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Kuwait Petroleum Corporation And Subsidiaries

CONSOLIDATED FINANCIAL STATEMENTS

31 MARCH 2007

TUESDAY



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COMPANIES HOUSE

His Excellency, Sheikh Nasser Al-Mohammed Al-Ahmed Al-Sabah
The Prime Minister and
Chairman of the Supreme Council for Petroleum
State of Kuwait

We have audited the accompanying consolidated financial statements of Kuwait Petroleum Corporation (the Corporation) and its subsidiaries (the Group) which comprise the consolidated balance sheet as at 31 March 2007, the consolidated statements of income, cash flows and changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Consolidated Financial Statements

The management of the Corporation is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

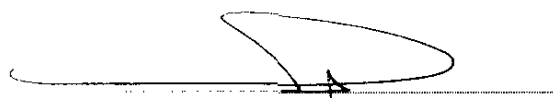
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 March 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on Other Legal and Regulatory Requirements

Furthermore, in our opinion, proper books of account have been kept by the Corporation and the consolidated financial statements, together with the contents of the report of the Board of Directors relating to these consolidated financial statements, are in accordance therewith. We further report that the consolidated financial statements include the disclosures required by Law Decree No. 6 of 1980, that we obtained all the information and explanations that we required for the purpose of our audit, that an inventory was duly carried out, and that to the best of our knowledge and belief no violations of Law Decree No. 6 of 1980 have occurred during the year ended 31 March 2007 that might have had a material effect on the business of the Group or on its financial position.



WALEED A. AL OSAIMI
LICENCE NO. 68 A
OF ERNST & YOUNG

6 June 2007
Kuwait

Kuwait Petroleum Corporation and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME

Year ended 31 March 2007

	<i>Notes</i>	<i>2007 KD'000</i>	<i>2006 KD'000</i>
REVENUES			
Sales of crude oil, gas, refined products and petrochemicals		21,548,819	19,694,623
Engineering and other operations	3	221,878	210,050
		21,770,697	19,904,673
COST OF REVENUES			
Cost of sales of crude oil, gas, refined products and petrochemicals		(19,963,674)	(17,673,868)
Engineering and other operations		(128,907)	(129,464)
		(20,092,581)	(17,803,332)
GROSS PROFIT		1,678,116	2,101,341
Depreciation and amortisation		(231,704)	(215,045)
General and administration expenses		(254,995)	(223,543)
Provision for inventory and doubtful debts		(2,300)	(469)
Impairment losses - goodwill	9	(1,212)	(4,385)
Interest income		100,720	57,662
Investment income	4	171,582	462,880
Share of profit from associates		95,848	100,674
Interest expense		(14,254)	(10,940)
Other income	5	227,398	144,810
Directors' fees	6	(90)	(103)
PROFIT BEFORE PROVISION FOR INCOME TAX		1,769,109	2,412,882
Income tax expense		(60,779)	(96,511)
PROFIT FOR THE YEAR	7	1,708,330	2,316,371
Attributable to:			
Equity holders of the Corporation		1,707,603	2,315,519
Minority interest		727	852
		1,708,330	2,316,371

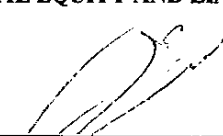
The attached notes 1 to 31 form part of these consolidated financial statements.

Kuwait Petroleum Corporation and Subsidiaries

CONSOLIDATED BALANCE SHEET

At 31 March 2007

ASSETS	Notes	2007 KD'000	2006 KD'000
Non-current assets			
Fixed assets	8	4,597,446	3,741,818
Goodwill	9	184,231	175,606
Other non-current assets	10	1,093,653	814,990
Securities	11	4,379,700	4,033,672
Associates and unconsolidated subsidiaries		358,361	314,485
		10,613,391	9,080,571
Current assets			
Inventories	12	1,184,834	1,181,975
Trade receivables	13	2,497,616	2,256,537
Other receivables and prepayments	14	496,565	361,156
Taxes receivable	15	46,380	30,614
Bank balances and cash	16	464,473	2,086,772
		4,689,868	5,917,054
TOTAL ASSETS		15,303,259	14,997,625
EQUITY AND LIABILITIES			
Equity			
Authorised and paid-up capital		2,500,000	2,500,000
Statutory reserve	17	1,250,000	1,250,000
Capital reserve	18	232,945	232,945
General reserve	19	4,336,506	4,165,737
Reserve for replacement and renewal of fixed assets	20	1,483,691	1,483,691
Cumulative changes in fair values		270,738	86,405
Foreign currency translation reserve		76,464	1,937
Equity attributable to equity holder of the Corporation		10,150,344	9,720,715
Minority interests		4,198	16,291
Total equity		10,154,542	9,737,006
Non-current liabilities	21	534,811	536,583
Current liabilities			
Trade payables		536,844	471,481
Other credit balances	22	3,436	30,145
Other payables and accruals	23	676,322	562,078
Taxes payable	15	316,986	212,356
Amounts due to Ministry of Oil	24	1,543,484	1,364,019
Profit to be distributed	25	1,536,834	2,083,957
		4,613,906	4,724,036
Total liabilities		5,148,717	5,260,619
TOTAL EQUITY AND LIABILITIES		15,303,259	14,997,625


Suhail Bograïs
Managing Director – Planning and Finance


Saad A. Al-Shuwaib
Acting Chief Executive Officer

The attached notes 1 to 31 form part of these consolidated financial statements.

Kuwait Petroleum Corporation and Subsidiaries
CONSOLIDATED STATEMENT OF CASH FLOWS
Year ended 31 March 2007

	Notes	2007 KD'000	2006 KD'000
OPERATING ACTIVITIES			
Profit for the year		1,708,330	2,316,371
Adjustments for:			
Depreciation and amortisation		231,704	215,045
Provision for doubtful debts		2,300	469
Impairment losses		1,212	4,385
Write off of unsuccessful exploration		25,842	25,510
Provision for employees' terminal benefits and pensions		(6,152)	10,161
(Gain) loss on disposal of fixed assets		(11,205)	1,830
Share of profit from associates		(95,848)	(100,674)
Interest income		(100,720)	(57,662)
Interest expense		14,254	10,940
Income tax expense		60,780	96,511
Investment income		(171,582)	(462,880)
Changes in operating assets and liabilities:		1,658,915	2,060,006
Increase in trade receivables		(475,642)	(700,316)
Increase in inventories		(2,860)	(243,929)
Increase in other receivables and prepayments		(135,408)	(24,171)
Increase in trade payables		65,363	103,254
Increase in other payables, accruals and other credit balances		39,571	80,518
(Decrease) increase in non-current liabilities		(2,490)	47,681
Increase in amounts due to Ministry of Oil		358,243	343,873
Cash generated from operations		1,505,692	1,666,916
Taxes received (paid)		28,083	(3,052)
Net cash from operating activities		1,533,775	1,663,864
INVESTING ACTIVITIES			
Decrease (Increase) in deposits maturing after 3 months		344,335	(298,009)
Net (increase) decrease in securities		(161,695)	478,061
Net movement in associates and unconsolidated subsidiaries		51,973	437,122
Additions to goodwill		(4,762)	(118,913)
Increase in other non-current assets (excluding trade receivables)		(46,400)	(43,250)
Purchase of fixed assets		(1,565,702)	(1,008,044)
Proceeds from disposal of fixed assets		336,911	192,468
Interest received		100,720	57,662
Amounts due from Ministry of Finance		-	32,284
Net Proceeds from sale of securities and associates		171,582	462,880
Net cash (used in) from investing activities		(773,038)	192,261
FINANCING ACTIVITIES			
Term loans, net		54,834	9,248
(Decrease) increase in minority interests		(12,820)	15,219
Interest paid		(14,254)	(10,940)
Profit distributed	25	(2,083,957)	(1,423,599)
Net cash used in financing activities		(2,056,197)	(1,410,072)
Net effect of foreign currency translation adjustments		17,496	(110,702)
Net (decrease) increase in cash and cash equivalents		(1,277,964)	335,351
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR		1,725,639	1,390,288
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	16	447,675	1,725,639
Short-term deposits maturing after 3 months	16	16,798	361,133
BANK BALANCES AND CASH AT END OF THE YEAR	16	464,473	2,086,772

The attached notes 1 to 31 form part of these consolidated financial statements.

Kuwait Petroleum Corporation and Subsidiaries

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 March 2007

	Attributable to equity holder of the Corporation							Minority interests	Total equity		
	Authorised and paid-up capital KD '000	Statutory reserve KD '000	Capital reserve KD '000	General reserve KD '000	Reserve for replacement and renewal of fixed assets KD '000	Cumulative changes in fair values KD '000	Foreign currency translation reserve KD '000	Profit available for distribution KD '000	Total KD '000	Minority interests KD '000	Total equity KD '000
Balance at 31 March 2005	2,500,000	1,250,000	232,945	3,934,175	1,483,691	9,805	71,322	-	9,481,938	220	9,482,158
Net movement in cumulative changes in fair values	-	-	-	-	-	76,600	-	-	76,600	-	76,600
Net exchange differences	-	-	-	-	-	-	(69,385)	-	(69,385)	-	(69,385)
Net income (expense) recognised directly in equity	-	-	-	-	-	76,600	(69,385)	-	7,215	-	7,215
Profit for the year	-	-	-	-	-	-	-	2,315,519	2,315,519	852	2,316,371
Total recognised income (expense) for the year	-	-	-	-	-	76,600	(69,385)	2,315,519	2,322,734	852	2,323,586
Transfer to general reserve	-	-	-	231,562	-	-	-	(231,562)	-	-	-
Profit to be distributed	-	-	-	-	-	-	-	(2,083,957)	(2,083,957)	-	(2,083,957)
Net movement in minority interests	-	-	-	-	-	-	-	-	-	15,219	15,219
Balance at 31 March 2006	2,500,000	1,250,000	232,945	4,165,737	1,483,691	86,405	1,937	-	9,720,715	16,291	9,737,006
Net movement in cumulative changes in fair values	-	-	-	-	-	184,333	-	-	184,333	-	184,333
Net exchange differences	-	-	-	-	-	-	74,527	-	74,527	-	74,527
Net income recognised directly in equity	-	-	-	-	-	184,333	74,527	-	258,860	-	258,860
Profit for the year	-	-	-	-	-	-	-	1,707,603	1,707,603	727	1,708,330
Total recognised income for the year	-	-	-	-	-	184,333	74,527	1,707,603	1,966,463	727	1,967,190
Transfer to general reserve	-	-	-	170,769	-	-	-	(170,769)	-	-	-
Profit to be distributed	-	-	-	-	-	-	-	(1,536,834)	(1,536,834)	-	(1,536,834)
Net movement in minority interests	-	-	-	-	-	-	-	-	-	(12,820)	(12,820)
Balance at 31 March 2007	2,500,000	1,250,000	232,945	4,336,506	1,483,691	270,738	76,464	-	10,150,344	4,198	10,154,542

The attached notes 1 to 31 form part of these consolidated financial statements.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

1 CORPORATE INFORMATION

The consolidated financial statements of Kuwait Petroleum Corporation (the Corporation) and its subsidiaries (the Group) for the year ended 31 March 2007 were authorised for issue in accordance with a resolution of the directors on 6 June 2007. These consolidated financial statements are subject to change upon approval of the Supreme Council of Petroleum. The Corporation is wholly-owned by the Government of the State of Kuwait. The Corporation was established by Law Decree No. 6 of 1980 which came into effect on 27 January 1980. The Group's principal activities include exploration, drilling, production, storage, refining, processing, transportation, distribution and marketing of crude oil, natural gas, chemical, petrochemical and associated products. The marketing of crude oil and petroleum products produced by subsidiaries in the State of Kuwait is undertaken by the Corporation. The entire Group's other activities, including the marketing of crude oil and petroleum products produced by subsidiaries outside the State of Kuwait are carried out through its subsidiaries, associates and joint ventures. The principal subsidiaries, associates and joint ventures are set out in Note 31. The Group operates principally in the Middle East, Western Europe and the U.S.A.

Crude oil produced in the State of Kuwait becomes the property of the Government of the State of Kuwait, which reimburses the production costs of the producing subsidiary. The Corporation purchases crude oil and natural gas from the Government of the State of Kuwait in accordance with the terms of the applicable Decree issued on 17 January 1981.

The address of the Corporation's registered office is P.O. Box 26565, Safat 13126, State of Kuwait.

2 SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

The consolidated financial statements are prepared under the historical cost convention, modified for the measurement at fair value of available for sale securities and derivative financial instruments.

The consolidated financial statements are presented in thousands of Kuwaiti Dinars.

Statement of compliance

The consolidated financial statements have been prepared in accordance with Law Decree No. 6 of 1980 and International Financial Reporting Standards (IFRS).

The accounting policies used in the preparation of the consolidated financial statements are consistent with those used in the previous year.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Corporation and its principal subsidiaries. Details of the principal consolidated subsidiaries are included in Note 31. Significant intercompany balances, transactions and profits are eliminated on consolidation.

The financial statements of subsidiaries are prepared using accounting policies that are consistent with those applied by the Corporation. Adjustments are made to conform any material dissimilar accounting policies that may exist.

Minority interests principally represent the portion of profit or loss and net assets in subsidiaries of KPC Holding (Aruba) E.C. and Petrochemical Industries Company K.S.C. not held by the Corporation and are presented separately in the consolidated income statement and within equity in the consolidated balance sheet, separately from the Corporation equity.

Subsidiaries are those enterprises controlled by the Corporation. Control exists when the Corporation has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of the subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. Significant inter-Group balances and transactions, including inter-group profits and unrealised profits and losses are eliminated on consolidation. The consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of consolidation (continued)

The financial statements of the subsidiaries are consolidated on a line-by-line basis by adding together like items of assets, liabilities, income and expenses.

The subsidiaries have been accounted for using the purchase method of accounting. The purchase method of accounting involves allocating the cost of the business combination to the fair value of the assets acquired and liabilities and contingent liabilities assumed at the date of acquisition.

Unconsolidated subsidiaries

The management is of the opinion that the total assets, liabilities and results of the unconsolidated subsidiaries are not significant to the Group's consolidated financial statements. Accordingly, these subsidiaries have not been consolidated. Also, these entities did not have significant operations during the year.

Accounting periods of group companies

The Group's financial year was from 1 April 2006 to 31 March 2007. The financial year of the Corporation's directly owned subsidiaries is the same as that of the Corporation with the exception of Kuwait Foreign Petroleum Exploration Company K.S.C., Kuwait Gulf Oil Company K.S.C. (Closed) and KPC Holdings (Cayman), Inc., whose financial periods were from 1 January 2006 to 31 December 2006. Where such subsidiaries do not prepare financial statements drawn up to the same date as that of the Group, adjustments are made for the effects of any significant events or transactions which have occurred in the months following the year end of these subsidiaries.

IASB Standards issued but not adopted

The following IASB Standards have been issued but are not yet mandatory, and have not yet been adopted by the Group:

- IAS 23 – Borrowing Costs
- IFRS 7 – Financial Instruments: Disclosures
- IFRS 8 – Operating segments
- IFRIC 9 – Reassessment of Embedded Derivatives
- IFRIC 12 – Service Concession Arrangements

The adoption of the revised version of IAS 23 for periods beginning on or after 1 January 2009 will require the Group to commence capitalising borrowing costs that are directly attributable to expenditure on qualifying assets.

The application of IFRS 7 and IFRS 8, which will be effective for the year ending 31 December 2007, will result in amended and additional disclosures relating to financial instruments and associated risks. The application of IFRIC 9 and IFRIC 12 which will be effective for 2007 and 2008 are not expected to have a material impact on the consolidated financial statements of the Group.

Revenue recognition

Sales are recognised on the date title passes to the customer in accordance with the contract of sale. Other operating revenues are recognised as work is performed or over the terms of the related contracts.

Interest is recognised on the accrual basis.

Dividend income is recognised when the shareholders' right to receive payment is established.

Leases

Rentals paid under operating leases are expensed on a straight-line basis over the lease term, irrespective of the terms of payment.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Fixed assets (property, plant and equipment)

(i) Oil and gas properties

Oil and gas exploration and producing activities are accounted for using the "successful efforts" method of accounting, whereby costs of geological and geophysical operations and exploratory drilling costs proven to be non-productive are expensed. Successful exploratory and developmental drilling costs are capitalised and amortised using the unit-of-production method for operations outside the State of Kuwait. Exploration and development drilling costs for operations in the State of Kuwait are capitalised and amortised on a straight-line basis over 10 years.

(ii) Other fixed assets

Other fixed assets are initially recorded at cost. Costs incurred for routine and cyclical maintenance and repairs and renewals are expensed when incurred. The costs of major inspection or overhaul costs are capitalised as a separate inherent component of an asset if they can be reliably estimated, future economic benefits are expected to flow and the Group has already depreciated an amount representing the inherent components that have been replaced or restored by the major inspection or overhaul. Major repairs and renewals of an asset or major components thereof, which improve the standard of performance or which extend the useful life of the asset beyond that originally assessed at the time of acquisition, are capitalised and depreciated over the useful life of the asset.

Depreciation

Depreciation is provided on a straight-line basis on other fixed assets, other than freehold land and assets under construction. The rates of depreciation are based upon the following estimated useful lives:

• Tankage, pipelines and jetties	5 - 25 years
• Plant and machinery	3 - 33 years
• Oil and gas tankers	5 - 20 years
• Camps, buildings and facilities	4 - 40 years
• Vehicles, transportation equipment and other assets	3 - 20 years
• Construction and general equipment	5 years
• Well drilling and seismic surveys	10 years

Goodwill

Goodwill recognised as an asset

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill on acquisitions after 31 March 2004 is not amortised. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units, or Groups of cash generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or Groups of units

Where recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash generating unit and part of the operation within that unit are disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Goodwill (continued)

Negative goodwill

Negative goodwill on acquisition is measured at the excess of the Corporation's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over the cost of the business combination. Negative goodwill is recognised immediately in the consolidated income statement.

Available for sale securities

Available for sale securities are recognised and derecognised, on a trade date basis, when the Group becomes, or ceases to be, a party to the contractual provisions of the instrument.

Investments designated as available for sale securities are initially recorded at cost and subsequently measured at fair value, unless this cannot be reliably measured in which case they are carried at cost less impairment losses. Changes in fair value are reported as a separate component of equity. On derecognition or impairment the cumulative gain or loss previously reported in equity is included in the consolidated statement of income for the year.

Investments in associated companies

The Group's investments in its associates are accounted for using the equity method of accounting.

An associate is an entity in which the Group has significant influence and which is neither a subsidiary nor a joint venture. Under the equity method, the investment in the associate is carried in the consolidated balance sheet at cost plus post acquisition changes in the Group's share of net assets of the associate.

The consolidated income statement reflects the share of the results of operations of the investee. Where there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of changes in equity. Profits and losses resulting from transactions between the Group and its associate are eliminated to the extent of the interest in the associate.

Distributions received from an associate reduce the carrying amount of the investment.

An assessment of investment in an associate is performed when there is an indication that the asset has been impaired, or that impairment losses recognised in prior years no longer exist.

Interests in Joint Ventures

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to joint control, and a jointly controlled entity is a joint venture that involves the establishment of a separate entity in which each venturer has an interest.

Interests in joint ventures are accounted for using proportionate consolidation method to comply with the accounting policies of the Group's ultimate Corporation. The Group combines its share of each of the assets, liabilities, income and expenses of the joint ventures with the similar items, line by line, in its consolidated financial statements. The financial statements of the joint ventures are prepared for the year ended 31 December; accordingly, adjustments are made for the effect of any significant event or transactions occurring in the months following the year end of the joint ventures and 31 March.

Where practicable, adjustments are made to the joint ventures' audited financial statements to bring them in line with the Group's accounting policies.

The joint ventures are proportionately consolidated from the date of acquisition of joint control until the date on which the Group ceases to have joint control over the joint ventures. All intra-group transactions and balances are eliminated to the extent of the Group's share in the joint ventures.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories

(i) Crude oil and petroleum products

Crude oil inventory is valued at the lower of average cost and net realisable value at the year end. The cost of crude oil to the Corporation is determined by the Government of Kuwait in accordance with the Decree issued on 17 January 1981. The formula for establishing the cost of crude oil has been revised in accordance with a resolution by the Supreme Council for Petroleum effective 1 July 1997.

Liquefied petroleum gas and finished products are valued at the lower of cost and net realisable value. Cost is determined using the weighted average method on an individual product basis. Costs are those expenses incurred in bringing each product to its present location and condition. This includes cost of crude oil and natural gas supplied plus an allocation of processing costs and overheads to each product based on their relative market values.

Net realisable value is based on estimated selling price less any further costs expected to be incurred on completion and disposal.

(ii) Other

Spare parts, materials and supplies mainly used in operations are valued at cost, determined principally by the weighted average cost method, less allowance for any obsolete or slow-moving items.

Trade receivables

Trade receivables are stated at original invoice amount less provisions for amounts estimated to be non-collectable. An estimate for doubtful accounts is made when collection of the full amount is no longer probable.

Cash and cash equivalents

Cash and cash equivalents for the purpose of preparing the consolidated statement of cash flows comprise cash, short-term bank deposits and highly liquid investments with a maturity date not exceeding 3 months from the date of acquisition.

Recognition and derecognition of financial assets and liabilities

A financial asset or a financial liability is recognised when the Group becomes a party to the contractual provisions of the instrument. A financial asset (in whole or in part) is derecognised either when the Group has transferred substantially all the risks and rewards of ownership or when it has neither transferred nor retained substantially all the risks and rewards and when it no longer has control over the asset or a proportion of the asset. A financial liability is de-recognised when the obligation specified in the contract is discharged, cancelled or expired.

Impairment of non financial assets

An asset is impaired if its carrying amount exceeds its estimated recoverable amount. The recoverable amount of an asset is the higher of an asset's net selling price and value in use. Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction. Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life. An assessment is made at each balance sheet date to determine whether there is objective evidence that an asset may be impaired. If such evidence exists, an impairment loss is recognised in the consolidated income statement.

Impairment and uncollectibility of financial assets

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset or group of financial assets may be impaired. If such evidence exists, any impairment loss is recognised in the statement of income. Impairment is determined as follows:

- (a) For assets carried at fair value, impairment is the difference between cost and fair value; and
- (b) For assets carried at cost, impairment is the difference between cost and the present value of future cash flows discounted at the current market rate of return for a similar financial asset.
- (c) For assets carried at amortised cost, impairment is the difference between carrying amount and the present value of future cash flows discounted at the original effective interest rate.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Trade payables

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether billed by the supplier or not.

Bank borrowings

Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis in the income statement using the effective interest rate method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Foreign currency translation

The consolidated financial statements are presented in Kuwaiti dinars, which is the Group's functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All differences are taken to the consolidated statement of income.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The Group's investments in foreign subsidiaries, associates and joint ventures are translated into Kuwaiti dinars at the year end rates of exchange and the results of the subsidiaries, associated companies and joint ventures are translated into Kuwaiti dinars at the average rates of exchange for the year. All foreign exchange translation adjustments are taken to the foreign currency translation reserve until disposal at which time they are recognised in the consolidated statement of income.

Fair values

For investments traded in an active market, fair value is determined by reference to quoted market bid prices.

For unquoted equity investments, fair value is determined by reference to recent arm's length market transactions, market value of a similar investment, expected discounted cash flows or other valuation models.

The fair value of interest-bearing items is estimated based on discounted cash flows using interest rates for items with similar terms and risk characteristics.

The fair value of forward foreign exchange contracts is calculated by reference to current forward exchange rates with the same maturity.

Investments with no reliable measures of their fair values and for which no fair value information could be obtained are carried at their initial cost less impairment in value.

Other financial assets and liabilities

For other financial assets and liabilities, fair value is determined based on expected future cash flows and management's estimate of the amount at which these assets could be exchanged for cash on an arm's length basis or a liability settled to the satisfaction of creditors.

Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Corporation commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

Kuwait Petroleum Corporation and Subsidiaries

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At 31 March 2007

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxes on income

Certain of the Corporation's subsidiaries are subject to taxes on income in various foreign countries of operation. Provision is made for current income taxes in the subsidiaries' financial statements based on the tax laws and the rates of the countries in which operations were conducted during the year. Provision for deferred income taxes reflects the net tax effects of timing differences between the carrying amounts of assets and liabilities used for financial and income tax reporting purposes, which are expected to reverse in the foreseeable future.

Derivatives

Derivative products principally include forward foreign exchange contracts, futures, options and swaps.

Derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market using prevailing market rates or internal pricing models. Derivatives with positive market values (unrealised gains) are included in other receivables and derivatives with negative market values (unrealised losses) are included in other payables in the balance sheet. The resultant gains and losses from derivatives held for trading purpose are included in the statement of income.

The Group also enters into sales and purchase contracts as part of its international operations. Where these contracts qualify as a derivative or include an embedded derivative as defined by IAS 39, they are stated at fair value. Fair value is assessed by applying prevailing market prices directly to the contract or embedded derivative, where possible, or by identifying separate financial instruments which have the same terms and are readily traded in the relevant markets.

Provisions

Provisions are recognised when an obligation (legal or constructive) arising from a past event, and the costs to settle the obligation, are both probable and able to be reliably measured.

Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated balance sheet when there is a legally enforceable right to set off the recognised amounts and the Group intends to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

Significant accounting judgement and estimates

Critical judgements in applying the group's accounting policies

In the process of applying the Group's accounting policies, which are described in this note, management has made the following judgments that have the most significant effect on the amounts recognised in the financial statements (apart from those involving estimations, which are dealt with below).

Recognition of provisions

The Group is subject to a number of matters which could lead to an outflow of economic benefits. In making an assessment as to whether such matters require either provision or disclosure, management is required to consider, amongst other factors, whether a constructive obligation exists at the balance sheet date and whether the resulting risk of an outflow of economic benefits is probable (requiring a provision), less than probable but more than remote (requiring disclosure) or remote (requiring neither provision nor disclosure).

In the current year, the most significant judgements made by management relating to the above are:

- The extent to which the Group has constructive obligations in relation to the clean up of environmental exposures in a number of different affiliates;
- The extent to which the Group has constructive obligations at the balance sheet date in relation to various restructuring programs; and
- The extent to which it is probable that the Group will have to make payments in respect of a number of tax, legal and regulatory disputes.

Further details of amounts for which either provision or disclosure was deemed to be required are given in Notes 13, 29 and 30 respectively.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the next financial year, are discussed below:

Measurement of provisions

Having concluded that a provision is required for a potential exposure (see above), the amount to be recognised shall be the best estimate of the expenditure required to settle the present obligation at the balance sheet date, taking into consideration any relevant risks and uncertainties and the time value of money. This requires management to make its best estimates of the likely future outflows, the expected timing of such outflows and the discount rate to be applied to such outflows, taking into account the risks specific to the particular exposure. Further details of the nature of provisions recorded by the Group are provided in Notes 10 and 13. The majority of these exposures are expected to be settled over a relatively limited number of years which limits the uncertainty in respect of the time value of money.

Impairment of Goodwill

Determining whether Goodwill is impaired requires an estimation of the value in use of the cash-generating units to which the cost has been allocated. The value in use calculation requires the entity to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value.

Actuarial gains and losses

In calculating the carrying value of its defined benefit schemes, management is required to apply a number of assumptions, the most significant of which are investment growth, future salary growth and discount rate.

Significant accounting judgement and estimates

Financial instruments

Financial instruments include bank balances and cash, trade receivables, securities, trade payables and certain other assets and liabilities. Off-balance sheet financial instruments include forward foreign exchange purchase contracts which are entered into in order to fix the exchange rate at which purchases will be settled and are disclosed at contracted rates, and other derivative products. Derivative products are financial contracts between two parties where payment is dependent upon movements in price in one or more underlying financial instruments, reference rates or index.

Fair values of on-balance sheet financial instruments are based on quoted prices for marketable instruments, or estimated fair values, calculated using methods such as net present values of future cash flows. Fair values of off-balance sheet financial instruments are based on the unrealised gain or loss from marking to market the derivatives using prevailing market rates or internal pricing models.

Impairment of available for sale securities

The Group treats available for sale securities as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is "significant" or "prolonged" requires considerable judgment.

In the case of available for sale securities, reversal of previously recognised impairment losses are no longer recorded through the consolidated income statement but as increases in cumulative changes in fair values.

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2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Classification of securities

Management decides on acquisition of securities whether they should be classified as investments carried at fair value through income statement or available for sale.

The management classifies its securities as carried at fair value through income statement if they are acquired primarily for the purpose of short term profit making and the fair value of those securities can be reliably determined.

Classification of securities as fair value through income statement depends on how management monitors the performance of these securities when they are not classified as held for trading but have readily available fair values and the changes in fair values are reported as part of profit or loss in the management accounts, they are classified as fair value through income statement. Other securities are classified as available for sale.

Valuation of unquoted equity securities

Valuation of unquoted equity securities is normally based on one of the following:

- recent arm's length market transactions;
- current fair value of another instrument that is substantially the same ;
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

The determination of the cash flows and discount factors for unquoted equity investments requires significant estimation.

3 REVENUES FROM ENGINEERING AND OTHER OPERATIONS

	<i>2007</i> <i>KD'000</i>	<i>2006</i> <i>KD'000</i>
Engineering and construction	9,587	5,317
Marine operations	31,517	31,061
Merchandise and other services	180,774	173,672
	<u>221,878</u>	<u>210,050</u>

4 INVESTMENT INCOME

	<i>2007</i> <i>KD'000</i>	<i>2006</i> <i>KD'000</i>
Income from managed portfolios and others	171,582	156,779
Gain on sale of associates	-	306,101
	<u>171,582</u>	<u>462,880</u>

Kuwait Petroleum Corporation and Subsidiaries

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5 OTHER INCOME

	2007 KD'000	2006 KD'000
Gain (loss) on disposal of fixed assets	11,205	(1,830)
Recovery of financial cost	153,974	95,327
Foreign currency exchange loss	(38,195)	(9,454)
Miscellaneous income	82,223	54,482
UN compensation claims (Note 26)	18,191	6,285
	<u>227,398</u>	<u>144,810</u>

6 DIRECTORS' FEES

The directors' fees are subject to approval of the Supreme Council for Petroleum.

7 PROFIT FOR THE YEAR

The profit is stated after charging staff costs and compensation of key management personnel as follows:

	2007 KD'000	2006 KD'000
Staff costs	<u>590,778</u>	<u>545,185</u>

Compensation of key management personnel

The remuneration of directors and other members of key management of the Group during the year were as follows:

	2007 KD'000	2006 KD'000
Short-term benefits	3,460	3,100
Termination benefits	983	930
	<u>4,443</u>	<u>4,030</u>

Kuwait Petroleum Corporation and Subsidiaries

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8 FIXED ASSETS

Balance at 1 April 2006, net of accumulated depreciation

	Oil and gas properties KD'000	Tankage, pipelines and jetties KD'000	Plant and machinery KD'000	Oil and gas tankers KD'000	Camps, buildings and facilities KD'000	Vehicles, transportation equipment and other assets KD'000	Construction and general equipment KD'000	Well drilling and seismic surveys KD'000	Assets under construction and in transit KD'000	Total KD'000
Additions	284,493	462,968	1,191,025	90,768	256,032	38,496	9,351	353,370	1,055,315	3,741,818
Disposals	74,133	14,493	41,992	-	60,926	7,889	477	140,780	1,225,012	1,565,702
Transfers	(46,466)	(49)	(5,660)	(1,638)	(2,060)	(2,059)	1,972	-	(269,746)	(325,706)
Currency translation effects	78,252	34,000	142,766	41,753	12,574	9,554	3,354	-	(322,253)	-
Depreciation for the year	(1,578)	3,974	30,348	-	9,622	370	600	-	8,620	51,956
Write off of unsuccessful exploration	(78,508)	(50,823)	(161,907)	(8,120)	(28,676)	(16,480)	(2,629)	(63,339)	-	(410,482)
	(25,842)	-	-	-	-	-	-	-	-	(25,842)
At 31 March 2007	<u>284,484</u>	<u>464,563</u>	<u>1,238,564</u>	<u>122,763</u>	<u>308,418</u>	<u>37,770</u>	<u>13,125</u>	<u>430,811</u>	<u>1,696,948</u>	<u>4,597,446</u>

Fixed assets

At cost	741,993	1,543,859	3,445,468	305,862	675,000	213,702	41,710	1,096,798	1,696,948	9,761,340
Accumulated depreciation	(457,509)	(1,079,296)	(2,206,904)	(183,099)	(366,582)	(175,932)	(28,585)	(665,987)	-	(5,163,894)
Net carrying amount at 31 March 2007	<u>284,484</u>	<u>464,563</u>	<u>1,238,564</u>	<u>122,763</u>	<u>308,418</u>	<u>37,770</u>	<u>13,125</u>	<u>430,811</u>	<u>1,696,948</u>	<u>4,597,446</u>

The depreciation charged in the consolidated statement of income is reduced by KD 179 million (2006: KD 152 million) being the amount charged to the Ministry of Oil in respect of the operations of local wholly owned subsidiaries, Kuwait Oil Company K.S.C. and Kuwait Gulf Oil Company K.S.C.

Kuwait Petroleum Corporation and Subsidiaries

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At 31 March 2007

9 GOODWILL

	2007 KD'000	2006 KD'000
Net book value at beginning of the year	175,606	68,740
Additions during the year, net	4,762	118,913
Impairment losses	(1,212)	(4,385)
Currency translation effects	5,075	(7,662)
Net book value at end of the year	<u>184,231</u>	<u>175,606</u>

10 OTHER NON-CURRENT ASSETS

	2007 KD'000	2006 KD'000
Long term portion of trade receivables	860,918	628,655
Deferred expenses	83,946	69,372
Deferred tax asset	25,100	28,866
Intangible assets	46,118	44,599
Other	77,571	43,498
	<u>1,093,653</u>	<u>814,990</u>

Included in trade receivables and non-current trade receivables are KD 255 million (2006: KD 245 million) and KD 861 million (2006: KD 629 million) respectively due from the Ministry of Electricity and Water which do not carry any interest or fixed or determinable repayment dates.

The above balances are stated net of a provision of KD 97 million (2006: KD 96 million). A significant portion of these receivables has been outstanding for a number of years, as payment of these balances is subject to formalities, including the approval of the Ministry of Electricity and Water expenditure budget. It has been resolved that the Ministry of Finance and Ministry of Oil will undertake to settle the amounts due upon the completion of these formalities.

Approximately KD 30 million (2006: KD 20 million) of deferred expenses represents catalysts used in the refining process which are amortised on a straight line basis over their estimated useful lives.

11 SECURITIES

	2007 KD'000	2006 KD'000
Managed portfolios and funds	4,340,935	3,989,704
Other	38,765	43,968
	<u>4,379,700</u>	<u>4,033,672</u>

Securities are denominated predominantly in US Dollars and Euros and represent investments in high credit quality bonds and equities quoted on international stock markets.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

12 INVENTORIES

	2007 KD'000	2006 KD'000
Crude oil	248,453	263,174
Liquefied petroleum gas	1,301	1,505
Refined petroleum products	644,848	682,204
Finished petrochemical products	29,836	22,088
Spare parts, materials and supplies	260,396	213,004
	<u>1,184,834</u>	<u>1,181,975</u>

13 TRADE RECEIVABLES

The Corporation and one of its major subsidiaries, comprising 74% (2006: 78%) of the consolidated total trade receivables, deal mainly with major state owned and international oil companies. Another major subsidiary operating mainly in Europe and accounting for approximately 21% (2006: 17%) of the consolidated total trade receivables deals with a large number of corporate customers in that region. The Group's 12 largest customers account for 37% of outstanding trade receivables at 31 March 2007 (2006: 32%).

Trade receivables are denominated predominantly in US Dollars and Kuwaiti dinars.

Trade receivables include KD 255 million (31 March 2006: KD 247 million), which represents the short-term portion of amounts due from Ministry of Electricity and Water (Note 10).

14 OTHER RECEIVABLES AND PREPAYMENTS

	2007 KD'000	2006 KD'000
Marine sub-charter and other receivables	164,709	52,377
Insurance, local tax and other claims	8,081	5,528
Prepaid expenses	38,915	28,390
Receivable from exchange and concession partners	17,400	12,733
Advances to contractors	103,349	131,532
Refundable deposits	20,330	19,597
Employee receivables	5,892	11,295
Other	137,889	99,704
	<u>496,565</u>	<u>361,156</u>

15 TAXES RECEIVABLE/PAYABLE

Taxes receivable mainly comprise corporate income tax and related refund claims recoverable by one of the Group's foreign subsidiaries. Taxes payable are predominantly on account of VAT and similar tax liabilities payable by another foreign subsidiary.

Kuwait Petroleum Corporation and Subsidiaries

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16 BANK BALANCES AND CASH

	2007 KD'000	2006 KD'000
Cash and current accounts at banks	89,646	113,742
Short-term bank deposits and highly liquid investments maturing within 3 months	358,029	1,611,897
Cash and cash equivalents	447,675	1,725,639
Short-term bank deposits maturing after 3 months	16,798	361,133
	<u>464,473</u>	<u>2,086,772</u>

Short-term bank deposits are mainly denominated in Kuwaiti Dinars, Euros and US Dollars. These deposits carry annual interest rates between 3.9% to 6.9 % (2006: 2.51% to 6.25%) and mature within six months from the balance sheet date. These balances are placed with high credit quality financial institutions.

Bank balances and cash also include:

US \$ 11.63 million (KD 3.37 million) recovered from former employees against whom one of the subsidiary companies has initiated legal proceedings for financial irregularities [(2006: US \$ 10.9 million and £ 1.5 million (KD 4 million))]. These amounts, which include accumulated interest, can only be utilised in accordance with the outcome of the litigation (Note 30).

£ 0.122 million (KD 0.069 million) recovered from former employees against whom the subsidiary company has initiated legal proceedings for financial irregularities [2006: US \$ 69.9 million, £ 8.1 million, EUR 1.7 million and CHF 4.1 million (KD 26 million)].

The total corresponding amount of KD 3.4 million (2006: KD 30 million) is reported as other credit balances (Note 22).

17 STATUTORY RESERVE

In accordance with Article 12 of Law Decree No. 6 of 1980, the Corporation has resolved to discontinue the annual transfer to statutory reserve since the reserve would exceed 50% of the authorised and paid-up capital.

18 CAPITAL RESERVE

The capital reserve mainly represents the difference between the Corporation's cost of acquisition of its original subsidiaries, which were transferred by the Government of the State of Kuwait, and their net asset values at 31 December 1979. No transfer to capital reserve has been made for the current year.

19 GENERAL RESERVE

In accordance with Article 12 of Law Decree No. 6 of 1980, 10% of the profit is to be transferred to the general reserve, the percentage of which may be changed in accordance with a resolution of the Supreme Council of Petroleum.

Kuwait Petroleum Corporation and Subsidiaries

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20 RESERVE FOR REPLACEMENT AND RENEWAL OF FIXED ASSETS

Article 10 of Law Decree No. 6 of 1980 states that the Corporation may provide part from its profits to meet the costs of replacement and renewal of the Corporation's and its subsidiaries' fixed assets, after approval of the Supreme Council for Petroleum. The reserve is based on the difference between depreciation, calculated on the historical cost of the fixed assets of the Corporation and its Kuwaiti subsidiaries, and depreciation calculated on the replacement cost of assets using their insured (generally replacement) values.

The Board of Directors has proposed no transfer to the reserve as of 31 March 2007 (2006: KD Nil), which is subject to approval of the Supreme Council of Petroleum.

21 NON-CURRENT LIABILITIES

	2007 KD'000	2006 KD'000
Employees' terminal benefits	186,124	187,680
Pension fund liabilities	18,784	23,380
Long-term loans	144,061	137,191
Deferred income taxes	67,174	71,265
Provisions	46,437	39,376
Other	72,231	77,691
	<u>534,811</u>	<u>536,583</u>

The long-term loans represent loans to KPC Holdings (Aruba) A.E.C., Kuwait Gulf Oil Company K.S.C. and Petrochemical Industries Company K.S.C.

KPC Holdings (Aruba) A.E.C. long-term loans are denominated in Euros and bear various interest rates, however the majority of the loan balance bears interest at a rate of EURIBOR plus a margin specific to each loan. Certain of the loan balances include covenants relating to the financial position of a subsidiary of KPC Holdings (Aruba) A.E.C. The long-term loan to Kuwait Gulf Oil Company K.S.C. represents a draw down under a facility amounting to US \$ 750 million provided to fund capital expenditures of Al Khafji Joint Operations during the years 2003 to 2007 and is repayable in five equal annual instalments starting from 16 December 2005 to 16 December 2009. This loan carries interest at 6 month LIBOR and a margin. The long term loans to Petrochemical Industries Company K.S.C. denominated in USD bear various interest rates, however majority of the loan balances bears average interest at one month LIBOR plus 1.1% per annum.

Provisions represent present obligations of one of the Corporation's subsidiaries in Europe relating mainly to environmental provisions and business restructuring in respect of the relocation of certain of the subsidiary's management and head office functions from London to Kuwait, together with restructuring of operations in Belgium and Denmark.

The principal defined benefit funds schemes relating to KPC Holding (Aruba) A.E.C. operate in the United Kingdom, Sweden, the Netherlands, Belgium and Italy. Provisions for pension obligations are established for benefits payable in the form of retirement, disability and surviving dependent pensions. The benefits offered vary according to the legal, fiscal and economic conditions of each country. Benefits are dependent on years of service and the respective employees' compensation.

The latest actuarial valuation took place as at 31 March 2007 and this showed that all funds and schemes were in deficit. The main assumptions used in the actuarial valuation were an expected return on assets of 4.2% to 6.9% per annum (2006: 3.7% to 6.9%), an annual salary increase of 3% to 4.8% (2006: 2.9% to 4.5%) and a discount rate of -4% to 5.4% (2006: 3.8% to 4.9%).

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22 OTHER CREDIT BALANCES

Other credit balances represent funds recovered from former employees against whom one of the subsidiary companies has initiated legal proceedings for financial irregularities; together with accumulated interest (refer Note 30a). A portion of the balances has been distributed during the year between the subsidiary and the Corporation based on an agreement reached during the year. The remaining balance, which includes accumulated interest, can only be utilised in accordance with the outcome of the litigation (refer Note 30a).

23 OTHER PAYABLES AND ACCRUALS

	2007 KD'000	2006 KD'000
Short-term bank loans	123,453	75,489
Provision for annual leave and accrued compensation	48,244	50,166
Payable to contractors	182,865	92,830
Accruals	66,140	66,341
Sundry payables	216,264	217,439
Payable to exchange partners	-	17,513
Marine sub-charter and other marine payables	39,356	42,300
	<u>676,322</u>	<u>562,078</u>

Short-term bank loans are unsecured, are denominated in Euros, or in the currency of the country in which the borrowing occurs, and bear interest at prevailing market rates.

24 AMOUNTS DUE TO MINISTRY OF OIL

Amounts due to the Ministry of Oil represent the net amounts payable for purchases of crude oil and natural gas and for certain activities performed by the Corporation and its subsidiaries on behalf of the Ministry of Oil. These activities primarily relate to the exploration for and production of crude oil and natural gas in the State of Kuwait and the local marketing (within the State of Kuwait) of refined products and liquefied petroleum gas. The costs of the wholly owned subsidiaries, Kuwait Oil Company K.S.C. and Kuwait Gulf Oil Company K.S.C., are charged to this account.

25 PROFIT TO BE DISTRIBUTED

	2007 KD'000	2006 KD'000
Balance at beginning of the year	2,083,957	1,423,599
Profit distributed during the year	(2,083,957)	(1,423,599)
Profit to be distributed	<u>1,536,834</u>	<u>2,083,957</u>
Balance at end of the year	<u>1,536,834</u>	<u>2,083,957</u>

In accordance with Article 12 of Law Decree No. 6 of 1980, the profit for the year, after transfer to reserves, is payable to the Government of the State of Kuwait.

26 UN COMPENSATION CLAIM

In respect of losses suffered as a result of the Iraqi invasion and occupation of Kuwait in 1990, the Governing Council of the United Nations Claims Commission has approved an amount of US \$ 18,864 million to the Group and the Government of the State of Kuwait for payment as and when funds become available. During the year, a further amount of KD 18.2 million (2006: KD 6.2 million) was received in part settlement. This amount is in respect of amounts due to the Group (Note 5).

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27 FAIR VALUES AND FINANCIAL INSTRUMENTS

In the normal course of business, the Group uses primary financial instruments such as cash and deposits, securities, short-term borrowings, receivables and payables. The Group, mainly through a wholly owned foreign subsidiary, uses derivative financial instruments for managing risks arising from changes in crude oil and petroleum product prices, exchange rates and interest rates. The Group does not use derivatives for speculative purposes.

Non-current trade receivables totalling KD 861 million (2006: KD 629 million) are due from the Ministry of Electricity and Water (Note 10). Since this balance does not carry a fixed or determinable date of future payment, it is not possible to estimate with sufficient reliability its fair value. However, since the balance does not carry interest, fair value is below carrying value.

All foreign currency derivative instruments are marked to market at the end of each month. At year end the gross contract amounts of such contracts, none of which extended beyond 12 months, were as follows:

	2007 USD'000	2006 USD'000	2007 KD'000	2006 KD'000
Foreign exchange contracts	866,136	783,400	250,790	229,077

The majority of the balances at 31 March 2007 relating to forward exchange contracts were in Euro/US dollars, Pounds Sterling/US \$ with minimal amounts in Danish Krone and Swedish Krona. The net fair value of the foreign exchange contracts at 31 March 2007 and 31 March 2006 is not significant.

28 RISK MANAGEMENT

Information on the financial risks of the Group's financial instruments is set out below:

Interest rate risk

The Group is exposed to interest rate risk on its interest bearing deposits and borrowings. The interest rates of deposits and borrowings are disclosed in Notes 16, 21 and 23 respectively.

Credit risk

The Group is exposed to credit risk in respect of losses that would have to be recognised if counterparties fail to perform as contracted. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

Credit risk with respect to trade receivables is limited due to the Group dealing mainly with state owned and major international oil companies, the use of letter of credit arrangements and the active monitoring of outstanding receivables.

The Group controls credit risk in relation to its securities and bank balances by rigorous screening and credit assessment of all proposed dealing counterparties and placing limits on the total financial exposure with each institution.

Liquidity risk

The Group has limited its liquidity risk by maintaining its managed portfolios of securities in quoted marketable bonds and equities. The Group's terms of sales are governed by contracts with customers but generally require payment within 30 days of the date of sale. Amounts due to the Ministry of Oil are normally settled within 30 days of the date of purchase.

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28 RISK MANAGEMENT (continued)

Currency risk

The Group does not generally use derivative forward foreign exchange contracts to hedge against foreign exchange currency risk, except for one of its overseas subsidiaries. The overseas subsidiary continuously seeks to identify and measure all risks arising from movements in foreign exchange rates. Such risks are routinely hedged using a variety of methods, including derivatives such as forward currency contracts and options.

Other than securities and loans, which are denominated in foreign currencies, mainly Euros, the Group is not exposed to significant currency risk.

As the Kuwaiti Dinar movements approximate that of the US Dollar, balances in US Dollars are not considered to represent significant currency risk.

Market risk

Market risk arises from fluctuations in interest rates, foreign exchange rates, equity prices and oil prices. The Group sets limits on the value of risk that may be accepted.

The Group considers that volatility in oil prices is a regular part of its business. To cover exceptional circumstances, one of the Group's subsidiaries has a hydrocarbon risk management policy under which it may make use of derivative instruments to hedge oil price related risks.

29 EXPENDITURE COMMITMENTS

a) Operating lease commitments

The minimum annual rental commitments under operating leases are as follows:

	2007 KD'000	2006 KD'000
Future minimum lease payments:		
Within 1 year	36,534	32,255
Between 1 and 5 years	99,185	86,633
After 5 years	38,906	46,637
Aggregate operating lease expenditure contracted for at the balance sheet date	<u>174,625</u>	<u>165,525</u>

b) Capital expenditure commitments

Estimated capital expenditure contracted for by the Group at the balance sheet date but not provided for amounted to KD 1,910 million (2006: KD 2,053 million).

30 CONTINGENCIES

Contingent liabilities

Pursuant to the acquisition by a subsidiary of an interest in a joint venture in Australia, encompassing production from the Harriet field and various exploration permits, the subsidiary has entered into three deeds of cross charges in favour of each of the other participants for the purpose of securing the subsidiary's obligations under the joint venture agreement. The cross charges comprise a prior ranking charge over the subsidiary's interest in the joint venture to a limit of Australian \$ 250 million (KD 57 million).

The Group had contingent liabilities of approximately US\$ 66.1 million at 31 March 2007 (2006: US\$ 223.6 million). These principally relate to a variety of tax, legal and regulatory disputes, all of which are being vigorously contested by one of the subsidiaries of the Group.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

30 CONTINGENCIES (continued))

Contingent assets

- (a) Having been formed in 1992, one of the subsidiary company's new management discovered certain fraud cases and financial irregularities in the subsidiary's contracts and bank accounts and, therefore, the subsidiary's board of directors formed a fact-finding committee to investigate those irregularities.

On 6 January 1993, the subsidiary company submitted a report to His Excellency, the Attorney General on its suspicion on occurrence of financial irregularities in previous years, whereby the Public Prosecution conducted the necessary investigations and prepared the indictment sheet in December 1993 and its regulation against five of the accused parties.

One of the accused party absconded before submitting the notification to His Excellency the Attorney General. Another party admitted the facts before the Attorney General, and made payment of US\$ 6,200 thousand on allegation that this was the entire amount taken by him. The amount was deposited in a special bank account as a fixed deposit of the subsidiary company and was invested until it became US\$ 11,626 thousand (KD 3,367 thousand) including interest as at 31 March 2007.

The case was deliberated before different Kuwaiti courts, culminating in the two cassation verdicts Nos. 137 and 138 of 1997.

Mandated by the former Minister of Oil, Sheikh Saud Al-Nasser Al-Sabah, the subsidiary company sent a letter to the Attorney General on 14 December 1998. The Attorney General considered this letter as a notification and transferred the same to the Investigating Committee concerned with court actions against Ministers, which, in its first formation, considered it as a notification and, subsequently, undertook the investigation procedures. The subsidiary company provided the committee with 40 documents including those deliberated to the English courts with respect to the certain amounts embezzled by the accused parties or other parties. This committee resigned and a new committee was formed on 29 April 2000. On 16 May 2001, the committee considered that the case was not fully complete, without discussions with any witness.

On 29 May 2001 the former Minister of Oil, Adel Al-Subaih sent a notification to this committee against the five defendants, among them is the former Minister of Oil. On 19 May 2003, the committee considered the action as serious and heard statements of three witnesses from the subsidiary company. The issue is still pending before this committee.

In parallel steps, the subsidiary company has initiated civil cases in the United Kingdom, Switzerland, and other countries, and with the efforts of those working on the case, it won the case filed in the United Kingdom and obtained a judgement against three of the defendants for an amount of US\$ 136,000 thousand other than the interest. In addition to this, the case ended with the rejection by the UK House of Lords on 10 December 2000 of the appeal submitted by one of the accused parties. An amount of US\$ 85,351 thousand has been collected till 7 May 2006. This collected amount was invested in deposits. The collected amounts along with interest till 7 May 2006 totalled US\$ 92,770 thousand plus an amount of US\$ 6,200 thousand transferred by the Public Prosecution from one of the accused parties, which was received by Kuwait Oil Tanker Company in Kuwait, which was invested in a deposit renewable with its interest thereon pending a decision on crime No.275/93. The gross amount with interest reached US\$ 11,626 thousand till 31 March 2007. Legal measures are being carried out to collect the remaining balance. However, the uncollected amounts of US\$ 151,709 thousand pending in the liability of the accused parties comprise of the balance remaining from the total amounts awarded in favour of the subsidiary company according to London's verdict, and inclusive of the interest, till August 2005, amounting to US\$ 123,559 thousand plus such amounts, being the difference between the amounts claimed before London Court and those mentioned in the Public Prosecution Charge Report in connection with crime No.275/93, which is the amount of US\$ 25,000 thousand, for which a civil case was filed and no final verdict has yet been pronounced, plus an amount of US\$ 3,150 thousand (Chesapeake- selling debris of Surf City Vessel) for which a case was filed and no final verdict has yet been pronounced.

30 CONTINGENCIES (continued))

Contingent assets (continued)

Further, the subsidiary company's attorney in Kuwait filed civil cases before the Kuwaiti courts against the accused parties and certain persons who received the embezzled amounts, to claim refunding the funds embezzled by the accused parties and others illegitimately. Verdicts were passed in a number of these cases to temporarily suspend the civil case pending a decision in crime No.275/93, while the other cases are still being deliberated before the courts and experts, in which no final verdicts have yet been pronounced.

An amount of Sterling Pounds 120 thousand was received on 11 October 2006, and invested in a deposit renewable with interest thereon. This amount plus interest amounted to Sterling Pounds 122 thousand (KD 69 thousand) as at 31 March 2007, and will be distributed later, according to the shares agreed upon above.

Dry Cargo (358/94 crimes)

This case has been filed against five indictees. This case was referred to the Criminal Court on 2 April 2006 for charges of embezzling funds, illegal profits and forgery. The value of the amounts claimed in the Public Prosecution's report amounted to approximately US\$ 10,000 thousand.

In the hearing on 17 June 2006, the court ruled for the imprisonment of indictees for five year with labour and execution, to dismiss them from their jobs, oblige them to refund the embezzled funds, and fine each of them an amount equivalent to that embezzled by him, as well as deport the third, fourth and fifth accused parties from the country after serving the said penalty, and to refer the civil case to the competent civil court. The fourth indictee, challenged the verdict passed against him. In the hearing on 16 September 2006, the court ruled to dismiss the objection and upheld the challenged verdict, which was appealed by the second and fourth indictees and postponed for hearing on 2 May 2007.

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At 31 March 2007

31 SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES

a) Principal subsidiaries registered in the State of Kuwait:

Directly held

<i>Name of company</i>	<i>Proportion held</i>	<i>Principal activities</i>
• Kuwait Oil Company K.S.C.	100%	Exploration for and production of crude oil and natural gas in the State of Kuwait.
• Kuwait National Petroleum Company K.S.C.	100%	Refining, LPG manufacturing, and local marketing of refined products.
• Kuwait Oil Tanker Company S.A.K.	100%	Operation of a fleet of crude oil tankers and liquefied petroleum gas and oil product carriers.
• Petrochemical Industries Company K.S.C.		Production of petrochemical products and their distribution and marketing.
• Kuwait Foreign Petroleum Exploration Company K.S.C.	100%	Exploration for and development of oil and gas outside the State of Kuwait.
• Kuwait Santa Fe for Engineering and Petroleum Projects Company K.S.C.	100%	Provision of design, engineering and related services to the petroleum industry.
• Kuwait Aviation Fuelling Company K.S.C.	100%	Supply of aviation fuel.
• Kuwait Gulf Oil Company K.S.C. (Closed)	100%	Exploration for and production of crude oil and natural gas.
• Oil Development Company K.S.C. (Closed)	100%	Manage and supervise operation services contract with international oil companies.
• Oil Sector Service Company K.S.C. (Closed)	100%	Liaison, public services and oil sector supporting services.

Oil Development Company K.S.C. (Closed) and Oil Sector Service Company K.S.C. (Closed) have not undertaken any commercial activities to date.

Indirectly held

<i>Name of company</i>	<i>Proportion held</i>	<i>Principal activities</i>
• Kuwait Aromatics Company K.S.C.C. ("KARO")	80%	Producing and selling perfume products and other derivatives.

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

31 SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES (continued)

b) Principal directly and wholly-owned subsidiaries registered outside the State of Kuwait:

<i>Name of company</i>	<i>Country of Incorporation</i>	<i>Principal activities</i>
• KPC Holdings (Cayman), Inc. (previously SFIC Holdings (Cayman), Inc.)	Cayman Islands	International contract drilling
• KPC Holdings (Aruba) AEC	Aruba	Refining, and marketing of refined products
• Petrochemical Resources Holding N.V.	Netherlands	Investment in other companies and financing activities

c) Principal associates

<i>Name of company</i>	<i>Country of incorporation</i>	<i>Proportion held</i>	<i>Principal activities</i>
• Kuwait Drilling Company K.S.C.	Kuwait	49%	Contract drilling
• Equate Petrochemical Company K.S.C.	Kuwait	42.5%	Petrochemicals
• Gulf Petrochemical Industries Company B.S.C.	Bahrain	33%	Petrochemicals
• Kuwait Olefins Company K.S.C.C	Kuwait	42.5%	Petrochemicals
• First Fuel Marketing Company K.S.C.	Kuwait	24%	Fuel marketing
• Al-Sour Fuel Marketing Company K.S.C.	Kuwait	24%	Fuel marketing

d) Principal joint ventures

<i>Name of the company</i>	<i>Country of incorporation</i>	<i>Effective equity interest as at 31 March 2007</i>
MEGlobal B.V. and subsidiaries	Netherlands	50%
Equipolymers B.V. and subsidiaries	Netherlands	50%
MEGlobal Canada Inc.	Canada	50%
OKQ8 AB	Sweden	50%
Reffineria di Milazzo S.p.A.	Italy	50%

Kuwait Petroleum Corporation and Subsidiaries

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 March 2007

31 SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES (continued)

d) Principal joint ventures (continued)

The share of the assets, liabilities, income and expenses of the jointly controlled entities for the two years presented are as follows:

	<i>2007</i> <i>KD'000</i>	<i>2006</i> <i>KD'000</i>
Current assets	211,757	212,795
Non-current assets	381,393	279,907
Current liabilities	(193,112)	(184,748)
Non-current liabilities	(78,239)	(90,512)
Net assets	321,799	217,442
Income	835,667	787,806
Expenses	(826,772)	(768,880)
Profit	8,895	18,926