# AJ LUCAS ANNUAL REPORT

## FOR THE YEAR ENDED 30 JUNE 2005

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Dear Shareholder,

This financial year can be characterised as "one of those years where you work very hard, but end up with little to show for it financially". The result is clearly disappointing and can be attributed to a mixture of bad luck, unfavourable circumstances and some poor judgements. Successfully putting together a $750 million deal, winning it in open competition, raising the finance and negotiating the documents; only for it to fall apart because the principals in the end couldn't agree – the Trans Territory Pipeline project pretty much typifies our year.

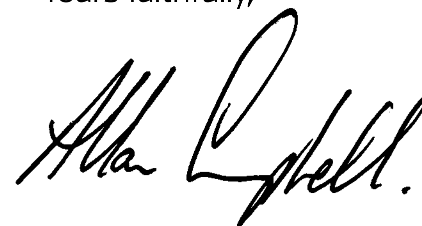
On the other hand, we do believe that the strategy for the Company is correct and that the marketplace is developing as we anticipated; such that we should continue to occupy the right space for the market's infrastructure requirements. In terms of wrong decisions, we have taken the medicine and restructured management.

Our mainstream businesses are going well and we expect the current financial year to be a good one. The coal seam gas business, in particular, is a business in which we expect to see the fruits of our labours crystallise: to create a fully integrated gas production services business to assist both coal miners and coal seam gas producers degasify their coals and enhance the value of their assets. The new businesses, particularly facilities management, require a lot of effort and we expect a number of further developments this year.

Whereas the past four years have seen a marketplace in which terms and conditions have been dictated strongly by the owners (advised by consultants who have no "skin on the table"), we are now seeing a much more equitable marketplace evolving where recognition is given to the skill sets required. This is important as, not only does the asset need to be delivered, all parties need to profit out of the exercise. It is unrealistic to think that one can use one's bargaining power to dictate one-sided terms which, ultimately, are not in the interests of the project.

The outlook for Lucas' services is good. It is therefore important for the Company to keep focused, work hard, avoid distractions and deliver on our projects. This is the essence of our strategy at the moment and it is only delivered by the quality of our people who, once again, have really put out during a hard year. We expect that 2006 financial year will show some real results for our labours. Lucas is, after all, a people business – the best people – and I am eternally grateful to all our employees for their efforts during the year.

Yours faithfully,



Allan Campbell

17 October 2005

# DIRECTORS' REPORT

**Allan Campbell** BCom LLB
**Executive chairman and CEO**
**Age 49**

Allan Campbell acquired a controlling interest in Lucas in 1995 following a successful career in investment banking and commerce including property, construction and building materials.

Since acquiring his shareholding, he has been responsible for the Company's strategic direction and has established its position as the leading outsource provider of infrastructure services in Australia.

**Andrew Lukas** BE
**Executive director**
**Age 58**

Andy Lukas joined Lucas in 1975, initially as a project manager and was appointed a director in 1985. After graduating in civil engineering from UNSW, followed by postgraduate studies at the Pipeline School of the University of Texas, he gained valuable experience with Williams Bros in the US and MacDonald Wagner & Priddle and Transfield in Australia.

He pioneered the development of directional drilling in Australia and is an authority on this technology and pipeline installation. He is also a leading proponent of HDD in coal seam gas extraction.

He is an executive committee member and past president of the Australian Pipeline Industry Association (APIA), a director and first vice president of the International Pipeline and Offshore Contractors Association and a director of CRC Mining Technology & Equipment.

**Ian Stuart-Robertson** AAIQS
**Executive director**
**Age 55**

Ian Stuart-Robertson is a qualified quantity surveyor with over 30 years experience in civil and building construction. He has considerable expertise in general construction and project cost reporting systems and also makes a vital contribution to the Group in his role as chairman of the tender review committee.

He is also non-executive director of quantity surveyors John Hollis & Partners.

**Martin Green** FCA
**Independent non-executive director, Chairman of audit committee**
**Age 60**

Martin Green is a fellow of the Institute of Chartered Accountants and has been in practice for 30 years, mainly specialising in business recovery and insolvency. He has substantial business and finance experience at senior levels.

He is currently a principal at Green Krejci, a former honorary director/treasurer of the National Trust of Australia (NSW) and has served at various times in many public roles and capacities.

**Garry O'Meally** BSc, BE
**Independent non-executive director, member of audit committee**
**Age 69**

Garry O'Meally has over 40 years experience in the oil and gas industries, mainly with Australian Gas Light Company where he served as general manager of AGL Gas Companies and later of AGL Petroleum. He was also general manager of Queensland and Northern Territory for Santos Limited and has consulted to many energy companies.
He has also served as president of the Australian Gas Association, as councillor and Queensland chairman of the Australian Petroleum Production and Exploration Association and as executive manager of APIA. Mr O'Meally's knowledge of the energy industries has been vitally important in the Group's expansion into its gas management activities.

Former directorships in last 3 years: non-executive chairman of Norwest Energy NL (resigned 30 June 2003).

**Julian Gregory** BA, LLB
**Independent non-executive director, member of audit committee**
**Age 48**

Julian Gregory is a qualified lawyer with considerable commercial, financial and legal experience at senior levels within both the private and public sectors. He was previously managing director of international fund manager the TP Group, prior to which he was a partner in the construction, infrastructure and government areas of Corrs Chambers Westgarth.

## Company secretary

Mr Nicholas Swan was appointed as company secretary on 15 November 2001. Mr Swan has held and holds the role of compliance manager and company secretary of several listed public companies and responsible entities for listed managed investment schemes.

## Directors' meetings

The number of directors' meetings (including meetings of committees of directors) held during the financial year and number of such meetings attended by each of the directors is:

| | Board of Directors | | Audit committee | |
|---|---|---|---|---|
| | Held | Attended | Held | Attended |
| Allan Campbell | 12 | 11 | - | - |
| Andrew Lukas | 12 | 11 | - | - |
| Ian Stuart-Robertson | 12 | 12 | - | - |
| Garry O'Meally | 12 | 11 | 2 | 2 |
| Martin Green | 12 | 12 | 2 | 2 |
| Julian Gregory | 12 | 12 | 2 | 2 |

## Corporate governance statement

The Board of directors is responsible for the corporate governance of the Group. This statement outlines the main corporate governance practices. Unless otherwise stated, these practices were in place for the entire year.

### Board of directors

The directors of the Company are accountable to shareholders for the proper management of the business and affairs of the Company.

The key responsibilities of the Board are to:

- establish and monitor the corporate strategies of the Company;
- ensure proper corporate governance;
- monitor the performance of management;
- ensure that appropriate risk management systems, internal controls, reporting systems and compliance frameworks are in place and operating effectively;
- monitor financial results;
- approve decisions concerning investments, acquisitions and dividends; and
- comply with reporting and other requirements of the law.

The Board's role and responsibilities are documented in a written Board charter which is available on request.

### Composition of the Board

The constitution of the Company requires between three and ten directors. Currently there are six, half of whom are independent non-executive and the rest executive.

The Board is committed to having a majority of independent non-executive directors and at some stage will appoint another director to achieve this.

Directors are appointed for their industry-specific expertise and commercial acumen. The Board believes that all the directors can make, and do make, quality and independent judgements in the best interest of the Company. Whilst the chairman is also the chief executive officer, his contribution to the Company is considered vital to direct the strategy of the Company in this still comparatively formative stage of the Company's growth. The directors are able to obtain independent advice at the expense of the Company.

There is no nomination committee. Instead, the Board assesses the performance of individual directors and the Board as a whole.

### Ethical and responsible decision making

The Company has a code of conduct to guide the directors and key executives. It includes disclosure of conflicts of interest and use of information not otherwise publicly known or available. Any director with an interest in matters being considered by the Board must take no part in decisions relating to those matters.

### Trading in Company securities

The Company has a share trading policy prohibiting directors, senior management and their associates from trading in the Company's securities other than in certain nominated periods (between two and thirty days following the release of the half yearly and annual results and the annual general meeting) and at such other times as the Board permits. Such persons must obtain prior approval before conducting any trade.

### Integrity in financial reporting

The Board has established an audit committee which provides assistance to the Board in fulfilling its corporate governance and oversight responsibilities in relation to the Company's financial reporting, internal control systems, risk management systems, regulatory compliance and external audit.

The committee must have at least two members. All members must be independent non-executive directors. At least one member must have financial expertise and some members shall have an understanding of the industry in which the Company operates.

The principal roles of the committee are to:

- assess whether the accounting methods and statutory reporting applied by management are consistent and comply with accounting standards and applicable laws and regulations;
- make recommendations on the appointment of the external auditors, assess their performance and independence and ensure that management responds to audit findings and recommendations;
- discuss the adequacy and effectiveness of the Company's internal control systems and policies to assess and manage business risks and its legal and regulatory compliance programmes; and
- ensure effective monitoring of the Company's compliance with its codes of conduct and Board policy statements.

The audit committee meets with the external auditors at least twice a year. The committee is authorised to seek information from any employee or external party and obtain legal or other professional advice.

### Timely and balanced disclosure

The Company has established policies and procedures designed to ensure compliance with ASX listing rules disclosure requirements so that investors have equal and timely access to all material information. Any broker or analyst presentations are released to the ASX. The Company also posts all information disclosed to the ASX on its website.

### Clear communication with shareholders

The Company has a communications strategy to promote effective communication with shareholders. Procedures include emailing public announcements to shareholders where they have provided their email address to the Company after acknowledgement of receipt of the announcement by ASX.

**Risk identification and management**
The Board has established policies on risk management. The systems of internal financial controls have been determined by senior management and are designed to provide reasonable but not absolute protection against fraud, material mis-statement or loss. The chief executive officer and chief financial officer provide representation to the audit committee and the Board on the risk management compliance and control systems for the Group.

**Encourage enhanced performance**
The performance of committees, individual directors and key executives is evaluated regularly by the Board. The Board also regularly evaluates the Board.

There has been no formal performance evaluation of the Board, directors or committees during the reporting period. The Board informally evaluates the performance of the Board, directors and committees each time it meets. The Board believes that the individuals on the Board have made quality and independent judgements in the best interests of the Company on all relevant issues during the reporting period. There has been a formal performance evaluation of all key executives (other than the executive directors) during the reporting period.

**Recognise the interests of all stakeholders**
The Company has established various codes of conduct to guide compliance with legal and other obligations to stakeholders and the community at large. These include ethical and work standards, employment practices including occupational health and safety and employment opportunities and environmental protection. The Company's compliance and that of its employees is monitored through internal review.

## Principal activities

The Group's principal activities during the financial year were the engineering, design and construction of projects in horizontal directional drilling ("HDD"), pipelines, coal mine gas management, gas exploration, building and civil engineering services and facilities management.

The Company is now engaged in the next stage of its corporate development to produce a stronger, more integrated and higher quality, maintainable earnings stream. This strategy is designed to:

- Ensure a more consistent cash flow from core businesses;
- Build annuity income streams;
- Exploit and commercialise the Company's proprietary technology;
- Leverage the Company's engineering expertise higher up the "food chain"; and
- Broaden the geographical spread of activities.

The key achievements this year are:

- Attaining preferred tenderer status for the Trans Territory Pipeline (TTP) project;
- Continued growth of the coal seam gas business with the successful award of larger contracts for surface to inseam (SIS) drilling with both coal mines and gas producers and the increase in the services capability of the business;
- Completion of the integration of the Lucas Stuart business, including the upgrading of management; and
- Improved risk management procedures across the Group, including the creation of the role of Group commercial manager and the consolidation of the HDD and Gas Management operations under one management structure.

The Company only operates in sectors where it is the sector leader or one of them; where high barriers to entry exist; where the projects require "value add" and in which Lucas sees opportunities for growth. Thus, Lucas aims to be a small company in terms of revenue (<$250 million) but a balanced business with the accent on profitability, profit/risk protection and quality of earnings.

During the year, the Company acquired the business of the Mace Group of Companies. The business provides facilities management services to the catering and prepared food industries and was purchased to facilitate the growth of the Group's facilities management business. There were no other significant changes in the nature of the Group's activities during the year.

## Review and results of operations

**Overview of the consolidated entity**
The consolidated entity recorded a net loss of $21,840,000 which includes a provision for the Nerdlihc receivable of $13,596,000 compared with a net profit of $7,052,000 in 2004. A summary of the results is set out in the following table:

**Summary of financial results**

| | 2005 $'000 | 2004 $'000 | Change % |
|---|---|---|---|
| Operating revenue | 74,278 | 116,760 | (36.4) |
| Total revenue | 74,541 | 123,533 | (39.7) |
| EBITDA | (21,527) | 12,297 | N/A |
| EBIT | (26,287) | 7,664 | N/A |
| (Loss)/profit before tax | (27,355) | 6,678 | N/A |
| Net (loss)/profit attributable to members | (21,840) | 7,052 | N/A |
| Total assets | 64,841 | 84,432 | (23.2) |
| Net assets | 18,923 | 44,264 | (57.2) |
| | | | |
| (Loss)/earnings per share | (42.6)¢ | 14.6¢ | N/A |
| Dividend | 8.0¢ | 8.0¢ | 0.0 |

## Divisional performance

Contributions from the business divisions were as follows:

| | Revenue | | Profit/(loss) before tax | | Margin | |
|---|---|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 | 2005 % | 2004 % |
| **Division** | | | | | | |
| Pipelines | 664 | 58,169 | (9,964) | 6,813 | N/A | 11.7 |
| Directional drilling | 11,538 | 21,053 | (7,747) | 2,790 | (67.1) | 13.3 |
| Gas management | 20,281 | 13,953 | 1,788 | 1,170 | 8.9 | 8.4 |
| Specialist infrastructure | 41,907 | 34,264 | 430 | 783 | 1.0 | 2.3 |

***Pipelines***

The pipeline division was impacted by the lack of a replacement contract for the SEA Gas project and the deferral of the TTP contract after being nominated part of the preferred Build Own Operate (BOO) consortium in March 2005. The loss reflects significant costs incurred on the TTP contract, unplanned SEA Gas subsidence rectification work and insufficient revenue to recover the overheads associated with this division and a provision for the Nerdlihc receivable of $6.8 million.

***Horizontal directional drilling (HDD)***

Operating revenue declined by 45% to $11.5 million reflecting delays in the commencement of projects. Similar to the pipeline division, HDD revenue was insufficient to recover divisional overheads, principally plant and equipment amounting to approximately $3 million. In addition, margins were reduced due to executional difficulties on some of the projects, recoverable amounts write-down and the non-recognition of insurance and variation claims as required under the accounting standards.

***Gas management***

Gas management continued to grow rapidly with revenue increasing by 45.3% over the previous year. Margins increased to 8.9% despite writing off $0.4 million for development expenditure on new technology. The growth in turnover reflects the market acceptance of Lucas' knowhow and the strength of the coal industry. Lucas is now the market leader in coal seam gas drainage and continues to develop new drilling techniques to maintain this leadership.

***Specialist infrastructure services***

Revenue grew strongly at Lucas Stuart increasing by 22.3% over the previous year to $41.9 million. While the revenue growth was not reflected in increased earnings, (net margins declined from 2.3% to 1.0%), the result includes substantial costs for the restructuring of the business. Margins are expected to improve in the current year.

***Income tax***

The income tax benefit included an estimated $0.75 million from research and development tax concessions. This reflects the Group's strong emphasis on research and development, particularly in drilling, to maintain its market leadership in its business segments. Also, $2 million of future income tax benefit arising from tax losses has not been recognised and has been written back to the income tax benefit.

## Review of principal businesses

***a) Management and planning***

The Group expects a strong recovery in 2005/06 with all divisions performing strongly. The recent merger of the HDD and the Gas Management divisions under one management team has greatly improved business planning and resource allocation with almost immediate improvements in productivity and margins.

Similarly, management has been restructured at Lucas Stuart and the business repositioned to secure a higher percentage of negotiated works rather than through competitive tender. Lucas Stuart was acquired in December 2003 and, after a period of integration, which necessarily incurred some short-term additional costs, is now starting to achieve substantially higher margins and a much higher quality revenue stream. A change in corporate culture and business focus is further contributing to the improved performance of the business.

Project risk management is still a major issue for construction businesses. We have appointed an experienced commercial manager with specific responsibility for contract management and review across the Group. We are seeing the benefits of this initiative already.

***b) Pipelines***

Being selected as the preferred tenderer for the TTP project confirmed that the Amec Spie Capag Lucas Joint Venture is the pre-eminent Engineer Procure and Construct (EPC) pipeline contractor currently operating in Australia. It was therefore very disappointing when Alcan decided in June 2005 to defer the project in its current form.

We believe the Group's strategy in pipelines is correct and its profile never better. The award in August 2005 of the Yaté Raw Water Pipeline contract in New Caledonia, a US$29 million project for the laying of a 33.6km pipeline to the Goro Nickel project, demonstrates this. This project has already commenced and is expected to be completed by July 2006. The award of this project means that the division's expected revenue exceeds budgeted revenue for 2005/06 by nearly 200%.

The PNG pipeline is now in the planing stage with a major Front End Engineering and Design (FEED) study currently underway and is expected to be completed by February 2006. The project is accelerating and, while much is required before financial close, it is clear that a contracting strategy will have to be in place well before then. The Australian pipeline contractors have much to add in assisting the project achieve certainty and bankability. Lucas is positioning itself accordingly.

In addition, there are a number of other smaller pipelines being planned for the short term. AJ Lucas, with its extensive pipeline experience, is strongly positioned to secure much of this work.

***c) Horizontal directional drilling***

HDD is also showing significant improvement with revenue budgeted in the current year at $32 million, nearly treble that undertaken in 2004/05. The Group is currently engaged on its first major contract in New Zealand at Pohokura. This is a landfall project in the Taranaki Region of the North Island to enable gas to be brought onshore from an offshore field. The New Zealand offshore gas fields are undergoing substantial development due to depletion of existing gas supplies and the Group is hopeful of winning further major work in the area after the Pohokura project is completed.

The current drought situation in Australia, particularly in New South Wales, is expected to require increasingly innovative methods either to recover water resources or to move it from areas of difficult access. For many such projects, the use of HDD represents the only viable solution. Lucas has significant experience in undertaking complex projects and is well positioned to secure much of such work. It is already in discussion with several water utilities and hopes to announce shortly the award of further significant work.

***d) Gas management***

The Group's gas management division is enjoying significant growth as global demand for coal grows. Lucas has pioneered innovative techniques in SIS drilling methods allowing holes as long as 2km to be drilled from the surface directly into the coal seam. This procedure allows coal seams to be drained of methane gas prior to mining the seams. This minimises mine disruption compared to underground mining methods where mining has to be suspended or moved to another location while the seam is degassed.

Lucas' SIS drilling methodologies has greatly reduced mine costs and led to great demand for the Group's services. Lucas is the market leader in the provision of such services and expects continued strong growth as more mines switch to SIS as the preferred method of degassing their coal seams.

In addition to degassing coal mines, the Group is applying its gas extraction expertise to managing the reticulation of such gas for operation of the mines. This activity is provided under contract and provides a recurring income stream for the Group.

Gas management revenues are forecast to increase by 67% in 2005/06 to $34 million from $20 million earned in the past year continuing the trend of the last four years as shown in the following table.

| Year ended 30 June | 2005 $m | 2004 $m | 2003 $m | 2002 $m |
|---|---|---|---|---|
| Revenue | 20.3 | 14.0 | 8.8 | 3.8 |
| Profit/(loss) | 1.8 | 1.2 | (0.5) | (0.6) |

This growth is limited only by the lack of capacity, both rigs and manpower. The Group has recently purchased two high capacity rigs which will allow the increased budgeted work to be carried out.

***e) Specialist infrastructure services***

Lucas Stuart is also experiencing strong growth and currently has a record order book. Budgeted revenue for this year is $65 million, a 55% increase over the $41.9 million earned in 2004/05 of which $58 million is already secured. Following the full integration of the business into the Lucas Group, Lucas Stuart is now experiencing much higher gross margins and a better quality client as a result of being part of a larger integrated group.

***f) Facilities management***

In December 2004, Lucas acquired the business of the Mace Group of Companies. The business, providing facilities management services to the catering and prepared foods industries, most notably Qantas Catering, was purchased as a building block to increase the Group's facilities management business. Due to a cost reduction programme at Qantas, the expected growth of this business has not occurred. However, management is close to securing other contracts to assist in the growth of this new business.

***g) Gloucester Basin***

The Company, together with its joint venture partner, recently commissioned an independent evaluation of the Gloucester Basin and recommendations of how to maximise the returns to shareholders. This study showed that the project had a current value substantially greater than the Group's carrying value. The significant size of the coal seam gas resource and the project's relative proximity to Newcastle and the Sydney market make the project highly prospective. Market soundings have been taken regarding the most appropriate course to adopt with respect to future development of this asset and it is expected that the joint venture partners may well introduce additional capital at some point. In the interim, work is proceeding on Phase II.

## State of affairs

Significant changes in the state of affairs of the Group during the financial year were as follows:

a) An increase in contributed equity of $480,000 through a private placement of 250,000 shares.
b) Issue of 10,000,000 $1.00 redeemable convertible notes for working capital. Interest is paid at 9.5% per annum. For valuation purposes, the Group has adopted the residual method of accounting for the notes and has valued the equity component at $128,000. This valuation method is also in accordance with International Financial Reporting Standards.
c) Other non-current assets increased by $1.5 million being a net increase of $0.6 million in capitalised development costs and $0.9 million incurred on developing the Group's coal seam gas prospect in the Gloucester Basin.
d) Intangible assets increased by $4.1 million being goodwill on the acquisition of the business of the Mace Group of Companies together with additional liabilities recognised on the acquisition of Stuart Pty Limited completed in 2003/04.

## Dividends

Dividends paid or declared by the Company to members since the end of the previous financial year are shown in the following table.

| | Cents per share | Total amount $'000 | Franked/ Unfranked | Date of Payment |
|---|---|---|---|---|
| Interim 2005 ordinary | 3.5 | 1,802 | unfranked | 24 June 05 |
| Final 2004 ordinary | 4.5 | 2,307 | 50% franked | 16 Dec 04 ($1,479,000) & 24 Feb 05 ($828,000) |
| | | **4,109** | | |

The Directors have resolved not to pay a final dividend for the 2004/05 financial year.

## Environmental regulations and native title

As infrastructure engineers, meeting stringent environmental and land use regulations, including native title issues, are an important element of our work. One of the key benefits of directional drilling is its ability to avoid or substantially mitigate environmental impact.

Lucas is committed to identifying environmental risks and engineering solutions to avoid, minimise or mitigate them. We work closely with all levels of government, landholders, Aboriginal land councils and other bodies to ensure our activities have minimal or no effect on land use and areas of environmental, archaeological or cultural importance.

Group policy requires all operations to be conducted in a manner that will preserve and protect the environment.

The directors are not aware of any significant environmental incidents, or breaches of environmental regulations during or since the end of the year.

## Events subsequent to reporting date

In September 2005, Molopo Australia Limited exercised its option to increase its participating interest in the Lucas Molopo Joint Venture from 14% to 30%.

As previously foreshadowed, the Directors have provided for the Nerdlihc receivables of $13,596,000 as payment was not received at the date of this report.

For reporting periods beginning on or after 1 July 2005, the consolidated entity must comply with Australian equivalents to International Financial Reporting Standards (AIFRS) as issued by the Australian Accounting Standards Board. The implementation plan and potential impact of adopting AIFRS are detailed in Note 32 to the financial statements.

Other than these matters, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material or unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Group, the results of those operations, or the state of affairs of the Group, in future financial years.

## Likely developments

AJ Lucas, at the completion of its current development phase, aims to be a niche, focused, vertically integrated infrastructure services business with an emphasis on the oil and gas, water and waste water, mining, property and construction sectors. The structure of the business is designed to weather the various business and sector cycles, with a low fixed cost base directed towards higher margin business, requiring engineering excellence and innovation, and involving a number of complementary but self-supporting income streams.

Further information about likely developments in the operations of the consolidated entity and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the consolidated entity.

## Remuneration report

This report outlines the remuneration policy for directors and senior executives of the company.

### Remuneration philosophy

The key principle of the Company's executive remuneration policy is to set remuneration at a level that will attract and retain qualified and experienced personnel and motivate and reward them to achieve strategic objectives and improve business results.

Remuneration is structured to reward employees for increasing shareholder value. This is achieved by providing a fixed remuneration component together with short and long term performance-based incentives.

Through creating goal congruence between directors, executives and shareholders, it is hoped to maximise shareholder value.

AJ Lucas aims to set fixed annual remuneration at market median levels for jobs of comparable size and responsibility using established job evaluation methods and to provide incentives to enable top performers to be remunerated at the upper end of the market, subject always to the performance of the Group.

The aim of the incentive plans is to drive performance to successfully implement annual business plans and increase shareholder value.

The remuneration for executive and staff is reviewed annually, using a formal performance appraisal process and market data derived from independent surveys of people with similar competencies and responsibilities.

### Remuneration structure

Remuneration packages include a mix of fixed and variable remuneration and long term incentives.

#### *Fixed remuneration*

Fixed remuneration consists of base remuneration (which is calculated on a total cost basis and includes any fringe benefit tax (FBT) charges related to employee benefits including motor vehicles) as well as employer contributions to superannuation.

***Incentive based remuneration***

Incentive based remuneration includes long term and short term incentives and is designed to reward executive directors and senior executives for meeting or exceeding their financial and personal objectives. The short term incentive (STI) is an "at risk" bonus provided in the form of cash and is subject to the over-riding discretion of the senior executive team.

The long term incentive is provided as rights over ordinary share of the Company under the rules of the Management Rights Plan, as approved by shareholders at the November 2001 annual general meeting. Each right entitles the holder to one ordinary share in the Company subject to performance hurdles, where applied, being attained and the holder remaining in employment with the Group until the rights vest. The performance hurdles are set by the Board.

*Executive directors*

The only grant of rights currently in place for the executive directors was approved by shareholders at the Annual General Meeting held in November 2002. The rights were issued to the directors on 27 December 2002 and vest in three tranches: one third two years after their grant; a further third after three years and the balance after four years and may only be exercised if the consolidated entity achieves the performance hurdle.

The performance hurdle is that the consolidated entity's averaged earnings per share (EPS) over the three financial years ended prior to any vesting date (two financial years in respect of the first tranche) must equal or exceed that amount that would arise at the rate of 10% per annum compound growth over a deemed EPS base of 12.7 cents per share. If the performance hurdle is not achieved in respect of a tranche, the Board may re-evaluate the performance at the end of a subsequent year and allow the rights to be exercised if the hurdle is subsequently satisfied. Assuming the performance hurdle is satisfied and the rights are exercised, the shares will be issued for nil consideration.

The fair value of the rights was calculated at grant date by an independent valuer using a Black-Scholes technique with the following assumptions:

| | |
|---|---:|
| Share price on grant date | $0.98 |
| Exercise price | Nil |
| Volatility | 35% |
| Risk free interest rate | 4.8% |
| Dividend yield | 7.7% |

The valuation model incorporates the likelihood of attaining the performance hurdle in the valuation but does not include any allowance for executive turnover. The fair value of tranches 2 and 3 based on EPS for the 2004/05 and 2005/06 financial years has been calculated at $nil as the performance hurdle is unlikely to be met.

*Named executives*

The rights' grants in place for the named executives were made on two separate occasions, May 2004 and June 2005. The May 2004 issue was awarded in part for several years of past performance. The June 2005 issue was awarded only to new executives commencing employment with the Group in 2004/05. The fair value of the rights awarded under each of the issues was calculated at grant date by an independent valuer using a Black-Scholes technique with the following assumptions:

| | May 2004 Grant | June 2005 Grant |
|---|---:|---:|
| Share price on grant date | $1.66 | $1.52 |
| Exercise price | Nil | Nil |
| Volatility | 38% | 39% |
| Risk free interest rate | 5.6% | 5.1% |
| Dividend yield | 5.4% | 5.6% |

The fair value of a right at grant date was calculated at $1.29 for the May 2004 issue and $1.20 for the June 2005 issue.

***Other benefits***

The remuneration policy provides that directors and senior executives may obtain loans from the Group. All such loans are made at commercial rates and therefore do not represent a benefit to the recipient or attract fringe benefit tax. Interest on the loans is payable quarterly in arrears. No loan amounts have been written down as the balances are considered fully collectible.

**Service agreements**

All executive directors and senior executives are employed under a standard AJ Lucas contract. The service contract outlines the components of remuneration but does not prescribe how remunerations levels are modified year to year. Remuneration levels are reviewed every year to take into account cost of living changes, any change in the scope of the role performed and any changes required to meet the principles of the remuneration policy.

The service contracts are unlimited in term. All contracts can be terminated without notice by the Company with compensation, if any, payable to the employee in accordance with the law or by negotiated agreement.

**Remuneration of non-executive directors**

Non-executive directors' individual fees are determined by the Board within the aggregate amount approved by shareholders. The current maximum aggregate amount that may be paid to all non-executive directors is $450,000 per annum as approved by shareholders at the annual general meeting held in November 2002.

Non-executive directors' base fees are presently $30,000 per annum, unchanged since 1999, including attendance at committee meetings. It is recognised that the level of such fees is less than generally paid to persons in such roles by comparable sized companies. Accordingly, the base fee has been increased to $45,000 per annum with effect from 1 July 2005.

In recognition of the level of base fees paid to non-executive directors, the Company has in the past periodically awarded shares under its Deferred Share Plan to such persons. Such shares vest from the date of issue but cannot be disposed of until the earlier of 10 years from the date of issue or the date their service with AJ Lucas ceases. The last issue of such shares occurred in December 2002 following approval being granted by shareholders.

Details of the nature and amount of the remuneration of each director of the Company and each of the five highest paid executives of the Company and Group are:

| | | Primary | | Post employment | Equity compensation | | | |
|---|---|---|---|---|---|---|---|---|
| | | Salary/ fees [1] $ | Non-cash benefits [2] $ | Superannuation contribution $ | Management rights [3] $ | Other benefits $ | Total $ | Proportion of remuneration performance related and value of rights as proportion of remuneration |
| **Executive directors** | | | | | | | | |
| Allan Campbell | 2005 | 364,410 | - | - | - | 4,673 | 369,083 | - |
| | 2004 | 364,410 | - | - | 100,208 | 7,000 | 471,618 | 21.2 |
| Andrew Lukas | 2005 | 218,707 | 6,752 | 18,000 | - | 4,673 | 248,132 | - |
| | 2004 | 232,062 | 9,402 | 18,000 | 100,208 | 7,000 | 366,672 | 27.3 |
| Ian Stuart-Robertson | 2005 | 247,419 | 3,940 | 18,578 | - | 4,673 | 274,610 | - |
| | 2004 | 213,500 | - | - | - | 7,000 | 220,500 | - |
| **Non-executive directors** | | | | | | | | |
| Martin Green | 2005 | 30,000 | - | - | - | 4,673 | 34,673 | - |
| | 2004 | 30,000 | - | - | - | 7,000 | 37,000 | - |
| Julian Gregory [4] | 2005 | 49,900 | - | - | - | 4,673 | 54,573 | - |
| | 2004 | 27,525 | - | - | - | 1,000 | 28,525 | - |
| Garry O'Meally | 2005 | 30,000 | - | - | - | 4,673 | 34,673 | - |
| | 2004 | 30,000 | - | - | - | 7,000 | 37,000 | - |
| **Total** | **2005** | **940,436** | **10,692** | **36,578** | **-** | **28,038** | **1,015,744** | **-** |
| **Total** | **2004** | **897,497** | **9,402** | **18,000** | **200,416** | **36,000** | **1,161,315** | **-** |
| **Executive officers** | | | | | | | | |
| Kevin Lester<br>General Manager Pipelines | 2005 | 243,367 | 1,445 | 17,077 | 71,446 | - | 333,335 | 21.4 |
| | 2004 | 277,361 | - | 12,870 | 189,400 | 1,000 | 479,631 | 39.3 |
| Tim Herlihy<br>Chief Financial Officer | 2005 | 204,215 | 18,617 | 20,000 | 39,693 | - | 282,525 | 14.0 |
| | 2004 | 201,109 | 30,650 | 20,000 | 104,667 | 1,000 | 357,426 | 29.3 |
| Ian Redfern [5]<br>General Manager Construction | 2005 | 223,627 | - | 17,752 | 55,000 | - | 296,379 | 18.6 |
| Mark Georgiadis [6]<br>Facilities Maintenance Manager | 2005 | 206,338 | 12,528 | 15,356 | 18,100 | - | 252,322 | 7.2 |
| Matthew Baker [6]<br>Commercial Manager | 2005 | 201,720 | 3,977 | 15,296 | 18,100 | - | 239,093 | 7.6 |
| **Total** | **2005** | **1,079,267** | **36,567** | **85,481** | **202,339** | **-** | **1,403,654** | |
| **Total** | **2004** | **478,470** | **30,650** | **32,870** | **294,067** | **2,000** | **837,057** | |
| **Total disclosed** | **2004** | **857,932** | **132,152** | **66,260** | **648,734** | **5,000** | **1,710,278** | |

(1) Salary and fees includes salary, annual leave and long service leave on an accrual basis.

(2) Non-cash benefits consists of the provision of a company car and mobile phone.

(3) The notional value ascribed to this long term incentive (management rights) has been determined by an independent consultant using the criteria set out in Accounting Standard AASB1046 and AASB1046A. The notional value of the management rights has been apportioned over their vesting period on a straight line basis. Each management right was valued at $1.29 other than those issued to Mr Ian Redfern which were each valued at $1.20. In valuing the rights, market conditions have been taken into account in both the current and prior periods. Comparative information has not been restated as market conditions were already included in the valuation. The valuation methodology and inputs to the valuation have been disclosed in the narrative preceeding this table.

(4) Mr Gregory was appointed a director on 29 April 2004. Fees disclosed include fees earned for providing consulting services to the Company.

(5) Mr Redfern was employed from 30 June 2004. He therefore had no remuneration in 2004.

(6) Messrs Georgiadis and Baker were both appointed to their positions during the year. Hence their prior year remuneration is not shown.

The remuneration disclosures in Note 28 to the financial statements differ from those in this table due to differences in definitions of remuneration between the Corporations Act 2001 and AASB 1046 Director and Executive Disclosures by Disclosing Entities.

### Analysis of share-based payments granted as remuneration

Details of the vesting profile of the rights granted as remuneration to each director of the Company and each of the named executives is detailed below:

| | Rights granted | | Vested | Forfeited | Financial years in which | Value yet to vest | |
|---|---|---|---|---|---|---|---|
| | Number | Date | in year | in year (A) | grant vests | Min (B) | Max (C) |
| ***Directors*** | | | % | % | | $ | $ |
| AS Campbell | 83,333 | 27 Dec 02 | 100 | 0 | - | - | - |
| | 83,333 | 27 Dec 02 | - | - | 2006 | Nil | Nil |
| | 83,334 | 27 Dec 02 | - | - | 2007 | Nil | Nil |
| AJ Lukas | 83,333 | 27 Dec 02 | 100 | 0 | - | - | - |
| | 83,333 | 27 Dec 02 | - | - | 2006 | Nil | Nil |
| | 83,334 | 27 Dec 02 | - | - | 2007 | Nil | Nil |
| ***Company and consolidated entity executives*** | | | | | | | |
| K Lester | 60,000 | 27 May 04 | 100 | 0 | - | - | - |
| T Herlihy | 33,334 | 27 May 04 | 100 | 0 | - | - | - |
| I Redfern | 25,000 | 27 Jun 05 | 100 | 0 | - | - | - |
| | 25,000 | 27 Jun 05 | - | - | 2006 | 30,000 | 30,000 |
| | 25,000 | 27 Jun 05 | - | - | 2007 | 30,000 | 30,000 |
| M Georgiadis | 10,000 | 27 May 04 | 100 | 0 | - | - | - |
| | 10,000 | 27 May 04 | - | - | 2006 | 12,000 | 12,000 |
| M Baker | 10,000 | 27 May 04 | 100 | 0 | - | - | - |
| | 10,000 | 27 May 04 | - | - | 2006 | 12,000 | 12,000 |

(A) The % forfeited in the year represents the reduction from the maximum number of rights available to vest due to the performance hurdle not being achieved.
(B) The minimum value of rights yet to vest for directors is $nil as the performance criteria may not be met and consequently the rights may not vest. The minimum value of rights yet to vest for the executives is based on a price of $1.20 per ordinary share of the Company.
(C) The maximum value of rights yet to vest is not determinable as it depends on the market price of shares of the Company on the Australian Stock Exchange on the date the right is exercised. No value has been disclosed for the directors as the performance criteria may not be met and consequently the rights may not vest. The maximum value of rights yet to vest for the executives is based on a price of $1.20 per ordinary share of the Company.

### Analysis of movements in rights

The movement during the reporting period by value, of rights over ordinary shares of the Company held by each Company director and each of the named executives is detailed below:

| | Value of rights | | Total option value |
|---|---|---|---|
| | Granted in year $(A) | Exercised in year $(B) | in year $ |
| I Redfern | 55,000 | Nil | 55,000 |
| M Baker | - | 16,500 | 16,500 |

(A) The value of rights granted in the year is the fair value of the rights calculated at grant date using a Black-Scholes model. The total value of the rights granted is included in the table above. This amount is allocated to remuneration over the vesting period (ie. in years 30 June 2005 to 30 June 2007).
(B) The value of the rights exercised during the year is calculated as the market price of shares of the Company on the Australian Stock Exchange as at close of trading on the date the rights were exercised after deducting the price paid to exercise the rights.

### Unissued shares under rights

At the date of this report, unissued shares of the Company under rights are:

| Expiry date | Exercise price | Number of shares |
|---|---|---|
| 23 December 2007 | $0.00 | 500,000 |
| 28 May 2009 | $0.00 | 1,101,333 |

All rights expire on the earlier of their expiry date or termination of the employee's employment or cessation of the officer's service. 38,000 rights were cancelled during the financial year and 10,000 rights have been cancelled since the end of the financial year because of the cessation of the employee's employment. In addition, the ability to exercise the rights issued to the executive directors is conditional on the Group achieving certain performance hurdles.

The rights do not entitle the holders to participate in any share issue of the Company.

### Shares issued on exercise of rights

During or since the end of the financial year, the Company issued ordinary shares as result of the exercise of rights as follows:

| Number of shares | Amount paid on each share |
|---|---|
| 372,667 | $Nil |

There were no amounts unpaid on the shares issued.

## Directors' shareholdings and other interests

The relevant interest of each director and their director-related entities in the shares and rights over shares issued by the Company, as notified by the directors to the Australian Stock Exchange in accordance with Section 205G(1) of the Corporations Act 2001, at the date of this report are as follows:

| | Ordinary Shares | Rights issued under Management Rights Plan |
|---|---|---|
| Allan Campbell | 10,056,750 | 250,000 |
| Andrew Lukas | 6,121,500 | 250,000 |
| Ian Stuart-Robertson | 1,386,750 | - |
| Martin Green | 75,000 | - |
| Garry O'Meally | 109,180 | - |

## Indemnification and insurance of officers and auditors

### Indemnification

The Company has agreed to indemnify all directors and officers of the Company against all liabilities including expenses to another person or entity (other than the Company or a related body corporate) that may arise from their position as directors or officers of the Group, except where the liability arises out of conduct involving a lack of good faith.

No indemnity has been provided to the auditors of the Company.

### Insurance premiums

Since the end of the previous financial year, the Company has paid premiums in respect of Directors' and Officers' liability and legal expenses insurance contracts for the year ended 30 June 2005 and, since the end of the financial year, the Company has paid or agreed to pay premiums in respect of Directors' and Officers' insurance for the year ending 30 June 2006.

## Non-audit services

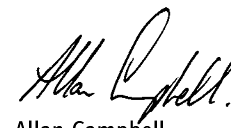
The Board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the audit committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporations Act 2001.

Payments to the auditor of the Company, KPMG, and its related practices for non-audit services provided during the year amounted to $75,330 (2004: $66,400).

### Rounding off

The Company is of a kind referred to in ASIC 98/100 dated 10 July 1998 and, in accordance with that Class Order, amounts in the directors' report and the financial report are rounded off to the nearest thousand dollars, unless otherwise stated.

Signed in accordance with a resolution of the directors pursuant to s.298 (2) of the Corporations Act 2001.



Allan Campbell
Director
Dated at Sydney, this 30th day of September 2005.

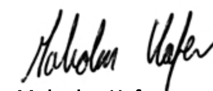
## Lead auditor's independence declaration under Section 307C of the Corporations Act 2001

To the directors of AJ Lucas Group Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2005 there have been:

- no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG



Malcolm Kafer
Partner
Sydney,
30 September 2005

# STATEMENTS OF FINANCIAL PERFORMANCE

**AJ Lucas Group Limited and its controlled entities**

## Statements of financial performance for the year ended 30 June 2005

The statements of financial performance are to be read in conjunction with the notes set out on pages 15 to 42

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| Revenue from rendering services | 2 | 74,278 | 116,760 | - | - |
| Other revenues from ordinary activities | 2 | 263 | 6,773 | 39 | 948 |
| **Total revenue from ordinary activities** | 2 | **74,541** | **123,533** | **39** | **948** |
| Sub-contractor costs | | (21,785) | (36,006) | - | - |
| Material costs | | (22,304) | (36,779) | - | - |
| Plant and other construction costs | | (7,780) | (12,510) | - | - |
| Employee expenses | | (21,689) | (21,388) | - | - |
| Depreciation and amortisation expenses | 3(b) | (4,760) | (4,633) | - | (30) |
| Borrowing costs | 3(b) | (1,127) | (986) | (1,284) | (892) |
| Debt recovery and legal costs | | (780) | (981) | - | - |
| Provision for receivables | | (13,596) | - | - | - |
| Write-off of loans to wholly owned entities | | - | - | (20,466) | (1,208) |
| Other expenses incurred in ordinary activities | | (8,075) | (3,572) | (80) | (72) |
| **(Loss)/profit from ordinary activities before related income tax** | | **(27,355)** | **6,678** | **(21,791)** | **(1,254)** |
| Income tax benefit/(expense)relating to ordinary activities | 4(a) | 5,515 | 104 | 82 | (1,308) |
| **(Loss)/profit from ordinary activities after related income tax** | | **(21,840)** | **6,782** | **(21,709)** | **(2,562)** |
| Net loss attributable to outside equity interest | | - | 270 | - | - |
| **Net (loss)/profit attributable to members of the parent entity** | 19 | **(21,840)** | **7,052** | **(21,709)** | **(2,562)** |
| **Non-owner transaction changes in equity** | | | | | |
| (Decrease) in asset revaluation reserve: | | | | | |
| Fair value adjustment | 18 | - | (94) | - | - |
| **Total changes in equity from non-owner related transactions attributable to the members of the parent entity** | 21 | **(21,840)** | **6,958** | **(21,709)** | **(2,562)** |
| Basic (loss)/earnings per share (cents) | 5 | (42.6) | 14.6 | | |
| Diluted (loss)/earnings per share (cents) | 5 | (42.6) | 14.4 | | |

**AJ Lucas Group Limited and its controlled entities**

## Statements of financial position as at 30 June 2005

The statements of financial position are to be read in conjunction with the notes set out on pages 15 to 42.

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **Current assets** | | | | | |
| Cash assets | 7 | 4,060 | 14,203 | 1,383 | 229 |
| Receivables | 8 | 11,626 | 25,676 | – | – |
| Inventories | 9 | 13,584 | 18,559 | – | – |
| Other | 10 | 786 | – | 340 | – |
| **Total current assets** | | **30,056** | **58,438** | **1,723** | **229** |
| **Non-current assets** | | | | | |
| Receivables | 8 | – | – | 37,196 | 57,940 |
| Plant and equipment | 11 | 20,687 | 18,509 | – | – |
| Intangible assets | 12 | 6,972 | 2,918 | 1,786 | 1,786 |
| Deferred tax assets | 4(d) | 2,651 | 1,598 | 2,651 | 1,518 |
| Other | 13 | 4,475 | 2,969 | 1,260 | 1,260 |
| **Total non-current assets** | | **34,785** | **25,994** | **42,893** | **62,504** |
| **Total assets** | | **64,841** | **84,432** | **44,616** | **62,733** |
| **Current liabilities** | | | | | |
| Payables | 14 | 20,229 | 20,778 | 672 | 465 |
| Interest-bearing liabilities | 15 | 6,309 | 5,857 | – | – |
| Current tax liabilities | 4(b) | 896 | 1,359 | – | – |
| Provisions | 16 | 1,402 | 4,419 | – | – |
| **Total current liabilities** | | **28,836** | **32,413** | **672** | **465** |
| **Non-current liabilities** | | | | | |
| Payables | 14 | – | – | 12,488 | 10,627 |
| Interest-bearing liabilities | 15 | 13,568 | 2,599 | 9,872 | – |
| Deferred tax liabilities | 4(c) | – | 4,847 | – | 4,847 |
| Provisions | 16 | 3,514 | 309 | – | – |
| **Total non-current liabilities** | | **17,082** | **7,755** | **22,360** | **15,474** |
| **Total liabilities** | | **45,918** | **40,168** | **23,032** | **15,939** |
| **Net assets** | | **18,923** | **44,264** | **21,584** | **46,794** |
| **Equity** | | | | | |
| Contributed equity | 17 | 29,236 | 28,628 | 29,236 | 28,628 |
| Reserves | 18 | 964 | 964 | 3,733 | 14,533 |
| (Accumulated losses)/retained profits | 19 | (11,277) | 14,672 | (11,385) | 3,633 |
| **Total equity** | 21 | **18,923** | **44,264** | **21,584** | **46,794** |

**AJ Lucas Group Limited and its controlled entities**

## Statements of cash flows for the year ended 30 June 2005

The statements of cash flows are to be read in conjunction with the notes set out on pages 15 to 42.

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **Cash flows from operating activities** | | | | | |
| Cash receipts in the course of operations | | 81,129 | 124,273 | - | 57 |
| Cash payments in the course of operations | | (86,165) | (142,763) | - | (72) |
| Interest received | | 59 | 1,148 | 39 | 115 |
| Income taxes paid | | (460) | - | - | - |
| Income taxes refunded | | - | 115 | - | - |
| Borrowing costs paid | | (1,127) | (986) | (488) | (57) |
| **Net cash (used in)/provided by operating activities** | 27(b) | **(6,564)** | **(18,213)** | **(449)** | **43** |
| **Cash flows from investing activities** | | | | | |
| Proceeds from sale of plant and equipment | | 117 | 3,355 | - | - |
| Loans to controlled entities | | - | - | (4,768) | (4,057) |
| Payments for plant and equipment | | (6,890) | (3,290) | - | - |
| Payments for exploration and development costs | | (1,861) | (2,076) | - | - |
| Loans to other entities | | - | (2,018) | - | - |
| Purchase of shares in controlled entity | | (2,411) | - | - | (197) |
| Net cash acquired on purchase of controlled entity | | - | 1,659 | - | - |
| **Net cash (used in) investing activities** | | **(11,045)** | **(2,370)** | **(4,768)** | **(4,254)** |
| **Cash flows from financing activities** | | | | | |
| Proceeds from issue of shares | | 480 | 10,100 | 480 | 10,100 |
| Transaction costs on issue of shares | | - | (301) | - | (301) |
| Proceeds of borrowing from related entity | | 285 | - | - | - |
| Repayment of borrowings from related entity | | - | (1,699) | - | (1,699) |
| Proceeds of borrowings - other | | 2,340 | - | - | - |
| Repayment of borrowings - other | | (1,079) | - | - | - |
| Dividends paid | | (4,109) | (3,827) | (4,109) | (3,827) |
| Proceeds from issue of convertible notes | | 10,000 | - | 10,000 | - |
| Finance lease payments | | (2,354) | (2,597) | - | - |
| **Net cash provided by financing activities** | | **5,563** | **1,676** | **6,371** | **4,273** |
| **Net (decrease)/increase in cash held** | | **(12,046)** | **(18,907)** | **1,154** | **62** |
| Cash at beginning of the year | | 12,540 | 31,447 | 229 | 167 |
| **Cash at end of the year** | 27(a) | **494** | **12,540** | **1,383** | **229** |

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## 1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The significant policies that have been adopted in the preparation of this financial report are:

### Basis of preparation

The financial report is a general purpose financial report, which has been prepared in accordance with Accounting Standards, Urgent Issues Group Consensus Views, other authoritative pronouncements of the Australian Accounting Standards Board and the Corporations Act 2001.

It has been prepared on the basis of historical cost and, except where stated, does not take into account changing money values or fair values of assets.

These accounting polices have been consistently applied by each entity in the consolidated entity and are consistent with those of the previous year.

The financial report of the Company and the consolidated entity have been prepared on a going concern basis, which contemplates continuity of normal business activities and the realisation of assets and settlement of liabilities in the ordinary course of business.

The consolidated entity made a loss after tax of $21,840,000 (2004: profit of $7,052,000). At year end, the consolidated entity had a total accumulated deficit of $11,277,000 (2004: retained profit of $14,672,000) and net assets of $18,923,000 (2004: $44,264,000).

The continuance of the Company and the consolidated entity as a going concern is dependent upon the Company and the consolidated entity both returning to profitable operation and having sufficient funding to enable them to meet current and future obligations. The consolidated entity is budgeting earnings before interest and tax for 2006 in the range of $8 million to $10 million and to generate cash from operations of $11 million. In addition, in August 2005, the consolidated entity entered into a new facility agreement with ANZ Bank which provides it with the necessary financial resources to execute the business plan and achieve its budget result. At 31 August 2005, bank facilities totalled $12.0 million with approximately $5.0 million unutilised.

No adjustments have been made to the financial report to take account of any changes that would be required relating to the recoverability and classification of recorded assets or to the amounts and classification of liabilities that might be necessary should the Company not continue as a going concern.

### Use and revision of accounting estimates

The preparation of the financial report requires the making of estimations and assumptions that affect the recognised amounts of assets, liabilities, revenues and expenses and the disclosure of contingent liabilities. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

### Principles of consolidation

#### Controlled entities

The consolidated financial statements are prepared by combining the financial statements of all the entities that comprise the Group, being the Company (the parent entity) and its controlled entities ("the Group"). A list of controlled entities appears in Note 25 to the financial statements.

The financial statements of controlled entities are included from the date control commences until the date control ceases.

Outside interests in the equity and results of the entities that are controlled by the Company are shown as a separate item in the consolidated financial statements.

#### Joint venture

A joint venture is an operation that is jointly controlled by the Group.

***Joint venture operations***

The Group's interests in unincorporated joint ventures are brought to account by including its proportionate share of joint ventures' assets, liabilities and expenses and the Group's

revenue from the sale of its share of output on a line-by-line basis, from the date joint control commences to the date joint control ceases.

**Transactions eliminated on consolidation**
Unrealised gains and losses and inter-entity balances resulting from transactions with or between controlled entities are eliminated in full on consolidation.

Unrealised gains resulting from transactions with joint ventures, including those relating to contributions of non-monetary assets on establishment, are eliminated to the extent of the Group's interest. Unrealised losses are eliminated in the same way as unrealised gains, unless they evidence a recoverable amount impairment.

## Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST) except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, it is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated inclusive of GST.

The net amount of GST recoverable from, or payable to, the taxation authority is included as a current asset or liability in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the taxation authority are classified as operating cash flows.

## Revenue recognition

Revenues are recognised at fair value of the consideration received net of the amount of goods and services tax (GST).

**Construction contracts**

***Recognition of profit***
Revenue and expenses are recognised on an individual project basis using the percentage of completion method when the stage of contract completion can be reliably determined, costs to date can be clearly identified, and total contract revenue and costs to complete can be reliably estimated.

Profits are not normally recognised until a project is at least 30% complete with the exception of design and construct contracts which are recognised from inception. Losses are recognised in the period they occur or are foreseeable.

Where the outcome of a contract cannot be reliably estimated, contract costs are expensed as incurred. Where it is probable that costs will be recovered, revenue is recognised to the extent of the costs incurred. An expected loss is recognised immediately as an expense.

***Recognition of profits – Cost plus contracts***
Revenue and expenses arising from cost plus contracts are recognised in the statement of financial performance by reference to the stage of completion of the contract when the following conditions are satisfied:

- it is probable that the economic benefits arising from the contract will flow to the Group; and
- costs related to the contract, whether or not specifically reimbursable, can be clearly identified and measured reliably.

***Stage of completion***
Stage of completion is measured by reference to an assessment of total labour hours and other costs incurred to date as a percentage of estimated total costs for each contract, unless an alternative measurement method provides a more accurate indication of the stage of completion.

**Asset sales**
The gross proceeds of asset sales are included as revenue of the Group. The profit or loss on disposal of assets is brought to account at the date an unconditional contract of sale is signed.

The gain or loss on disposal is calculated as the difference between the carrying amount of the asset at the time of disposal and the net proceeds on disposal.

**Interest revenue**
Interest income is recognised as it accrues.

**Dividends**
Revenue from distributions from controlled entities is recognised by the parent entity when they are declared by the controlled entities.

Revenue from dividends from other investments is recognised when received.

## Foreign currency

**Transactions**
Foreign currency transactions are translated to Australian currency at rates of exchange in effect at the dates of the transactions. Foreign currency monetary balances at reporting date have been translated into Australian currency at the exchange rate ruling on that date with exchange differences brought to account in the statement of financial performance as exchange gains or losses.

**Translation of controlled foreign entities**
The assets and liabilities of foreign operations, including controlled entities, that are integrated are translated using the temporal method. Monetary assets and liabilities are translated into Australian currency at rates of exchange current at reporting date, while non-monetary items and revenue and expense items are translated at exchange rates current when the transactions occurred. Exchange differences arising on translation are brought to account in the statement of financial performance.

## Borrowing costs

Borrowing costs include interest, foreign exchange losses and finance charges in respect of finance leases. Borrowing costs are expensed as incurred.

## Taxation

**Income tax**
The Group adopts the income statement liability method of tax effect accounting.

Income tax expense is calculated on profit from ordinary activities adjusted for permanent differences between taxable and accounting income. The tax effect of timing differences, which arise from items being brought to account in different periods for income tax and accounting purposes, is carried forward in the statement of financial position at current taxation rates as a future income tax benefit or a provision for deferred income tax.

Future income tax benefits are not brought to account unless realisation of the asset is assured beyond reasonable doubt or, if relating to tax losses, when realisation is virtually certain.

### Tax consolidation

The Company is the head entity in the tax-consolidated group comprising all the Australian wholly-owned subsidiaries set out in Note 25. The head entity recognises all of the current and deferred tax assets and liabilities of the tax-consolidated group (after elimination of intragroup transactions).

The tax-consolidated group has entered into a tax funding agreement that requires wholly-owned subsidiaries to make contributions to the head entity for current tax assets and liabilities and movements in deferred tax balances arising from external transactions during the year.

Under the tax funding agreement, the contributions are calculated on a "stand-alone basis" so that the contributions are equivalent to the tax balances generated by external transactions entered into by wholly-owned subsidiaries. The contributions are payable as set out in the agreement and reflect the timing of the head entity's obligations to make payments for tax liabilities to the relevant tax authorities. The assets and liabilities arising under the tax funding agreement are recognised as intercompany assets and liabilities with a consequential adjustment to income tax expense/revenue.

## Earnings per share

Basic earnings per share (EPS) is calculated by dividing the net (loss)/profit attributable to members of the parent entity for the reporting period, after excluding any costs of servicing equity (other than ordinary shares and converting notes classified as ordinary shares for EPS calculation purposes), by the weighted average number of ordinary shares of the Company.

Diluted EPS is calculated by dividing the basic EPS earnings, adjusted by the after tax effect of financing costs associated with dilutive potential ordinary shares and the effect on revenues and expenses of conversion to ordinary shares associated with dilutive potential ordinary shares, by the weighted average number of ordinary shares and dilutive potential ordinary shares.

## Cash assets

Cash and short-term deposits are carried at face value of the amounts deposited. The carrying amounts of cash and short-term deposits approximate net fair value. Interest revenue is accrued at the market or contracted rates and is receivable at the conclusion of the deposit term.

## Receivables

### Trade debtors

Trade debtors are recorded at amounts due less any provision for doubtful debts. The carrying amount of trade debtors approximates net fair value. Trade debtors are normally settled within 60 days.

### Other debtors

Other debtors and amounts owing by related entities are carried at amounts due less any provision for doubtful debts, are repayable at call and are not subject to interest. The carrying amount of other debtors approximates net fair value.

## Inventories

Materials and stores are carried at the lower of cost and net realisable value.

### Construction work in progress

Work in progress is carried at cost plus profit recognised to date based on the value of work completed, less progress billing and less provision for foreseeable losses, allocated between amount due from customers and amounts due to customers (included in trade creditors).

Cost includes both variable and fixed costs directly related to specific contracts, and those costs related to contract activity in general which can be allocated to specific contracts on a reasonable basis. Costs that are expected to be incurred under penalty clauses and warranty provisions are also included.

## Investments

### Controlled entities

Investments in controlled entities are carried in the Company's financial statements at the lower of cost and recoverable amount.

## Acquisition of assets

Unless otherwise stated, all assets acquired other than goodwill are initially recorded at their cost of acquisition at the date of acquisition, being the fair value of the purchase consideration plus incidental costs directly attributable to the acquisition. When equity instruments are issued as consideration, their market price at the date of issue is used as fair value except where the notional price at which they could be placed in the market is a better indication of fair value. Transaction costs arising in the issue of equity instruments are recognised directly in equity. Where settlement of any part of cash consideration is deferred, the amounts payable are recorded at their present value, discounted at the rate applicable to the Group if a similar borrowing was obtained from an independent financier under comparable terms and conditions. The unwinding of the discount is treated as interest expense.

Expenditure is only recognised as an asset when the entity controls future economic benefits as a result of the costs incurred that are probable and can be reliably measured.

### Assets under construction

The costs of assets constructed or internally generated by the Group, other than goodwill, include the cost of materials and direct labour. Directly attributable overheads and borrowing costs for assets which are likely to take more than 12 months to get ready for their intended use on sale are also capitalised.

### Subsequent additional costs

Costs incurred on assets subsequent to initial acquisition are capitalised when it is probable that future economic benefit, in excess of the originally assessed performance of the asset will flow to the Group in future years. Otherwise, the costs are expensed as incurred.

## Goodwill

Goodwill, representing the excess of purchase consideration over the fair value of net assets acquired, is amortised on a straight-line basis over the appropriate period during which benefits are expected to arise.

The unamortised balance of goodwill is reviewed at least at each reporting date. Where the balance exceeds the value of expected future benefits, the difference is charged to the statement of financial performance.

## Leased assets

Leases under which the Group assumes substantially all the risks and benefits of ownership are classified as finance leases. Other leases are classified as operating leases.

**Finance leases**
A lease asset and a lease liability equal to the present value of the minimum lease payments are recorded at the inception of the lease.

Lease liabilities are reduced by repayments of principal. The interest components of the lease payments are expensed.

**Operating leases**
Payments made under operating leases are expensed on a straight line basis over the term of the lease, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased property.

## Intangible assets

Intangible assets are initially measured at cost and are amortised over the periods the benefits are expected to arise.

## Deferred expenditure

Development or start-up costs are charged against income as incurred, except to the extent that such costs, together with unamortised deferred or start-up costs in relation to any project, are expected, beyond any reasonable doubt, to be recoverable.

The deferred costs are amortised over the period in which the corresponding benefits are expected to arise, commencing with the commercial introduction of the service.

The unamortised balance of costs deferred in previous periods is reviewed regularly and at each reporting date to ensure the criteria for deferral continue to be met. When such costs are no longer considered recoverable, they are charged to the statement of financial performance for the financial period.

## Research and development

Research and development expenditure is expensed as incurred except to the extent that its recoverability is assured beyond any reasonable doubt, in which case it is capitalised.

The capitalised costs are amortised over the period in which the corresponding benefits are expected to arise, currently 3 to 5 years, commencing with the commercial introduction of the service.

## Exploration, evaluation and development expenditure

Exploration, evaluation and development costs are accumulated in respect of each separate area of interest.

Exploration and evaluation costs are carried forward where right of tenure of the area of interest is current and they are expected to be recouped through sale or successful development and exploitation of the area of interest, or, where exploration and evaluation activities in the area of interest have not yet reached a stage that permits reasonable assessment of the existence of economically recoverable reserves.

Development costs related to an area of interest are carried forward to the extent that they are expected to be recouped through sale or successful exploitation of the area of interest.

When an area of interest is abandoned or the directors decide that it is not commercial, any accumulated costs in respect of that area are written off in the financial period the decision is made.

## Depreciation and amortisation

All assets, including intangibles, are depreciated/amortised using the straight-line method over their estimated useful lives, taking into account estimated residual values, except for finance lease assets which are amortised over the term of the relevant lease, or where it is likely the Group will obtain ownership of the asset, the life of the asset. Assets are depreciated or amortised from their date of acquisition or, in the case of internally constructed assets, from the time an asset is completed and held ready for use. Depreciation and amortisation rates and methods are reviewed annually for appropriateness and were unchanged from the previous year. When changes are made, adjustments are reflected prospectively in current and future periods only.

The depreciation and amortisation rates used for each class of asset are as follows:

| | |
|---|---|
| **Plant and equipment** | |
| Plant and equipment | 10-27% |
| Motor vehicles | 15% |
| Office equipment | 13-25% |
| Computer equipment | 24-27% |
| Leased plant and equipment | 10% |
| **Intangibles** | |
| Goodwill | 10 years |
| **Other non-current assets** | |
| Research and development costs | 3-5 years |

## Recoverable amount of non-current assets valued on cost basis

The carrying amounts of non-current assets valued on the cost basis are reviewed to determine whether they are in excess of their recoverable amount at reporting date. If the carrying amount of a non-current asset exceeds its recoverable amount, the asset is written down to the lower amount. The write-down is expensed in the reporting period in which it occurs.

In assessing recoverable amounts of non-current assets, the relevant cash flows have not been discounted to their present value.

Where a group of assets working together supports the generation of cash inflows, recoverable amount is assessed in relation to that group of assets.

## Revaluations of non-current assets

Classes of non-current assets measured at fair value are revalued with sufficient regularity to ensure the carrying amount of each asset in the class does not differ materially from fair value at reporting date. Revaluation increments, on a class of assets basis, are recognised in the asset revaluation reserve except for amounts reversing a decrement previously recognised as an expense, which are recognised as revenues. Revaluation decrements are only offset against revaluation increments relating to the same class of asset and any excess is recognised as an expense.

Potential capital gains tax is only taken into account if the asset is held for sale.

## Payables

Liabilities are recognised for amounts to be paid in the future for goods and services received. Trade accounts payable are normally settled within 60 days.

## Interest-bearing liabilities

Bank loans are recognised at their principal amount, subject to set-off arrangements. Interest expense is accrued at the contracted rate and included in Note 14 Payables "Other creditors and accruals".

### Financial instruments issued

The convertible notes issued by the Company are financial instruments, and the holder has the option to convert them into ordinary shares of the Company. Accordingly, they are classified as compound instruments. The liability component is measured as the present value of the principal and interest obligations, discounted at the prevailing market rate for a similar liability that does not have an equity component. The residual of the net proceeds received on issuing the instrument is classified as equity.

Interest expense on compound instruments is determined based on the liability component and includes the actual interest paid to holders. The liability accrues over the life of the instruments to the original face value if they are not previously converted. There are no dividends associated with the equity component.

### Employee entitlements

#### Wages, salaries and annual leave

Liabilities for employee entitlements to wages, salaries and annual leave expected to be settled within 12 months of the year-end represent present obligations resulting from employees' services provided to the reporting date, calculated at undiscounted amounts based on wage and salary rates that the Group expects to pay as at reporting date including related on-costs such as workers compensation, insurance and payroll tax.

#### Long service leave

The provision for employee entitlements to long service leave represents the present value of the estimated future cash outflows to be made resulting from employees' services provided to reporting date.

The provision is calculated using estimated future increases in wage and salary rates including related on-costs and expected settlement dates based on turnover history and is discounted using the rates attaching to national government securities at balance date which most closely match the terms of maturity of the related liabilities. The unwinding of the discount is treated as long service leave expense.

#### Employee share and options plans

The Company adopted various employee incentive schemes on 28 November 2001. Rights to subscribe for shares were issued under these plans during the financial year. The difference between the fair value of these rights and shares and the consideration received, if any, from the recipients was not expensed. Other than the costs incurred in administrating the schemes which are expensed as incurred, the schemes did not result in any expense to the Group.

#### Superannuation plan

Contributions to employee superannuation funds are charged against income as they are made. Further information is set out in Note 29.

### Dividends

A provision for dividends payable is recognised in the reporting period in which the dividends are declared, for the entire undistributed amount, regardless of the extent to which they will be paid in cash.

## 2. REVENUE FROM ORDINARY ACTIVITIES

| | Consolidated | | Company | |
|---|---|---|---|---|
| | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** |
| Rendering of services revenue from operating activities | 74,278 | 116,760 | - | - |
| **Other revenues:** | | | | |
| *From operating activities* | | | | |
| Net foreign exchange gain | 37 | 1,755 | - | - |
| Interest: | | | | |
| Related parties | - | - | - | 833 |
| Other parties | 59 | 1,148 | 39 | 115 |
| *From outside operating activities* | | | | |
| Gross proceeds from disposal of non-current assets | 117 | 3,355 | - | - |
| Other | 50 | 515 | - | - |
| **Total other revenues** | 263 | 6,773 | 39 | 948 |
| **Total revenue from ordinary activities** | **74,541** | **123,533** | **39** | **948** |

## 3. (LOSS)/PROFIT FROM ORDINARY ACTIVITIES BEFORE INCOME TAX

**(a) Individually significant items included in (loss)/ profit from ordinary activities before income tax:**

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| Payment & provision in respect of claim made by DrillTec GUT GmbH | - | 5,003 | - | - |
| Movement in provision for doubtful debts | 6,946 | (4,291) | - | - |
| Write off non-collectable intercompany receivables | - | - | 20,466 | 1,208 |
| Write off of amounts due from Nerdlihc | 13,596 | - | - | - |

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| **(b) (Loss)/profit from ordinary activities before income tax has been arrived at after charging/(crediting) the following items:** | | | | |
| Depreciation of: | | | | |
| Plant and equipment | 2,752 | 1,945 | - | - |
| Motor vehicles | 61 | 52 | - | - |
| Office equipment | 262 | 229 | - | - |
| | 3,075 | 2,226 | - | - |
| Amortisation of: | | | | |
| Goodwill | 248 | 37 | - | 30 |
| Leased plant and equipment | 982 | 1,514 | - | - |
| Leased office equipment | 62 | 63 | - | |
| Leased motor vehicles | 38 | 62 | - | |
| Research and development expenditure | 355 | 355 | - | - |
| Bonding costs | - | 376 | - | - |
| | 1,685 | 2,407 | - | 30 |
| Total depreciation and amortisation | 4,760 | 4,633 | - | 30 |
| Net bad and doubtful debts expense including movement in provision for doubtful debts | 6,946 | (4,291) | - | - |
| Loan write off | 6,789 | - | - | - |
| Operating lease rental expense - minimum lease payments | 88 | 167 | - | - |
| Movement in provisions for employee entitlements | 266 | (100) | - | - |
| Movement in provision for contractual dispute | (78) | 3,313 | - | - |
| Unrealised net foreign exchange (gain) | (64) | (357) | - | - |
| Realised net foreign exchange loss/(gain) | 27 | (1,397) | - | - |
| *Net loss/(gain) on sales of non-current assets:* | | | | |
| Plant and equipment | 885 | (256) | - | - |
| *Borrowing costs:* | | | | |
| Related parties | - | - | 796 | 833 |
| Other parties | | | | |
| Bank loans and overdraft | 188 | 267 | 20 | 59 |
| Finance charges on leases | 471 | 719 | - | - |
| Convertible notes classified as liabilities | 468 | - | 468 | |
| | **1,127** | **986** | **1,284** | **892** |

## 4. TAXATION

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| **(a) Income tax expense** | | | | |
| Prima facie income tax (benefit)/expense calculated at 30% (2004:30%) on the (loss)/profit from ordinary activities | (8,207) | 2,004 | (6,537) | (376) |
| Decrease in income tax benefit due to: | | | | |
| Amortisation of goodwill | 74 | 11 | - | 9 |
| Non-deductible expenses | 10 | 26 | - | - |
| Depreciation attributable to asset revaluation | 93 | 72 | - | - |
| Foreign exchange loss on translation of foreign subsidiary | 108 | 117 | - | - |
| Permanent timing difference on loan write off | 2,037 | - | - | - |
| Foreign income | - | 530 | 239 | 258 |
| Sundry items | 17 | 247 | 17 | - |
| Tax losses not carried forward | 2,000 | - | - | - |
| Net movements in non-deductible provisions | - | - | - | 887 |
| Increase in income tax benefit due to: | | | | |
| Net movements in non-deductible provisions | - | (81) | 6,139 | - |
| Research and development allowance | (776) | (603) | - | - |
| Foreign subsidiary income non-assessable | (95) | (1,906) | - | - |
| | (4,739) | 415 | (142) | 778 |
| Individually significant income tax items: | | | | |
| Net deferred tax balances recognised by head entity in relation to wholly-owned subsidiaries within the tax consolidated group upon implementation of tax consolidation | - | - | 2,411 | 3,684 |
| Recovery of income tax expense under a tax funding agreement at transition | - | - | (2,411) | (3,684) |
| | (4,739) | 415 | (142) | 778 |
| Income tax under/(over) provided in prior year | (776) | (519) | 60 | 530 |
| **Income tax (benefit)/expense attributable to (loss)/profit from ordinary activities** | **(5,515)** | **(104)** | **(82)** | **1,308** |
| **(b) Current tax liabilities** | | | | |
| *Provision for current income tax* | | | | |
| **Movements during the year** | | | | |
| Balance at beginning of year | 1,359 | 1,444 | - | - |
| Income tax (paid)/refunded | (460) | 115 | - | - |
| Translation gain on foreign taxes payable | (121) | (75) | - | - |
| Under/(over) provision in prior year | 118 | (125) | - | - |
| Balance at end of year | **896** | **1,359** | **-** | **-** |

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| **(c) Deferred tax liabilities** | | | | |
| *Provision for deferred income tax* | | | | |
| Provision for deferred tax comprises the estimated expense at the applicable rate of 30% (2004: 30%) on the following items: | | | | |
| Difference between contract profit recognised for accounting and tax purposes | 2,145 | 4,315 | - | 4,315 |
| Deferred tax liability no longer required | (2,145) | - | - | - |
| Timing differences | - | 532 | - | 532 |
| | - | **4,847** | - | **4,847** |
| **(d) Deferred tax assets** | | | | |
| *Future income tax benefit* | | | | |
| Future income tax benefit comprises the estimated future benefit at the applicable rate of 30% (2004: 30%) on the following items: | | | | |
| Tax losses carried forward | 419 | - | 419 | - |
| Timing differences | 2,232 | 1,598 | 2,232 | 1,518 |
| | **2,651** | **1,598** | **2,651** | **1,518** |
| *Future income tax benefit* | | | | |
| The potential future income tax benefit in a controlled entity, which is a company, arising from tax losses and timing differences has not been recognised as an asset because recovery of tax losses is not virtually certain: | | | | |
| Tax losses carried forward | 2,000 | - | 2,000 | - |

The potential future income tax benefit will only be obtained if:

(i) the head entity derives future assessable income of a nature and an amount sufficient to enable the benefit to be realised;

(ii) the head entity continues to comply with the conditions for deductibility imposed by the law; and

(iii) no changes in tax legislation adversely affect the head entity in realising the benefit.

## 5. EARNINGS PER SHARE

### Classification of securities as potential ordinary shares

Only ordinary shares have been considered for the purpose of calculating earnings per share. None of the rights granted and outstanding under the Management Rights Plan or any of the 10,000,000 redeemable convertible notes issued during the year have been included in the weighted average number of ordinary shares used to calculate basic or diluted earnings per share for the year ended 30 June 2005 as the consolidated entity made a loss for the year. Shares issued during the year pursuant to the exercise of management rights have been weighted according to the date of exercise.

Further details of these securities are contained in Notes 15, 17 and 29.

| | 2005 Number | 2004 Number |
|---|---|---|
| **Weighted average number of shares used as the denominator** | | |
| *Number for basic earnings per share* | | |
| Ordinary shares | 51,315,776 | 48,281,371 |
| *Number for diluted earnings per share* | | |
| Ordinary shares | 51,315,776 | 48,281,371 |
| Effect of rights on issue under Management Rights Plan | - | 621,415 |
| | **51,315,776** | **48,902,786** |

## 6. SEGMENT REPORTING

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest-earning assets and revenue, interest-bearing loans, borrowings and expenses, and corporate assets and expenses. Inter-segment pricing is determined on an arms length basis.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets that are expected to be used for more than one period.

**Business segments**

The Group comprises the following main business segments based on the Group's reporting system:

| | |
|---|---|
| Directional drilling | Trenchless installation of pipes, conduits or cables under obstacles using a surface drilling rig. |
| Pipelines | Construction and installation of pipelines including hydrostatic testing. |
| Gas management services | Application of directional drilling services to degasification of underground coal mines and recovery and commercialisation of coal seam gas. |
| Specialist infrastructure services | Construction, facilities management and civil engineering services. |

**Primary reporting – business segments**

| | Directional drilling | | Pipelines | | Gas management services | | Specialist infrastructure services | | Other | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** | **2005 $'000** | **2004 $'000** |
| **Revenue** | | | | | | | | | | | | | | |
| External segment revenue | 10,852 | 16,590 | 664 | 58,169 | 20,281 | 13,953 | 42,593 | 34,264 | 151 | 557 | - | - | 74,541 | 123,533 |
| Inter-segment revenue | 686 | 4,463 | - | - | - | - | (686) | - | - | - | - | (4,463) | - | - |
| Total segment revenue | **11,538** | **21,053** | **664** | **58,169** | **20,281** | **13,953** | **41,907** | **34,264** | **151** | **557** | **-** | **(4,463)** | **74,541** | **123,533** |
| **Result** | | | | | | | | | | | | | | |
| Segment (loss)/profit | (7,747) | (2,213)[ii] | (9,964)[i] | 6,813 | 1,788 | 1,170 | 430 | 783 | (11,862)[i] | 125 | - | - | (27,355) | 6,678 |
| (Loss)/profit from ordinary activities before income tax | | | | | | | | | | | | | (27,355) | 6,678 |
| Income tax benefit | | | | | | | | | | | | | 5,515 | 104 |
| **Net (loss)/profit** | | | | | | | | | | | | | **(21,840)** | **6,782** |
| Depreciation and amortisation | 2,275 | 2,252 | 585 | 1,069 | 1,520 | 1,262 | 380 | 50 | - | - | - | - | 4,760 | 4,633 |
| **Assets** | | | | | | | | | | | | | | |
| Segment assets | 23,881 | 22,372 | 10,540 | 31,044 | 11,972 | 16,044 | 15,192 | 13,188 | 3,256 | 1,784 | - | - | 64,841 | 84,432 |
| **Liabilities** | | | | | | | | | | | | | | |
| Segment liabilities | 20,009 | 12,096 | 2,194 | 7,078 | 7,802 | 8,372 | 14,414 | 11,622 | 1,499 | 1,000 | - | - | 45,918 | 40,168 |
| Acquisitions of non-current assets | 4,639 | 5,633 | 600 | 1,441 | 2,869 | 1,542 | 4,749 | 1,368 | - | - | - | - | 12,857 | 9,984 |

(i) Includes provision for Nerdlihc receivable of $6,807,000 in Pipelines and $6,789,000 in Other.

(ii) Includes a non-operating expense of $5,003,000 in respect of the payment and provision relating to the contractual dispute with DrillTec.

**Secondary reporting – geographical segments**
Geographical segment revenue and assets are based on the respective geographical location of customers and assets.

| | Australia | | Asia/Pacific | | Consolidated | |
|---|---|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Operating revenue | 70,010 | 114,853 | 4,268 | 1,907 | 74,278 | 116,760 |
| Other revenue | 76 | 6,684 | 187 | 89 | 263 | 6,773 |
| Total revenue | 70,086 | 121,537 | 4,455 | 1,996 | 74,541 | 123,533 |
| Assets | 63,205 | 82,423 | 1,636 | 2,009 | 64,841 | 84,432 |
| Acquisitions of non-current assets | 12,857 | 9,984 | - | - | 12,857 | 9,984 |

## 7. CASH ASSETS

| | | Consolidated | | Company | |
|---|---|---|---|---|---|
| | Note | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Cash at bank and on hand | 27(a) | 4,060 | 14,203 | 1,383 | 229 |

## 8. RECEIVABLES

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **Current** | | | | | |
| Trade debtors | | 17,619 | 15,281 | - | - |
| Less: Provision for doubtful trade debtors | | (7,053) | (107) | - | - |
| | | **10,566** | **15,174** | **-** | **-** |
| Accrued revenue | | - | 5,803 | - | - |
| Retentions | | 17 | 75 | - | - |
| Other receivables | | 676 | 293 | - | - |
| Other loans | | 6,789 | 4,017 | - | - |
| Provision for other loans | | (6,789) | - | - | - |
| Sundry debtors | | 367 | 314 | - | - |
| | | **11,626** | **25,676** | **-** | **-** |
| **Non-current** | | | | | |
| Loans to controlled entities | 30 | **-** | **-** | **37,196** | **57,940** |

## 9. INVENTORIES

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Materials and stores | - | 144 | - | - |
| Construction work in progress | 13,584 | 18,415 | - | - |
| | **13,584** | **18,559** | **-** | **-** |
| *Construction work in progress comprises:* | | | | |
| Contract costs incurred to date | 147,092 | 264,541 | - | - |
| Profit recognised to date | 11,996 | 28,745 | - | - |
| | 159,088 | 293,286 | - | - |
| Less: progress billings | (148,432) | (276,875) | - | - |
| **Net construction work in progress** | **10,656** | **16,411** | **-** | **-** |
| *Net construction work in progress comprises:* | | | | |
| Amounts due from customers - inventories | 13,584 | 18,415 | - | - |
| Excess of progress billings over costs incurred included in payables | (2,928) | (2,004) | - | - |
| | **10,656** | **16,411** | **-** | **-** |

## 10. OTHER CURRENT ASSETS

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| Prepayments | **786** | **-** | **340** | **-** |

## 11. PLANT AND EQUIPMENT

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| **Leasehold improvements** | | | | |
| At cost | 105 | 105 | - | - |
| Accumulated amortisation | (59) | (49) | - | - |
| | 46 | 56 | - | - |
| **Plant and equipment** | | | | |
| At directors' valuation - June 2005 | 8,469 | 3,972 | - | - |
| Accumulated depreciation | (2,359) | (406) | - | - |
| At independent valuation - June 2003 | 7,325 | 7,335 | - | - |
| Accumulated depreciation | (2,287) | (1,489) | - | - |
| | 11,148 | 9,412 | - | - |

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| **Leased plant and equipment** | | | | |
| At directors' valuation – June 2005 | 6,865 | 5,282 | - | - |
| Accumulated amortisation | (1,524) | (737) | - | - |
| At independent valuation – June 2003 | 4,155 | 4,179 | - | - |
| Accumulated amortisation | (921) | (733) | - | |
| | 8,575 | 7,991 | - | - |
| **Capital works in progress** | | | | |
| At cost | 359 | 271 | - | - |
| | 359 | 271 | - | - |
| **Motor vehicles** | | | | |
| At cost | 378 | 366 | - | - |
| Accumulated depreciation | (252) | (229) | - | - |
| | 126 | 137 | - | - |
| **Leased motor vehicles** | | | | |
| Capitalised cost | 99 | 241 | - | - |
| Accumulated amortisation | (13) | (137) | - | - |
| | 86 | 104 | - | - |
| **Furniture and fixtures** | | | | |
| At cost | 251 | 116 | - | - |
| Accumulated depreciation | (187) | (57) | - | - |
| | 64 | 59 | - | - |

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| **Office equipment** | | | | |
| At cost | 1,164 | 1,295 | - | - |
| Accumulated depreciation | (928) | (925) | - | - |
| | 236 | 370 | - | - |
| **Leased office equipment** | | | | |
| Capitalised cost | 237 | 237 | - | - |
| Accumulated amortisation | (190) | (128) | - | - |
| | 47 | 109 | - | - |
| Total plant and equipment net book value | **20,687** | **18,509** | **-** | **-** |

### Valuations of plant and equipment

Plant and equipment, including leased plant and equipment, are measured on a fair value basis, being the amount for which the assets could be exchanged between knowledgeable and willing parties in an arm's length transaction, having regard to the highest and best use of the asset for which the other parties would be willing to pay. The current year's valuation was determined by directors, taking into account the independent valuation in June 2003, additions and disposals during the year and market movements. The valuation previously undertaken was determined by an independent valuer on the basis of open market values for existing use.

### Reconciliations

Reconciliations of the carrying amounts for each class of plant and equipment are set out below.

| | Leasehold improvements $'000 | Plant & equipment $'000 | Leased plant & equipment $'000 | Capital works in progress $'000 | Motor vehicles $'000 | Leased motor vehicles $'000 | Furniture & fixtures $'000 | Office equipment $'000 | Leased office equipment $'000 | Total $'000 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Consolidated** | | | | | | | | | | |
| Carrying amount at beginning of year | 56 | 9,412 | 7,991 | 271 | 137 | 104 | 59 | 370 | 109 | 18,509 |
| Additions | - | 4,775 | 1,583 | 359 | 80 | - | 7 | 86 | - | 6,890 |
| Acquisition of business | - | 303 | - | - | 15 | 99 | 30 | - | - | 447 |
| Disposals | - | (590) | (17) | (271) | (45) | (79) | - | - | - | (1,002) |
| Depreciation | (10) | (2,752) | - | - | (61) | - | (32) | (220) | - | (3,075) |
| Amortisation | - | - | (982) | - | - | (38) | - | - | (62) | (1,082) |
| Carrying amount at end of year | **46** | **11,148** | **8,575** | **359** | **126** | **86** | **64** | **236** | **47** | **20,687** |

## 12. INTANGIBLE ASSETS

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| Goodwill | | | | | |
| at cost | | 5,432 | 1,130 | 150 | 150 |
| Accumulated amortisation | | (285) | (37) | (150) | (150) |
| | | 5,147 | 1,093 | - | - |
| Formation costs | | 39 | 39 | - | - |
| Pipeline rights | | 1,786 | 1,786 | 1,786 | 1,786 |
| | | **6,972** | **2,918** | **1,786** | **1,786** |

## 13. OTHER NON-CURRENT ASSETS

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| Investments | 19 | 19 | 1,260 | 1,260 |
| Deferred expenditure | 36 | 16 | - | - |
| Research and development costs | 1,070 | 426 | - | - |
| Exploration, evaluation and development expenditure - at cost | 3,350 | 2,508 | - | - |
| | **4,475** | **2,969** | **1,260** | **1,260** |

The exploration, evaluation and development expenditure relates to exploration and evaluation of the Group's interests in the Gloucester and Bowen Basins.

## 14. PAYABLES

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **Current** | | | | | |
| Trade creditors | | 9,500 | 15,328 | 46 | 45 |
| Other creditors and accruals | | 7,366 | 3,296 | 341 | 420 |
| Excess of progress billings over costs incurred | | 2,928 | 2,004 | - | - |
| Loan from related entity | | 435 | 150 | 285 | - |
| | | **20,229** | **20,778** | **672** | **465** |
| **Non-current** | | | | | |
| Other loans - controlled entities | 30 | **-** | **-** | **12,488** | **10,627** |

## 15. INTEREST-BEARING LIABILITIES

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **Current** | | | | | |
| Bank overdraft - secured | 27(a) | 3,566 | 1,663 | - | - |
| Other borrowings - unsecured | | 409 | - | - | - |
| Other borrowings - secured | | 852 | - | - | - |
| Lease liabilities - secured | 23 | 1,482 | 4,194 | - | - |
| | | **6,309** | **5,857** | **-** | **-** |
| **Non-current** | | | | | |
| Lease liabilities - secured | 23 | 3,696 | 2,599 | - | - |
| Convertible notes - unsecured | 17(b) | 9,872 | - | 9,872 | - |
| | | **13,568** | **2,599** | **9,872** | **-** |
| **Financing arrangements** | | | | | |
| The Group has access to the following lines of credit: | | | | | |
| Bank overdraft | | 2,960 | 3,738 | 2,960 | 3,738 |
| Bank indemnity guarantees and standby letter of credit | | 3,740 | 3,039 | 1,834 | - |
| | | **6,700** | **6,777** | **4,794** | **3,738** |
| Total facilities utilised at balance date: | | | | | |
| Bank overdraft | | 3,566 | 1,663 | - | - |
| Less: Right of set off | | (3,566) | - | - | - |
| Net overdraft | | - | 1,663 | - | - |
| Bank indemnity guarantees and standby letter of credit | | 2,970 | 3,039 | 1,591 | - |
| | | **2,970** | **4,702** | **1,591** | **-** |
| Total facilities not utilised at balance date: | | | | | |
| Bank overdraft | | 2,960 | 2,075 | 2,960 | 3,738 |
| Bank indemnity guarantees and standby letter of credit | | 770 | - | 243 | - |
| | | **3,730** | **2,075** | **3,203** | **3,738** |

### Bank facilities

The bank overdraft, indemnity guarantee and standby letter of credit are all secured by a registered fixed and floating charge over all the assets of the consolidated entity and are subject to annual review.

**Finance lease facilities**
The Group's lease liabilities are secured by the leased assets of $8,707,000 (2004: $8,204,000), and in the event of default, the assets revert to the lessor.

**Convertible notes**
In December 2004 and February 2005, the Company issued 10,000,000 $1.00 unsecured redeemable convertible notes. The notes carry a fixed coupon of 9.5% per annum and have a term of 3 years unless converted or redeemed beforehand. Interest is cumulative in the event that an interest payment is not made.

## 16. PROVISIONS

| | Note | Consolidated | | Company | |
|---|---|---|---|---|---|
| | | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| **Current** | | | | | |
| Employee benefits | 29 | 1,402 | 1,106 | - | - |
| Provision for contractual dispute | | - | 3,313 | - | - |
| | | **1,402** | **4,419** | **-** | **-** |
| **Non-current** | | | | | |
| Employee benefits | 29 | 279 | 309 | - | - |
| Provision for contractual dispute | | 3,235 | - | - | - |
| | | **3,514** | **309** | **-** | **-** |

As reported in the 2004 Annual Report, the Company and entities within the consolidated entity are engaged in litigation with DrillTec GUT GmbH in Germany over a contract undertaken in Hong Kong in 2000 and 2001. A judgement was awarded in 2004 against the Company for which full provision was made. The consolidated entity refutes the judgement and has appealed the decision and initiated separate proceedings to recover amounts paid. During the year, the consolidated entity appealed to the Federal Court in Germany on both jurisdictional grounds and points of law. Additionally, claims and counterclaims totalling approximately HK$31 million were filed against DrillTec in Hong Kong. The nature of the claims are complex and are unlikely to be resolved in the next 12 months. Accordingly, the provision has been classified as non-current.

## 17. CONTRIBUTED EQUITY

| | Company | | Company | |
|---|---|---|---|---|
| | 2005 No. of Shares | 2004 No. of Shares | 2005 $'000 | 2004 $'000 |
| Share capital | | | | |
| Ordinary shares, fully paid | 51,582,937 | 50,904,270 | 29,108 | 28,628 |
| Other contributed equity | | | | |
| Redeemable convertible notes - equity portion | | | 128 | - |
| | | | **29,236** | **28,628** |
| **(a) Ordinary shares** | | | | |
| **Movements during the year** | | | | |
| Balance at beginning of year | 50,904,270 | 45,394,990 | 28,628 | 18,178 |
| Private placement for cash net of transaction costs | 250,000 | 5,000,000 | 480 | 9,699 |
| Shares issued in consideration for acquisitions | - | 350,000 | - | 651 |
| Exercise of rights under the Management Rights Plan | 287,667 | 100,000 | - | 100 |
| Payment of fees and costs | 141,000 | - | - | - |
| Shares issued under the Employee Share Acquisition Plan | - | 59,280 | - | - |
| Balance at end of year | **51,582,937** | **50,904,270** | **29,108** | **28,628** |

Holders of ordinary shares are entitled to receive dividends and, in the event of a winding up of the Company, to any proceeds of liquidation after all creditors and other stockholders.

On a show of hands, every holder of ordinary shares present at a shareholder meeting in person or by proxy is entitled to one vote and upon a poll, each share is entitled to one vote.

| | Company | |
|---|---|---|
| | 2005 $'000 | 2004 $'000 |
| **(b) Redeemable convertible notes** | | |
| **Movements during the year** | | |
| Balance at beginning of year | - | - |
| Equity portion of 10,000,000 redeemable convertible notes issued during the year | 128 | - |
| Balance at end of year | **128** | **-** |

In December 2004 and February 2005, the Company issued 10,000,000 $1.00 redeemable convertible notes. The conversion price is 90% of the volume weighted average sale price of the Company's shares over the 30 days prior to conversion subject to a minimum and maximum conversion price respectively of $2.00 and $2.50 per share. Holders may convert up to 50% of their notes during the first year and the balance thereafter. Prior to maturity, the Company may redeem up to 50% of the notes on or after the first year of their issue. The Company's right of redemption prevails over the conversion rights of the holder. The notes carry no voting rights.

The convertible notes have been accounted for as compound financial instruments in accordance with accounting policy Note 1.

In the event of the winding up of the Company, the holders of convertible notes rank above shareholders and are entitled to the proceeds of liquidation only to the extent of the face value of the notes and any accumulated interest.

The proceeds received have been accounted for as follows:

| | | Consolidated | | Company | |
|---|---|---|---|---|---|
| | Note | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Non-current interest bearing liabilities | 15 | 9,872 | - | 9,872 | - |
| Contributed equity | | 128 | - | 128 | - |
| **Total** | | **10,000** | **-** | **10,000** | **-** |

### Management rights

Details relating to the Management Rights Plan including details of rights issued, exercised and cancelled during the financial year and rights outstanding at the end of the financial year are set out in Note 29.

### Employee share scheme

Details relating to the Employee Share Acquisition Plan are set out in Note 29.

## 18. RESERVES

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Asset revaluation | 964 | 964 | - | - |
| Capital profits | - | - | 3,733 | 14,533 |
| | **964** | **964** | **3,733** | **14,533** |
| **Movements during the year** | | | | |
| *Asset revaluation* | | | | |
| Balance at beginning of year | 964 | 1,058 | - | - |
| Revaluation (decrements): | | | | |
| Plant and equipment | - | (94) | - | - |
| Balance at end of year | **964** | **964** | **-** | **-** |
| *Capital Profit* | | | | |
| Balance at beginning of year | - | - | 14,533 | 24,533 |
| Transfer to retained profits | - | - | (10,800) | (10,000) |
| Balance at end of year | **-** | **-** | **3,733** | **14,533** |

### Nature and purpose of reserves

***Asset revaluation***

The asset revaluation reserve includes the net revaluation increments and decrements arising from the revaluation of non-current assets measured at fair value in accordance with AASB 1041.

***Capital profits***

The capital profits reserve represents profits from the sale of businesses to subsidiary entities.

## 19. (ACCUMULATED LOSSES)/RETAINED PROFITS

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Retained profits at beginning of year | 14,672 | 11,447 | 3,633 | 22 |
| Transfer from reserves | - | - | 10,800 | 10,000 |
| Net (loss)/profit attributable to members of the parent entity | (21,840) | 7,052 | (21,709) | (2,562) |
| Dividends recognised during the year | (4,109) | (3,827) | (4,109) | (3,827) |
| **(Accumulated losses)/retained profits at end of year** | **(11,277)** | **14,672** | **(11,385)** | **3,633** |

## 20. DIVIDENDS

| | Cents per share | Total amount $'000 | Franked/ unfranked | Date of Payments |
|---|---|---|---|---|
| Dividends recognised in the current year by the Company are: | | | | |
| **2005** | | | | |
| Interim 2005 - ordinary | 3.5 | 1,802 | unfranked | 24 June 2005 |
| Final 2004 - ordinary | 4.5 | 2,307 | 50% franked | 16 December 2004 ($1,479,000) & 24 February 2005 ($828,000) |
| Total amount | | 4,109 | | |
| **2004** | | | | |
| Interim 2004 - ordinary | 3.5 | 1,779 | unfranked | 24 June 2004 |
| Final 2003 - ordinary | 4.5 | 2,048 | unfranked | 16 December 2003 |
| Total amount | | 3,827 | | |

| | Company | |
|---|---|---|
| | 2005 $'000 | 2004 $'000 |
| **Dividend franking account** | | |
| 30% franking credits available to shareholders of the Company for subsequent financial year. | 777 | 1,508 |

The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends.

## 21. TOTAL EQUITY RECONCILIATION

| | Note | Consolidated | | Company | |
|---|---|---|---|---|---|
| | | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Total equity at beginning of year | | 44,264 | 30,683 | 46,794 | 42,733 |
| Total changes in parent entity interest in equity recognised in statement of financial performance | | (21,840) | 6,958 | (21,709) | (2,562) |
| Transactions with owners as owners: | | | | | |
| Contributions of ordinary shares | 17 | 480 | 10,450 | 480 | 10,450 |
| Equity portion of convertible notes | 17 | 128 | - | 128 | - |
| Dividends | 20 | (4,109) | (3,827) | (4,109) | (3,827) |
| **Total equity at end of year** | | **18,923** | **44,264** | **21,584** | **46,794** |

## 22. ADDITIONAL FINANCIAL INSTRUMENT DISCLOSURE

**(a) Interest rate risk exposure**

The Group's exposure to interest rate risk and the effective weighted average interest rate for classes of financial assets and financial liabilities is set out below:

| | Note | Weighted average interest rate % | Floating interest rate $'000 | Fixed interest maturing in: Less than 1 year $'000 | 1 to 5 years $'000 | More than 5 years $'000 | Non-interest bearing $'000 | Total $'000 |
|---|---|---|---|---|---|---|---|---|
| **2005** | | | | | | | | |
| *Financial Assets* | | | | | | | | |
| Cash assets | 7 | 5.00 | 4,060 | - | - | - | - | 4,060 |
| Receivables | 8 | - | - | - | - | - | 11,626 | 11,626 |
| | | | **4,060** | **-** | **-** | **-** | **11,626** | **15,686** |
| *Financial Liabilities* | | | | | | | | |
| Provision | 16 | 6.50 | 3,235 | - | - | - | - | 3,235 |
| Bank overdraft | 15 | 9.60 | 3,566 | - | - | - | - | 3,566 |
| Other borrowings | 15 | 9.60 | 1,261 | - | - | - | - | 1,261 |
| Payables | 14 | - | - | - | - | - | 16,866 | 16,866 |
| Lease liabilities | 15 | 10.65 | - | 1,482 | 3,696 | - | - | 5,178 |
| Employee benefits | 16,29 | - | 279 | - | - | - | 1,402 | 1,681 |
| Related party loans | 14 | - | - | - | - | - | 435 | 435 |
| | | | **8,341** | **1,482** | **3,696** | **-** | **18,703** | **32,222** |

| | Note | Weighted average interest rate % | Floating interest rate $'000 | Fixed interest maturing in: Less than 1 year $'000 | 1 to 5 years $'000 | More than 5 years $'000 | Non-interest bearing $'000 | Total $'000 |
|---|---|---|---|---|---|---|---|---|
| **2004** | | | | | | | | |
| *Financial Assets* | | | | | | | | |
| Cash assets | 7 | 4.75 | 14,203 | - | - | - | - | 14,203 |
| Receivables | 8 | - | - | - | - | - | 25,676 | 25,676 |
| | | | **14,203** | **-** | **-** | **-** | **25,676** | **39,879** |
| *Financial Liabilities* | | | | | | | | |
| Provision | 16 | 6.50 | 3,313 | - | - | - | - | 3,313 |
| Bank overdraft | 15 | 9.60 | 1,663 | - | - | - | - | 1,663 |
| Payables | 14 | - | - | - | - | - | 18,624 | 18,624 |
| Lease liabilities | 15 | 10.65 | - | 4,194 | 2,599 | - | - | 6,793 |
| Employee benefits | 16,29 | - | 309 | - | - | - | 1,106 | 1,415 |
| Related party loans | 14 | - | - | - | - | - | 150 | 150 |
| | | | **5,285** | **4,194** | **2,599** | **-** | **19,880** | **31,958** |

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| **(b) Foreign exchange risk** | | | | |
| The Australian dollar equivalents of unhedged amounts payable or receivable in foreign currencies calculated at year-end exchange rates, are as follows: | | | | |
| **United States Dollars** | | | | |
| *Amounts payable:* | | | | |
| Current | 105 | 97 | - | - |
| *Amounts receivable:* | | | | |
| Current | 8,933 | 9,532 | - | - |
| **Hong Kong Dollars** | | | | |
| *Amounts payable:* | | | | |
| Current | 1,314 | 12 | - | - |
| *Amounts receivable:* | | | | |
| Current | 1,552 | 153 | - | - |

**(c) Credit risk exposure**

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The carrying amount of financial assets recorded in the financial statements, net of any allowances for losses, represents the Group's maximum exposure to credit risk without taking account of the value of any collateral or other security obtained.

The Group is not materially exposed to any individual customer. The credit risk to the Group of trade debtors due from customers other than that described above is concentrated in the engineering and construction industry.

**(d) Net fair value**

The carrying amount of financial assets and financial liabilities recorded in the financial statements represents their respective net fair values, determined in accordance with the accounting policies disclosed in Note 1 to the financial statements.

The net fair value of financial assets and financial liabilities are determined as follows:

- the net fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- the net fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow theory.

The net fair value of the following financial assets and liabilities approximate the carrying value: cash assets, receivables, investments, bank overdraft, payables, bank loans, lease liabilities, employee benefits, related party loans and other loans.

## 23. COMMITMENTS

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Refer to Note 26 for joint venture commitments. | | | | |
| **Finance lease payment commitments** | | | | |
| Finance lease commitments are payable: | | | | |
| Within 1 year | 1,868 | 1,377 | - | - |
| 1 year or later and no later than 5 years | 4,042 | 6,014 | - | - |
| | **5,910** | **7,391** | **-** | **-** |
| Less: future lease finance charges | (732) | (598) | - | - |
| **Total lease liability** | **5,178** | **6,793** | **-** | **-** |
| Lease liabilities provided for in the financial statements: | | | | |
| Current | 1,482 | 4,194 | - | - |
| Non-current | 3,696 | 2,599 | - | - |
| **Total lease liability** | **5,178** | **6,793** | **-** | **-** |

The Group leases plant and equipment under finance leases expiring from one to four years. At the end of the lease terms, the Group has the option to purchase the plant and equipment.

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| **Non-cancellable operating lease expense commitments** | | | | |
| Future operating lease commitments not provided for in the financial statements and payable: | | | | |
| Within 1 year | 468 | 107 | - | - |
| 1 year or later and no later than 5 years | 498 | - | - | - |
| | **966** | **107** | **-** | **-** |

The consolidated entity leases properties under non-cancellable operating leases expiring from one to three years. The leases generally provide the consolidated entity with a right of renewal.

## 24. CONTINGENT LIABILITIES

Details of contingent liabilities and contingent assets where the probability of future payments/receipts is not considered remote are set out below, as well as details of contingent liabilities and contingent assets, which although considered remote, the directors consider should be disclosed.

The directors are of the opinion that provisions are not required in respect of these matters, as it is not probable that a future sacrifice of economic benefits will be required or the amount is not capable of reliable measurement.

### Bonding & bank indemnity guarantees

The consolidated entity has insurance bonding in place totalling $10,573,000 (2004: $10,465,000) of which $2,379,000 (2004: $600,000) is on projects which are yet to achieve practical completion.

The consolidated entity has bank indemnity guarantees in place totalling $3,142,000 (2004: $2,304,000) of which $1,456,000 (2004: $1,890,000) are on projects which are yet to achieve practical completion. No bid bonds were outstanding at 30 June 2005 (2004: $735,000).

### Indemnities

Indemnities have been provided to directors and certain executive officers of the Company in respect of liabilities to third parties arising from their positions, except where the liability arises out of conduct involving a lack of good faith. No monetary limit applies under these indemnities.

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 $'000 | 2004 $'000 | 2005 $'000 | 2004 $'000 |
| Total estimated contingent liabilities | 3,835 | 3,225 | 3,835 | 3,225 |

There is no known current exposure under these indemnities.

## 25. CONTROLLED ENTITIES

Particulars in relation to controlled entities:

| Name of entity | Country of incorporation | Ownership interest 2005 % | Ownership interest 2004 % |
|---|---|---|---|
| **Parent entity** | | | |
| AJ Lucas Group Limited | | | |
| **Controlled entities** | | | |
| AJ Lucas Operations Pty Limited (i) | Australia | 100 | 100 |
| AJ Lucas Plant & Equipment Pty Limited | Australia | 100 | 100 |
| AJ Lucas Drilling Pty Limited | Australia | 100 | 100 |
| AJ Lucas Pipelines Pty Limited | Australia | 100 | 100 |
| AJ Lucas Testing Pty Limited | Australia | 100 | 100 |
| Smart Electrical & Power Services Pty Limited | Australia | 100 | 100 |
| AJ Lucas Joint Ventures Pty Limited | Australia | 100 | 100 |
| Coastal Sand Technologies Pty Limited | Australia | 100 | 100 |
| AJ Lucas (Hong Kong) Limited | Hong Kong | 100 | 100 |
| Lucas Coal Seam Gas Pty Limited | Australia | 100 | 100 |
| AJ Lucas Coal Technologies Pty Limited | Australia | 100 | 100 |
| AJ Lucas (USA) Inc. | USA | 100 | 100 |
| Lucas Stuart Pty Limited (ii) | Australia | 100 | 100 |
| Wholly owned subsidiaries of Lucas Stuart Pty Ltd | | | |
| Ketrim Pty Limited | Australia | 100 | 100 |
| Stuart Painting Services Pty Ltd | Australia | 100 | 100 |
| Lucas Stuart Projects Pty Ltd | Australia | 100 | 100 |

(i) AJ Lucas Admin Pty Limited changed its name during the year to AJ Lucas Operations Pty Limited
(ii) Stuart Pty Limited changed its name during the year to Lucas Stuart Pty Limited

## 26. INTERESTS IN JOINT VENTURE OPERATIONS

| Joint venture name | Principal activities | Participation interest 2005 % | Participation interest 2004 % | Contribution to operating results of the consolidated entity 2005 $'000 | Contribution to operating results of the consolidated entity 2004 $'000 |
|---|---|---|---|---|---|
| Clough Lucas | Pipe laying and related construction activities | 50 | 50 | 13 | 52 |
| Clough Lucas Bundeena | Pipe laying and related construction activities | 20 | 20 | 78 | 42 |
| Amec Spie Capag Lucas | Engineering, design, procurement & construction of pipeline | 50 | 50 | (665) | 4,116 |
| Lucas Molopo | Exploration for methane gas | 86 | 75 | - | - |

In September 2005, Molopo Australia Limited exercised its option to increase its participating interest in the Lucas Molopo Joint Venture from 14% to 30%.

Included in the assets and liabilities of the Group are the following items which represent the Group's interest in the assets and liabilities employed in the joint ventures, recorded in accordance with the accounting policies described in Note 1.

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current assets** | | | | |
| Cash assets | 2,070 | 10,195 | - | - |
| Receivables | 179 | 2,114 | - | - |
| Work in progress | 74 | - | - | - |
| **Total current assets** | **2,323** | **12,309** | **-** | **-** |
| **Liabilities** | | | | |
| **Current liabilities** | | | | |
| Payables | 941 | 4,852 | - | - |
| **Total liabilities** | **941** | **4,852** | **-** | **-** |

**Commitments**

The Group has commitments to all joint ventures of which it is a party to supply loan funds as and when needed. Failure to supply funds may result in exclusion from the joint ventures. It is not possible to estimate the funding requirements of the joint ventures.

In respect of the Lucas Molopo Joint Venture, it is a condition of the Petroleum Exploration License (PEL 285) that $1.8 million be spent by September 2007 of which the Group is required to fund 70%.

## 27. NOTES TO THE STATEMENTS OF CASH FLOWS

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| **(a) Reconciliation of cash** | | | | | |
| For the purposes of the statements of cash flows, cash includes cash at bank and on hand. Cash as at the end of the financial year as shown in the statements of cash flows is reconciled to the related items in the statements of financial position as follows: | | | | | |
| Cash assets | 7 | 4,060 | 14,203 | 1,383 | 229 |
| Bank overdraft | 15 | (3,566) | (1,663) | - | - |
| **Total cash** | | **494** | **12,540** | **1,383** | **229** |
| **(b) Reconciliation of (loss)/profit from ordinary activities after income tax to net cash (used in)/provided by operating activities** | | | | | |
| (Loss)/profit from ordinary activities after income tax | | (21,840) | 6,782 | (21,709) | (2,562) |
| Add/ (less) items classified as investing/ financing activities: | | | | | |
| Interest on capitalised leases | | 602 | 743 | - | - |
| Loss/(gain) on sale of non-current assets | | 885 | (256) | - | - |

| | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|
| Add /(less) non-cash items: | | | | |
| Depreciation | 3,075 | 2,226 | - | - |
| Increase/(decrease) in provision for doubtful debts | 6,946 | (2,213) | - | - |
| Decrease in provision for other loans | - | (2,078) | - | - |
| *Amortisation of:* | | | | |
| Leased assets | 1,082 | 1,639 | - | - |
| Goodwill | 248 | 37 | - | 30 |
| Research and development expenditure | 355 | 355 | - | - |
| Bonding costs | - | 376 | - | - |
| Unrealised foreign exchange (gains) | (64) | (357) | - | - |
| (Decrease)/increase in deferred tax liabilities | (4,847) | (1,172) | (4,847) | 4,847 |
| (Increase)/decrease in deferred tax assets | (1,053) | 883 | (1,133) | (788) |
| Increase/(decrease) in provisions for employee entitlements | 228 | (100) | - | - |
| (Decrease)/increase in other provisions | (14) | 3,313 | - | - |
| Decrease/(increase) in loans to controlled entities | - | - | 27,373 | (1,542) |
| (Decrease) in current tax liabilities | (463) | (82) | - | - |
| **Net cash (used in)/provided by operating activities before changes in assets and liabilities** | **(14,860)** | **10,096** | **(316)** | **(15)** |
| Change in assets and liabilities adjusted for effects of purchase and disposal of controlled entities during the financial year: | | | | |
| Decrease in receivables | 7,831 | 7,580 | - | 56 |
| (Increase)/decrease in other current assets | (779) | 10 | (340) | - |
| Decrease/(increase) in inventories | 4,975 | (8,954) | - | - |
| (Increase) in other non-current assets | (2,702) | - | - | - |
| (Decrease)/increase in payables | (1,029) | (26,945) | 207 | 2 |
| **Net cash (used in)/provided by operating activities** | **(6,564)** | **(18,213)** | **(449)** | **43** |

**(c) Business acquisition**

On 16 December 2004, the Company acquired the business of the Mace Group of Companies (2004: acquisition of Stuart Pty Limited). Details of the acquisition are as follows:

| | Consolidated | |
|---|---|---|
| | **2005 $'000** | **2004 $'000** |
| **Consideration** | | |
| Gross cost | 2,908 | 1,043 |
| Acquisition costs | 100 | 197 |
| Total consideration | 3,008 | 1,240 |
| **Fair value of net assets acquired** | | |
| **Current assets** | | |
| Cash | 597 | 1,856 |
| Receivables (net) | 727 | 239 |
| Inventories | - | 4,980 |
| Other | 7 | - |
| **Total current assets** | **1,331** | **7,075** |
| **Non-current assets** | | |
| Plant and equipment | 445 | 193 |
| Deferred tax asset | - | 419 |
| **Total non-current assets** | **445** | **612** |
| **Total assets** | **1,776** | **7,687** |
| **Current liabilities** | | |
| Interest-bearing liabilities | 135 | - |
| Trade creditors | 195 | 6,245 |
| Employee entitlements | 38 | 606 |
| Other loans | - | 150 |
| **Total current liabilities** | **368** | **7,001** |
| **Non-current liabilities** | | |
| Deferred tax liability | - | 576 |
| **Total non-current liabilities** | **-** | **576** |
| **Total liabilities** | **368** | **7,577** |
| Net assets acquired | 1,408 | 100 |
| Goodwill on acquisition | 1,600 | 1,130 |
| Total consideration | 3,008 | 1,240 |
| **Net cash inflow on acquisition** | | |
| Cash consideration | (3,008) | (197) |
| Less cash balances acquired | 597 | 1,856 |
| Net cash (outflow)/inflow | (2,411) | 1,659 |

**(d) Non-cash financing and investment activities**

During the year, the consolidated entity acquired plant and equipment with an aggregate fair value of $2,037,000 (2004: $5,510,000) by means of finance leases. These purchases are not reflected in the Statements of Cash Flows.

**(e) Financing arrangements**

Refer note 15.

## 28. DIRECTOR AND EXECUTIVE DISCLOSURES

**Remuneration philosophy**

The key principle of the Company's executive remuneration policy is to set remuneration at a level that will attract and retain qualified and experienced personnel and motivate and reward them to achieve strategic objectives and improve business results.

Remuneration is structured to reward employees for increasing shareholder value. This is achieved by providing a fixed remuneration component together with short and long term performance based incentives.

Through creating goal congruence between directors, executives and shareholders, it is hoped to maximise shareholder value.

AJ Lucas aims to set fixed annual remuneration at market median levels for jobs of comparable size and responsibility using established job evaluation methods and to provide incentives to enable top performers to be remunerated at the upper end of the market, subject always to the performance of the Group.

The aim of the incentive plans is to drive performance to successfully implement annual business plans and increase shareholder value.

The remuneration for executive and staff is reviewed annually, using a formal performance appraisal process and market data derived from independent surveys of people with similar competencies and responsibilities.

**Remuneration structure**

Remuneration packages include a mix of fixed and variable remuneration and long term incentives.

***Fixed remuneration***

Fixed remuneration consists of base remuneration (which is calculated on a total cost basis and includes any fringe benefit tax (FBT) charges related to employee benefits including motor vehicles) as well as employer contributions to superannuation.

***Incentive based remuneration***

Incentive based remuneration includes long term and short term incentives and is designed to reward executive directors and senior executives for meeting or exceeding their financial and personal objectives. The short term incentive (STI) is an “at risk” bonus provided in the form of cash and is subject to the over-riding discretion of the senior executive team.

The long term incentive is provided as rights over ordinary share of the Company in accordance with the rules of the management rights plan, as approved by shareholders at the November 2001 annual general meeting. Each right entitles the holder to one ordinary share in the Company subject to performance hurdles, where applied, being attained and the holder remaining in employment with the Group until the rights vest. The performance hurdles are set by the Board.

*Executive directors*

The only grant of rights currently in place for the executive directors was approved by shareholders at the November 2002 AGM. The rights were issued to the directors on 27 December 2002 and vest in three tranches: one third two years after their grant; a further third after three years and the balance after four years and may only be exercised if the consolidated entity achieves the performance hurdle.

The performance hurdle is that the consolidated entity's averaged earnings per share (EPS) over the three financial years ended prior to any vesting date (two financial years in respect of the first tranche) must equal or exceed that amount that would arise at the rate of 10% per annum compound growth over a deemed EPS base of 12.7 cents per share. If the performance hurdle is not achieved in respect of a tranche, the Board may re-evaluate the performance at the end of a subsequent year and allow the rights to be exercised if the hurdle is subsequently satisfied. Assuming the performance hurdle is satisfied and the rights are exercised, the shares will be issued for nil consideration.

The fair value of the rights was calculated at grant date by an independent valuer using a Black-Scholes technique with the following assumptions:

| | |
|---|---|
| Share price on grant date | $0.98 |
| Exercise price | Nil |
| Volatility | 35% |
| Risk free interest rate | 4.8% |
| Dividend yield | 7.7% |

The valuation model incorporates the likelihood of attaining the performance hurdle in the valuation but does not include any allowance for executive turnover. The fair value of tranches 2 and 3 based on EPS for the 2004/05 and 2005/06 financial years has been calculated as $nil as the performance hurdle is unlikely to be met.

*Named executives*

The rights' grant in place for the named executives were made on two separate occasions, May 2004 and June 2005. The May 2004 issue was awarded in part for several years of past performance. The June 2005 issue was awarded only to new executives commencing employment with the Group in 2004/05. The fair value of the rights awarded under each of the issues was calculated at grant date by an independent valuer using a Black-Scholes technique with the following assumptions:

| | **May 2004 Grant** | **June 2005 Grant** |
|---|---|---|
| Share price on grant date | $1.66 | $1.52 |
| Exercise price | Nil | Nil |
| Volatility | 38% | 39% |
| Risk free interest rate | 5.6% | 5.1% |
| Dividend yield | 5.4% | 5.6% |

The fair value of a right at grant date was calculated as $1.29 for the May 2004 issue and $1.20 for the June 2005 issue.

***Other benefits***

The remuneration policy provides that directors and senior executives may obtain loans from the Group. All such loans are made at commercial rates and therefore do not represent a benefit to the recipient or attract fringe benefit tax. Interest on the loans is payable quarterly in arrears. No loan amounts have been written down as the balances are considered fully collectible.

**Service agreements**

All executive directors and senior executives are employed under a standard AJ Lucas contract. The service contract outlines the components of remuneration but does not prescribe how remunerations levels are modified year to year. Remuneration levels are reviewed every year to take into account cost of living changes, any change in the scope of the role performed and any changes required to meet the principles of the remuneration policy.

The service contracts are unlimited in term. All contracts can be terminated without notice by the Company with compensation, if any, payable to the employee in accordance with the law or by negotiated agreement.

**Remuneration of non-executive directors**

Non-executive directors' individual fees are determined by the Board within the aggregate amount approved by shareholders. The current maximum aggregate amount that may be paid to all non-executive directors is $450,000 per annum as approved by shareholders at the annual general meeting held in November 2002.

Non-executive directors' base fees are presently $30,000 per annum, unchanged since 1999, including attendance at committee meetings. It is recognised that the level of such fees is less than generally paid to such persons by comparable sized companies. Accordingly, the base fee has been increased to $45,000 per annum with effect from 1 July 2005.

In recognition of the level of base fees paid to non-executive directors, the Company has in the past periodically awarded shares under its Deferred Share Plan to such persons. Such shares vest from the date of issue but cannot be disposed of until the earlier of 10 years from the date of issue or the date their service with AJ Lucas ceases. The last issue of such shares occurred in December 2002 following approval being granted by shareholders.

The following table shows details of the nature and amount of the remuneration of the directors of the Company ("specified directors") and the five executives of the Group with the greatest authority ("specified executives") for the year ended 30 June 2005.

| | | Primary | | Post- employment | Equity compensation | | |
|---|---|---|---|---|---|---|---|
| | | Salary/fees [1] $ | Non-cash benefits [2] $ | Superannuation contribution $ | Management rights [3] $ | Other benefits $ | Total $ |
| **Specified directors** | | | | | | | |
| **Executive** | | | | | | | |
| Allan Campbell | 2005 | 364,410 | - | - | - | 4,673 | 369,083 |
| | 2004 | 364,410 | - | - | 100,208 | 7,000 | 471,618 |
| Andrew Lukas | 2005 | 218,707 | 6,752 | 18,000 | - | 4,673 | 248,132 |
| | 2004 | 232,062 | 9,402 | 18,000 | 100,208 | 7,000 | 366,672 |
| Ian Stuart-Robertson | 2005 | 247,419 | 3,940 | 18,578 | - | 4,673 | 274,610 |
| | 2004 | 213,500 | - | - | - | 7,000 | 220,500 |
| **Non-executive** | | | | | | | |
| Martin Green | 2005 | 30,000 | - | - | - | 4,673 | 34,673 |
| | 2004 | 30,000 | - | - | - | 7,000 | 37,000 |
| Julian Gregory [4] | 2005 | 49,900 | - | - | - | 4,673 | 54,573 |
| | 2004 | 27,525 | - | - | - | 1,000 | 28,525 |
| Garry O'Meally | 2005 | 30,000 | - | - | - | 4,673 | 34,673 |
| | 2004 | 30,000 | - | - | - | 7,000 | 37,000 |
| **Total** | **2005** | **940,436** | **10,692** | **36,578** | **-** | **28,038** | **1,015,744** |
| **Total** | **2004** | **897,497** | **9,402** | **18,000** | **200,416** | **36,000** | **1,161,315** |

| | | Primary | | Post- employment | Equity compensation | | |
|---|---|---|---|---|---|---|---|
| | | Salary/fees (1) $ | Non-cash benefits (2) $ | Superannuation contribution $ | Management rights (3) $ | Other benefits $ | Total $ |
| **Specified executives** | | | | | | | |
| Kevin Lester | 2005 | 243,367 | 1,445 | 17,077 | 71,446 | - | 333,335 |
| General Manager Pipelines | 2004 | 277,361 | - | 12,870 | 188,400 | 1,000 | 479,631 |
| Tim Herlihy | 2005 | 204,215 | 18,617 | 20,000 | 39,693 | - | 282,525 |
| Chief Financial Officer | 2004 | 201,109 | 30,650 | 20,000 | 104,667 | 1,000 | 357,426 |
| Ian Redfern (5) | 2005 | 223,627 | - | 17,752 | 55,000 | - | 296,379 |
| General Manager Construction | | | | | | | |
| Brett Tredinnick | 2005 | 160,108 | 5,635 | 12,023 | 23,815 | - | 201,581 |
| Operations Manager Drilling | 2004 | 130,144 | 37,580 | 12,240 | 62,800 | 1,000 | 243,764 |
| Mark Tonkin | 2005 | 159,860 | 2,468 | 12,600 | 71,446 | - | 246,374 |
| General Manager Drilling | 2004 | 134,318 | 15,000 | 10,800 | 188,400 | 1,000 | 349,518 |
| **Total** | **2005** | **991,177** | **28,165** | **79,452** | **261,400** | **-** | **1,360,194** |
| **Total** | **2004** | **742,932** | **83,230** | **55,910** | **544,267** | **4,000** | **1,430,339** |
| **Total disclosed** | **2004** | **878,171** | **111,818** | **71,260** | **559,967** | **5,000** | **1,629,216** |

(1) Salary and fees includes salary, annual leave and long service leave on an accrual basis.
(2) Non-cash benefits consists of the provision of a company car and mobile phone.
(3) The notional value ascribed to this long term incentive (management rights) has been determined by an independent consultant using the criteria set out in Accounting Standard AASB1046 and AASB1046A. The notional value of the management rights has been apportioned over their vesting period on a straight line basis. Each management right was valued at $1.29 other than those issued to Mr Ian Redfern which were each valued at $1.20. In valuing the rights, market conditions have been taken into account in both the current and prior periods. Comparative information has not been restated as market conditions were already included in the valuation. The valuation methodology and inputs to the valuation have been disclosed in the narrative preceeding this table. With the exception of management rights granted to Mr Redfern, no management rights were granted in the current year.
(4) Mr Gregory was appointed a director on 29 April 2004. Fees disclosed include fees earned for providing consulting services to the Company.
(5) Mr Redfern was employed from 30 June 2004. His 2004 remuneration is therefore not shown.

**Rights holdings**

The movement in the reporting period in the number of rights over ordinary shares in the Company held directly, indirectly or beneficially, by each specified director and specified executive, including their personally-related entities, is as follows:

| | Held at 1 July 2004 | Granted as remuneration | Exercised | Held at 30 June 2005 | Vested and exercisable at 30 June 2005 |
|---|---|---|---|---|---|
| **Specified directors** | | | | | |
| Allan Campbell | 250,000 | - | - | 250,000 | 83,333 |
| Andrew Lukas | 250,000 | - | - | 250,000 | 83,333 |
| **Specified executives** | | | | | |
| Kevin Lester | 180,000 | - | - | 180,000 | 180,000 |
| Tim Herlihy | 100,000 | - | - | 100,000 | 100,000 |
| Ian Redfern | - | 75,000 | - | 75,000 | 25,000 |
| Brett Tredinnick | 60,000 | - | - | 60,000 | 60,000 |
| Mark Tonkin | 180,000 | - | (60,000) | 120,000 | 120,000 |

**Equity holdings and transactions**

The movement during the reporting period in the number of ordinary shares of the Company held directly, indirectly or beneficially by each specified director and specified executive, including their personally-related entities, is as follows:

| | Held at 1 July 2004 | Received on exercise of rights (i) | Sales | Held at 30 June 2005 |
|---|---|---|---|---|
| **Specified directors** | | | | |
| Allan Campbell | 10,056,750 | - | - | 10,056,750 |
| Andrew Lukas | 6,121,500 | - | - | 6,121,500 |
| Ian Stuart-Robertson | 1,386,200 | - | - | 1,386,200 |
| Martin Green | 75,000 | - | - | 75,000 |
| Garry O'Meally | 109,180 | - | - | 109,180 |
| **Specified executives** | | | | |
| Mark Tonkin | - | 60,000 | (60,000) | - |

(i) No amount was paid on exercise of rights.

**Other transactions with the Company or its controlled entities**

A number of specified directors, or their personally-related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities.

A number of these entities transacted with the Company or its subsidiaries in the reporting period. The terms and conditions of those transactions were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to unrelated entities on an arm's length basis.

The aggregate amounts recognised during the year relating to specified directors and their personally-related entities, were total expense of $525,990. Details of the transactions are as follows:

| Specified directors | Transaction | Note | 2005 $ |
|---|---|---|---|
| Allan Campbell | Executive director services | (i) | 364,410 |
| Ian Stuart-Robertson | Quantity surveyors | (ii) | 141,680 |
| Julian Gregory | Consulting services | (iii) | 19,900 |

(i) Mr Campbell's services to the Company are provided through Argyll Capital Partners Pty Limited. Such services were provided in the ordinary course of business and on normal terms and conditions. The amount payable for these services is shown earlier in this note.

(ii) Mr Stuart-Robertson is a director of John Hollis & Partners which provided quantity surveying services. Amounts were billed based on normal market rates for such services and were due and payable under normal payment terms.

(iii) The Company used the consulting services of Julian Gregory in relation to the review of contracts for services provided by the Group. Amounts were billed based on normal market rates for such services and were due and payable under normal payment terms.

AJ Lucas Holdings Pty Ltd, a company associated with Messrs Campbell, Lukas and Stuart-Robertson, loaned the Company and the Group various amounts throughout the year as follows:

| Balance 1 July 2004 $ | Balance 30 June 2005 $ | Interest paid and payable in the reporting period $ | Highest balance in period $ |
|---|---|---|---|
| 150,000 | 435,000 | - | 435,000 |

The loans were made interest free and without security

| | 30 June 2005 $ |
|---|---|
| **Assets and liabilities arising from the above transactions** | |
| Current liabilities | |
| Loan from related entity | 435,000 |

## 29. EMPLOYEE BENEFITS

| | Note | Consolidated 2005 $'000 | Consolidated 2004 $'000 | Company 2005 $'000 | Company 2004 $'000 |
|---|---|---|---|---|---|
| Aggregate liability for employee benefits, including on-costs | | | | | |
| Current | 16 | 1,402 | 1,106 | - | - |
| Non-current | 16 | 279 | 309 | - | - |
| | | **1,681** | **1,415** | **-** | **-** |
| The present values of employee entitlements not expected to be settled within twelve months of reporting date have been calculated using the following weighted averages: | | | | | |
| Assumed rate of increase in wage and salary rates | | 2.5% | 2.5% | | |
| Discount rate | | 5.1% | 5.1% | | |
| Settlement term (years) | | 10 | 10 | | |
| Number of employees at year end | | 217 | 161 | 5 | 5 |

### Superannuation plans

The Company and certain controlled entities contribute to several defined contribution superannuation funds. Contributions on behalf of employees are payable based on various percentages of their gross salaries.

### Equity-based plans

The Company has three employee incentive schemes approved by shareholders at the annual general meeting held on 28 November 2001. Total securities granted but unissued under these schemes cannot exceed 15% of the total number of shares on issue.

***a) Management rights plan***

The management rights plan (MRP) is available to employees, non-executive directors and other persons at the discretion of the Board. Nominated persons are granted rights to acquire shares in the Company. The issue of these rights can take the form of the award of shares for no monetary consideration, traditional priced options or performance rights (which have no exercise price).

Each right is convertible to one ordinary share. There are no voting or dividend rights attaching to the rights nor are there voting rights attaching to the unissued ordinary shares.

During the year, rights were granted to 3 senior employees. These rights vest at various times as set out in the following table:

| Vesting Date | Vesting proportion |
|---|---|
| 30 June 2005 | 1/3 |
| 30 June 2006 | 1/3 |
| 30 June 2007 | 1/3 |

All these rights expire on the earlier of 28 May 2009 or termination of the employee's employment. There is no performance hurdle for the rights to be exercised and no consideration is payable on their exercise.

Details of rights in aggregate over unissued ordinary shares at the beginning and ending of the reporting period and movements during the year are set out below.

| Grant date | Exercise date on or after | Expiry date | Number of rights at beginning of year | Rights granted | Rights exercised | Rights cancelled | Number of rights On issue | Number of rights Vested |
|---|---|---|---|---|---|---|---|---|
| **Consolidated & Company 2005** | | | | | | | | |
| 23 Dec 2002 | 23 Dec 2004 | 23 Dec 2007 | 166,666 | - | - | - | 166,666 | 166,666 |
| 23 Dec 2002 | 23 Dec 2005 | 23 Dec 2007 | 166,666 | - | - | - | 166,666 | - |
| 23 Dec 2002 | 23 Dec 2006 | 23 Dec 2007 | 166,668 | - | - | - | 166,668 | - |
| 28 May 2004 | 30 Jun 2004 | 28 May 2009 | 808,333 | - | (287,667) | - | 520,666 | 520,666 |
| 28 May 2004 | 30 Jun 2005 | 28 May 2009 | 435,667 | - | - | (33,000) | 402,667 | 402,667 |
| 28 May 2004 | 30 Jun 2006 | 28 May 2009 | 63,000 | - | - | (5,000) | 58,000 | - |
| 27 June 2005 | 30 Jun 2005 | 28 May 2009 | - | 40,000 | - | - | 40,000 | 40,000 |
| 27 June 2005 | 30 Jun 2006 | 28 May 2009 | - | 40,000 | - | - | 40,000 | - |
| 27 June 2005 | 30 Jun 2007 | 28 May 2009 | - | 40,000 | - | - | 40,000 | - |
| | | | **1,807,000** | **120,000** | **(287,667)** | **(38,000)** | **1,601,333** | **1,129,999** |

All rights are exercisable for nil consideration.

***b) Deferred share plan***

The deferred share plan (DSP) is available to chosen directors, including non-executives, and employees to allow them to take a part of their annual remuneration in the form of shares in the Company. Shares vest from the date of issue but cannot be disposed of until the earlier of 10 years from the date of issue or the date their employment or service with the Group ceases. No shares (2004: nil) were issued during the year.

***c) Employee share acquisition plan***

The employee share acquisition plan (ESAP) is available to all eligible employees to acquire ordinary shares in the Company for no consideration as a bonus component of their remuneration. The ESAP complies with current Australian tax legislation, enabling permanent employees to have up to $1,000 of free shares per annum, in respect of an employee share scheme, excluded from their assessable income.

Employees must have been employed by any entity within the consolidated entity for a minimum period of one year to be eligible. Shares issued under the ESAP rank equally with other fully paid ordinary shares including full voting and dividend rights from the date they vest. No consideration for the shares is receivable from the employees.

Shares are issued in the name of the participating employee and vest from the date of issue. However, they cannot be disposed of until the earlier of 3 years from the date of issue or the date their employment with the Group ceases. The Board has the discretion to vary this restriction. The ESAP has no conditions that could result in a recipient forfeiting ownership of shares.

No shares under this plan were issued during the year.

***Summary of share movements in the plan:***

| | Opening balance | Granted & vested during the year | | Trading restriction lifted during the year | Closing balance | |
|---|---|---|---|---|---|---|
| **Grant dates** | **Number** | **Number of shares** | **Fair value per share $** | **Number** | **Number** | **Fair value aggregate $** |
| **2005** | 59,280 | - | - | (10,830) | 48,450 | 67,350 |
| **2004** | | | | | | |
| 28 May 2004 | - | 59,280 | 1.39 | - | 59,280 | 74,456 |

The trading restrictions lifted during the year all relate to employees who ceased employment with the Group during the year.

## 30. NON-DIRECTOR RELATED PARTIES

The only class of non-director parties is wholly-owned controlled entities.

Details of interests in wholly-owned controlled entities are set out in Note 25. These companies trade with each other from time to time on normal commercial terms.

The aggregate amounts included in the (loss)/profit from ordinary activities before income tax that resulted from transactions between entities in the Group are:

| | 2005 $'000 | 2004 $'000 |
|---|---|---|
| Interest revenue | - | 833 |
| Interest expense | - | 833 |
| *Receivables:* | | |
| Aggregated amount receivable from wholly owned controlled entities of the Company: | | |
| Coastal Sand Technologies Pty Limited | 55 | 55 |
| Less: Provision for doubtful loan | (55) | (55) |
| | - | - |
| AJ Lucas Drilling Pty Limited | - | 12,028 |
| AJ Lucas Testing Pty Limited | - | 1,036 |
| AJ Lucas Pipelines Pty Limited | - | 13,593 |
| AJ Lucas Joint Ventures Pty Limited | 5,085 | 12,867 |
| AJ Lucas Operations Pty Limited | 18,124 | 700 |
| Lucas Coal Seam Gas Pty Limited | 3,429 | 2,253 |
| AJ Lucas Coal Technologies Pty Limited | 5,783 | 6,739 |
| AJ Lucas Plant & Equipment Pty Limited | - | 7,617 |
| Smart Electrical & Power Services Pty Limited | 1 | - |
| AJ Lucas (USA) Inc. | 27 | 27 |
| Lucas Stuart Pty Limited | 4,747 | 1,080 |
| | **37,196** | **57,940** |
| *Payables:* | | |
| Aggregate amount payable to wholly controlled entities of the Company: | | |
| AJ Lucas (Hong Kong) Limited | **12,488** | **10,627** |

## 31. AUDITORS' REMUNERATION

| | Consolidated | | Company | |
|---|---|---|---|---|
| | 2005 | 2004 | 2005 | 2004 |
| | $ | $ | $ | $ |
| Audit services: | | | | |
| Auditors of the Company - KPMG | 237,287 | 167,142 | 18,500 | 16,000 |
| Other services: | | | | |
| Auditors of the Company - KPMG | | | | |
| Taxation services | 75,330 | 66,400 | - | - |

## 32 IMPACT OF ADOPTING AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

AJ Lucas Group will be required to prepare financial statements complying with Australian equivalents to International Financial Reporting Standards (AIRFS) as issued by the Australian Accounting Standards Board for the first time for the half year ending 31 December 2005 and year ending 30 June 2006.

This financial report has been prepared in accordance with Australian accounting standards and other financial reporting requirements (Australian GAAP) applicable for the reporting period ended 30 June 2005.

### Transition management

The chief financial officer has established a formal implementation project to manage the transition to AIFRS including training of finance personnel, identification of the key impacts of AIFRS, quantification of the impacts on the opening balance sheet and determining the changes to accounting policies on adoption of AIFRS. At the date of this report, the project is on schedule and nearing completion.

Set out below are the key areas where accounting policies are expected to change on adoption of AIFRS and management's best estimate of the quantitative impact on the financial statements. The actual effects of transition of AIFRS may differ from the estimates being disclosed due to:

- ongoing work being undertaken by the AIFRS project team;
- new or revised standards or interpretations;
- additional guidance on the application of AIFRS to a particular industry or transaction; and
- emerging accepted practice in the interpretation and application of AIFRS and Urgent Issues Group Interpretations.

The application of AIFRS will have no material effect on the Group's strategy. The main areas of effect are accounting based measurement, recognition and disclosure requirements.

**(a) Reconciliation of net loss under AGAAP to that expected under AIFRS**

| | Note | 30 June 2005 $'000 |
|---|---|---|
| Net loss after tax benefit as reported under AGAAP | | (21,840) |
| Share based payments expense | (iii) | (606) |
| Goodwill amortisation written back | (ii) | 248 |
| Impairment write down | (ii) | (250) |
| Taxation expense impact of the above | (vi) | 182 |
| Total AIFRS adjustments | | (426) |
| **Net loss after tax under AIFRS** | | **(22,266)** |

**(b) Reconciliation of equity as presented under AGAAP to that expected under AIFRS**

| | Note | 30 June 2005 $'000 |
|---|---|---|
| Accumulated deficit as reported under AGAAP | | (11,277) |
| AIFRS adjustments as per Note (a) above | | (426) |
| AIFRS transition adjustments | | |
| Goodwill amortisation written back | (ii) | 37 |
| Recognition of share based payments expense | (iii) | (46) |
| Transfer asset revaluation reserve to retained earnings | (v) | 964 |
| Taxation expense impact of the above | (vi) | 14 |
| Total AIFRS transition adjustments | | 969 |
| Total AIFRS adjustments to accumulated deficit | | 543 |
| **Accumulated deficit under AIFRS** | | **(10,734)** |
| Other reserves as reported under AGAAP | | 964 |
| Transfer asset revaluation reserve to retained earnings | (v) | (964) |
| Equity compensation reserve | (iii) | 652 |
| Total AIFRS transition adjustments | | (312) |
| **Other reserves under AIFRS** | | **652** |

**(c) Restated balance sheet as at 30 June 2005**

| | Consolidated | | | Company | | |
|---|---|---|---|---|---|---|
| | AGAAP $'000 | IFRS financial adjustments $'000 | AIFRS $'000 | AGAAP $'000 | IFRS financial adjustments $'000 | AIFRS $'000 |
| Current assets | 30,056 | - | 30,056 | 1,723 | - | 1,723 |
| Non-current assets | 34,785 | 231[(1)] | 35,016 | 42,893 | 2,061[(ii)] | 44,954 |
| **Total assets** | **64,841** | **231** | **65,072** | **44,616** | **2,061** | **46,677** |
| Current liabilities | 28,836 | - | 28,236 | 672 | - | 672 |
| Non-current liabilities | 17,082 | - | 17,082 | 22,360 | - | 22,360 |
| **Total liabilities** | **45,918** | **-** | **45,918** | **23,032** | **-** | **23,032** |
| **Net assets** | **18,923** | **231** | **19,154** | **21,584** | **2,061** | **23,645** |
| Contributed equity | 29,236 | - | 29,236 | 29,236 | - | 29,236 |
| Reserves | 964 | (964) | - | 3,733 | (3,733) | - |
| Equity compensation reserve | - | 652 | 652 | - | - | - |
| (Accumulated deficit)/ retained earnings | (11,277) | 543 | (10,734) | (11,385) | 5,794 | (5,591) |
| **Total equity** | **18,923** | **231** | **19,154** | **21,584** | **2,061** | **23,645** |

(i) Comprises reversal of goodwill amortisation ($285,000) less goodwill impairment ($250,000) plus the deferred tax asset ($196,000) relating to share based payments.

(ii) Re-establishment of amounts due from subsidiaries based on reversal of goodwill amortisation.

**(d) Restated AIFRS statement of cash flows for the year ended 30 June 2005**

No material impacts are expected to the cash flows presented under AGAAP on adoption of AIFRS.

The key potential implications of the conversion to AIFRS on AJ Lucas Group effective 1 July 2004 including transitional elections in accordance with AASB 1 "First Time Adoption of Australian Equivalents to International Financial Reporting Standards" are as follows:

***(i) Business combinations***

As permitted under AASB 1, the classification and accounting treatment of business combinations that occurred before 1 July 2004 have not been restated in preparing the opening AIFRS balance sheet.

***(ii) Intangible assets***

*Goodwill*

Current AJ Lucas Group accounting policy is to amortise goodwill on a straight line basis over 20 years. Under AIFRS, goodwill is not subject to amortisation but must be tested for impairment annually. Goodwill amortisation amounting to $248,000 charged in 2004/05 and $37,000 as at transition date has been written back. The adjusted goodwill amount has been subject to an impairment test and written down by $250,000. This test has been performed at the appropriate cash generating unit (CGU) levels. In addition, goodwill amortisation in wholly-owned subsidiaries of $2,061,000 will be written back.

*Research and development*

Under AIFRS, expenditure on research activities will be expensed as incurred whereas the Group's current AGAAP policy allows for the capitalisation of research expenditure where future benefits are expect beyond reasonable doubt.

Under AIFRS, expenditure on development activities must be capitalised if the product or process is technically and commercially feasible and the consolidated entity has sufficient resources to complete the development. Capitalised development expenditure will be stated at cost less accumulated amortisation and impairment losses.

All research expenditure previously capitalised had been fully amortised at the transition date. Accordingly, no adjustment is required on the change to AIFRS either at the transition date or for the year ended 30 June 2005. Development costs are being reviewed against the recognition criteria and tested for impairment. No impairment losses are expected.

***(iii) Share based payments***

AJ Lucas Group provides equity based compensation to staff in the form of management rights over shares and shares issued under the Employee Share Acquisition Plan. Under AGAAP, no expense is recognised for the issue of these securities to employees. Under AIFRS, such securities must be recognised as an employee benefit expense based on the fair value of the instrument at grant date, and this amount will be recognised over the relevant period of service i.e. the vesting period.

In accordance with AASB 1, no retrospective adjustment has been made for management rights issued prior to 7 November 2002 which vested before 1 January 2005.

At 1 July 2004, retained earnings will be reduced by $46,000 and a corresponding equity compensation reserve will be created. For the financial year ended 30 June 2005, share based payments of $606,000 which were not recognised under AGAAP will be recognised as an expense under AIFRS with a corresponding increase in the equity compensation reserve. There is no effect on the consolidated entity's or Company's total equity.

***(iv) Revenue from ordinary activities***

Although not affecting the net profit of the Company or the consolidated entity, the adoption of AIFRS will result in a number of transactions being recorded on a "net" rather than a "gross" basis. In addition, the adoption of AIFRS results in the reclassification of proceeds from sale of non-current assets from revenue from ordinary activities to other income and expense items in the statement of financial performance.

As a consequence, revenue from ordinary activities for the financial year ended 30 June 2005 will decrease by $117,000 (Company: $nil), expenses will decrease by $1,002,000 (Company: nil) and the net loss on the sale of non-current assets of $885,000 will be separately disclosed in the statement of financial performance. No adjustments are required for the Company,

***(v) Plant and equipment***

Plant and equipment will be measured at cost under AIFRS. However, as permitted by the election available under AASB 1, at transition date certain items of plant and equipment are expected to be recognised at deemed cost, being a revalued amount prior to transition date that approximates the fair value as at the date of transition.

Any asset revaluation reserve balance relating to these assets will be derecognised at transition date and adjusted against retained earnings. Consequently, at 1 July 2004, an amount of $964,000 will be reclassified in the consolidated entity from asset revaluation reserve to retained earnings. As carrying amounts, depreciation rates and useful economic lives did not change in the financial year ended 30 June 2005, there is no effect on the income statement for this year under AIFRS.

***(vi) Income tax***

On transition to AIFRS, the income tax balances will be calculated based on the "balance sheet approach" replacing the "income statement approach" currently used under AGAAP. This method recognises deferred tax balances when there is a difference between the carrying value of an asset or liability for accounting purposes and its tax base. The impact on the consolidated entity as a result of this change in approach for the financial year ended 30 June 2005 is to increase earnings by $182,000 and deferred tax assets by an equivalent amount.

At 1 July 2004, the transition adjustments identified above result in taxation impacts that increase retained earnings and deferred tax assets by $14,000.

***(vii)Earnings per share***

Under AIFRS, basic and diluted earnings per share are calculated using the profit or loss from continuing operations attributable to the ordinary equity holders of the parent entity. The earnings per share for the financial year ended 30 June 2005 calculated on the AIFRS adjusted results are expected to be:

| | |
|---|---|
| Basic (loss) per share from continuing operations | (42.8) cents |
| Diluted (loss) per share from continuing operations | (42.8) cents |

## 33. EVENTS SUBSEQUENT TO BALANCE DATE

In September 2005, Molopo Australia Limited exercised its option to increase its participating interest in the Lucas Molopo Joint Venture from 14% to 30%.

For reporting periods beginning on or after 1 July 2005, the consolidated entity must comply with Australian equivalents to International Financial Reporting Standards (AIFRS) as issued by the Australian Accounting Standards Board. The implementation plan and potential impact of adopting AIFRS are detailed in Note 32.

As previously foreshadowed, the directors have provided for the Nerdlihc receivable of $13,596,000 as payment not received at the date of this report.

Other than these matters, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material or unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Group, the results of those operations, or the state of affairs of the Group, in future financial years.

# DIRECTORS' DECLARATION

1. In the opinion of the directors:

(a) the financial statements and notes, set out on pages 12 to 42, are in accordance with the Corporations Act 2001, including:

  (i) giving a true and fair view of the financial position of the Company and consolidated entity as at 30 June 2005 and of their performance, as represented by the results of their operations and cash flows, for the year ended on that date; and
  (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

2. The directors have been given the declarations required by Section 295A of the Corporations Act 2001 from the chief executive officer and chief financial officer for the year ended 30 June 2005.

Signed in accordance with a resolution of the directors:

Allan Campbell
Director
30 September 2005

# INDEPENDENT AUDIT REPORT

## INDEPENDENT AUDIT REPORT TO MEMBERS OF AJ LUCAS GROUP LIMITED

### Scope

**The financial report and directors' responsibility**
The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes 1 to 33 to the financial statements, and the directors' declaration set out on pages 12 to 43 for both AJ Lucas Group Limited ("the Company") and AJ Lucas Group Limited and its controlled entities ("the consolidated entity") for the year ended 30 June 2005. The consolidated entity comprises both the Company and the entities it controlled during the year.

The directors of the Company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Corporations Act 2001. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

**Audit approach**
We conducted an independent audit in order to express an opinion to the members of the Company. Our audit was conducted in accordance with Australian Auditing Standards in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001, Australian Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the Company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

### Audit opinion

In our opinion, the financial report of AJ Lucas Group Limited is in accordance with:

(a) the Corporations Act 2001, including:
  (i) giving a true & fair view of the Company's and consolidated entity's financial position as at 30 June 2005 and of their performance for the year ended on that date; and
  (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

(b) other mandatory financial reporting requirements in Australia.

KPMG
KPMG

Malcolm Kafer
Partner
Sydney,
30 September 2005

## SECURITY HOLDINGS (as at 31 August 2005)

### a) Distribution of security holders

| | Number of Security Holders | | |
|---|---|---|---|
| Securities held | Ordinary Shares | Rights | Redeemable convertible notes |
| 1 - 1,000 | 406 | - | - |
| 1,001 - 5,000 | 1,458 | 4 | - |
| 5,001 - 10,000 | 588 | 11 | - |
| 10,001 - 100,000 | 395 | 19 | - |
| 100,001 and over | 25 | 4 | 17 |
| Total | 2,872 | 38 | 17 |

53 shareholders held less than a marketable parcel of ordinary shares.

### b) Twenty largest shareholders

| Name | Number of Ordinary Shares held | % of Issued Shares |
|---|---|---|
| AJ Lucas Holdings Pty Limited | 13,990,000 | 27.15 |
| JP Morgan Nominees Australia Limited | 4,011,236 | 7.78 |
| ANZ Nominees Limited | 3,186,952 | 6.18 |
| National Nominees Limited | 2,930,592 | 5.69 |
| Amalgamated Dairies Limited | 2,090,000 | 4.06 |
| Forty Traders Limited | 1,538,001 | 2.98 |
| Citicorp Nominees Pty Ltd (CFSIL CWLTH BOFF Super A/C) | 967,376 | 1.88 |
| Gwynvill Trading Pty Ltd | 959,546 | 1.86 |
| Gwynvill Trading Pty Ltd | 367,400 | 0.71 |
| Westpac Custodian Nominees Limited | 308,100 | 0.60 |
| HSBC Custody Nominees (Australia) Limited | 300,000 | 0.58 |
| New Zealand Guardian Trust Company Limited | 290,950 | 0.56 |
| Maminda Pty Ltd | 250,000 | 0.49 |
| ASB Nominees Limited | 241,000 | 0.47 |
| Bruce Birnie Pty Ltd | 200,000 | 0.39 |
| Tricom Nominees Pty Limited (LPG A/C) | 200,000 | 0.39 |
| Kisantelle Pty Limited | 150,000 | 0.29 |
| Mr Alistair Peter Wright | 150,000 | 0.29 |
| Questor Financial Services Limited | 147,000 | 0.29 |
| Mr Alexander Stuart & Mrs Elizabeth Diane Stuart Ballabourneen Super Fund A/C | 138,000 | 0.27 |
| Total | 32,416,153 | 62.91 |

### c) Substantial shareholders

| Name | Number of Ordinary Shares held | % of Issued Shares |
|---|---|---|
| AJ Lucas Holdings Pty Limited | 17,490,000 | 33.91 |
| Acorn Capital Limited | 4,097,030 | 7.95 |
| Amalgamated Dairies Group | 3,728,001 | 7.23 |
| Challenger Financial Services Group | 2,877,923 | 5.59 |

### On-market buy back

There is no current on-market buy back.

### Unquoted equity securities

As at 31 August 2005, there were 1,601,333 rights over unissued ordinary shares in the Company.

***Redeemable convertible notes***

JP Morgan Nominees Australia Ltd holds 3,500,000 redeemable convertible notes representing 35% of the total number on issue.

***Restricted securities***

As at 31 August 2005, there were 48,450 shares issued under the Employee Share Acquisition Plan. These shares are not quoted and are restricted from sale until the earlier of the employee owning the relevant shares ceasing to be employed by the Group and 28 May 2007.

### Voting rights

***Ordinary shares***

Refer to Note 17.

***Redeemable convertible notes***

Refer to Note 17.

***Rights***

Refer to Note 29.

# DIRECTORY

**Company secretary**
Nicholas Swan MA, ACA, MBA, ASIA

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**Share registry**
Computershare Investor Services Pty Limited
Level 5, 115 Grenfell Street
ADELAIDE SA 5000
GPO Box 1903
ADELAIDE SA 5001
Enquiries within Australia: 1300 556 161
Enquiries outside Australia: +61 3 9615 5970
Email: web.queries@computershare.com.au
Website: www.computershare.com

**Stock exchange**
The Company is listed on the Australian Stock Exchange with the code 'AJL'. The Home Exchange is Sydney.

**Auditors**
KPMG
10 Shelley Street
Sydney NSW 2000

**Bankers**
ANZ Bank
67 Albert Street
Chatswood NSW 2067

**Quality certifiers (AS/NZS ISO 9001:2000)**
BVQI

**Australian business number**
12 060 309 104

**Other information**
AJ Lucas Group Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.

www.lucas.com.au

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