KERN RIVER plc

DIRECTORS' REPORT AND ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2000

Company Number: 3262305

KERN RIVER plc

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KERN RIVER plc

CHAIRMAN'S STATEMENT

I am pleased to be able to report that the Company has made substantial progress in recent months.

As most shareholders will be aware, the prevailing oil prices in 1998 and 1999 forced the Group to adopt a minimal overhead, survival strategy. During the course of last year oil prices firmed very substantially, enabling a profit to be made in the period to 30 September 2000 in spite of the low level of production available. More importantly, the improved outlook for average oil prices provided the background to propose active development of the Company's proven asset base. Following the end of the financial year we completed a Placing and Open Offer which raised £2.7m net, enabling us to remove our historic debt burden and finance a substantial production enhancement programme at the Starks Field.

We are now also in a position to consider ways to unlock the substantial value at our Nukern Lease and to quantify natural gas prospects at Starks. Kern River has been re-activated and we are ambitious to build shareholder value rapidly by exploiting the existing assets by selective acquisitions.

In the year ended 30 September 2000 the Group achieved gross production of 63,510 barrels (1999: 61,000 barrels) nearly all of which arose at the Starks Field. Production at the Nukern Lease remained at a minimal level. Turnover was £685,441 (1999: £340,147) and profit on ordinary activities before tax was £117,784 (1999: loss £195,903).

During the period oil prices recovered from the low levels of the previous years. Production at Starks Field realised an average price of $22.37 per barrel for the year (1999: $12.03) and the price per barrel was $27.50 at 30 September 2000. Since the year end prices have fluctuated and were $27.50 at 5 February 2001, the latest practicable date prior to printing this report. We expect that oil prices will continue to fluctuate but believe that the improved prospects for average oil prices provides clear support for our development programme at the Starks Field.

The Group's independent petroleum engineers have reviewed its oil reserves at 30 September 2000 and have assessed the proven reserves at 5.3 million barrels (1999: 5.3 million barrels) with a net present value to the Group of $55 million (£37 million) at a discount rate of 10 per cent. and assuming constant oil prices of $27.50 per barrel at Starks and $25.75 per barrel at Nukern. More details of the petroleum engineers' review are contained in the operational review.

The development programme at the Starks Field covers a three year period and is planned to increase production at the field from 185 barrels per day in the first half of September 2000 to a peak of approximately 585 barrels per day. I am pleased to report that the development programme commenced in December 2000.

We intend to seek opportunities to build the Group through the acquisition of additional businesses and assets. In addition to considering producing oil assets in the United States where such can be secured on attractive terms, we also intend to consider other energy related businesses and other opportunities which present the potential for substantial growth in shareholder value.

I was appointed Chairman at the time of the Placing and Open Offer in November last year. I would like to give credit to my predecessor, Neville A. Brown, to Anthony Carroll, and to the other directors for their steadfast and prudent management of the Group, particularly in the very difficult trading conditions of previous periods. I would also like to take this opportunity to thank shareholders for their support of Kern River during the past year and all who supported the placing and open offer which provides the platform for the Company's rapid development.

I expect to be able to report positive progress during the coming year.

Stuart Bickerstaff

Chairman

6 February 2001

OPERATIONAL REVIEW

CSV Holdings, Inc. ("CSV") is a wholly-owned subsidiary of Kern River plc which owns the Group's two oil field interests: the Starks Field and the Nukern Lease. At both locations CSV sub-contracts operational activities to Churchill Energy, Inc., an external operator, whose services are provided through Joint Operating Agreements. CSV maintains close control on activities.

Starks Field, Louisiana (Proven Reserves: 1.07 million barrels net, as at 30 September 2000)

The Starks Lease comprises 680 acres located on top of a salt dome in Calcasieu Parish, Louisiana. CSV acquired its interest in the second half of 1996 and our development of the field began in January 1997 following flotation of Kern River plc.

In the year ended 30 September 2000, CSV achieved gross production of 63,510 barrels. Oil prices began a slow but steady improvement during late 1999 which continued into 2000. Gross oil sales from Starks in the year of $1,477,000 approximately doubled the revenue received in 1999 on comparable sales volume.

During the period we used some of the cash flow generated by the improved operating results to initiate two flank-well recompletions. One of the recompletions resulted in what appears to be a gas reservoir discovery. We are currently evaluating the prospects for commercial exploitation of the natural gas reservoir. The second recompletion resulted in the discovery of four potential oil intervals between 3300 - 3840 feet within the common well bore. The balance of the effort during the year on the shallow producing area consisted of installation of a gas vent system to relieve casing head gas build up in the wells, thereby improving down hole equipment performance and overall longer-life of the components.

Permits were filed during the year to drill and complete three shallow caprock wells. At year-end, two of the three wells had been drilled and cased. CSV has its own drilling rig for this type of shallow well; therefore, it is not subject to the industry-wide shortage of available equipment for drilling and completion of such wells. The drilling rig is rated at 1500 feet and was overhauled during the year.

A number of exploration prospects remain at Starks, including the rim area which lies between the crest of the dome and the flanks. In the 1930's and early 1940's a large number of wells were drilled along the rim down to 2000 feet to exploit the caprock sulphur deposits. Drillers' logs for a number of these wells evidence the presence of oil and gas, which, upon further analysis, suggest oil accumulations in five concentrated areas on the rim.

In December 2000 we began implementation of the three year development plan at Starks. The plan involves the drilling of 25 new wells and recompletion of seven existing wells on the caprock and of 10 flank wells. It also involves enhancement of the salt water disposal facilities and initiation of a reservoir pressure maintenance programme.

Nukern Lease, California (Proven Reserves: 4.27 million barrels net, as at 30 September 2000)

The Nukern Lease consists of 55 acres of land in the South West portion of the Kern River Field, which is in Bakersfield, California. CSV's working interest stands at 93.4% with a net revenue interest of 77.84% after allowing for payments to the mineral owners.

For the period under review and prior periods, production at Nukern has been targeted at the minimum necessary to maintain the lease.

The Nukern reserves are of heavy viscosity oil (API 13 degrees), requiring the application of Enhanced Oil Recovery techniques. Most local fields utilise some form of steam heating. CSV favours adoption of the same steamflood technique which has been employed successfully by Arco and Texaco on neighbouring leases, including Texaco's substantial activity along our property lease line. This approach to Enhanced Recovery is reflected in the above latest estimate of Proven Reserves (made by independent Petroleum Consulting Engineers).

Whilst it remains necessary to invest in steam generation on the Nukern lease, much of the other infrastructure for steam injection into the wells, oil/water separation, water injection and storage is already in place. Key personnel, with excellent knowledge and experience of the Kern River reservoirs, have been retained. Accordingly, CSV has been in a position to continue to satisfy regulatory requirements and has the capacity to prepare exploitation plans.

Development of the Nukern lease is most likely to be achieved through a joint venture or farm-out arrangement. Posted prices for the Kern River AP1 13 gravity oil ranged from a low of $16.50 per barrel to a high of $30.50 for the year ended 30 September 2000.

At 5 February 2001, the latest practicable date prior to printing this report, the prices of oil were $19.75 per barrel at Nukern and $27.50 per barrel at Starks.

Anthony J Carroll

General Manager

6 February 2001

KERN RIVER plc

OFFICERS AND ADVISERS

DIRECTORS	Stuart W. Bickerstaff (Non Executive, Chairman) Anthony Carroll Garry Butterfield Neville A. Brown (Non Executive) Colin Weaver (Non Executive)
SECRETARY	Garry Butterfield
BANKERS	Bank of Scotland 124 Colmore Row Birmingham B3 3AU
AUDITORS	BDO Stoy Hayward 8 Baker Street London W1U 3LL
REGISTERED OFFICE	Cooper Street Wolverhampton WV2 2JL
CONSULTING PETROLEUM ENGINEERS	SAVAGEngineers 7291 S. Highland Littleton, Colorado 80120 U.S.A.
REGISTRARS	Northern Registrars Limited Northern House Woodsome Park Fenay Bridge Huddersfield HD8 0LA
NOMINATED ADVISER AND AND NOMINATED BROKER	Marshall Securities Limited Crusader House 145-157 St John Street London EC1V 4RE

KERN RIVER plc

DIRECTORS' PROFILES

Stuart Bickerstaff

Stuart Bickerstaff, aged 59 is Non-Executive Chairman of the Company and was appointed to the board on 15 November 2000. Stuart Bickerstaff was founder and managing director of Lamar UK Limited, a company involved in the supply of materials and services to the printed circuit board industry, from 1984 to 1997 when the company was sold. Prior to this he was chief executive of a number of companies in the electronics and publishing industries. Stuart Bickerstaff is a non-executive director of Ultrasis plc.

Anthony Carroll

Anthony Carroll, aged 64, is an Executive Director and General Manager of the Company and was appointed to the Board on 6 November 1996. Anthony Carroll holds a BSc from West Texas Agriculture and Mechanical University. He worked from 1961 to 1981 for the Bureau of Mines in the US Department of Interior. From 1984, until he resigned in 1990, he was President and Chairman of the Board of Churchill Technology, Inc., an oil and gas company based in Denver. Since June 1990 Anthony Carroll has been Chairman of the Board, Chief Executive and President of Caspen Oil, Inc. As General Manager he provides Kern River with the benefit of his particular knowledge and experience of the industry in the USA.

Garry Butterfield

Garry Butterfield, aged 41, is Finance Director and Company Secretary of the Company. He was appointed to the Board on 6 November 1996. He qualified as a chartered accountant in 1986 after training with Longcrofts. He joined Villiers Limited in 1989 and from 1994 to 1999 he was a director of Villiers Group plc (now Ultrasis plc). Garry Butterfield is a director of a private engineering company and provides his services on a part time basis to the Company.

Neville A. Brown

Neville A. Brown, aged 61, is an independent non-Executive Director of the Company and was appointed to the Board on 6 November 1996. He has worked within the Shell group of companies for forty years. From 1989, until his retirement at the end of 1995, he was appointed Head of Commercial Business Development with Shell UK Exploration and Production. Now a consultant, he is providing Kern River with the benefit of his long and varied career in the oil industry. Neville A. Brown was a non-Executive Director of Gall Thomson Environmental plc from July 1996 until December 1999. He is Chairman of the Remuneration Committee and a member of the Audit Committee.

Colin Weaver

Colin Weaver, aged 68, is an independent non-Executive Director of the Company and was appointed to the Board on 6 November 1996. He has worked for over thirty years as a stock jobber and market maker in the London Stock Exchange of which he became a member in 1963. He was a partner with Pinchin Denny & Co before it became Morgan Grenfell Securities, where he joined as Senior Assistant Director. Colin Weaver is a Member of the Securities Institute (MSI) and maintains an active interest in the Stock Market. Colin Weaver is Chairman of the Audit Committee and a member of the Remuneration Committee.

KERN RIVER plc

DIRECTORS' REPORT

The Directors submit their report and the accounts for the year to 30 September 2000.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The principal activity of the Group during the year was the management of two established producing oil fields in the USA. Details of this activity are included in the operational review.

RESULTS AND DIVIDENDS

The profit for the period after taxation was £115,834 (1999: loss £199,721).
The Directors are unable to recommend the payment of a dividend and therefore the balance on the profit and loss account has been carried forward.

CREDITOR PAYMENT POLICY

The Group seeks to maintain good terms with all of its trading partners. In particular, it is the Group's policy to agree appropriate terms and conditions for its transactions with suppliers, and provided the supplier has complied with them, to abide by the terms of payment agreed. For the Company the number of days' purchases outstanding at 30 September 2000 was 142 (1999: nil).

IMPORTANT EVENTS SINCE THE YEAR END

On 18 October 2000 the Company announced that it was raising £2.7 million net of expenses by way of a placing and open offer to repay its borrowings and to finance a development programme at the Starks Field in order to increase production substantially. Under the placing and open offer the Company issued 11,500,000 new ordinary shares at 25p per share. The placing and open offer was described in the prospectus issued on 18 October 2000, and was approved by shareholders at an extraordinary general meeting held on 14 November 2000. The placing and open offer was completed on 15 November 2000 with the result that the Group has settled all of its borrowings, which were from Ultrasis plc, a founder shareholder. Settlement was in the form of £1.5million cash and the issue of a $1million production note. Repayment of the production note is to commence at the later of 1 January 2004 or the date at which C.S.V. Holdings, Inc. has received $6million in profit from Starks Field. Payments will then be made quarterly equal to 20% of the net production revenue in the period, up to the value of $1million plus accrued interest charged at the rate of 5.84% per annum.

At the extraordinary general meeting on 14 November 2000 shareholders also approved, subject to Court confirmation, the reduction of the share premium account by £241,810 to create a reserve against which the deficit on the profit and loss account as at 31 March 2000 of the same amount may be set off. The application to the Court is in progress at this time and it is expected that the order of the Court confirming the reduction of share premium account will be made in the middle of February 2001.

KERN RIVER plc

DIRECTORS' REPORT *(Continued)*

IMPORTANT EVENTS SINCE THE YEAR END *(Continued)*

The following is a pro forma statement of the net assets of the Group following the Placing and Open Offer as if it had taken place at 30 September 2000. The pro forma has been prepared for illustrative purposes and is not intended to show the actual financial position of the Group following the Placing and Open Offer as all other transactions entered into by the Group between 30 September 2000 and 15 November 2000 are not reflected. The pro forma statement should be read in conjunction with the notes below.

Notes	(1)	(2)	(3)	(4)
	The Group	Placing and Open Offer	Repayment of loans	Pro forma
	£	£	£	£
Fixed assets				
Tangible assets	7,351,374	-	-	7,351,374
Current assets				
Debtors	123,611	-	-	123,611
Cash at bank	240,460	2,735,000	(1,500,049)	1,475,411
	364,071	2,735,000	(1,500,049)	1,599,022
Creditors: amounts falling due within one year				
Borrowings	(2,190,952)	-	2,190,952	-
Other creditors	(248,469)	-	-	(248,469)
	(2,439,421)	-	2,190,952	(248,469)
Net current assets/(liabilities)	(2,075,350)	2,735,000	690,903	1,350,553
Total assets less current liabilities	5,276,024	2,735,000	690,903	8,701,927
Creditors: amounts falling due after more than one year				
Borrowings	-	-	-	-
Other creditors	-	-	(690,903)	(690,903)
	-	-	(690,903)	(690,903)
Net assets	5,276,024	2,735,000	-	8,011,024

IMPORTANT EVENTS SINCE THE YEAR END *(Continued)*

Notes to pro forma statement of net assets

1 Column 1 represents the consolidated balance sheet of the Group at 30 September 2000 as extracted from the audited accounts for the year then ended.

2	The figures in column 2 represent the proceeds of the Placing and Open Offer as follows:	£
	Gross proceeds of issue of 11,500,000 new shares at 25 p	2,875,000
	Expenses of issue	(140,000)
	Cash receipt of net proceeds	2,735,000
3	The adjustments in column 3 reflect the repayment of borrowings from Ultrasis plc as follows:	£
	Repayment of working capital loans – balance as at 30 September 2000	500,049
	Cash repayment against Starks Loan Note	1,000,000
	Total	1,500,049
	Amount of loans from Ultrasis plc	2,190,952
	Total amount of cash repaid	(1,500,049)
	Balance - book value of Production Note	690,903

4 Column 4 reflects the pro forma statement of net assets of the Group following the Placing and Open Offer and repayment of debt. No account has been taken of trading since 30 September 2000.

DIRECTORS' REPORT (continued)

DIRECTORS AND INTERESTS IN SHARES

The Directors of the Company at the date of this report are set out below. All directors other than Mr Bickerstaff, who was appointed on 15 November 2000, served throughout the year. The Directors' interests and those of their connected persons in the ordinary shares of the Company, all of which are beneficial, at 2 February 2001, 30 September 2000 and 30 September 1999 or the date of appointment, were:

	Ordinary shares of 25p each		
	2 February 2001	30 September 2000	30 September 1999
S W Bickerstaff (non-executive Chairman)	1,616,769	-	-
A J Carroll	513,621	513,621	613,621
G Butterfield	-	-	-
N A Brown (non-executive)	40,696	10,000	10,000
C R Weaver (non-executive)	80,696	30,000	30,000

SUBSTANTIAL SHARE INTERESTS

The following interests in three per cent or more of the issued ordinary share capital has been notified to the Company as at 31 January 2001.

	Ordinary shares of 25p each	
	Number	Per cent.
Swan Corporation Limited	4,844,785	21.06%
Discretionary funds under management of Aberdeen Asset Managers Limited	3,304,427	14.37%
Axa S.A.	2,807,631	12.21%
AIM Trust plc	2,669,628	11.61%
Ultrasis plc	2,272,500	9.88%
Caspen Oil, Inc.	2,123,879	9.23%
S W Bickerstaff	1,616,769	7.03%

DIRECTORS' RESPONSIBILITIES

Company law requires the Directors to prepare accounts that give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for the financial year. In doing so the Directors are required to:

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

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

CORPORATE GOVERNANCE

Directors

During the year the board consisted of two non-executive directors and two executive directors. Since the appointment of Stuart Bickerstaff in November 2000 the board has consisted of a non-executive chairman, two independent non-executive directors and two executive directors. Details of these board members are given on page 6 of this report. The board meets at least 4 times each year and more frequently as and when required. As a consequence of the small size of the Company, all material matters are dealt with by the board.

Statement of Compliance with the Code of Best Practice

The Company has voluntarily applied the Principles of Good Governance set out in section 1 of the Combined Code which apply to fully listed companies.

The Company has complied throughout the year with the Provisions of the Code of Best Practice set out in section 1 of the Combined Code except for the following matters:

- Under the terms of the Company's Articles of Association one third of the directors are required to retire by rotation each year. This could result in a breach of Code Provision A.6.2 which required that all directors are subject to re-election at intervals not exceeding 3 years. The directors intend to resolve that every director will stand for re-election at least every 3 years.

- Under Code Provision D.2.1 the Directors should at least annually conduct a review of the effectiveness of the Group's system of internal control and should report to shareholders that they have done so. This review should cover all controls, including financial, operational and compliance controls and risk management.

  No formal review was carried out by the Directors during the year. The Directors have concentrated on preserving value in the Company and managing its resources. The Company is a relatively small operation with all material matters reported to the full board. Regular board meetings are held throughout the period at which the board considers all major business and financial risks. Accepting that no system of financial control can provide absolute assurance against material loss or misstatement or loss, the directors believe that the established systems of internal control are appropriate to the business.

  During the current period the Directors intend to carry out a full review which will ensure compliance with *Internal Control: Guidance for Directors on the Combined Code* "The Turnbull Report".

- The Company does not currently meet the requirements of Code Provision D.2.2. This states that companies which do not have an internal audit function should from time to time review the need for one. The board will review this in the current financial period in conjunction with the review of internal control.

- Under Code Provision D.3.1 the board should establish an audit committee of at least three Directors, all of which should be non-executive. The audit committee is currently comprised of two non-executive directors, Messrs N A Brown and C Weaver. Since the year end the Company has taken corrective action to ensure compliance with this provision. It is proposed that a third non-executive director Mr S Bickerstaff will join the audit committee. This appointment is subject to approval at the next board meeting.

Further explanations of how the Principles have been applied is set out below and in connection with directors' remuneration, in the Remuneration Report.

DIRECTORS' REPORT (continued)

CORPORATE GOVERNANCE (continued)

Dialogue with institutional shareholders

The Company reports formally to shareholders twice a year, when its half-year and full-year results are announced and an Interim Report and Annual Report are sent to shareholders. The Annual Report includes notice of the Annual General Meeting of the Company at which a presentation is given and directors are available to take questions, both formally during the meeting and informally after the meeting. The chairman is available for dialogue with major shareholders on the Company's plans and objectives and from time to time meets with them.

Audit Committee

The audit committee provides a link between the board and the company's auditors on matters falling within the scope of the Company's audit. These matters include accounting standards and policies, internal financial control procedures and the Company's financial statements and reports, which are intended for publication.

Going Concern

After making enquiries, the Directors have formed a judgement at the time of approving the accounts that there is a reasonable expectation that the Group has adequate resources to continue its operations for the foreseeable future. For this reason, the Directors continue to adopt the going concern basis in preparing the accounts.

REMUNERATION REPORT

The Remuneration Committee is comprised of Neville A Brown and Colin Weaver. The committee last met in September 2000.

Fees

Total fees of £40,000 for the year were £3,000 above the estimated amount last year as a result of fees paid to Mr Butterfield for the preparatory work which he undertook in connection with the Placing and Open Offer. Details of each individual director's remuneration are shown in note 5 to the financial statements.

Current estimates of fees for the year ending 30th September 2001 are as shown in the prospectus dated 18 October 2000; namely £82,000 for five Directors.

Remuneration Policy

The remuneration and terms and conditions of service of the Executive Directors are determined by the Board, based on recommendations made by the Remuneration Committee. The Board's policy is to pay competitive salaries having regard to the director's experience, the size and complexity of the job and any special factors which may arise from time to time. From the outset, the Directors consider that the Group has taken due account of the principles of the Combined Code.

The Board has always recognised that, in order to attract high calibre executives, it would need to design schemes which more properly reward each of the Executive Directors for their individual contributions to the Group's performance. A simple bonus scheme has been devised for Mr Carroll which may be triggered during the current year, subject to the achievement of certain production targets.

DIRECTORS' REPORT (continued)

ANNUAL GENERAL MEETING

As special business at the Annual General Meeting, shareholders are being asked to renew the Directors authority to allot relevant securities up to a maximum nominal amount of £1,900,000 and to grant authority to the Directors to issue equity shares (as defined in section 94 of the Companies Act 1985) up to a maximum aggregate nominal amount of £287,500 for cash without being limited by the restrictions otherwise imposed by the statutory pre-emption provisions set out in section 89(1) of the Companies Act 1985. The Board has no intention, at present, of issuing any part of the unissued share capital.

AUDITORS

A resolution will be proposed at the Annual General Meeting to re-appoint BDO Stoy Hayward as auditors to the Company for the ensuing year.

By order of the board

Garry Butterfield
Secretary
6 February 2001

Registered Office:
Cooper Street
Wolverhampton WV2 2JL

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF KERN RIVER plc

We have audited the financial statements of Kern River Plc for the year ended 30 September 2000 which comprise the Consolidated Profit and Loss Account, the Consolidated Balance Sheet, the Balance Sheet, the Consolidated Statement of Total Recognised Gains and Losses, the Consolidated Cash Flow Statement and the related notes. These financial statements have been prepared under the historical cost convention and the accounting policies set out therein.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards are set out in the Statement of Directors' Responsibilities. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board and by our profession's ethical guidance. Where a company is fully listed, there are additional responsibilities for auditors contained in the Listing Rules of the Financial Services Authority. As a company quoted on the Alternative Investment Market, Kern River plc voluntarily complied with the requirements of rule 12.43A of the Listing Rules in preparing its annual report. As auditors, we have agreed that our responsibilities in relation to the annual report will be those set out below.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or rule 12.43A of the Listing Rules regarding directors' remuneration and transactions with the group is not disclosed.

We review whether the corporate governance statement reflects the company's compliance with the seven provisions of the Combined Code as specified for our review by the Listing Rules where a company is fully listed, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the company's corporate governance procedures or its risk and control procedures.

We read the other information contained in the annual report and consider whether it is consistent with the audited financial statements. This other information comprises only the Directors' Report, the Chairman's Statement, the Operating and Financial Review and the Corporate Governance Statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

BASIS OF AUDIT OPINION

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

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

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF KERN RIVER plc *(Continued)*

OPINION

In our opinion the financial statements give a true and fair view of the state of the Group's and the Company's affairs as at 30 September 2000 and of the Group's profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

BDO Stoy Hayward
Chartered Accountants
Registered Auditors
London

6 February 2001

KERN RIVER plc

CONSOLIDATED PROFIT AND LOSS ACCOUNT
Year ended 30 September 2000

	Note	2000 £	1999 £
TURNOVER	1,2	685,441	340,147
Cost of sales		534,850	475,227
GROSS PROFIT/(LOSS)		150,591	(135,080)
Administrative expenses		9,584	60,901
OPERATING PROFIT/(LOSS)		141,007	(195,981)
Interest receivable		6,826	4,083
Interest payable	3	(30,049)	(4,005)
PROFIT/(LOSS) ON ORDINARY ACTIVITIES BEFORE TAXATION	4	117,784	(195,903)
Tax on profit/(loss) on ordinary activities	6	(1950)	(3,818)
PROFIT/(LOSS) FOR THE YEAR	7, 17	115,834	(199,721)
EARNINGS/(LOSS) PER SHARE – basic and diluted	8	1.01p	(1.74)p

All disclosures relate only to continuing operations.

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

	2000 £	1999 £
Profit/(Loss) for financial year	115,834	(199,721)
Currency translation differences	450,938	126,445
Total recognised gains and losses of the year	566,772	(73,276)

KERN RIVER plc

CONSOLIDATED BALANCE SHEET
As at 30 September 2000

			2000		1999
FIXED ASSETS	Note	£	£	£	£
Tangible assets	9		7,351,374		6,373,538
CURRENT ASSETS					
Debtors	11	123,611		62,403	
Cash at bank and in hand		240,460		96,797	
		364,071		159,200	
CREDITORS - amounts falling due within one year	12	(248,469)		(165,482)	
NET CURRENT ASSETS/ (LIABILITIES)			115,602		(6,282)
TOTAL ASSETS LESS CURRENT LIABILITIES			7,466,976		6,367,256
CREDITORS - amounts falling due after more than one year	13		(2,190,952)		(1,658,004)
			5,276,024		4,709,252
CAPITAL AND RESERVES					
Called up share capital	15		2,875,000		2,875,000
Share premium	16		381,325		381,325
Merger reserve	16		2,197,944		2,197,944
Exchange equalisation reserve	16		225,601		(225,337)
Profit and loss account	17		(403,846)		(519,680)
EQUITY SHAREHOLDERS' FUNDS	18		5,276,024		4,709,252

Approved by the Board on 6 February 2001

G. Butterfield - Director

KERN RIVER plc

BALANCE SHEET
As at 30 September 2000

	Note		2000		1999
FIXED ASSETS		£	£	£	£
Investments	10		2,250,002		2,250,002
CURRENT ASSETS					
Debtors	11	1,289,493		963,876	
Cash at bank and in hand		41,734		20,065	
		1,331,227		983,941	
CREDITORS - amounts falling due within one year	12	(46,971)		(27,692)	
NET CURRENT ASSETS			1,284,256		956,249
TOTAL ASSETS LESS CURRENT LIABILITIES			3,534,258		3,206,251
CREDITORS - amounts falling after more than one year	13		(500,049)		(140,000)
			3,034,209		3,066,251
CAPITAL AND RESERVES					
Called up share capital	15		2,875,000		2,875,000
Share premium	16		381,325		381,325
Profit and loss account	17		(222,116)		(190,074)
EQUITY SHAREHOLDERS' FUNDS	18		3,034,209		3,066,251

Approved by the Board on 6 February 2001

G. Butterfield - Director

KERN RIVER plc

CONSOLIDATED CASHFLOW STATEMENT
Year ended 30 September 2000

	Note	2000 £	1999 £
NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES	19	158,054	(17,530)
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE	20	6,826	4,078
TAX PAID		(1,950)	(3,818)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT	20	(364,700)	(230,141)
NET CASH OUTFLOW BEFORE FINANCING		(201,770)	(247,411)
FINANCING	20	360,049	140,000
INCREASE/(DECREASE) IN CASH	21	158,279	(107,411)

RECONCILIATION OF NET CASHFLOW TO MOVEMENT IN NET DEBT

	2000 £	1999 £
INCREASE/(DECREASE) IN CASH IN YEAR	158,279	(107,411)
CASH INFLOW FROM INCREASE IN NET DEBT	(360,049)	(140,000)
TRANSLATION DIFFERENCES	(187,515)	(45,608)
MOVEMENT IN NET DEBT IN THE YEAR	(389,285)	(293,019)
NET DEBT AT 1 OCTOBER 1999	(1,561,207)	(1,268,188)
NET DEBT AT 30 SEPTEMBER 2000	(1,950,492)	(1,561,207)

1. ACCOUNTING POLICIES

Accounting conventions
The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards.

Basis of consolidation
The consolidated accounts include the Company and its subsidiaries. Merger accounting has been used to reflect the combination of CSV Holdings, Inc. on 19 November 1996 by way of share for share exchange.

Turnover
Turnover represents sales to external customers at invoiced amounts less value added tax or local taxes.

Oil and gas interests and depletion
Oil and gas properties are accounted for using the full cost method of accounting, whereby all productive and non productive costs are capitalised. Costs relating to non-producing mineral properties are excluded from those amounts being amortised until such time as there are indications of impairment, or appraisal programmes are complete. Costs relating to evaluated properties are amortised on a unit of production basis over Proven Reserves. Such calculation takes account of estimates of the future costs of development relating to those Reserves based on current price levels.

The capitalised costs of evaluated properties are compared to estimates of future net revenues attributable to the Group's interests in the cost pool. In accordance with Financial Reporting Standard 11, such net revenues and costs are discounted at 10% and prices, cost levels and exchange rates are those anticipated for future periods. Any shortfall of future net revenues over capitalised costs net of deferred tax is provided as additional depletion in the profit and loss account.

Depreciation of other tangible fixed assets
Depreciation is provided on all other tangible fixed assets by equal instalments over their estimated useful lives on a straight line basis:

Motor vehicles	33.3%

Financial Instruments
In relation to the disclosures made in note 22:

- Short term debtors and creditors are not treated as financial assets or financial liabilities.
- The group does not hold or issue derivative financial instruments for trading purposes.

Foreign currencies
Foreign currency transactions of individual companies are translated at the rates ruling when they occurred. Foreign currency monetary assets and liabilities are translated at the rates ruling at the balance sheet date. Any differences are taken to the profit and loss account.

The results of overseas operations are translated at the average rates of exchange during the year and their balance sheets translated into sterling at the rates of exchange ruling on the balance sheet date. Exchange differences which arise from translation of the opening net assets and results of foreign subsidiary undertakings are taken to reserves.

1. ACCOUNTING POLICIES *(Continued)*

Deferred tax
Deferred tax is provided under the liability method on those timing differences which are expected to reverse in the foreseeable future.

2. TURNOVER, PROFIT AND NET ASSETS

Turnover relates solely to the principal activities of the company and is derived entirely within the USA. All sales are made to customers in the USA.

	Pre-tax profit		Net assets	
	2000	1999	2000	1999
	£	£	£	£
Analysis by class of business and geographical market				
Kern River plc (all entirely in UK)	(32,042)	(56,466)	(502,736)	(146,515)
CSV Holdings, Inc. (all entirely USA)	149,826	(139,437)	5,778,760	4,855,767
	117,784	(195,903)	5,276,024	4,709,252

3. INTEREST PAYABLE

	2000	1999
	£	£
Bank loans and overdrafts	-	5
Other loans	30,049	4,000
	30,049	4,005

4. PROFIT/(LOSS) ON ORDINARY ACTIVITIES BEFORE TAXATION

	2000	1999
	£	£
Loss on ordinary activities before taxation is stated after charging/(crediting):		
Auditors' remuneration – audit fees	15,000	10,000
Auditors' remuneration – non-audit fees	4,637	1,750
Depreciation of fixed assets	2,147	1,649
Depletion of oil and gas reserves	109,605	101,117
Exchange gains	(116,484)	(25,339)

5. DIRECTORS AND OTHER EMPLOYEES

The Group had no employees, other than the directors during the accounting period.

The emoluments of the Directors were as follows:

	2000 £	1999 £
For services as Directors – fees received	40,000	27,500
Directors fees by individual		
Neville A. Brown	12,000	11,000
Garry Butterfield	13,000	3,583
Colin Weaver	6,000	5,500
Anthony Carroll	9,000	7,417
	40,000	27,500

The directors are not paid benefits, pensions or any other remuneration, other than that set out above.

	2000 Number	1999 Number
Average number of employees in the year including Directors (both part time)	2	2

6. TAX ON PROFIT/(LOSS) ON ORDINARY ACTIVITIES

	2000 £	1999 £
Overseas tax	1,950	3,818

No liability to UK corporation tax arises on the results for the year. The Company has tax losses available for offset against future taxable profits in the UK.

7. PROFIT/(LOSS) FOR THE YEAR

The company has taken advantage of the exemption allowed under Section 230 of the Companies Act 1985 and has not presented its own profit and loss account in these financial statements. The group profit figure includes a loss after tax of £32,042 (1999: £56,466) which is dealt with in the accounts of the parent company.

8. EARNINGS/(LOSS) PER SHARE

The calculation of earnings per share and the diluted earnings per share is based on the profit for the year of £115,834 and on the weighted average number of ordinary shares in issue of 11,500,000. (1999: Loss of £199,721, shares in issue 11,500,000). The figures for basic and diluted earnings per share are the same as there are no dilutive potential ordinary shares.

9. TANGIBLE FIXED ASSETS – GROUP

	Oil reserves £	Motor vehicles £	Total £
Cost			
At 1 October 1999	6,650,197	7,985	6,658,182
Additions	364,700	-	364,700
Translation adjustment	757,452	909	758,361
At 30 September 2000	7,772,349	8,894	7,781,243
Depreciation and depletion			
At 1 October 1999	279,668	4,976	284,644
Charge for period	109,605	2,147	111,752
Translation adjustment	32,907	566	33,473
At 30 September 2000	422,180	7,689	429,869
Net book value at 30 September 2000	7,350,169	1,205	7,351,374
Net book value at 30 September 1999	6,370,529	3,009	6,373,538

Net Proven Reserves of oil (number of barrels)	Total
At 1 October 1999	5,328,161
Net increase in period	16,738
At 30 September 2000	5,344,899

The Reserve quantities above represent those confirmed by SAVAGEngineers, Consulting Petroleum Engineers, as at 30 September 2000.

10. FIXED ASSET INVESTMENTS COMPANY

	Subsidiary undertakings	Total
Cost at 30 September 2000 and 30 September 1999	£2,250,002	£2,250,002

The subsidiary undertakings are:

	Country of incorporation and of operations	Proportion of share capital held	Nature of business
CSV Holdings, Inc.	USA	100%	Oil fields
Kern River Investments Ltd	UK	100%	Dormant

11. DEBTORS

	Group 2000 £	Group 1999 £	Company 2000 £	Company 1999 £
Trade debtors	120,772	61,292	-	-
Amounts owed by Group undertakings	-	-	1,286,946	962,765
Other debtors	599	50	307	50
Prepayments and accrued income	2,240	1,061	2,240	1,061
	123,611	62,403	1,289,493	963,876

All amounts shown under debtors are due for payment within one year

12. CREDITORS – amounts falling due within one year

	Group 2000 £	Group 1999 £	Company 2000 £	Company 1999 £
Trade creditors	225,150	137,790	23,650	-
Accruals and deferred income	23,319	27,692	23,321	27,692
	248,469	165,482	46,971	27,692

13. CREDITORS – amounts falling due after more than one year

	Group 2000 £	Group 1999 £	Company 2000 £	Company 1999 £
Working capital loan	500,049	140,000	500,049	140,000
Secured Loan note	1,690,903	1,518,004	-	-
	2,190,952	1,658,004	500,049	140,000

All of the amounts shown above are due for repayment within two years. The secured loan note which bears no interest is for US$2,500,000 and is repayable in two equal instalments on 20 October 2001 and 20 April 2002 and is secured on Starks oil field. The working capital loan carries interest at 2% above Lloyds Bank base rate and is repayable on 31 October 2001. Both of these loans are from Ultrasis plc, which holds 9.88% of the shares of Kern River plc. As described in note 26 these loans were fully settled in November 2000.

14. DEFERRED TAXATION

The Group has £905,256 (1999 - £707,209) of unprovided deferred taxation at the balance sheet date, all of which relates to accelerated capital allowances.

15. CALLED UP SHARE CAPITAL

	2000 £	1999 £
Authorised		
15,300,000 ordinary shares of £0.25 each	3,825,000	3,825,000
Allotted and fully paid:		
11,500,000 ordinary shares of £0.25 each	2,875,000	2,875,000

16. OTHER RESERVES

	Group and Company Share Premium Reserve £	Group Exchange Equalisation Reserve £	Group Merger Reserve £
At 1 October 1999	381,325	(225,337)	2,197,944
Exchange differences on consolidation	-	450,938	-
At 30 September 2000	381,325	225,601	2,197,944

17. PROFIT AND LOSS ACCOUNT

	Group 2000 £	Group 1999 £	Company 2000 £	Company 1999
Profit/(loss) for the period	115,834	(199,721)	(32,042)	(56,466)
Profit and loss brought forward	(519,680)	(319,959)	(190,074)	(133,608)
Deficit at 30 September 2000	(403,846)	(519,680)	(222,116)	(190,074)

18. RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	Group 2000 £	Group 1999 £	Company 2000 £	Company 1999 £
Profit/(loss) for the financial period	115,834	(199,721)	(32,042)	(56,466)
Translation adjustments	450,938	126,445	-	-
Net increase/(reduction) in shareholders' funds	566,772	(73,276)	(32,042)	(56,466)
Opening shareholders' funds	4,709,252	4,782,528	3,066,251	3,122,717
Closing shareholders' funds	5,276,024	4,709,252	3,034,209	3,066,251

19. RECONCILIATION OF OPERATING PROFIT/(LOSS) TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES

	2000 £	1999 £
Operating profit/(loss)	141,007	(195,981)
Depreciation and depletion charges	111,752	102,766
Exchange gain	(116,484)	(25,339)
(Increase)/decrease in debtors	(61,208)	8,466
Increase in creditors	82,987	92,558
Net cash inflow/(outflow) from operating activities	158,054	(17,530)

20. ANALYSIS OF CHANGES IN CASHFLOWS DURING THE YEAR

	2000 £	1999 £
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE		
Interest received	6,826	4,083
Interest paid	-	(5)
	6,826	4,078
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT		
Purchase of tangible fixed assets	(364,700)	(230,141)
FINANCING		
Increase in working capital loan	360,049	140,000

21. ANALYSIS OF CHANGES IN NET DEBT

	1 October 1999 £	Cash Flow £	Translation Difference £	30 September 2000 £
Cash at bank and in hand	96,797	158,279	(14,616)	240,460
Debt due after one year	(1,658,004)	(360,049)	(172,899)	(2,190,952)
	(1,561,207)	(201,770)	(187,515)	(1,950,492)

22. FINANCIAL INSTRUMENTS

The majority of the Group's assets and long term loans are in US Dollars, which is the functional currency of the Group. The parent company reports in sterling. The directors consider the Group's key financial risks to be currency risk and interest rate risk.

Currency risk

The majority of the Group's assets and liabilities are denominated in the local currency of the operation, US Dollars, which is the functional currency of the Group. The directors do not consider the financial risks associated with operational currency risks to be sufficient to justify entering into derivative financial instruments.

Interest rate risk

The Group is party to a variable rate loan with Ultrasis plc. The balance on this loan at the year end was £500,049 and the interest rate is 2% above Lloyds Bank base rate. The directors do not consider it necessary to enter into derivative financial instruments to hedge against movement in interest rates.

Interest rate, currency profile and maturity of long term borrowings:

	Floating rate borrowing		Fixed rate borrowing	
	2000	1999	2000	1999
	£	£	£	£
Currency:				
US Dollars	-	-	1,690,903	1,518,004
Sterling	500,049	140,000	-	-

The Sterling floating rate borrowing bears interest at 2% above Lloyds Bank base rate. The US Dollar borrowings bear no interest.

The long term borrowings were settled in November 2000 as described in note 26.

Fair Values

At 30 September 2000 and 1999 the book values of financial instruments do not differ materially from their fair values.

23. CONTINGENT LIABILITY

CSV Holdings, Inc. is party to a letter of credit arrangement that provides for up to $100,000 (£60,606) (1999 - $100,000 (£58,844)) in the event of future liabilities arising in connection with site reinstatement at Starks Oilfield. No provision has been made in the accounts for such potential liabilities. An amount of $100,000 (£60,606) (1999: $100,000 (£58,844)) included in cash at bank and in hand is secured against this potential liability by bankers of CSV Holdings, Inc.

24. SIGNIFICANT CONTRACTS

Churchill Energy, Inc., a subsidiary of Churchill U.S.A., Inc., is the licensed operator of the oilfields at Nukern and Starks, under agreements dated 3 July 1989 and 19 November 1996 respectively, on behalf of CSV Holdings, Inc.. The turnover in respect of these agreements for the year was £685,441 (1999 - £340,147) and the related expenditure was £375,791 (1999 - £348,435).

25. RELATED PARTIES

At the year end Kern River plc had outstanding long term borrowings of £2,190,952 (1999 - £1,658,004) with Ultrasis plc, a company which has a substantial share interest in Kern River plc. During the year Kern River received an additional £330,000 in long term loans.

Included in the borrowings above is £30,049 in accrued interest at the year end.

26. POST BALANCE SHEET EVENTS

On 18 October 2000 the Company announced that it was raising £2.7 million net of expenses by way of a placing and open offer to repay its borrowings and to finance a development programme at the Starks Field in order to increase production substantially. Under the placing and open offer the Company issued 11,500,000 new ordinary shares at 25p per share. The placing and open offer was described in the prospectus issued on 18 October 2000, and was approved by shareholders at an extraordinary general meeting held on 14 November 2000. The placing and open offer was completed on 15 November 2000 with the result that the Group has settled all of its borrowings, which were from Ultrasis plc, a founder shareholder. Settlement was in the form of £1.5million cash and the issue of a $1million production note. Repayment of the production note is to commence at the later of 1 January 2004 or the date at which C.S.V. Holdings, Inc. has received $6million in profit from Starks Field. Payments will then be made quarterly equal to 20% of the net production revenue in the period, up to the value of $1million plus accrued interest charged at the rate of 5.84% per annum.

At the extraordinary general meeting on 14 November 2000 shareholders also approved, subject to Court confirmation, the reduction of the share premium account by £241,810 to create a reserve against which the deficit on the profit and loss account as at 31 March 2000 of the same amount may be set off. The application to the Court is in progress at this time and it is expected that the order of the Court confirming the reduction of share premium account will be made in the middle of February 2001.