

CANARGO ENERGY CORP

Form PRE 14A

March 07, 2005

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

SCHEDULE 14A

**Proxy Statement Pursuant to Section 14(a) of the Securities
Exchange Act of 1934
(Amendment No.)**

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

Confidential, For Use of the Commission Only
(as permitted by Rule 14a-6(e)(2))

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Materials Pursuant to Rule 14a-11(c) or
Rule 14a-12

CANARGO ENERGY CORPORATION

(Name of Registrant as Specified in Its Charter)

(Name of Person(s) Filing Proxy Statement, If Other Than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

o Fee paid previously with preliminary materials:

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the form or schedule and the date of its filing.

(1) Amount previously paid:

(2) Form, Schedule or Registration Statement no.:

(3) Filing Party:

(4) Date Filed:

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

TO BE HELD ON MAY 9, 2005

[Date] , 2005

To Our Stockholders:

NOTICE IS HEREBY GIVEN that the 2005 Annual Meeting of Stockholders of CanArgo Energy Corporation (the Company) will be held at the offices of The American Stock Exchange, 86 Trinity Place, New York NY10006 on May 9, 2005 at 3.00 p.m. local time for the following purposes:

1. To elect directors to serve until the next annual meeting of stockholders or until their respective successors are duly elected and qualified;
2. To approve the Company s Change of Control Stock Option Plan; and

3. To transact such other business as may properly come before the annual meeting and any adjournments thereof. The Board of Directors has fixed the close of business on March 14, 2005 as the record date for determination of the stockholders entitled to notice of and to vote at the annual meeting and any postponement or adjournment thereof. All holders of record of shares of the Company s common stock at the close of business on the record date are entitled to vote at the meeting by sending in the proxy voting form PRIOR to the meeting by the specified deadline.

Please complete, date, sign and return the enclosed proxy card promptly to ensure that your shares will be represented at the annual meeting. If you attend the annual meeting you may vote in person unless you hold your shares in street name so please send in your proxy card ahead of time.

IF YOU PLAN TO ATTEND:

Please note that space limitations make it necessary to limit attendance to stockholders and one guest. Admission to the meeting will be on a first-come, first served basis. Registration and seating will begin at 2:30 p.m. Each shareholder will be asked to present valid picture identification, such as a driver s license or passport. Cameras, recording devices and other electronic devices will not be permitted at the meeting. Please ensure you return the proxy card by the deadline (indicated on the proxy card) in order to make sure your votes will be counted.

By Order of the Board of Directors,

Liz Landles
Corporate Secretary

[Date] , 2005, St. Peter Port, Guernsey, British Isles

Table of Contents

<u>ABOUT THE MEETING</u>	3
<i><u>What is the purpose of the annual meeting?</u></i>	3
<i><u>Who is entitled to vote at the meeting?</u></i>	3
<i><u>What are the voting rights of the holders of the Company's common stock?</u></i>	3
<i><u>Who can attend the meeting?</u></i>	3
<i><u>What constitutes a quorum?</u></i>	3
<i><u>How do I vote?</u></i>	3
<i><u>What if my shares are held in Street Name?</u></i>	4
<i><u>Can I change my vote after I return my proxy card?</u></i>	4
<i><u>What are the Board's recommendations?</u></i>	4
<i><u>What vote is required to approve each item?</u></i>	4
<u>GOVERNANCE OF THE COMPANY</u>	4
<i><u>Who are the current members of the Board and Executive Officers?</u></i>	4
<i><u>How does the Board select nominees for the Board?</u></i>	5
<i><u>How does the Board determine which directors are considered independent?</u></i>	6
<i><u>How are non-employee directors compensated?</u></i>	6
<i><u>Certain Relationships and Related Transactions What related party transactions involved directors?</u></i>	7
<i><u>How do shareholders communicate with the Board and the Audit Committee?</u></i>	7
<i><u>Does the Company have a Code of Ethics?</u></i>	8
<u>AUDIT COMMITTEE REPORT</u>	8
<u>EXECUTIVE COMPENSATION</u>	9
<i><u>Compensation Committee Report on Executive Compensation</u></i>	9
<i><u>Compensation Committee Interlocks and Insider Participation</u></i>	12
<i><u>Management Agreements</u></i>	12
<i><u>Summary Compensation Table</u></i>	13
<i><u>Option Grants During the Year Ended December 31, 2004</u></i>	13
<i><u>Equity Compensation Plans</u></i>	14
<i><u>Option Values at December 31, 2004</u></i>	16
<i><u>Performance Measurement Comparison</u></i>	16
<u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT</u>	17
<i><u>Security Ownership of Certain Beneficial Owners</u></i>	17
<i><u>Security Ownership by Management</u></i>	18
<i><u>Description of Voting Securities</u></i>	18
<i><u>Section 16 (a) Beneficial Ownership Reporting Compliance</u></i>	18
<u>PROPOSAL 1. ELECTION OF DIRECTORS</u>	19
<u>PROPOSAL 2. APPROVAL OF THE CHANGE OF CONTROL STOCK OPTION PLAN</u>	20
<i><u>What Is the Purpose of the Change of Control Stock Option Plan?</u></i>	20
<i><u>What Types of Options can be Granted Under the Change of Control Stock Option Plan?</u></i>	20
<i><u>How Will the Change of Control Stock Option Plan Be Administered?</u></i>	20
<i><u>How Much Stock Will Be Available Under the Change of Control Stock Option Plan?</u></i>	20

<u><i>Who Is Eligible to Participate in the Change of Control Stock Option Plan?</i></u>	21
<u><i>What Happens If the Number of Outstanding Shares Changes Because of a Merger, Consolidation, Recapitalization or Reorganization?</i></u>	21

<i><u>When Will the Change of Control Stock Option Plan Terminate?</u></i>	21
<i><u>What Changes Can the Board Make to Change of Control Stock Option Plan?</u></i>	21
<i><u>What Are the Important Provisions of the Change of Control Stock Option Plan?</u></i>	21
<i><u>What are the US Federal Income Tax Consequences of the Change of Control Stock Option Plan?</u></i>	22
<u>STOCKHOLDER PROPOSALS</u>	23
<u>DISCRETIONARY AUTHORITY</u>	23
<u>GENERAL</u>	23
<u>FORM 10-K ANNUAL REPORT</u>	24
<u>ANNEX I</u>	25
<u>ANNEX II</u>	29
<u>ANNEX III</u>	30

CANARGO ENERGY CORPORATION

P.O. Box 291, St. Peter Port, Guernsey GY1 3RR, British Isles

PROXY STATEMENT

ABOUT THE MEETING

This proxy statement contains information relating to the annual meeting of stockholders of CanArgo Energy Corporation (the Company) to be held on May 9, 2005, beginning at 3.00 p.m., at the offices of American Stock Exchange 86 Trinity Place, New York NY10006, and at any postponements or adjournments thereof. This proxy statement is being mailed to stockholders on or about March 17, 2005 at the direction of the Board of Directors of the Company.

ABOUT THE MEETING

What is the purpose of the annual meeting?

At our annual meeting, stockholders will act upon the matters outlined in the notice of meeting on the cover page of this proxy statement, including the election of directors, approval of our Change of Control Stock Option Plan, and such other matters as may be properly brought before the meeting. In addition, management will report on the performance of the Company and respond to questions from stockholders.

Who is entitled to vote at the meeting?

Only stockholders of record at the close of business on March 14, 2005, the record date for the meeting, are entitled to receive notice of and to participate in the annual meeting and at any postponements or adjournments thereof. If you were a stockholder of record on that date, you will be entitled to vote all of the shares that you held on that date at the meeting, or any postponements or adjournments of the meeting.

What are the voting rights of the holders of the Company's Common Stock?

Each outstanding share of the Company's common stock will be entitled to one vote on each matter considered at the meeting.

Who can attend the meeting?

Subject to space availability, all stockholders as of the record date, or their duly appointed proxies, may attend the meeting, and each may be accompanied by one guest. Since seating is limited, admission to the meeting will be on a first-come, first-served basis. Registration and seating will begin at 2.30 p.m. If you attend, please note that you may be asked to present valid picture identification, such as a driver's license or passport. Cameras, recording devices and other electronic devices will not be permitted at the meeting.

What constitutes a quorum?

The presence at the meeting by proxy of the holders of a majority of the aggregate voting power of the common stock outstanding on the record date will constitute a quorum, permitting the meeting to conduct its business. As of the record date, [] update this on March 14, 2005] shares of common stock, representing the same number of votes, were outstanding. Thus, the presence of the holders of common stock representing at least [] [update this on March 14, 2005] votes will be required to establish a quorum.

Proxies received but marked as abstentions and broker non-votes will be included in the calculation of the number of votes considered to be present at the meeting.

How do I vote?

If you complete and properly sign the accompanying proxy card and return it as directed on the form, it will be voted as you direct. A properly signed and dated proxy card which does not specify any voting directions will be voted in accordance with the recommendations of the Board.

Because the Company's stock is traded on the American and the Oslo Stock Exchanges, two separate forms of substantially identical proxy cards are being mailed out to stockholders depending upon the manner in which stockholders hold their stock, that is, generally, to stockholders who hold their shares in registered or street name form and to those stockholders whose shareholdings are registered in the Verdipapirservice (VPS) system used in Norway. Please note that the appropriate proxy card must be received by the party listed on the proxy card as receiving your completed, dated and signed proxy (i.e., Signature Stock Transfer, Inc. or Registrars Department, Den Norske Bank, ASA, respectively) by the date and time set forth therein in order for the proxy to be counted in time to be voted at the annual meeting.

What if my shares are held in Street Name ?

We will request brokerage firms, bank nominees and other institutions that act as nominees or fiduciaries for owners of common stock, to forward this proxy statement and proxies to persons for whom they hold shares and to obtain authorization for the execution of proxies. If your shares of common stock are held in the name of a brokerage firm, bank or other nominee, only it can sign a proxy with respect to your shares. Accordingly, you will not be able to vote your shares in person if you attend the meeting. Instead, please contact the person responsible for your account and give instructions for a proxy representing your shares to be signed and voted as you direct.

If you hold your shares in street name through a broker, bank or other nominee, your broker, bank or nominee may not be permitted to exercise voting discretion with respect to some of the matters to be acted upon. Thus, if you do not give your broker, bank or nominee specific instructions, your shares may not be voted on those matters and will not be counted in determining the number of shares necessary for approval. Shares represented by such broker non-votes will, however, be counted in determining whether there is a quorum present at the meeting.

Can I change my vote after I return my proxy card?

Yes. Even after you have submitted your proxy, you may revoke or change your vote at any time before the proxy is exercised by filing with the Corporate Secretary of the Company either a notice of revocation or a duly executed proxy bearing a later date, provided that you were a stockholder of record on the record date.

What are the Board's recommendations?

Unless you give other instructions on your proxy card, the persons named as proxy holders on the proxy card will vote in accordance with the recommendations of the Board. The Board's recommendation is set forth together with the description of each item in this proxy statement. In summary, the Board recommends a vote:

For election of the nominated slate of directors (see Proposal 1); and

For the approval of the Company's Change of Control Stock Option Plan (see Proposal 2).

With respect to any other matter that properly comes before the meeting, the proxy holders will vote as recommended by the Board or, if no recommendation is given, at their own discretion. If you sign your proxy but fail to mark your vote, your shares shall be voted in favor of all the proposals.

What vote is required to approve each item?

Election of Directors. The affirmative vote of a plurality of the votes cast at the meeting is required for the election of directors. A properly executed proxy marked "Withhold authority" with respect to the election of one or more directors will not be voted with respect to the director or directors indicated, although it will be counted for purposes of determining whether there is a quorum.

Other Items. For each other item, the affirmative vote of the holders of a majority of the shares represented at the meeting in person or by proxy and entitled to vote on the item will be required for approval. A properly executed proxy marked "Abstain" with respect to any such matter will not be voted, although it will be counted for purposes of determining whether there is a quorum. Accordingly, an abstention will have the effect of a negative vote.

GOVERNANCE OF THE COMPANY***Who are the current members of the Board and Executive Officers?***

The members of the Board of Directors on the date of this proxy statement, the Committees of the Board on which they serve, and the Executive Officers of the Company are identified below:

Name	Age	Positions Held
David Robson	47	Chairman of the Board, Chief Executive Officer and President
Vincent McDonnell	46	Director, Chief Financial Officer and Chief Commercial Officer
Michael Ayre (1)	48	Director
Russ Hammond (1) (2)	63	Director
Nils Trulsvik (1) (2)	56	Director
Liz Landles	44	Corporate Secretary

(1) Member of Audit Committee

(2) Member of Compensation Committee

See Proposal 1. Election of Directors for biographical information regarding the Directors.

Liz Landles, a resident of Guernsey, was appointed Corporate Secretary on August 1, 2002, having served as Assistant Corporate Secretary of the Company since December 2000. Mrs Landles also acts as the Company's Administration Manager and is responsible for organising the Company's administrative activities. Mrs Landles has worked for the Company since October 1997, principally in an administrative role and more recently as a Director of some of the Company's subsidiaries. She holds an Advanced Diploma of Business Administration and is a Fellow of The Institute of Business Administration (FIInstBA).

Directors hold office until the next annual meeting of stockholders and until their respective successors are duly elected and qualified. Officers serve at the pleasure of the Board of Directors.

The Company's Board of Directors held ten meetings during the year ended December 31, 2004. No director has attended less than 75% of all meetings of the Board and those Committees on which he served in 2004.

The Board of Directors has standing Audit and Compensation Committees. The Board of Directors has not designated a nominating committee, the functions of such committee being performed by a majority of the independent directors.

Audit Committee. The functions of the Audit Committee are described below under the heading *Report of the Audit Committee*. The charter of the Audit Committee is attached to this proxy statement as Annex I and is available on the Company's website (www.canargo.com). The Audit Committee met four times during fiscal 2004.

The members of the Audit Committee at the end of 2004 were Michael Ayre (Chairman of the Audit Committee), Russ Hammond and Nils Trulsvik. All of the members of the Audit Committee are independent within the meaning of SEC regulations and the listing standards of the American Stock Exchange. Mr Ayre, the Chairman of the Committee, is qualified as an audit committee financial expert within the meaning of SEC regulations and the Board has determined, in the exercise of its business judgment, that he has accounting and related financial management expertise within the meaning of the listing standards of the American Stock Exchange.

Compensation Committee. The members of the Compensation Committee at the end of 2004 were Nils Trulsvik and Russ Hammond. The function of the Compensation Committee is described in *Executive Compensation* below, under the heading *Compensation Committee Report on Executive Compensation*. In fiscal 2004, the Compensation Committee met 3 times. All of the members of the Committee are independent within the meaning of the listing standards of the American Stock Exchange.

How does the Board select nominees for the Board?

The Board does not have a nominating committee, the functions of which are performed by a majority of the independent directors who consider candidates for Board membership suggested by Board members, as well as management and stockholders and make recommendations for the Board's selection. The Board may also retain a third-party executive search firm from time to time if it believes such engagement is advisable in order to identify suitable candidates. A shareholder who wishes to recommend a prospective nominee for the Board should notify any independent director in writing with whatever supporting material the shareholder considers appropriate.

Once the independent directors have identified a prospective nominee, the Board makes an initial determination as to whether to conduct a full evaluation of the candidate. This initial determination is based on whatever information is provided to the Board with the recommendation of the prospective candidate, as well as the Board's own knowledge of the prospective candidate, which may be supplemented by inquiries to the person making the recommendation or others. The preliminary determination is based primarily on the need for additional Board members to fill vacancies or to expand the size of the Board and the likelihood that the prospective nominee can satisfy the evaluation factors described below. If the Board determines, in consultation with the independent directors and other Board members as appropriate, that additional consideration is warranted, it may request the third-party search firm to gather additional information about the prospective nominee's background and experience and to report its findings to the Board. The Board then evaluates the prospective nominee against the following standards and qualifications, including:

the prospective nominee's standards of integrity, commitment and independence of thought and judgment;

the prospective nominee's ability to dedicate sufficient time, energy and attention to the diligent performance of his or her duties, including the prospective nominee's service on other public company boards;

the extent to which the prospective nominee contributes to the range of talent, skill and expertise appropriate for the Board; and

the extent to which the prospective nominee helps the Board reflect the diversity of the Company's stockholders, employees, customers and communities in which the Company operates.

The Board also considers such other relevant factors as it deems appropriate, including the current composition of the Board, the balance of management and independent directors, the need for Audit Committee expertise and the evaluations of other prospective nominees. In connection with this evaluation, the Board determines whether to interview the prospective nominee, and if warranted, one or more members of the Board, and others, including members of management, as appropriate. After completing this evaluation and interview, the Board determines the nominees after considering the recommendations and views of the directors and others as appropriate. The Board has adopted Resolutions addressing the nominations process and such related matters as may be required under U.S. federal securities laws and the rules of the American Stock Exchange (the Exchange). A copy of the Resolutions is attached as Annex II and is available on the Company's website (www.canargo.com).

The Company has not received any nominations for director(s) from stockholders in connection with the forthcoming meeting.

How does the Board determine which directors are considered independent?

On April 21, 2004, the common stock began trading on the Exchange. In connection with its common stock listing the Company became subject to the new listing standards adopted by the Exchange. The full text of the American Stock Exchange requirements can be found on its website (www.amex.com).

Pursuant to Exchange requirements, the Board undertook its annual review of director independence in February 2005. During this review, the Board considered transactions and relationships between each director or any member of his immediate family and the Company and its subsidiaries and affiliates, including those reported under *Certain Relationships and Related Transactions* below. The Board also examined transactions and relationships between directors or their affiliates and members of the Company's senior management or their affiliates. As provided in the Exchange requirements, the purpose of this review was to determine whether any such relationships or transactions were inconsistent with a determination that the director is independent.

As a result of this review, the Board affirmatively determined that other than for David Robson and Vincent McDonnell all of the directors nominated for election at the annual meeting are independent of the Company and its management under the standards set forth in the requirements of the Exchange. In addition, as further required by the exchange's listing standards, the Board has made an affirmative determination as to each independent director that no material relationships exist between any non-management director and the Company which, in the opinion of the Board, would interfere with the exercise of their independent judgment. David Robson and Vincent McDonnell are considered inside directors because of their employment as senior executives of the Company. We provide additional information regarding Mr Hammond under *Certain Relationships and Related Transactions* below.

How are non-employee directors compensated?

Base Compensation. In 2004 the Company paid directors' fees on an adjusted quarterly basis at a rate of £38,920.60 Pounds Sterling (£) per year plus £1,000 for each meeting of the Audit Committee that they attend, as adjusted for a one time increase in fees payable in U.S. dollars that occurred in September 2004 (using an exchange rate of £1 = \$1.927 as at December 31, 2004 (as quoted on www.oanda.com)). The Company also reimburses ordinary out-of-pocket expenses for attending Board and Committee meetings. Directors who are also employees of the Company receive no additional compensation for service as a director. The Company does not provide retirement benefits to directors under any current program.

Options. Each non-employee director that was serving in 2004 received options to purchase 255,000 shares of the Company's common stock in fiscal 2004. Each option grant, vesting over two years in three equal tranches with the first tranche vesting immediately and having a seven-year term, permits the holder to purchase shares at \$0.65, which exceeded their fair market value on the date of grant, which was \$0.59 in the

case of options granted in 2004. All of these options must be exercised within three months of termination, but in no event longer than the original expiration date of the option. Michael Ayre also received options to purchase 250,000 shares of the Company's common stock on joining the Board of Directors in March 2004. These options vested immediately and have a five year term, with an option price of \$1.00.

The following table shows the compensation paid to all persons who were non-employee directors, including their respective affiliates, during the fiscal year ended December 31, 2004:

Name	Directors Fees and Other Compensation*	Consulting Payments	Options and Warrants Granted
	\$	\$	
Russ Hammond	\$ 138,591(1)		255,000
Nils Trulsvik	\$ 138,591(1)		255,000
Michael Ayre	\$ 128,956(1)		505,000

(1) Using December 31, 2004 exchange rate of £1 = \$1.927 (as quoted on www.oanda.com)

* The Directors compensation included a one time adjustment to their Directors' fee in the amount of \$75,000 which was paid in US Dollars (\$). The balance of their compensation was paid in Pounds Sterling (£).

Certain Relationships and Related Transactions

Dr David Robson, Chief Executive Officer, provides all of his services to the Company through Vazon Energy Limited of which he is the Managing Director. See *Executive Compensation Management Agreements* below for a description of Vazon Energy Limited's agreement with the Company.

Mr Russ Hammond, a non-executive director of the Company, is also an Investment Advisor to Provincial Securities Limited who became a minority shareholder in the Norio and North Kumisi (Block XI^c) Production Sharing Agreement through a farm-in agreement to the Norio MK72 well. On September 4, 2003 the Company concluded a deal to purchase Provincial Securities Limited's minority interest in CanArgo Norio Ltd by a share swap for shares in the Company. The purchase was achieved by issuing 6 million restricted common shares in the Company to the minority interest holders in CanArgo Norio Ltd. Of the interests in CanArgo Norio Ltd, Provincial Securities Limited owned 4% and received 2,234,719 shares of the Company's common stock. Provincial Securities Limited also has an interest in Tethys Petroleum Investments Limited, a company in which the Company holds a 45% interest, which was established to develop potential projects in Kazakhstan. Mr Hammond did not receive any compensation in connection with these transactions and disclaims any beneficial ownership of any shares of Company common stock received by Provincial Securities Limited. Mr. Julian Hammond, Mr. Hammond's son, is employed by the Company as consultant providing investor relations services at an annual salary of £64,800 Pounds Sterling (£).

Transactions with affiliates or other related parties including management of affiliates are to be undertaken on the same basis as third party arms-length transactions. Transactions with affiliates are reviewed and voted on solely by the Audit Committee.

How do stockholders and employees communicate with the Board and the Audit Committee?

Stockholders and other parties interested in communicating directly with the non-management directors as a group may do so by writing to: Nils Trulsvik c/o The Corporate Secretary, CanArgo Energy Corporation, PO Box 291, St.

Peter Port, Guernsey, GY1 3RR, British Isles in an envelope marked Confidential . The Corporate Secretary of the Company will promptly forward to Mr. Trulsvik all such correspondence. In addition, if you wish to communicate generally with the Board you may do so by writing to: The Corporate Secretary, CanArgo Energy Corporation, PO Box 291, St. Peter Port, Guernsey, GY1 3RR, British Isles. The Corporate Secretary of the Company reviews all such non-confidential correspondence and regularly forwards to the Board a summary of all correspondence as well as copies of all correspondence that, in the opinion of the Corporate Secretary, deals with the functions of the Board or its Committees or that she otherwise determines requires their attention. Directors may at any time review a log of all correspondence received by the Company that is addressed to members of the Board and request copies of any such non-confidential correspondence. Any shareholder and employee may submit at any time a good faith complaint regarding any questionable accounting, internal controls or auditing matters concerning the Company without fear of dismissal or retaliation of any kind. All such complaints are immediately brought to the attention of the Company's internal audit department and handled in accordance with procedures established

by the Audit Committee with respect to such matters. Confidential, anonymous reports may be made by writing to the Chair of the Audit Committee, c/o The Corporate Secretary, CanArgo Energy Corporation, PO Box 291, St. Peter Port, Guernsey, GY1 3RR, British Isles, in an envelope marked Confidential .

Does the Company have a Code of Ethics?

The Company has a single *Code of Business Conduct and Ethics*, which sets forth the Company's standards of expected business conduct and which is applicable to all employees, including the chief executive officer, the principal financial officer, principal accounting officer or controller, and persons performing similar functions (each a Principal Officer), as well as the directors of the Company. A copy of the Company's *Code of Business Conduct and Ethics* is available on the Company's website (www.canargo.com). The Company intends to post amendments to or waivers from its *Code of Business Conduct and Ethics* (to the extent applicable to or affecting any Principal Officer) at this location on its website.

AUDIT COMMITTEE REPORT

The following Report of the Audit Committee does not constitute soliciting material and should not be deemed filed or incorporated by reference into any other Company filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent the Company specifically incorporates this Report by reference therein.

The Audit Committee of the Board of Directors is responsible for the review and oversight of the Company's performance with respect to its financial responsibilities and the integrity of the Company's accounting and reporting practices. The Audit Committee, in its capacity as a Committee of the Board of Directors, is also responsible for the appointment, compensation, retention and oversight of the work of any registered public accounting firm engaged for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the Company (including resolution of disagreements between management and the auditor regarding financial reporting), and each such registered public accounting firm must report directly to the Audit Committee. The Board of Directors has determined that the members of the Audit Committee are independent in accordance with American Stock Exchange listing standards and are financially literate, as required by such requirements, as such qualification is interpreted by the Board of Directors in its business judgment. The Audit Committee is composed of three non-employee directors and operates under a written charter, a copy of which is attached as Annex I.

The Company, not the Audit Committee or the independent auditor, is responsible for the preparation of its financial statements and its operating results and for the appropriate safekeeping of the Company's assets. The independent auditor's responsibility is to attest to the fair presentation of the financial statements. The role of the Audit Committee is to be satisfied that both the Company and the independent auditor discharge their respective responsibilities effectively. However, no member of the Audit Committee is professionally engaged in the practice of accounting or auditing of the Company's accounts, including with respect to auditor independence. The Audit Committee relies, without independent verification, on the information provided to it and on the representations made by management and the independent auditors.

The Audit Committee held four meetings during the fiscal year 2004. The meetings were designed, among other things, to facilitate and encourage communication among the Audit Committee, the Company, and the Company's independent auditors, L J Soldinger Associates LLC. The Audit Committee discussed with L J Soldinger Associates LLC the overall scope and plan for their audit, and met with L J Soldinger Associates LLC, with and without management present. The Audit Committee has reviewed and discussed the audited financial statements with management.

The Audit Committee also discussed with the independent auditors matters required to be discussed with audit committees under generally accepted auditing standards, including, among other things, matters related to the conduct of the audit of the Company's consolidated financial statements, the Company's internal accounting controls and the matters required to be discussed by Statement on Auditing Standards No. 61, as amended, *Communication with Audit Committees* .

The Company's independent auditors also provided to the Audit Committee the written disclosures and the letter required by Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committee* , and discussed their independence from the Company. The Audit Committee also reviewed, among other things, the amount of fees paid to PricewaterhouseCoopers LLP and L J Solding Associates LLC for audit and non-audit services.

In accordance with the rules of the SEC, the following chart outlines fees billed during the years ended December 31, 2004 and December 31, 2003 by L J Soldinger Associates LLC:

SERVICES PERFORMED	2004	2003
Audit Fees(1)	\$ 527,645	\$ 177,316
Audit-Related Fees(2)	\$ 125,686	\$ 23,897
Tax Fees(3)	\$ 36,615	\$ 113,140
All Other Fees(4)		
Total Fees	\$ 689,946	\$ 314,353

NOTES TO PRECEDING TABLE

(1) Audit fees represent fees billed for professional services provided in connection with the audit of our annual financial statements, reviews of our quarterly financial statements and audit services provided in connection with statutory and regulatory filings for those years.

(2) Audit-related fees represent fees billed primarily for assurance and related services reasonably related to the performance of the audit or reviews of our financial statements.

(3) Tax fees principally represent fees billed for tax preparation, tax advice and tax planning services.

(4) All other fees principally would include fees billed for products and services provided by the accountant, other than the services reported under the three captions above.

Based on its review and these meetings, discussions and reports, and subject to the limitations on its role and responsibilities referred to above and in the Audit Committee Charter, the Audit Committee recommended to the Board of Directors and the Board approved, that the Company's audited consolidated financial statements for the fiscal year ended December 31, 2004 be included in the Company's Annual Report on Form 10-K, for filing with the SEC.

Michael Ayre, Chairman
Russ Hammond
Nils Trulsvik

EXECUTIVE COMPENSATION

Compensation Committee Report on Executive Compensation

The following Report of the Compensation Committee and the performance graph included elsewhere in this proxy statement do not constitute soliciting material and should not be deemed filed or incorporated by reference into any other Company filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent the Company specifically incorporates this Report or the performance graphs by reference therein.

The Compensation Committee of the Board has furnished the following report on executive compensation for fiscal 2004.

The Committee's Responsibilities

The Compensation Committee of the Board of Directors is composed entirely of non-employee directors. The Compensation Committee is responsible for setting and administering policies which govern the Company's executive compensation programs. The purpose of this report is to summarize the compensation philosophy and policies that the Compensation Committee applied in making executive compensation decisions in 2004.

Compensation Philosophy

The Compensation Committee has approved compensation programs intended to:

Attract and retain talented executive officers and key employees by providing total compensation competitive with that of other executives employed by companies of similar size, complexity and lines of business;

Motivate executives and key employees to achieve strong financial and operational performance;

Emphasize performance-based compensation, which balances rewards for short-term and long-term results;

Reward individual performance;

Link the interests of executives with stockholders by providing a significant portion of total pay in the form of stock incentives; and

Encourage long-term commitment to the Company.

The Compensation Committee held three meetings during fiscal 2004

Stock Based Compensation Plans

At December 31, 2004, stock options and warrants had been issued from the following stock based compensation plans:

1995 Long-Term Incentive Plan. Adopted by the Company in February 1996, this plan allows for up to 7,500,000 shares of the Company's common stock to be issued to officers, directors, employees, consultants and advisors. As of December 31, 2004, 2,931,500 options issued under this plan were outstanding;

Amended and Restated CEI Plan. Adopted by the Company following the acquisition by the Company of CanArgo Oil & Gas Inc. in 1998, this plan allowed for 988,000 shares of the Company's common stock to be issued to employees, consultants and advisors. As of December 31, 2004, 525,000 options issued under this plan were outstanding;

Special Stock Options and Warrants. Adopted by the Company in September 2000, this plan was created to allow the Company to retain and provide incentives to existing executive officers and directors and to allow recruitment of new officers and directors following the Company's decision to relocate finance and administrative functions from Calgary, Canada, to London, England. As of December 31, 2004, 1,928,333 special stock options and warrants issued under this plan were outstanding; and

2004 Long Term Stock Incentive Plan. Adopted by the Company in May 2004, this plan allows for up to 10,000,000 shares of the Company's common stock to be issued to officers, directors, employees, consultants and advisors. As of December 31, 2004, 5,088,000 options issued under this plan were outstanding.

Compensation Methodology

Each year the Compensation Committee reviews data from market surveys, proxy statements issued by competitors and independent consultants to assess the Company's competitive position with respect to the following three components of executive compensation:

base salary;

annual incentives; and

long-term incentives.

- 10 -

The Compensation Committee also considers individual performance, level of responsibility, and skills and experience in making compensation decisions for each executive.

Components of Compensation

Base Salary: Base salaries for executives are determined based upon job responsibilities, level of experience, individual performance, comparisons to the salaries of executives in similar positions obtained from market surveys, and competitive data obtained from consultants and staff research. The goal for the base pay component is to compensate executives at a level which approximates the median salaries of individuals in comparable positions with comparable companies in the oil and gas industry. The Compensation Committee approves all salary increases for executive officers.

Long-Term Incentive Compensation: The Compensation Committee has structured long-term incentive compensation to provide for an appropriate balance between rewarding performance and encouraging employee retention. Long-term incentives are granted primarily in the form of stock options. The purpose of stock options is to align compensation directly with increases in shareholder value. The number of options granted is determined by reviewing survey data to determine the compensation made to other executives and management employees in comparable positions with comparable companies in the oil and gas sector. In determining the number of options to be awarded, the Compensation Committee also considers the grant recipient's qualitative and quantitative performance, the size of stock option awards in the past, and expectations of the grant recipient's future performance.

In 2004, the Compensation Committee approved the grant of a series of new stock options to a broad range of employees and officers. The stock option awards were granted under the various available Company plans.

Compliance with Section 162(m) of the Internal Revenue Code

Under Section 162(m) of the Internal Revenue Code, the Company may not deduct annual compensation in excess of \$1 million paid to certain employees; generally its Chief Executive Officer and its four other most highly compensated executive officers, unless that compensation qualifies as performance-based compensation. While the Compensation Committee intends to structure performance-related awards in a way that will preserve the maximum deductibility of compensation awards, the Compensation Committee may from time to time approve awards which would vest upon the passage of time or other compensation which would not result in qualification of those awards as performance-based compensation. It is not anticipated that compensation realized by any executive officer under the Company's plans and programs now in effect will result in a material loss of tax deductions.

Compensation of the Chief Executive Officer

The Compensation Committee annually reviews the compensation of the Chief Executive Officer. The Chief Executive Officer participates in the same programs and receives compensation under the same programs as other executives. However, the Chief Executive Officer's compensation reflects the greater policy and decision-making authority that the Chief Executive Officer holds and the higher level of responsibility he has with respect to the strategic direction of the Company and its financial and operating results. For 2004, the components of Dr. Robson's compensation were:

Base Salary: After considering the Company's overall performance and competitive practices, and the signing of a new contract, the Compensation Committee approved a base salary of £175,000 for Dr. Robson, effective January 1, 2004.

Performance Bonus: In September 2004, the Compensation Committee, after considering the overall performance of the Company, awarded the Chief Executive Officer a performance bonus of \$150,000. There is no defined

Short-Term Incentive scheme for the Chief Executive Officer, and any bonus is at the discretion of the Compensation Committee. Under Dr. Robson's previous contract a quarterly Short-Term Incentive scheme was in place. This was replaced by a discretionary scheme in his new contract.

It is the Compensation Committee's intention that, when taken together, the components of Dr. Robson's pay, including base salary, performance, annual incentives, short-term incentive opportunity and long-term incentives, will result in compensation which approximates compensation paid by companies of similar size in the same industry.

This report has been provided by the Compensation Committee.

Nils Trulsvik, Chairman.

Russ Hammond

Compensation Committee Interlocks and Insider Participation

During 2004, the Company's Compensation Committee consisted of Nils Trulsvik and Russ Hammond, both currently independent non-employee directors. See the section entitled *Certain Relationships and Related Transactions*.

Management Agreements

Dr David Robson serves as Chairman and Chief Executive Officer of the Company pursuant to an agreement with Vazon Energy Limited of which Dr Robson is the sole owner and Managing Director. Dr Robson through Vazon Energy Limited has signed a comprehensive Management Services Agreement with a rolling six-month termination notice period and a two-year non-competition clause effective from the date of termination of the agreement.

Under the terms of the Management Services Agreement Dr Robson received during 2004 a base salary of £14,583.33 per calendar month. Dr Robson is further entitled to a cash bonus payable at the discretion of the Compensation Committee (or failing that the Company's Board) upon the occurrence of certain specified events reflecting the value to the Company of such an event. The Management Services Agreement does not contain any provisions in relation to stock options.

The Management Services Agreement became effective on June 30, 2000 and terminates on either party giving 6 months written notice to terminate in which case the agreement will terminate 6 months after receipt of the notice. Other grounds for termination are the liquidation or dissolution of the Company, mutual agreement of the parties to terminate and the occurrence of an Event of Default as defined in the Management Services Agreement. In the event of a change of control of the Company, the Company must give Dr Robson not less than 12 months written notice to terminate the Management Services Agreement. The Management Services Agreement contains a covenant in terms of which Dr Robson will not, for a period of two years following the termination of the agreement, directly or indirectly induce any consultant of the Company to terminate their employment, hire by direct approach any consultant of the Company, or in any way interfere with the relationship of the Company and any consultant, agent or representative. Furthermore, Dr Robson is prohibited from directly or indirectly soliciting, diverting or attempting to divert business or related business from the Company for a period of two years from the date of termination of the Management Services Agreement.

Under the terms of the agreement, Dr Robson has a duty not to disclose any confidential information of the Company and he must use such information solely for the benefit of the Company. Dr Robson has a contractual obligation under this agreement to disclose and deliver to the Company for its exclusive use and benefit any inventions as a direct result of work performed for the Company.

In terms of benefits, the Company will make a monthly contribution of 9% of base salary to Dr Robson's pension requirements. Dr Robson will further be provided with life insurance with death cover of four times his base salary (excluding any bonus), permanent health insurance and comprehensive BUPA Travel Insurance.

The Management Services Contract does not contain any gross-up provisions for excess parachute payments, severance provisions or provisions requiring Dr Robson's nomination to the Board of the Company.

Summary Compensation Table

The following table shows all compensation paid or accrued by the Company and its subsidiaries during the years ended December 31, 2004, 2003 and 2002 to the Chief Executive Officer and the two other most highly compensated executive officers of the Company who served in such capacities as of such dates and one additional individual for whom disclosures would have been provided but for the fact that the individual was not serving as an executive officer as at December 31, 2004 (the Named Officers) for services rendered to the Company and its subsidiaries during each of the past three fiscal years.

Name and Principal	Year	Annual Compensation		Bonus	Securities Underlying options	All Other Compensation	
		Salary (6)				(5), (6)	
Position	Ended	(GBP)	(\$ equiv)	(\$)	/ SAR's	(GBP)	(\$ equiv)
David Robson	2004	175,000	337,225	150,000	3,500,000	15,750	30,350
Chairman & CEO (1)	2003	150,000	266,775	17,573	3,000,000	13,500	24,010
	2002	150,000	240,660	29,000	2,666,667	13,500	19,575
Vincent McDonnell	2004	140,000	269,780	150,000	1,200,000	12,600	24,280
CFO and CCO(2)	2003	120,000	213,420		600,000	10,800	19,207
	2002	106,000	170,066		300,000	9,540	13,822
Murray Chancellor	2002	120,000	192,528		0	10,800	15,660
COO (3)							
Liz Landles	2004	73,625	141,875	75,000	610,000	6,626	12,769
Corporate Secretary (4)	2003	57,000	101,374		200,000	5,130	9,124
	2002	57,000	91,451		170,000	5,130	7,695

(1) Dr Robson has served as Chairman and Chief Executive Officer since July 15, 1998 and provides services to the Company through Vazon Energy Limited.

(2) Mr McDonnell has served as Chief Commercial Officer since April 1, 2001. Prior thereto he served as Commercial Manager from December 1, 2000. On September 18, 2002 he was appointed Chief Financial Officer of the Company and on May 2, 2003 he was appointed Director.

(3) Mr Chancellor served as Chief Operating Officer from

September 12, 2000 to March 31, 2003.

- (4) Mrs Landles has served as Company Secretary since August 1, 2002.
- (5) Primarily the Company's contributions to or accruals with respect to non-Company sponsored individual retirement and pension plans.
- (6) Salaries and Other Compensation, excluding bonuses, were paid in UK Pounds Sterling (GBP). Bonuses were paid in US Dollars (\$). Exchange rates used to convert from GBP to \$ used were as follows; for 2002 1 GBP = \$1.6044, for 2003 the year end rate of 1 GBP = \$1.778 and for 2004 the year end rate of 1 GBP = \$1.927.

Option Grants during the Year Ended December 31, 2004

The following table sets forth information concerning options granted to the Named Officers who were employed during the year ended December 31, 2004.

Name	Number of Securities Underlying Options Granted	% of Total Options Granted to Employees in 2004	Exercise Price	Expiration Date	Grant Date Present Value (2)	
					Per Share	Total
David Robson (1)	1,500,000	24%	\$ 0.65	Sep 24, 2011	\$ 0.52	\$ 780,000
Vincent McDonnell (1)	900,000	14%	\$ 0.65	Sep 24, 2011	\$ 0.52	\$ 468,000
Liz Landles (1)	510,000	8%	\$ 0.65	Sep 24, 2011	\$ 0.52	\$ 265,200

- (1) The options were granted at an exercise price of \$0.65 at the time of issue. All the options vest over two years from the date of issue, 1/3 vesting immediately, 1/3 after 1 year and 1/3 after 2 years.

- (2) The hypothetical value of the options as of their date of grant has been calculated using the Black-Scholes option pricing model, as permitted by SEC rules, based upon a set of assumptions set forth in the following table. It should be noted that this model is only one method of valuing options, and the Company's use of the model should not be interpreted as an endorsement of its accuracy. The actual value of the options may be significantly different, and the value actually realized, if any, will depend upon the excess of the market value of the common stock over the option exercise price at the time of exercise.

<i>Exercise Price</i>	Dividend Yield	Volatility	Risk-Free Interest Rate	Expected Term
\$0.65	0.00%	102%	3.69%	