
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 20-F

(Mark one)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g)
OF THE SECURITIES EXCHANGE ACT OF 1934
OR
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended: December 31, 1997
OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number: 1-11912

LASMO plc

(Exact name of Registrant as specified in its charter)

England and Wales

(Jurisdiction of incorporation or organization)

101 Bishopsgate, London EC2M 3XH, England

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
American Depositary Shares Ordinary shares of 25p each	New York Stock Exchange New York Stock Exchange*
American Depositary Shares, Series A	New York Stock Exchange
Cumulative Dollar Preference Shares, Series A (nominal value of \$25 each)	New York Stock Exchange*

* Not for trading, but only in connection with the registration of American Depositary Shares representing such shares, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the Annual Report:

Ordinary shares of 25p each 965,966,362
Cumulative Dollar Preference Shares, Series A (nominal value of \$25 each) 10,000,000

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes

No

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17

Item 18

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INTRODUCTION

LASMO plc (the “Company”) is a public limited company incorporated in England and Wales. The Company conducts its operations directly and through subsidiaries. The term “LASMO” as used in this Annual Report on Form 20-F (the “Annual Report”) refers to the Company and/or its subsidiaries as appropriate and the term “Group” refers to the Company and its subsidiaries.

For reporting purposes, LASMO presently divides its activities into three regional areas: UK (comprising the UK Continental Shelf (“UKCS”) and The Netherlands North Sea interests), Indonesia and International (comprising all of LASMO’s interests outside UK and Indonesia). The data in this Annual Report is presented according to these geographical segments.

References contained in this Annual Report to net acreage and interests in oil and gas licenses are specified throughout on a working interest basis.

In this Annual Report, oil and gas reserve information is presented on the proved reserves basis, estimated in accordance with definitions specified by the Securities and Exchange Commission (the “Commission”). Reserve amounts are estimates and are subject to revision. See “Item 1. Description of Business — Reserves”. Reserves and production included in respect of interests subject to production sharing contracts (“PSCs”), such as LASMO’s interests in Indonesia, are stated net of government share.

For conversion factors and definitions of certain oil and gas terms used throughout this Annual Report, see “Conversion Table” and “Certain Oil and Gas Terms”.

References in this Annual Report to the “AUK Loan Notes” are to the Guaranteed Unsecured Floating Rate Notes 2003, guaranteed by Elf Aquitaine Société Nationale, issued in 1988 by AUK (formerly AUK Limited, formerly Aquitaine UK Limited) as consideration for the purchase of LASMO’s 25.2% investment in Enterprise Oil plc, which was sold on December 22, 1988. For further discussion of the AUK Loan Notes, see “Item 9. Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Financing” and Notes 14 of Notes to the Financial Statements included elsewhere herein.

References in this Annual Report to “Sterling Preference Shares” are to the Cumulative Redeemable Preference Shares of £1 each, which were redeemed on July 15, 1996. References to “Dollar Preference Shares” are to the Cumulative Dollar Preference Shares, Series A of \$25 each.

The Company publishes its consolidated financial statements in pounds sterling. In this Annual Report, references to “pounds sterling”, “£”, “pence” or “p” are to UK currency, references to “US dollars”, “US\$” or “\$” are to US currency. Merely for the convenience of the reader, this Annual Report contains translations of certain pound sterling amounts into US dollars at specified rates, or, if not so specified, the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York (the “Noon Buying Rate”) on December 31, 1997 of £1.00 = \$1.64. No representation is made that the pound sterling amounts have been, could have been or could be converted into US dollars at the rates indicated or at any other rates. See “Item 8. Selected Consolidated Financial Data — Exchange Rates” for historical information regarding Noon Buying Rates.

The principal executive office of the Company is located at 101 Bishopsgate, London EC2M 3XH, England and its telephone number is 011-44171-892-9000.

This Annual Report on Form 20-F contains certain forward-looking statements as defined in Section 21E of the United States Securities Exchange Act of 1934 with respect to the financial condition, results of operations and business of LASMO and certain of the plans and objectives of management of LASMO with respect thereto. Such statements include, but are not limited to, statements contained in or implied by the discussion under “Item 1. Description of Business”, “Item 9. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Item 9A. Qualitative and Quantitative Disclosures on Market Risks”.

By their nature, forward-looking statements involve risk and uncertainty, and the factors described in the context of such forward-looking statements, and other factors referred to in this Annual Report on Form 20-F, particularly in “Item 1. Description of Business — Reserves”, “— Regulation” and “— Additional Factors Which May Affect Business”, “Item 9. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Item 9A. Qualitative and Quantitative Disclosures on Market Risks”, could cause actual results and developments to differ materially from those expressed in or implied by such forward-looking statements.

CONVERSION TABLE

1 acre	= 0.405 hectares
1 barrel	= 42 US gallons
1 barrel of oil equivalent	= 1 barrel of crude oil
	= 6,000 cubic feet of natural gas

CERTAIN OIL AND GAS TERMS

Unless the context indicates otherwise, the following terms have the meanings shown below:

“acre gross”	The total area, expressed in acres, over which LASMO has the interests in question.
“acre net”	The proportion of the total area, expressed in acres, equal to LASMO’s percentage interest in the relevant exploration or production area.
“appraisal well”	A well drilled for the purpose of further assessing a discovery.
“barrels” or “bbls”	Barrels of crude oil.
“Bcf”	Billions (000,000,000s) of standard cubic feet.
“blocks”	The commonly used term for concession areas.
“boe”	Barrels of oil equivalent.
“boepd”	Barrels of oil equivalent per day.
“bopd”	Barrels of oil per day.
“Btu”	British thermal unit.
“condensate”	Liquid hydrocarbons which are sometimes produced with natural gas and liquids derived from natural gas.
“crude oil”	Crude oil, including condensate, natural gas liquids and LPG.
“entitlement reserves”	In Indonesia, Algeria and Libya, LASMO has no ownership interest in oil and gas reserves, but rather has the right to receive production and/or revenues from the sale of oil, condensate, gas, liquefied natural gas and petroleum gas in accordance with PSCs and other agreements. The reserves have therefore been presented on a net entitlement basis, which takes into account projections of government share of production calculated in accordance with certain price and expenditure assumptions.
“farmin/farmout”	The acquisition/disposal of an interest by a means which generally involves the performance of work, such as drilling a well or the payment for work to be performed by a third party.
“LNG”	Liquefied natural gas.

“LPG”	Liquefied petroleum gas.
“Mbopd”	Thousands of barrels of oil per day.
“Mboepd”	Thousands of barrels of oil equivalent per day.
“Mcf”	Thousands of standard cubic feet.
“Mcfd”	Thousands of standard cubic feet per day.
“MMb”	Millions of barrels.
“MMboe”	Millions of barrels of oil equivalent.
“MMcfd”	Millions of standard cubic feet per day.
“MMBtu”	Millions of British thermal units.
“natural gas”	Any hydrocarbons or mixture of hydrocarbons and other gases consisting primarily of methane which at normal operating conditions is in a gaseous state.
“natural gas liquids”	Light hydrocarbons consisting mainly of propane and butane which are liquid under pressure at normal temperature.
“operator”	The company appointed to conduct operations under the license or concession.
“proved reserves”	<p>The estimated quantities of crude oil, natural gas, and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made. Prices include consideration of changes in existing prices provided only by contractual arrangements, but not on escalations based upon future conditions.</p> <p>(i) Reservoirs are considered proved if economic producibility is supported by either actual production or conclusive formation test. The area of a reservoir considered proved includes (A) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any; and (B) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of hydrocarbons controls the lower proved limit of the reservoir.</p> <p>(ii) Reserves which can be produced economically through application of improved recovery techniques (such as fluid injection) are included in the “proved” classification when successful testing by a pilot project, or the operation of an installed program in the reservoir, provides support for the engineering analysis on which the project or program was based.</p> <p>(iii) Estimates of proved reserves do not include the following: (A) oil that may become available from known reservoirs but is classified separately as “indicated additional reserves”; (B) crude oil, natural gas, and natural gas liquids, the recovery of which is subject to reasonable doubt because of uncertainty as to geology, reservoir characteristics, or economic factors; (C) crude oil, natural gas, and natural gas liquids, that may occur in undrilled prospects; and (D) crude oil, natural gas, and</p>

natural gas liquids, that may be recovered from oil shales, coal, gilsonite and other such sources.

“proved developed reserves”

The crude oil and natural gas reserves expected to be recovered through existing wells with existing equipment and operating methods. Additional oil and gas expected to be obtained through the application of fluid injection or other improved recovery techniques for supplementing the natural forces and mechanisms of primary recovery should be included as “proved developed reserves” only after testing by a pilot project or after the operation of an installed program has confirmed through production response that increased recovery will be achieved.

“proved undeveloped reserves”

The crude oil and natural gas reserves expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion. Reserves on undrilled acreage shall be limited to those drilling units offsetting productive units that are reasonably certain of production when drilled. Proved reserves for other undrilled units can be claimed only where it can be demonstrated with certainty that there is continuity of production from the existing productive formation.

“proven and probable reserves”

Proven and probable reserves and commercial reserves form the basis for unit-of-production calculations presented in accordance with UK GAAP in the financial statements. Proved crude oil and natural gas reserves as presented in this Annual Report have been calculated in accordance with the Commission definitions and differ significantly from proven and probable reserves which LASMO publishes in accordance with UK practice.

Proven and probable reserves are the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty (see below) to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50% statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and probable and a 50% statistical probability that it will be less. The equivalent statistical probabilities for the proven component of proven and probable reserves are 90% and 10%, respectively.

Commercial reserves are those quantities of petroleum which are considered, on the basis of information currently available and current economic forecasts, to be commercially recoverable from fields currently in production, fields under development, fields for which a development plan is under active preparation and fields whose proximity to established infrastructure assure their future development.

“TBtu”

Trillions (000,000,000,000s) of British thermal units.

“Tcf”

Trillions of cubic feet.

“unitization”

Where a field located in two or more blocks is operated as one field under an agreement between all the various participants.

PART I

ITEM 1. DESCRIPTION OF BUSINESS

General

The Company, which is the holding company of the Group, was incorporated as London & Scottish Marine Oil Company Limited on April 23, 1971. It was formed by a number of UK financial institutions to explore for and produce oil and gas, initially in the UK sector of the North Sea. Following the Ninian discovery in 1974, LASMO commenced international expansion. At the end of 1991, LASMO acquired control of Ultramar PLC and its subsidiaries ("Ultramar") through a public offer for Ultramar shares. The Ultramar businesses acquired by LASMO included oil and gas exploration and production activities and, in particular, a significant position in the Pacific Basin LNG market through a 37.81% interest in a joint venture that produces natural gas and, to a lesser but nonetheless significant extent, oil and condensate from several fields in Indonesia. LASMO merged Ultramar's upstream businesses with its existing business and completed the disposal of Ultramar's downstream businesses during 1992.

LASMO is now a substantial international oil and gas exploration and production company whose producing assets are presently concentrated primarily in the UK and Indonesia regions, and these regions together with Venezuela and Algeria are the major contributors to reserves. At the end of 1997, LASMO was active in thirteen countries around the world, in eight of which it acted as operator. Production during 1997 was derived from seven of these countries, principally the United Kingdom, The Netherlands, Indonesia, Colombia and Pakistan.

At December 31, 1997, LASMO's net proved oil and gas reserves were estimated at 849 MMboe, of which approximately 62% relate to oil and approximately 38% relate to gas, with 21% of the Group's net proved reserves located in the UK region, 29% located in the Indonesia region, 26% located in Venezuela and 11% located in Algeria. For the year ended December 31, 1997, approximately 55% of the Group's average daily production of 173 Mboepd derived from the UK region (where at December 31, 1997, LASMO had interests in 21 fields in production, three fields under development and a further four fields subject to development studies) and approximately 36% derived from the Indonesia region. In the same period, production of crude oil and natural gas each accounted for approximately 51% and 49% respectively of LASMO's average daily production.

LASMO aims to create value through international oil and gas exploration, production and related business activities, thereby providing shareholders with a competitive return on investment over the long term, principally through capital growth. The Group seeks to build on existing significant businesses while looking to identify material platforms for growth in new areas, targeting prolific hydrocarbon basins with low cost structures, of particular value in a low oil price environment. In addition to its existing core areas of the UK and Indonesia, LASMO has identified North Africa, Venezuela and Pakistan as three new core areas with material businesses at varying degrees of maturity. Where a region fails to demonstrate the potential to develop a material business, LASMO will consider withdrawing. In this context, it withdrew from Gabon effective January 1, 1997, has announced its intention of withdrawing from Colombia and is reviewing its business in Italy.

This asset management program continues earlier rationalization. In the period 1992 to 1996, LASMO rationalized the Group's portfolio by actively managing its assets through disposals, farmouts and swaps. Disposals in 1992 raised £732 million and by the end of 1996 asset sales had raised a further £552 million. LASMO will continue to manage its assets through disposals, farmouts and swaps in order to seek to reduce its cost base and improve efficiency. LASMO will also consider selective acquisitions in the pursuit of its objectives consistent with its stated strategy.

The table below sets forth an analysis of LASMO's sales and profit/(loss) by operating region for each of the years ended December 31, 1997, 1996 and 1995. See Note 2 of Notes to the Financial Statements for an analysis of sales by category.

	UK			Indonesia			International			Total		
	Year ended December 31											
	1997	1996	1995	1997	1996	1995	1997	1996	1995	1997	1996	1995
	(£ million)											
Sales (by source)	405	350	255	272	344	285	45	55	97	722	749	637
Cost of sales before exceptional items	(283)	(257)	(219)	(129)	(164)	(151)	(40)	(46)	(67)	(452)	(467)	(437)
Gross profit before exceptional items	122	93	36	143	180	134	5	9	30	270	282	200
Net exploration costs	(18)	(16)	(10)	(8)	(3)	(4)	(28)	(29)	(22)	(54)	(48)	(36)
Administrative expenses	(11)	(7)	(10)	(2)	(4)	(3)	(5)	(3)	—	(18)	(14)	(13)
Operating profit/(loss) before exceptional items	93	70	16	133	173	127	(28)	(23)	8	198	220	151
Exceptional items												
Net provisions for oil and gas assets	—	—	(17)	—	—	—	—	2	2	—	2	(15)
Provision for reorganization costs	—	—	(5)	—	—	—	—	—	—	—	—	(5)
Profit/(loss) on sale of fixed assets	—	—	15	—	—	(1)	—	20	—	—	20	14
Profit/(loss)	<u>93</u>	<u>70</u>	<u>9</u>	<u>133</u>	<u>173</u>	<u>126</u>	<u>(28)</u>	<u>(1)</u>	<u>10</u>	198	242	145
Unallocated administrative expenses										(14)	(14)	(9)
Provision for reorganization costs										—	—	(10)
										184	228	126
Downstream (provision)/release										—	(2)	17
Net interest (expense)/income and similar items										(30)	(20)	1
Profit before taxation										<u>154</u>	<u>206</u>	<u>144</u>

Reserves

Proved crude oil and natural gas reserves as presented in this Annual Report have been calculated in accordance with Commission definitions and differ significantly from proven and probable reserves which LASMO publishes in accordance with UK practice. See "Certain Oil and Gas Terms".

Proved Reserves

At December 31, 1997, LASMO's combined net proved reserves of crude oil and natural gas were estimated at 849 MMboe. Of this total, approximately 53% consisted of proved developed reserves and approximately 47% consisted of proved undeveloped reserves. Crude oil represented approximately 62% of the combined net proved reserves and natural gas represented approximately 38%. The proved reserves are principally located in the UK and Indonesia regions and in Venezuela and Algeria, accounting for 21%, 29%, 26% and 11% respectively, of total Group proved reserves. Of total net proved natural gas reserves at December 31, 1997, 68% was located in the Indonesia region.

During 1997, discoveries and extensions have resulted in the addition of 58.1 MMboe of net proved reserves, replacing 92% of production in the same period. Including net revisions of 61.4 MMboe, this percentage increases to 189%. Taking account of an increase of 234.4 MMboe due to acquisitions net of disposals, the overall net proved reserve replacement during 1997 amounted to 561%.

From the beginning of 1995 to the end of 1997, discoveries and extensions have resulted in the addition of 127.0 MMboe of net proved reserves, replacing 68% of production in the same period. Including net revisions of 88.1 MMboe, this percentage increases to 115%. Taking account of an increase of 221.5 MMboe due to acquisitions net of disposals, the overall net proved reserve replacement in the period from January 1, 1995 to December 31, 1997 amounted to 233%.

The table below sets forth by geographic area net proved developed and undeveloped crude oil and natural gas reserves. For fields in the Sanga Sanga PSC, gross field oil and wet gas reserves were estimated by DeGolyer and MacNaughton, independent petroleum engineering consultants, and net field oil and dry gas

reserves were estimated by petroleum engineers employed by LASMO in reliance on the report prepared by DeGolyer and MacNaughton as experts with respect to such matters contained therein. For further information, see “Supplementary Disclosures relating to Crude Oil and Natural Gas Producing Activities (Unaudited)”.

	Crude Oil and Natural Gas Reserves(1)								
	UK		Indonesia		International		Total		
	Crude Oil	Natural Gas	Crude Oil	Natural Gas	Crude Oil	Natural Gas	Crude Oil	Natural Gas	Combined
	(MMb)	(Bcf)	(MMb)	(Bcf)	(MMb)	(Bcf)	(MMb)	(Bcf)	(MMboe)
At January 1, 1995	127.8	584.5	43.9	1,610.3	44.2	102.8	215.9	2,297.6	598.9
Revisions of previous estimates	12.5	12.2	(1.9)	(27.0)	6.2	(41.3)	16.8	(56.1)	7.4
Extensions, discoveries and other	—	0.2	—	—	19.4	—	19.4	0.2	19.4
Sales of reserves in place . .	(2.2)	—	(9.0)	—	—	—	(11.2)	—	(11.2)
Purchases of reserves in place	—	20.1	—	—	—	—	—	20.1	3.4
Production for the year	<u>(17.1)</u>	<u>(47.3)</u>	<u>(3.4)</u>	<u>(133.5)</u>	<u>(8.0)</u>	<u>(7.3)</u>	<u>(28.5)</u>	<u>(188.1)</u>	<u>(59.9)</u>
At December 31, 1995	121.0	569.7	29.6	1,449.8	61.8	54.2	212.4	2,073.7	558.0
Revisions of previous estimates	4.1	23.0	4.3	11.7	6.0	(5.5)	14.4	29.2	19.3
Extensions, discoveries and other	—	—	—	—	49.5	—	49.5	—	49.5
Sales of reserves in place . .	—	—	—	—	(6.7)	—	(6.7)	—	(6.7)
Purchases of reserves in place	0.1	8.7	—	—	—	—	0.1	8.7	1.6
Production for the year	<u>(21.2)</u>	<u>(59.9)</u>	<u>(3.4)</u>	<u>(143.9)</u>	<u>(3.8)</u>	<u>(9.5)</u>	<u>(28.4)</u>	<u>(213.3)</u>	<u>(64.0)</u>
At December 31, 1996	104.0	541.5	30.5	1,317.6	106.8	39.2	241.3	1,898.3	557.7
Revisions of previous estimates	26.8	(47.8)	2.1	121.3	20.4	(0.9)	49.3	72.6	61.4
Extensions, discoveries and other	—	—	—	—	31.4	160.0	31.4	160.0	58.1
Sales of reserves in place . .	—	—	—	—	(2.4)	—	(2.4)	—	(2.4)
Purchases of reserves in place	—	—	—	—	236.8	—	236.8	—	236.8
Production for the year	<u>(24.9)</u>	<u>(58.4)</u>	<u>(3.5)</u>	<u>(117.0)</u>	<u>(3.9)</u>	<u>(9.3)</u>	<u>(32.3)</u>	<u>(184.7)</u>	<u>(63.1)</u>
At December 31, 1997	<u>105.9</u>	<u>435.3</u>	<u>29.1</u>	<u>1,321.9</u>	<u>389.1</u>	<u>189.0</u>	<u>524.1</u>	<u>1,946.2</u>	<u>848.5</u>
Proved developed reserves									
At December 31, 1995	55.9	127.4	25.6	1,220.6	13.5	54.2	95.0	1,402.2	328.7
At December 31, 1996	68.2	310.1	26.9	1,087.2	23.4	36.4	118.5	1,433.7	357.5
At December 31, 1997	86.4	388.5	27.4	1,052.9	87.7	27.1	201.5	1,468.5	446.3

(1) The data in the above table is compiled on the basis of the Commission’s definitions of proved developed reserves and proved undeveloped reserves and not the definition of proven and probable reserves used for purposes of LASMO’s financial statements. See “Certain Oil and Gas Terms” and “Financial Statements — Supplementary Disclosures Relating to Crude Oil and Natural Gas Producing Activities (Unaudited)”.

There are numerous uncertainties inherent in estimating quantities of reserves and in projecting future rates of production and timing of development expenditures, including many factors beyond the control of the producer. The reserve data set forth in this Annual Report only represents estimates. Reserve engineering is a subjective process of estimating underground accumulations of oil and gas that cannot be measured in an

exact way, and the accuracy of any reserve estimate is a function of the quality of available data and of engineering and geological interpretation and judgment. As a result, estimates of different engineers often vary. In addition, results of drilling, testing and production subsequent to the date of an estimate may justify revision of such estimates so that reserve estimates at a specific time are often different from the quantities of oil and gas that are ultimately recovered. In addition, the estimates of future net revenues from proved reserves of the Group and the present value thereof are based upon assumptions about future production levels, prices and costs that may not prove to be correct over time. Predictions about future prices, costs and production levels are subject to great uncertainty. The meaningfulness of such estimates is highly dependent upon the accuracy of the assumptions upon which they are based. In addition, reserves included in respect of interests subject to PSCs are stated net of government share and are subject to revision as prices fluctuate, due to cost recovery features under the terms of the PSCs.

Information regarding reserves in Venezuela (included under “International” in the above table) relates to LASMO’s interest in an operating agreement for the Dacion Area between LASMO and a subsidiary of Petroleos de Venezuela SA, the government-owned petroleum company (“PDVSA”). LASMO has no ownership interest in the oil reserves but instead will receive a service fee based upon production and calculated in accordance with the terms of the operating agreement. The agreement allows for full recovery of capital and operating costs out of production. Remaining profit will be shared with the government on a rate of return basis set forth in the agreement. A company sponsored by PDVSA and formed for the purpose of investing in the Venezuelan energy sector has an option to participate at the level of a 10% interest in the operating agreement. The reserves have been presented on a gross basis after taking account of such contractual back-in rights.

In general, LASMO’s volume of production from oil and gas properties declines with the passage of time. In addition, LASMO’s and its co-venturers’ participation share of gas volumes supplied to support Indonesian LNG sales contract extensions or additions will be significantly less than their participation share under the original long-term sales contracts. See “— Oil and Gas Interests — Indonesia”. Except to the extent LASMO acquires additional properties containing proved reserves or conducts successful exploration or development activities, or both, LASMO’s proved reserves, and the revenues generated from production thereof (assuming no price increases), will decline as reserves are produced. Drilling activities are expensive and subject to numerous risks, including the risk that no commercially viable oil or gas production will be obtained. Increases or decreases in prices of oil and gas and in cost levels, along with the timing of development projects, will also affect revenues generated by LASMO and the present value of estimated future net cash flows from its properties. Revenues generated from future activities of LASMO are highly dependent upon the levels of success in acquiring, finding or developing additional reserves.

Exploration and Production

As is commonplace in the oil and gas exploration and production industry, LASMO generally participates in exploration and production activities in conjunction with several co-venturers. LASMO’s co-venturers include other oil and gas companies, state oil companies and other government entities. Contractual arrangements between co-venturers are generally governed by an operating agreement, which provides for costs, entitlements to production and liabilities to be shared according to percentage interests in the venture. One co-venturer will generally be appointed operator to conduct operations under the overall supervision and control of an operating committee consisting of representatives of each co-venturer.

While operating agreements generally provide for liabilities to be borne by the co-venturers according to their respective percentage interests, licenses from the relevant government authority generally provide that the co-venturers are jointly and severally liable for their obligations to that government authority under the applicable license.

Exploration

A total of 52 exploration wells and 22 appraisal wells in which LASMO participated were completed in the three years ended December 31, 1997. Of the completed wells, 16 exploration wells led to the discovery of

either new crude oil or natural gas accumulations and 18 appraisal wells led to the upgrading of existing discoveries (although development of certain of these discoveries may not be economically viable at current crude oil and natural gas prices). See “— Operational Statistics”.

In 1997, LASMO participated in 28 exploration wells and 8 appraisal wells and a further 3 exploration wells and six appraisal wells were still being drilled at the end of the period. Of the completed wells, 11 exploration wells led to the discovery of either new crude oil or natural gas deposits and 7 appraisal wells led to the upgrading of existing discoveries (although development of certain of these discoveries may not be economically viable at current crude oil and natural gas prices).

LASMO’s acreage portfolio decreased from 78,900 net square kilometers (19.49 million acres) at the end of 1992 to 71,014 net square kilometers (17.54 million acres) at the end of 1997 due to asset sales, farmouts and relinquishment. The table below summarizes the estimated net acreage held by LASMO at December 31, 1997.

<u>Country(1)</u>	<u>Net sq. km(2)</u>
The United Kingdom and The Netherlands	3,738
Indonesia	6,024
Algeria	4,674
Colombia	1,297
Egypt	4,320
Falkland Islands	2,012
Italy	2,277
Libya	6,458
Pakistan	36,118
Tunisia	3,668
Venezuela	<u>428</u>
Total acreage	<u><u>71,014</u></u>

(1) LASMO sold its interests in Gabon with effect from January 1, 1997.

(2) Estimated.

Production

In 1997, LASMO’s average daily production of crude oil and natural gas was 173 Mboepd, representing a 1% decrease over the average daily production for 1996. The decrease was primarily due to the expected reduction in deliveries under the Package I sales contract in Indonesia in which LASMO had a high participating interest. The reduction in Indonesian production has been largely offset by a full-year contribution from the Liverpool Bay and Andrew fields and the start-up of the MacCulloch field in the UK. Production increased significantly during the last quarter of the year, following first production from the MacCulloch field and the year end target of 200 Mboepd was reached. Production of crude oil accounted for 51% of LASMO’s average daily production and natural gas for 49%. In 1996, LASMO’s average daily production of crude oil and natural gas was 175 Mboepd, representing a 7% increase over the average daily production for 1995 of 164 Mboepd.

Appraisal and development activity is expected to have a positive impact on LASMO’s production, enabling the Company to target production of over 250 Mboepd by 2001. This assumes that the performance of currently producing assets and the development timing and performance of fields under development will be as currently estimated by the relevant operator, that the oil price does not vary significantly from LASMO’s current estimates, that there will be no further acquisitions or disposals of producing assets and that there will be no significant unforeseen interruptions to production. Estimates of future production are inherently uncertain and caution must be exercised in relying on such estimates which represent the Company’s best estimate of a range of possible estimates. See “— Additional Factors Which May Affect Business — Political and Economic Considerations” for other factors that may affect this expectation.

In 1997, the Sanga Sanga PSC in Indonesia accounted for 36% of LASMO's total production, with, in the North Sea, the Piper, Saltire and Claymore fields providing 17% of the total and the Liverpool Bay fields providing a further 10% of the total. In 1996, the Sanga Sanga PSC accounted for 43% of total production with the Piper, Saltire and Claymore fields providing 19% of the total and the Liverpool Bay fields, in their first year of production, providing a further 4% of the total. In 1995, the Sanga Sanga PSC accounted for 43% of total production with the Piper, Saltire and Claymore fields providing a further 23% of the total.

For LASMO's average daily production of crude oil and natural gas by geographic area for each of the three years ended December 31, 1995, 1996 and 1997, see "Operational Statistics".

Oil and Gas Interests

LASMO's producing assets are concentrated primarily in the UK and Indonesia regions, which are presently regarded by the Company as its two principal areas of activity. At the end of 1997, LASMO was the operator of exploration and development projects in eight countries and has active interests in a further five countries. During 1997, production was derived from seven of these countries, principally the United Kingdom, The Netherlands, Indonesia, Colombia and Pakistan.

The following is a description of LASMO's principal oil and gas interests.

UK

The UK region had 21% of the Group's net proved reserves at December 31, 1997 and 55% of production for 1997 and had interests in 21 fields in production. Production from the UK averaged 95 Mboepd in 1997, an increase of 11% over 1996 levels, reflecting a full year of production from the Andrew and Liverpool Bay fields, together with start-up of the MacCulloch field. During 1997, project sanction was given for the Galley, Larch and Ross fields. The following is a description of LASMO's principal fields in production and certain other key interests in the UK region.

Claymore and Scapa (LASMO interest 20%). LASMO gained its interests in the Claymore and Scapa oil fields, both located in block 14/19, through its acquisition of Thomson North Sea Holdings Ltd ("TNS") in March 1989. Production, which had been shut down following the Piper Alpha incident in 1988 (described below under "Piper area"), recommenced the following year. In addition to its own production, the Claymore platform receives oil from the Scapa subsea development, Texaco's Tartan complex of fields and Amerada Hess's Ivanhoe/Rob Roy fields. Production from these fields is transported by a pipeline to the Flotta oil handling terminal in Orkney, in which LASMO holds a 20% interest. Considerable emphasis is being placed on third party utilization of the production facilities and pipeline to the Flotta terminal. LASMO continues to work closely with the operator, Elf, to improve operating efficiency. The benefits of changes to working practices and asset organization should result in the reduction of future operating costs.

Average daily production net to LASMO from the Claymore field was 8.6 Mbopd and from the Scapa field was 3.8 Mbopd for 1997. LASMO's net proved reserves at December 31, 1997 for the Claymore and Scapa fields are estimated at 24 MMB.

The Claymore field pays government royalty and is subject to Petroleum Revenue Tax ("PRT"). Scapa is not subject to a government royalty interest and it is not anticipated that PRT will be paid on production from the field. See "— Additional Factors Which May Affect Business — Production Revenue Taxes".

Piper area (LASMO interest 20%). LASMO acquired its interest in the Piper area through its acquisition of TNS in March 1989. In July 1988, the Piper Alpha platform had been destroyed in an explosion. This led to the suspension of production not only from the Piper field but also from the Claymore and Scapa fields whose oil had been transported via a common pipeline. All North Sea fields underwent safety reviews and upgrades as a result of the incident. The related redevelopment costs, which were more than double the originally projected costs, were immediately allowable for PRT purposes, resulting in semi-annual refunds with interest on previously paid PRT, thereby significantly reducing development costs on an after-tax basis.

Redevelopment of the Piper oil field, located in block 15/17, has incorporated facilities for the Chanter, Saltire and Iona fields. MacCulloch liquids are also transported via Piper. Production from Piper recommenced in February 1993 and averaged 10.6 Mboepd net to LASMO during 1997. LASMO's net proved reserves at December 31, 1997 for the Piper field are estimated at 14 MMboe.

The Piper field pays government royalty and PRT.

The Saltire field is connected to the new Piper Bravo platform and first production commenced in May 1993. It uses a fixed platform which provides preliminary processing, with further processing undertaken on the Piper main platform. Production averaged 9.7 Mboepd net to LASMO in 1997. LASMO's net proved reserves at December 31, 1997 for the Saltire field are estimated at 2 MMboe.

Markham (LASMO interest 35.88%). The LASMO-operated Markham gas field commenced production in November 1992. This field was discovered in 1984 and is located partially in the UKCS and partially in The Netherlands North Sea. The Netherlands blocks J3b and J6 contain approximately 65% of the Markham field's gross proved reserves and UK blocks 49/5a and 49/10b are attributed with approximately 35% of the gross proved reserves. A treaty between the UK and The Netherlands governments, signed in May 1992 and ratified in March 1993, paved the way for the first export of gas from the UKCS to continental Europe. The gas produced at Markham is sold into The Netherlands and Germany. An offshore compression facility which was installed in the second half of 1996 and commissioned at the end of the first quarter of 1997, now maximizes field recoveries and provides capacity for third party gas throughput. Third party gas transportation for production from the J3-Charlie and K4a-d blocks, was completed in 1997. Production from the field averaged 10.5 Mboepd net to LASMO in 1997. LASMO's net proved reserves at December 31, 1997 for the Markham field are estimated at 16 MMboe.

Caister (LASMO interest 21%). The development of the Caister field has been undertaken as part of an integrated development with the nearby Murdoch field, owned by third parties. This integrated approach, in which common facilities between the two fields are shared, has reduced development costs.

In April 1992, development of the Caister and Murdoch gas fields commenced with a new shared gas gathering system (the "Caister Murdoch System" — LASMO interest 10.5%). Production from the Caister field commenced in October 1993. The development consists of two not-normally-manned production platforms controlled from the Theddlethorpe terminal and linked to a complex of pipelines that gathers the produced gas and transports it to the terminal for processing and delivery to customers. The pipeline system has a potential capacity of 750 MMcfd, enabling it to handle production from future developments in the area. An agreement has been signed for the transportation of gas from the Schooner field through the Caister Murdoch System. Average daily production net to LASMO was 3.5 Mboepd in 1997. LASMO's net proved reserves for the Caister field at December 31, 1997 are estimated at 3 MMboe.

The offshore compression project was completed on schedule in 1996 and provides capacity which could lead to the development of a number of neighboring accumulations. One of these accumulations, Boulton, was sanctioned for development in 1996 and first gas, originally anticipated in 1998, was produced at the end of December 1997. LASMO has a 44.5% interest in this development and net proved reserves at December 31, 1997 were estimated at 9 MMboe.

Liverpool Bay (LASMO interest 25%). In the Irish Sea, LASMO has a 25% interest in block 110/13 which contains the Hamilton and Hamilton North gas fields and the Douglas oil field and a 25% interest in the Lennox oil field in block 110/15, approximately 12 miles east of the Hamilton and Douglas fields. First production of oil from the Liverpool Bay development was achieved in January 1996, following shortly after the delivery of first commissioning gas. Development drilling progressed smoothly during 1996 and well productivities were better than expected. Commissioning problems offshore and at PowerGen's Connah's Quay power station restricted production during 1996, and in June 1996 leaks were detected in the pipeline used to transport gas for reinjection into the Lennox field from the main Douglas processing facility. While there was no environmental impact from the leak, it restricted oil production from the Lennox field during 1996 and 1997. A replacement line was laid and injection recommenced in the second quarter of 1997.

LASMO is negotiating to reclaim these costs from insurers and the pipeline manufacturer. Production averaged 18.0 Mboepd net to LASMO in 1997.

LASMO's net proved reserves at December 31, 1997 for these four fields are estimated at 55 MMboe.

Block 16/12a (LASMO interest 46.79%). Block 16/12a, which LASMO operates, lies between the Brae and Miller fields to the north and the T-block fields to the south. Twenty-two wells have been drilled in the block, resulting in four discoveries (Elm, Birch, Larch and Pine). There is extensive infrastructure in place in the area. Government consent for the subsea development of the Birch oil field was received in March 1994. Production from the field, which commenced in September 1995, is processed through the Brae platform facilities and transported to shore through the Forties system. Average daily production net to LASMO from the Birch field was 10.9 Mboepd during 1997.

The Larch field received project sanction in 1997. A longreach horizontal well is expected to be completed for first oil in the second quarter of 1998. LASMO's net proved reserves for block 16/12a at December 31, 1997 are estimated at 9 MMboe.

Andrew (LASMO interest 16.21%). The Andrew oil and gas field, discovered in 1974, straddles blocks 16/27a (South) and 16/28. LASMO has a 43.52% interest in block 16/27a (South) and is operator of the interest, although BP operates the unitized development. Plans for development of the field through a manned platform, with transportation through the Forties system, received partner and government approval in August 1994. Production commenced six months ahead of schedule at the end of June 1996 and under budget. Average daily production net to LASMO from the Andrew field was 10.0 Mboepd during 1997. LASMO's net proved reserves for the Andrew field at December 31, 1997 are estimated at 20 MMboe.

MacCulloch (LASMO interest 40%). Annex B approval was received in November 1995 for the Conoco operated MacCulloch field floating production system development. Development of the MacCulloch oil field in the Central North Sea continued throughout 1996. First oil was achieved in August 1997, later than planned due to delays in delivery of the floating production vessel and commissioning difficulties, and averaged 5.0 Mbopd. LASMO's net proved reserves for the MacCulloch field at December 31, 1997 are estimated at 13 MMboe.

Cavendish (LASMO interest 25%). Development planning is currently underway on the Cavendish gas field (block 43/19a). Project sanction originally targeted for late-1997 has been delayed while export routes are re-evaluated.

Mariner (LASMO interest 20%). Successful appraisal drilling was undertaken during 1997, together with an extended well test. Well performance during the test met expectations and the project is now entering the final phase of appraisal drilling.

Galley (LASMO interest 15.17%). Project sanction for the Galley field was granted in 1997. First oil from the Galley field was produced in late March 1998 and a gas compression system is due to be commissioned at the beginning of May 1998.

Other. Following the evaluation of LASMO's West of Shetland acreage, up to four exploration wells are planned in 1998, targeting sizable prospects. LASMO has acquired seismic over its UK 17th Licensing Round acreage awarded in 1997, and is positioned to apply for acreage in the 18th UK Licensing Round and the First Faroe Islands Licensing Round.

A gas discovery was made in the Southern North Sea block 49/3, which is believed to be an extension of the Ketch field. The implications of this are currently under review.

Project sanction for the Ross field was granted in 1997. First production is expected by the end of 1998.

LASMO continued to manage its existing exploration portfolio in 1997 and successfully farmed out part of its working interest in a number of exploration and appraisal wells. LASMO also traded its working interest in block 15/27 for an interest in block 15/18a.

The UK Government announced on March 17, 1998 certain proposals which may result in the abolition of government royalty together with amendments to production revenue taxes. See “— Additional Factors Which May Affect Business — Production Revenue Taxes”.

Indonesia

The Indonesia region, with 29% of the Group’s net proved reserves at December 31, 1997 and approximately 36% of production in 1997, occupies a key place in the Group’s portfolio. The Sanga Sanga PSC, operated by LASMO’s affiliate, Virginia Indonesia Company (“VICO”), is the largest single contributor to Group reserves and production. LASMO holds interests in and is operator of two further PSCs, Cumi Cumi and Runtu.

Sanga Sanga (LASMO interest 37.81%). LASMO’s net proved reserves for the Sanga Sanga PSC at December 31, 1997 are estimated at 249 MMboe, 100% of LASMO’s net proved reserves in Indonesia. Average daily production from the Sanga Sanga PSC net to LASMO was 63.0 Mboepd in 1997, comprising oil production of 9.6 Mbopd and 321 MMcfd of net LASMO entitlement gas production.

LASMO has a significant position in the Pacific Basin LNG market through its 37.81% interest in a joint venture in Indonesia (the “IJV”) which produces natural gas, oil and condensate pursuant to a PSC with Perusahaan Pertambangan Minyak Dan Gas Bumi Negara (“Pertamina”), the Indonesian state oil company. LASMO holds its interests in the IJV directly through a wholly owned subsidiary and indirectly through its 50% interest in Unimar Company (“Unimar”), a partnership with Union Texas Petroleum Holdings, Inc. Unimar owns ENSTAR Corporation and its subsidiaries, including VICO.

The IJV’s PSC grants the IJV participants an exclusive right to explore for and develop oil and gas resources in an onshore area in East Kalimantan (the “Contract Area”). The Contract Area includes two significant fields Badak and Nilam which are both partly unitized outside the contract area, and other smaller fields including Semberah, Mutiara, Beras and Pamagan. As with any PSC, the IJV has no ownership interest in the oil and gas reserves but has the right to share revenues from production. Under the PSC, the IJV participants are entitled to recover most operating costs, as well as capital depreciation, and to receive, subject to applicable Indonesian taxes, 79.55% of the remaining gas revenues until August 1998, and, for the remaining term of the contract, 57.69% or, in some cases, 48.08% of such revenues.

After cost oil, the IJV retains approximately 34% (reducing to approximately 29% after August 1998) of the proceeds from oil and condensate production, subject to applicable Indonesian taxes.

Substantially all of the natural gas produced by the IJV is supplied pursuant to long-term supply contracts with Pertamina to a liquefaction plant owned by Pertamina at Bontang Bay. The Bontang plant is operated on a cost-reimbursement basis by a corporation owned in part by the IJV. Following completion of the seventh processing train in November 1997, the plant is expected to process approximately 900 bcf of gas in 1998 or approximately 320 cargoes (1997 275; 1996 267). An eighth LNG processing train is under construction, with first production scheduled for late 1999. The Bontang plant is then expected to produce at the upgraded capacity of 1,100 bcf/year (390 - 410 cargoes per year) until after the year 2005.

Extensions to the Bontang plant and facilities are funded without recourse to the participants in the IJV.

The supply agreements between the IJV and Pertamina support long-term LNG sales contracts of Pertamina and obligate the IJV to provide certain quantities of natural gas for fulfillment of Pertamina’s obligations thereunder. Quantities in excess of the contracted amounts are sometimes sold as spot cargoes to the same buyers as under the long-term LNG contracts. The IJV’s obligations to supply natural gas in support of the long-term LNG sales contracts and its rights to receive revenues attributable to the sale of LNG under such contracts vary.

The amount of revenue that LASMO receives as a result of the production of natural gas in support of the long-term LNG sales contracts is dependent upon the number of cargoes shipped each year, LASMO’s ultimate participation in each cargo and the price paid for the LNG purchased. LASMO’s net share of standard cargoes is expected to stabilize at about 43 cargoes until 2002 following the recent decline (1997 44;

1996 52) due to the changing participation in sales contracts and the termination of Package I sales in which the IJV has a 97.9% interest.

LNG currently produced by the Bontang plant is principally sold under long-term LNG sales contracts to Japanese, Korean and Taiwanese buyers. The long-term LNG sales contracts contain take-or-pay provisions that generally require that the purchasers either take the contracted quantities or pay for such quantities even if not taken. Pertamina has from time to time entered into short-term LNG sales contracts with various Japanese and Korean buyers.

In 1997, approximately 80% of the Joint Venture PSC's share of LNG was sold by Pertamina to Japanese customers. The 1998 program expects about 74% of LNG sales to be sold to Japanese customers, with Korean and Taiwanese customers purchasing the remaining 16% and 10% respectively. The current economic uncertainties in Southeast Asia could impair the ability of certain customers to take their contracted commitments. However, only the Japanese contracts allow customers to lift a minimum of 95% fixed contractual volumes under take-or-pay provisions. All underlifted volumes must be rescheduled within five years. All other contracts require full lifting of fixed contractual quantities.

All Sanga Sanga revenue is received in US dollars and 99.5% is received directly from customers outside Indonesia, not via Pertamina. LNG revenue is paid directly to the Bank of America Trustee and liquids revenue is received directly from customers. Also, almost half of current costs are Rupiah based thereby resulting in cost savings with the devaluation of the Indonesian currency. LASMO's cashflow from Indonesia is expected to decline steadily in coming years from 27% of Group cashflow currently to about 16% by 2001.

LNG Contracts are in place to supply a total of 15,182 TBtu of which the IJV's share at December 31, 1997 was estimated at 3,750 TBtu (approximately 4.3 Tcf gas).

The price of LNG sold from the Bontang plant is primarily based on the market value of oil. Prices are quoted on the Btu content of the LNG. At December 31, 1997, the average price per MMBtu under all contracts supplied from the Bontang plant was \$2.75, excluding transportation on CIF contracts. Prices under the contracts are subject to monthly adjustments. At December 31, 1997, the average price for the basket of crude oils which is used to determine the price of LNG was \$19.47 per barrel. The Company is unable to predict the amount or timing of future changes in the price of this basket of crude oils.

The Company believes that there are adequate reserves in the Contract Area to supply natural gas under the IJV's contractual commitments as of December 31, 1997.

The following table sets forth information regarding the Bontang LNG sales contracts grouped together by the IJV's participating percentage in the sales contracts (each such group being referred to as a "Package") as at December 31, 1997:

	<u>Contract Term</u>	<u>Remaining LNG Sales Volumes (TBtu)</u>	<u>IJV Participation Percentage (%)</u>	<u>IJV's Share of Remaining LNG Sales Volumes(1) (TBtu)</u>
<i>Package I</i>				
1973	1977-1999	3	97.9	3
<i>Package II</i>				
1981	1983-2003	898	66.4	596
<i>Package IIIA</i>				
Korean Carryover	1986-2006	130	50.0	65
<i>Package IIIB</i>				
Taiwan LNG	1990-2009	1,058	29.6	313
Additional 1981	1990-2003	95	29.6	28
<i>Package IV</i>				
Train F LNG	1994-2014	1,914	27.2	521
Korea II	1994-2014	808	27.2	220
1973 Extension	1997-1999	361	27.2	98
MCGC	1996-2015	349	27.2	95
Others	1990-1999	11	27.2	3
<i>Package V</i>				
1973 Extension	2000-2009	4,356	21.6	941
Korea Medium Term	1995-1999	283	21.6	61
Taiwan Medium Term	1998-1999	46	21.6	10
Badak V	1998-1999	106	21.6	23
Badak VI	1998-1999	43	21.6	9
Aquarius/Aries Extension	1997-1999	32	21.6	7
<i>Package VI</i>				
1981 Extension	2003-2008	942	16.5	155
Badak V	2000-2017	956	16.5	158
Badak VI	2000-2017	1,686	16.5	278
<i>Package VII(2)</i>				
1973 extension	2010	436	14.8	65
1981 extension	2009-2011	565	14.8	84
Additional Sales	2000-2017	<u>104</u>	14.8	<u>15</u>
		15,182		3,748

- (1) The IJV's share of remaining LNG sales volumes represents volumes available to the IJV under the sales contracts for recovering exploration, development and production costs and profit sharing between the IJV and Pertamina and for servicing its share of plant operating and debt service costs.
- (2) Package VII participation percentage is assumed to be 14.8%. LASMO cannot predict the percentage participation that the IJV will have in future contracts.
- (3) Note that the above sales volumes are for gas sold as LNG, 854 TBtus (IJV share 150 TBtus) are expected to be sold as LPG and 3,957 TBtus (IJV share 738 TBtus) as domestic gas to the Kaltim Industrial Estate in East Kalimantan.

LNG to be delivered under sales contracts is supplied from Bontang and from a separate facility at Arun in Sumatra (the "Arun Plant"). The IJV does not supply gas to the Arun Plant or have any interest in revenue from the sale of its production. The allocation of contract quantities between the two plants is determined by Pertamina.

Under the majority of contracts, LNG is sold on a delivered basis (i.e., title and risk of loss do not pass until the LNG is unloaded at the customers' facilities). Under the 1981 Train F and Korea II contracts and some KGC contracts, LNG is delivered free on board ("f.o.b.", i.e., title and risk of loss pass upon loading at Pertamina's port facility). Payment for all contracts is made by the purchasers in US dollars directly to a bank in the United States that acts as trustee and paying agent with respect to sales proceeds. Bontang plant processing fees, debt service with respect to plant financing, transportation (as required) and other costs are deducted from sales proceeds, and the balance is then distributed to Pertamina, the members of the IJV and other production sharing contractors.

A 935 sq km. 3-D seismic program covering Nilam, Badak and Semberah fields commenced in 1997 and continues in 1998. The surveys are intended to help identify any additional reserve potential within and adjacent to the fields.

LASMO had been pursuing a number of new business initiatives that are based both on adding value to the Sanga Sanga PSC and broader gas related opportunities in Indonesia. The economic climate in Indonesia has rendered many of these initiatives unattractive and LASMO has withdrawn from the company that was pursuing new business.

Other Areas. In early 1998, LASMO completed a three well wildcat drilling program in the northern portion of the Runtu PSC. There were good hydrocarbon shows in all the wells, but poor reservoir quality meant that they were not commercial. The remaining potential of the PSC will be evaluated during 1998.

LASMO continues to seek opportunities to add to its already substantial position in Indonesia. The Company is negotiating to acquire a new license in Irian Jaya.

International

Algeria

LASMO and its partners had found 12 fields in Algeria by the end of 1997 in blocks 401a, 402a, 404, 208, 211 and 245. These include RBK, QBN, HBNSE and BSFN/ROD that were discovered during the year, but exclude discoveries from two wells, EMN-1 and BSF-1, that started drilling in 1997 and which were successfully completed in 1998. LASMO and its partners made the first discovery, EMK, in 1993 and have continued with a successful exploration and appraisal program since that time. To the end of 1997, 35 exploration and appraisal wells had been completed of which 25 were successful, equating to a 71% success rate. During 1997, 10 out of the 15 wells were successful.

Further Algerian exploration and appraisal will be undertaken during 1998, together with an increasing level of development drilling as milestones are reached in developing major fields.

Blocks 404, 208, 211 and 245 (LASMO interest 25%)

Following the award of a Provisional Exploitation License ("PEA") in June 1996, there has been continuous development activity on the HBNS oil field located in Block 404. Production facilities with a gross capacity of 60,000 bopd are being constructed by Brown and Root Condor under an engineering and procurement contract signed in September 1996. First oil is expected by the middle of 1998.

Transportation for the first stage and subsequent stages of production is expected to be via a new 30 inch pipeline to Hassi Massaoud, currently under construction by Sonatrach, which is now forecast to be completed at the time of first oil production. Links to other pipelines are being completed as short term cover for any pipeline delays.

There was no further drilling activity on the BKE field in block 404 during 1997. However, progress was made on discussions with the adjacent operators and Sonatrach, the Algerian National Oil Company, to define the extent to which the oil field extends outside of block 404. The field has been renamed Qoubba and a development program is expected in 1998.

Also on block 404, three new discoveries were made in 1997 at RBK, QBN and HBNSE. The latter well was the most significant, producing 17,092 bopd and 37.5 MMcfd under a high rate test. The well was

successfully appraised with HBNSE-2. A fourth exploration well, HBNC, was successfully drilled on an accumulation which was determined to be part of the HBNS field. The EMN-1 well on block 208, which was completed in 1998, tested at a rate of 21,394 bopd and 15.3 MMcfd.

Blocks 401a and 402a (LASMO interest will be 13.75%)

Four successful exploration and appraisal wells were completed during 1997. The wells on the BSFN and ROD prospects indicate this to be a single accumulation. The most successful test result was on BSFN-2 which flowed at 6,108 bopd and 7.32 MMcfd. A further appraisal well, ROD-3, which was started in 1997 and completed in 1998, was not successful. Appraisal will continue in 1998. On the BSF prospect an exploration well was started in 1997 and successfully completed in 1998.

Net proved reserves booked by LASMO in respect of its Algerian fields at December 31, 1997 totaled 96 MMb.

Colombia

Following re-evaluation of businesses in non-core areas, LASMO announced in February 1998 its intention to withdraw from Colombia which contributed 11.3 Mboepd of production in 1997.

Egypt

Acquisition of 3-D seismic over the North Red Sea Block 1 (*LASMO interest 36%*) in 1998 will guide further activity on the block.

Falkland Islands

During 1997, seismic was acquired over the LASMO operated offshore Falkland Islands acreage (*LASMO interest 62.5%*) and the first well on Tranche C is due to be drilled in the middle of 1998. This frontier acreage provides early entry to a high risk but potentially high reward geological basin. LASMO is currently negotiating a farmin to two offshore Argentine blocks adjacent to the Falklands/Argentine Special Area of Co-operation.

Gabon

Following a review of businesses in non-core areas, and re-evaluation of the remaining potential of the Obando, Octopus and Pelican fields, LASMO disposed of its 50% interest in those fields with effect from January 1997, thereby withdrawing from Gabon. LASMO received a share of net production to June 30, 1997 which averaged 1.2 Mbopd, calculated on an annual basis.

Italy

Activity in Italy continued in the two primary areas of the Southern and Central Apennines. At the Tempa Rossa field in the Southern Apennines, the success of the Tempa D'Emma-1 appraisal well (*LASMO interest 20.46%*) extended the known thickness of the oil column to 1,300 meters.

Additional acreage has been acquired adjacent to the Tempa Rossa field to secure any upside that may exist from an extension of the field into these blocks. A contract for front end engineering design of processing facilities was completed in 1997, based upon initial production of 50 Mbopd. Commercial discussions are ongoing regarding the preferred export route for Tempa Rossa oil.

Evaluation of acreage in the Central Apennines continued during 1997 and the first exploration well in the LASMO operated Roccasicura block is expected to spud in the second half of 1998.

In February 1998, LASMO announced its intention to review its business in Italy.

Libya

In 1997, the Libyan government's ratification of the farmout by LASMO of a 33.33% interest in NC173/4 to Agip North Africa BV was received. LASMO's working interest in its operated blocks NC173 and NC174 is now 33.33% with a Korean Consortium led by Pedco holding the remaining 33.33% share. The government also approved a further one year extension to the exploration term of the Exploration and Production Sharing Agreement until December 1998.

In October 1997, LASMO announced the F1-NC174 discovery, on the Elephant prospect in the NC174 block located in the Murzuk Basin of Southwest Libya. The F2-NC174 appraisal well tested at a rate of 9 Mbopd and confirmed that the field could hold significant recoverable reserves.

The field will be appraised further during 1998 and plateau production is scheduled for 2002. Export is expected to utilize existing infrastructure, located approximately 70 kilometers to the north. The option of early production prior to 2002 is also being investigated.

Morocco

During 1997, LASMO was awarded a Reconnaissance License, which may lead to the application for an Exploration License late in 1998. On April 17, 1998, agreement was reached with Office National de Recherches et d'Exploitations Pétroliers, the government vehicle for petroleum exploration and development, that, subject to contract, LASMO will be awarded a new offshore Reconnaissance License adjacent to the current onshore license. LASMO is currently reviewing the logistics and timing of a seismic survey in the new block.

Pakistan

The Kadanwari gas field (*LASMO interest 18.42%*) produced 13 MMcfd net to LASMO during 1997. One well was recompleted in early 1997 and a development well drilled at the end of 1997. A further development well is planned for early 1998.

In April 1997, LASMO as operator announced the success of the Bhit-2 exploration well on the Kirthar concession (*LASMO interest 47.5%*). The well encountered 150 meters of net gas pay and test results indicate it to be capable of flowing at rates in excess of 60 MMcfd when completed for production.

Net proved reserves booked by LASMO at December 31, 1997 totaled 27 MMboe equivalent to a gross 0.4 Tcf. Additional reserves are expected to be booked as appraisal drilling in 1998 confirms the full potential of this field. Bhit-2 was drilled solely on the basis of a large surface anticline structure, of which there are repeated examples on LASMO's adjacent acreage. LASMO believes the probability of finding additional gas reserves in these lookalike structures has been increased considerably by the success of the Bhit-2 well.

In order to capitalize upon its success with Bhit-2, LASMO secured six additional exploration concessions in southern Pakistan during 1997 and at the year end it was the largest independent acreage holder in the country. A feature of the Group's exploration portfolio in Pakistan is that all interests are operated by LASMO, with sizable equity. Working interests (after Government back-in) range from 40% in the Kirthar concession to a more typical 85%.

A comprehensive seismic program is being pursued over LASMO's Kirthar Foldbelt acreage to optimize drilling locations. The Kirthar concession has already been evaluated and early in March 1998 a five well drilling campaign commenced to appraise the Bhit structure and test other prospects in the Kirthar and Kirthar West licenses. The preliminary development plan for the Bhit field targets first production in 2000.

Further south, the Bela North and South concessions were awarded to LASMO in 1997, along with the offshore Indus A and B blocks. Seismic programs run during the year have identified several large prospects in Bela South and led to the relinquishment of Bela North. The seismic evaluation of the Indus A and B blocks will continue in 1998.

Tunisia

Evaluation of LASMO's Tunisian acreage progressed during 1997, with the acquisition of new seismic. The first exploration well on the Jenein South block (*LASMO interest 40%*) will be drilled in the first half of 1998, testing the easterly extension of the prolific Berkine Basin, the source of LASMO's Algerian discoveries.

Venezuela

In early 1997, LASMO, in a technology alliance with Schlumberger, commenced evaluation of the 20 blocks available for bidding in the Venezuelan 3rd Operating Agreement round. The Dacion Area, lying within the prolific Oficina trend of the eastern Venezuela basin, was identified as LASMO's primary target for the June bidding round. A 90% working interest in the block for a period of 20 years was secured in a competitive bidding process at a cost of \$453 million. LASMO assumed operatorship of the Dacion Area on March 31, 1998.

The Dacion Area contains very significant reserves potential. After more than 50 years of production, it is estimated that only a small amount of the oil from the Dacion Area has been produced. Current gross production is approximately 11.6 Mbopd. With additional investment and the application of current technology, LASMO plans to increase gross production from existing fields to 90 Mbopd by the year 2001. Net proved reserves booked by LASMO at December 31, 1997 totaled 224 MMboe, with substantial further bookings expected as development drilling and production performance confirm the full potential of the fields. LASMO estimates that an additional investment of some US\$750 million will be required during the first phase of the redevelopment project in the period through 2001.

In addition to the substantial reserves attributable to the redevelopment of existing fields in the Dacion Area, the remainder of the block holds significant exploration potential. LASMO has exploration rights to the Dacion Area for seven years and plans an extensive exploration program, aimed at realizing the full potential of the block. 70% of the block has not been subject to any previous exploration activity.

Major activities for 1998 include the upgrading of existing surface facilities, commencement of the extensive well work-over program and the acquisition of 3-D seismic.

LASMO's success in securing operatorship of the Dacion Area is viewed as a first step in one of the major hydrocarbon provinces of the world. Opportunities to expand upon and diversify this position are being actively evaluated.

Sales

Crude Oil

During 1997, LASMO sold 29.96 MMb of crude oil and LPG from its production. Approximately 54.78% was sold on a cargo by cargo basis into the spot market. The balance was sold under pre-existing contracts with terms of up to one year at prices related to spot market prices for "marker grades" or official selling prices. Of crude oil and LPG sold by LASMO, 89.58% was sold f.o.b. customers' vessels or into pipeline systems. The remaining 10.42% was sold and delivered to destinations in Europe and North America.

Natural Gas

Natural gas attributable to LASMO and not used in production operations or flared is sold on long-term contracts, most of which oblige the purchaser to take or pay for a substantial proportion of the contracted gas. These generally cover all the natural gas exported from the particular field. The natural gas price is usually linked to various fuel and price indices. UK North Sea natural gas is sold primarily to European utilities. Most exports of LNG from Indonesia are similarly sold on long-term contracts to Japanese, Korean and Taiwanese utilities. The LNG prices are directly linked to a basket of Indonesia crude oil prices. See "— Oil and Gas Interests — Indonesia".

Tariff Income

Tariff income, income arising from the provision of transportation and processing facilities and other services, is generated mainly in the North Sea. Tariff income received during 1997 was £17 million, principally from usage of the Flotta terminal.

Regulation

Environmental Protection

The Group's operations are subject to environmental laws and regulation in each of the areas in which it operates. These laws and regulations affect the business of the Group both in terms of the costs of compliance with and the risk of liabilities arising from such laws and regulations. LASMO conducts its business so as to comply with both its own environmental policy and the environmental regulatory regimes pertaining to each of the countries in which it operates.

Environmental policy. LASMO has adopted an environmental policy and implements this policy through an environmental management system which provides, among other things, that (i) environmental analyses are carried out at defined stages of exploration, development and production (e.g., at conceptual design and during operation), (ii) wastes are minimized, treated and controlled and (iii) sites are cleared and restored after seismic, drilling, or production activity. The Group has an ongoing audit program developed to monitor its seismic, drilling and producing operations for compliance with its own and governmental regulatory systems. LASMO believes that the Group's operations and facilities are in compliance in all material respects with applicable environmental regulations.

Environmental regulation. Environmental laws and regulations have had an increasing impact on LASMO's operations. The risks of substantial environmental costs and liabilities are inherent in oil and gas operations, and there can be no assurance that significant costs and liabilities will not be incurred in the future. Moreover, it is possible that other developments, such as increasingly strict environmental laws, regulations and enforcement policies and claims for damages to property and person resulting from the Group's operations, could result in substantial costs and liabilities in the future. Although the Group is unable to predict what such costs and liabilities would be, based upon presently available information, it does not currently expect any material adverse effect upon its consolidated financial position as a result of compliance with such laws and regulations nor does it expect to be more adversely affected than its competitors by the costs of compliance with future such laws and regulations.

North America. LASMO has, in the past, acquired properties that had been used for the transportation, production, treatment and storage of oil or gas for many years. Although these properties utilized operating and disposal practices that were standard in the industry at the time, certain wastes may have been disposed of or released on or under the properties owned, leased or operated by the Group. In the United States, state and federal laws applicable to oil and gas wastes and properties have gradually become more strict. Under these laws, the Group could be required to remove or remediate previously disposed of wastes or property contamination (including groundwater contamination at onshore locations) or to perform remedial plugging operations to prevent further contamination.

The Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), also known as "Superfund", and similar state laws impose joint and several liability, without regard to fault or the legality of the original conduct, on certain classes of persons for costs associated with a release or a threat of release of a "hazardous substance" into the environment. These persons include the owner or operator of a site and companies that disposed of or arranged for the disposal of the hazardous substance found at a site. In the course of its ongoing operations, the Group may generate or may have generated wastes that fall within CERCLA or state law definitions of "hazardous substances". The Group may be responsible under CERCLA or state law for all or part of the costs to clean up sites at which such wastes from any of its operations have been disposed.

A subsidiary of the Company, LASMO Petroleum, Inc. ("LASMO Petroleum") (formerly Ultramar Petroleum Inc.) owns a site in Tankport, New Jersey, formerly used for petroleum storage and marketing.

LASMO Petroleum ceased operations at Tankport in 1987. The site is regulated by the New Jersey Department of Environmental Protection and Energy pursuant to the Industrial Site Recovery Act. An administrative consent order was signed in 1990 requiring PPG Industries, Inc. to clean up chromium contamination. LASMO Petroleum and The Pittston Companies are conducting remedial investigations of petroleum contamination at the site with a view to redevelopment.

LASMO Petroleum has made claims under its insurance policies and brought suit in New Jersey for defense and indemnity in connection with property damage for Tankport. As a result of the settlement LASMO Petroleum has reached with other responsible parties, LASMO is not expected to experience material costs for the remediation of contamination at the site.

In February 1988, LASMO Petroleum received a notice letter from the US Environmental Protection Agency (the "EPA") under CERCLA in connection with the Pine Street Barge Canal Superfund site in which LASMO Petroleum owns a now closed petroleum marketing terminal. The Pine Street Canal site has been placed on the National Priority List because of the presence of large quantities of coal tar that resulted from discharges from a Burlington coal gasification plant which operated long ago. The alleged generators of the coal tar contaminants are all existing utility companies which have been named by the EPA as potentially responsible parties, along with other property owners, including LASMO Petroleum. The EPA has not yet approved a final cleanup plan, however, LASMO has entered into a settlement agreement with the utility companies that significantly limits LASMO's financial exposure. The site may also be subject to petroleum hydrocarbon cleanup under State of Vermont guidelines but current data does not indicate a material liability for LASMO.

LASMO Oil and Gas, Inc. is currently remediating groundwater contamination at a refinery site in Carson City, California, which was formerly Ultramar's Golden Eagle Refinery. LASMO Oil and Gas, Inc. has submitted ground water cleanup performance data to California EPA agencies and is negotiating for a reduction of future groundwater cleanup activities. Soil excavation and treatment have been certified complete by the California Environmental Protection Agency and further cleanup costs are not expected to be material. LASMO is marketing and developing the site through the Carson General Development Partnership.

LASMO Oil and Gas, Inc. has made claims under its insurance policies and brought suit in California for defense and indemnity for past and future cleanup investigation and cleanup costs expended by LASMO.

LASMO has conducted environmental impact studies on a former Ultramar bulk plant in Belleville, Ontario, Canada, resulting in the identification of petroleum hydrocarbon contamination. Based upon present information, the total remediation and clean-up obligations are not expected to be material.

Total future environmental remediation costs cannot reasonably be estimated due to unknown factors at a number of sites such as the magnitude of possible contamination, the timing of expenditures, the determination of appropriate remediation requirements, the resolution of LASMO's liability in relation to other parties, the extent to which such costs are recoverable from insurance and the extent to which environmental remediation laws and regulations may change in the future. Notwithstanding this difficulty, based on currently available information, including outside consultants' studies, the Company believes that environmental remediation costs are not likely to have a materially adverse effect on the Company's financial position.

Venezuela. Prior to takeover of the Dacion Area, LASMO completed an environmental assessment which provided evidence of the existing environmental conditions. Under the terms of the operating agreement entered into with PDVSA, all pre-takeover environmental liabilities remain the responsibility of PDVSA. The environmental assessment carried out does not limit LASMO's subsequent right to demonstrate that any environmental impacts arising in the future resulted from pre-takeover activities.

Risk assessments have also been carried out with respect to ongoing health, safety and environmental hazards present in the existing operations and installations within the Dacion Area. LASMO has initiated an interim program of risk control measures, during which time a program of upgrades will be carried out to existing installations, to bring all such installations up to current recognised international standards.

Regulation of Exploration and Production Activities — Licenses

In order to carry out its exploration and production activities, LASMO is required to comply with a number of different regulatory regimes, particularly those concerning the granting and retention of the various types of licenses governing oil and gas rights. The effect on LASMO of compliance with these different regulatory regimes varies by country and type of regulation and affects virtually all aspects of its operations. Under the various forms of licenses, LASMO generally is obligated to carry out agreed work programs, to bear the risk of exploration, development and production activities and to provide financing for its operations.

LASMO's exploration and production activities are conducted in many different countries and are therefore subject to a broad range of legislation and regulations. These cover virtually all aspects of exploration and production activities, including matters such as land tenure, obligations to carry out minimum work programs, approval of development and other projects, obligations to remove installations on cessation of operations, production rates, royalties, pricing, environmental protection, health and safety, exports, taxes and foreign exchange. The terms and conditions of the leases, licenses, conventions, permits, concessions and contracts, each a "license", under which these oil and gas interests are held vary from country to country. They are generally granted by or entered into with a government entity or state company.

Licenses in the United Kingdom and The Netherlands give the holder the right to explore for and exploit a commercial discovery and in some cases obligations to survey and drill. Under a license, the holder bears the risk of exploration, development and production activities and provides the financing for these operations. Depending on the date of government approval and the size of the field, a license holder may be required to pay royalties and special petroleum production taxes.

A form of license which is common internationally, and is in use in Indonesia, is the PSC entered into with a government entity or a state company. Although PSCs may be in a standard form in each country, many of LASMO's PSCs have been individually negotiated and thus may vary from permit to permit within any one country and be substantially different from country to country. PSCs generally obligate the contractor party to provide all or a major part of the financing and to bear the risk of exploration, development and production activities in exchange for a share of production. In some instances the contractor's production shares will be subject to the payment of royalties and/or tax to the government. Usually a fixed or variable percentage of production is reserved for the recovery of the contractor's costs ("cost oil") and the remainder ("profit oil") is shared with the government generally on a volume-dependent basis. The right of the contractor to recover cost oil is limited in certain cases by a requirement that the cost oil does not exceed a specified maximum percentage of production. This right is also limited in certain cases by a requirement that costs be amortized over a specified period of time. PSCs may require the sale of certain quantities of hydrocarbons to local markets at preferential prices. In some cases, the government entity or state company will participate in the rights and obligations and will share in the costs of development and production and sometimes exploration. State participation in development and production operations is normally restricted to the relevant discovery/development area.

In Venezuela the rights and obligations concerning LASMO's exploration and production activities are set forth in an operating agreement with a subsidiary of the government-owned petroleum company. The agreement grants LASMO the right to operate and redevelop the existing fields within a specified Area during the 20 year contract period and to explore for oil and gas in that Area during the first seven years of that period with the right to develop any oil and gas that LASMO discovers during that exploration period. The agreement allows for full recovery of LASMO's capital and operating costs out of production. Remaining profit will be shared between LASMO and the government on a rate of return basis set forth in the agreement.

In certain countries, separate licenses are required for exploration, development and production activities. Such licenses will be for a specified period of time and may be terminated earlier provided certain conditions are fulfilled; for example if no discovery has been made at the end of the exploration period, or where continued economically viable production is not possible. Conversely, extensions are also possible; for example where work is in progress at the end of a prescribed term or where production is maintainable following the expiration of the license. The terms of LASMO's licenses and the extent to which these licenses may be renewed vary from area to area.

Another form of license under which LASMO currently holds exploration rights is the concession agreement, under which the contractor will be subject to the same type of obligations as under a PSC except that the government's share of production is generally replaced with the payment of royalties and taxes on income.

As is commonplace in the oil and gas exploration and production industry, LASMO generally participates in exploration and production activities in conjunction with several co-venturers pursuant to an operating agreement. While these agreements generally provide for liabilities to be borne by the co-venturers according to their respective percentage interests, licenses from the relevant government authority generally provide that the co-venturers are jointly and severally liable for their obligations to that government authority under the applicable license.

Additional Factors Which May Affect Business

Presented below are a number of additional factors which may affect LASMO's business. These factors, among others, could also cause LASMO's actual production and results to differ materially from those expressed in or implied by certain forward looking statements contained in this report. Such forward looking statements are based upon management's good faith assumptions relating to the financial, market, operating and other relevant environments that will exist and affect LASMO's business and operations in the future. No assurance can be made that the assumptions upon which management based its forward looking statements will prove to be correct, or that LASMO's business and operations will not be affected in any substantial manner by other factors not currently foreseeable by management or beyond LASMO's control. Other factors which could affect such statements include the impact of extraordinary items resulting from LASMO's ongoing evaluation of its business strategies and asset management and acquisition program, and the effect of activities of governments, agencies and similar organizations. All forward looking statements involve risks and uncertainty, including those described in this report, and such statements shall be deemed in the future to be modified in their entirety by LASMO's public pronouncements, including those contained in all future reports and other documents filed by LASMO with the Commission.

Production Revenue Taxes

LASMO is subject to a number of production revenue taxes, of which the most significant is Petroleum Revenue Tax ("PRT"). PRT is a tax applied to the oil and gas industry operating within the UKCS. As such, it can have a significant impact on LASMO's results of operations and cash flows. The following discussion relates to the system of PRT currently in place.

PRT is a tax on production revenue and chargeable asset disposal receipts from oil and gas fields within the UKCS and on tariff income. PRT is assessed on a field by field basis and is computed by reference to chargeable periods which are the six months ending June 30 and December 31 of each year. The tax is only levied on fields for which development consent had been granted by the UK Secretary of State for Trade and Industry by March 16, 1993. PRT is computed by reference to production revenue, tariff income and disposal receipts after deducting UK government royalties and allowable costs (the "assessable profit"). Tax is payable on the assessable profit within two months of the end of each period and is currently levied at a 50% rate on the assessable profit from the above activities after deducting allowable costs. To the extent that allowable costs exceed current revenue, losses calculated for PRT purposes may be carried back to earlier periods with resultant PRT cash recoveries. In addition, such recoveries attract interest or "supplement".

There are two special allowances. First, an Oil Allowance effectively exempts from PRT 500,000 metric tonnes of production per chargeable period for each field (about 20 Mbopd) to an aggregate limit of ten million metric tonnes. These amounts are halved for fields which were under development before April 1982, and quartered, from July 1, 1988, for fields in the Southern Gas Basin. Second, a Tariff Receipts Allowance effectively exempts from PRT tariff income relating to 250,000 metric tonnes of throughput from each user field per chargeable period, unless that user field is exempt from PRT by virtue of development consent having been granted after March 15, 1993.

The “field” basis of computing PRT is often referred to as the PRT ring-fence. The ring-fence concept, which treats each field as a separate taxable entity, does not allow income of one field to be relieved by costs arising in another field. This rule is varied where production from a field is determined to have permanently ceased and over the life of that field there have been cumulative net PRT losses. In such circumstances these PRT losses can be relieved against PRT profits arising in other fields.

PRT is deductible in calculating the UKCS profits subject to UK corporation tax.

LASMO treats PRT as a production cost in cost of sales and it has been charged or credited before arriving at operating profits. PRT supplement is included in interest income on a receivable basis except for amounts which arose in respect of the Piper field redevelopment expenditure claims which have been deferred to be released through interest income as oil is produced from the field.

In general, in addition to special petroleum production taxes and royalties, an oil and gas company is required to pay income taxes on income generated from production, though some PSCs provide for such tax to be paid by the state entity on the company’s behalf. This means that the total government percentage taken from oil and gas production revenues may be, and in many areas such as the North Sea currently is, substantially higher than the percentage of tax levied on other businesses.

The UK Government Budget of March 17, 1998, contained a proposal that government royalty and PRT Tariff Receipts Allowance be abolished. It was also proposed that a consultation period with the UK oil industry commence in April 1998 with a view to agreeing other possible fiscal changes. These would include either reinstatement, at half the current Oil Allowance level, of PRT on post March 16, 1993 fields with the allowance of abortive exploration costs, or the imposition of a “Supplementary Corporation Tax” on UKCS profits, exclusive of finance costs. There has been no statement on the likely rate of such a tax. The Corporation Tax rate will be reduced to 30%, effective April 1999.

Technical Considerations

The actual amount of LASMO’s production in any year will be affected by a number of factors including the ability of LASMO’s operations and infrastructure (or those of a field’s operators) to achieve production goals and the absence of disturbances affecting LASMO’s operations.

Oil and gas exploration and production activities are subject to natural hazards and uncertainties including those relating to the physical characteristics of oil and gas fields. These characteristics, including the proportion of reserves ultimately producible and the rate of production, are difficult to estimate and cannot always be reliably estimated even using modern technology and exploration techniques. Oil and gas production usually requires the installation of expensive and complex extraction equipment for operational use in what may be a hostile environment, in particular offshore, for long periods of time and with a consequent risk of failure. Hazards, some of which are particularly applicable to offshore operations, include collision, bad weather, pollution, fire and explosion and well blowout, some of the consequences of which cannot or may not reasonably be insured against. LASMO’s production operations are also subject to scheduled and unscheduled maintenance shutdowns which affect output. In addition, in general as oil fields mature production naturally declines.

Exploratory drilling carries the risk that no economically viable oil or gas production will be obtained, while the cost of drilling, completing and operating wells is often uncertain. Furthermore, drilling may be curtailed or delayed as a result of many factors including weather conditions, availability of suitable drilling rigs and title disputes.

In the past, LASMO’s production has been affected by these and other factors and, as a result, there can be no assurance that LASMO will be able to produce at its budgeted levels in any financial year.

Political and Economic Considerations

Oil and gas production requires high levels of investment and has particular economic risks and opportunities. There is strong competition within the oil and gas production industry and with other industries in supplying fuel needs.

The oil and gas production industry is highly regulated and is subject to intervention by governments throughout the world in matters such as the award of exploration and production interests, the imposition of specific drilling and other work obligations, environmental protection measures and control over the development and abandonment of fields and installations (including restrictions on production, for example, in order to comply with quota allocations set by the Organization of Petroleum Exporting Countries (“OPEC”)).

LASMO’s principal oil and gas reserves and exploration acreage are currently located in the UK and Indonesia regions and in Venezuela and Algeria. LASMO also has reserves and exploration interests in certain other countries, which may from time to time be considered politically and economically unstable. Reserves and the related operations in the countries in which LASMO operates are in varying degrees subject to certain risks, including increases in taxes and royalties, the establishment of production and export limits, the renegotiation or cancellation of contracts, the nationalization, renationalization or expropriation of assets, other risks relating to changes in local government regimes and policies and resulting changes in business customs and practices, payment delays, currency exchange restrictions and losses and impairment of operations by actions of insurgents. LASMO, like other international oil and gas exploration and production companies, attempts to conduct its business and financial affairs so as to spread and minimize such political and economic risks.

Financial Considerations

Ceiling Tests. In accordance with recommended practice, LASMO applies ceiling tests to oil and gas assets at the end of each year, under which net book amounts carried in respect of each field are compared with the estimated undiscounted net realizable amount of proven and probable reserves at year end prices and exchange rates. Any impairment identified in respect of tangible assets is written off to the extent that such impairment is considered, in the opinion of management, to be permanent. See “Item 9. Management’s Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations — 1997 Compared with 1996 — Operating Profit”, “— 1996 Compared with 1995 — Operating Profit” and Note 4 of Notes to the Financial Statements.

Under US Statement of Financial Accounting Standards 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of” (“FAS 121”), the US GAAP net book amounts carried in respect of each field are compared with the undiscounted net cash flows estimated by management. For those fields where deficits are identified, provision for impairment which is considered to be other than temporary is made by reference to the estimated discounted cash flows. See Note 29 of Notes to the Financial Statements.

Acquisitions and Disposals

Acquisitions

LASMO from time to time has acquired both assets and other oil and gas companies. Such acquisitions have varied in size but some have been significant. LASMO has considered and will continue to consider acquisitions if it believes that assets are available at attractive prices or where it believes that its technical abilities or the spread of its assets permit adding value. At the end of 1991, LASMO acquired control of Ultramar through an offer of LASMO shares or LASMO shares and cash for Ultramar shares. The total consideration for the acquisition was approximately £1 billion, consisting of LASMO ordinary shares and £103 million of cash. The Ultramar businesses acquired by LASMO included oil and gas exploration and production, refining and marketing activities and shipping. At the time of the offer, LASMO declared its

intention to merge Ultramar's exploration and production activities with those of LASMO and to dispose of the refining, marketing and shipping businesses.

Disposals

In the period 1992 to 1996, LASMO rationalized the Group's portfolio by actively managing its assets through disposals, farmouts and swaps. Disposals in 1992 raised £732 million and by the end of 1996 asset sales had raised a further £552 million.

This rationalization includes the disposal of Ultramar's refining and marketing businesses, which was completed during 1992 for \$949 million. The disposal was effected by sale of the business to a new company, Ultramar Corporation, which funded the acquisition by sale of its shares through an initial public offering and an associated debt offering. The refining and marketing companies sold were Canadian Ultramar Limited, Ultramar Canada Inc. and subsidiaries and Ultramar Inc. and subsidiaries. Certain other downstream businesses were also sold, principally Ultramar's shipping fleet for \$125 million.

In 1997, LASMO withdrew from Gabon and acquired an interest in the Trinidad field in Colombia. It has continued to evaluate its businesses in non-core areas. It plans to withdraw from Colombia and is reviewing its business in Italy.

There were no other material acquisitions or disposals during 1997.

Insurance

LASMO maintains an insurance program which, in the view of management, is adequate in relation to its activities. The policies making up the program contain specific terms and conditions, including wordings, limits and deductibles, as offered by the insurance markets used by LASMO. Insurance is provided for risk of death or injury to LASMO personnel, and for physical loss or damage to assets owned by the Group and liabilities to third parties arising out of the Group's operations.

In accordance with usual industry standards, LASMO also maintains insurance for well control operations and pollution incidents. LASMO insures against loss of income in the event of an interruption to production operations in the Sanga Sanga PSC in Indonesia.

Insurance cover is maintained as required to meet legal and statutory obligations in areas where the Group operates. In addition, LASMO is a party to the Offshore Pollution Liability Agreement ("OPOL"). OPOL resolves to provide an orderly means for compensating and reimbursing any person who sustains pollution damage and any public authority which incurs costs for remedial measures following a discharge of oil from the operated offshore facilities within certain designated states, including the United Kingdom and the Netherlands. LASMO utilizes insurance to evidence its financial responsibility for up to a maximum of US\$120 million per incident and US\$240 million in the annual aggregate.

Staff

At December 31, 1997, LASMO had 832 staff worldwide, of whom 323 were located in the UK region. LASMO's headquarters are in London and it also has offices in Aberdeen and eleven other countries.

Operational Statistics

The following tables set forth operational and statistical information of LASMO relating to production, drilling, productive wells and acreage.

Production

The following table sets forth average daily production of crude oil and natural gas during the years ended December 31, 1997, 1996 and 1995.

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
Crude oil (bopd)				
1997	68,200	9,600	10,700	88,500
1996	58,000	9,400	10,600	78,000
1995	46,800	9,300	22,000	78,100
Natural gas (Mcf)				
1997	159,900	320,600	25,500	506,000
1996	163,700	393,200	25,900	582,800
1995	129,600	365,600	20,100	515,300

Production included in respect of interests subject to PSCs is stated net of government share and is subject to revision as prices fluctuate, due to the cost recovery features under the terms of the PSCs. Thus, an increase in crude oil prices will result in a decrease in such entitlement production.

Crude Oil and Natural Gas Prices and Cost of Sales

The Group's average sales prices and cost of sales (including depletion and decommissioning) of crude oil and natural gas for the years ended December 31, 1997, 1996 and 1995 were as follows:

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	<u>£</u>	<u>£</u>	<u>£</u>	<u>£</u>
Average sales prices				
Per bbl of crude oil				
1997	11.47	10.03	9.10	11.03
1996	11.61	11.17	11.57	11.55
1995	10.40	10.48	10.90	10.58
Per Mcf of natural gas				
1997	1.75	2.10	1.05	1.93
1996	1.56	2.35	1.06	2.06
1995	1.46	2.05	0.99	1.85
Average cost of sales per boe				
1997	8.19	5.61	6.99	7.16
1996	8.24	5.97	8.33	7.29
1995	8.81	5.91	7.13	7.30

Average sales prices for sales of natural gas in Indonesia relate principally to sales of LNG. The average sales price is based upon liftings of LNG from the Bontang liquefaction plant and is determined according to Btu content. Production of LNG in Indonesia is based on gas volumes delivered to the plant, with approximately 11% of natural gas delivered consumed in the liquefaction process.

Productive Wells and Acreage

The following tables show the number of gross and net productive crude oil and natural gas wells and total gross and net developed and undeveloped acres in which the Group had interests as at December 31, 1997. A "gross" well or acre is one in which a whole or fractional working interest is owned, whereas the number of "net" wells or acres is the sum of the whole or fractional working interests in gross wells or acres. Productive wells are producing wells and wells capable of production. Developed acreage is acreage within the boundary of a field, on which development wells have been drilled, which could produce the reserves, while undeveloped acres are those on which wells have not been drilled or completed to a point that would permit the production of commercial quantities of crude oil and natural gas, whether or not such acres contain proved reserves.

Number of productive crude oil and natural gas wells

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
At December 31, 1997				
Crude oil wells(1) — gross	108	104	26	238
— net	22	38	13	73
Natural gas wells(1) — gross	58	381	8	447
— net	9	133	2	144

(1) Includes no multiple completion wells (more than one formation producing into the same well bore).

Crude oil and natural gas acreage

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(acres)			
At December 31, 1997				
Developed — gross	373,136	115,153	163,834	652,123
— net	131,462	43,491	67,461	242,414
Undeveloped — gross	3,146,204	3,745,940	27,406,476	34,298,620
— net	792,235	1,445,099	15,068,521	17,305,855

Net crude oil and natural gas wells completed or abandoned

The following table shows the number of exploration and development crude oil and natural gas wells completed or abandoned by the Group in the years indicated. Productive wells include wells in which hydrocarbons were encountered and the drilling or completion of which, in the case of exploration wells, has been suspended pending further drilling or evaluation. A dry well is an exploration or development well found to be incapable of producing hydrocarbons in sufficient quantities to justify completion and therefore abandoned.

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
1997				
Exploration — productive	1.3	—	3.5	4.8
— dry	2.3	1.4	1.9	5.6
Development — productive	3.3	2.6	1.1	7.0
— dry	0.2	—	—	0.2
1996				
Exploration — productive	1.0	—	1.7	2.7
— dry	2.0	0.9	2.6	5.5
Development — productive	5.8	3.0	0.5	9.3
— dry	0.6	—	0.3	0.9
1995				
Exploration — productive	0.1	—	1.3	1.4
— dry	0.7	0.4	1.6	2.7
Development — productive	3.2	6.4	0.7	10.3
— dry	0.2	—	0.2	0.4

Present Drilling Activities

The following table shows the number of exploratory and development crude oil and natural gas wells in the process of being drilled by the Group at December 31, 1997. Suspended development wells and long-term suspended exploratory wells are also included in the table.

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
At December 31, 1997				
Exploratory — gross	1.0	—	5.0	6.0
— net	0.2	—	1.1	1.3
Development — gross	9.0	1.0	1.0	11.0
— net	2.2	0.3	0.1	2.6

ITEM 2. DESCRIPTION OF PROPERTY

LASMO has freehold and leasehold interests in real estate in a number of countries but none of these is significant to the Group as a whole. See “Item 1. Description of Business” for a description of the Group’s other properties, reserves and sources of crude oil and natural gas.

ITEM 3. LEGAL PROCEEDINGS

Neither LASMO nor any of its subsidiaries is involved in any legal or arbitration proceedings which it believes may have a material adverse effect on the financial position of LASMO nor, so far as it is aware, are any such proceedings pending or threatened against LASMO or any of its subsidiaries.

ITEM 4. CONTROL OF REGISTRANT

As far as is known to the Company, it is not directly or indirectly owned or controlled by another corporation or by any government and there are no arrangements the operation of which may result in change in its control. Except as detailed below, as of April 16, 1998, there were no persons known to the Company owning individually more than 10% of any class of the Company’s voting securities. As of April 16, 1998, the Company had received notifications from the following of interests held by them equal to or in excess of 3% of the issued ordinary share capital of the Company.

	<u>Ordinary shares</u>	<u>Percentage of class</u>
Schroder Investment Management Limited.....	125,848,957	13.0%

As of April 16, 1998, the directors and the executive officer of the Company as a group beneficially owned 377,005 ordinary shares which constituted less than 1% of the issued ordinary shares on such date. Their ownership of ordinary shares is set forth below.

	<u>Beneficially owned at April 16, 1998</u>
<u>Directors</u>	<u>Ordinary shares (1)</u>
R I J Agnew	10,000
A P Hichens	14,000
J Darby	71,185
T P Brennand	10,000
W G Cochrane	25,000
J A Hogan	44,283
T G King	11,400
P C Murray	26,451
H E Norton	—
R G Reynolds	—
R L Smernoff	100,000
N V Turnbull	15,000
C A Wright	25,000
<u>Executive Officer</u>	
J A T Wedgwood	24,686
	<u>377,005</u>

(1) Includes ordinary shares held by family members of directors and executive officer.

ITEM 5. NATURE OF TRADING MARKET

Trading market for ordinary shares

The principal trading market for the Company's ordinary shares is the London Stock Exchange (the "LSE"). Trading takes place on a new order-driven system, the Stock Exchange Electronic Trading Service ("SETS"), introduced on October 20, 1997. Under SETS, buy and sell orders at specific prices may be sent to the exchange electronically by any firm which is a member of the LSE, on behalf of a client or on behalf of itself acting as a principal. The orders are then anonymously displayed in the order book. Where a buyer and seller are prepared to deal at a common price, the trade will match electronically and is automatically reported to the LSE. Dealings in the Company's ordinary shares may also take place between an investor and a market-maker, via a member firm, outside the electronic order book.

The Company's ordinary shares are also traded on the Montreal and Toronto stock exchanges.

ADSs, each representing three ordinary shares, are listed on the New York Stock Exchange. The Bank of New York is the depositary (the "Depositary") of the ADRs representing the ADSs. Trading in ADSs commenced on the New York Stock Exchange on June 8, 1993.

The following table shows, for the calendar quarters indicated, the reported high and low middle market quotations (which represent an average of bid and asked prices) for the ordinary shares on the London Stock Exchange, as derived from its Daily Official List, and the highest and lowest sales prices of ADSs as derived from the New York Stock Exchange composite tape.

<u>Fiscal Year</u>	<u>Ordinary Shares</u>		<u>ADSs</u>	
	<u>High</u>	<u>Low</u>	<u>High</u>	<u>Low</u>
	<u>p</u>	<u>p</u>	<u>\$</u>	<u>\$</u>
1996				
First quarter	189	164	8.75	7.38
Second quarter	194	175	8.75	8.00
Third quarter	218.5	172	10.13	8.00
Fourth quarter	239	199	12.13	9.63
1997				
First quarter	242.5	232.5	11.88	11.88
Second quarter	275.5	218.5	13.38	13.13
Third quarter	287.5	257.5	13.19	13.00
Fourth quarter	285.0	249.5	13.13	12.69
1998				
First quarter	292.25	248.0	13.81	12.75

At March 31, 1998 3,194,436 ADSs (equivalent to 9,583,308 ordinary shares or approximately 1% of the total ordinary shares outstanding) were registered in the name of 283 US holders and 258,081 ordinary shares (less than 1% of total ordinary shares outstanding) were registered in the name of 221 US holders. Since certain of such ordinary shares or ADSs are held by nominees, the number of holders may not be representative of the number of beneficial owners in the US or the ordinary shares held by them.

Trading Market for Dollar Preference Shares

The Dollar Preference Shares are traded in the form of ADSs (the “Series A ADSs”) on the New York Stock Exchange. Trading commenced in Series A ADSs on June 23, 1993. The following table shows the highest and lowest sales prices of Series A ADSs as derived from the New York Stock Exchange composite tape.

	<u>Series A ADSs(1)</u>	
	<u>High</u>	<u>Low</u>
	<u>\$</u>	<u>\$</u>
1996		
First quarter	25.63	24.00
Second quarter	25.63	24.00
Third quarter	25.88	24.95
Fourth quarter	26.38	25.38
1997		
First quarter	25.63	25.50
Second quarter	26.06	25.94
Third quarter	26.31	26.25
Fourth quarter	26.31	26.25
1998		
First quarter	26.50	26.06

(1) Each Series A ADS represents one Dollar Preference Share.

At March 31, 1998, 10,000,000 Series A ADSs (100% of the total) were outstanding and were held by 319 holders.

ITEM 6. EXCHANGE CONTROLS AND OTHER LIMITATIONS AFFECTING SECURITY-HOLDERS

There are currently no UK foreign exchange control restrictions that restrict the export or import of capital, or any other governmental laws, decrees or regulations in the UK that affect the payment of dividends, interest or other payments to non-resident holders of the Company's securities.

There are no restrictions under the Company's Memorandum and Articles of Association (the "Articles of Association") or under English law that limit the right of non-resident or foreign owners to hold or vote the Company's securities.

ITEM 7. TAXATION

The following summary of certain US federal income tax considerations and of certain UK tax considerations describes the principal US federal and UK tax consequences to beneficial owners that are residents or citizens of the United States of the ownership and disposal of ADSs or ordinary shares and Series A ADSs or Dollar Preference Shares and is not a complete analysis or listing of all of the possible tax consequences of such ownership or disposal. Such beneficial owners are advised to consult their tax advisers with respect to the overall tax consequences of the ownership and disposal of the ADSs or ordinary shares and Series A ADSs or Dollar Preference Shares, including specifically the treatment under US state and local tax laws.

The statements regarding US and UK tax laws set out below are based (i) on those laws and the conventions between the United States and the United Kingdom for the avoidance of double taxation with respect to taxes on income and capital gains (the "Income Tax Convention") and with respect to estate and gift taxes (the "Estate Tax Convention") as in force on the date of this Annual Report and on the practice of the UK Inland Revenue as at such date, all of which are subject to any change (including any change having retroactive effect) and (ii) in part upon representations of the Depositary for the ADSs and Series A ADSs and assumes that each obligation in the Deposit Agreements relating to the ADSs and Series A ADSs and any related agreements will be performed in accordance with their terms.

Beneficial owners of the ADSs and the Series A ADSs who are residents or citizens of the United States will be treated as the owners of the underlying ordinary shares or Dollar Preference Shares, respectively, for purposes of the Income Tax Convention and the US Internal Revenue Code of 1986, as amended. For purposes of this summary, the term "US Holders" refers to the beneficial owners of the ADSs or the ordinary shares and Series A ADSs or Dollar Preference Shares (as the context may require) that are residents or citizens of the United States.

Taxation of Dividends

For the purposes of this summary, the term "Eligible US Holder" means a beneficial owner of an ADS or an ordinary share or a Series A ADS or a Dollar Preference Share that derives and beneficially owns the cash dividend paid thereon that is a resident of the United States for the purposes of the Income Tax Convention and that satisfies the following conditions:

(i) is an individual, a corporation, a partnership, a trust or an estate resident in the United States for purposes of the Income Tax Convention (and, in the case of a corporation, not also resident in the United Kingdom for UK tax purposes);

(ii) is not a corporation which, alone or together with one or more associated corporations, controls directly or indirectly, 10% or more of the Company's voting stock;

(iii) whose holding of the ADSs or ordinary shares or a Series A ADS or a Dollar Preference Share, as the case may be, is not effectively connected with a permanent establishment in the United Kingdom through which such holder carries on a business or with a fixed base in the United Kingdom from which such holder performs independent personal services; and

(iv) under certain circumstances, is not a corporation 25% or more of the capital of which is owned, directly or indirectly, by persons that are neither individual residents of, nor citizens of, the United States.

The Company is required when paying a dividend other than a foreign income dividend (a “FID”, as discussed below) to account to the UK Inland Revenue for an advance payment of corporation tax (“ACT”) currently equal to 25% of the dividend. Individuals who are resident in the UK and who receive a dividend (other than a FID) from the Company are entitled to a tax credit (the “associated UK tax credit”) equal to 25% of the dividend (i.e. the equivalent of 20% of the sum of the dividend and the associated UK tax credit).

Under the Income Tax Convention and under current UK law, an Eligible US Holder will be entitled to receive, in addition to the dividend (other than a FID), an amount equal to the associated UK tax credit less UK withholding tax equal to 15% of the sum of the dividend and the associated UK tax credit.

As a result, assuming continuance of the associated UK tax credit at its current rate of 25% of the dividend (i.e. the equivalent of 20% of the sum of the dividend and the associated UK tax credit), payment to such an Eligible US Holder of a dividend (other than a FID) of £80 would result in a payment of £5 (an amount equal to the associated UK tax credit of £20 less the UK withholding tax of £15), giving a total net receipt after UK taxes but before US taxes of £85.

As described below, the UK Inland Revenue has agreed to procedures under which qualifying Eligible US Holders who receive a dividend (other than a FID) from the Company may receive the payment due in respect of the associated UK tax credit, net of UK withholding tax, at the same time as and together with the dividend. These procedures can be terminated or altered without notice by the UK Inland Revenue. Eligible US Holders who do not come within those arrangements must make an individual claim for refund by sending the appropriate UK form to the US Internal Revenue Service or the UK Inland Revenue, as described below under “General”.

Special rules apply if the Eligible US Holder:

- (i) is exempt from tax in the United States on dividends paid by the Company; or
- (ii) is the owner of at least 10% of the class of shares in respect of which the dividend is paid.

In addition, if the Eligible US Holder is a US partnership, trust or estate, a payment in respect of the associated UK tax credit will be available only to the extent that the income derived by such partnership, trust or estate is subject to US federal income tax as the income of a resident either in its hands or in the hands of its partners or beneficiaries, as the case may be. However, if a US trust or estate is also a resident of the United Kingdom for the purposes of the Income Tax Convention, a payment in respect of the associated UK tax credit may not be available.

The Finance Act 1994 contained provisions allowing companies to elect to pay a FID which do not require the Company to account for ACT and do not carry an associated UK tax credit. A US Holder receiving a FID would not be entitled to receive an associated UK tax credit payment in respect of the FID but would suffer no withholding tax. Where the Company pays no regular UK corporation tax, a dividend (other than a FID) of £80 gives an Eligible US shareholder a net receipt of £85 before US taxes (as described above), but costs the Company £100 (including ACT of £20, as described above). A FID of £100 which costs the Company £100, would give an Eligible US Holder a total net receipt before US taxes of £100.

On March 17, 1998, the UK Government announced a proposal to abolish ACT effective April 6, 1999. If the proposal is enacted, all dividends thereafter will be treated in the hands on an Eligible US shareholder in the same manner as that described above in relation to FID’s.

Payments of dividends and amounts in respect of any associated UK tax credit (including any related UK withholding tax) to US Holders will be dividend income to them for US federal income tax purposes but US Holders will not be eligible for the dividends-received deduction otherwise allowed to corporations. The amount includable in income will be the US dollar value of the payment regardless of whether the payment is in fact made in or converted into US dollars. The US dollar value of a dividend paid in pounds sterling will be determined at the spot rate on the date such dividend is actually or constructively received by the US Holder,

in the case of ordinary shares, or the Depository in the case of ADSs. Gain or loss, if any, realized on a sale or other disposition of the pounds sterling will be ordinary income or loss. Subject to certain limitations, the 15% UK withholding tax will be treated as a foreign income tax eligible for credit against such US Holder's US federal income taxes.

Holders of ADSs or Series A ADSs

Under arrangements agreed with the UK Inland Revenue, an Eligible US Holder of ADSs or Series A ADSs that is:

- (i) a US corporation;
- (ii) an individual resident in the United States and not resident in the United Kingdom; or
- (iii) a trust or estate all the beneficiaries of which are resident in the United States

will generally receive a payment in respect of the associated UK tax credit to which such Eligible US Holder is entitled, net of the applicable UK withholding tax, at the same time as and together with the payment of the dividend as long as the registered holder completes the declaration on the reverse of the dividend check confirming the Eligible US Holder's entitlement to a payment in respect of the associated UK tax credit and presents the check for payment within three months from the date of issue of the check or, in the case of ADSs or Series A ADSs held through the Depository Trust Company ("DTC"), as long as a declaration as to the conditions entitling the Eligible US Holder to a payment in respect of the associated UK tax credit is completed by the broker-dealer or bank-member of DTC which holds the ADSs or Series A ADSs on behalf of the Eligible US Holder.

These arrangements do not apply where the dividend is a FID or to an Eligible US Holder that is:

- (i) exempt from US tax in respect of the dividend (except in certain limited circumstances);
- (ii) an owner of 10% or more of the class of shares in respect of which the dividend is paid;
- (iii) an investment or holding company, 25% or more of the capital of which is owned, directly or indirectly, by persons that are neither individual residents of, nor citizens of, the United States;
- (iv) engaged in business or performing independent personal services through a permanent establishment or fixed base in the United Kingdom; or
- (v) a US corporation which either alone or together with one or more associated corporations controls, directly or indirectly, 10% or more of the voting power in the Company.

Holders of ordinary shares and Dollar Preference Shares

Under arrangements agreed with the UK Inland Revenue, in order to receive a payment in respect of the associated UK tax credit at the same time as and together with the payment of the dividend (other than a FID), a qualifying Eligible US Holder's ordinary shares or Dollar Preference Shares must be registered in the name of a nominee approved by the UK Inland Revenue for the purpose, and the nominee must follow certain procedural requirements. In addition, the qualifying Eligible US Holder must be either:

- (a) an individual who:
 - (i) is not resident in the United Kingdom;
 - (ii) has not during the previous four years been in the United Kingdom for as much as three months a year on average, or for a period or periods amounting in all to six months in the relevant UK income tax year;
 - (iii) has not been absent from the United States for a complete US tax year in any of the previous four years;
 - (iv) does not have a permanent establishment in the United Kingdom; and

- (v) does not own 10% or more of the class of shares in respect of which the dividend is paid; or
- (b) a corporation:
 - (i) which is managed and controlled in the United States and does not have a permanent establishment in the United Kingdom;
 - (ii) which does not, either alone or together with one or more associated corporations, control, directly or indirectly, 10% or more of the voting power in the Company;
 - (iii) which does not own 10% or more of the class of shares in respect of which the dividend is paid;
 - (iv) which is liable to US tax on the dividend; and
 - (v) at least 75% of the capital of which is owned directly or indirectly by persons who are US residents. These arrangements will be extended to trusts, estates in the course of administration, pension funds, foundations and similar bodies only with the prior approval of the UK Inland Revenue.

General

Eligible US Holders that do not come within the above arrangements must make an individual claim for a refund of the associated UK tax credit, net of withholding tax, in the manner and at the times described in US Revenue Procedure 80-18, 1980-1 C.B. 623, and US Revenue Procedure 81-58, 1981-2 C.B. 678. Claims for refund must be made within six years of the UK year of assessment (generally, the 12-month period ending April 5 in each year) in which the related dividend was payable. This first claim for a refund under these procedures is made by sending the appropriate UK form in duplicate to the Director of the Internal Revenue Service Center with which the Eligible US Holder's last US federal income tax return was filed. Forms may be obtained from the Internal Revenue Service, Assistant Commissioner (International), 950 L'Enfant Plaza South, S.W., Washington D.C. 20024. Because a refund claim is not considered made until the UK tax authorities receive the appropriate form from the Internal Revenue Service, forms should be sent to the Internal Revenue Service well before the end of the applicable limitation period. Any claim for refund of the associated UK tax credit (net of UK withholding tax) by an Eligible US Holder after the first claim should be filed directly with the UK Inland Revenue, Financial Intermediaries and Claims office, Fitzroy House, PO Box 46, Nottingham, NG2 1BD, England.

Taxation of Capital Gains

A US Holder that is not resident or ordinarily resident for UK tax purposes in the United Kingdom will not be liable for UK taxation on capital gains realized or accrued on the sale or other disposal of ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares unless the US Holder carries on a trade, profession or vocation in the United Kingdom through a branch or agency and such ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares are or have been used, held or acquired for the purposes of such trade, profession or vocation or such branch or agency. A US Holder will be liable for US federal income tax on such gains to the same extent as on any other gains from sales of stock.

A US citizen who is resident or ordinarily resident in the United Kingdom, a US corporation which is resident in the United Kingdom by reason of its business being managed and controlled in the United Kingdom or a US citizen who, or US corporation which, is trading or carrying on a profession or vocation in the United Kingdom through a branch or agency, and has used, held or acquired ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares for the purpose of such trade, profession or vocation or such branch or agency, may be liable for both UK and US tax on a capital gain realized or accrued on the disposal of ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares. Such holder, however, generally will be entitled to a foreign tax credit, subject to certain limitations, against any US federal tax liability for the amount of any UK tax (namely, capital gains tax in the case of an individual and corporation tax on chargeable gains in the case of a corporation) which is paid in respect of such gain.

Redemption of Dollar Preference Shares

In the event that the Company redeems a Dollar Preference Share, any special dividend paid by the Company will be treated for UK tax purposes in the manner described under “Taxation of Dividends” above.

Estate and Gift Tax

UK inheritance tax (“IHT”) is a tax levied at death on the value of an individual’s estate at death and on the value of certain gifts. It may also apply to certain lifetime transfers or to property comprised in a trust or settlement. In general, a domiciliary of the United States need only be concerned about liability for IHT if he or she is or is deemed to be also a UK domiciliary or if he or she owns any UK situs property. Ordinary shares and Dollar Preference Shares are, and ADSs and Series A ADSs in certain circumstances may be, assets situated in the United Kingdom for the purposes of IHT. Under the Estate and Gift Tax Convention, an individual who is domiciled for the purpose of the Estate and Gift Tax Convention in the United States and is not for the purposes of the Estate and Gift Tax Convention a national of the United Kingdom will not, provided any applicable US tax is paid, generally be subject to IHT in respect of the ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares on the individual’s death or on a gift of the ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares unless the ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares are part of the business property of a permanent establishment of the individual in the United Kingdom or, in the case of a holder who performs independent personal services, pertain to a fixed base situated in the United Kingdom. In the exceptional case where the ADSs or ordinary shares or Series A ADSs or Dollar Preference Shares are subject both to IHT and to US federal gift or estate tax, the Estate and Gift Tax Convention generally provides for tax paid in the United Kingdom to be credited against tax payable in the United States or for tax paid in the United States to be credited against tax payable in the United Kingdom based on priority rules set forth in the Estate and Gift Tax Convention.

UK Stamp Duty and UK Stamp Duty Reserve Tax

ADSs and Series A ADSs

No UK stamp duty reserve tax (“SDRT”) will be payable on an agreement to transfer ADSs or Series A ADSs in the form of ADRs or Series A ADRs, as the case may be, nor will UK stamp duty be payable on the acquisition or transfer of ADSs or Series A ADSs provided that the instrument of transfer is executed outside the United Kingdom and subsequently remains at all times outside the United Kingdom.

A transfer of ordinary shares or Dollar Preference Shares by the Depositary or its nominee to the beneficial owner of the relative ADSs or Series A ADSs, as the case may be, or his nominee, when that beneficial owner is not transferring beneficial ownership will give rise to UK stamp duty at the rate of £0.50 per transfer.

Ordinary shares and Dollar Preference Shares

A sale of ordinary shares or Dollar Preference Shares in registered form by an investor will normally give rise to UK stamp duty or (unless both vendor and purchaser are resident outside the United Kingdom for UK tax purposes and the transaction is carried out outside the United Kingdom) SDRT generally at the rate of £0.50 per £100 (or part thereof) of the price. However, where such ordinary shares or Dollar Preference Shares sold are transferred to an issuer of depositary receipts or a provider of clearance services or a nominee or agent of such person, a higher UK stamp duty or SDRT charge will normally arise equal to £1.50 per £100 (or part thereof) of the price. A transfer of ordinary shares or Dollar Preference Shares to an issuer of depositary receipts or a provider of clearance services or a nominee or agent of such a person where there is no transfer of beneficial ownership will give rise to UK stamp duty or SDRT generally at the rate of £1.50 per £100 (or part thereof) of the value of the ordinary shares or Dollar Preference Shares, as the case may be.

SDRT is generally the liability of the purchaser and UK stamp duty is usually paid by the purchaser or transferee.

ITEM 8. SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated financial data for the five years in the period ended December 31, 1997 are derived from consolidated financial statements of LASMO which have been audited by its independent auditors, Ernst & Young, chartered accountants, restated to accord with the Group's current accounting policies. See Note 1 of Notes to the Financial Statements. The financial results should not be construed as indicative of financial results for subsequent periods. Fluctuations in crude oil prices, exchange rates and the success of exploration activity in particular may have a material impact on the Group's financial results.

LASMO prepares its consolidated financial statements in accordance with UK GAAP which differ in certain respects from US GAAP. A description of the significant differences applicable to LASMO and reconciliations of profit/(loss) for the year and shareholders' equity are set forth in Note 29 of Notes to the Financial Statements.

The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, the LASMO Financial Statements and the Notes thereto which are included in this Annual Report.

	Year ended December 31					
	1997(1)	1997	1996	1995	1994	1993
		(in millions, except per share amounts)				
	\$	£	£	£	£	£
INCOME STATEMENT DATA						
Amounts in accordance with UK GAAP						
Sales	1,184	722	749	637	648	678
Cost of sales	(741)	(452)	(467)	(437)	(469)	(497)
Provision for oil and gas assets(2)	—	—	—	(17)	3	(49)
Release of petroleum revenue tax provisions(3)	—	—	—	—	—	6
Gross profit	443	270	282	183	182	138
Exploration costs written off (net of PRT relief) (2) (3)	(89)	(54)	(46)	(34)	(48)	(62)
Operating profit	302	184	208	112	112	46
Profit on sale of						
fixed assets	—	—	20	14	39	3
assets/businesses held for resale(4)	—	—	(2)	17	(1)	(10)
Interest receivable	67	41	64	80	60	71
Interest payable	(116)	(71)	(84)	(79)	(94)	(123)
Profit/(loss) before taxation	253	154	206	144	92	(9)
Taxation(5)	(174)	(106)	(139)	(110)	(95)	(109)
Profit/(loss) for the year						
Before exceptional items	79	48	47	33	(20)	(46)
Exceptional items(6)	—	—	20	1	17	(72)
Total	79	48	67	34	(3)	(118)
Preference dividends	(20)	(12)	(16)	(19)	(19)	(13)
Profit/(loss) attributable to ordinary shareholders	59	36	51	15	(22)	(131)
Per ordinary share						
Earnings/(loss) for the year before exceptional items	\$ 0.06	3.7p	3.2p	1.5p	(4.3)p	(7.6)p
Earnings/(loss) for the year	\$ 0.06	3.7p	5.3p	1.6p	(2.4)p	(16.8)p
Dividends	\$ 0.04	2.3p	2.0p	1.25p	1.25p	1.3p
Amounts in accordance with US GAAP						
(Loss)/profit for the year	(3)	(2)	70	(29)	(34)	(184)
Preference dividends	(20)	(12)	(16)	(19)	(19)	(13)
(Loss)/profit for the year attributable to ordinary shareholders	(23)	(14)	54	(48)	(53)	(197)
Per ordinary share as so adjusted						
Basic	\$(0.02)	(1.5)p	5.7p	(5.1)p	(6.0)p	(25.9)p
Diluted	—	—	5.6p	—	—	—
Per American Depositary Share as so adjusted						
Basic	\$(0.07)	(4.5)p	17.1p	(15.3)p	(18.0)p	(77.7)p
Diluted	—	—	16.8p	—	—	—
CAPITAL EXPENDITURE DATA						
Amounts in accordance with UK GAAP						
Capital expenditure						
Exploration and appraisal	156	95	75	54	45	84
Development and production	302	184	153	247	252	215
Acquisitions	477	291	8	3	9	—
Disposals	(7)	(4)	(33)	(27)	(196)	(112)
Total	928	566	203	277	110	187

	Year ended December 31					
	1997(1)	1997	1996	1995	1994	1993
	\$	£	(in millions)		£	£
BALANCE SHEET DATA						
Amounts in accordance with UK GAAP						
Total assets	4,733	2,886	2,528	2,923	2,856	2,988
Long-term debt	1,914	1,167	873	1,088	1,074	1,180
Net debt(7)	1,005	613	346	429	384	734
Sterling Preference Shares	—	—	—	60	60	60
Shareholders' equity	2,093	1,276	1,260	1,240	1,235	1,058
Gearing(8)	48%	48%	27%	39%	36%	75%
Amounts in accordance with US GAAP						
Total assets	4,417	2,693	2,361	2,844	2,900	3,163
Shareholders' equity	1,599	975	1,002	970	1,028	870
Net debt as a percentage of net debt and shareholders' equity(9)	39%	39%	26%	31%	28%	46%

- (1) US dollar amounts have been translated solely for convenience at the Noon Buying Rate on December 31, 1997 of £1.00: \$1.64.
- (2) In 1995, taking account of the likely range of future oil prices at the time, the directors provided £17 million in respect of the Piper field group. In 1993, exceptional provisions reflecting lower oil price expectations and a more conservative assessment of reserves in certain fields were made in respect of tangible oil and gas assets totaling £94 million. The provision was reduced by the release of £45 million, which had been provided for UKCS oil and gas assets on which the impact of the March 1993 UK Budget proposals had still to be fully determined, and the release of PRT provisions of £6 million — note (3) below. In addition, exploration costs written off in 1993 includes exceptional provisions of £21 million. See Note 4 of Notes to the Financial Statements and "Item 1. Description of Business — Additional Factors Which May Affect Business — Financial Considerations — Ceiling Tests".
- (3) In 1993, £6 million of deferred PRT provisions were released on the write down of UKCS oil and gas assets offset by a release of provision for deferred corporation tax of £1 million.
- (4) The loss of £2 million in 1996 represents a provision for liabilities relating to downstream businesses acquired with Ultramar. The gain in 1995 of £17 million on assets held for resale represents the release of a provision for certain exposures in the United States established at the time of the acquisition of Ultramar. In 1994, £1 million (1993 £10 million) was provided for loss on disposal of the remaining assets held for resale.
- (5) Taxation includes a £6 million credit in 1997 in respect of advance corporation tax written back and £4 million, £4 million, £4 million and £9 million in 1996, 1995, 1994 and 1993, respectively, in respect of advance corporation tax written off.
- (6) Exceptional items are reflected in each income statement heading to which they relate. See Note 4 of Notes to the Financial Statements.
- (7) Net debt comprises total borrowings (net of unamortized issue expenses) less cash, short-term deposits, government securities, other unlisted investments and the AUK Loan Notes.
- (8) Gearing comprises net debt, and for years prior to 1996 the Sterling Preference Shares, expressed as a percentage of shareholders' equity.
- (9) Net debt under US GAAP does not include unamortized issue expenses.

Dividends

The table below sets forth the amount of interim, final and total dividends paid on each ordinary share in respect of each financial year indicated, increased by the associated UK tax credit (except in the case of the Foreign Income Dividends for 1994, 1995, 1996 and 1997) but before deduction of UK withholding tax (as described under "Item 7. Taxation — Taxation of Dividends") and translated into US dollars per ADS (each ADS representing three ordinary shares) at the Noon Buying Rate on each of the respective payment dates. The amounts per ordinary share and per ADS have been adjusted for the effects of the bonus element of the 1994 Rights Issue.

Year ended December 31	Pence per ordinary share			Cents per ADS(1)		
	Interim	Final	Total	Interim	Final	Total
1993	1.61	—	1.61	7.19	—	7.19
1994	—	1.25	1.25	—	6.00	6.00
1995	—	1.25	1.25	—	5.62	5.62
1996	—	2.00	2.00	—	9.83	9.83
1997	—	2.30(2)	2.30(2)	—	—	—

- (1) Dividends paid in US dollars by the Depository may be based on a market exchange rate other than the Noon Buying Rate.
- (2) Subject to approval at the Annual General Meeting to be held on April 28, 1998 and payable on May 6, 1998. The payment of future dividends will depend upon the Group's net income, financial condition and such other factors, in particular prevailing oil prices, as the Board of Directors deems relevant.

Exchange Rates

The table below sets forth, for the periods and dates indicated, certain information regarding the US dollar/pound sterling exchange rate, based on the Noon Buying Rate, expressed in US dollars per £1.00. Such rates are not used by the Company in the preparation of its consolidated financial statements included in this Annual Report.

<u>Year</u>	<u>Period End</u>	<u>Average Rate(1)</u>	<u>High</u>	<u>Low</u>
1993	1.48	1.50	1.59	1.42
1994	1.57	1.54	1.64	1.46
1995	1.55	1.58	1.64	1.53
1996	1.71	1.57	1.71	1.49
1997	1.64	1.64	1.70	1.58
1998 (through March 31, 1998)	1.68	1.65	1.69	1.61

(1) The average of the Noon Buying Rates on the last business day of each full month during the relevant period.

For information regarding the effects of currency fluctuations on LASMO's results, see "Item 9. Management's Discussion and Analysis of Financial Condition and Results of Operations — Overview — Key Factors", "Item 1. Description of Business — Additional Factors Which May Affect Business" and "Item 9A. Qualitative and Quantitative Disclosures on Market Risks".

ITEM 9. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

LASMO aims to create value through international oil and gas exploration, production and related business activities, thereby providing shareholders with a competitive return on investment over the long term, principally through capital growth. The Group seeks to build on existing significant businesses while looking to identify material platforms for growth in new areas, targeting prolific hydrocarbon basins, with low cost structures, of particular value in a low oil price environment. In addition to its existing core areas of the UK and Indonesia, LASMO has identified North Africa, Venezuela and Pakistan as three new core areas with material businesses at varying degrees of maturity. Where a region fails to demonstrate the potential to develop a material business, LASMO will consider withdrawing. In this context, it withdrew from Gabon effective January 1, 1997, has announced its intention of withdrawing from Colombia and is reviewing its business in Italy.

This asset management continues previous activity whereby in the period 1992 to 1996, LASMO rationalized the Group's portfolio by actively managing its assets through disposals, farmouts and swaps. Disposals in 1992 raised £732 million and by the end of 1996 asset sales had raised a further £552 million. LASMO will continue to manage its assets through disposals, farmouts and swaps in order to seek to reduce its cost base and improve efficiency. LASMO will also consider selective acquisitions in the pursuit of its objectives consistent with its stated strategy.

For a summary of factors which may affect LASMO's operating results and financial condition, see "Item 1. Description of Business — Additional Factors Which May Affect Business" and "Item 9A. Qualitative and Quantitative Disclosures on Market Risks".

Accounting Principles. The following discussion is based on the consolidated financial statements of LASMO included in this Annual Report which have been prepared in accordance with UK GAAP which differ in certain respects from US GAAP. The significant differences relevant to LASMO relate to depletion

(because of the requirement to use only proved developed reserves for US GAAP rather than proven and probable reserves as permitted under UK GAAP) and deferred tax (because of the requirement to provide for deferred tax on all temporary differences under US GAAP rather than only to the extent that deferred tax liabilities will crystallize as required under UK GAAP). See Note 29 of Notes to the Financial Statements for a discussion of the significant differences between US GAAP and UK GAAP relevant to LASMO.

Results of Operations

Information regarding average prices realized and average daily production volumes of LASMO's oil and gas operations is as follows:

	Average Prices			Average Daily Production Volumes		
	Year ended December 31			Year ended December 31		
	1997	1996	1995	1997	1996	1995
	\$	\$	\$			
	(per barrel)			(bopd)		
Crude Oil						
UK	18.82	18.17	16.40	68,200	58,000	46,800
Indonesia	16.45	17.39	16.53	9,600	9,400	9,300
International	14.90	18.03	17.20	<u>10,700</u>	<u>10,600</u>	<u>22,000</u>
Total	18.10	18.06	16.69	<u>88,500</u>	<u>78,000</u>	<u>78,100</u>
	\$	\$	\$			
	(per Mcf)			(Mcf)		
Natural Gas						
UK	2.87	2.45	2.30	159,900	163,700	129,600
Indonesia(1)	3.44	3.67	3.23	320,600	393,200	365,600
International	1.72	1.66	1.56	<u>25,500</u>	<u>25,900</u>	<u>20,100</u>
Total	3.17	3.21	2.91	<u>506,000</u>	<u>582,800</u>	<u>515,300</u>
				(boepd)		
Combined Crude Oil and Natural Gas						
UK				94,900	85,300	68,400
Indonesia				63,000	74,900	70,200
International				<u>14,900</u>	<u>14,900</u>	<u>25,400</u>
Total				<u>172,800</u>	<u>175,100</u>	<u>164,000</u>
Average Exchange Rates \$/£(2)	1.64	1.56	1.58			

(1) The price of most Indonesian LNG sold by LASMO is based on the price of a basket of Indonesian crude oils. Average sales prices for sales of natural gas in Indonesia relate principally to sales of LNG. The average sales price is based upon liftings of LNG from the Bontang liquefaction plant and is determined according to Btu content. Production of LNG in Indonesia is based on gas volumes delivered to the plant, with approximately 11% of natural gas delivered consumed in the liquefaction process.

(2) Exchange rates shown are average rates for the financial year.

For an analysis of LASMO's sales and profit/(loss) by operating region, see "Item 1. Description of Business — General".

1997 Compared to 1996

Sales. Total sales for 1997 of £722 million were 4% lower than 1996, due to a combination of the 1% decrease in average daily production and the weaker oil price (the average realizations per barrel of oil equivalent being 6% lower in sterling terms).

Sales realizations in US dollar terms were lower year-on-year, averaging \$18.55 per boe compared to \$18.72 per boe in 1996, a decrease of 1%. Coupled with the weakening of the US dollar against sterling —

averaging 5% in 1997 — this resulted in the 6% decline in average sterling realizations to £11.31 per boe in 1997 from £11.98 per boe in 1996.

LASMO's average daily production of crude oil and natural gas in 1997 was 173 Mboepd, representing a decrease of 1% from 175 Mboepd in 1996. The decrease over 1996 levels was due primarily to the expected reduction in deliveries under the Package I sales contract in Indonesia in which LASMO had a high participating interest. The reduction in Indonesian production has, however, been largely offset by a full year contribution from the Liverpool Bay and Andrew fields and the start up of the MacCulloch field during 1997. In 1997 LASMO's average daily production comprised 51% oil (1996 45%) and 49% gas (1996 55%). See also "Item 1. Description of Business — Operational Statistics".

Operating Profit. Operating profit in 1997 of £184 million was 12% lower than 1996 levels of £208 million due to lower average production and sales realizations. Cost of sales — principally depletion and operating costs — was £452 million in 1997, compared with £467 million in 1996, and average cost of sales fell from £7.29 per boe in 1996 to £7.16 per boe in 1997. The focus on cost reduction brought benefits for the fourth year in succession; with unit operating costs falling 1% to £2.85 per boe from £2.87 per boe in 1996. See Note 3 of Notes to the Financial Statements.

A total of 36 exploration and appraisal wells (1996 — 23) were completed in the year and net exploration and appraisal expenditure totaled £95 million (1996 £75 million); with £54 million being written off (1996 £46 million). At the year end, capitalized exploration expenditure carried forward pending determination amounted to £57 million (1996 £35 million), with the majority concentrated in the UK (Mariner oil field and 49/3 gas field) and North Africa (Berkine Basin in Algeria).

Total administrative expenses of £32 million (1996 £28 million) included £9 million (1996 £7 million) of costs related to identifying new business opportunities. Excluding these costs, administrative expenses were £0.36 per boe, a rise of 9% on the 1996 level of £0.33 per boe. See Note 5 of Notes to the Financial Statements.

Profit before taxation. The profit before taxation in 1997 amounted to £154 million, with no exceptional items recorded (1996 £206 million, including exceptional income of £20 million).

Net interest payable amounted to £30 million compared to £20 million in 1996. This reflects the full year effect of reduced levels of interest income consequent upon the disposal of part of the investment in the AUK Loan Notes in 1996, and reduced income from treasury management activities partially offset by lower interest payable on bank loans. Interest capitalized in respect of fields under development totaled £15 million, higher than the 1996 level of £10 million due to the acquisition of the Dacion Area block in Venezuela and the high level of development activity in Algeria.

Taxation. LASMO's tax charge in 1997 was £106 million (1996 £139 million). The reduction arose primarily from lower tax charges in Indonesia on lower net revenues. No Advance Corporation Tax (ACT) was written off (1996 £4 million) as the Group is now paying UK corporation tax; and £6 million (1996 £nil) of ACT previously written off was written back. The payment of the proposed 1997 dividend as a Foreign Income Dividend will again ensure no irrecoverable ACT arises. See "Item 7. Taxation — Taxation of Dividends".

Profit for the year. After deducting preference dividends of £12 million (1996 £16 million) the profit attributable to ordinary shareholders was £36 million compared with £51 million in 1996.

(Loss)/profit for the year as adjusted to accord with US GAAP. The loss for the year as adjusted to accord with US GAAP was £2 million (1996 profit £70 million), compared with the profit for the year under UK GAAP of £48 million (1996 £67 million). The principal adjustments in the reconciliation of UK GAAP profit to US GAAP loss for the year are depletion and taxation. The depletion adjustment reduced the profit for the year by £34 million (1996 £82 million); the taxation adjustment reduced the profit for the year by £2 million (1996 increased profit by £96 million).

1996 Compared with 1995

Sales. Total sales were £749 million in 1996 compared with £637 million in 1995, an increase of 18%, attributable primarily to a 7% rise in average daily production, a firmer oil price with average realizations per barrel of oil equivalent being 10% higher in sterling terms and higher tariff income. Of total sales in 1996, £350 million related to UK production, £344 million related to Indonesia production and £55 million to International production. The reduction of International sales by £42 million from £97 million in 1995 is primarily attributable to the disposal of the offshore Nova Scotia fields.

Sales realizations for the full year averaged £11.98 per boe compared with £10.85 per boe in 1995. The net impact of the oil price hedging program was to reduce 1996 average sales realizations by £0.40 per boe, compared to 1995 where hedging improved realizations by £0.01 per boe. Sales realizations in US dollar terms were significantly higher in 1996, averaging \$18.72 per boe compared to \$17.09 per boe in 1995. Results in sterling terms reflected the improvement in US dollar revenues as well as the strengthening of the average US dollar rate against sterling in 1996.

LASMO's average daily production of crude oil and natural gas in 1996 was 175 Mboepd, representing an increase of 7% from 164 Mboepd in 1995. The increase over 1995 levels was mainly due to the commencement of production from the Liverpool Bay and Andrew fields and a full year contribution from the Birch field in the UK. Production from new fields, together with the first full year of production from the Birch and Kadanwari fields, more than offset the decline in production from existing fields and the disposal of producing interests in offshore Nova Scotia. In 1996, LASMO's average daily production comprised 45% oil (1995 48%) and 55% gas (1995 52%). See also "Item 1. Description of Business — Operational Statistics".

Operating profit. Operating profit after exceptional items was £208 million in 1996, significantly ahead of 1995 levels, increasing 86% from £112 million. This improvement resulted principally from higher operating profit for Indonesia and the UK operating region offset by a loss in the International region. Operating profit for Indonesia, which was £173 million in 1996 compared with £127 million in 1995, and for the UK region, which totaled £70 million in 1996 compared with a loss of £6 million in 1995 (after exceptional provisions of £17 million against the carrying value of assets and £5 million for reorganization costs), improved largely due to higher production levels and higher average realized prices in both regions. The operating loss in the International region of £21 million compared with a profit of £10 million in 1995 (after an exceptional provision release of £2 million in both years) mainly arose from the disposal of operations in Nova Scotia which was effective January 1, 1996.

Cost of sales before exceptional items was £467 million in 1996, compared with £437 million in 1995. The Group's average cost of sales before exceptional items in 1996, comprising principally depletion and operating costs, was £7.29 per boe compared with £7.30 per boe in 1995. The focus on cost reduction, including the sale of mature high cost assets continued to produce benefits in the year. Unit operating costs, which fell by 7% in 1995 to £3.17 per boe, were reduced further to £2.87 per boe in 1996, a fall of 10% over 1995 levels. See Note 3 of Notes to the Financial Statements. There was no provision against the carrying value of assets in 1996 (1995 £17 million). See Note 4 of Notes to the Financial Statements and "Item 1. Description of Business — Additional Factors Which May Affect Business — Financial Considerations — Ceiling Tests".

A total of 23 exploration and appraisal wells were completed in the year and net exploration and appraisal expenditure totaled £75 million (1995 £54 million) with £46 million being written off (1995 £34 million). At the year end, capitalized exploration expenditure carried forward pending determination amounted to £35 million (1995 £28 million). This low level of carry forward, despite higher levels of expenditure, reflects the continued success of the Group's significant programs in Algeria and Italy and progress in both these areas towards the first development phase.

Underlying administrative expenses in 1996 of £21 million were the same as in 1995. In addition, there were higher levels of expenditure associated with identifying new business opportunities which totaled £7 million in 1996 compared to £1 million in 1995. Administrative expenses (excluding new business research costs and, in 1995, provision for reorganization costs) fell to £0.33 per boe, 6% below 1995 levels (1995 £0.35 per boe). See Note 5 of Notes to the Financial Statements.

Profit before taxation. The profit before taxation in 1996 after exceptional items was £206 million, compared with £144 million in 1995.

Net finance charges amounted to £20 million for the year compared to net finance income of £1 million in 1995. This turnaround principally reflects reduced levels of interest income consequent upon the disposal of part of the investment in the AUK Loan Notes, lower levels of interest and similar income which, in 1995, were derived from gains arising on revaluation of investments and treasury management activities. Interest capitalized in respect of fields under development, which totaled £10 million in 1996, was less than half the level in 1995 of £22 million due to the completion of the Liverpool Bay, Birch and Andrew developments.

Profit on the disposal of fixed assets totaled £20 million (1995 £14 million). Oil and gas interests disposed of principally comprised the Group's interests offshore Nova Scotia which resulted in a gain of some £23 million.

Taxation. LASMO's tax charge in 1996 was £139 million, compared with £110 million in 1995. The increase arises primarily from higher tax charges in Indonesia on increased net revenues and provisions for UK deferred corporation tax. Advance Corporation Tax ("ACT") written off in 1996 was £4 million, the same as in 1995. The payment of the proposed 1996 dividend as a Foreign Income Dividend will again ensure no irrecoverable ACT arises. See "Item 7. Taxation — Taxation of Dividends".

Profit for the year. After deducting preference dividends of £16 million (1995 £19 million), the profit for the year attributable to ordinary shareholders was £51 million compared with £15 million in 1995.

Profit/(loss) for the year as adjusted to accord with US GAAP. The profit for the year as adjusted to accord with US GAAP was £70 million (1995 loss of £29 million) compared to the profit for the year under UK GAAP of £67 million (1995 £34 million). The principal adjustments in the reconciliation of UK GAAP to US GAAP profit for the year are depletion and taxation. The depletion adjustment reduced the profit for the year by £82 million compared with £123 million in 1995. The taxation adjustment increased the profit for the year by £92 million compared with £41 million in 1995.

Liquidity and Capital Resources

Cash flows. Net cash inflow from operating activities in 1997 was £464 million (1996 £454 million). Net cash outflows from returns on investments and servicing of finance increased to £64 million from £55 million. Taxation paid decreased to £97 million (1996 £122 million). Net cash outflow from investing activities and capital investment during 1997 totaled £538 million (1996 £28 million). This included £248 million (1996 £193 million) of cash outflows on exploration and appraisal and production and development; £272 million (1996 £nil) on acquisition of oil and gas assets; while 1996 benefited from £178 million proceeds on disposal of part of the AUK Loan Notes. £21 million was received in 1996 from business acquisitions net of disposals.

Capital expenditure. Capital expenditure on production and development activities was £184 million in 1997 (including £15 million of capitalized interest) compared with £153 million in 1996 (including capitalized interest of £10 million) and £247 million in 1995 (including capitalized interest of £22 million). Development expenditure was £108 million compared with £64 million in 1996, the increase due to increased activity in the North Sea, in Algeria and in Venezuela. Exploration and appraisal expenditure was £95 million compared with £75 million in 1996 and £54 million in 1995. The increase in expenditure in 1997 over 1996 levels reflected the increased activity in the most prospective areas, principally in the North Sea, Pakistan and Algeria.

At December 31, 1997 capital expenditure of £435 million had been authorized, of which £51 million had been contracted for. Most of this is expected to be spent over the next two years.

Although the actual amount of LASMO's future capital expenditures and investments in acquisitions will depend on various factors that cannot be predicted, including the success of its exploration program, LASMO believes that it has sufficient financing available to meet its current commitments for capital expenditure.

Financing. The Group's financing activities are primarily concentrated on raising funds in the capital markets rather than on maintaining committed, undrawn bank facilities. The Group generally arranges borrowings in advance of development expenditures.

LASMO had total borrowings of £1,184 million at December 31, 1997, £886 million at December 31, 1996 and £1,241 million at December 31, 1995. After deduction of cash and short-term investments (comprising cash and short-term deposits, securities (but not investments in the Company's own shares) and the AUK Loan Notes), the Group's net debt at December 31, 1997 was £613 million, giving a balance sheet gearing (defined as net debt as a percentage of shareholders equity) of 48% at that date (1996 £346 million and 27% respectively and 1995 £429 million and 39% respectively). At December 31, 1997 the average maturity of total borrowings due after more than one year was approximately 13.4 years (9.6 years at December 31, 1996). Borrowings due within one year amounted to £17 million at December 31, 1997 (1996 £13 million). At the same date LASMO had £300 million committed but undrawn bank facilities (1996 £236 million).

The Group has maintained significant balances of cash, short term bank deposits and liquid investments (£384 million at December 31, 1997 compared with £353 million at December 31, 1996) in order to assist it in financing its continuing operations. The Company also held as a fixed asset £187 million of AUK Loan Notes at December 31, 1997 (£187 million at December 31, 1996). The AUK Loan Notes were acquired in connection with the sale by LASMO in 1988 of its investment in Enterprise Oil plc and in August 1996 LASMO sold £181 million of the Notes for a consideration of £178 million in cash. The £187 million AUK Loan Notes which have been retained receive interest based on six month sterling rates and were used to secure the £150 million sterling debenture issued by LASMO plc in 1989.

LASMO from time to time examines acquisition possibilities. Funds for any such acquisitions would be drawn from the proceeds of future dispositions, internally generated cash, bank borrowings, or the issuance of debt or equity securities in an amount that cannot now be determined. Dispositions are also considered from time to time.

Other balance sheet movements. Other significant changes in the balance sheet between December 31, 1996 and December 31, 1997 are as follows:

Cash at bank at the end of 1997 was £375 million (1996 £353 million).

Provisions for liabilities and charges were reduced by £6 million to the end of 1996 reflecting movements in deferred PRT provisions (£14 million released) and decommissioning provisions (£8 million charged).

Financial Condition. The Company cannot predict with any degree of certainty the prices it will receive in future years for its oil and gas sales. LASMO's financial condition, operating results and liquidity will be materially affected by any significant fluctuations in oil prices.

Other

Year 2000. A Group-wide project is addressing the impact of the Year 2000 on computer systems and computer-controlled processes. The initial assessment phase of the project has been completed with systems and processes, worldwide, ranked according to the level of risk to the Group. Necessary conversion and replacement activities have begun and will continue through mid 1999. Testing of systems has begun and will continue throughout the process.

An internal engineering group, responsible to an executive director, is working with an oil industry task force and joint venture partners in the North Sea and internationally to complete this important project. Progress on the Year 2000 issue and associated projects is regularly reviewed by LASMO's Audit Committee.

While the work is ongoing, LASMO is unable to quantify the costs associated with any remedial action with any degree of certainty. However, based on the information currently available, there is no reason to believe that the total cost will have a material adverse effect on the consolidated financial position or results of operations of LASMO. LASMO is unable to assess the impact of the failure of third parties to fully comply with Year 2000 requirements.

European Monetary Union. LASMO is also evaluating the impact of European Monetary Union (EMU) on its business, but does not expect that EMU will have a material adverse impact on its financial position or results of operations.

ITEM 9A QUALITATIVE AND QUANTITATIVE DISCLOSURES ON MARKET RISKS

Qualitative information about market risk

LASMO's results are affected by several key factors, including crude oil prices, exchange rates and interest rates. Lower crude oil prices have a negative effect on the operating income and cash flow of LASMO.

A weakening US dollar against the pound sterling generally also has a negative effect on operating income and cash flow because LASMO reports in pounds sterling. A strengthening US dollar against the pound sterling generally has a positive effect on operating income, cash flow and dollar denominated assets, but with three quarters of LASMO's debt denominated in US dollars, also results in increased gearing.

Crude oil prices are subject to international supply and demand with consequent effect on LASMO's profitability. Political developments, especially in the Middle East, and the outcome of meetings of OPEC can particularly affect world supply and prices of oil. Such factors could also affect the price of LNG sold under long-term contracts as the LNG price is typically tied to crude oil prices. Crude oil prices are generally set in US dollars while costs may be incurred in a variety of currencies. Fluctuations in exchange rates can therefore give rise to foreign exchange exposures. LASMO is vulnerable to movements in the crude oil price and the US dollar/pound sterling exchange rate. Both are impossible to predict with any degree of certainty.

Financial Risk Management.

The Group may, from time to time, use non-leveraged derivative financial instruments ("derivatives") to manage its exposure to fluctuations in foreign currency exchange rates, interest rates, and some movements in crude oil prices. Most of the Group's borrowings are in US dollars or swapped into dollars where this achieves a lower cost of financing. The Group also manages the balance between floating rate and fixed rate debt. The Group does not become a party to derivatives for trading purposes; they are used exclusively for hedging purposes. See Note 22 of Notes to the Financial Statements.

Prior to 1994, LASMO accepted oil price risk. However, in 1994, LASMO commenced oil price hedging on a modest scale and from time to time hedges its oil and gas price realizations to avoid undue financial risk, within the overall objective of retaining shareholder exposure to oil and gas prices. LASMO's debt is denominated in pounds sterling (25%) and US Dollars (75%). The Group borrows in currencies other than pounds sterling in order to minimize currency losses arising from the translation of foreign currency assets into sterling. As at December 31, 1997, approximately 100% of total borrowings were at fixed rates of interest (1996 93% after taking account of interest rate swaps). No interest rate or currency swaps were outstanding at December 31, 1997.

At December 31, 1996, LASMO had oil swaps outstanding up to seven months forward in respect of 3,000,000 barrels of 1997 production and in 1997 entered into oil swaps in respect of a further 850,000 barrels of 1997 production up to ten months forward. In total these swaps represented 6% of production for the year (1996 19%). The effect of this program was to reduce the total average price realizations by 1 pence per boe (1996 reduction of 40 pence per boe, equivalent to some 3% of total realizations). At December 31, 1997, there were no oil swaps outstanding.

Quantitative information about market risk

Interest rate sensitivity

The table below provides information about the Group's derivatives and other financial instruments that are sensitive to changes in interest rates. Weighted average variable rates are based on the implied forward rates in the yield curve at the balance sheet date. The information is presented in sterling which is the Group's functional currency. The actual currencies of the instruments are indicated in parentheses.

	Expected to mature before December 31						Total	Fair value
	1998	1999	2000	2001	2002	Thereafter		
	(£ million, except percentages)							
Assets								
<i>Cash at bank and in hand:</i>								
Fixed rate (£)	375	—	—	—	—	—	375	375
Average interest rate	6.56%						6.56%	
<i>Unlisted securities:</i>								
Fixed rate (£)	7	—	—	1	—	—	8	8
Average interest rate	7.44%			7.00%			7.38%	
<i>Unlisted securities:</i>								
Floating rate (£)	—	—	—	—	1	—	1	1
Average interest rate					7.34%		7.34%	
<i>AUK Loan Notes:</i>								
Floating rate (£)	—	—	—	—	—	187	187	187
Average interest rate						7.54%	7.54%	
Liabilities								
<i>Total debt:</i>								
Fixed rate (£)	—	(59)	—	—	—	(229)	(288)	(330)
Average interest rate		9.50%				9.46%	9.36%	
Fixed rate (US\$)	(14)	(15)	(73)	(18)	(19)	(754)	(893)	(955)
Average interest rate	8.75%	8.75%	9.82%	8.75%	8.75%	7.41%	7.70%	

Exchange rate sensitivity

The following table provides information concerning the Group's derivatives and other financial instruments by currency presented in sterling equivalents. The table presented under "Interest rate sensitivity" provides details of non-sterling denominated monetary assets and liabilities which are subject to foreign currency exchange rate movement while the table below presents the amount and weighted average exchange rates of foreign currency forward exchange contracts held at December 31, 1997. All forward exchange contracts mature within one year.

Currency	Receive for £		Pay for £	
	Contract amount (£ million)	Average contractual exchange rate	Contract amount (£ million)	Average contractual exchange rate
US Dollars	63	1.64	98	1.64
Netherlands Guilder	—		18	3.28
	<u>63</u>		<u>116</u>	
Fair value	<u>63</u>		<u>116</u>	

ITEM 10. DIRECTORS AND OFFICER OF REGISTRANT

Certain information concerning the directors and officer of the Company is set forth below. Non-executive directors are not full-time employees of the Company.

<u>Name</u>	<u>Age</u>	<u>Position Held</u>
Directors		
R I J Agnew(3)	64	Chairman
A P Hichens(1,3,4)	61	Deputy Chairman
J Darby(3)	49	Chief Executive
T P Brennand(2,4)	63	Non-executive director
W G Cochrane(1,4)	62	Non-executive director
J A Hogan	45	Chief Operating Officer and executive director
T G King(2)	59	Non-executive director
P C Murray	36	Executive director Corporate Development
H E Norton(1,4)	61	Non-executive director
R G Reynolds(2,4)	58	Non-executive director
R L Smernoff	56	Finance Director
N V Turnbull(1,4)	56	Non-executive director
C A Wright	50	Executive director New Business
Executive Officer		
J A T Wedgwood	57	Group Secretary

- (1) Member of Audit Committee
- (2) Member of Health, Safety, Environment and Security Committee
- (3) Member of Nominations Committee
- (4) Member of Remuneration Committee

Chairman

Mr Agnew joined the Board in April 1994 and was appointed Chairman on April 29, 1994. With over 30 years' experience in the commodity business, he was formerly Chairman and Group Chief Executive of Consolidated Gold Fields PLC and a director of Hanson PLC. He is Chairman of Bona Shipbuilding, Bermuda, Star Mining Corporation NL, Australia and Stena International BV, The Netherlands. Other directorships include, Stena Line (UK) Limited and Newmont Mining Corp., USA.

Executive Directors

Mr Darby, formerly Chief Operating Officer, was appointed Chief Executive in January 1993. He has been a director since January 1990. He was previously Chairman and Chief Executive Officer of Thomson North Sea Limited which was acquired by LASMO in 1989. He is a graduate of the Royal School of Mines, Imperial College.

Mr Hogan was appointed Chief Operating Officer and executive director in February 1993. He joined LASMO in 1981 and was Vice President of the Company's United States operations prior to being appointed Managing Director of LASMO North Sea PLC in 1989. He is a graduate of King's College, University of London.

Mr Murray joined LASMO in 1989 following the acquisition of Thomson North Sea. He was appointed General Manager, Corporate Development in March 1996 and Corporate Development Director on January 1, 1998. He is a graduate of Durham University.

Mr Smernoff is Finance Director and joined the Board in March 1994. He has spent some seventeen years in senior finance positions in the oil and gas industry. Prior to joining LASMO, he was Chief Financial

Officer of Datascope Corp, having previously been Senior Vice President with Amerada Hess Corporation in the United States. He is a graduate of the City College of New York and a Certified Public Accountant.

Dr Wright joined the Board on July 21, 1997. Having previously worked for Burmah Oil, he spent 20 years in the UK and the US for British Petroleum (BP) in various senior positions, most recently as Chief Executive, Frontier and International. On leaving BP he joined Mobil Oil where he was President, New Business Development, Asia Pacific and Middle East. He is a graduate of Bristol University.

Non-executive Directors

Mr Hichens joined the Board in January 1995 and was appointed Deputy Chairman in April 1995. He is Chairman of Caradon plc and Deputy Chairman of Courtaulds Textiles plc and Candover Investments plc. Other directorships include London Insurance Market Investment Trust plc.

Dr Brennand joined the Board in May 1996. He spent some 33 years in Europe, Africa and the Far East for Shell, most recently as Chairman for Shell Hong Kong and China. On retiring from Shell in 1993, he spent three years as a director of Goal Petroleum.

Mr Cochrane has been a non-executive director since July 1989 having previously served as a non-executive director from 1975 to 1982. He was formerly Chairman of Dunedin Fund Managers Ltd. His current directorships include Newcastle Building Society, TR Property Investment Trust PLC and City Merchants High Yield Trust PLC. He is retiring from the Board at the conclusion of the Annual General Meeting to be held on April 28, 1998.

Mr King joined LASMO in 1987 as General Manager, Engineering and Operations, and was appointed Production Director in 1988, Exploration and Production Director in 1992 and Director, New Business in 1994, a post he held until stepping down as an executive director on April 29, 1997. He has spent over 37 years in the oil industry, in the United States, the United Kingdom, the Middle East and Africa. He was previously the President and Chief Executive Officer of Trafalgar House Oil and Gas in Houston. He is Chairman of METOC plc and Pipeline & Engineering Co Ltd. Mr King will retire from the Board at the conclusion of the Annual General Meeting on April 28, 1998.

Mr Norton joined the Board on July 1, 1997. He spent some 36 years with British Petroleum, where he held the position of Chief Executive, BP Exploration Company before being appointed to the BP Board as Managing Director. Other directorships include Inchcape plc and Standard Chartered PLC.

Dr Reynolds joined the Board on July 1, 1997. He spent 28 years with Shell and held senior positions in oil refining and LNG before being appointed Managing Director of Shell UK Oil in 1988, a position he held until the end of 1991. He is currently Chief Executive of the Commonwealth Development Corporation.

Mr Turnbull joined the Board in January 1995. He has been Finance Director of The Rank Group Plc since 1987.

The business address of each director is 101 Bishopsgate, London EC2M 3XH, England.

Executive Officer

Mr Wedgwood joined LASMO as Group Secretary in February 1992.

Term of Office of Directors and Officer

One-third of the directors, or if their number is not three or any multiple of three, then the number nearest to and less than one-third, shall retire by rotation at each Annual General Meeting and are eligible for reappointment. In addition, any director appointed since the latest Annual General Meeting shall retire at the next Annual General Meeting and is eligible for reappointment. At the Annual General Meeting held on April 29, 1997, Mr Agnew, Mr Smernoff, Dr Brennand and Mr Brading retired by rotation and Mr Agnew, Mr Smernoff and Dr Brennand were reappointed. Mr Brading did not seek re-appointment. At the Annual General Meeting to be held on April 28, 1998, Mr Norton, Dr Reynolds, who were appointed to the Board on

July 1, 1997 and Dr Wright, and Mr Murray, who were appointed to the Board on July 21, 1997 and January 1, 1998 respectively, retire from the Board, and being eligible, will offer themselves for reappointment. Mr Hichens, Mr Turnbull and Mr King retire by rotation and, being eligible, Mr Hichens and Mr Turnbull will offer themselves for reappointment. Mr King is not seeking reappointment and he, together with Mr Cochrane, will retire as non-executive directors at the conclusion of the Annual General Meeting.

All executive directors have service contracts with an unexpired period of two years entered into as part of a competitive package providing a reasonable degree of security and affording terms of employment which are considered appropriate to attract, motivate and retain executives of the quality required to manage the Company's international business. All service contracts include a liquidated damages clause whereby, in the event of early termination without cause, the executive director concerned would receive a payment of an amount less than the amount calculated by reference to the unexpired term of the contract.

Non-executive directors generally have written terms of engagement whereby they are appointed for an initial fixed period of approximately three years, renewable for similar periods by mutual agreement subject to the retirement by rotation requirements of the Company's Articles of Association. With the exception of the Chairman, non-executive directors are not entitled to receive any compensation if their appointment is terminated for any reason. In the event of early termination of the Chairman's terms of engagement, he is entitled to twelve months' fees or, if less, fees for the unexpired term of his engagement.

Mr Wedgwood has a service contract terminable by the Company by not less than two years' notice.

ITEM 11. COMPENSATION OF DIRECTORS AND OFFICERS

Remuneration Committee — Composition and Terms of Reference

The Committee is responsible, on behalf of the Board and the shareholders, for determining the Company's policy on remuneration and benefits for executive directors and for certain senior executives. It also determines the specific remuneration and terms and conditions of employment of the executive directors and certain other senior executives.

The Committee is chaired by Mr Hichens and includes Dr Brennand, Mr Cochrane, Mr Norton, Dr Reynolds and Mr Turnbull, all of whom are non-executive directors with no personal financial interests, other than as shareholders, in the matters they decide. It is advised by independent specialist consultants as appropriate.

Compliance

The text in this Item 11 has been extracted from a report prepared in accordance with the Listing Rules of the London Stock Exchange which implemented the recommendations of the Greenbury Committee on Directors' Remuneration and adopted the Greenbury Committee Code of Best Practice. The Company has complied throughout the year with Section A, and the Remuneration Committee has given full consideration to Section B, of the best practice provisions annexed to the Listing Rules.

Remuneration policy

Remuneration arrangements must facilitate the recruitment, motivation and retention of executives and staff with the necessary skills to run an international business. There are four key elements in the compensation of the executive directors and other senior executives: a basic salary, a performance related cash bonus scheme, long term incentives in the form of equity participation plans and a benefits package comprising pension benefits, vacation, medical and other insurances, and car benefits.

Base pay

Base pay ranges for senior executives are set by reference to jobs of comparable size in industrial and service companies of similar size and focus to LASMO. Individuals' pay is differentiated according to performance.

Annual bonus

An annual bonus scheme rewards the achievement of challenging targets related to the short term performance of the business and personal objectives. Targets are set through the annual performance appraisal process and include achievement of quantifiable performance elements such as profit and/or cash goals. A maximum bonus of 30% of base pay may be paid where exceptional performance is achieved. Annual bonus payments are not pensionable.

Equity participation plans — See “Item 12. Options to Purchase Securities from Registrant or Subsidiaries”.

Pension arrangements

The Group runs a number of pension schemes, the principal one being the LASMO Pension Plan (the Plan) which operates in the United Kingdom. The Plan, which is funded, provides defined benefits based on basic salary for approximately 380 employees in the Group. It is a non-contributory scheme and is governed by an independent trust. The contribution which the Company made to the Plan in the year under review was 16.5% of salary. The Plan enables members to achieve the maximum pension permitted by the Inland Revenue of two-thirds of their final salary after 36 years’ service at normal retirement age of 60. It also provides for early retirement in certain circumstances, payment of a lump sum in the event of death in service and a dependent’s pension.

All UK employees, including executive directors, are eligible to participate in the Plan on the same basis. Of the executive directors on the Board at the end of 1997, Mr Darby and Mr Hogan were members of the Plan. Mr Smernoff, a US citizen, is employed by LASMO America Limited (LAL), a subsidiary of LASMO. LAL contributed 15% of Mr Smernoff’s salary to a Retirement Benefit Program for his benefit. LASMO contributed 9% of Dr Wright’s salary to a personal pension plan for his benefit. Non-executive directors are not eligible to join the Plan.

Details of the executive directors’ pension entitlements for 1997 were as follows:

<u>Defined benefit arrangements</u>	<u>Age at December 31, 1997</u>	<u>Years of pensionable service at December 31, 1997</u>	<u>Increase in accrued pension in 1997(a)</u>	<u>Accrued pension at December 31, 1997(b)</u>	<u>Transfer value of the increase in accrued 1997(c)</u>
			<u>£000 pa</u>	<u>£000 pa</u>	<u>£000</u>
J Darby	49	9	9	52	112
J A Hogan	44	17	10	73	108
	<u>Age at December 31, 1997</u>				<u>Contributions in respect of 1997</u>
<u>Defined contribution arrangements</u>					<u>£000</u>
R L Smernoff	56				34
C A Wright	50				9

- (a) The increase in accrued pension during the year excludes any increase due to inflation.
- (b) The accrued pension entitlement is that which would be paid annually to the executive director concerned at normal retirement age and is based on service to the end of 1997.
- (c) The transfer value has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11 issued by the Institute and Faculty of Actuaries.
- (d) The aggregate amount paid by LASMO during the year in respect of pension contributions for the executive directors and the executive officer was £162,626.
- (e) On his retirement as an executive director on April 29, 1997, Mr King was entitled to an accrued pension of £39,931 pa which included £3,959 pa accrued since December 31, 1996, before reduction for early retirement. This was increased to £44,444 pa and the value of the augmentation and additional accrual together amounted to £139,000.

Remuneration of Directors

The aggregate compensation paid by the Group to the Chairman, the directors and the executive officer as a group for services in all capacities for the year ended December 31, 1997 was £1,723,000.

The remuneration of the Chairman and the directors (excluding pension contributions) for the year ended December 31, 1997 were as follows:

	1997						1996	
	Salary £000	Increase in salary over 1996	Bonus (a) £000	Benefits (b)	Directors' fees £000	Other fees £000	Total £000	Total £000
<i>Chairman</i>								
R I J Agnew					20	130	150	150
<i>Executive</i>								
J Darby	322	12.2	66	18	—	—	406	347
J A Hogan	231	12.0	45	10	—	—	286	250
R L Smernoff	225	6.4	46	27	—	—	298	270
C A Wright	123	—	24	—	—	—	147	—
<i>Non-executive</i>								
J E Brading					7	3	10	26
T P Brennand					20	6	26	15
W G Cochrane					20	11	31	29
A P Hichens					20	28	48	45
<i>(Deputy Chairman)</i>								
T G King (c)	87			14	13	2	116	240
H E Norton					10	2	12	—
R G Reynolds					10	2	12	—
N V Turnbull					20	8	28	26
Total	<u>988</u>		<u>181</u>	<u>69</u>	<u>140</u>	<u>192</u>	<u>1,570</u>	<u>1,398</u>

(a) The discretionary bonuses shown were paid to the executive directors on March 26, 1998 in recognition of their performance in 1997 (1996 £122,000).

(b) Benefits provided include personal accident and medical insurance, and car benefits.

(c) Mr King retired as an executive director on April 29, 1997, remaining on the Board as a non-executive director. He received £237,000 by way of compensation for change of status and consultancy fees of £12,500 for the period from May 15, 1997 to December 31, 1997 under the terms of an agreement which expires on May 31, 1998. In addition, Mr King's pension benefits were augmented as set out on page 53.

The four executive directors and Mr King (1996 four) waived fees totaling £76,000 (1996 £77,000). The fees paid to non-executive directors take into account the time devoted to Committees of the Board and are recommended to the Board by the Chairman, after reviewing fee payments made to non-executive directors in organizations of similar size. The Board determines the Chairman's fees on the recommendation of the Remuneration Committee.

Mr Darby and Mr Hogan were each allocated shares to the value of £8,000 (1996 Mr Darby £8,000, Mr Hogan £7,685) under the terms of the LASMO Profit Sharing Scheme.

ITEM 12. OPTIONS TO PURCHASE SECURITIES FROM REGISTRANT OR SUBSIDIARIES

Equity participation plans

The Company encourages share ownership by executive directors and other senior executives as it aligns their personal interests and those of shareholders. The Company has in place the following equity participation plans for which the executive directors and other senior executives are eligible:

Executive Share Option Schemes

Options over ordinary shares in the Company may be granted under the LASMO 1984 Executive Share Option Scheme (the 1984 Scheme) and the LASMO International Executive Share Option Scheme (the International Scheme), normally exercisable between three and ten years after grant. The 1984 Scheme is an Inland Revenue approved scheme. The International Scheme is unapproved, with UK and overseas executives eligible to participate. Options may be granted at not less than the market value of an ordinary share in the Company on the date of grant. The aggregate price payable by a participant on the exercise of all options under the 1984 Scheme, the International Scheme and the closed LASMO Executive Share Option Scheme established in 1980 (the 1980 Scheme), in any ten year period, may not exceed four times such participant's annual earnings. The Company's policy is that, whilst higher awards may be given to reward exceptional individual performance, the grant of options to an individual at any one time should not normally exceed an amount equivalent to 40% of that individual's annual earnings.

The exercise of options granted under the 1984 Scheme and the International Scheme since April 1995 is subject to the achievement of total shareholder return (TSR — change in share price plus re-invested dividends) relative to a comparator group (the Comparator Group) of ten international oil and gas exploration and production companies. The performance target enabling options to be exercised is on a sliding scale whereby 33.33% is exercisable only if the Company's performance places it in the third quartile and 100% is exercisable only if the Company's performance places it in the top quartile of the Comparator Group over a rolling three year period.

No options have been or will be granted under the Executive Share Option Schemes to executives who are eligible to participate in the LASMO Equity Plan.

At April 16, 1998 the number of ordinary shares under option outstanding under the Executive Share Option Schemes was 6,816,975 with exercise prices ranging from 126.25p to 456.03p, exercisable over the period 1998-2008.

Equity Plan

The Trustee of the LASMO Equity Plan may notionally allocate ordinary shares in the Company annually to executive directors and other senior executives based on a percentage of salary and calculated by reference to share price. Participants may choose to commit to the Plan up to the same number of LASMO shares which will be matched by a further notional allocation of shares by the Trustee.

Subject to the achievement of two performance targets, the actual number of shares (if any) to be given to each participant in respect of any Equity Plan year will be determined after the end of the third year performance period or, if the targets have not been met by then, after the fourth or fifth year. The performance targets operate as follows: first, the number of shares notionally allocated to a participant will be adjusted so that, on a sliding scale, 100 % is carried forward if there is an increase in the LASMO share price of 2.5% per annum over the Retail Price Index over the award period, with a further 100% for each additional 5% per annum real increase. Secondly, the actual number of shares to be ultimately available will be determined by comparing the TSR to LASMO ordinary shareholders against the Comparator Group. In respect of notional allocations made in the years 1995 to 1997, if LASMO's TSR is bottom, none of the shares notionally allocated will be confirmed. If LASMO's TSR ranks number 10, shares equal to 20% of the adjusted notional allocation will be confirmed, increasing by incremental amounts of 20% up to a maximum of 200% if the LASMO TSR is in first place. For notional allocations made in 1998 and subsequent years, no shares will be confirmed if LASMO's TSR ranks number 9 or lower against the Comparator Group. If LASMO's TSR ranks number 8, shares equal to 60% of the adjusted notional allocation will be confirmed, increasing by incremental amounts of 20% up to a maximum of 200% if the LASMO TSR is in first place. In general, commencing with the 1998 notional allocations, confirmed shares to any one individual will not exceed five times the notional allocation to that individual in respect of any particular year. Awards over confirmed shares are normally exercisable by the participant between five and seven years from the date of notional allocation. The shares will be provided from existing ordinary shares in issue acquired by the Trustee. A charge of

£4,165,000 (1996 £2,208,000) has been included in the financial statements in respect of the cost of the Equity Plan for the year ended December 31, 1997.

The Comparator Group of companies currently used in the Executive Share Option Schemes and the Equity Plan comprises:

Anadarko Petroleum Corporation	Oryx Energy Limited
Apache Corporation	Ranger Oil Limited
British-Borneo Petroleum Syndicate, PLC	Saga Petroleum AS
Enterprise Oil plc	Talisman Energy Inc
Monument Oil and Gas plc	Union Texas Petroleum Holdings Inc

SAYE Share Option Scheme

All employees, including executive directors, are invited to save up to £250 a month for three or five years to acquire ordinary shares in LASMO under the Company's SAYE Share Option Scheme at not less than 80% of the middle market price of an ordinary share in the Company on the business day preceding the invitation date.

At April 16, 1998, the number of ordinary shares under option outstanding under the SAYE scheme was 2,698,151 with an exercise price range of 100.00p to 300.5p exercisable over the period 1998 to 2005.

Profit Sharing Scheme

All UK resident employees of the Company, including executive directors, participate in the LASMO Profit Sharing Scheme under which the Trustee of the Scheme may acquire ordinary shares of the Company for the benefit of participants. The maximum amount which may be made available in any year may not exceed 5% of the Group's pre-tax profits. The current permitted value of the shares that may be given to any participant in any year is the lower of £8,000 or 10% of salary and the shares will be held in trust for at least two years. An accrual for the estimated cost of profit sharing totaling £635,000 (1996 £604,000) has been included in the financial statements for the year ended December 31, 1997.

Other Plans

The Group has other stock options plans in which former employees of the Ultramar Group participate. At April 16, 1998 the total number of LASMO ordinary shares under option in these plans was 293,463 with an exercise price range of 249.6p to 280.5p, exercisable over the period 1998-2001.

The Company also has a stock appreciation rights ("SAR") plan under which SARs have been granted to US residents who previously held options under the Ultramar stock option plans. On valid exercise of a SAR, LASMO pays to the option holder the difference between the calculated exercise price of equivalent LASMO ordinary shares underlying the SAR and the market value of LASMO ordinary shares on the date of exercise, either in cash or LASMO ordinary shares at the option of the Company. At April 16, 1998 there were 3,600 SARs outstanding. In addition, there are options over 48,000 Ultramar shares which remain outstanding.

Options held by the Executive Directors and the Executive Officer

The interests of the executive directors and the executive officer in options over ordinary shares of the Company under the Company's Executive Share Option Schemes and SAYE Share Option Scheme at the dates stated were as follows:

<u>Executive Director</u>	<u>Number of options at December 31, 1997</u>	<u>Number of options at January 1, 1997</u>	<u>Exercise price per share</u>	<u>Normal exercise dates</u>	
				<u>From</u>	<u>To</u>
J Darby	78,120	78,120	339.22p	09.25.1992	09.25.1999
	40,622	40,622	385.94p	03.12.1993	03.12.2000
	49,996	49,996	375.38p	03.11.1994	03.11.2001
	26,040	26,040	238.09p	01.28.1995	01.28.2002
	52,079	52,079	154.57p	04.02.1996	04.02.2003
	108,870	108,870	147.00p	04.25.1997	04.25.2004
	53,000	53,000	166.00p	05.24.1998	05.24.2005
	SAYE 13,582	13,582	127.00p	10.26.1999	04.26.2000
	<u>422,309</u>	<u>422,309</u>			
J A Hogan	15,624	15,624	275.85p	04.14.1992	04.14.1999
	29,685	29,685	385.94p	03.12.1993	03.12.2000
	22,915	22,915	375.38p	03.11.1994	03.11.2001
	31,248	31,248	182.41p	04.06.1995	04.06.2002
	41,663	41,663	154.57p	04.02.1996	04.02.2003
	61,530	61,530	147.00p	04.25.1997	04.25.2004
	45,000	45,000	166.00p	05.24.1998	05.24.2005
	SAYE 13,582	13,582	127.00p	10.26.1999	04.26.2000
	<u>261,247</u>	<u>261,247</u>			
R L Smernoff	100,000	100,000	147.00p	04.25.1997	04.25.2004
	75,000	75,000	166.00p	05.24.1998	05.24.2005
		<u>175,000</u>			
<u>Executive Officer</u>					
J A T Wedgwood	52,080	52,080	126.25p	08.10.1995	10.08.2002
	26,039	26,039	154.57p	04.02.1996	04.02.2003
	75,000	75,000	147.00p	04.25.1997	04.25.2004
	25,000	25,000	166.00p	05.24.1998	05.24.2005
	SAYE 13,582	13,582	127.00p	10.26.1999	04.26.2000
	<u>191,701</u>	<u>191,701</u>			

Following his retirement as an executive director on April 29, 1997, Mr King exercised options over 120,047 ordinary shares as set out below and SAYE options over 7,606 ordinary shares held by him were cancelled during the year. As at December 31, 1997, Mr King retained options over 117,179 ordinary shares of the Company (January 1, 1997 244,832) issued at a weighted average price of 352.08p exercisable at any time up to April 29, 1998.

	<u>Date of exercise</u>	<u>Number of shares</u>	<u>Exercise price per share</u>	<u>Mid-market price</u>	<u>Gain £</u>
T G King	09.29.1997	48,818	212.01p	271.0p	28,798
	09.29.1997	64,579	238.09p	271.0p	21,250
	10.02.1997	6,650	121.00p	270.0p	9,908
		<u>120,047</u>			<u>59,956</u>

The gain is calculated on the difference between the exercise price and the mid-market price on the date of exercise.

Save as stated, no options were granted to or exercised by any director during the year, and no options lapsed.

The mid-market price of the Company's ordinary shares on the first and last dealing days of 1997 taken from the London Stock Exchange Daily Official List was 230.5p and 273.5p respectively and on April 16, 1998 was 257.75p. The market price ranged between 218.5p and 287.5p during 1997.

At the date of his appointment to the Board, January 1, 1998, Mr Murray had the following interests in options over ordinary shares under the Company's Executive Share Option Scheme and SAYE Share Option Scheme:

	<u>Number</u>	<u>Exercise price per share</u>	<u>Normal exercise dates</u>	
			<u>From</u>	<u>To</u>
P C Murray	20,832	182.41p	04.06.1995	04.06.2002
	31,247	154.57p	04.02.1996	04.02.2003
	50,000	147.00p	04.25.1997	04.25.2004
	20,000	166.00p	05.24.1998	05.24.2005
SAYE	<u>17,250</u>	100.00p	05.25.1999	11.25.1999
	<u>139,329</u>			

There has been no further change in the interests shown above between December 31, 1997 and April 16, 1998.

Executive Directors' and the Executive Officer's interest in Shares under the Equity Plan

The number of ordinary shares of the Company notionally allocated to executive directors and the executive Officer or confirmed under the Company's Equity Plan (the "Plan"), for the Plan years stated, were as follows:

	<u>Notional allocation</u>		<u>Confirmed shares</u>
	<u>1997</u>	<u>1996</u>	<u>1995</u>
<u>Executive Directors</u>			
J Darby	27,250	31,966	213,000
J A Hogan	19,654	22,376	166,142
R L Smernoff	18,828	22,908	170,405
C A Wright	14,796	—	—
<u>Executive Officer</u>			
J A T Wedgwood	10,074	12,254	89,452

On retiring as an executive director, Mr King exercised his rights on May 16, 1997 to receive 200,696 confirmed shares. Based upon the mid-market price of LASMO ordinary shares on the date of exercise of 240p, the value of the shares received was £481,670.

Mr Murray has notional allocations under the Plan of 11,720 and 12,386 ordinary shares for the years 1996 and 1997 respectively, and 80,939 confirmed shares in respect of 1995.

There has been no change in the interests shown above between December 31, 1997 and April 16, 1998.

ITEM 13. INTEREST OF MANAGEMENT IN CERTAIN TRANSACTIONS

There have been no material transactions with the Company or any of its subsidiaries during the last three years in which any executive director or the executive officer, or any relative or spouse thereof had an interest and no such transactions are presently proposed. There is no significant outstanding indebtedness to the Company by any executive director or the executive officer or 10% shareholder.

PART II

ITEM 14. DESCRIPTION OF SECURITIES TO BE REGISTERED

Not applicable.

PART III

ITEM 15. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 16. CHANGES IN SECURITIES AND CHANGES IN SECURITY FOR REGISTERED SECURITIES AND USE OF PROCEEDS

None.

PART IV

ITEM 17. FINANCIAL STATEMENTS

Not applicable.

ITEM 18. FINANCIAL STATEMENTS

See pages F-1 through F-52 incorporated herein by reference.

ITEM 19. FINANCIAL STATEMENTS AND EXHIBITS

(a) The following financial statements, together with the reports of Ernst & Young thereon, are filed as part of this Annual Report:

	<u>Page</u>
Report of Independent Auditors	F-1
Consent of Independent Auditors	F-1
Audited Financial Statements	
Consolidated Statement of Income for the years ended December 31, 1997, 1996 and 1995	F-2
Consolidated Balance Sheet as at December 31, 1997 and 1996	F-3
Consolidated Statement of Movements in Shareholders' Equity for the years ended December 31, 1997, 1996 and 1995	F-4
Consolidated Statement of Cash Flows for the years ended December 31, 1997, 1996 and 1995	F-6
Consolidated Statement of Total Recognized Gains and Losses for the years ended December 31, 1997, 1996 and 1995	F-7
Notes to the Financial Statements	F-8
Supplementary Disclosures relating to Crude Oil and Natural Gas Producing Activities (Unaudited)	F-46

Financial Statement Schedules

The schedules are omitted either because they are not required or the required information is given in the financial statements.

(b) The following documents are filed as exhibits to this Annual Report:

**Exhibit
Number**

2.1 Consent of DeGolyer and MacNaughton.

Except for the £300,000,000 Reducing Revolving Credit Facility Agreement between LASMO (ULX) Limited as Borrower, LASMO plc as Guarantor, Chemical Bank as Arranger, Nat West Capital Markets Limited as Co-Arranger, the Banks and Lending Institutions named therein as Lenders and National Westminster Bank plc as Agent, dated November 20, 1995 and the Indenture, dated as of June 1, 1993, among LASMO (USA) Inc. as Issuer, LASMO plc as Guarantor and The Bank of New York as Trustee (filed as Exhibit 4.1 to the Company's Registration Statement on Form F-3 (Commission File No. 333-4832) and incorporated herein by reference), the total amount of long-term debt securities of the Registrant and its subsidiaries authorized under any one instrument does not exceed 10% of the total assets of LASMO and its subsidiaries on a consolidated basis. LASMO agrees to furnish copies of any or all such instruments to the Securities and Exchange Commission upon request.

SIGNATURES

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the Registrant, LASMO plc, certifies that it meets all of the requirements for filing on Form 20-F and has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

LASMO plc

By: /s/ R. L. SMERNOFF

Name: R. L. Smernoff

Title: Director

Date: April 22, 1998

LASMO plc AND SUBSIDIARY COMPANIES

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors
LASMO plc

We have audited the accompanying consolidated balance sheets of LASMO plc as of December 31, 1997 and 1996, and the related consolidated statements of income, movements in shareholders' equity, total recognized gains and losses and cash flows for each of the three years in the period ended December 31, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with United Kingdom auditing standards which do not differ in any significant respect from United States generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurances 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 the management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of LASMO plc at December 31, 1997 and 1996, and the consolidated results of its operations and its consolidated cash flows for each of the three years in the period ended December 31, 1997 in conformity with accounting principles generally accepted in the United Kingdom which differ in certain respects from those followed in the United States (see Note 29 of Notes to the Financial Statements).

London, England
February 26, 1998

ERNST & YOUNG
Chartered Accountants

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in the Registration Statement (Form S-8 No. 333-07150) pertaining to the Employee Thrift and Retirement Plan of Virginia Indonesia Company of the reference to our firm in "Item 8. Selected Consolidated Financial Data" and of our report dated February 26, 1998, with respect to the consolidated financial statements of LASMO plc all included in the Annual Report (Form 20-F) for the year ended December 31, 1997.

London, England
April 22, 1998

ERNST & YOUNG
Chartered Accountants

LASMO plc AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF INCOME

	<u>Notes</u>	<u>Year ended December 31</u>		
		<u>1997</u>	<u>1996</u>	<u>1995</u>
				(£ million, except per ordinary share amounts)
Sales	2	722	749	637
Cost of sales	3	<u>(452)</u>	<u>(467)</u>	<u>(454)</u>
Gross profit		270	282	183
Exploration costs written off	4	(54)	(46)	(34)
Administrative expenses	4,5	<u>(32)</u>	<u>(28)</u>	<u>(37)</u>
Operating profit	5	184	208	112
Profit on disposal of fixed assets	4	—	20	14
Downstream (provision)/release	4	—	(2)	17
Interest receivable and similar income	7	41	64	80
Interest payable and similar charges	8	<u>(71)</u>	<u>(84)</u>	<u>(79)</u>
Profit before taxation	2	154	206	144
Taxation on profit on ordinary activities	9	(112)	(135)	(106)
Advance corporation tax written back/(written off)	9	<u>6</u>	<u>(4)</u>	<u>(4)</u>
Profit for the year*		48	67	34
Preference dividends	10	<u>(12)</u>	<u>(16)</u>	<u>(19)</u>
Profit for the year attributable to ordinary shareholders		36	51	15
Ordinary dividends	10	<u>(22)</u>	<u>(19)</u>	<u>(12)</u>
Retained profit for the financial year		<u>14</u>	<u>32</u>	<u>3</u>
Earnings per ordinary share before exceptional items		3.7p	3.2p	1.5p
Exceptional items		<u>—</u>	<u>2.1p</u>	<u>0.1p</u>
Earnings per ordinary share	11	<u>3.7p</u>	<u>5.3p</u>	<u>1.6p</u>
Average number of ordinary shares outstanding during the year (in millions)		<u>966.0</u>	<u>965.9</u>	<u>965.5</u>

* A summary of the adjustments to the profit for the year that would be required had United States generally accepted accounting principles been applied instead of those generally accepted in the United Kingdom is set forth in Note 29 of Notes to the Financial Statements.

The Notes to the Financial Statements are an integral part of these Financial Statements

LASMO plc AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEET

	<u>Notes</u>	December 31	
		1997	1996
		(£ million)	
ASSETS			
Current assets			
Cash at bank and in hand		375	353
Unlisted investments		9	—
Petroleum revenue tax and corporation taxation recoverable	12	32	31
Accounts receivable	13	207	197
Inventories		16	14
Total current assets		639	595
Fixed assets	14		
Intangible assets		57	35
Tangible assets		1,974	1,678
Investments		216	220
Total fixed assets		2,247	1,933
Total assets		2,886	2,528
 LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Trade payables		41	53
Accruals and other payables	15	269	203
Bank loans and overdrafts	15	17	13
Total current liabilities		327	269
Noncurrent liabilities			
Bank loans	16	69	145
Loan capital	16	1,098	728
Deferred income and other accounts payable	16	27	31
Total noncurrent liabilities		1,194	904
Provisions for liabilities and charges	18	89	95
Total liabilities		1,610	1,268
Shareholders' equity *			
Share capital		393	388
Share premium		557	558
Other reserves		90	90
Retained earnings		236	224
Total shareholders' equity		1,276	1,260
Total liabilities and shareholders' equity		2,886	2,528

* A summary of the adjustments to shareholders' equity that would be required had United States generally accepted accounting principles been applied instead of those generally accepted in the United Kingdom is set forth in Note 29 of Notes to the Financial Statements.

The Notes to the Financial Statements are an integral part of these Financial Statements

LASMO plc AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF MOVEMENTS IN SHAREHOLDERS' EQUITY

	Share capital				
	Number of preference shares*	Preference Shares of \$25 each*	Number of ordinary shares	Ordinary shares of 25p each	Total
	(000's)	(£ million)	(000's)	(£ million)	(£ million)
Authorized					
At January 1, 1995	10,000	160	1,320,000	330	490
Exchange adjustment	—	1	—	—	1
At December 31, 1995	10,000	161	1,320,000	330	491
Exchange adjustment	—	(15)	—	—	(15)
At December 31, 1996	10,000	146	1,320,000	330	476
Exchange adjustment	—	5	—	—	5
At December 31, 1997	<u>10,000</u>	<u>151</u>	<u>1,320,000</u>	<u>330</u>	<u>481</u>
Issued					
At January 1, 1995	10,000	160	965,413	242	402
Share option and profit sharing schemes	—	—	242	—	—
Exchange adjustment	—	1	—	—	1
At December 31, 1995	10,000	161	965,655	242	403
Share option and profit sharing schemes	—	—	311	—	—
Exchange adjustment	—	(15)	—	—	(15)
At December 31, 1996	10,000	146	965,966	242	388
Exchange adjustment	—	5	—	—	5
At December 31, 1997	<u>10,000</u>	<u>151</u>	<u>965,966</u>	<u>242</u>	<u>393</u>

* The Dollar Preference Shares are redeemable in whole or in part at the option of the Company at par plus accrued dividends on or after June 16, 1998. A special dividend of \$1.25 per share is payable for redemptions prior to June 16, 1999 and thereafter of amounts declining to zero for redemptions on or after June 16, 2003.

The Dollar Preference Shares carry no votes at general meetings of the Company unless a resolution is proposed to reduce the Dollar Preference Share capital or to vary or abrogate any of the rights attaching to the Dollar Preference Shares or to wind up or liquidate the Company or where the two most recent quarterly dividends payable on the Dollar Preference Shares have not been paid in full, in which event each holder of the Dollar Preference Shares shall have one vote on a show of hands and on a poll each such holder will be entitled to ten votes for each \$25 in nominal amount of Dollar Preference Shares held. The Dollar Preference Shares have a right, in preference to the ordinary shares, to receive on a winding up the amount of \$25 per share plus accrued dividend.

The Notes to the Financial Statements are an integral part of these Financial Statements

LASMO plc AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF MOVEMENTS IN SHAREHOLDERS' EQUITY — (Continued)

	Share capital	Share premium(i)	Other reserves(i)			Retained earnings	Total
			Merger reserve	Capital reserve (£ million)	Capital redemption reserve		
At January 1, 1995 (ii) (iii)	402	559	28	2	—	244	1,235
Issue expenses	—	(1)	—	—	—	1	—
Amount transferred to retained earnings	—	—	—	—	—	3	3
Exchange adjustments	<u>1</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>1</u>	<u>2</u>
At December 31, 1995 (ii) (iii)	403	558	28	2	—	249	1,240
Transfer to capital redemption reserve	—	—	—	—	60	(60)	—
Amount transferred to retained earnings	—	—	—	—	—	32	32
Exchange adjustments	<u>(15)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>3</u>	<u>(12)</u>
At December 31, 1996 (ii) (iii)	388	558	28	2	60	224	1,260
Issue expenses	—	(1)	—	—	—	1	—
Amount transferred to retained earnings	—	—	—	—	—	14	14
Exchange adjustments	<u>5</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>(3)</u>	<u>2</u>
At December 31, 1997 (ii) (iii)	<u>393</u>	<u>557</u>	<u>28</u>	<u>2</u>	<u>60</u>	<u>236</u>	<u>1,276</u>

(i) In accordance with section 131 of the Companies Act 1985, as amended, of Great Britain, the premium arising on the issue of shares in connection with the acquisition of Ultramar PLC was credited to a non-distributable merger reserve. In July 1996 £60 million was transferred from retained earnings to the capital redemption reserve on the redemption of the Sterling Preference Shares. The share premium, merger reserve, capital reserve and capital redemption reserve are not distributable.

(ii) Net exchange losses of £1 million on foreign currency loans (1996 gains £17 million; 1995 gains £8 million) have been offset against exchange losses arising on the net investment in overseas subsidiaries. Cumulative exchange gains included in retained earnings at December 31, 1997 amounted to £25 million (1996 £28 million; 1995 £25 million).

(iii) Cumulative goodwill set off against retained earnings and other reserves at December 31, 1997 is £30 million (1996 £30 million; 1995 £30 million).

The Notes to the Financial Statements are an integral part of these Financial Statements

LASMO plc AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF TOTAL RECOGNIZED GAINS AND LOSSES

	Year ended December 31		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
		(£ million)	
Profit for the year.....	48	67	34
Currency translation gains/(losses) on foreign currency net investments.....	<u>2</u>	<u>(12)</u>	<u>2</u>
Total recognized gains and losses relating to the year.....	<u><u>50</u></u>	<u><u>55</u></u>	<u><u>36</u></u>

The Notes to the Financial Statements are an integral part of these Financial Statements

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS

Note 1 — Accounting policies

Basis of preparation

Principal accounting policies are set out below. These policies are consistent with those adopted in previous years.

The financial statements have been prepared under the historical cost convention, using the “successful efforts” method of accounting, and in accordance with applicable accounting standards as defined by the Companies Act 1985, as amended, of Great Britain (the “Companies Act”).

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Basis of consolidation

The consolidated financial statements include the financial statements of LASMO plc and all its subsidiary undertakings for the year ended December 31, 1997. All these undertakings are companies, and hereafter are identified as such, except for a 50% interest in a general partnership (Unimar Company) which is consolidated on a proportionate basis.

The Group conducts substantially all of its oil and gas exploration and development activity through unincorporated joint ventures. The share of these joint ventures’ results and net assets attributable to LASMO are reflected in the Group’s consolidated financial statements except where LASMO acts as operator on behalf of a consortium of partners, in which case, amounts due to/from third parties are reported gross as are amounts due to/from the non-operating partners.

Subsidiaries acquired or sold during the year are included from the effective date of acquisition or to the effective date of disposal.

Goodwill

Goodwill, which comprises the amounts by which the cost of acquiring shares in subsidiaries exceeds the fair value of net assets acquired, is written off to retained earnings and other reserves in the year of the acquisition.

Sales

Sales comprise amounts receivable for invoiced sales, exclusive of value added taxation and similar levies. The Group’s entitlement to proceeds from Indonesian LNG sales is included in sales after adjustment to add back the Group’s share of transportation and liquefaction costs and debt service which is deducted on an incurred basis on loans raised by the owner to finance the construction and expansion costs of the Bontang LNG plant which is operated on a break even basis. Cost of sales is also adjusted to reflect these deductions, except that only equal annual charges for debt service are deducted so as to spread the financing costs over the remaining lives of the respective sales contracts rather than the uneven repayment schedules established for the loans. The resultant deferred debt service charges are included in accounts receivable.

Petroleum Revenue Tax (“PRT”)

PRT is treated as a production cost and has been charged or credited before arriving at operating profit. Provision is made for current PRT on revenue from petroleum sales less all allowable deductions for the period.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 1 — Accounting policies — (continued)

Deferred taxation

Deferred taxation is provided in respect of liabilities relating to timing differences between profits as computed for taxation purposes and profits as stated in the financial statements, except to the extent that the liability is not expected to crystallize in the foreseeable future. The provision arises principally from the different accounting and tax treatments for amortizing oil and gas expenditure. No provision is made for the taxation which would arise if the retained earnings of certain overseas subsidiaries were distributed as dividends.

Foreign currencies

Transactions in foreign currencies are recorded at exchange rates ruling at the date of each transaction or a contract rate where applicable.

Assets and liabilities of overseas subsidiary and associated companies and of UK companies with non-sterling functional currencies are translated into sterling at rates current at the balance sheet date. Trading results and cash flows of such companies are translated into sterling at average rates. Unrealized gains or losses on revaluation of net assets of overseas subsidiary and associated companies and on revaluation of Group borrowings arranged to finance or hedge those net assets are taken directly to retained earnings. All other gains and losses on translation are dealt with in the income statement.

Derivative financial instruments

The Group may, from time to time, use derivative financial instruments (“derivatives”) to limit its exposure to fluctuations in foreign currency exchange rates and interest rates, and to manage some of its exposure to changes in oil prices.

Gains or losses arising on oil price derivatives are deferred and recognized in revenues from oil production when hedged volumes are sold.

As part of exchange risk management, foreign currency swap agreements and forward contracts are used to hedge movements in underlying currencies of certain borrowings. Gains and losses on these derivatives are deferred and recognized on maturity of the underlying debt together with the matching exchange loss or gain on the debt.

Foreign currency forward contracts and options are used to hedge significant non-sterling firm commitments or receivables. Gains or losses on these derivatives are deferred and recognized in the income statement or as adjustments to carrying amounts, as appropriate when the underlying transaction is completed.

The Group also enters into forward rate agreements and interest rate swap transactions in its management of interest rate exposure. Interest rate swap agreements generally involve the exchange of fixed and floating interest rate payment obligations without exchange of the underlying principal amounts. The results of these transactions are recognized in interest expense in the period hedged by the agreements.

Where derivatives, which are used to manage interest rate or foreign currency exposures, are terminated before the underlying debt or investment matures, or the hedged transaction occurs, the resulting gain or loss is recognized in the income statement on termination.

In the statement of cash flows the effects of interest rate swap agreements are reflected in returns on investments and servicing of finance. The effect of foreign currency derivatives used for hedging debt is included under financing. The cash flow effects of foreign currency derivatives used to hedge firm commitments or receivables are included in net cash inflow from operating activities for items relating to

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 1 — Accounting policies — (continued)

earnings or in capital expenditure or acquisitions, as appropriate, for items of a capital nature. The cash flow effects of all oil price derivatives are included in net cash inflow from operating activities.

Pension costs

The Group operates a number of pension schemes worldwide, the principal scheme being that in the United Kingdom, which is of the defined benefits type. Contributions to this scheme are charged to the income statement so as to spread the cost of pensions over the employees' working lives within the Group. The regular cost is attributed to individual years using the projected unit method. Variations in pension cost, which are identified as a result of actuarial valuations, are amortized over the average expected remaining working lives of employees. Differences between amounts funded and the amounts charged to the income statement are treated as either provisions or prepayments in the balance sheet.

Fixed assets

Exploration and appraisal expenditure

Exploration expenditure comprises all costs, including premium payments, associated with the acquisition of new acreage, the drilling of exploratory wells and other costs incurred in evaluating the commercial viability of geological entities.

Appraisal expenditure comprises costs incurred in the survey, exploration and appraisal of license areas not yet under development or in production.

Exploration and appraisal expenditure is classified as an intangible fixed asset until a decision is reached concerning the commercial viability of the field to which it relates. Expenditure is then either written off or transferred to tangible fixed assets. General seismic and other expenditure not connected with a specific exploration license is written off to the income statement immediately.

Development expenditure

Development expenditure comprises all costs including financing costs, exploration and appraisal expenditure incurred in bringing a field to commercial production and is classified as a tangible asset. No depletion is charged in respect of development expenditure. Once a field achieves commercial production, development expenditure is transferred to production assets.

Production assets

Expenditure on production assets represents the Group's share of total expenditure on the exploration, appraisal and development of oil and gas fields which are currently in commercial production. This expenditure includes costs of capital assets, financing costs and general technical and supervisory services plus, for depletion calculation purposes only, any anticipated further development expenditure and is stated at cost. Production assets are depleted by field on a unit of production method, in the proportion of actual production for the period to the total estimated remaining commercial reserves of the field on an entitlement basis. The remaining commercial reserves figure is that estimated at the end of the period plus the production during the period.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 1 — Accounting policies — (continued)

Fixed assets — (continued)

Impairment of value

Each year management compares the net book amounts carried in respect of each field with the estimated net realizable amount of proven and probable reserves. Any permanent impairment of tangible assets identified is provided for.

Oil and gas reserves

Proven and probable oil and gas reserves are estimated quantities of commercially producible hydrocarbons which existing geological, geophysical and engineering data show to be recoverable in future years from known reservoirs.

Other tangible assets

Office equipment and vehicles are stated at cost less accumulated depreciation, which is provided so as to write off those assets over their estimated useful lives, ranging from three to 15 years.

Decommissioning provisions

Provision is made for the cost of decommissioning of Group-owned assets, using the unit of production method based on proven and probable reserves on an entitlement basis. Such provision represents the Group's share of the estimated liability for costs which may be incurred in removing production platforms and facilities at the end of the producing life of each field.

Effect of changes in estimates

The effect of revisions of previous estimates of proven and probable oil and gas reserves and of costs is taken up prospectively in unit of production calculations.

Inventories

Inventories are stated at the lower of cost and net realizable value.

Investments

Investments included in current assets are stated at the lower of cost and net realizable value.

Note 2 — Segment information and certain risks and uncertainties

For the purposes of the Companies Act, the operations of the Group constitute one class of business, the exploration for and production of hydrocarbon liquids and gas.

The two major areas of operation of the Group are the UK and Indonesia regions. The UK region, for the purposes of providing segment information, includes The Netherlands. All other operations are included under International.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 2 — Segment information and certain risks and uncertainties — (continued)

Analysis of sales, profit and net assets by region

	Sales by source			Profit/(loss) before taxation			Net assets/(liabilities)		
	Year ended December 31			December 31			December 31		
	1997	1996	1995	1997	1996	1995	1997	1996	1995
	(£ million)								
UK	405	350	255	93	70	9	830	877	866
Indonesia	272	344	285	133	173	126	551	567	696
International	45	55	97	(28)	(1)	10	468	126	130
	<u>722</u>	<u>749</u>	<u>637</u>	198	242	145	1,849	1,570	1,692
Unallocated administrative expenses and net assets				(14)	(14)	(19)	40	36	37
Downstream (provision)/release				—	(2)	17	—	—	—
Net interest (expense)/income and net debt items				(30)	(20)	1	(613)	(346)	(429)
				<u>154</u>	<u>206</u>	<u>144</u>	<u>1,276</u>	<u>1,260</u>	<u>1,300</u>

In the UK region, sales sourced in the United Kingdom were £392 million (1996 £337 million; 1995 £245 million) with the balance of £13 million (1996 £13 million; 1995 £10 million) sourced in The Netherlands. Profit before taxation generated in The Netherlands was £5 million (1996 £4 million; 1995 £3 million).

Sales by destination are not materially different from those reported above, except for sales sourced in Indonesia which are substantially all sold within the Far East.

Analysis of sales by category

	Year ended December 31		
	1997	1996	1995
	(£ million)		
Production:			
Oil and LPG	370	340	308
Natural gas	335	398	321
Tariff income	17	11	8
	<u>722</u>	<u>749</u>	<u>637</u>

Analysis of total assets by region

	December 31		
	1997	1996	1995
	(£ million)		
UK	1,687	1,694	1,953
Indonesia	607	619	737
International	592	215	233
	<u>2,886</u>	<u>2,528</u>	<u>2,923</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 2 — Segment information and certain risks and uncertainties — (continued)

Certain risks and uncertainties

LASMO's results are affected by several key factors, namely production volumes, crude oil prices and exchange rates. In addition, costs of sales (including PRT and other production related taxes), and the level of exploration and development expenditure (which vary from year to year) and the timing of the related write off or depletion also affect results. Lower crude oil prices have a negative effect on the operating income and cash flow of LASMO. A weakening US dollar against the pound sterling generally has a negative effect on reported pound sterling operating income and cash flow because LASMO reports in pounds sterling. A strengthening US dollar against the pound sterling generally has a positive effect on operating income, cash flow and dollar denominated assets, but with approximately three quarters of LASMO's debt denominated in US dollars, also results in increasing gearing. LASMO, in the ordinary course of its business and like other oil and gas companies, enters into transactions to hedge to some extent the results of its operations against movements in exchange rates, interest rates and oil price movements.

Note 3 — Cost of sales

	Year ended December 31		
	1997	1996	1995
	(£ million)		
Operating costs	180	184	190
Depletion	233	234	203
Provision for decommissioning	8	8	10
Royalties	26	31	29
PRT charge	5	10	5
	452	467	437
Provision for oil and gas assets (Note 4)	—	—	17
	452	467	454

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 4 — Exceptional items

	Year ended December 31		
	1997	1996	1995
	(£ million)		
Cost of sales:			
Provision for tangible oil and gas assets(a)	—	—	(17)
Other operating items:			
Exploration provision release	—	2	2
Provision for reorganization costs(b)	—	—	(15)
	—	2	(13)
Non-operating items:			
Profit on disposal of oil and gas assets(c)	—	23	11
Loss on disposal of part of the AUK Loan Notes	—	(3)	—
Release of provision for loss on disposal of tangible oil and gas assets	—	—	3
	—	20	14
Downstream (provision)/release(d)	—	(2)	17
	—	18	31
	—	20	1
	—	20	1

(a) In 1995 £17 million was provided in respect of the Piper field group.

(b) LASMO initiated a major program for change during 1995 (“LASMO 2000”), aimed at further improving the efficiency and cost effectiveness of the Company. A provision of £15 million was charged through administrative expenses for changes in organization and operating practices and the consolidation of offices in the UK.

(c) The profit on disposal of oil and gas assets in 1996 arose principally on the sale of the Group’s operations in Nova Scotia and in 1995 on its interests in the Beatrice and Forties fields in the UK. The disposals of the Group’s interests in the Kakap and Malacca Strait PSCs were completed in 1995.

(d) The loss of £2 million in 1996 represents a provision for liabilities relating to downstream businesses acquired with Ultramar. The gain of £17 million in 1995 represents the release of a provision for certain exposures in the US established at the time of the acquisition of Ultramar.

Note 5 — Operating profit

Administrative expenses:

	Year ended December 31		
	1997	1996	1995
	(£ million)		
Administration costs	23	21	21
New business expenditure	9	7	1
Provision for reorganization costs	—	—	15
	32	28	37
	32	28	37

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 5 — Operating profit — (continued)

Operating profit for the year has been arrived at after charging:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Depletion and depreciation	237	238	225
Staff costs:			
Wages and salaries	35	29	30
Social security costs	3	2	2
Other pension costs	4	3	3
Operating lease rentals:			
Land and buildings	4	5	5
Other	<u>7</u>	<u>1</u>	<u>1</u>

Fees paid to auditors and other accounting firms:

	<u>Year ended December 31</u>					
	<u>1997</u>		<u>1996</u>		<u>1995</u>	
	<u>UK</u>	<u>Overseas</u>	<u>UK</u>	<u>Overseas</u>	<u>UK</u>	<u>Overseas</u>
	(£000)					
Audit of Group:						
Ernst & Young	348	23	400	95	480	105
Other accounting firms	—	18	—	19	—	14
Non audit fees:						
Ernst & Young	256	62	1,170	53	765	108
Other accounting firms	<u>—</u>	<u>41</u>	<u>43</u>	<u>79</u>	<u>39</u>	<u>102</u>

The UK non audit fees paid to Ernst & Young in 1996 and 1995 principally related to the LASMO 2000 program.

The average monthly number of employees (including directors) during the year was as follows:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(Number of employees)		
UK	310	292	280
Overseas	<u>464</u>	<u>453</u>	<u>561</u>
Total Group	<u>774</u>	<u>745</u>	<u>841</u>

At December 31, 1997 the total number of employees was 832 (1996 767; 1995 840).

Note 6 — Directors' emoluments and interests

Details of directors' emoluments and directors' interests in options are given in "Item 11. Compensation of Directors and Officers" and "Item 12. Options to Purchase Securities from Registrant or Subsidiaries".

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 7 — Interest receivable and similar income

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Bank interest receivable	25	26	23
Income from listed investments	13	21	26
Increase in value of investments	—	—	5
Petroleum revenue tax interest	3	5	7
Gain on repurchase of loan capital	—	—	1
Other income	<u>—</u>	<u>12</u>	<u>18</u>
	<u>41</u>	<u>64</u>	<u>80</u>

Note 8 — Interest payable and similar charges

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Bank loans and overdrafts	16	26	31
Other loans	67	65	64
Other finance charges	<u>3</u>	<u>3</u>	<u>6</u>
	86	94	101
Less: capitalized interest	<u>(15)</u>	<u>(10)</u>	<u>(22)</u>
	<u>71</u>	<u>84</u>	<u>79</u>

Other loans includes amounts paid and payable to holders of Oil Production Stock (“OPS”) units of £0.3 million (1996 £0.4 million; 1995 £0.4 million) net of taxation. These payments are calculated on 8.75% of the sales value of production from 8.62608% of the Ninian field after deducting Government royalties and operating costs incurred in extracting the oil and conveying and treating it at Sullom Voe. The Group sold its interest in the Ninian field with effect from January 1, 1994. As part of the consideration, LASMO received unlisted securities with identical terms to the OPS units. The income from these securities is equal to the OPS payments and is included within interest receivable and similar income.

Note 9 — Taxation

Profit before tax is analyzed as follows:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
United Kingdom	119	144	91
Overseas	<u>35</u>	<u>62</u>	<u>53</u>
	<u>154</u>	<u>206</u>	<u>144</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 9 — Taxation — (continued)

The charge for taxation is as follows:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
UK corporation tax:			
Current year charge	58	61	48
Less: double tax relief	(45)	(61)	(48)
Deferred taxation	1	8	8
Prior year items	(1)	—	—
	<u>13</u>	<u>8</u>	<u>8</u>
Overseas taxation:			
Current year charge	99	127	97
Prior year items	—	—	1
	<u>99</u>	<u>127</u>	<u>98</u>
	<u>112</u>	<u>135</u>	<u>106</u>
Advance corporation tax (written back)/written off	<u>(6)</u>	<u>4</u>	<u>4</u>

A reconciliation of the statutory rate of UK corporation tax to the effective rate of taxation is as follows:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(%)		
UK statutory rate	31.5	33.0	33.0
Effect of overseas taxes	27.8	34.9	30.1
Permanent differences	(1.0)	(8.1)	(11.6)
Advance corporation tax (written back)/written off	(4.3)	1.9	3.1
Non taxable income	(1.6)	(0.7)	(2.2)
Timing differences for which no provision is required	16.9	3.9	19.2
Other items	(0.5)	2.8	4.4
	<u>68.8</u>	<u>67.7</u>	<u>76.0</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 10 — Dividends

	Year ended December 31		
	1997	1996	1995
	(£ million)		
<i>Non-equity shares</i>			
Preference shares:			
£60 million 9% Cumulative Redeemable Preference Shares	—	3	6
US\$250 million Cumulative Dollar Preference Shares, Series A	<u>12</u>	<u>13</u>	<u>13</u>
	<u>12</u>	<u>16</u>	<u>19</u>
<i>Equity shares</i>			
Ordinary shares:			
Final — proposed 2.30 pence per share (1996 2.00p; 1995 1.25p)	<u>22</u>	<u>19</u>	<u>12</u>
	<u>34</u>	<u>35</u>	<u>31</u>

The final dividend for 1997 will be paid in the form of a Foreign Income Dividend.

Note 11 — Earnings per share

The calculation of earnings per ordinary share is based on the profit for the year, after taxation and preference dividends, of £36 million (1996 £51 million; 1995 £15 million). Earnings per ordinary share before exceptional items is based on a profit of £36 million (1996 £31 million; 1995 £14 million). The weighted average number of ordinary shares in issue for earnings per share was 965,966,362 shares (1996 965,895,800 shares; 1995 965,460,518 shares).

Note 12 — Petroleum revenue tax and corporation taxation recoverable

Petroleum revenue tax and corporation taxation recoverable includes £14 million (1996 £12 million) expected to be realized after more than one year.

Note 13 — Accounts receivable

	December 31	
	1997	1996
	(£ million)	
Trade receivables	140	124
Other receivables	60	67
Prepayments	<u>7</u>	<u>6</u>
	<u>207</u>	<u>197</u>

Of other receivables, £47 million (1996 £42 million) is expected to be realized after more than one year.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 14 — Fixed assets

Intangible assets: exploration and appraisal expenditure

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(£ million)			
Cost:				
At January 1, 1995	8	5	17	30
Additions	11	3	40	54
Acquisitions	2	—	—	2
Amounts written off	(10)	(4)	(22)	(36)
Transfers	(3)	—	(16)	(19)
Disposals	(3)	—	—	(3)
At December 31, 1995	<u>5</u>	<u>4</u>	<u>19</u>	<u>28</u>
Additions	22	2	51	75
Amounts written off	(16)	(3)	(29)	(48)
Transfers	(3)	—	(18)	(21)
Exchange adjustments	—	—	1	1
At December 31, 1996	<u>8</u>	<u>3</u>	<u>24</u>	<u>35</u>
Additions	37	6	52	95
Amounts written off	(18)	(8)	(28)	(54)
Transfers	1	—	(20)	(19)
At December 31, 1997	<u><u>28</u></u>	<u><u>1</u></u>	<u><u>28</u></u>	<u><u>57</u></u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 14 — Fixed assets — (continued)

Tangible assets

	Freehold land*	Office equipment and vehicles	Oil and gas expenditure			Total
			Fields in production	Fields under development	Fields awaiting development	
			(£ million)			
Cost:						
At January 1, 1995	—	30	2,385	390	39	2,844
Exchange adjustments	—	—	14	—	—	14
Acquisitions	—	—	1	—	—	1
Additions	—	5	58	187	2	252
Disposals	—	(2)	(257)	(17)	—	(276)
Transfers	—	—	116	(95)	(2)	19
Transfers from current assets ..	39	—	—	—	—	39
At December 31, 1995	39	33	2,317	465	39	2,893
Exchange adjustments	(4)	(1)	(121)	(1)	(2)	(129)
Acquisitions	—	—	8	—	—	8
Additions	4	4	70	64	19	161
Disposals	—	(2)	(103)	(5)	—	(110)
Transfers	—	—	497	(458)	(18)	21
At December 31, 1996	39	34	2,668	65	38	2,844
Exchange adjustments	1	—	34	—	(1)	34
Acquisitions	—	—	15	275	1	291
Additions	3	19	67	108	9	206
Disposals	—	(6)	(60)	—	—	(66)
Transfers	—	—	66	(59)	12	19
At December 31, 1997	43	47	2,790	389	59	3,328

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 14 — Fixed assets — (continued)

Tangible assets — (continued)

	Freehold land*	Office equipment and vehicles	Oil and gas expenditure			Total
			Fields in production (£ million)	Fields under development	Fields awaiting development	
Depletion and depreciation:						
At January 1, 1995	—	23	1,058	5	2	1,088
Exchange adjustments	—	—	9	—	—	9
Charge for the year	—	5	203	—	—	208
Exceptional provision	—	—	17	—	—	17
Provisions utilized	—	—	6	—	—	6
Disposals	—	(2)	(245)	—	—	(247)
Transfers from current assets ..	5	—	—	—	—	5
At December 31, 1995	5	26	1,048	5	2	1,086
Exchange adjustments	—	(1)	(56)	—	—	(57)
Charge for the year	—	4	234	—	—	238
Disposals	—	(1)	(95)	(5)	—	(101)
At December 31, 1996	5	28	1,131	—	2	1,166
Exchange adjustments	—	—	13	—	—	13
Charge for the year	—	4	233	—	—	237
Disposals	—	(6)	(56)	—	—	(62)
Transfers	—	—	—	2	(2)	—
At December 31, 1997	5	26	1,321	2	—	1,354
Net book amounts:						
At December 31, 1997	38	21	1,469	387	59	1,974
At December 31, 1996	34	6	1,537	65	36	1,678
At December 31, 1995	34	7	1,269	460	37	1,807
Cost at December 31, 1997						
includes capitalized interest of:	—	—	153	11	—	164

* Comprises real estate located in the US which is held for resale and is expected to be sold over the next four years.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 14 — Fixed assets — (continued)

Oil and gas expenditure: regional analysis

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(£ million)			
Cost:				
Fields in production	1,737	914	139	2,790
Fields under development	45	—	344	389
Fields awaiting development	<u>—</u>	<u>—</u>	<u>59</u>	<u>59</u>
At December 31, 1997	1,782	914	542	3,238
Depletion:				
At December 31, 1997	<u>871</u>	<u>378</u>	<u>74</u>	<u>1,323</u>
Net book amounts:				
At December 31, 1997	<u>911</u>	<u>536</u>	<u>468</u>	<u>1,915</u>
At December 31, 1996	<u>977</u>	<u>551</u>	<u>110</u>	<u>1,638</u>

Investments

	<u>AUK Loan</u>	<u>Own</u>	<u>Other</u>	<u>Total</u>
	Notes (a)	Shares (b)		
	(£ million)			
At January 1, 1997	187	32	1	220
Disposals	<u>—</u>	<u>(4)</u>	<u>—</u>	<u>(4)</u>
At December 31, 1997	<u>187</u>	<u>28</u>	<u>1</u>	<u>216</u>

(a) The AUK Guaranteed Unsecured Floating Rate Notes 2003 (“AUK Loan Notes”) are guaranteed by Elf Aquitaine Soci t  Nationale and are listed on the Luxembourg Stock Exchange. The investment is included in the balance sheet at cost which is equivalent to par value as the directors currently intend to hold the AUK Loan Notes until maturity. The AUK Loan Notes are pledged as collateral for certain Group borrowings (Note 16).

(b) The Group held 16,162,083 LASMO plc ordinary shares as at December 31, 1997 (1996 18,416,225 shares) arising from its acquisition of Ultramar. The market value of these shares at December 31, 1997 was £45 million (1996 £44 million). The historical cost of these shares at December 31, 1997 was £44 million (1996 £50 million).

Note 15 — Current liabilities

Accruals and other payables

	<u>December 31</u>	
	<u>1997</u>	<u>1996</u>
	(£ million)	
PRT and other taxation	39	38
Social security	1	1
Dividends	25	22
Accruals	153	97
Other current liabilities	<u>51</u>	<u>45</u>
	<u>269</u>	<u>203</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 15 — Current liabilities — (continued)

Bank loans and overdrafts

	December 31	
	1997	1996
	(£ million)	
Bank loans and overdrafts	17	13

Short-term bank loans of £15 million (1996 £12 million) comprise current maturities of long-term debt.

Note 16 — Noncurrent liabilities

Bank loans

The average interest rate charged on bank loans due after more than one year was 7.087 per cent (1996 6.813 per cent).

Loan capital

	December 31	
	1997	1996
	(£ million)	
£59 million 9½% Notes 1999	59	59
US\$93 million 10.13% Notes 2000	56	54
US\$200 million 7½% Guaranteed Notes 2003	120	115
US\$20 million 10.30% Notes 2005	12	12
£81 million 7¾% Convertible Bonds 2005(a)	79	79
US\$300 million 7.50% Guaranteed Notes 2006	179	172
US\$200 million 6.75% Guaranteed Notes 2007(b)	120	—
£150 million 10¾% Debenture Stock 2009(c)	149	149
US\$150 million 8¾% Guaranteed Notes 2023	90	87
US\$400 million 7.30% Guaranteed Debentures 2027(d)	233	—
OPS units of 10p each(e)	1	1
	1,098	728

(a) The £81 million 7¾% Convertible Bonds 2005 (initial issue £90 million) are convertible at the option of the holder into ordinary shares of the Company at a price of 541p per ordinary share on or before September 27, 2005 subject to adjustment in certain circumstances.

(b) The US\$200 million 6.75% Guaranteed Notes 2007 were issued on December 10, 1997. The net proceeds will be used for general corporate purposes.

(c) Payment of principal and interest on the £150 million 10¾% Debenture Stock 2009 is guaranteed by LASMO Securities (Jersey) Limited, a wholly-owned subsidiary of the Company, and the guarantee is secured by a charge over the AUK Loan Notes held by LASMO Securities (Jersey) Limited.

(d) The US\$400 million 7.30% Guaranteed Debentures 2027 were issued on November 6, 1997. The net proceeds were used to repay borrowings incurred in connection with the Dacion Area project in Venezuela.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 16 — Noncurrent liabilities — (continued)

(e) Oil Production Stock

	(Number of units)	(£000)
At January 1, 1996 and December 31, 1996 and 1997	<u>5,562,990</u>	<u>556</u>

The OPS is repayable at par on the earliest of:

- the date when the total quantity of petroleum won and saved from the 8.62608% interest in the Ninian field to which the OPS relates, reaches 120 million barrels;
- the termination of production from the field; or
- December 31, 2010.

At December 31, 1997 cumulative production from the Ninian field attributable to the interest on which OPS payments have become due amounted to 93.4 million barrels (1996 91.9 million barrels).

Deferred income and other accounts payable

	December 31	
	1997	1996
	(£ million)	
Deferred income(a)	19	25
Other accounts payable	8	6
	<u>27</u>	<u>31</u>

(a) Interest is receivable on PRT refunds which have arisen from the carryback of excess current UK North Sea expenditure against prior year PRT payments. To the extent that such interest relates to PRT receipts, which totalled £9 million (1996 £13 million) arising in respect of the Piper field redevelopment, it has been deferred and is being released to income as Piper production is received. Also included in deferred income is £10 million (1996 £12 million) which relates to a prepayment received under a contract for sale of gas. The income is being released to profits as deliveries are made.

Note 17 — Total borrowings

	December 31	
	1997	1996
	(£ million)	
Due after ten years	472	236
Due between five and ten years	511	461
	983	697
Due within:		
four to five years	19	19
three to four years	18	70
two to three years	73	74
one to two years	74	13
Due after more than one year (Note 16)	1,167	873
Due within one year (Note 15)	17	13
	<u>1,184</u>	<u>886</u>
Gross borrowings secured on assets of Group companies	<u>150</u>	<u>150</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 17 — Total borrowings — (continued)

Analysis by currency:

	December 31	
	1997	1996
	(£ million)	
Sterling	291	290
US dollars	893	596
	1,184	886

Total borrowings are stated net of unamortized issue expenses totalling £18 million (1996 £9 million).

The amount of bank loans repayable by instalment, with payments due after more than 5 years, total £nil (1996 £92 million). All other amounts payable after more than 5 years are not repayable by instalment.

The Company is empowered under its Articles of Association to borrow up to twice the aggregate amount of the share capital and reserves of the Company and its subsidiaries as indicated by the latest audited consolidated financial statements, subject to certain adjustments.

At December 31, 1997, the Group had undrawn borrowing facilities of £300 million which were covered by formal commitments.

Note 18 — Provisions for liabilities and charges

	Deferred PRT	Deferred taxation	Decommissioning provisions	Acquisition provisions	Other provisions	Total
	(£ million)					
Balance at January 1, 1995	84	(12)	43	17	25	157
(Credit)/charge	(16)	8	10	(17)	(4)	(19)
Transfer/disposal	—	—	(12)	—	(2)	(14)
Utilized	—	—	(2)	—	(10)	(12)
Balance at December 31, 1995	68	(4)	39	—	9	112
(Credit)/charge	(19)	8	8	—	(1)	(4)
Transfer/disposal	—	—	(6)	—	—	(6)
Utilized	—	—	(3)	—	(4)	(7)
Balance at December 31, 1996	49	4	38	—	4	95
(Credit)/charge	(14)	1	8	—	—	(5)
Utilized	—	—	(1)	—	—	(1)
Balance at December 31, 1997	35	5	45	—	4	89

The provisions for decommissioning represent the accumulated amount of the Group's share of decommissioning costs of £45 million (1996 £38 million) for all North Sea fields in which the Group has an interest and which are currently in production. The total estimated liability for the Group's share of decommissioning costs for fields in production is currently forecast at £103 million (1996 £102 million).

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 18 — Provisions for liabilities and charges — (continued)

Deferred taxation

	December 31	
	1997	1996
	(£ million)	
The potential liability for deferred taxation is:		
Accelerated capital allowances and other timing differences	127	72
Roll-over relief — AUK Loan Notes	—	33
Overseas deferred taxation	<u>11</u>	<u>27</u>
	138	132
Deduct: advance corporation tax	<u>(82)</u>	<u>(64)</u>
	<u>56</u>	<u>68</u>
of which the following amounts have been recognized in the financial statements:		
Accelerated capital allowances and other timing differences	<u>5</u>	<u>4</u>

The amount provided in respect of accelerated capital allowances and other timing differences includes £8 million (1996 £11 million) relating to refunds of petroleum revenue tax arising from the Piper redevelopment and which are included in deferred petroleum revenue tax.

Deferred taxation is not provided in respect of liabilities which might arise on the distribution of profits of overseas subsidiary companies, due to the availability of foreign tax credits.

Note 19 — 9½% Cumulative Redeemable Preference Shares of £1 each (“Sterling Preference Shares”)

At December 31, 1997 and 1996 the authorized sterling preference share capital was £100 million.

Note 20 — Employee share schemes

LASMO has four employee share option schemes of which two are principally for UK employees, including executive directors. The four schemes are the LASMO 1980 Executive Share Option Scheme established in 1980 (the “1980 Scheme”), the LASMO SAYE Share Option Scheme established in 1982 (the “SAYE Scheme”), the LASMO 1984 Executive Share Option Scheme established in 1984 (the “1984 Scheme”) and the LASMO International Executive Share Option Scheme established in 1995 (the “International Scheme”). The initial ten year period of the 1984 Scheme ended on December 21, 1994 but shareholders approved the extension of that scheme for a further ten years (in modified form) in 1995 and, at the same time, approved the establishment of the International Scheme, the provisions of which are, in all material respects, identical to those of the 1984 Scheme, but enable both UK and overseas executives to participate. The 1980 Scheme also ended on December 21, 1994 and no further options will be granted under that scheme. Outstanding options granted during the period of the 1980 Scheme will continue to be exercisable for up to ten years from the date of grant in accordance with the rules of the scheme. See “Item 12. Options to Purchase Securities from Registrant or Subsidiaries”.

The exercise of options granted under the 1984 Scheme and the International Scheme since April 1995 is subject to the achievement of total shareholder return (TSR — change in share price plus re-invested dividends) relative to a comparator group (the “Comparator Group”) of ten international oil and gas exploration and production companies.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 20 — Employee share schemes — (continued)

The performance target enabling options to be exercised is on a sliding scale whereby 33.33% is exercisable only if the Company's performance places it in the third quartile and 100% is exercisable only if the Company's performance places it in the top quartile of the Comparator Group over any three year period.

No options have been or will be granted under the Executive Share Option Schemes to executives who are eligible to participate in the LASMO Equity Plan.

Eligible directors and employees of the Company and its participating subsidiaries who enter into a three or five year save-as-you-earn savings contract to make monthly contributions of not less than £10 or more than £250 per month each may be granted options to subscribe for ordinary shares under the SAYE Scheme following the announcement of the Group's results for the immediately preceding financial year or half year. Option holders are entitled to use their savings and the bonus payable at the end of the savings contract to subscribe for the ordinary shares under option at a price which may not be less than the higher of (i) 80% of the average of the middle market quotation for an ordinary share on the business day immediately preceding the date of the invitation and (ii) the nominal value of such a share.

Movements in the options outstanding under these schemes for the three years ended December 31, 1997 are as follows:

	<u>Executive Schemes</u>		<u>SAYE Scheme</u>	
	<u>No. of shares</u>	<u>Price range (p)</u>	<u>No. of shares</u>	<u>Price range (p)</u>
Outstanding January 1, 1995	7,120,911	70.67-456.03	2,886,466	100.00-308.50
Granted	1,425,685	166.00-176.00	236,930	121.00
Exercised	(222,337)	70.67-137.65	(19,614)	100.00-145.93
Lapsed/cancelled	(891,848)	147.00-456.03	(419,840)	100.00-308.50
Outstanding December, 31 1995	7,432,411	126.25-456.03	2,683,942	100.00-308.50
Granted	575,000	187.00	304,960	150.00
Exercised	(701,974)	126.25-182.41	(78,669)	100.00-145.93
Lapsed/cancelled	(363,985)	147.00-456.03	(339,940)	100.00-300.50
Outstanding December, 31 1996	6,941,452	126.25-456.03	2,570,293	100.00-308.50
Granted	636,000	241.50-244.50	490,533	194.00
Exercised	(1,008,635)	133.45-238.10	(571,124)	100.00-145.93
Lapsed/cancelled	(196,033)	166.00-385.94	(138,787)	100.00-308.50
Outstanding December, 31 1997	<u>6,372,784</u>	<u>126.25-456.03</u>	<u>2,350,915</u>	<u>100.00-300.50</u>
Options exercisable at December 31, 1997	<u>4,048,099</u>	<u>126.25-456.03</u>	<u>17,250</u>	<u>100.00</u>
Options available for grant at				
December 31, 1997	<u>85,566,995</u>		<u>40,292,516</u>	
Fair value of options granted in the years ended				
December 31, 1997		<u>1.39</u>		<u>0.94</u>
December 31, 1996		<u>1.12</u>		<u>0.93</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 20 — Employee share schemes — (continued)

Movements in the options outstanding under the option schemes and the weighted average option price of these movements are as follows:

	Executive Schemes		SAYE Scheme	
	No. of shares	Weighted average option price (p)	No. of shares	Weighted average option price (p)
Outstanding January 1, 1997	6,941,452	228.09	2,570,293	123.32
Granted	636,000	244.23	490,533	194.00
Exercised	(1,008,635)	180.49	(571,124)	144.80
Lapsed/cancelled	(196,033)	292.18	(138,787)	142.75
	<u>6,372,784</u>	<u>235.26</u>	<u>2,350,915</u>	<u>131.70</u>
Options exercisable at December 31, 1997	<u>4,048,099</u>	<u>260.41</u>	<u>17,250</u>	<u>100.00</u>

Summarised information about options outstanding under the share option schemes is as follows:

	Options outstanding			Options exercisable	
	No. of shares	Weighted average remaining contract life (years)	Weighted average option price (p)	No. exercisable	Weighted average option price (p)
<i>Executive schemes</i>					
126.25-187.00	3,681,962	0.3	164.49	1,971,277	157.73
212.01-456.03	2,690,822	0.5	332.09	2,076,822	358.07
	<u>6,372,784</u>	<u>0.4</u>	<u>235.26</u>	<u>4,048,099</u>	<u>260.41</u>
<i>SAYE scheme</i>					
100.00-127.00	1,524,207	1.5	107.47	17,250	100.00
145.93-194.00	820,809	3.4	175.66	—	—
247.70-300.50	5,899	0.5	274.49	—	—
	<u>2,350,915</u>	<u>2.2</u>	<u>131.70</u>	<u>17,250</u>	<u>100.00</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 20 — Employee share schemes — (continued)

Assumptions made in determining the fair value of options granted for the purpose of the date of grant fair value amounts above, and the pro forma disclosures shown in Note 29, using the Black-Scholes model, include:

- all relevant performance tests will be fully satisfied at the earliest possible date. Therefore, options may be exercised at any time between three years from grant and expire at a date 10 years from grant;
- a risk free interest rate of 6.5% (1996 7.5%, 1995 8.1%);
- expected share price volatility of 29.5%; and
- dividend growth of 5%, which amount does not represent a forecast.

Other share option plans

The Company has other stock option plans in which former employees of the Ultramar Group participate. At December 31, 1997 there were outstanding options exercisable during the years 1998 to 2001, to acquire 305,441 ordinary shares at prices ranging from £2.50 to £2.81 per share.

The Company also has a stock appreciation rights (“SAR”) plan under which SARs have been granted to US residents who previously held options under Ultramar stock option plans. The number of SARs so granted was based on a percentage of their holdings under the Ultramar stock options plans, and the corresponding exercise value of such SARs was based on the Ultramar stock option exercise prices. On valid exercise of a SAR, LASMO pays to the option holder the difference between the calculated exercise price of equivalent LASMO ordinary shares underlying the SAR and the market value of LASMO ordinary shares on the date of exercise, either in cash or LASMO ordinary shares at the option of the Company. The base price range for SARs is £59.80 to £67.20 (or 249.616p to 280.505p per ordinary share) and their exercise price on any date is the market value of 23.9568 ordinary shares. At December 31, 1997 3,600 SARs were outstanding.

In addition there are options over 48,000 Ultramar shares which remain outstanding.

LASMO Profit Sharing Scheme

Under the terms of the LASMO Profit Sharing Scheme (the “Profit Sharing Scheme”), employees (including executive directors) of the Company and its participating subsidiaries and who are resident and ordinarily resident in the United Kingdom shall be eligible to participate in the Profit Sharing Scheme. The Profit Sharing Scheme allows for LASMO Trustee Company Limited (“the Trustee”) to acquire ordinary shares of the Company for the benefit of the participants up to a maximum value as is from time to time permitted by the Income and Corporation Taxes Act 1988. Currently, the annual limit is the lower of £8,000 or 10% of salary per participant. The maximum amount which may be made available in any year under the Profit Sharing Scheme may not exceed 5% of the Group’s pre-tax profits. The shares are held in trust for participants for at least two years during which period they may not ordinarily be transferred or sold. Thereafter, the Trustee will act in accordance with the directions of participants and voting rights attaching to shares will only be exercised by the Trustees in accordance with the directions of participants.

Equity Plan

Executive directors and other senior executives may be granted a notional allocation of ordinary shares in the Company by the Trustee of the LASMO Equity Plan based on a percentage of salary and calculated by reference to middle market share price. Participants may choose to commit to the plan up to the same number of LASMO shares which will be matched by a further notional allocation of shares by the Trustee.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 20 — Employee share schemes — (continued)

Subject to the achievement of two performance targets, the actual number of shares (if any) to be given to each participant will be determined after the third year or, if not met by then, after the fourth or fifth year. The shares, which will be provided from existing ordinary shares in issue acquired by the Trustee, will not normally be released to participants earlier than five years from the date of the award. The performance targets operate as follows: first, the number of shares notionally allocated to a participant will be adjusted so that, on a sliding scale, 100% will become available if there is an increase in the LASMO share price of 2.5% per annum over the Retail Price Index over the award period, with a further 100% for each additional 5% per annum real increase. Secondly, the actual number of shares to be awarded will be determined by comparing the total shareholder return (“TSR”) to LASMO ordinary shareholders against the Comparator Group. In respect of notional allocations made in the years 1995 to 1997, if LASMO’s TSR is bottom, the participant will get none of the shares notionally allocated to him or her. If LASMO’s TSR ranks number 10, the participant will receive shares equal to 20% of the adjusted notional allocation, increasing by incremental amounts of 20% up to a maximum of 200% if the LASMO TSR is in first place. For notional allocations made in 1998 and subsequent years, no shares will be confirmed if LASMO’s TSR ranks number 9 or lower against the Comparator Group. If LASMO’s TSR ranks number 8, shares equal to 60% of the adjusted notional allocation will be confirmed, increasing by incremental amounts of 20% up to a maximum of 200% if LASMO’s TSR is in first place. In general, commencing with the 1998 notional allocations, confirmed shares to any one individual will not exceed five times the notional allocation to that individual in respect of any particular year. Awards over confirmed shares are normally exercisable by the participant between five and seven years from the date of notional allocation. The shares will be provided from existing ordinary shares acquired by the Trustee. The Comparator Group of companies used in the Executive Share Option Schemes and the Equity Plan comprises:

Anadarko Petroleum Corporation	Oryx Energy Limited
Apache Corporation	Ranger Oil Limited
British-Borneo Petroleum Syndicate, P.L.C.	Saga Petroleum AS
Enterprise Oil plc	Talisman Energy Inc.
Monument Oil and Gas plc	Union Texas Petroleum Holdings Inc.

Total compensation cost in 1997 for stock based employee compensation schemes amounted to £4.8 million (1996 £2.8 million; 1995 £1.5 million).

Note 21 — Pension costs

The LASMO Group operates a number of pension schemes. The principal scheme is the LASMO Pension Plan (“the Plan”) which operates in the United Kingdom and which is of the funded and defined benefits type. The Plan covers approximately 380 Group employees (1996 340) and its assets are held in trust in a separately administered fund.

The latest actuarial valuation of the Plan was carried out as at March 31, 1996 and was prepared using the projected unit method. This valuation, which assumed investment returns of 1% per annum in excess of salary increases and 4% per annum in excess of pension increases, disclosed a funding level of 110%. The market value of the Plan’s assets at the valuation date was £42 million.

The surplus disclosed by the valuation has been used to reduce the Company contributions. The pension cost assessed on the basis of actuarial advice and charged in the financial statements was £4 million (1996 £3 million; 1995 £3 million).

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 21 — Pension costs — (continued)

Additional information required by FAS 87 in respect of the Group's UK pension plan

The pension cost for the Plan computed in accordance with the requirements of FAS 87 comprises:

	Year ended December 31		
	1997	1996	1995
	(£ million)		
Service cost	4	4	4
Interest cost	3	3	2
Actual return on Plan assets	(6)	(5)	(6)
Net amortization and deferral	2	1	2
Net periodic pension cost	3	3	2

The major assumptions used in computing the funded status of the Plan under FAS 87 were as follows:

	December 31	
	1997	1996
Expected long-term rate of return on Plan assets	8.00%	8.25%
Discount rate	7.25%	8.25%
Expected long-term rate on earnings increases	6.00%	6.25%

	December 31	
	1997	1996
	(£ million)	
Accumulated benefit obligation (all vested)	42	30
Fair value of Plan assets	55	47
Projected benefit obligation	(54)	(38)
Plan assets in excess of projected benefit obligations	1	9
Unrecognized net gain	(3)	(11)
Net pension provision	(2)	(2)

The assets of the Plan principally comprise UK and other listed equities, bank deposits and UK Government index-linked stocks.

Note 22 — Derivative financial instruments and fair value of financial instruments

The Group uses non-leveraged derivative financial instruments (“derivatives”) to manage its exposure to fluctuations in foreign currency exchange rates, interest rates, and some movements in crude oil prices. Most of the Group’s borrowings are in US dollars or swapped into dollars where this achieves a lower cost of financing. The Group also manages the balance between floating rate and fixed rate debt. The Group does not become a party to derivatives for trading purposes; they are used exclusively for hedging purposes.

Derivatives involve, to varying degrees, credit and market risk. With regard to credit risk, the Group may be exposed to loss in the event of non-performance by a counterparty. The Group controls credit risk by entering into derivative contracts only with highly credit rated counterparties and through credit approvals, limits and monitoring procedures. The Group has not experienced material non-performance by any counterparty.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 22 — Derivative financial instruments and fair value of financial instruments — (continued)

Market risk is the possibility that a change in interest rates, currency exchange rates or oil prices will cause the value of a financial instrument to decrease or its obligations to become more costly to settle. When derivatives are used for the purpose of risk management they do not expose the Group to market risk because gains and losses on the derivatives offset losses and gains on the asset, liability or transaction being hedged.

Risk management strategies are reviewed and approved by senior management before being implemented. Policy controls limit the maximum amount of positions that can be taken in any instrument and with any single counterparty.

Interest rate risk management

In order to reduce the interest rate risk in respect of its investment and debt portfolio, the Group enters into forward rate and interest rate swap agreements to change the interest payable on parts of its underlying borrowings from fixed rates to variable or variable rates to fixed. Accordingly, the Group is exposed to market risk to the extent that receipts and payments under interest rate agreements are affected by market interest rates. The Group accounts for interest rate agreements in the period hedged by the agreement.

There were no outstanding forward rate agreements at December 31, 1997 or 1996.

In the event of counterparty default, the exposures created would be the difference between the then prevailing market and the forward interest rates.

Foreign exchange risk management

The Group enters into various types of foreign exchange contracts in managing its foreign exchange risk. The Group seeks, where possible, to minimise the balance sheet translation exposure of non-sterling denominated assets by arranging borrowings in matching currencies. At December 31, 1997, 75% of the Group's gross borrowings were denominated in US dollars, the balance of the Group's gross borrowings was denominated in sterling.

The Group also enters into forward exchange contracts to hedge foreign currency transactions. At December 31, 1997, the Group had contracted to exchange the equivalent of £53 million (1996 £55 million) of US dollars and Netherlands Guilders, all of which are accounted for as hedges under accounting principles generally accepted in the United Kingdom. In the event of counterparty default, the exposure created would be the difference between the contracted rate and the then prevailing market exchange rate in the case of these contracts. The Group has no reason currently to expect non-performance by counterparties to these arrangements.

Oil price risk management

To reduce exposure to periods of price weakness, LASMO may, from time to time, hedge its near term oil and gas price realizations. The objective remains to stabilize the near term financial position while retaining shareholder exposure to oil and gas prices in the medium and longer term. The Group uses swaps and futures to hedge future sales of crude oil; the terms of these derivative contracts are usually less than one year.

Under swaps, LASMO agrees with other parties to pay or receive the difference between a fixed and variable price, at a range of specified dates, determined by reference to an agreed notional volume of crude oil. LASMO only enters into swap agreements with credit worthy counterparties and only using standard International Swap Dealers Association ("ISDA") documentation.

As at December 31, 1997, there were no contracts outstanding.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 22 — Derivative financial instruments and fair value of financial instruments — (continued)

Crude oil futures are fixed price commitments, traded on regulated exchanges, to purchase or sell a contract, whose value is derived from the price of crude oil at a specified future date. Initial margin requirements and daily cash settlements for these contracts are met either by bank guarantees or in cash. There is little credit risk under these contracts as regulated exchanges are the counterparties which require margin settlement on a daily basis. Oil swaps were entered into in 1997 in respect of some 6% of total Group production for the year. The effect of this program was to reduce the total average realised price of a barrel of oil equivalent by £0.01. The Group accounts for oil price derivatives under the deferral method.

Carrying values and fair values of financial instruments

The carrying values and fair values of the material financial instruments of the Group held at December 31, 1997 and 1996, none of which were held for trading purposes, are set out in the table below:

	December 31			
	1997		1996	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(£ million)			
Assets				
Cash at bank and in hand	375	375	353	353
Unlisted securities	9	9	—	—
Other listed securities				
AUK Loan Notes	187	187	187	187
Liabilities				
Total borrowings				
Loan capital and noncurrent bank loans	(1,167)	(1,274)	(873)	(926)
Bank loans and overdrafts	(17)	(16)	(13)	(13)
Off-balance sheet instruments				
Exchange rate swaps	—	—	—	1
Oil price contracts	—	—	—	(9)

The following methods and assumptions were used by the Group in estimating fair value of financial instruments:

Cash at bank and in hand: the carrying amount reported in the balance sheet for cash at bank and in hand approximates its fair value.

Other listed securities: the AUK Loan Notes are valued based on market prices for similar investments. The other securities are valued based on their quoted prices.

Borrowings: the carrying amount of the Group's bank loans and overdrafts approximate their fair value. The fair value of the Group's loan capital and noncurrent bank loans (including short-term portion) are estimated using quoted prices or, where such prices are not available, discounted cash flow analyses, based on the Group's current incremental borrowing rates for similar types of borrowing arrangements and maturities.

Off-balance sheet instruments: the fair values of the Group's interest rate swap agreements are based on discounted cash flow analyses. Fair values for the Group's exchange rate swap agreements are based on market prices of comparable instruments. Oil price contracts are those which require settlement in cash and include futures contracts and swap agreements. Fair values of these contracts are based on quoted prices or discounted cash flow analyses.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 23 — Contingencies

The Company is involved in litigation and is subject to governmental and regulatory controls arising in the ordinary course of business. It is the opinion of the Company's management that all claims and litigation involving the Company are not likely to have a material adverse effect on its financial position or results of operations.

Note 24 — Commitments

The following amounts, including information supplied by the operators, were contracted for at December 31:

	December 31	
	1997	1996
	(£ million)	
Oil and gas expenditure	51	88

At December 31, operating lease obligations existed which were payable within one year in respect of leases expiring:

	December 31			
	1997			1996
	Land and buildings	Other	Total	Total
	(£ million)			
Within 1 year	—	—	—	7
Within 2-5 years	—	22	22	28
After 5 years	5	—	5	3
	5	22	27	38

The future minimum lease payments were as follows:

	December 31
	(£ million)
1998	27
1999	27
2000	21
2001	13
2002	9
Thereafter	31
	128

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 25 — Reconciliation of operating profit to net cash inflow from operating activities

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Operating profit	184	208	112
Exploration costs written off (net of provision release)	54	46	34
Provision for decommissioning	7	5	8
Depletion and depreciation	237	238	208
Provision for oil and gas assets	—	—	17
(Utilization)/provision for reorganization costs	(8)	(2)	15
Changes in PRT provisions and other balances	(16)	(16)	(9)
(Increase)/decrease in inventory	(2)	2	3
Increase in receivables	(16)	(25)	(25)
Increase in payables	26	—	2
Deferred income	(2)	(2)	—
Net cash inflow from operating activities	<u>464</u>	<u>454</u>	<u>365</u>

Note 26 — Financing cashflow

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Borrowings raised	(659)	(241)	(180)
Borrowings repaid	372	514	49
Preference shares repaid	—	60	—
Net cash (inflow)/outflow from financing	<u>(287)</u>	<u>333</u>	<u>(131)</u>

Note 27 — Reconciliation of net cash flow to movement in Group net debt

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Increase in cash in the year	3	10	4
Cash (inflow)/outflow from increase/decrease in debt	(287)	273	(131)
Cash outflow/(inflow) from increase/decrease in liquid resources	30	(85)	89
Changes resulting from cash flow	(254)	198	(38)
Exchange difference	(23)	63	(5)
Other	10	3	(2)
Movement in debt net of cash and liquid resources in the year	(267)	264	(45)
Repayment of Sterling Preference Shares	—	60	—
Decrease in AUK Loan Notes	—	(181)	—
Movement in Group net debt	(267)	143	(45)
Group net debt at January 1	<u>(346)</u>	<u>(489)</u>	<u>(444)</u>
Group net debt at December 31	<u>(613)</u>	<u>(346)</u>	<u>(489)</u>

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 28 — Analysis of movement in Group net debt

	<u>January 1, 1997</u>	<u>Cashflow</u>	<u>Other non-cash changes</u>	<u>Exchange movements</u>	<u>December 31, 1997</u>
			(£ million)		
Cash repayable on demand	7	4	—	1	12
Overdrafts	<u>(1)</u>	<u>(1)</u>	<u>—</u>	<u>—</u>	<u>(2)</u>
	6	3	—	1	10
Bank loans due after 1 year	(145)	59	14	3	(69)
Loan capital due after 1 year	(728)	(358)	10	(22)	(1,098)
Bank loans and loan capital due within 1 year	<u>(12)</u>	<u>12</u>	<u>(14)</u>	<u>(1)</u>	<u>(15)</u>
	(885)	(287)	10	(20)	(1,182)
Liquid resources	<u>346</u>	<u>30</u>	<u>—</u>	<u>(4)</u>	<u>372</u>
Debt net of cash and liquid resources	(533)	(254)	10	(23)	(800)
AUK Loan Notes	<u>187</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>187</u>
Group net debt	<u>(346)</u>	<u>(254)</u>	<u>10</u>	<u>(23)</u>	<u>(613)</u>

Liquid resources principally comprise short-term deposits.

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles

The Group's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United Kingdom ("UK GAAP") which differ in certain respects from United States generally accepted accounting principles ("US GAAP"). The significant differences as they apply to the Group are summarized below.

Fixed assets

The Group accounts for oil and gas exploration and development expenditure in accordance with the successful efforts method under UK GAAP which, except for the matters referred to below, conforms in all significant respects to US GAAP.

Exploration and appraisal expenditure

Under UK GAAP, successful efforts accounting, the Group initially capitalizes all costs relating to geological and geophysical ("G&G") activities and subsequently accounts for them in accordance with the policy for exploration and appraisal expenditure, except that expenditure on general seismic data and other costs not specifically related to an identified exploration license are expensed in the year in which they arise. Under US GAAP successful efforts accounting, G&G costs are expensed as incurred.

Under UK GAAP, exploration and appraisal expenditure is classified as an intangible asset until a decision is reached concerning the commercial viability of the field to which it relates. Expenditure is then either written off or transferred to tangible fixed assets. Under US GAAP, exploration and appraisal expenditure would be classified as tangible fixed assets from the time it is incurred.

Production assets

Under UK GAAP, the Group provides for depletion on production assets on a field by field basis on a unit of production method, in the proportion of actual production for the period to the total estimated proven and

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

probable reserves of the field, estimated at the commencement of the period. Under US GAAP successful efforts accounting, depletion of producing assets other than leasehold costs is calculated by reference to proved developed reserves only. Under US GAAP, leasehold costs are calculated by reference to proved reserves. Additionally, under US GAAP, only costs incurred in gaining access to proved developed reserves are depleted whereas, under UK GAAP, the costs to be depleted include estimated amounts in respect of future development costs based on price levels ruling at the balance sheet date.

Impairment of value

Under UK GAAP, successful efforts accounting, at each year end, management compares the net book amounts carried in respect of each field with the estimated undiscounted net realizable amount (net of tax and decommissioning costs) from commercial reserves within each field at year end prices. Any permanent impairment identified is provided against. Under US Statement of Financial Accounting Standards (“FAS”) 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of”, the US GAAP net book amounts carried in respect of each field are compared with the undiscounted net cash flows estimated by management. For those fields where deficits are identified, provision for impairment which is considered to be other than temporary is made by reference to the estimated discounted cash flows. For the purposes of the reconciliation below, FAS 121 was implemented in 1995 and resulted in a write down of the Claymore field group carrying value of £42 million. The £17 million write down of the Piper field group recognized under UK GAAP was not required under US GAAP as the US GAAP basis carrying value was below the UK GAAP carrying value. A net additional depletion charge of £25 million was therefore recognized under US GAAP in 1995. Both the Claymore and the Piper groups are within the UK fourth licensing round area.

Decommissioning provisions

Under UK GAAP, provision is made for the cost of decommissioning of Group-owned assets, using the unit of production method based on proven and probable reserves. Such provision represents the Group’s share of the estimated liability for costs which may be incurred in removing production platforms and facilities and site restoration costs at the end of the producing life of each field. Under US GAAP, provision for decommissioning is calculated by reference to proved reserves only.

Investment by a subsidiary in LASMO ordinary shares

Under UK GAAP the Group’s investment in LASMO plc shares is reported under fixed asset investments. Under US GAAP this investment would be deducted from shareholders’ equity.

Deferred taxation

LASMO provides for deferred taxation using the liability method, only to the extent that, in the opinion of the directors, it is probable that the tax liability will crystallize within the foreseeable future. Under US GAAP, deferred taxation is generally fully provided using the liability method. LASMO recognizes deferred tax assets only to the extent they are deemed to be recoverable in the foreseeable future. Under US GAAP, all deferred tax assets are recognized to the extent that it is more likely than not that ultimately they will be recoverable. In addition, deferred tax is provided under US GAAP on the difference between the accounting and tax bases of assets and liabilities of subsidiaries acquired. Further, to the extent it would be offsettable against the deferred tax liability provided under US GAAP, ACT would not be written off.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

Pension costs

The Group provides for the cost of retirement benefits based upon consistent percentages of employees' pensionable pay as recommended by actuaries. US GAAP requires that the projected benefit obligation be matched against the fair value of the plans' assets and be adjusted to reflect any unrecognized obligations or assets in determining the pension cost or credit for the year. No significant adjustments to profit for the year or shareholders' equity would be required under US GAAP with respect to the Group's plans.

Provision for reorganization costs

Under UK GAAP, in the year ended December 31, 1995, the Group provided £15 million for reorganization costs. Under US GAAP, this provision would not have been charged because the amount included therein relating to severance costs (£3 million) would only be recognized once the employees had been identified and informed and the balance, which relates to the cost of vacating properties, had not been incurred by December 31, 1995.

During the years ended December 31, 1997 and 1996 severance payments totaling £1 million and £2 million respectively, and other reorganization costs (relating primarily to the cost of vacating properties) of £7 million and £nil respectively were, under UK GAAP, set against the provision for reorganization costs. Under US GAAP these costs would have been included in the profit for the year.

Ordinary dividends

Under UK GAAP, final ordinary dividends, along with the related ACT, are provided in the year to which they relate. Under US GAAP dividends and the related ACT are not provided for until the dividend is declared.

Forward exchange contracts

Under US GAAP, the notional gain or loss arising on the translation of certain outstanding foreign currency forward exchange contracts at each balance sheet date, at the forward rates of exchange prevailing at that date, would have been included in the determination of net income. LASMO does not take account of such notional gains and losses. This difference between UK GAAP and US GAAP was not significant in any of the three years in the period ended December 31, 1997.

Investment in Unimar Company

Under UK GAAP the Group consolidates its 50% interest in Unimar Company on a proportionate basis. Under US GAAP this interest would be accounted for on the equity method.

Gain on interest rate swap

Under US GAAP, the gain on a close out of interest rate swaps used to hedge interest rate risk on the AUK Loan Notes still held at December 31, 1997 would have been deferred and spread over the remaining period of the swap. Under UK GAAP, the gain was included in profit for the year ended December 31, 1996.

Exceptional items

Under US GAAP, the profit on disposal of fixed assets and downstream (provision)/release ("exceptional items") would have been included in the determination of operating profit.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

The following is a summary of the adjustments to the profit for the year and shareholders' equity which would be required if US GAAP were to be applied instead of UK GAAP.

Profit for the year

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million, except per share amounts)		
Profit for the year as reported in the consolidated statement of income	<u>48</u>	<u>67</u>	<u>34</u>
Adjustments			
Exploration costs written off	(5)	(3)	—
Depletion	(34)	(82)	(123)
Provision for decommissioning	(3)	(2)	(1)
Deferred taxation	4	92	41
Advance corporation tax (written back)/written off	(6)	4	4
(Utilization)/provision for reorganization costs	(8)	(2)	15
Deferred gain on interest rate swaps	1	(2)	—
Other	<u>1</u>	<u>(2)</u>	<u>1</u>
	<u>(50)</u>	<u>3</u>	<u>(63)</u>
(Loss)/profit for the year as adjusted to accord with US GAAP	(2)	70	(29)
Preference dividends	<u>(12)</u>	<u>(16)</u>	<u>(19)</u>
(Loss)/profit for the year as adjusted to accord with US GAAP attributable to ordinary shareholders	<u>(14)</u>	<u>54</u>	<u>(48)</u>
Per ordinary share as so adjusted:			
Basic	(1.5)p	5.7p	(5.1)p
Diluted	<u>—</u>	<u>5.6p</u>	<u>—</u>
Per American Depositary Share(i):			
Basic	(4.5)p	17.1p	(15.3)p
Diluted	<u>—</u>	<u>16.8p</u>	<u>—</u>

(i) each American Depositary Share represents three ordinary shares of the Company.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

A reconciliation of the numerators and denominators of the basic and diluted US GAAP earnings per share calculations in accordance with FAS 128 “Earnings per share” is as follows:

	Year ended December 31		
	1997	1996	1995
Basic EPS calculation:			
Numerator, (loss)/profit for the year as adjusted to accord with US GAAP attributable to ordinary shareholders (£ million)	(14)	54	(48)
Denominator, ordinary shares outstanding (millions)	949	947	946
Diluted EPS calculation:			
Numerator, (loss)/profit for the year as adjusted to accord with US GAAP attributable to ordinary shareholders (£ million)	—	54	—
Denominator, ordinary shares outstanding (millions)	—	947	—
potential ordinary shares:			
employee stock options (millions)	—	8	—
	—	955	—

Shareholders' equity

	December 31	
	1997	1996
	(£ million)	
Shareholders' equity as reported in the consolidated balance sheet	1,276	1,260
Adjustments		
Current assets — other receivables	(6)	(5)
Fixed assets		
Investment by a subsidiary in LASMO ordinary shares	(28)	(32)
Intangible assets: exploration and appraisal	(26)	(21)
Tangible assets: oil and gas expenditure — cost	(294)	(280)
Tangible assets: oil and gas expenditure — accumulated depletion	143	162
Current liabilities — PRT and other taxation	6	5
Decommissioning provisions	(14)	(11)
Deferred taxation	(108)	(106)
Deferred gain on interest rate swap	(1)	(2)
Provision for reorganization costs	5	13
Ordinary dividend	22	19
	(301)	(258)
Shareholders' equity as adjusted to accord with US GAAP	975	1,002

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

Effect of proportionate consolidation of Unimar Company

The following summarized financial information shows the effect of the proportionate consolidation of Unimar Company, which is included in the Indonesia region:

	December 31, 1997		
	Group as presented in these financial statements	Effect of proportionate consolidation	As on equity basis
	(£ million)		
Consolidated balance sheet			
Current assets	639	(5)	634
Fixed assets	2,247	(9)	2,238
Current liabilities	327	(12)	315
Noncurrent liabilities	1,194	(3)	1,191
Provision for liabilities and charges	89	—	89
	Year ended December 31, 1997		
	Group as presented in these financial statements	Effect of proportionate consolidation	As on equity basis
	(£ million)		
Consolidated statement of income			
Sales	722	(83)	639
Gross profit	270	(40)	230
Operating profit	184	(41)	143
Associated company's profit	—	41	41
Consolidated statement of cash flows			
Net cash flow from operating activities	464	(74)	390
Returns on investments and servicing of finance	(64)	—	(64)
Taxation	(97)	34	(63)
Net cash (outflow)/inflow from capital expenditure and financial investment	(538)	6	(532)
Dividends paid — ordinary shares	(19)	—	(19)
Cash outflow before use of liquid resources and financing	(254)	(34)	(288)
	December 31, 1996		
	Group as presented in these financial statements	Effect of proportionate consolidation	As on equity basis
	(£ million)		
Consolidated balance sheet			
Current assets	595	(19)	576
Fixed assets	1,933	(28)	1,905
Current liabilities	269	(44)	225
Noncurrent liabilities	904	(3)	901
Provision for liabilities and charges	95	—	95

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

Effect of proportionate consolidation of Unimar Company — (continued)

	Year ended December 31, 1996		
	Group as presented in these financial statements	Effect of proportionate consolidation	As on equity basis
	(£ million)		
Consolidated statement of income			
Sales	749	(105)	644
Gross profit	282	(49)	233
Operating profit	208	(48)	160
Associated company's profit	—	48	48
Consolidated statement of cash flows			
Net cash flow from operating activities	454	(70)	384
Returns on investments and servicing of finance	(55)	—	(55)
Taxation	(122)	40	(82)
Net cash (outflow)/inflow from capital expenditure and financial investment	(28)	5	(23)
Net cash inflow from acquisitions and disposals	21	—	21
Dividends	(12)	—	(12)
Cash inflow/(outflow) before use of liquid resources and financing	258	(25)	233
Year ended December 31, 1995			
	Group as presented in these financial statements	Effect of proportionate consolidation	As on equity basis
	(£ million)		
Consolidated statement of income			
Sales	637	(87)	550
Gross profit	183	(37)	146
Operating profit	112	(36)	76
Associated company's profit	—	36	36
Consolidated statement of cash flows			
Net cash flow from operating activities	365	(53)	312
Returns on investments and servicing of finance	(49)	—	(49)
Taxation	(87)	31	(56)
Net cash (outflow)/inflow from capital expenditure and financial investment	(255)	6	(249)
Dividends paid — ordinary shares	(12)	—	(12)
Cash outflow before use of liquid resources and financing	(38)	(16)	(54)

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

Additional information in respect of deferred taxation

The components of the net deferred tax liability that would be recognized under FAS 109 are as follows:

	December 31	
	1997	1996
	(£ million)	
Deferred tax liability		
Accelerated depreciation for tax purposes	202	187
Roll-over relief — AUK Loan Notes	—	33
Overseas temporary differences	23	20
	225	240
Less: Advance corporation tax recoverable	(53)	(59)
	172	181
Deferred tax assets		
Net operating loss carry forwards	(277)	(295)
Other temporary differences	(28)	(35)
	(305)	(330)
Valuation allowance	248	259
	(57)	(71)
Net deferred tax liability under US GAAP*	115	110

* Noncurrent

Consolidated statement of cash flows

The consolidated statement of cash flows prepared in accordance with UK GAAP presents substantially the same information as that required under US GAAP. The statements differ, however, with regard to classification of items within the statements and as regards the definition of cash and cash equivalents.

Under UK GAAP, cash is defined as cash in hand and deposits repayable on demand less overdrafts repayable on demand. Under US GAAP, cash and cash equivalents would not include bank overdrafts but would include short-term deposits with initial maturities of less than three months. Under UK GAAP, cash flows are presented separately for operating activities, servicing of finance and returns on investments, taxation, capital expenditure and financial investment, acquisitions and disposals, equity dividends, management of liquid resources and financing. US GAAP, however, require only three categories of cash flow activity to be reported: operating, investing and financing. Cash flows from taxation and servicing of finance and returns on investments shown under UK GAAP would, with the exception of non equity dividends paid, be included as operating activities under US GAAP. The payment of dividends, equity and non equity, would be included as a financing activity under US GAAP. Cash flows in respect of capital expenditure and financial investment and acquisitions and disposals are included in investing activities under US GAAP. Under US GAAP, capitalized interest is treated as part of the cost of the asset to which it relates and thus included as part of investing cash flows; under UK GAAP all interest is treated as part of servicing of finance and returns on investments.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

Consolidated statement of cash flows — (continued)

The categories of cash flow activity under US GAAP can be summarized as follows:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)		
Cash flows from operating activities	330	306	270
Cash outflows on investing activities	(553)	(17)	(277)
Cash flows from financing activities	<u>184</u>	<u>(164)</u>	<u>(36)</u>
(Decrease)/increase in cash and cash equivalents	(39)	125	(43)
Effect of foreign exchange rate changes	—	(14)	(2)
Cash and cash equivalents at January 1	<u>340</u>	<u>229</u>	<u>274</u>
Cash and cash equivalents at December 31	<u><u>301</u></u>	<u><u>340</u></u>	<u><u>229</u></u>

Fair value of employee share option schemes

Under UK GAAP, no compensation expense is recognised on fixed share option schemes other than on options granted with attached stock appreciation rights which may, at the employees' option, be settled in cash or the issuance of shares. Had compensation costs been charged against income based on the fair value at the dates of grant for awards under the share option plans, consistent with the method of US Statement of Financial Accounting Standards No. 123, Group net income and earnings per share under US GAAP would have been as shown in the pro forma disclosures below:

	<u>Year ended December 31</u>		
	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million, except per share amounts)		
Net (loss)/income:			
As reported	(14)	54	(48)
Pro forma	(15)	53	(49)
Basic (loss)/earnings per share:			
As reported	(1.5)p	5.7p	(5.1)p
Pro forma	(1.6)p	5.6p	(5.1)p
Diluted earnings per share:			
As reported	—	5.6p	—
Pro forma	—	5.5p	—

The above pro forma net income and earnings per share calculations take no account of the impact on fair values of performance tests which will determine whether certain of such options are in fact exercisable, nor of any capitalization of compensation costs as part of exploration or development costs, nor of any recoveries from joint ventures operated by the Group. They therefore only represent approximations of the position which would have resulted had the Group adopted fair value based accounting for options granted and to the eventual outcome which will result from exercise of options in due course.

LASMO plc AND SUBSIDIARY COMPANIES

NOTES TO THE FINANCIAL STATEMENTS — (Continued)

Note 29 — Differences between accounting principles generally accepted in the United Kingdom and United States generally accepted accounting principles — (continued)

New Accounting Standards — UK

Associates and joint ventures: In November 1997, the Accounting Standards Board published Financial Reporting Standard No. 9 “Associates and joint ventures” (“FRS 9”). FRS 9 revises the rules governing the consolidation of associates and trading joint ventures into group accounts, is effective for accounting periods ending on or after June 23, 1998 and requires restatement of prior period financial information. The adoption of FRS 9 will result in the Group’s 50% investment in Unimar Company being accounted for on the gross equity method which is comparable to the equity method of accounting under US GAAP. The effects of this standard on the Group consolidated statements of income and cash flows for the three years ended December 31, 1997 and the consolidated balance sheet at December 31, 1997 and 1996 are shown above under “Effect of proportionate consolidation of Unimar Company”.

New Accounting Standards — US

Reporting comprehensive income: In June 1997, the FASB issued Statement No. 130, “Reporting Comprehensive Income” (“FAS 130”). FAS 130 establishes standards for the reporting and display of comprehensive income, is effective for accounting periods beginning after December 15, 1997 and requires reclassification of prior year financial information. The adoption of FAS 130 will have no impact on the Group’s results of operations or financial position as adjusted to accord with US GAAP.

Segmental reporting: In June 1997, the FASB issued Statement No. 131, “Disclosures about Segments of an Enterprise and Related Information” (“FAS 131”); effective for accounting periods beginning after December 15, 1997 and requiring reclassification of prior period financial information. FAS 131 establishes standards concerning the way information about operating segments is reported in annual financial statements and requires the inclusion of selected information about operating segments in interim financial reports. It also establishes standards for related disclosures about products and services, geographic areas and major customers. The Company has not yet determined the disclosure format that it will adopt. The adoption of FAS 131 will have no impact on the Group’s results of operations or financial position as adjusted to accord with US GAAP.

Pensions and other post-retirement benefits: In February 1998 the FASB issued Statement No. 132 “Employers Disclosures about Pensions and Other Post-retirement Benefits” (“FAS 132”). This statement revises employers’ disclosures about pension and other post-retirement benefit plans, without changing the measurement or recognition of those plans. FAS 132 is effective for accounting periods beginning after December 15, 1997 and requires, except where information is not readily available, restatement of prior year financial information. The adoption of FAS 132 will have no effect on the Group’s results of operations or financial position as adjusted to accord with US GAAP.

Computer software costs: In March 1998, the American Institute of Certified Public Accountants issued Statement of Position No. 98-1 “Accounting for the Cost of Computer Software Developed For or Obtained For Internal Use” (“SOP 98-1”). This statement establishes standards regarding the capitalization of certain costs incurred in connection with developing or obtaining software for internal use. Under current practice, the company generally expenses such costs as incurred. SOP 98-1 is effective for accounting periods beginning after December 15, 1998 and is to be applied prospectively. Early adoption of SOP 98-1 is permitted. The Company has not yet determined the impact of adopting SOP 98-1 on the Group’s future results of operations and financial position as adjusted to accord with US GAAP.

LASMO plc AND SUBSIDIARY COMPANIES

SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND NATURAL GAS PRODUCING ACTIVITIES (UNAUDITED)

The following supplemental information on oil and gas exploration and production activities of the Group is presented in accordance with FASB Statement No. 69 — “Disclosures about Oil and Gas Production Activities” (“FAS 69”). Reserves and production figures quoted are on an entitlement basis unless otherwise stated.

Oil and gas reserve quantities

The Group’s estimated proved developed and undeveloped reserves of oil and gas and changes thereto for the years 1997, 1996 and 1995 and proved developed reserves of oil and gas are set forth in the following tables. For each of the three years 1995, 1996 and 1997 oil and gas reserves in Sanga Sanga, Indonesia were estimated by petroleum engineers employed by LASMO, based on gross oil and wet gas reserves which are estimated by DeGolyer and MacNaughton, independent petroleum engineering consultants.

There are numerous uncertainties inherent in estimating quantities of reserves and in projecting future rates of production and timing of development expenditures, including many factors beyond the control of the producer. The reserve data set forth in this Annual Report only represents estimates. Reserve engineering is a subjective process of estimating underground accumulations of oil and gas that cannot be measured in an exact way, and the accuracy of any reserve estimate is a function of the quality of available data and of engineering and geological interpretation and judgement. As a result, estimates of different engineers often vary. In addition, results of drilling, testing and production subsequent to the date of an estimate may justify revision of such estimates. Accordingly, reserve estimates at a specific point in time are often different from the quantities of oil and gas that are ultimately recovered. In addition, the estimates of future net revenues from proved reserves of the Group and the present value thereof are based upon certain assumptions about future production levels, prices and costs that may not prove correct over time. Predictions about future prices and production levels are subject to great uncertainty. The meaningfulness of such estimates is highly dependent upon the accuracy of the assumptions upon which they are based. Net proved reserves of crude oil and natural gas exclude production royalties due to others.

Information regarding Indonesian reserves relates principally to LASMO’s net interest in a production sharing contract between an Indonesian joint venture and Pertamina which includes the Sanga Sanga PSC. The joint venture has no ownership interest in the reserves but does have the right to share revenues and production and is entitled to recover most field and other operating and capital costs. The reserve estimates are subject to revision as prices fluctuate due to the cost recovery feature under the production sharing contract. Debt relating to the LNG processing facilities owned by Pertamina is serviced from proceeds of LNG sales prior to distribution of such proceeds primarily to the members of the joint venture and Pertamina. The debt obligation is that of Pertamina and not the joint venture. Debt service relating to such facilities is accounted for by LASMO as a cost of production and operation. Such debt service is deducted in estimating future net revenues to be distributed among Pertamina and the production sharing contractors including the joint venture.

Information regarding Venezuelan reserves (included under “International” in the following tables) relates to LASMO’s interest in an operating agreement for the Dacion Area between LASMO and a subsidiary of Petroleos de Venezuela SA (PDVSA). LASMO has no ownership interest in oil reserves but instead will receive a service fee based upon production and calculated in accordance with the terms of the operating agreement. The agreement allows for full recovery of capital and operating costs out of production. Remaining profit will be shared with the government on a rate of return basis set forth in the agreement. A company sponsored by PDVSA and formed for the purpose of investing in the Venezuelan energy sector has an option to participate at the level of a 10% interest in the operating agreement. The reserves have been presented on a gross basis after taking account of such contractual back-in rights.

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Net proved reserves of crude oil

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(millions of barrels)			
At January 1, 1995	127.8	43.9	44.2	215.9
Revisions of previous estimates	12.5	(1.9)	6.2	16.8
Extensions, discoveries and other	—	—	19.4	19.4
Sales of reserves in place	(2.2)	(9.0)	—	(11.2)
Production for the year	<u>(17.1)</u>	<u>(3.4)</u>	<u>(8.0)</u>	<u>(28.5)</u>
At December 31, 1995	121.0	29.6	61.8	212.4
Revisions of previous estimates	4.1	4.3	6.0	14.4
Extensions, discoveries and other	—	—	49.5	49.5
Sales of reserves in place	—	—	(6.7)	(6.7)
Purchases of reserves in place	0.1	—	—	0.1
Production for the year	<u>(21.2)</u>	<u>(3.4)</u>	<u>(3.8)</u>	<u>(28.4)</u>
At December 31, 1996	104.0	30.5	106.8	241.3
Revisions of previous estimates	26.8	2.1	20.4	49.3
Extensions, discoveries and other	—	—	31.4	31.4
Sales of reserves in place	—	—	(2.4)	(2.4)
Purchases of reserves in place	—	—	236.8	236.8
Production for the year	<u>(24.9)</u>	<u>(3.5)</u>	<u>(3.9)</u>	<u>(32.3)</u>
At December 31, 1997	<u>105.9</u>	<u>29.1</u>	<u>389.1</u>	<u>524.1</u>
<i>Proved developed reserves</i>				
December 31, 1995	55.9	25.6	13.5	95.0
December 31, 1996	68.2	26.9	23.4	118.5
December 31, 1997	<u>86.4</u>	<u>27.4</u>	<u>87.7</u>	<u>201.5</u>

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Net proved reserves of natural gas

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(billions of cubic feet)			
At January 1, 1995	584.5	1,610.3	102.8	2,297.6
Revisions of previous estimates	12.2	(27.0)	(41.3)	(56.1)
Extensions, discoveries and other	0.2	—	—	0.2
Purchases of reserves in place	20.1	—	—	20.1
Production for the year	<u>(47.3)</u>	<u>(133.5)</u>	<u>(7.3)</u>	<u>(188.1)</u>
At December 31, 1995	569.7	1,449.8	54.2	2,073.7
Revisions of previous estimates	23.0	11.7	(5.5)	29.2
Purchases of reserves in place	8.7	—	—	8.7
Production for the year	<u>(59.9)</u>	<u>(143.9)</u>	<u>(9.5)</u>	<u>(213.3)</u>
At December 31, 1996	541.5	1,317.6	39.2	1,898.3
Revisions of previous estimates	(47.8)	121.3	(0.9)	72.6
Extensions, discoveries and other	—	—	160.0	160.0
Production for the year	<u>(58.4)</u>	<u>(117.0)</u>	<u>(9.3)</u>	<u>(184.7)</u>
At December 31, 1997	<u>435.3</u>	<u>1,321.9</u>	<u>189.0</u>	<u>1,946.2</u>
<i>Proved developed reserves</i>				
December 31, 1995	127.4	1,220.6	54.2	1,402.2
December 31, 1996	310.1	1,087.2	36.4	1,433.7
December 31, 1997	<u>388.5</u>	<u>1,052.9</u>	<u>27.1</u>	<u>1,468.5</u>

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Net proved reserves of crude oil and natural gas combined

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(millions of barrels of oil equivalent(i))			
At January 1, 1995	225.2	312.4	61.3	598.9
Revisions of previous estimates	14.6	(6.5)	(0.7)	7.4
Extensions, discoveries and other	—	—	19.4	19.4
Sales of reserves in place	(2.2)	(9.0)	—	(11.2)
Purchases of reserves in place	3.4	—	—	3.4
Production for the year	<u>(25.0)</u>	<u>(25.7)</u>	<u>(9.2)</u>	<u>(59.9)</u>
At December 31, 1995	216.0	271.2	70.8	558.0
Revisions of previous estimates	7.9	6.3	5.1	19.3
Extensions, discoveries and other	—	—	49.5	49.5
Sales of reserves in place	—	—	(6.7)	(6.7)
Purchases of reserves in place	1.6	—	—	1.6
Production for the year	<u>(31.2)</u>	<u>(27.4)</u>	<u>(5.4)</u>	<u>(64.0)</u>
At December 31, 1996	194.3	250.1	113.3	557.7
Revisions of previous estimates	18.8	22.3	20.3	61.4
Extensions, discoveries and other	—	—	58.1	58.1
Sales of reserves in place	—	—	(2.4)	(2.4)
Purchases of reserves in place	—	—	236.8	236.8
Production for the year	<u>(34.6)</u>	<u>(23.0)</u>	<u>(5.5)</u>	<u>(63.1)</u>
At December 31, 1997	<u>178.5</u>	<u>249.4</u>	<u>420.6</u>	<u>848.5</u>
<i>Proved developed reserves</i>				
December 31, 1995	77.1	229.0	22.6	328.7
December 31, 1996	119.9	208.1	29.5	357.5
December 31, 1997	<u>151.2</u>	<u>202.9</u>	<u>92.2</u>	<u>446.3</u>

(i) Gas reserves have been converted at 6,000 cubic feet to 1 barrel of oil equivalent.

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Capitalized costs related to oil and gas producing activities

The following table summarizes capitalized costs for oil and gas exploration and production activities, and the related accumulated depreciation, depletion and amortization, under UK GAAP.

	<u>UK</u>	<u>Indonesia</u>	<u>International</u>	<u>Total</u>
	(£ million)			
At December 31, 1997				
Unproved properties	28	1	28	57
Proved properties	<u>1,782</u>	<u>914</u>	<u>542</u>	<u>3,238</u>
Total before depreciation, depletion and amortization	1,810	915	570	3,295
Accumulated depreciation, depletion and amortization	<u>(871)</u>	<u>(378)</u>	<u>(74)</u>	<u>(1,323)</u>
Net capitalized costs	<u>939</u>	<u>537</u>	<u>496</u>	<u>1,972</u>
At December 31, 1996				
Unproved properties	8	3	24	35
Proved properties	<u>1,691</u>	<u>861</u>	<u>219</u>	<u>2,771</u>
Total before depreciation, depletion and amortization	1,699	864	243	2,806
Accumulated depreciation, depletion and amortization	<u>(714)</u>	<u>(310)</u>	<u>(109)</u>	<u>(1,133)</u>
Net capitalized costs	<u>985</u>	<u>554</u>	<u>134</u>	<u>1,673</u>

Costs incurred in crude oil and natural gas property acquisition, exploration and development activities

The following table sets forth costs incurred in oil and gas property acquisition, exploration and development activities under UK GAAP.

	<u>UK</u>			<u>Indonesia</u>			<u>International</u>			<u>Total</u>		
	Year ended December 31											
	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>
	(£ million)											
Property acquisitions												
unproved	—	—	2	—	—	—	—	—	—	—	—	2
proved	2	8	1	—	—	—	289	—	—	291	8	1
Property disposals												
unproved	—	—	—	—	—	—	—	—	—	—	—	—
proved	—	—	(2)	—	—	(25)	(4)	(33)	—	(4)	(33)	(27)
Exploration and appraisal	37	22	11	6	2	3	52	51	40	95	75	54
Development	<u>94</u>	<u>119</u>	<u>211</u>	<u>22</u>	<u>17</u>	<u>20</u>	<u>68</u>	<u>17</u>	<u>16</u>	<u>184</u>	<u>153</u>	<u>247</u>
Total costs incurred	<u>133</u>	<u>149</u>	<u>223</u>	<u>28</u>	<u>19</u>	<u>(2)</u>	<u>405</u>	<u>35</u>	<u>56</u>	<u>566</u>	<u>203</u>	<u>277</u>

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Results of operations for crude oil and natural gas producing activities

The following table sets forth the results of operations of crude oil and natural gas producing activities under UK GAAP.

	UK			Indonesia			International			Total		
	Year ended December 31											
	1997	1996	1995	1997	1996	1995	1997	1996	1995	1997	1996	1995
	(£ million)											
Sales(i)	405	350	255	272	344	285	45	55	97	722	749	637
Operating costs	(103)	(84)	(70)	(65)	(83)	(81)	(12)	(17)	(39)	(180)	(184)	(190)
Royalties	(11)	(12)	(13)	(7)	(9)	(6)	(8)	(10)	(10)	(26)	(31)	(29)
PRT	(5)	(10)	(5)	—	—	—	—	—	—	(5)	(10)	(5)
Depletion	(158)	(143)	(140)	(57)	(72)	(64)	(18)	(19)	(16)	(233)	(234)	(220)
Decommissioning	(8)	(8)	(8)	—	—	—	—	—	(2)	(8)	(8)	(10)
Exploration costs written off	(18)	(16)	(10)	(8)	(3)	(4)	(28)	(27)	(20)	(54)	(46)	(34)
Profit/(loss) on disposal	—	—	15	—	—	(1)	—	20	—	—	20	14
Result before taxes	102	77	24	135	177	129	(21)	2	10	216	256	163
Allocable taxes	(7)	(7)	(8)	(89)	(116)	(88)	(3)	(3)	(3)	(99)	(126)	(99)
Results of operations	<u>95</u>	<u>70</u>	<u>16</u>	<u>46</u>	<u>61</u>	<u>41</u>	<u>(24)</u>	<u>(1)</u>	<u>7</u>	<u>117</u>	<u>130</u>	<u>64</u>

(i) Includes tariff income

Results of operations include revenues and expenses associated directly with LASMO's crude oil and natural gas exploration and producing activities. They do not include interest expense or income or corporate administration expenses, nor their associated tax effects. As a result of this, the results of operations are not necessarily indicative of the contribution to consolidated profit after tax of these activities.

Changes in standardized measure of discounted future net cash flows

The standardized measure of discounted future net cash flows related to proved crude oil and natural gas reserves is calculated in accordance with the requirements of FAS 69 and uses reserve definitions as prescribed therein. Estimated future cash flows from production are computed in applying year end prices for crude oil and natural gas and year end exchange rates to year end quantities of estimated net proved reserves. Future price changes are limited to those provided by contractual arrangements in existence at the end of the reporting year. Future development and production costs are those estimated future expenditures necessary to develop and produce year end estimated proved reserves based on year end price levels and assuming the continuance of year end economic conditions. Future production costs include estimated decommissioning liabilities. Estimated future taxes are calculated by applying appropriate year end statutory tax rates and reflect allowable deductions, tax credits and the tax basis of related assets. Discounted future net cash flows are calculated using 10% mid-period discount factors.

The information provided below does not represent management's estimate of the Group's expected future cash flows or value of proved reserves. Estimates of proved reserve quantities are imprecise and change over time as new information becomes available and, in particular, probable and possible reserves, which may become proved reserves in due course, are excluded from the calculations. Also, assumptions have been made regarding the timing of future production and the timing and amount of future development and production costs. The calculations assume that economic conditions existing at the end of the reporting year will continue. Other different but equally valid assumptions might lead to significantly different final results.

LASMO plc AND SUBSIDIARY COMPANIES

**SUPPLEMENTARY DISCLOSURES RELATING TO CRUDE OIL AND
NATURAL GAS PRODUCING ACTIVITIES — (Continued)
(UNAUDITED)**

Therefore, although it is calculated in accordance with FAS 69, the Company cautions against the placing of unwarranted reliance on this information in view of the highly arbitrary nature of the assumptions on which it is based.

	UK			Indonesia			International			Total		
	Year ended December 31											
	1997	1996	1995	1997	1996	1995	1997	1996	1995	1997	1996	1995
Future cash inflows	1,951	2,554	2,545	2,173	2,960	2,555	2,518	1,364	812	6,642	6,878	5,912
Future production costs	(960)	(996)	(1,059)	(426)	(485)	(429)	(721)	(245)	(283)	(2,107)	(1,726)	(1,771)
Future development costs	(115)	(89)	(171)	(102)	(52)	(87)	(614)	(273)	(111)	(831)	(414)	(369)
Future tax expenses	(72)	(162)	(133)	(736)	(1,082)	(910)	(32)	(5)	(5)	(840)	(1,249)	(1,048)
Undiscounted future net cash flows	804	1,307	1,182	909	1,341	1,129	1,151	841	413	2,864	3,489	2,724
10% discount	(195)	(337)	(322)	(456)	(690)	(560)	(767)	(484)	(200)	(1,418)	(1,511)	(1,082)
Standardized measure of discounted future net cash flows	<u>609</u>	<u>970</u>	<u>860</u>	<u>453</u>	<u>651</u>	<u>569</u>	<u>384</u>	<u>357</u>	<u>213</u>	<u>1,446</u>	<u>1,978</u>	<u>1,642</u>

The following are the principal changes in the standardized measure of discounted future net cash flows during the years ended December 31, 1997, 1996 and 1995.

	Total		
	1997	1996	1995
	(£ million)		
Present value at January 1	1,978	1,642	1,293
Sales of crude oil and natural gas produced, net of production costs (including PRT)	(501)	(532)	(409)
Net changes in prices and production costs(i)	(874)	421	367
Extensions and discoveries, less related costs(i)	72	55	78
Development costs incurred	138	72	252
Revisions of previous quantity estimates(i)	130	260	15
Changes in future development costs(ii)	(1)	(46)	(79)
Purchase of reserves in place(i)	14	9	7
Sales of reserves in place(i)	(10)	(29)	(18)
Accretion of discount(i)	244	203	182
Net changes in taxes	232	(89)	(44)
Other	<u>24</u>	<u>12</u>	<u>(2)</u>
Net change for the year	<u>(532)</u>	<u>336</u>	<u>349</u>
Present value at December 31	<u>1,446</u>	<u>1,978</u>	<u>1,642</u>

(i) Net changes in prices and production costs, extensions and discoveries, future development costs, revisions, purchases and sales of reserves in place and accretion of discount are stated pre-tax. The associated tax effects are all included within net changes in taxes, as are taxes associated with net revenues and costs for the period.

(ii) Changes in future development costs in production sharing contracts in Indonesia and Gabon ultimately affect a contractor's entitlement production. These changes have therefore been accounted for as revisions of previous quantity estimates.