

Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Financial Statements

March 31, 2006 and 2005

Auditors' Report

To the Shareholders of Primeline Energy Holdings Inc.

We have audited the consolidated balance sheets of **Primeline Energy Holdings Inc.** as at March 31, 2006 and 2005 and the consolidated statements of operations and deficit and cash flows for each of the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at March 31, 2006 and 2005 and the results of its operations and its cash flows for each of the years then ended in accordance with Canadian generally accepted accounting principles.

(signed) PricewaterhouseCoopers LLP

Chartered Accountants

Vancouver, British Columbia
July 10, 2006

Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Balance Sheets

As at March 31, 2006 and 2005

	2006 \$	2005 \$
Assets		
Current assets		
Cash and cash equivalents	158,272	84,818
Prepaid expenses and deposit	103,885	2,994
	<hr/>	<hr/>
	262,157	87,812
Deferred petroleum exploration costs (note 4)	19,325,792	18,687,077
	<hr/>	<hr/>
	19,587,949	18,774,889
	<hr/>	<hr/>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	433,557	76,827
Advances from Primeline International (Holdings) Inc. (notes 5 and 12)	8,322,506	7,868,298
	<hr/>	<hr/>
	8,756,063	7,945,125
	<hr/>	<hr/>
Shareholders' Equity		
Capital stock (note 6)	34,311	32,807
Contributed surplus (note 6)	13,147,654	12,558,999
Deficit	(2,350,079)	(1,762,042)
	<hr/>	<hr/>
	10,831,886	10,829,764
	<hr/>	<hr/>
	19,587,949	18,774,889
	<hr/>	<hr/>

Nature of operations and going concern (note 1)

Commitments (note 7)

Subsequent events (note 12)

Approved by the Board of Directors

(signed) Peter Kelty Director

(signed) Guang Ming Wang Director

Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Statements of Operations and Deficit

For the years ended March 31, 2006 and 2005

	2006	2005
	\$	\$
Revenue		
Interest income	136	-
	<hr/>	<hr/>
Expenses		
Bank charges and interest	1,767	1,107
Foreign exchange loss	4,588	243
Office	27,735	18,780
Professional fees	282,096	168,791
Stock-based compensation (note 6(b))	235,159	25,008
Travel	36,828	1,764
	<hr/>	<hr/>
	588,173	215,693
	<hr/>	<hr/>
Loss for the year	(588,037)	(215,693)
Deficit - Beginning of year	(1,762,042)	(1,546,349)
	<hr/>	<hr/>
Deficit - End of year	(2,350,079)	(1,762,042)
	<hr/>	<hr/>
Basic and diluted loss per common share	(0.024)	(0.009)
	<hr/>	<hr/>
Weighted average number of common shares outstanding	24,619,619	23,987,290
	<hr/>	<hr/>

Primeline Energy Holdings Inc.

(an exploration stage company)

Consolidated Statements of Cash Flows

For the years ended March 31, 2006 and 2005

	2006 \$	2005 \$
Cash flows from operating activities		
Loss for the year	(588,037)	(215,693)
Item not affecting cash - stock-based compensation	235,159	25,008
	<hr/>	<hr/>
	(352,878)	(190,685)
Changes in non-cash working capital items		
Prepaid expenses and deposit	(100,891)	(990)
Accounts payable and accrued liabilities	356,730	22,723
	<hr/>	<hr/>
	255,839	21,733
	<hr/>	<hr/>
	(97,039)	(168,952)
Cash flows from investing activities		
Expenditures on deferred petroleum exploration costs	(998,898)	(363,175)
	<hr/>	<hr/>
Cash flows from financing activities		
Advances from Primeline International (Holdings) Inc.	814,391	548,384
Stock options exercised	355,000	-
	<hr/>	<hr/>
	1,169,391	548,384
Increase in cash and cash equivalents	73,454	16,257
Cash and cash equivalents - Beginning of year	84,818	68,561
Cash and cash equivalents - End of year	<hr/>	<hr/>
	158,272	84,818
Supplemental cash flow information		
Non-cash investing activities		
Accrued interest and foreign exchange gain capitalized to deferred petroleum exploration costs	(360,183)	(137,310)
Non-cash financing activities		
Accrued interest on advances from Primeline International (Holdings) Inc.	590,396	576,163
Foreign exchange gain on advances from Primeline International (Holdings) Inc.	(950,579)	(438,853)

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

1 Nature of operations and going concern

Primeline Energy Holdings Inc. (PEHI) was incorporated under the Companies Law of the Cayman Islands on March 31, 1995 and is in the business of exploration and development of off-shore oil and gas properties. To date, PEHI has not realized any revenues from its oil and gas properties and is considered to be an exploration stage company.

Primeline Energy China Ltd. (PECL), a wholly owned subsidiary, owns a 75% interest in a petroleum sharing contract (the Petroleum Contract) which entitles PECL to participate in the exploration, development and production of oil and gas in Block 25/34 in the East China Sea. The participation interests are detailed in note 4. Primeline Energy Operations International Limited (PEOIL), another wholly owned subsidiary, holds the operator rights under the Petroleum Contract.

PECL is currently exploring for oil and gas under the Petroleum Contract for Block 25/34 in the East China Sea of the People's Republic of China (PRC). The Block contains the Lishui 36-1 (Vicky) gas discovery, which the company discovered in 1997, and its surrounding area. There have been two successful wells drilled in the discovery, both of which had significant gas flows during testing. However, it has not yet been determined whether this area contains reserves that are economically recoverable. The potential for recovery of costs incurred in this area may therefore be dependent upon the discovery of economically recoverable reserves and the ability to obtain financing to complete the exploration and development of potential reserves.

These consolidated financial statements are prepared on the basis that PEHI will continue as a going concern, which assumes that the company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. As at March 31, 2006, the company had net current liabilities of \$171,400 (2005 - working capital of \$10,985) and had a deficit of \$2,350,079 (2005 - \$1,762,042). The Private Placement on April 4, 2006 (see note 12) provided the company with sufficient funds to complete its minimum commitments under Phase 1 of its exploration period (note 4) and for general and administration activities for the next year.

2 Summary of accounting policies

Principles of consolidation

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include the accounts of PEHI and its wholly owned subsidiaries, PECL and PEOIL, also incorporated in the Cayman Islands (collectively, the company). Intercompany balances and transactions are eliminated on consolidation.

Cash and cash equivalents

Cash and cash equivalents consist of cash and highly liquid short-term interest-bearing securities with maturities at the purchase date of three months or less.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

Deferred petroleum exploration costs

The company follows the full cost method of accounting for oil and gas exploration expenditures, wherein all costs related to the exploration of oil and natural gas properties are capitalized. Costs capitalized include acquisition costs, geological and geophysical expenditures, rentals on undeveloped properties, costs of drilling productive and non-productive wells, overhead directly related to exploration activities and lease of well equipment. Costs capitalized will be depleted using the unit-of-production method based on proven gross oil and natural gas reserves determined by the company and independent engineers.

The company is in the process of exploring off-shore oil and gas properties and has not yet determined the amount of reserves available in its properties. Management's estimate of probable reserves and resources are subject to risks and uncertainties affecting the recoverability of the company's investment in deferred petroleum exploration costs. Although management has made its best estimate of these factors based on current conditions, it is reasonably possible that changes could occur in the near term that could materially affect management's estimate of the recoverability of deferred costs and the need for asset impairment writedowns.

Senior management regularly reviews the carrying values of deferred petroleum exploration costs to assess whether there has been any impairment in value. If it is determined that the carrying value is not recoverable and exceeds its fair value, a writedown to the fair value amount is made by a charge to earnings.

Foreign currency translation

The company translates foreign currency transactions and accounts using the temporal method. Monetary assets and liabilities are translated at the exchange rate in effect on the balance sheet date. Non-monetary assets and liabilities are translated at the exchange rate in effect on the transaction date. Expenses are translated at monthly average exchange rates. Foreign currency translation gains and losses are reflected in the consolidated statements of operations and deficit, except for those gains and losses that relate to the deferred petroleum exploration costs which are deferred.

Use of estimates, risks and uncertainties

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. While management believes that these estimates and assumptions are reasonable, actual results could vary significantly.

A significant area requiring the use of management estimates relates to the recoverability of the deferred petroleum exploration costs. Realization of the company's assets is subject to risks and uncertainties, including reserves estimation; future oil and gas prices; estimated costs of future production; changes in government legislation and regulations; and various operational factors.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

Capitalization of interest

The company capitalizes interest to deferred petroleum exploration costs until commencement of commercial production.

Income taxes

Income taxes are calculated using the liability method. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse. A valuation allowance is applied to the extent that it is more likely than not that future income tax assets will not be realized.

Stock-based compensation

The company applies the fair value method of accounting for stock-based compensation for both employees and non-employees. The fair value method requires recognition of an expense arising from stock options granted to both employees and non-employees, at the date of grant, in an amount equal to the fair value of the options granted. The fair value of option grants is generally established at the date of grant using the Black-Scholes option pricing model, and the compensation expense, equal to the option's fair value, is then recognized over the option's vesting periods. Consideration paid for shares on exercise of a stock option is credited to capital stock.

Asset retirement obligations

Asset retirement obligations are recorded for statutory, contractual, or legal obligations associated with the retirement of property, plant and equipment, when those obligations result from the acquisition, construction, development, or normal operation of the assets. The obligations are measured initially at fair value (using present value methodology), and the resulting costs capitalized into the carrying amount of the related asset. In subsequent periods, the liability is adjusted for the accretion of discounts and any changes in the amount or timing of the underlying future cash flows. The related asset is adjusted only as a result of changes in the amount or timing of the underlying cash flows. The capitalized asset retirement cost is depreciated on the same basis as the related asset; discount accretion is included in determining the results of operations. Management has determined that, based on the exploration work carried out to date, there is no legal obligation requiring remediation of the company's oil and gas property at this time.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

3 Changes in accounting policies

Variable interest entities

The company has adopted Accounting Guideline 15, "Consolidation of Variable Interest Entities" issued by the Canadian Institute of Chartered Accountants for annual and interim periods beginning on or after November 1, 2004. This guideline addresses the application of consolidation principles to entities that are subject to control on a basis other than ownership of voting interests. The adoption of this guideline did not have any impact on the company's consolidated financial statements.

4 Deferred petroleum exploration costs

	2006	2005
	\$	\$
Drilling and exploration	5,471,552	5,471,552
Consulting fees	5,629,392	5,007,799
Interest	3,561,432	2,971,468
Deferred costs acquired	1,394,307	1,394,307
Project administration	1,721,911	1,485,604
Salaries and benefits	946,727	908,438
Travel and accommodation	919,737	822,016
Contract signing fee	539,917	539,917
Foreign exchange (gain) loss	(859,183)	85,976
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	19,325,792	18,687,077
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Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

The company and Primeline Petroleum Corporation (PPC), an affiliated company, are contractors (collectively, the Contractors) to the Petroleum Contract dated March 24, 2005 with CNOOC to explore, develop and produce oil and gas reserves that may exist in an area known as Block 25/34 (the Contract Area) in Lishui and Oujian Grabens, East China Sea. The Contract Area covers 7,006 square kilometres, including the majority of previous Block 32/32 (including the Lishui 36-1 (Vicky) gas discovery) under another petroleum contract between the Contractors and CNOOC which was in effect during the period from December 12, 1994 to February 28, 2005. The company and PPC hold 75% and 25% of the Contractors' interest, respectively. The Petroleum Contract became effective on May 1, 2005, and has three periods: exploration, development and production, with a maximum contract term of 30 years. The exploration period is normally seven years while the production period is normally 15 years. The exploration period is further subdivided into three exploration phases, which includes the first phase of three contract years (the first contract year through the third contract year); the second phase of two contract years (the fourth contract year through the fifth contract year); and the third phase of two contract years (the sixth contract year through the seventh contract year). The Contractors are committed to drilling one exploration well in each of the three exploration phases (with additional 200 square kilometres of 3D seismic in phase one) and expending minimum qualifying exploration costs of US\$6,000,000 in the first phase and US\$5,000,000 in each of the second and third phases. At the end of each of the first and second exploration phases, the Contractors must decide whether to enter into the next exploration phase and relinquish 25% of the remaining Contract Area, or terminate the Petroleum Contract. At the end of the third exploration phase, the Contract Area, except any discovery, development, production area that may exist in the Contract Area, is relinquished.

The Petroleum Contract provides that the Contractors will fund all costs incurred during the exploration period, and CNOOC has the right to participate up to 51% in any future development and production of oil and/or gas fields in the Contract Area by paying its pro rata share of the development and production costs. The Contractors remain as operators for the development and production period until at least full cost recovery.

5 Advances from Primeline International (Holdings) Inc.

	2006	2005
	\$	\$
Principal	4,761,594	4,896,830
Interest	3,560,912	2,971,468
Total	<u>8,322,506</u>	<u>7,868,298</u>

The amounts due to Primeline International (Holdings) Inc. (PIHI) of \$8,322,506 (4,132,327 GBP) (2005 - \$7,868,298 (3,459,355 GBP)) bear interest at the Bank of England's prime rate plus 3% and are due one year plus one day from the date of demand for repayment. Interest charges accrued during the year amounted to \$589,444 (2005 - \$576,163) and have been recorded as deferred petroleum exploration costs. All amounts owing to PIHI are denominated in Great British Pounds. On April 4, 2006, a total of \$7.9 million of the advances outstanding were converted into units of the company (see note 12).

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

6 Capital stock and contributed surplus

a) Authorized

	<u>Number of shares</u>		
	<u>2006</u>	<u>2005</u>	
Common shares with a par value of US\$0.001 each	500,000,000	50,000,000	
Issued and outstanding			
	Number of common shares	Amount \$	Contributed surplus \$
Balance - March 31, 2004	23,987,290	32,807	12,533,991
Fair value of options	-	-	25,008
Balance - March 31, 2005	23,987,290	32,807	12,558,999
Exercise of options	1,100,000	1,504	353,496
Fair value of options	-	-	235,159
Balance - March 31, 2006	25,087,290	34,311	13,147,654
		2006	2005
Weighted average number of common shares outstanding		24,619,619	23,987,290

At the Annual and Extraordinary General Meeting held on August 30, 2005, the shareholders of the company approved to increase the authorized capital of the company from US\$50,000 divided into 50,000,000 shares of a nominal or par value of US\$0.001 each to US\$500,000 divided into 500,000,000 shares of a nominal or par value of US\$0.001 each by creating an additional 450,000,000 shares of a nominal or par value of US\$0.001 each.

b) Stock options

The company has a stock option plan (the Plan), pursuant to which the directors are authorized to grant up to 10% of the issued and outstanding common shares in options. The options enable the directors, officers, consultants and employees to acquire common shares. The exercise price of a share option will be set by the board of directors and will not be less than the Discounted Market Price of the company's common shares on the day preceding the grant date. Options granted under the Plan generally have a term of five years and vest in stages over 12 months with no more than 25% of the options vesting in any three-month period, as determined by the board of directors at the grant date.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

The following table summarizes information about the stock options outstanding and exercisable at March 31, 2006 and 2005:

	2006		2005	
	Options outstanding	Weighted average exercise price \$	Options outstanding	Weighted average exercise price \$
Outstanding - Beginning of year	1,425,000	0.33	1,225,000	0.35
Granted	-	-	200,000	0.20
Exercised	(1,100,000)	0.32	-	-
Expired	(325,000)	0.35	-	-
Outstanding - End of year	-	-	1,425,000	0.33
Options exercisable - End of year	-	-	1,247,465	-

On July 14, 2000, the company granted 1,225,000 options at an exercise price of CA\$0.35 per share to directors, officers, consultants and employees of the company entitling them to purchase shares in the company until July 14, 2005. Before the expiry date, 900,000 options were exercised and on July 15, 2005, the unexercised 325,000 options were cancelled.

On February 18, 2005, the company granted 200,000 options at an exercise price of CA\$0.20 per share to Port Mercantile Capital Inc., a corporate communications advisor, entitling it to purchase shares in the company. The options were exercised on February 18, 2006. The fair value of the 200,000 options granted was measured at the date services were completed for an overall average of \$1.30 per option, and expensed over the service period, for total compensation expense of \$260,167, using the Black-Scholes option pricing model. A total of \$235,159 has been expensed in the year ended March 31, 2006 (2005 - \$25,008).

Assumptions used in the Black-Scholes option pricing model for measurement of the options during the year ended March 31, 2006 are as follows:

Risk-free interest rate	2.78% - 4.01%
Expected life	1 year
Expected volatility	104% - 235%
Expected dividends	Nil

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

Option pricing models require the input of highly subjective assumptions, including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate and, therefore, the existing models do not necessarily provide a reliable single measure of the fair value of stock options granted by the company.

7 Commitments

- a) The company, through PPC, entered into an agreement on January 1, 2001 with a consultant for advice on corporate governance and structure, contract negotiations and financial issues relating to the operations and capital of PEHI. The agreement shall continue until determined by not less than six months' notice in writing by either party to the other. Payment under the agreement amounts to \$3,430 (1,500 GBP) per month.
- b) On October 26, 2005, the company entered into an agreement for re-processing of 233 square kilometres of 3D seismic data that the company acquired in 1998 over the Lishui 36-1 gas discovery. The re-processing was completed in April 2006 with a total cost of \$322,913 (RMB2,193,700), of which \$82,064 (RMB557,500) had been paid during the year and the balance of \$240,849 (RMB1,636,200) was paid in June 2006.
- c) The company entered into a lease agreement for the rental of PEHI's Shanghai office in the PRC. The lease is for a period of three years from August 24, 2005 to August 31, 2008 with a monthly rental fee of \$4,260 (RMB28,946).
- d) The company has minimum qualifying exploration commitments of \$6,000,000 in phase 1 and \$5,000,000 in both phases 2 and 3 of the exploration period of the petroleum contract (see note 4).

8 Related party transactions

During the year ended March 31, 2006, the company paid the following:

- a) Shanghai office rent of \$86,412 (2005 - \$89,792) to a company under common control of which the shareholder of that company is also the shareholder of the company's ultimate holding company, PIHI, a private British Virgin islands corporation, all of the issued and outstanding shares of which are beneficially owned by Mr. Victor Hwang, president and a director of the company, and members of the Hwang family.
- b) fees and expenses of \$28,272 (2005 - \$30,102) to a company controlled by Mr. Peter Kelty, a director for investor relations, securities exchange matters and other administrative services.

These transactions, which occur in the normal course of operations, are measured at the exchange amount, which is the amount of the consideration established and agreed to by the related parties.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

Other related party balances are disclosed elsewhere in these consolidated financial statements.

9 Income taxes

The company is domiciled in an income tax-exempt jurisdiction and carries out its oil exploration activities in the PRC; these activities are subject to PRC income tax at a rate of 33%. In accordance with PRC tax regulation, exploration costs incurred by foreign oil and gas enterprises can be deferred and amortized from commencement of oil/gas production. As there are no differences between the accounting and tax treatment of exploration costs, there are no resulting temporary differences.

10 Financial instruments

Interest rate exposure

All of the company's financial instruments are non-interest bearing except cash and cash equivalents, which earn interest at a floating rate, and advances from PIHI, which bear interest as described in note 5.

Fair value of financial assets and liabilities

The fair values of cash and cash equivalents and accounts payable and accrued liabilities approximate to their carrying values due to the short-term nature of those instruments.

Management has determined that it is not practical to determine the fair value of advances from PIHI because of the lack of availability of similar borrowing arrangements on an arm's-length basis.

11 Segmented reporting

The company's principal activity is the exploration of oil and gas properties. The company's oil and gas property is located in China as described in note 4.

Primeline Energy Holdings Inc.

(an exploration stage company)

Notes to Consolidated Financial Statements

March 31, 2006 and 2005

12 Subsequent events

a) Private Placement, debt conversion and granting of options

On February 22, 2006, the company announced a private placement (the Private Placement) of up to \$25 million by issuance of up to 16,666,666 Units of the company at a price of \$1.50 per Unit (the Offering), each Unit consisting of one common share of the company and one-half of one common share purchase warrant, each full warrant being exercisable at a price of \$2.00 per share, for a term of two years from closing of the Private Placement. Compensation for the financing consisted of a commission of 6.5% of the gross proceeds of the Offering, agents' Warrants equal to 5% of the Units sold under the Offering, and a 2% finder's fee, payable in cash.

In conjunction with the closing of the Private Placement, the company's major shareholder, PIHI agreed to convert \$7.9 million of advances into 5,266,667 Units of the company, at a debt conversion price of \$1.50 per Unit, such Units to be issued on the same terms and conditions as the Units issuable upon the Private Placement.

The Private Placement was completed on April 4, 2006, with a net proceeds of about \$22 million. The securities issued under the Private Placement are subject to a four-month hold period. On the same date, the debt conversion was completed and 4,500,000 options were granted to directors, officers, employees and consultants, such options to be exercisable at a price of \$1.50 per share for a term of five years.

b) 3D seismic survey in Block 25/34

On May 9, 2006, the company signed a geophysical services contract with China Oilfield Services Ltd. (COSL) for the planned 3D seismic survey over the identified prospects and leads near its existing gas discovery Lishui 36-1 in Block 25/34 in the East China Sea. The survey was designed to better evaluate the nearby prospects to the existing gas discovery Lishui 36-1, and is a crucial step in the selection of the next well location. The survey commenced on May 30, 2006 and is estimated to last approximately two months, with processing and interpretation planned for the second half of 2006. The total costs of the survey are estimated to be approximately US\$6 million to US\$7 million depending on the outcome of variables in operations and weather conditions.

FORM 51-101F1
STATEMENT OF RESERVES DATA
AND OTHER OIL AND GAS INFORMATION

DATE OF STATEMENT

This Form 51-101 F1 submitted by Primeline Energy Holdings Inc. (“PEH” or the “Company”) is related to events and activities with an effective date of the March 31 2006. The statement is dated and prepared as at July 14, 2006

DISCLOSURE OF RESERVES DATA

Primeline Energy Holdings Inc. currently has no proven or probable reserves in its property that can be categorized in accordance with the principles and definitions presented in the COGE Handbook.

OIL AND GAS PROPERTY AND LICENSE STATUS

The Company, under a Petroleum Contract with China National Offshore Oil Corp. (“CNOOC”), owns exclusive rights and undertakes petroleum operations in the 7,006 sq. km Block 25/34 in the East China Sea. Primeline Energy China Ltd. (“PECL”), a wholly owned subsidiary of the Company, and Primeline Petroleum Corporation (“PPC”) (Jointly as “Primeline”), an affiliated company, are jointly “Contractor(s)” in the Petroleum Contract. PECL and PPC own 75% and 25% of the Contractor’s interest respectively in the said Contract. Primeline Energy Operations International Ltd. (“PEOIL”), another wholly owned subsidiary of the Company, is designated as “Operator” of the Petroleum Contract.

Pursuant to the Petroleum Contract, the Contractor will fund all the exploration expenditure during the exploration phase and CNOOC has the right to participate in up to 51% of any commercial development by paying its pro rata share of the development costs. The exploration period is 7 years, divided into 3 phases of 3, 2, 2 years. The Contractor commits to a minimum work program and budget in each exploration phase. In the first phase of the Exploration Period (ending April 30 2008), the Contractor is committed to acquire at least 200 sq km of 3D seismic and drill one well, with a minimum expenditure of US\$6m. At the end of each of the first and second exploration phases, the Contractor must decide whether to enter into the next exploration phase and relinquish 25% of the remaining Contract Area, or terminate the Petroleum Contract. At the end of the third exploration phase, the Contract Area, except for any discovery that may exist in the Contract Area, is relinquished.

The Petroleum Contract for Block 25/34 is the continuation of the Company’s activities in the Lishui Basin in the East China Sea under a previous Petroleum Contract for Block 32/32. On February 28, 2005, the Petroleum Contract for Block 32/32 officially expired and Primeline applied to terminate the Contract whilst negotiating a new contract with CNOOC. The Petroleum Contract for Block 25/34 was signed on March 24, 2005 in the People’s Great Hall in Beijing. Subsequently, the Contract was ratified by Ministry of Commerce of China on 22nd April 2005 and became effective on 1st May 2005. Phase one exploration period will expire on 30th April 2008, otherwise, the total Contract may extend up to 30 years, including development and production periods.

Block 25/34 covers a total area of 7,006 sq kms (net to Company 5,255 sq km) in the East China Sea in water depth between 75 and 90 metres. It is located approximately 100 km from the coast of China. The Block covers all the material areas of Primeline’s previous Block 32/32, including

the Lishui 36-1 (Vicky) gas discovery and its surrounding area, particularly, the majority of the deep part of the Lishui basin.

Primeline made the Lishui 36-1 (Vicky) gas discovery in 1997 in the Lishui Graben in the East China Sea under the Petroleum Contract for Block 32/32. Two appraisal wells were drilled on the discovery during 2000 and 2001. The discovery well and the first appraisal well proved that sizeable hydrocarbon resources exist in the discovery and the Block.

The discovery is located in the deepest part of the Lishui Graben in the East China Sea which is a Tertiary rift basin developed on the western margin of the Pacific tectonic plate. The main reservoir discovered is the Paleocene Lingfeng Formation sandstone buried at the location of the Lishui 36-1 discovery at around 2500m. The discovery is 140 km from the city of Wenzhou, a city with a population of around 2 million people on the Chinese coast.

The Company has net 75% interest in the discovery and the Petroleum Contract subject to future CNOOC back-in rights as described above.

EXPLORATION AND DEVELOPMENT ACTIVITY

The Company has participated in two gas wells and one dry well under the previous Petroleum Contract 32/32.

- Well LS36-1-1 (Vicky-1) was drilled in October 1997 as a gas discovery, testing at 9.86 MMSCFD.
- Well LS36-1-2 was drilled in December 2000 as the first appraisal well and confirmed the gas discovery by testing at 12.62 MMSCFD.
- Well LS36-1-3 was drilled in December 2001 as the second appraisal well and was abandoned without encountering hydrocarbons.
- A 3D seismic survey covering 233 square kilometers was acquired in 1998 around the Lishui 36-1 discovery.

All the above well and seismic area are included in the current Block 25/34.

During fiscal year 2005/2006, the Company undertook geological and geophysical works as follows:

- Acquired all existing 2D seismic data and well information for Block 25/34 from CNOOC
- Integrated these data into the existing Primeline database
- Commenced the geological and geophysical analysis of the regional potential in the Block.
- Reprocessed the 233 sq km of 3D seismic data over the discovery which was acquired by the Company in 1998
- Designed and commenced the 3D seismic survey over the analogous and related nearby prospect and leads around the gas discovery.
- Completed Phase One of the 3D survey (after yearend 2005/2006) and commenced processed (July 2006).

The Company did not participate in any drilling activity during fiscal year 2004/2005. The total exploration expenditure during the fiscal year of 2005/2006 was C\$993,910 (excluding interest and exchange gain).

In the next fiscal year, the Company plans to

- ◆ Continue and complete the current 3D survey near the discovery
- ◆ Process and interpret the 3D data leading to recommendations for well locations

- ◆ Continue the regional evaluation of the Block, build up prospect inventories
- ◆ Based on the result of the above work program, design and drill one or two wells subject to rig availability

TAX HORIZON

The Company was not required to pay income taxes during the year ended March 31, 2006. The Company estimates that it will not be required to pay income taxes to Chinese Authorities until there is a commercial development.

FORM 51-101F2
REPORT ON RESERVES DATA
BY
INDEPENDENT QUALIFIED RESERVES
EVALUATOR OR AUDITOR

To the board of directors of Primeline Energy Holdings Inc. (the "Company"):

1. We have evaluated and reviewed the Company's reserves data as at March 31, 2006. It is our opinion that the Company has no reserves that can be categorized in accordance with the principles and definitions presented in the COGE Handbook (as defined below).
2. The reserves data are the responsibility of the Company's management. Our responsibility is to express an opinion on the reserves data based on our evaluation and review.

We carried out our evaluation and review in accordance with the standards set out in the Canadian Oil and Gas Evaluation Handbook (the "COGE Handbook") prepared jointly by the Society of Petroleum Evaluation Engineers (Calgary Chapter) and the Canadian Institute of Mining, Metallurgy & Petroleum (Petroleum Society).

3. Those standards require that we plan and perform an evaluation and review to obtain reasonable assurance as to whether the reserves data are free of material misstatement. An evaluation and review also includes assessing whether the reserves data are in accordance with the principles and definitions presented in the COGE Handbook.
4. Because the reserves data are based on judgments regarding future events, actual results will vary and the variations may be material.

Dated the 24th day of July, 2006.

RPS ENERGY CANADA LIMITED

Per: Signed "*Robert Dick*"
Robert Dick
Director

FORM 51-101F3
REPORT OF MANAGEMENT AND DIRECTORS
ON OIL AND GAS DISCLOSURE

Management of Primeline Energy Holdings Inc. (the "Company") is responsible for the preparation and disclosure of information with respect to the Company's oil and gas activities in accordance with securities regulatory requirements. The Company has no reserves as at March 31, 2006.

At this time, management considers that the Company has no reserves that fall into the categories required for reporting purposes. This has been confirmed by an independent qualified reserves evaluator who has evaluated and reviewed the Company's reserves data. The report of the independent qualified reserves evaluator will be filed with securities regulatory authorities concurrently with this report.

The board of directors of the Company has:

- (a) reviewed the Company's procedures for providing information to the independent qualified reserves evaluator;
- (b) met with the independent qualified reserves evaluator to determine whether any restrictions affected the ability of the independent qualified reserves evaluator to report without reservation; and
- (c) reviewed the reserves data with management and the independent qualified reserves evaluator.

The board of directors has reviewed the Company's procedures for assembling and reporting other information associated with oil and gas activities and has reviewed that information with management. The board of directors has approved:

- (a) the content and filing with securities regulatory authorities of the reserves data and other oil and gas information;
- (b) the filing of the report of the independent qualified reserves evaluator on the reserves data; and
- (c) the content and filing of this report.

Because the reserves data are based on judgments regarding future events, actual results will vary and the variations may be material.

Dated this 24th day of July, 2006.

Signed "Victor Hwang"
Victor Hwang
President

Signed "Guang Ming Wang"
Guang Ming Wang
Chief Executive Officer

Signed "Brian Chan"
Brian Chan
Chief Financial Officer and Director

Signed "Peter Kelty"
Peter Kelty
Director

**PRIMELINE ENERGY HOLDINGS INC. (TSX VENTURE-PEH)
MANAGEMENT DISCUSSION AND ANALYSIS FOR QUARTER ENDED
MARCH 31, 2006 AND 2005/2006 YEAR-END
(PREPARED BY MANAGEMENT)**

Introduction

This management discussion and analysis, which takes into account information available up to July 11, 2006, should be read in conjunction with the audited consolidated financial statements for year ended March 31, 2006, which have been prepared in accordance with Generally Accepted Accounting Principles in Canada. All amounts in this discussion and analysis are expressed in Canadian dollars, unless otherwise noted.

Cautionary Note Regarding Forward-Looking Statements

Except for historical information contained in this discussion and analysis, the following disclosures contain forward-looking statements that are made based on management's judgment and expectations, but are inherently subject to risks and uncertainties beyond management's and the Company's control. These risks and uncertainties include the recoverability of the deferred exploration costs; realisation of the Company's assets including reserves estimation; future oil and gas prices; estimated costs of future production; changes in government legislation and regulations; various operational factors, and the procurement of new financing or new exploration partners to enable the Company to continue its exploration activities. Actual results may differ materially from those anticipated in the forward-looking statements. The Company assumes no obligation to update its forward-looking statements to reflect actual results, changes in assumptions or changes in other factors affecting such statements.

Company and Project Overview

Primeline Energy Holdings Inc. ("PEHI" or the "Company") is an independent energy company that is focusing exclusively on upstream opportunities in China. The Company, under a Petroleum Contract with China National Offshore Oil Corp. ("CNOOC"), owns rights and operates in Block 25/34 in the East China Sea. Primeline Energy China Ltd. ("PECL"), a wholly owned subsidiary of the Company, and Primeline Petroleum Corporation ("PPC") (collectively referred to as "Primeline"), an affiliated company, are jointly "Contractors" in the Petroleum Contract. PECL and PPC own 75% and 25% of the Contractors' interests respectively in the Contract. Primeline Energy Operations International Ltd. ("PEOIL"), another wholly owned subsidiary of the Company, is designated as "Operator" of the Petroleum Contract.

Annual Progress Review

Petroleum Contract for Block 25/34, East China Sea

Primeline has been operating in the East China Sea since 1994, initially under a Petroleum Contract for Block 32/32. Primeline made a gas discovery (Lishui (LS) 36-1 or Vicky) in 1997 in the Lishui Basin in the East China Sea and joint-ventured with CNOOC on two appraisal wells on the discovery which were drilled during 2000 and 2001. The discovery well and the first appraisal well proved that sizeable hydrocarbon resources exist in the discovery. However, at that time, such resources did not justify a commercial development based on market conditions and infrastructure requirements.

Management of the Company believes that there is sufficient potential in the Basin to justify further exploration and that only a relatively modest additional resource would be required to justify commercial development of the discovery. Accordingly, when the Petroleum Contract for Block 32/32 expired, the Company entered into negotiations with CNOOC which resulted into the signing of the Petroleum Contract for Block 25/34 on 24th March 2005, thereby enabling the Company to continue its efforts to commercialise the discovery. The Petroleum Contract was subsequently ratified by the Ministry of Commerce of China on 22nd April and became effective on 1st May 2005.

Block 25/34 extends over a total area of 7,006 sq kms in the East China Sea, covering all of the material parts of the area of Primeline's previous Block 32/32, including the Lishui 36-1 (Vicky) gas discovery, and the majority of the deep part of the Lishui Basin. Near the gas discovery there are several analogous prospects and leads that have similar geological and geophysical characteristics including similar direct hydrocarbon indicators such as Bright Spots and Amplitude Variation with Offset (AVO). The potential natural gas resources in place in these prospects and leads, if successfully tested, could be sufficient to justify a commercial development.

In the Lishui Basin there are a total of seven previously drilled wells (in addition to Primeline's discovery) that have encountered various hydrocarbon occurrences (shows or flows). Management of the Company believes that these wells, together with Primeline's discovery, prove the existence of very extensive oil and gas play(s) in the basin. Primeline's discovery and first appraisal well also produced commercial rates of hydrocarbon flow. Based on this information and its exploration work, Primeline is extremely excited about the remaining potential of the Basin. Primeline is undertaking a preliminary review and has identified numerous prospect leads additional to those in the vicinity of LS 36-1. Whilst an extensive programme of data gathering and interpretation will be required to convert these leads to drillable prospects, Primeline is very positive about the remaining potential of this basin which is anticipated to have oil as well as gas potential.

Technical Work Overview

A significant challenge in the oil industry today, due to the current high oil prices and consequent high level of global activity, is the shortage of available resources, both equipment and personnel. This shortage results in increased costs and longer lead times for any planned work programmes. Since the commencement of the Petroleum Contract for Block 25/34, the Company has worked diligently to meet this challenge and has been

able to secure the necessary resources in order to carry out the following exploration work:

Geophysical and Geological Evaluation of the Existing Data

In autumn 2005, the Company acquired from CNOOC all the existing seismic data and well information inside Block 25/34. This seismic data was integrated into Primeline's pre-existing database and, in November 2005, a regional evaluation was commenced utilising over 23,000 km of digital 2D seismic data and information from 12 wells within the Lishui Basin. This regional evaluation will identify and document the exploration potential in the Basin to provide the Company with prospect inventories that will guide future exploration work programmes.

In order to better define the existing Lishui 36-1 gas discovery, Primeline decided to reprocess the existing 233 sq km of 3D seismic data over the existing gas discovery which was acquired by the Company in 1998. Following an extensive trial and test programme, Primeline awarded the reprocessing contract to Hispec Research Corp. ("Hispec") (<http://www.hispecgeo.com>) in October 2005.

Hispec is a geophysical service company specialising in seismic processing. They have developed leading-edge processing techniques and software which have been successfully applied to reprocess the existing data held by Primeline. Hispec completed the reprocessing in April 2006 and achieved significantly improved quality of the data which has allowed Primeline to commence a new in-depth evaluation of the gas discovery. The objective is to produce a detailed reservoir model that will be used for development planning.

New 3D Seismic Survey

The main work programme for 2006 is to acquire new 3D seismic data over the wider area of the Lishui 36-1 gas play to better evaluate the analogous and related nearby prospects to the existing gas discovery. The 3D reprocessing confirmed that it was not necessary to re-shoot seismic over the Lishui 36-1 discovery. As a result, Primeline has decided to focus its efforts on the surrounding prospects and leads. The interpretation of this new data, integrated with the reprocessed 3D data, will be important for the selection of the next well locations.

The design of the new 3D survey was finalised in April 2006 and, in very competitive market conditions, the Company secured a vessel for its survey from China Oilfield Services Ltd. ("COSL") (<http://www.cosl.com.cn>). The geophysical services contract for the new 3D seismic survey was signed on 9th May 2006 and the survey commenced on 30th May using vessel Binhai 512, one of four-streamer seismic vessels owned by COSL, a Hong Kong Stock Exchange listed company. COSL is the leading oilfield services provider in the offshore China market and its services cover every phase of oil and gas exploration, development and production.

COSL completed the Phase One survey of over 300 sq km of 3D seismic data in early July 2006. The Phase One survey data was transferred to shore where COSL immediately commenced processing the data. The vessel Binhai 512 then departed the East China Sea to fulfil its commitments in another region. The vessel will return to Primeline's survey in late August for acquisition of additional data, originally designated as a Contingency Programme by Primeline.

The Company is very pleased with the current progress of the new 3D seismic programme. The Phase One survey, which is currently being processed, covered the area to the west of Lishui 36-1 discovery which is the area of greatest interest to the Company. Furthermore, the Company has secured a vessel to survey the area to the north and east of the existing discovery. Originally, the Company did not expect this Phase Two programme to be completed this year as vessel availability is so scarce.

The Company plans to drill one or two wells in the gas play aiming to increase the current resource base in order to justify a commercial development. The drilling campaign is planned to commence around the end of 2006 or early in 2007, subject to rig availability. The Company is currently in discussions with drilling contractors to secure a rig for the drilling programme.

Corporate Development

During the year, the Company has made significant progress in its corporate development.

The Company's past 10 years' operations were funded through the support of its major Shareholder, Primeline International Holdings Inc. ("PIHI"), which is controlled by Mr. Victor Hwang. Through these operations, the Company made a significant gas discovery with sizeable resources and acquired a Petroleum Contract for a vast concession of the East China Sea with huge exploration potential. As a result, the Company has been able to obtain institutional funding to support its future exploration work. The Company completed a Private Placement of \$25m, arranged by Jennings Capital Inc. as agent, in April 2006. At the same time, PIHI converted \$7.9 million of debt to shares on the same terms of the Private Placement.

As a result of the Private Placement, the Company now has a significant number of new shareholders, many from major global financial institutions. The Company is now debt free and fully funded for the work programme committed in the current Contract Phase. The Private Placement has also served to increase the awareness of the Company in the global market place, thus strengthening the Company's ability to obtain future funding.

During the year, the Company confirmed the appointment of Dr. Ming Wang as CEO (September 2005) and Graeme Phipps was appointed as an independent director (March 2006).

The Company is committed to further strengthening of its management team to ensure that the Company's operations are efficiently and professionally implemented. At the same time, the Company will continue to improve its corporate communications programme to ensure that the underlying value of the Company's project is fully understood by the investment community.

Gas Market Development

The Company continues its efforts to develop the market for the gas resources in its property. The continued expansion and rapid development of the Chinese economy has considerably enhanced the market options and potential value of the gas resources from Block 25/34. The Lishui 36-1 gas discovery is only 140 km from the major industrial coastal city of Wenzhou which is the closest potential market for any gas production from the Block.

China Energy Overview

The growth in China's economy has resulted in a sharp increase in demand for energy. In 1996, China became a net oil importer for the first time. Ten years later, China imports over 40% of its crude requirements, consuming over 6 million barrels a day. Today, China is the world's second largest oil consumer, although, on a per capita basis, China's consumption is still less than one tenth of that of the United States.

High international oil prices and environmental concerns have both served to increase the world's demand for cleaner natural gas. Currently, world gas consumption constitutes about 25% of the entire energy mix, whilst in China it is only about 3%. China's natural gas industry is still in the early stages of development, but natural gas development and utilisation is a key government energy policy. Construction of various major gas infrastructures has commenced in the last 5 years, including:

- A 4000+ km long "West to East Gas Pipeline" - this pipeline is intended to link Shanghai and all the cities along the line to the gas fields in the Tarim basin (completed) and eventually to the Central Asian resources.
- LNG terminals along the coast - the first terminal in Shenzhen received the first shipment in May 2006, and there are at least six other terminals under construction and planning.
- A coastal national gas grid intended to link major coastal cities is currently under development.

The gas resources from Block 25/34 are ideally positioned to benefit from this new government initiative and improved infrastructure.

Wenzhou's New Development

Wenzhou is a city of 2 million people with an administrative region that covers a population of 7 million. It is one of the most dynamic economies in China. The last ten

years have seen the continuation of growth in the region, with GDP tripling and export values increasing by over 12 times. Wenzhou is now one of the major manufacturing areas with a very high market share in China and the world for products such as shoes, garments, spectacles, metal-case cigarette lighters, hardware and electrical equipment, motor car parts and pumps.

For many years, Wenzhou's development has been hampered by the shortage of land and energy resources and industrial infrastructure. The local government has been striving to rectify the situation by implementing a policy of improving the infrastructure, with the construction of motorways, railways, port facilities, power stations as well as major reclamation projects. Many of these projects have been implemented and completed in the last five years.

The "Peninsula Project" is one of the projects intended to implement the new Wenzhou economic strategy and turns Wenzhou into a more dynamic city with a greater mix of industries. This project includes the construction of roads and bridges linking the mainland with the five main islands offshore, major port facilities and reclamation of over 20 sq km of land along a 14 km dam. The project started about three years ago and is near completion. The reclaimed land will be mainly used for industrial installations. This establishment of the infrastructure and facilities on the islands will potentially shorten the planned pipeline from Block 25/34 to market from 140 km to around 100 km.

The development of Wenzhou's local economy and that of the entire East China Region has given Primeline improved confidence that the a commercially sustainable local gas market price will be established. The Company is continuing its discussions with the local government and industry in preparation for a gas sales contract once the Block 25/34 gas resource base is adequately increased. Whilst the demand from Wenzhou's local economy is more than sufficient to absorb Primeline's currently identified gas resources plus significant expansion of these resources, there are also many other nearby markets of a similar scale along the East China Coast which provide the demand to justify an accelerated exploration programme in the remainder of Block 25/34.

Financial Information

Results of Operation

The Company's audited results for the financial year ended March 31, 2006 were a loss of \$588,037 compared to a loss of \$215,693 for the previous year. The increase in loss of \$372,344 or 173% was mainly due to the \$113,305 increase in professional fees because of the additional consultancy fee for corporate communications and an increase in financing activities. In addition, the recognition of stock-based compensation was increased by \$210,151 on the 200,000 options granted on February 18, 2005. Loss per share was \$0.024 (2004 - \$0.009).

The Company has been financially supported by PIHI to carry out its exploration program and day-to-day operations by way of shareholder's loan which denominated in

Great British Pounds (GBP). The Canadian dollar experienced an appreciation against the GBP. The exchange rate for the GBP which started in the fiscal year at GBP1.00/C\$2.275, ended the fiscal year at GBP1.00/C\$2.014, an appreciation of 11.5%. The currency exchange gain of \$950,579 in respect of the shareholder's loan for the year was capitalized to the deferred petroleum exploration costs.

Liquidity and Capital Resources

As at March 31, 2006, net current liabilities of the Company amounted to \$171,400 whereas net current assets of \$10,985 was recorded in the previous year. The current ratio for the year was 0.60:1 (2005 - 1.14:1). The increase in net current liabilities of \$182,385 was mainly due to an increase of accounts payable of \$356,730.

During the year, exploration expenditures of \$638,715, net of foreign exchange gains of \$950,579 (2005 - \$500,485 which included an exchange gain of \$438,854) were incurred which were mainly financed by a shareholder's loan. As at March 31, 2006, the total amount of deferred petroleum exploration expenses incurred and capitalized amounted to \$19,325,792 (2005 - \$18,687,077) which may be broken down as follows:

	2006	2005
	\$	\$
Drilling and exploration	5,471,552	5,471,552
Consulting fees	5,629,392	5,007,799
Interest	3,561,432	2,971,468
Deferred costs acquired	1,394,307	1,394,307
Project administration	1,721,911	1,485,604
Salaries and benefits	946,727	908,438
Travel and accommodation	919,737	822,016
Contract signing fee	539,917	539,917
Foreign exchange (gain)loss	(859,183)	85,976
	<u>19,325,792</u>	<u>18,687,077</u>

The project administration may further be broken down as follows:

	2006	2005
	\$	\$
Bank charges	9,807	9,644
Consulting fees	13,359	13,359
Office rental	1,103,703	993,902
Sundries expenses	397,273	299,959
Postage	22,965	21,947
Printing and stationery	20,594	18,592
Professional fees	103,270	82,394
Telephone	50,940	45,807
	<u>1,721,911</u>	<u>1,485,604</u>

The Company had total assets of \$19,587,949 (2005 - \$18,774,889) which were financed by net shareholders' equity of \$10,831,886 (2005 - \$10,829,764), advances from controlling shareholder, Primeline International (Holdings) Inc. ("PIHI") of \$8,322,506 (2005 - \$7,868,298) and current liabilities of \$433,557 (2005 - \$76,827). The gearing ratio, representing the ratio of total borrowings to total assets, was 42.5% (2005 - 41.9%).

The Company has been financially supported by PIHI to carry out its exploration program and day-to-day operations. This support is provided by way of shareholder's loans. During the year, PIHI advanced \$814,391 to the Company and together with the proceeds from the exercise of stock options of \$355,000, these funds were mainly applied to finance daily administration expenses of \$352,878 and expenditure on deferred petroleum exploration costs of \$998,898 leaving a cash balance of \$158,272 as at March 31, 2006.

The consolidated financial statements are prepared on the basis that the Company will continue as a going concern, which assumes that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. As at March 31, 2006, the Company had net current liabilities of \$171,400 (2005 - working capital of \$10,985) and had a deficit of \$2,350,079 (2005 - \$1,762,042). The private placement on April 4, 2006 provided the Company with sufficient funds to complete its minimum commitments under Phase 1 of its exploration program and for general and administration activities for the next year.

Financial Instruments

Interest rate exposure

All of the Company's financial instruments are non-interest bearing except cash and cash equivalents, which earn interest at a floating rate, a bank overdraft which bears interest at a floating rate, and advances from PIHI which bear interest at a rate of Bank of England's prime rate plus 3%.

Fair value of financial assets and liabilities

The fair values of cash and cash equivalents, accounts payable and accrued liabilities approximate to their carrying values due to the short term to maturity of those instruments.

Management has determined that it is not practical to determine the fair value of advances from PIHI because of the lack of availability of similar borrowing arrangements on an arm's-length basis.

Transactions with Related Parties and Directors

During the year ended March 31, 2006, the Company paid

- a) office rent of \$86,412 (2005 - \$89,792) to a company under common control of which the shareholder of that company is also the shareholder of the Company's ultimate holding company, PIHI, a private British Virgin Islands corporation, all of the issued and outstanding shares of which are beneficially owned by Mr. Victor Hwang, President and a director of the Company, and members of the Hwang family.
- b) fees and expenses of \$28,272 (2005 - \$30,102) to a company controlled by Mr. Peter Kelty, a director of the Company, for investor relations, securities and exchange administrative services.

These transactions, which occur in the normal course of operations, are measured at the exchange amount, which is the amount of the consideration established and agreed to by the related parties.

Change in Accounting Policies

Variable interest entities

Effective April 1, 2005, the Company has adopted Accounting Guideline 15, "Consolidation of Variable Interest Entities" issued by the CICA for annual and interim periods beginning on or after November 1, 2004. This guideline addresses the application of consolidation principles to entities that are subject to control on a basis other than ownership of voting interests. The adoption of this guideline did not have any impact on the company's consolidated financial statements.

Disclosure Controls and Procedures

The Company has conducted a review and evaluation of its disclosure controls and procedures, with the conclusion that it has an effective system of disclosure controls, and procedures as defined under MI 52-109. In reaching this conclusion, the Company recognizes that two key factors must be and are present:

- a) the Company is very dependant upon its advisors and consultants (principally its legal counsel) to assist in recognising, interpreting, understanding and complying with the various securities regulations disclosure requirements; and
- b) an active Board and management with open lines of communication.

The Company has a small staff with varying degrees of knowledge concerning the various regulatory disclosure requirements. The Company is not of a sufficient size to justify a separate department or one or more staff member specialists in this area. Therefore the Company must rely upon its advisors and consultants to assist it and as such they form part of the disclosure controls and procedures.

Proper disclosure necessitates that one not only be aware of the pertinent disclosure requirements, but one is also sufficiently involved in the affairs of the Company and/or receives the communication of information to assess any necessary disclosure requirements. Accordingly, it is essential that there be proper communication among

those people who manage and govern the affairs of the Company, this being the Board of Directors and senior management. The Company believes this communication exists.

While the Company believes it has adequate disclosure controls and procedures in place, lapses in the disclosure controls and procedures could occur and/or mistakes could happen. Should such occur, the Company will take whatever steps necessary to minimize the consequences thereof.

Outstanding Share Data

On April 4, 2006, the Company completed a Private Placement and a Debt Conversion resulted in issuing additional 21,933,333 voting common shares and 11,799,999 warrants. On the same date, the Company granted 4,500,000 options to directors, officers, employees and consultants.

As at July 11, 2006, there are 47,020,623 common shares outstanding, 11,799,999 warrants and 4,500,000 stock options outstanding.

Quarter ended March 31, 2006

The Company incurred a loss for the quarter ended March 31, 2006 of \$174,462 compared to \$101,306 for the prior year quarter. The increase in loss was mainly due to the recognition of a \$58,841 stock-based compensation charge during the quarter and a \$85,417 increase in professional fees as a result of the year end audit fee accrual and additional consultancy fees.

During the quarter, \$668,157 of exploration expenditures were incurred, comprising mainly interest expenses of \$131,955, consulting fees of \$397,856, project administration fees of \$65,560. Such amounts were capitalized to the deferred petroleum exploration expenses.

Selected Annual Information

The following information has been extracted from the Company's audited financial statements:

Years Ended March 31,	2006 \$	2005 \$	2004 \$
Net loss	(588,037)	(215,693)	(130,089)
Per basic share	(0.024)	(0.009)	(0.005)
Per diluted share	(0.024)	(0.009)	(0.005)
Total assets	19,587,949	18,774,889	18,257,157
Total long-term financial liabilities	8,322,506	7,868,298	7,182,604

The increase in loss of \$85,604 between 2005 and 2004 was mainly due to the increase of \$58,499 in professional fees, and the recognition of the stock-based compensation of \$25,008.

Summary of Quarterly Results (Unaudited)

Quarter Ended	2006 Mar 31 \$	2005 Dec 31 \$	2005 Sep 30 \$	2005 Jun 30 \$
Net loss	(174,462)	(101,306)	(213,424)	(98,845)
Per basic share	(0.007)	(0.004)	(0.009)	(0.004)
Per diluted share	(0.007)	(0.004)	(0.009)	(0.004)

Quarter Ended	2005 Mar 31 \$	2004 Dec 31 \$	2004 Sep 30 \$	2004 Jun 30 \$
Net loss	(129,743)	(36,819)	(32,188)	(16,943)
Per basic share	(0.005)	(0.002)	(0.001)	(0.001)
Per diluted share	(0.005)	(0.002)	(0.001)	(0.001)

The loss of \$129,743 for the quarter ended March 31, 2005 was due to professional fees of C\$94,987 paid and stock-based compensation of \$25,008 recognised in the quarter. The loss of \$213,424 for the quarter ended September 30, 2005 was mainly due to professional fees of C\$79,847 paid and stock-based compensation of C\$107,789 recognised in the quarter.

The variations in the quarterly loss in 2005 and 2004 were mainly due to the amounts of professional fees paid/accrued for that quarter.

PEHI has a Vancouver investor relations representative, Irene Yu, 1-877-818-0688. PEHI has a website at www.primelineenergy.com. The site features information on PEHI, new releases, background information, technical summary, location maps and photographs.