

**KAROON GAS AUSTRALIA LIMITED
AND CONTROLLED ENTITIES
ABN 53 107 001 338**

**QUARTERLY FINANCIAL REPORT
FOR THE QUARTER ENDED 31ST DECEMBER 2006**

Review of Operations

Browse Basin Assets WA-314-P and WA-315-P

Seismic Update

Karoon Gas has taken possession of the final processed 3D data from its 284 sq km seismic acquisition in WA-315-P. This completes the 2D and 3D seismic data set that was acquired throughout 2006. This data will be interpreted over the coming months, and is expected to be completed in the 2nd Quarter 2007.

Interpreted data has already confirmed the position and size of the two leads (Updip Buffon and A Lead) in the survey area.

Improved data quality and coverage has allowed the volcanic's and reservoir intervals within the closures to be mapped far more accurately to better define leads and prospects from the earlier 2D seismic mapping. An extensive and detailed mapping and analysis program is ongoing to best define drilling locations.

Joint Venture with ConocoPhillips

On the 9th of October 2006 Karoon Gas Australia Ltd entered into agreements to farm out up to a 60% interest in its Browse Basin permits, WA-314-P and WA-315-P, to the ConocoPhillips Group subsidiary company, ConocoPhillips SH2 Pty Ltd.

Acquisition of 51% Interest

Pursuant to the agreements, consisting of a joint operating agreement and separate farmin agreement, ConocoPhillips SH2 have acquired a 51% interest in the permits by:

1. Paying Karoon US\$9.6 million in reimbursement of approximately 80% of the costs incurred in carrying out the second year work programme for the permits. This involved the acquisition, processing and interpretation of seismic surveys completed throughout 2006, comprising approximately 1200 sq kms of 3D Seismic and 800 kms of 2D seismic.
2. Funding 80% of the costs of the third year work programme for the permits which will require the drilling of one exploration well in each permit including testing. The cost of the third year work programme which is subject to the 80% funding arrangement is estimated to be between US\$60-80 million.

Drilling Update

Karoon with its joint venture partner, ConocoPhillips, is currently in the process of area mapping and target selection.

An application has been submitted to the DOIR for a permit extension within which to complete its Year 3 work commitments by February 2008. Drilling is planned for the second half of 2007, the delay is due to the availability of an offshore rig.

Karoon interest 49%

Karoon will retain 49% equity in the permits WA-314-P and WA-315-P.

Gippsland Assets PEP162 and EL4537

Karoon secured the Drilling Services Company Upstream Petroleum Service to contract with Century Drilling Services and Operate a Drilling program for Karoon. The first well in the drilling program was spudded 13th December 2006 and completed on the 28th December 2006. Karoon successfully re-entered, sidetracked the original Megascolides-1 hole and cored the Rintouls Creek Formation sandstones. High gas readings were recorded with good oil fluorescence and oil staining seen over much of the recovered core sections. Core recovery was 85% with porosities up to 11 percent measured from core analysis.

Permeability measurements however were all very low, indicating very low potential for this formation to flow oil at this location. With these results Karoon is plugging and abandoning the Megasscolides-1 well.

The drilling program will continue into 2007. The next well, Megascolides-2, located 1.2 km to the east and near the crest of the greater Megascolides structure has the Rintouls Creek Formation target over 200m shallower. Here the well is located within a closure and at these shallower depths porosity and permeability are expected to be improved offering an attractive target.

Karoon interest 100%

Karoon Gas (through its 100% owned subsidiary Karoon Gas Pty Ltd) has a 100% Registered interest in PEP162 and EL4537, within the Western on-shore Gippsland Basin of Victoria. The Megascolides – 1 drilling site is located approximately 100 Kilometres South East of Melbourne.

For further information please contact:

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Company Secretary

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Appendix 5B

Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/2001.

Name of entity

Karoon Gas Australia Ltd

ABN

53 107 001 338

Quarter ended ("current quarter")

December 2006

Consolidated statement of cash flows

Cash flows related to operating activities	Current quarter \$A'000	Year to date (12 months) \$A'000
1.1 Receipts from product sales and related debtors		
1.2 Payments for (a) exploration and evaluation (b) development (c) production (d) administration	10,917	6,060
1.3 Dividends received	(1,054)	(1,371)
1.4 Interest and other items of a similar nature received	443	639
1.5 Interest and other costs of finance paid		
1.6 Income taxes paid		
1.7 Other - GST refunds	124	659
Net Operating Cash Flows	10,430	5,987
Cash flows related to investing activities		
1.8 Payment for purchases of: (a)prospects (b)equity investments (c) other fixed assets	(58)	(112)
1.9 Proceeds from sale of: (a)prospects (b)equity investments (c)other fixed assets		
1.10 Loans to other entities		
1.11 Loans repaid by other entities		
1.12 Other (provide details if material)		
Net investing cash flows	(58)	(113)
1.13 Total operating and investing cash flows (carried forward)	10,372	5,874

1.13	Total operating and investing cash flows (brought forward)	10,372	5,874
	Cash flows related to financing activities		
1.14	Proceeds from issues of shares, options, etc.	21,260	21,532
1.15	Proceeds from sale of forfeited shares		
1.16	Proceeds from borrowings		
1.17	Repayment of borrowings		
1.18	Dividends paid		
1.19	Other (provide details if material)		
	Net financing cash flows	21,260	21,532
	Net increase (decrease) in cash held	31,632	27,406
1.20	Cash at beginning of quarter/year to date	11,471	15,701
1.21	Exchange rate adjustments to item 1.20	(539)	(543)
1.22	Cash at end of quarter	42,564	42,564

Payments to directors of the entity and associates of the directors
Payments to related entities of the entity and associates of the related entities

		Current quarter \$A'000
1.23	Aggregate amount of payments to the parties included in item 1.2	95
1.24	Aggregate amount of loans to the parties included in item 1.10	Nil

1.25 Explanation necessary for an understanding of the transactions

Directors Fees included in 1.23 : \$ 33
Consulting Fees included in 1.23 : \$ 62

Non-cash financing and investing activities

2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

Nil

2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

Nil

Financing facilities available

Add notes as necessary for an understanding of the position.

	Amount available \$A'000	Amount used \$A'000
3.1 Loan facilities	Nil	Nil
3.2 Credit standby arrangements	Nil	Nil

Estimated cash outflows for next quarter

	\$A'000
4.1 Exploration and evaluation	6,500
4.2 Development	Nil
Total	

Reconciliation of cash

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.

	Current quarter \$A'000	Previous quarter \$A'000
5.1 Cash on hand and at bank	842	6,297
5.2 Deposits at call (see note 6)	41,722	5,174
5.3 Bank overdraft		
5.4 Other (provide details)		
Total: cash at end of quarter (item 1.22)	42,564	11,471

Changes in interests in mining tenements

	Tenement reference	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1	Interests in mining tenements relinquished, reduced or lapsed			
6.2	Interests in mining tenements acquired or increased			

Issued and quoted securities at end of current quarter

Description includes rate of interest and any redemption or conversion rights together with prices and dates.

	Total number	Number quoted	Issue price per security (see note 3) (cents)	Amount paid up per security (see note 3) (cents)
7.1 Preference securities (description)				
7.2 Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions				
7.3 +Ordinary securities	94,427,897	94,427,897		
7.4 Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs (c) Shares out of escrow	13,186,000	13,186,000		
7.5 +Convertible debt securities (description)				
7.6 Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7 Options (description and conversion factor)	500,000 1,500,000 1,500,000 1,500,000 500,000 500,000 100,000 475,000		<i>Exercise price</i> 25 cents 175 cents 200 cents 235 cents 165 cents 135 cents 160 cents 203 cents	<i>Expiry date</i> 30 June 2007 30 Sept 2008 30 Sept 2008 30 Sept 2008 31 Oct 2007 30 June 2007 1 August 2008 31 Oct 2008
7.8 Issued during quarter				
7.9 Exercised during quarter	1,000,000		25 cents	
7.10 Expired during quarter				
7.11 Debentures (totals only)				
7.12 Unsecured notes (totals only)				

Compliance statement

- 1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX (see note 5).
- 2 This statement does give a true and fair view of the matters disclosed.

Sign here: Date:30 January 2006
(Company secretary)

Print name: ..Scott Hosking.....

Notes

- 1 The quarterly report provides a basis for informing the market how the entity's activities have been financed for the past quarter and the effect on its cash position. An entity wanting to disclose additional information is encouraged to do so, in a note or notes attached to this report.
- 2 The "Nature of interest" (items 6.1 and 6.2) includes options in respect of interests in mining tenements acquired, exercised or lapsed during the reporting period. If the entity is involved in a joint venture agreement and there are conditions precedent which will change its percentage interest in a mining tenement, it should disclose the change of percentage interest and conditions precedent in the list required for items 6.1 and 6.2.
- 3 **Issued and quoted securities** The issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.
- 4 The definitions in, and provisions of, *AASB 1022: Accounting for Extractive Industries* and *AASB 1026: Statement of Cash Flows* apply to this report.
- 5 **Accounting Standards** ASX will accept, for example, the use of International Accounting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.
- 6 **Deposits at Call** Included in the deposits at call is a US dollar term deposit for \$12,678,561.00 which has been converted to Australian dollars for recording purposes only at a rate of .7913 (the USD/AUD exchange rate on the last day of the period).

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Note 1

Schedule of Exploration Permits

Held by the Consolidated Entity

At 31st December 2006

<u>Exploration Permits</u>	<u>Basin</u>	<u>Interest %</u>
PEP162	Gippsland	100
EL 4537	Gippsland	100
WA 314-P	Browse	100
WA 315-P	Browse	100