to Statoil Natural Gas LLC (SNG) in the USA. Since these rights are associated with LNG from Snøhvit, straight-line depreciation over the duration of the agreement on these rights will begin when Snøhvit comes on stream in 2007.
- Investments in rights related to the storage of gas in the UK. The development of gas storage at Aldbrough will provide a combined capacity for the SDFI and Statoil of 140 million scm, of which the SDFI share is 57.7 per cent. Plans call for the facility to come into commercial operation towards the end of 2007, and the amount of the investment will be depreciated on a straight-line basis over the estimated economic life.

Other fixed assets relate to machinery and technical equipment in Statpipe and Åsgard Transport. The SDFI also owns shares in Norseas Gas AS with a book value of NOK 3.98 million and shares in Norpipe Oil AS, which were transferred free of charge from Statoil with effect from 15 October 2005.

NOK 270 million of capitalised exploration expenses at 31 December relate to wells which have been capitalised for a period of more than a year in anticipation of further appraisal drilling, evaluation or early field planning. These expenses relate to nine wells.

NOTE 3 – SPECIFICATION OF OPERATING REVENUE

All figures in NOK million	2005	2004	2003
Troll	47 650	34 207	32 368
Oseberg	25 158	20 332	14 617
Tampen	26 752	22 963	18 915
Norwegian Sea	38 591	34 078	28 766
Gassled and other infrastructure	9 819	8 457	8 119
Net profit agreements	1 688	210	200
Other revenue	6 964	4 271	2 200
Elimination internal sales	(3 938)	(3 712)	(3 486)
Total NGAAP	152 683	120 807	101 699
Conversion to cash basis	(8 502)	(475)	(514)
Total – cash basis	144 181	120 332	101 185

Classification by geographical area has changed from reporting in previous years. Information in the note has been updated and amended in accordance with the new organisation.

NOTE 4 – SPECIFICATION OF OPERATING REVENUE BY PRODUCT

All figures in NOK million	2005	2004	2003
Crude oil and NGL*	96 460	80 927	67 727
Gas	45 205	32 072	25 803
Transport and processing revenue	8 564	7 603	7 229
Net profit agreements	765	(5)	740
Other revenue	1 688	210	200
Total NGAAP	152 683	120 807	101 699
Conversion to cash basis	(8 502)	(475)	(514)
Total cash basis	144 181	120 332	101 185

*Includes condensate.

In accordance with the marketing and sales instruction, all crude oil and NGL are sold to Statoil. Gas is sold mainly to customers in Europe with the addition of a small quantity sold to the USA.

NOTE 5 – SPECIFICATION OF OTHER OPERATING EXPENSES

All figures in NOK million	2005	2004	2003
Troll	6 448	5 216	5 642
Oseberg	4 860	4 848	4 130
Tampen	4 012	3 591	3 324
Norwegian Sea	4 805	4 624	4 469
Gassled and other infrastructure	1 879	1 695	1 422
Other operating expenses	6 955	4 761	2 058
Elimination internal purchases	(3 938)	(3 712)	(3 486)
Total NGAAP	25 020	21 025	17 557
Conversion to cash basis	(731)	671	(195)
Total – cash basis	24 289	21 696	17 362

Classification by geographical area has changed from reporting in previous years. Information in the note has been updated and amended in accordance with the new organisation.

The figures include activities related to the operation of fields and installations, processing and transport costs, purchase of gas for onward sale, and administrative costs for Statoil related to gas sales.

NOTE 6 – INTEREST ON FIXED CAPITAL

Interest on the government’s fixed capital is to be charged to operations in order to take account of capital costs and to provide a more accurate picture of resource use. This is a calculated cost without a cash flow effect.

Interest on the government’s fixed capital is included in the accounts. The amount of interest is calculated as specified in Proposition no 1 Appendix no 7 (1993-1994) to the Storting (the Finance Bill) and in item 5.6 in the 2005 Letter of Award to Petoro AS from the Ministry of Petroleum and Energy.

The accounts compiled on a cash basis include an open account with the government for the difference between recording by chapter/item in the appropriation accounts and liquidity movements.

Interest on the government account is calculated as specified in item 5.7 in the 2005 Letter of Award to Petoro AS from the Ministry of Petroleum and Energy. The interest rate applied is the rate earned by the government’s current account with the Bank of Norway, and interest is calculated on the average monthly balance in the government’s account.

NOTE 7 – NET FINANCIAL ITEMS

All figures in NOK million	2005	2004	2003
Interest	96	25	36
Other financial revenue	61	60	17
Currency gain	2 900	3 457	1 556
Currency loss	(2 247)	(4 482)	(1 742)
Interest costs	(60)	(73)	(45)
Interest on removal liability	(646)	(297)	(288)
Net financial items	103	(1 310)	(467)

NOTE 8 – CASH BALANCE

All figures in NOK million	2005	2004	2003
Open account government	(737)	(663)	(542)
Account for real investment	128 878	121 119	118 556
Total	128 140	120 456	118 014
Open account government	737	663	542
Fixed capital at 31 Dec 05	(128 878)	(121 119)	(118 556)
Total	(128 140)	(120 456)	(118 014)

NOTE 9 – GOVERNMENT PETROLEUM INSURANCE FUND

Transfers from the Government Petroleum Insurance Fund relate to the settlement of insurance claims. These amounts are added to investment, operating revenue and operating expenses, depending on the type of claim and the accounting treatment in the operator’s accounts. Settlements added to investment are subsequently presented as amortisation of write-down in the accounts compiled on a cash basis.

NOTE 10 – RELATED PARTIES

The government (represented by the Ministry of Petroleum and Energy) owns 70.9 per cent of Statoil and 100 per cent of Gassco. These companies are classified as related parties to the SDFI.

Statoil is the buyer of the government’s oil, condensate and NGL. Sales of oil, condensate and NGL to Statoil totalled NOK 97.4 billion (293 million boe) for 2005 and NOK 80.9 billion (326 million boe) for 2004. The amount and quantities are exclusive of the government’s royalty oil.

Statoil markets and sells the government’s natural gas at the government’s expense and risk together with its own production. The government receives the market value for these sales. The government sold dry gas worth NOK 262 million directly to Statoil in 2005 and NOK 237 million in 2004. Statoil is reimbursed by the government for its relative share of costs associated with the transport, storage and processing of dry gas, the purchase of dry gas for onward sale and administrative expenses relating to gas sales. These reimbursements amounted to NOK 10.7 billion in 2005 and NOK 9.3 billion in 2004. In addition came costs associated with the activity in the USA.



NATALIA GONCHAROVA:
Rayonist Composition.
Oil on canvas. Thyssen
Collection, Madrid.

Russian Rayonism was
closely related to
Futurism. An abstract
imagery was developed
through a system of
crossing rays which
represented a pure
description of abstract
motion and dynamism.

Open accounts with Statoil relating to these revenues and costs are recorded as trade debtors and current debt respectively in the balance sheet.

In addition to the above-mentioned amounts, the SDFI accounts consist of other open accounts/transactions with Statoil, primarily concerning provisions related to year-end closing of the accounts and transactions related to long-term liabilities which fall under the marketing and sales instruction. See note 13.

Open accounts and transactions relating to activities in the production licences are not included in the above-mentioned amounts. Hence, no information has been included with regard to open accounts and transactions relating to licence activities with Statoil and Gassco.

No open accounts existed at 31 December 2005 between Statoil and SDFI relating to the marketing and sales instructions.

NOTE 11 – TRADE DEBTORS

No confirmed loss has been recorded for SDFI operations, and there are no unobtainable recordings or remissions of claims.

A small provision has been made for bad debts following an assessment of possible losses on debtors from trading in the UK. No losses had been confirmed at 31 December.

Trade debtors and other debtors are otherwise recorded at face value.

Trade debtors due later than 12 months after the balance sheet date amounted to NOK 0.9 million.

NOTE 12 – ABANDONMENT/REMOVAL

A new method of recording abandonment and removal liabilities, the capitalisation method, was implemented on 1 January 2004. This means that existing technology and information from the respective operators provide the basis for calculating the liability. Great uncertainty prevails over both estimated removal costs and the removal date. See note 21.

The removal liability comprises future abandonment of oil and gas installations. Norwegian government legal requirements and the Oslo-Paris (Ospar) convention for the protection of the marine environment of the north-east Atlantic provide the basis for determining the extent of the removal liability.

Interest expense on the liability is classified as a financial expense in the income statement. The discount rate is based on the interest rate for Norwegian government bonds with the same maturity as the removal liability.

All figures NOK million

Liabilities at 1 Jan 05	14 930
New liabilities	191
Actual abandonment	(31)
Changes to estimates	1 654
Change in discount rate	1 148
Interest expense	646
Liabilities at 31 Dec 05	18 538

NOTE 13 – OTHER LONG-TERM LIABILITIES

Other long-term liabilities comprise:

- prepayment from Electrabel for gas purchases
- debt relating to the final settlement of commercial arrangements concerning the move to company-based gas sales
- provision for possible payment of environmental tax relating to the sale of gas to the Netherlands.

Liabilities falling due longer than five years total NOK 331 million.

NOTE 14 – OTHER CURRENT LIABILITIES

Other current liabilities include liabilities due no later than 31 December 2005, and comprise:

- provisions for unpaid costs accrued by licence operators in the accounts at November
- provisions for accrued unpaid costs at December, adjusted for cash calls in December
- other provisions for accrued unpaid costs not included in the accounts received from operators
- current share of long-term liabilities.

NOTE 15 – FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The SDFI makes very limited use of financial instruments (derivatives) to manage risk. This is primarily because the SDFI belongs to the state and is accordingly included in the government’s overall risk management. The SDFI does not have significant interest-bearing debt, and all crude oil and NGL are sold to Statoil. Instruments used to hedge gas sales relate to forwards and futures. Eliminations are made where legal rights are available to counterclaim unrealised loss and gain, or where paid and capitalised deposits/margins exist which reflect the market value of the derivatives. At 31 December 2005, the market value of the instruments was NOK 245 million in assets and NOK 293 million in liabilities. The comparable figures at the end of 2004 were NOK 114 million and NOK 106 million respectively.

PRICE RISK

The SDFI is exposed to fluctuations in oil and gas prices in the world market. Statoil purchases all oil and NGL from the SDFI at market-based prices. SDFI revenue from gas sales to end users reflects market value. Based on the arrangement relating to the marketing and sales instruction together with the SDFI’s participation in the government’s overall risk management, the SDFI’s strategy is to make limited use of financial instruments (derivatives) to counteract fluctuations in profit and loss owing to variations in commodity prices.

CURRENCY RISK

The most significant part of the SDFI’s revenue from the sale of oil and gas is billed in USD, EUR or GBP. Part of its operating expenses and investments is also billed in equivalent currencies. When converting to NOK, currency fluctuations will affect the SDFI’s income statement and balance sheet. Petoro does not make use of currency hedging in relation to future sales of the SDFI’s petroleum, and its exposure in the balance sheet at 31 December 2005 related to one month’s outstanding revenue.

INTEREST RISK

The SDFI does not have significant interest-bearing debt, and is not financially exposed to interest rate fluctuations.

CREDIT RISK

The SDFI’s sales are made to a limited number of parties, with all oil and NGL sold to Statoil. In accordance with the marketing and sales instruction, financial instruments are purchased from other parties with sound credit ratings. Credit risk relating to the inability of other parties to meet their financial commitments is normally limited to an amount exceeding the SDFI’s liability. Financial instruments are only established with a large bank or financial institution, at levels of exposure approved in advance. The SDFI’s credit-related risk during consecutive transactions is regarded as insignificant.

LIQUIDITY RISK

The SDFI generates a significant positive cash flow from its operations. Internal guidelines on managing the flow of liquidity have been established.

NOTE 16 – LEASES/CONTRACTUAL OBLIGATIONS

Leases represent operation-related contractual obligations for the chartering of rigs, supply ships and standby vessels and the leasing of helicopters, bases and so forth as specified by the individual operator. The figures represent cancellation costs.

Transport obligations relate to the sale of gas, and consist mainly of transport and storage liabilities in the UK and continental Europe as well as obligations relating to the Cove Point terminal in the USA. The SDFI’s share of installations and pipelines on the NCS is generally higher than or equal to the transport share. Hence, no obligations are calculated for these systems.

All figures in NOK million	Leases	Transport obligations
2006	1 502	546
2007	708	512
2008	413	522
2009	291	471
2010	180	446
Beyond	328	5 613

In addition to the above-mentioned leasing obligations, the SDFI will also have a financial obligation under the marketing and sales instruction related to chartering of carriers to ship LNG from the Snøhvit field. These vessels were still under construction at 31 December. The capital element in these charters is about USD 520 million over a 23-year period, undiscounted at an exchange rate of NOK 6.75/USD. The charters will be effective from the delivery of the vessels. The first two ships were delivered in January and February 2006. Onward charters fixed for these vessels cover part of their charter costs.

In connection with the award of a licence to explore for and produce oil and gas, licensees undertake to drill a certain number of wells. Petoro was committed at 31 December to participating in eight wells with an expected cost to the company of NOK 496 million.

The company has also accepted contractual obligations relating to the development of new fields, represented by the expected total development costs. These obligations total NOK 11.2 billion for 2006 and NOK 7.6 billion thereafter, a total of NOK 18.4 billion. In addition, Petoro is committed through approved licence budgets to operating and investment expenses for 2006 which will be on a par with the 2005 figure. Commitments toward third parties amounting to NOK 142 million relate to the SDFI’s share in the construction of a terminal at Aldbrough in the UK. Of this, NOK 48 million is expected to be incurred in 2006.

In connection with the sale of the SDFI’s oil and gas, Statoil has issued a limited number of warranties to vendors and owners of transport infrastructure relating to operations in the USA and the UK. Their extent is restricted, and they are considered to be immaterial for the company.

The SDFI and Statoil deliver gas to customers under common gas sale agreements. SDFI gas reserves will be utilised in accordance with the SDFI’s share of production from the field selected to deliver the gas. Proven reserves exceed total sales obligations.

NOTE 17 – OTHER LIABILITIES

The SDFI could be exposed to possible legal actions and disputes in which Petoro is involved as a participant in production licences, fields, pipelines and land-based plants, and through Statoil’s sale of the SDFI’s gas. The SDFI is involved in current disputes relating to issues in joint ventures in which Petoro is a licensee and in outstanding cases relating to the asset sales in 2001 and 2002. Provisions have been made in the accounts for issues where a negative outcome for Petoro is thought to be more likely than not. In addition, the company is aware under the marketing and sales instruction that negotiations relating to two long-term gas sales contracts have gone to arbitration. Contractual prices for an overall volume of 3.2 billion scm delivered up to 31 December 2005 and for volumes related to future deliveries could be positively or negatively affected. It is not possible at the present moment to estimate the outcome.

NOTE 18 – EQUITY

All figures in NOK million	2005	2004	2003*
Cash transfers to the Bank of Norway	(619 888)	(520 713)	(439 312)
Capital contribution	9 082	9 082	9 082
Accumulated earnings at 1 Jan	661 075	578 732	510 764
Accumulated transfer of interests in 2001-02	(29 922)	(29 874)	(30 109)
Conversion differences	(9)	(84)	(11)
Implementation effect, new removal model	1 044	1 044	859
Net income for the year	113 172	82 343	68 154
Total equity	134 554	120 530	119 427

* Figures for 2003 have been revised to take account of the change in the principles for abandonment and removal (note 12).

Cash transfers to the Bank of Norway are the amount which the government has received from the SDFI (payments from the SDFI less payments to the SDFI, with the exception of NOK 9 082 million in capital contribution).



FERNAND LEGER:
The Card Game, 1917.
Oil on canvas. Kröller-Müller Museum, Otterlo.

Leger presented his variant of Cubism in 1909 under the name Tubism, from the French word for pipe. His worship of the strength and future opportunities of the machine also led him to describe humans as composed of tubular structures.

The capital contribution is the sum paid to Statoil at 1 January 1985 for the assets acquired by the SDFI from Statoil (repaid on debt owed by Statoil to the government). Accumulated earnings at 1 January represent accumulated operating revenue since the SDFI was established on 1 January 1985.

Accumulated transfer of interests relates to the sale of 15 per cent of the SDFI’s value in 2001 and 6.5 per cent in 2002. The amount for 2003 is shown as the accumulated effect on equity of the NOK 21 339 million and NOK 8 770 million received from the sales in 2001 and 2002 respectively. Retrospective settlements with an accounting effect of NOK 235 million in 2004 and NOK 48 million in 2005 have been made with respect to the 2001 sale. The effect of this settlement is recorded against equity and is presented as the accumulated transfer of assets in 2001 and 2002.

The transfer of assets from the SDFI to Statoil in 2001 has been recorded using the pooling of interests method, since it occurred between units under common control. This method implies that assets in the SDFI accounts are reduced by the book value of the transferred assets, with equity as the contra entry.

Asset transfers in 2002 occurred between independent parties. These transfers are recorded using the transaction principle, with the associated calculation of accounting gain and loss.

Under intangible fixed assets, the SDFI has recorded sales and processing rights for LNG at the Cove Point terminal in the USA. The SDFI’s share of these rights is denominated in foreign currency, but has been converted to and recorded in the accounts in NOK. The share has been converted at the exchange rate prevailing on 31 December, and changes in the NOK figure owing to changes in exchange rates are recorded as a conversion difference in the NGAAP accounts.

NOTE 19 – AUDITORS

The SDFI is subject to the regulations and provisions concerning government financial management, which specify in accordance with the Act on the Auditing of Governmental Accounts of 7 May 2004 that the Office of the Auditor General is the external auditor for the SDFI. The Auditor General submits the final audit report to the board of directors.

In addition, Deloitte Statsautoriserte Revisorer AS has been engaged by the board of directors of Petoro AS to perform a financial audit of the SDFI as a part of the internal audit. Deloitte submits its audit report to the board in accordance with Norwegian auditing standards.

Deloitte’s fee is expensed in the Petoro AS accounts.

NOTE 20 – EXPECTED OIL AND GAS RESERVES

Oil* in mill bbl Gas in bn scm	2005		2004		2003	
	Oil	Gas	Oil	Gas	Oil	Gas
Expected reserves at 1 Jan	2 499	997	2 689	1 018	2 876	891
Corrections for earlier years**	(5)	(11)				
Change in estimates	(7)	3	40	3	65	5
Extensions and discoveries	3	3	24	1	84	146
Improved recovery	108	6	70	0	5	0
Purchase of reserves	0	0	0	0	0	0
Sale of reserves	0	0	0	0	0	0
Production	(288)	(26)	(324)	(24)	(341)	(24)
Expected reserves at 31 Dec	2 311	971	2 499	997	2 689	1 018

* Oil includes NGL and condensate

** The increase in reserves for Åsgard in 2004 was inaccurately reported, and has been corrected in 2005. In addition, historical production has been adjusted to accord with official reporting by the NPD.

The table presents the total remaining reserves (P50 estimate in accordance with the NPD’s resource categories 1-3) without regard to the duration of licences. Information on estimated production periods and current licence durations is given in the overview of government participation interests in note 21, SDFI overview of interests.

Expected reserves represent the estimated value of resources in categories 1-3 of the NPD’s resource classification system, as specified in the guidelines for classification of petroleum resources on the NCS.

Reserves in production are the sum of expected remaining recoverable, marketable and deliverable quantities of petroleum in production, and also include cases in which production has been temporarily shut down. These quantities satisfy resource category 1 in the NPD classification.

Total expected remaining reserves at 31 December 2005 were 8 420 million boe (NPD resource category 1).

Expected reserves in production (NPD resource category 1) at 31 December 2005 were 2 078 million barrels of oil, condensate and NGL, and 624 billion standard cubic metres of gas. That corresponds to a total of 6 360 million boe. Expected reserves in resource categories 2 and 3 consists primarily of Snøhvit and Ormen Lange.

NOTE 21 – SDFI OVERVIEW OF INTERESTS

Production licence	At 31 Dec 05 Interest (%)	At 31 Dec 04 Interest (%)	Production licence	At 31 Dec 05 Interest (%)	At 31 Dec 04 Interest (%)
18	5.00	5.00	134	13.55	13.55
018 B	5.00	5.00	152	30.00	30.00
018 C	5.00	5.00	153	30.00	30.00
028 C	30.00	30.00	169	30.00	30.00
34	40.00	40.00	169 B1	37.50	37.50
036 BS	20.00	20.00	169 B2	30.00	30.00
37	30.00	30.00	171 B	33.60	33.60
037 B	30.00	30.00	176	47.88	47.88
037 E	30.00	30.00	185	13.40	13.40
38	30.00	30.00	190	40.00	40.00
038 B	30.00	30.00	193	30.00	30.00
40	30.00	30.00	195	35.00	35.00
43	30.00	30.00	195 B*	35.00	-
043 BS*	30.00	-	199	27.00	27.00
50	30.00	30.00	208	30.00	30.00
050 B	30.00	30.00	209	35.00	35.00
050 C	30.00	30.00	237	35.50	35.50
51	31.40	31.40	248	40.00	40.00
52	37.00	37.00	248 B*	40.00	-
052 B	37.00	37.00	250	45.00	45.00
53	33.60	33.60	253	20.00	20.00
053 B	25.40	25.40	255	30.00	30.00
54	40.80	40.80	256	20.00	20.00
55	13.40	13.40	264	20.00	20.00
055 B	13.40	13.40	265	30.00	30.00
055 C	33.60	33.60	275	5.00	5.00
57	30.00	30.00	276	-	37.00
62	19.95	19.95	277	30.00	30.00
64	30.00	30.00	277 B*	30.00	-
74	19.95	19.95	281	20.00	20.00
77	30.00	30.00	283	20.00	20.00
78	30.00	30.00	291	14.26	14.26
79	33.60	33.60	309	33.60	33.60
85	62.92	62.92	315	30.00	30.00
085 B	62.92	62.92	318	20.00	20.00
085 C	56.00	56.00	327	20.00	20.00
085 D*	56.00	-	328	20.00	20.00
89	30.00	30.00	329	20.00	20.00
93	47.88	47.88	331	20.00	20.00
94	14.95	14.95	345	30.00	30.00
094 B	35.50	35.50	347	7.50	7.50
95	59.00	59.00	348	7.50	7.50
97	30.00	30.00	374 S*	20.00	-
99	30.00	30.00	384*	20.00	-
100	30.00	30.00			
102	30.00	30.00	Net profit licences**		
103 B	30.00	30.00	027		
104	33.60	33.60	028		
107	7.50	7.50	029		
110	30.00	30.00	033		
110 B	30.00	30.00			
120	16.94	16.94			
124	27.09	27.09			
128	24.55	24.55			
128 B	54.00	54.00			
128 C*	24.55	-			
132	7.50	7.50			

* The SDFI’s interests in production licences approved by the King in Council on 6 January 2006, but announced by the Ministry of Petroleum and Energy on 13 December 2005.

** Production licences where the SDFI is not a licensee, but has a right to a share of possible profit.

	At 31 Dec 05	At 31 Dec 04	Remaining	
Unitised fields	Interest (%)	Interest (%)	production period	Licence term
Brage Unit	14.26	14.26	2014	2015
Grane Unit	30.00	30.00	2026	2030
Halten Bank West (Kristin)	18.90	18.90	2025	2033
Heidrun Unit	58.16	58.16	2033	2024
Huldra Unit	31.96	31.96	2011	2015
Jotun Unit	3.00	3.00	2015	2021
Njord Unit	7.50	7.50	2017	2021
Norne Unit	54.00	54.00	2016	2026
Ormen Lange Unit	36.48	36.48	2046	2040
Oseberg South Unit	33.60	33.60	2050	2031
Oseberg Unit	33.60	33.60	2026	2031
Ringhorne East	7.80	-	2021	2030
Snorre Unit	30.00	30.00	2029	2015
Snøhvit Unit	30.00	30.00	2038	2035
Statfjord East Unit	30.00	30.00	2018	2024
Sygna Unit	30.00	30.00	2018	2024
Tor Unit	3.69	3.69	2015	2028
Troll Unit	56.00	56.00	2053	2030
Visund Unit	30.00	30.00	2027	2023
Åsgard Unit	35.50	35.50	2029	2027
Fields				
Draugen	47.88	47.88	2021	2024
Ekofisk	5.00	5.00	2028	2028
Eldfisk	5.00	5.00	2028	2028
Embla	5.00	5.00	2028	2028
Gullfaks	30.00	30.00	2027	2016
Gullfaks South	30.00	30.00	2025	2016
Heimdal	20.00	20.00	2006	2021
Kvitebjørn	30.00	30.00	2021	2031
Oseberg East	33.60	33.60	2024	2031
Skirne	30.00	30.00	2012	2025
Statfjord North	30.00	30.00	2018	2026
Tordis	30.00	30.00	2019	2024
Tune	40.00	40.00	2011	2032
Urd	24.55	24.55	2016	2026
Varg	30.00	30.00	2010	2011
Veslefrikk	37.00	37.00	2014	2015
Vigdis	30.00	30.00	2020	2024
Shut-in fields				
Albuskjell				
Cod				
Edda				
Frøy Unit				
West Ekofisk				
East Frigg				

	At 31 Dec 05	At 31 Dec 04	
Pipelines and land-based plants	Interest (%)	Interest (%)	Licence term
Frostpipe	30.00	30.00	-
Oseberg Transport System (OTS)	48.38	48.38	2028
Troll Oil Pipelines I + II	55.77	55.77	-
Grane Oil Pipeline	43.60	43.60	-
Kvitebjørn Oil Pipeline	30.00	30.00	-
Norpipe Oil AS (interest)	5.00	-	-
Oil – land-based plants			
Mongstad Terminal DA	35.00	35.00	-
Gas pipelines			
Gassled***	38.63	38.29	2028
Haltenpipe	57.81	57.81	2020
Langeled****	32.95	32.95	2035
Tampen Link	7.00	-	2032
Gas – land-based plants			
Dunkerque Terminal DA*****	25.11	24.89	-
Zeepipe Terminal J.V.*****	18.93	18.76	-
Etanor DA	62.70	62.70	-
Vestprosess DA	41.00	41.00	-
Kollsnes (gas processing plant)*****	38.63	38.29	-
Snøhvit LNG plant	30.00	30.00	2028
Norsea Gas AS (Eierandel)	40.01	40.01	-

The SDFI also has intangible fixed assets relating to sales and processing rights for LNG in the USA and gas storage in the UK.

*** The interest in Gassled including Norsesea Gas is 39.50%

**** Northern leg (Nyhamna-Sleipner Riser): 37.48%. Southern leg (Sleipner Riser-Easington): 28.36%

***** Included in Gassled from 1 January 2003

***** The Kollsnes gas processing plant was incorporated in Gassled from 1 February 2004.

Audit letter from the Office of the Auditor General



Riksrevisjonen
Office of the Auditor General
of Norway

Audit of the accounts for 2005 for the State’s Direct Financial Interest in the petroleum activity

Pursuant to Act no 21 of 7 May 2004 relating to the Office of the Auditor General (Auditor General Act), the Office of the Auditor General of Norway is the auditor for the state’s direct financial interest in the petroleum activity.

Following its annual audit, the Office of the Auditor General issues a final audit letter (report) which summarises the conclusions of its audit work. The audit letter will first be made public when the Office of the Auditor General has reported the results of the audit to the Storting (parliament) in October/November, pursuant to section 18 of the Auditor General Act.

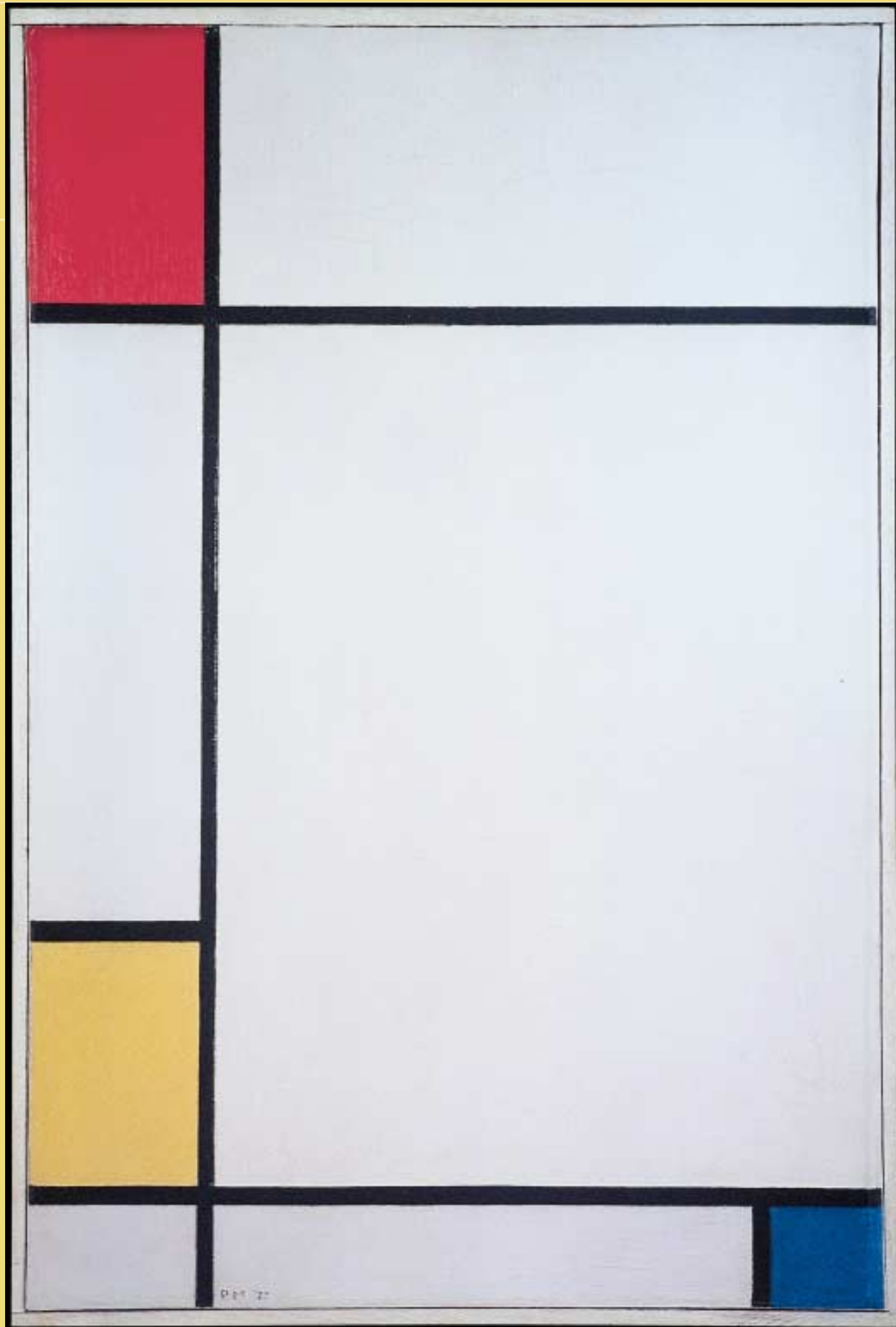
The board of directors and possibly the annual general meeting will be briefed on the results of the audit for the year.

Hans Conrad Hansen
Director general

Tom Arild Hanekamhaug
Deputy director general

Painting as an autonomous mode of expression

Tendencies quickly emerged within the dawning modernist movement of the early 20th century which rejected references to “reality”. The concept of a “picture”, with its implication that an artist is somebody who depicts reality, was taboo in these quarters. The word “painting” was used instead. These painters moved partly towards the abstract form or went even further by maintaining that a painting is an object which depicts nothing but itself – in other words, a canvas covered with blocks of colour. The subject of the painting thereby became the painting itself.



PIET MONDRIAN:
Composition No. III, with Red, Yellow and Blue,
 1927, Oil on canvas, 61 x 40 cm.

Petoro AS income statement

All figures in NOK 1 000	Note	2005	2004	2003
Invoiced government contribution	1	174 320	163 710	177 419
Other revenue	1	189	712	0
Deferred revenue investments	2	(2 429)	(5 875)	(15 400)
Deferred revenue recorded	2	5 806	4 279	524
Total operating revenue		177 886	162 825	162 543
Payroll expenses	3,9	79 306	74 637	72 751
Depreciation	4	6 098	4 646	924
Administrative fees	12, 15	2 714	3 760	455
Accounting fees	14	16 440	16 868	20 583
Office expenses	13	8 695	10 274	12 204
ICT expenses	14	12 287	12 139	16 103
Other operating expenses	11, 14, 15	52 384	44 374	44 818
Total operating expenses		177 924	166 698	167 837
Operating loss		(38)	(3 873)	(5 294)
Financial income		1 117	1 010	2 034
Financial expenses		(142)	(15)	(10)
Net financial result		975	994	2 024
NET INCOME/(LOSS)		937	(2 879)	(3 271)
TRANSFERS				
Transfer to other equity		937	(2 879)	(3 271)
Total transfers		937	(2 879)	(3 271)

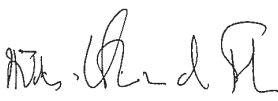
Stavanger, 23 February 2006


Bente Rathe
Chair


Jørgen Lund
Deputy chair


Ingelise Arntsen
Director


Per-Christian Endsjø
Director


Nils-Henrik M. von der Fehr
Director


John Magne Hvidsten
Worker director


Elen Carlson
Worker director


Kjell Pedersen
President and CEO

Petoro AS balance sheet

All figures in NOK 1 000	Note	2005	2004	2003
ASSETS				
Fixed assets				
Operating equipment, fixtures, etc	4	13 352	17 020	15 792
Total tangible assets		13 352	17 020	15 792
Total fixed assets		13 352	17 020	15 792
Current assets				
Trade debtors		2 445	1 200	0
Other debtors	5	388	2 820	3 355
Bank deposits	6	49 385	59 439	73 815
Total current assets		52 218	63 459	77 170
TOTAL ASSETS		65 570	80 479	92 961
EQUITY AND LIABILITIES				
Equity				
Paid-in capital				
Share capital (10 000 shares at NOK 1 000)	7	10 000	10 000	10 000
Total paid-in capital		10 000	10 000	10 000
Retained earnings				
Other equity	8	5 653	4 716	7 595
Total retained equity		5 653	4 716	7 595
Total equity	8	15 653	14 716	17 595
Liabilities				
Provisions				
Pension liabilities	9	9 202	16 875	9 247
Deferred recording government contribution	2	13 095	16 472	14 877
Total provisions		22 298	33 347	24 124
Current liabilities				
Trade creditors	15	10 636	5 571	14 021
Withheld taxes and social security	10	3 856	11 232	13 822
Other current liabilities	10	13 127	15 613	23 400
Total current liabilities		27 619	32 416	51 243
Total liabilities		49 917	65 763	75 366
TOTAL EQUITY AND LIABILITIES		65 570	80 479	92 961

Petoro AS cash flow statement

All figures in NOK 1 000		2005	2004	2003
NET CASH FLOW FROM OPERATING ACTIVITIES				
	Cash generated from operations for the year*	7 035	1 767	(2 347)
+/-	Change in debtors	(1 245)	(665)	(250)
+/-	Change in trade creditors	5 065	(8 449)	(13 042)
+/-	Change in other accrued items	(18 480)	(1 154)	31 556
	Net cash flow provided by operating activities	(7 625)	(8 501)	15 918
NET CASH FLOW FROM INVESTING ACTIVITIES				
-	Investments in tangible fixed assets	(2 429)	(5 875)	(15 400)
	Net cash flow from investing activities	(2 429)	(5 875)	(15 400)
NET CASH FLOW FROM FINANCING ACTIVITIES				
+	Proceeds from share issue	0	0	0
	Net cash flow from financing activities	0	0	0
	Net changes in liquid assets	(10 054)	(14 376)	519
+	Cash and equivalents at 1 January	59 439	73 815	73 296
	Cash and cash equivalents at 31 December	49 385	59 439	73 815
* This figure is obtained as follows				
	Net income/loss	937	(2 879)	(3 271)
+	Ordinary depreciation	6 098	4 646	924
	Cash generated from operations for the year	7 035	1 767	(2 347)

Petoro AS notes



WASSILY KANDINSKY:
Untitled, First Abstract Watercolour, 1910.
Watercolour on paper,
Musée National de
l'Art Moderne, Paris.

Kandinsky started from Expressionist painting, and developed this around 1910 into a genuinely abstract form through Automatism. This involves creating a painting as quickly as possible through a technique which permits fast working and prevents reflection. The pictorial expressions are thereby held to emanate from the sub-conscious, since the rational mind does not have time to intervene. In that respect, Kandinsky was to some extent a precursor of Abstract Surrealism.

ACCOUNTING PRINCIPLES FOR PETORO AS

The annual accounts have been prepared in accordance with the provisions of the Norwegian Accounting Act and Norwegian generally-accepted accounting principles.

DESCRIPTION OF THE COMPANY’S BUSINESS

Petoro AS was established by the Ministry of Petroleum and Energy on behalf of the Norwegian government on 9 May 2001. The company’s object is to be responsible for and manage the commercial aspects of the state’s direct involvement in petroleum activities on the NCS, and all activities related hereto.

The state is the majority shareholder in Statoil ASA and the owner of the SDFI. On that basis, Statoil handles marketing and sales of the government’s petroleum. Petoro is responsible for supervising the way Statoil discharges its responsibilities under its marketing and sales instruction.

Petoro is also responsible for presenting separate annual accounts for the SDFI portfolio, and the cash flow for the SDFI is accordingly excluded from the limited company’s annual accounts.

VALUATION AND CLASSIFICATION OF ASSETS AND LIABILITIES

Assets intended for permanent ownership or use in the business are classified as fixed assets. Other assets are classed as current assets. Debtors due within one year are classified as current assets. Classification of current and long-term liabilities is based on the same criteria.

Fixed assets are carried at historical cost with a deduction for planned depreciation. Should the fair value of a fixed asset be lower than the book value, and this decline is not expected to be temporary, the asset will be written down to its fair value. Fixed assets with a limited economic lifetime are depreciated on a straight-line basis over their economic lifetime.

Current assets are valued at the lower of historic cost and fair value.

Current liabilities are carried at nominal value.

TANGIBLE FIXED ASSETS

Tangible fixed assets are capitalised and depreciated over the asset’s expected economic lifetime. Direct maintenance of tangible fixed assets is expensed when incurred under operating expenses, while upgrading or improvements are added to the asset’s historical cost and depreciated accordingly. Should the recoverable value of the fixed asset be lower than its book value, the asset will be written down to the recoverable amount. The recoverable amount is the higher of net sales value and utility value. Utility value is the present value of future cash flows which will be generated by the asset.

DEBTORS

Trade debtors and other debtors are carried at face value after a possible deduction for expected bad debts. Provision for bad debts is based on an individual assessment of each debtor.

BANK DEPOSITS

Bank deposits include bank deposits and other monetary instruments with a maturity of less than three months at the date of purchase.

PENSIONS

Pension costs and obligations are calculated on a linear earning of pension rights, based on a number of assumptions such as the discount rate, future pay adjustments, state pensions and other social security benefits, the expected return on pension fund assets, and actuarial assumptions on mortality and voluntary retirement. Pension funds are recorded in the balance sheet at their fair value less net pension commitments.

The company changed its method for the accounting treatment of actuarially-calculated estimate changes in 2005. Changes in pension commitments relating to changes in pension plans are allocated over the average remaining period of service. Changes in the commitment and in pension funds which arise as a result of changes to and variances in underlying pension assumptions (estimate changes) are allocated over the estimated average remaining pension-earning period to the extent that these variances exceed 10 per cent of the larger of gross pension commitments and pension fund assets at 1 January.

GOVERNMENT CONTRIBUTION

The company receives an operating grant over the central government budget for the specific fiscal year. Petoro invoices the government for the services it provides to the Ministry of Petroleum and Energy, up to the amount of operating grant appropriated for the year. This operating contribution is presented as operating revenue in the accounts. The invoiced operating grant for the year is intended to cover the company's operating costs and investments in the specific year. The contribution applied to investment for the year is accrued as deferred recording of revenue.

The services are subject to VAT, and the invoices submitted to the Ministry of Petroleum and Energy accordingly include output VAT.

LEASES

Leases which transfer a significant part of the financial risk and control from the lessor are treated as financial leases and capitalised. Other leases are treated as operational, and the associated expenses are expensed.

INCOME TAXES

The company is exempt from tax under section 2-30 of the Income Tax Act.

CASH FLOW STATEMENT

The cash flow statement has been prepared using the indirect method. Cash and cash equivalents include cash, bank deposits and other short-term liquid placements.

NOTE 1 – GOVERNMENT CONTRIBUTION AND OTHER REVENUE

The company received an operating contribution from the Norwegian government totalling NOK 174.3 million excluding VAT in 2005. The government contribution for the year and deferred recording of revenue and other revenue, a total of NOK 180.3 million, covered operating costs of NOK 177.9 million. In addition, the contribution covered net investment of NOK 2.4 million in 2005. Other revenue primarily relates to invoicing of services provided to operators of joint ventures.

NOTE 2 – DEFERRED REVENUE

The contribution received by Petoro from the government is primarily applied to meeting current operating expenses. Where new capital spending is concerned, part of the contribution received is applied to the capitalised investment. Under Norwegian accounting standard NRS 4, contributions applied to investment must be capitalised on a gross basis. The asset is booked at acquisition cost and depreciated over its economic life. The contribution is treated as deferred recording of revenue and entered as a provision in the balance sheet. The contribution is recorded as revenue as the investment is depreciated, and specified as operating revenue in the income statement.

Capitalised deferred revenue	All figures in NOK 1 000	2005	2004	2003
Capitalised deferred revenue at 1 Jan		16 472	14 877	0
Deferred recording of revenue in the balance sheet		2 429	5 875	15 400
Recording of deferred revenue in the income statement		(5 806)	(4 279)	(524)
Capitalised deferred revenue at 31 Dec		13 095	16 472	14 877

NOTE 3 – PAYROLL EXPENSES, NUMBER OF EMPLOYEES, BENEFITS, ETC

Payroll expenses	All figures in NOK 1 000	2005	2004	2003
Pay		50 647	48 143	48 632
Payroll taxes		10 142	8 774	7 533
Pensions (note 9)		17 077	16 477	15 614
Other benefits		1 441	1 243	973
Total		79 306	74 637	72 751

Employees at 31 December	53	59	55
Employees with a signed contract who had not started work at 31 December	4	0	1
Average number of work-years	57	57	55

Remuneration of senior executives	All figures in NOK 1 000	Pay	Recorded pension liability	Other benefits
President and CEO		2 559	1 596	123

The president's retirement age is 62. He can choose to retire on a full pension upon reaching the age of 60. Should he exercise this right, he must make himself available to the company for 25 per cent of full-time employment until the age of 62. Recorded pension liability represents the actuarially-estimated cost for the year of the pension obligation for the president.

DIRECTORS' FEES

Fees paid in 2004 totalled NOK 270 000 for the chair and NOK 937 500 for the other directors combined.

NOTE 4 – TANGIBLE FIXED ASSETS

All figures in NOK 1 000	Fixed fittings, leased building	Equipment, etc	ICT	Total tangible assets
Purchase cost 1 Jan 05	3 075	6 787	13 057	22 919
Additions (purchased)	0	0	2 429	2 429
Disposals	0	0	0	0
Purchase cost at 31 Dec 05	3 075	6 787	15 486	25 348
Accumulated depreciation	629	3 953	7 414	11 996
Book value at 31 Dec 05	2 446	2 834	8 072	13 352
Depreciation for the year	280	1 491	4 327	6 098
Economic life	11 years	3/5 years	3 years	
Depreciation plan	Linear	Linear	Linear	
Annual rent, non-capitalised fixed assets		406	240	

NOTE 5 – OTHER DEBTORS

Other debtors consist in their entirety of pre-paid costs, relating primarily to rent, insurance, ICT licences and subscriptions for market information.

NOTE 6 – BANK DEPOSITS

Bank deposits comprise NOK 3 199 305 in withheld tax.

NOTE 7 – SHARE CAPITAL AND SHAREHOLDER INFORMATION

The share capital of the company at 31 December 2005 comprised 10 000 shares with a nominal value of NOK 1 000 each.

All the shares are owned by the Ministry of Petroleum and Energy on behalf of the Norwegian government, and all have the same rights.

NOTE 8 – EQUITY

All figures in NOK 1 000	Share capital	Other equity
Equity at 1 Jan 05	10 000	4 716
Current changes in equity:		
Net income/(loss)	0	937
Equity at 31 Dec 05	10 000	5 653

NOTE 9 – PENSION COSTS, FUNDS AND LIABILITIES

The company has collective pension plans covering all its employees. This scheme gives the right to defined future benefits. These depend primarily on the number of years of pensionable earnings, the level of pay at retirement and the size of national insurance benefits. Pension liabilities are funded.

Net pension cost	All figures in NOK 1 000	2005	2004	2003
Net present value of benefits earned during the year		12 027	11 429	12 102
Interest expense on pension obligation		3 598	2 552	595
Return on pension funds		(3 180)	(2 447)	(661)
Recorded change in estimates		4 305	3 814	1 145
Payroll tax		2 362	2 164	1 858
Net pension cost		19 112	17 512	15 039

Net pension liability	All figures in NOK 1 000	2005	2004	2003
Estimated pension obligation at 31 Dec		75 581	56 518	22 619
Pension plan assets (market value) at 31 Dec		(65 117)	(41 729)	(14 515)
Capitalised pension obligations before payroll tax		10 464	14 789	8 104
Unrecorded change in estimates		(3 450)	0	0
Payroll tax		2 188	2 085	1 143
Net pension liability		9 202	16 875	9 247

The following financial assumptions have been applied in calculating net pension cost and liability:

Discount rate	6.0%
Expected increase in pay/NI base rate	3.0%
Expected increase in pensions	2.5%
Expected return on plan assets	7.0%

The company changed its method for the accounting treatment of actuarially-calculated estimate changes in 2005. Changes in pension funds from 2004 are recorded in their entirety in 2005. The accounting consequence of these estimate changes total NOK 0.9 million in higher pension costs.

NOTE 10 – CURRENT LIABILITIES

Other than trade creditors, the company’s current liabilities relate almost wholly to public duties payable and provision for costs incurred but not invoiced.

NOTE 11 – AUDITOR’S FEES

Erga Revisjon AS is the elected auditor of Petoro AS. Fees charged by Erga Revisjon to Petoro for external auditing in 2004 totalled NOK 200 625 excluding VAT. In accordance with the Act on Government Auditing of 7 May 2004, the Auditor General is the external auditor for the SDFI. Deloitte has also been engaged to conduct a financial audit of the SDFI as part of the company’s internal audit function. Deloitte charged NOK 1.5 million for this service in 2005. Deloitte has also performed services relating to partner audits, reviewed pro and contra in connection to the SDFI asset sales, and provided services relating to the assessment of changed accounting principles in the SDFI accounts. Deloitte charged a total of NOK 1.2 million for these services.



GERRIT RIETFELD:
The Schröder House,
Utrecht, 1923-24.

The architects and sculptors in the De Stijl group worked along the same lines, and sought a common idiom in every medium. In Reitfeld’s Schröder House, the boundaries between surfaces, sculpture and architecture are fluid, since the interaction between colours, structural blocks and three-dimensional space create tension and harmony in the building. The house is a precursor of Functionalism.

NOTE 12 – BUSINESS MANAGEMENT AGREEMENTS

To ensure efficient resource utilisation with an organisation of 60 employees, Petoro prioritises its work commitments in and between the interests it manages in the various joint ventures. This prioritisation reflects the significance of each joint venture to the overall value of the portfolio and risk assessments related to the various phases in a joint venture (exploration, development and production). To permit such prioritisation, Petoro has concluded business management agreements with licence partners such as Statoil, ConocoPhillips, Lundin and Total. These agreements delegate daily administrative supervision of selected production licences in the portfolio. Petoro nevertheless retains the formal responsibility, including responsibility for on-going financial management of the interest in the production licence.

NOTE 13 – LEASES

The company has leased office premises from Smedvig Eiendom AS. This lease runs for nine years. The expected annual rent is NOK 5.3 million.

The company has no lease agreements which fulfil the requirements for capitalisation.

NOTE 14 – SIGNIFICANT CONTRACTS

Petoro has concluded an agreement with Accenture ANS covering accounting-related transaction processing and system applications for the SDFI and Petoro AS. This agreement was concluded in 2002 for five years, with an option for a further two years. The option for that part of the contract relating to accounting services for the SDFI was exercised in 2005.

Petoro concluded a frame agreement in 2005 with Alliance ANS on operation and maintenance of Petoro’s computer systems, infrastructure and communication. This agreement runs for three years, with options to two one-year extensions.

NOTE 15 – RELATED PARTIES

Statoil ASA and Petoro AS have the same owner in the Ministry of Petroleum and Energy, and are accordingly related parties. Petoro purchased services in 2005 relating to business management agreements, cost sharing for the audit of licence accounts, insurance services for the Government Petroleum Insurance Fund and other minor services. NOK 3.5 million was charged to the accounts in 2005 for the purchase of services from Statoil. These services were purchased at market price on the basis of hours worked. At 31 December 2005, Petoro owed NOK 44 360 to Statoil. This amount is included under trade creditors in the balance sheet.



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To the Annual Shareholders' Meeting of PETORO AS

Auditor’s report for 2005

We have audited the annual financial statements of the PETORO AS as of 31 December 2005, showing a profit of NOK 937 000. We have also audited the information in the Board of Directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the profit. The annual financial statements comprise the balance sheet, the statements of income and cash flows and the accompanying notes. The rules of the Norwegian accounting act and good accounting practice in Norway have been applied to produce the financial statements. 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 the other information according to the requirements of the Norwegian Act on Auditing and Auditors.

We conducted our audit in accordance with the Norwegian Act on Auditing and Auditors and good auditing practice in Norway, including standards on auditing adopted by Den Norske Revisorforening. 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 good auditing practice 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 are 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 for the year then ended, in accordance with good accounting practice in Norway
- 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 Board of Directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the profit are consistent with the financial statements and comply with the law and regulations.

Stavanger, 23 February 2006.
Erga Revisjon as

Sven Erga (not to be signed)
State Authorised Public Accountant (Norway)
Note: The translation from Norwegian has been prepared for information purposes only.

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