# Annual Financial Report

# Hydromet Corporation Limited
# and its controlled entities

## ABN 71 002 802 646

## 30 June 2004

## Offices and officers

**Principal registered office**
Lot 3 Five Islands Road
Unanderra NSW 2526

Telephone: 02 4271 1822
Facsimile: 02 4271 6151
**www.hydromet.com.au**

**Company Secretary**
Pipvide Tang

**Offices**
**Hydromet Corporation Limited**
**Hydromet Operations (Southern) Limited**
Lot 3 Five Islands Road
Unanderra NSW 2526

Telephone: 02 4271 1822
Facsimile: 02 4271 6151

**Hydromet Operations Limited**
**Tasmania operation**
Risdon Road
New Town TAS 7008

Telephone: 03 6278 9287
Facsimile: 03 6278 9320

**MinMet Operations Pty Limited**
25 School Drive
Tomago NSW 2322

Telephone: 02 4964 8266
Facsimile: 02 4966 5958

**Location of share registry**
*Sydney*
Computershare Investor Services Pty Limited
Level 3 60 Carrington Street
Sydney NSW 2000

Telephone: 02 8234 5000
Facsimile: 02 8216 5500
Investor enquiries: 02 8216 5700

**Stock Exchange**
The Company is listed on the Australian Stock Exchange. The Home Exchange is Sydney.

**Other information**
Hydromet Corporation Limited, incorporated and domiciled in Australia, is a publicly listed company limited by shares.

**Auditor**
KPMG
Level 3
63 Market Street
PO Box 866
Wollongong NSW 2500

**Hydromet Corporation Limited and its controlled entities**
**for the year ended 30 June 2004**

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**Hydromet Corporation Limited and its controlled entities**
**for the year ended 30 June 2004**

## Chairman's report

The Company managed to reduce the full year loss from that reported for the half year to December 2003 ($1,446,000) to $989,655 for the year ended June 2004. Whilst not returning to profits for the full 2004 year it is a substantial improvement compared to a loss of $4,452,966 in the previous year. The Company earned a profit of $456,345 for the second half of the financial year.

The moderate profit achieved in the second half of the year reflects the new era and what we believe is the beginning of sustainable profitability for Hydromet which is expected to continue for the future.

In this financial year, the Company was able to lay down a solid foundation for growth by achieving sustainable revenue improvements, winning new contracts and developing new projects. I am confident as a result of these outcomes the Company will be able to deliver profits for the year 2004/05 and onwards. A comprehensive review of the operations is contained in the Directors' Report.

At our Unanderra plant in NSW we have secured three major contracts to process a total quantity of up to 22,000 tonnes/year of Electric Arc Furnace dust from the three steel mini mills in Australia. Hydromet has emerged as the preferred establishment in Australia capable of processing these dusts. Zinc sulphate produced from this process is entering the market with a promising future. The Company is also investigating other value added zinc products from Electric Arc Furnace dust to enhance the profitability of the project. The Unanderra plant will now benefit from the combined revenue earned both from the treatment fees and sale of zinc sulphate products on a sustainable basis. Based on a process developed by Hydromet, we have commissioned a pilot plant to purify spent waste sulphuric acid generated by major oil refineries in Australia. Subject to the success of the pilot plant we will benefit from recycled acid by way of reduced cost of sulphuric acid which we consume in the EAF dust project currently in progress. Hydromet will endeavour to sign a long term contract with a major oil refinery to process up to 7,000 tonnes/year spent sulphuric acid at the Unanderra facility once the pilot work is completed. We are also at the final stage of obtaining the development consent from Wollongong City Council to convert the pilot project to a full scale commercial processing facility. This project is expected to generate further revenue for Unanderra from treatment fees and acid sales.

The Minmet Operations in Tomago NSW have also performed extremely well treating significant quantities of selenium precious metal bearing residues from overseas, producing 149 Mt of selenium product sold to the export market. Our state of the art selenium technology applied at Minmet is receiving worldwide recognition with international clients. Falconbridge has extended their contract for a further three years with potential to treat other wastes produced by Falconbridge as well. We have secured another selenium sludge processing contract with a major United States based copper producer on a long term basis. Our Tomago operation is conducting a plant trial for a Canadian nickel producer with the view to processing their selenium bearing residue. Following the recommendation from the reputation gained from our existing international clientele, we expect that other generators will be interested in Hydromet's services to treat similar residues. Over the past six months, we have witnessed a significant worldwide price increase for selenium with the price lifting from AUS$20,000 to AUS$60,000/tonne. We expect the selenium price will be maintained around the current level due to world demand and a shortage of selenium.

We successfully commenced the lead slag immobilisation project for Exide Technologies Ltd in Wellington, New Zealand The project has an initial revenue value of AUS$1 million. We expect this project will continue on a long-term basis, and are in the final stages of negotiating a contract to treat daily arisings from the smelter.

The Company commenced a mercury stabilisation project with Zinifex Ltd in Hobart and expects to continue this project on a long term basis.

## Hydromet Corporation Limited and its controlled entities
## for the year ended 30 June 2004

## Chairman's report (cont'd)

Following successful pilot plant trials on behalf of a major Western Australian mining company we entered into a heads of agreement to install an arsenic immobilisation plant for on their site.

Our proposal for a used lead acid battery crushing and recycling plant at Unanderra received development consent from Wollongong City Council in August 2004. The proposed process will offer a complete environmental recycling solution to the waste lead batteries generated in Australia. Furthermore, the Company will have the potential to become a major player in the used lead acid battery market producing clean upgraded lead feed for sale to secondary lead smelters in Australia and around the world.

Finally, we have entered into an option agreement with Conico Ltd in July 2004 for our Stanton (cobalt, nickel and copper) prospect. If the option agreement is exercised after due diligence work and the successful listing of Conico, Hydromet will receive $500,000 in cash and 12.5 million ordinary shares in Conico Ltd.

***Outlook for the Future***

As outlined in the report, the Company expects strong revenue streams to continue in the 2004/05 financial year. With this solid foundation our vision is to further develop as a leader in the environmental field, achieve expansion, revenue growth and profit through new contracts and projects.

I am very grateful to the staff and the management of Hydromet for their contribution and dedication. Finally, I am also thankful to the shareholders and other stakeholders including debenture and convertible note holders of the Company.

Dr Lakshman Jayaweera
*Chairman*

Dated this 27th day of August 2004

## Directors' report

The directors present their report together with the financial report of Hydromet Corporation Limited ("the Company") and of the consolidated entity, being the Company and its controlled entities, for the year ended 30 June 2004 and the auditor's report thereon.

## Directors

The directors of the Company at any time during or since the end of the financial year are:

| Name and qualifications | Experience and special responsibilities |
|---|---|
| Dr Lakshman D Jayaweera<br>MSc, PhD<br>Executive Chairperson | Dr Jayaweera is one of the founders and the head of the technical team of the Company. He holds a PhD in Chemical Engineering and has considerable experience in mineral processing and hazardous waste recycling.<br>Director since 1991- Deputy Chairman from September 2000 to January 2001 and appointed Chairman in January 2001. |
| Mr Gregory W Wrightson<br>Managing Director | Mr Wrightson has over 18 years experience in chemical manufacturing and was appointed General Manager of the Company in 1997.<br>Director since 1998 - appointed Managing Director in September 2000. |
| Mr Stephen H Kwan, MPhil, ATI, MBIM<br>Independent Non-Executive Director | Mr Kwan has over 26 years experience in metals and chemicals trading and is a co-founder of the Kee Shing Group in Hong Kong.<br>Member of the Audit and Remuneration Committee.<br>Director since 1991. |
| Mr Pipvide S Tang, MBA, CPA<br>Independent Non-Executive Director | Mr Tang has more than 25 years experience in accounting, financial management and corporate finance.<br>Chair of the Audit and Remuneration Committee from October 2001.<br>Director from 1991 to 1996 and since 1997. Mr Tang was an Executive Director until August 2000. |
| Mr Timothy R Allen<br>Independent Non-Executive Director | Mr Allen has extensive engineering and banking experience with qualifications in mining, engineering and economics and he is a member of the Securities Institute of Australia.<br>Director since October 2001. |
| Mr Stephen B Wolfe, MBA<br>Non-Executive Director | Mr. Wolfe has twenty years experience in the banking, resource, logistic, chemicals and raw materials industry.<br>Appointed director on 2 February 2004. |

## Directors' report (cont'd)

## Directors' meetings

The number of directors' meetings (including meetings of committee of directors) and number of meetings attended by each of the directors of the Company during the financial year are:

| | **Board meetings** | | **Audit and remuneration committee meetings** | |
|---|---|---|---|---|
| **Directors** | **Number eligible to attend** | **Number attended** | **Number eligible to attend** | **Number attended** |
| Mr SH Kwan | 7 | 5 | 2 | 2 |
| Mr GW Wrightson | 7 | 6 | - | - |
| Dr LD Jayaweera | 7 | 7 | - | - |
| Mr PS Tang | 7 | 7 | 2 | 2 |
| Mr TR Allen | 7 | 7 | - | - |
| Mr SB Wolfe | 5 | 5 | - | - |

## Corporate governance statement

This statement outlines the main Corporate Governance practices in place throughout the financial year which comply with the ASX Corporate Governance Council recommendations, unless otherwise stated.

### *Board of Directors*

#### Role of the board

The Board's primary role is the protection and enhancement of long-term shareholder value.

To fulfil this role, the Board is responsible for the overall corporate governance of the consolidated entity including formulating its strategic direction, approving and monitoring capital expenditure, setting remuneration, appointing, removing and creating succession policies for directors and senior executives, establishing and monitoring the achievement of management's goals and ensuring the integrity of internal control and management information systems. It is also responsible for approving and monitoring financial and other reporting.

The Board has delegated responsibility for operating and administration of the company to the Managing Director and the executive chairperson.

#### Board processes

To assist in the execution of its responsibilities, the Board has established an Audit and Remuneration Committee, which operates under a charter approved by the Board. The Board also established a business risk management process and the establishment of appropriate ethical standards.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

The full Board currently holds meetings every two months, plus any extraordinary meetings at such other times as necessary to address any specific matters that may arise.

The agenda for meetings is prepared in conjunction with the Chairman, Managing Director and Company Secretary. Standing items include the Managing Director's report, financial reports, strategic matters, governance and compliance. Submissions are circulated in advance. Operational management is regularly involved in board discussions and directors have other opportunities, including visits to business operations, for contact with a wider group of employees.

### Director education

The consolidated entity has a process to educate new directors about the nature of the business, current issues, the corporate strategy and the expectations of the consolidated entity concerning performance of directors. Directors also have the opportunity to visit consolidated entity facilities and meet with management to gain a better understanding of business operations. Directors are given access to continuing education opportunities to update and enhance their skills and knowledge.

### Independent professional advice and access to company information

Each director has the right access to all relevant company information and company employees and, subject to prior consultation with the Chairman, may seek independent professional advice from a suitable qualified adviser at the consolidated entity's expense. The director must consult with an advisor suitably qualified in the relevant field, and obtain the Chairman's approval of the fee payable for the advice before proceeding with the consultation. A copy of the advice received by the director is made available to all other members of the Board.

### Composition of the Board

The names of the directors of the Company in office at the date of this report are set out in the Directors' report on page 3 of this report.

The composition of the Board is reviewed by the Audit and Remuneration Committee to ensure that the Board has the appropriate mix of expertise and experience. When a vacancy exists, through whatever cause, or it is considered the Board could benefit from the services of a new director with particular skills, the committee will select a panel of candidates with the appropriate expertise and experience. The Board then appoints the most suitable candidate who must stand for election at the next general meeting of shareholders. At each annual general meeting of members one-third of the Board automatically retire by rotation and are eligible for re-appointment by the members.

The composition of the Board is determined using the following principles:

- A minimum of five directors, with a broad range of expertise.
- A majority of directors having extensive knowledge of the Company's industries, and those which do not, have extensive expertise in significant aspects of auditing and financial reporting, or risk management of large companies.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

- Enough directors to serve on committee without overburdening the directors or making it difficult for them to fully discharge their responsibilities.

- The roles of Chairperson and Managing Director are not exercised by the same director.

Due to the size of the Company, resources available and the specialized nature of the Company's business, the Company did not meet Corporate Governance Council recommendations in the following area:

- The board comprises three independent non-executive directors, one non-executive director and two executive directors. Non-executive directors do not play a role in the day to day management of the company.

- The Audit and Remuneration Committee is comprised of two independent non-executive directors and not the recommended three.

- An executive director is the Chairperson.

- No Nomination Committee has been established. The Audit & Remuneration Committee is responsible for the selection and nomination of new directors.

An independent director is a director who is not a member of management (a non-executive director) and who:

- Hold less than 5% of the voting shares of the Company and is not an officer of, or otherwise associated, directly or indirectly, with a shareholders of more than 5% of the voting shares of the Company.

- Has not within the last three years been employed in an executive capacity by the Company or another group member, or been a director after ceasing to hold any such employment.

- Within the last three years has not been a principal or employee of a material professional adviser or a material consultant to the Company or another group member.

- Is not a material supplier or customer of the Company or another group member, or an officer of or otherwise associated, directly or indirectly, with a material supplier or customer.

- Has no material contractual relationship with the Company or another group member other than as a director of the Company.

- Is free from any interest and any business or other relationship which could, or could reasonably by perceived to, materially interfere with the director's ability to act in the best interests of the Company.

The Board considers, 'material', in this context, where any director-related business relationship has represented, or is likely in the future to represent the lesser of at least 10% of the Company's or the director-related business's revenue. The Board considered the nature of relevant industries' competition, and the size and nature of each director-related business relationship, in arriving at this threshold.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

### *Audit and Remuneration Committee*

The Audit and Remuneration Committee has a documented charter, approved by the Board. All members must be non-executive directors with a majority being independent. The Chairperson may not be the Chairperson of the Board. The Committee advises on the establishment and maintenance of framework of internal control and appropriate ethical standards for the management of the consolidated entity, the remuneration of executives and directors and the composition of the Board.

The members of Audit and Remuneration Committee during the year were:

- Mr SH Kwan, Independent Non Executive Director; and
- Mr PS Tang, Independent Non Executive Director.

The Audit and Remuneration Committee is responsible for making recommendations to the Board on remuneration policies and packages applicable to the Board members and senior executives of the Company. The broad remuneration policy is to ensure the remuneration package properly reflects the person's duties and responsibilities and that remuneration is competitive in attracting, retaining and motivating people of the highest quality. Consideration is specifically made to the current operating situation and environment of the Company. Further details of the directors' remuneration, superannuation and retirement payments are set out in the Directors' Report and Note 28 of the financial statement.

The charter of the Audit and Remuneration Committee is available at the office of the Company.

The responsibilities of the Audit and Remuneration Committee also include:

- reviewing the annual, half-year financial reports and other financial information distributed externally. This includes approving new accounting policies to ensure compliance with Australian Accounting Standards and generally accepted accounting principles, and assessing whether the financial information is adequate for shareholder needs;
- assessing the adequacy of the internal control framework and the Company's code of ethical standards;
- to give the Board of Directors additional assurance regarding the quality and reliability of financial information prepared for use by the Board in determining policies or for inclusion in the financial report;
- assessing corporate risk assessment processes;
- monitoring the procedures to ensure compliance with the Corporation Act 2001 and the ASX Listing Rules and all other regulatory requirements;
- assessing whether non-audit services provided by the external auditor are consistent with maintaining the external auditor's independence. The external auditor provides an annual declaration of independence which is consistent with Professional Statement F.1 of the Code of Professional Conduct as recognised by Australia's professional accounting body; and
- reviewing the nomination and performance of the external auditor. The committee is responsible for ensuring that the audit partner rotation requirements are met and that the transition to the new partner is smooth and efficient.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

The Audit and Remuneration Committee reviews the performance of the external auditors on an annual basis and normally meets with them during the year as follows:

- to discuss the external audit plans, identifying any significant changes in structure, operations, internal controls or accounting policies likely to impact the financial statements and to review the fees proposed for the audit work to be performed;
- prior to announcement of results:
  - to review the half year and preliminary final report prior to lodgement with ASX, and any significant adjustments required as a result of the auditor's finding; and
  - to recommend Board approval of these documents.
- to finalise half-year and annual reporting:
  - review the results and findings of the auditor, the adequacy of accounting and financial controls, and to monitor the implementation of any recommendations made; and
  - review the draft financial report and recommend Board approval of the financial report;
- as required, to organise, review and report on any special reviews or investigations deemed necessary by the Board.

### *Remuneration report*

The Audit and Remuneration Committee reviews and makes recommendations to the Board on remuneration package and policies applicable to the Managing Director, Chairperson and other non-executive directors. It is also responsible for the share option scheme, superannuation entitlements, retirement and termination entitlements, fringe benefits policies and professional indemnity and liability insurance policies.

#### Remuneration policies

The broad remuneration policy is to ensure the remuneration package properly reflects the person's duties and responsibilities and that remuneration is competitive in attracting, retaining and motivating people of the highest quality. Consideration is specifically made to the current operating situation and environment of the Company. Remuneration packages include a mix of fixed remuneration and equity-based remuneration. The Company does not currently include performance linked bonus payments in its remuneration structures.

The remuneration structures explained below are designed to attract suitably qualified candidates, and to effect the broader outcome of increasing the consolidated entity's net profit attributable to members of the parent entity. The remuneration structures took into account:

- the overall level of remuneration for each director and executive; and
- the executives' ability to control performance.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

Non-executive directors' base fees are presently $25,000 per annum. The Chairperson and committee members receive no extra fees. Directors' fees cover all main board activities and membership of committee. Non-executive directors may receive additional payments for services required by the Company which are outside normal board and committee activities.

The Company has no schemes for retirement benefits, other than statutory superannuation, for directors.

**Directors' and senior executives' emoluments**

The Company has no senior executives who are not a director of the Company. Details of the nature and amount of each major element of the remuneration of each director of the Company are:

| | Base emolument $ | Non-cash benefits $ | Super contributions $ | Options issued (i) $ | Total $ |
|---|---|---|---|---|---|
| **Executive Directors** | | | | | |
| Mr GW Wrightson | 188,460 | 34,872 | 15,162 | - | 238,494 |
| Dr LD Jayaweera | 159,998 | 47,176 | 12,000 | - | 219,174 |
| **Non - Executive Directors** | | | | | |
| Mr SH Kwan | 25,000 | 13,225 | 2,250 | - | 40,475 |
| Mr PS Tang | 25,000 | 13,225 | 2,250 | - | 40,475 |
| Mr TR Allen | 25,000 | 13,225 | 4,979 | - | 43,204 |
| Mr SB Wolfe | 10,417 | 4,935 | 938 | - | 16,290 |

(i) 2,000,000 options were issued to each of Mr. G Wrightson, Dr. L Jayaweera, Mr. S Kwan, Mr. P Tang and Mr. T Allen on 19 December 2002 of which 500,000 out of the 2,000,000 options were vested and exercisable at the reporting date. The options were independently valued at a fair value of $Nil at the date of grant using Black-Scholes Option Pricing model.

The following factors and assumptions were used in determining the fair value of options on grant date:

| Grant date | Expiry date | Fair value per option | Exercise price | Price of shares on grant date | Estimated volatility | Risk free interest rate | Dividend yield |
|---|---|---|---|---|---|---|---|
| 19 December 2002 | 31 March 2007 | $Nil | $0.08 | $0.047 | 7.31% | 4.79% | N/A |

Estimated volatility approximates historic volatility. Each option entitles the holder to purchase one ordinary share in the Company. 2,500,000 options are exercisable after 31 December 2003, 2,500,000 after 31 December 2004; 2,500,000 after 31 December 2005 and 2,500,000 after 31 December 2006. All these options expire on 31 March 2007.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

### Options

During or since the end of the financial year, the Company granted 5,315,000 options for no consideration over unissued ordinary shares of the Company to 30 eligible employees under the Hydromet Employee Share Option Plan. None of these options were issued to the Directors. The options have an 8 cents exercise price and cannot be exercised before 16 February 2005 and have an expiry date of 16 February 2007.

### Unissued shares under option

At the date of this report unissued ordinary shares of the Company under option are:

| Expiry date | Exercise price | Number of options |
|---|---|---|
| 31 March 2007 | $0.08 | 10,000,000 |
| 16 February 2007 | $0.08 | 5,315,000 |

During or since the end of the financial year, the Company has not issued ordinary shares as a result of the exercise of options.

These options do not entitle the holder to participate in any share issue of the Company or any other body corporate.

### *Risk management*

**Oversight of the risk management system**

The Board oversees the establishment, implementation and annual review of the Company's risk management program. Management has established and implemented the risk management program for assessing, monitoring and managing operational, financial reporting and compliance risks for the consolidated entity. The Managing Director has declared that the financial reporting risk management and associated compliance and controls have been assessed and found to be operating efficiently and effectively. The operational and other compliance risk management have also been assessed and found to be operating efficiently and effectively. All risk assessments covered the whole financial year and the period up to the signing of the annual financial report for all material operations in the consolidated entity.

**Risk profile**

The Board reviews regularly the status of risks through integrated risk management programs aimed at ensuring risks are identified, assessed and appropriately managed. Major risks arise from such matters as action by customers, competitors, government policy changes, environment, occupational health and safety, the impact of exchange rate and product price movements, difficulties in sourcing feed materials, and problems in the development of technical processes. The Company has not established a formal risk management policy and internal compliance and control system. It is expected that the policy and the system will be established in the next six months.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

### Risk management and compliance and control

The Board is responsible for the overall internal control framework, but recognises that no cost effective internal control system will preclude all errors and irregularities. The system is based upon written procedures, policies and guidelines, organisational structures that provide an appropriate division of responsibility and the careful selection and training of qualified personnel.

In this regard, the Company has an Environmental Policy Statement, Occupational Health and Safety Policy Statement and Quality Policy Statement which set out the standards in accordance with which each director, officer and employee of the Company is expected to act. The requirement to comply with these policies is communicated to all employees. The statements are available at the office of the Company.

Comprehensive practices have been established to ensure:

- Capital expenditure and revenue commitments above a certain size obtain prior Board approval.
- Financial exposures are controlled, including the use of derivatives.
- Occupational health and safety standards and management systems are monitored and reviewed to achieve high standards of performance and compliance with regulations.
- Business transactions are properly authorised and executed.
- The quality and integrity of personnel.
- Financial reporting accuracy and compliance with the financial reporting regulatory framework.
- Environmental regulation compliance.

### Financial reporting

The Managing Director has declared, in writing to the board that the Company's financial reports are founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board.

Monthly actual results are reported against budgets approved by the directors and revised forecasts for the year are prepared regularly.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

### *Environmental regulation*

The Company acknowledges the importance of its environmental obligations and employs effective systems and procedures to protect those interests and to minimise risk to employees, the community and the environment.

All operating sites of the consolidated entity are subject to licence requirements issued under the Protection of the Environment Operations Act 1997 (POEO Act ).

The Consolidated Entity's business of processing industrial residues and manufacturing chemical products include treatment processes, immobilisation of by products, disposal of effluent streams and transportation of materials that are subject to specific approvals from and close scrutiny by the Commonwealth and State Department of Environment and Conservation.

Site managers are responsible for management and monitoring of compliance with the various licences, environmental regulations and specific requirements of site environmental licence conditions under which the facilities operate. Site managers report environmental performance to the Managing Director on a monthly basis who then reports to the Board. Performance against the licence conditions are reported to the Managing Director, Board of Directors and various state regulators on an annual basis and were substantially achieved across all operations. There has been no material non – compliance in relation to these licences' requirements during the financial year.

The Company is currently reviewing existing environmental systems and procedures with the objective of upgrading these via the implementation of an Environmental Management System, which will integrate with the Safety Management System and will apply uniformly across the group, including processing facilities in New Zealand.

The POEO Act remains under review by the NSW Department of Environment and Conservation (DEC) and will lead to further changes to regulations and group a number of regulations under the one Act.

Hydromet is committed to seeking improvement in environmental management and awareness of its employees to ensure continuing compliance with its obligations.

### Occupational Health and Safety

As with environmental matters Hydromet is acutely conscious of its health and safety obligations to its workforce who by the very nature of our industry are exposed to a range of chemicals and hazardous materials in carrying out their work.

Occupational health and safety issues are governed by the OHS Regulation 2001 in New South Wales and monitored by Workcover Authority.

Significant advancement has been made with the implementation of an integrated Safety Management System during the financial year. System implementation and training of managers and operations personnel is a continuous process to ensure a duty of care philosophy is adopted across the group.

We are pleased to report that there were no serious injuries or lost time incidents during the financial year.

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

### *Ethical standards*

All directors, managers and employees are expected to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of the consolidated entity. Every employee has a nominated supervisor to whom they may refer any issues arising from their employment. The board reviews the Ethical Standards policy regularly and processes are in place to promote and communicate these policies. The policy is available at the office of the Company.

#### Conflict of interest

Directors must keep the Board advised, on an ongoing basis, of any interest that could potentially conflict with those of the company. The Board has developed procedures to assist directors to disclose potential conflicts of interest.

Where the Board believes that a significant conflict exists for a director on a Board matter, the director concerned does not receive the relevant board papers and is not present at the meeting whilst the item is considered. Details of director related entity transactions with the company and consolidated entity are set out in Note 28.

#### Code of conduct

The consolidated entity has advised each director, manager and employee that they must comply with the Ethical Standards Policy. The policy is available to be viewed in the office of the company, and it covers the following:

- aligning the behaviour of the board and management with the code of conduct by maintaining appropriate core company values and objective;
- fulfilling responsibilities to shareholders by delivering shareholder value;
- usefulness of financial information by maintaining appropriate accounting policies and practices and disclosure;
- fulfilling responsibilities to customers by maintaining high standards of product quality, service standards, commitments to fair value, and safety of goods produced;
- employment practice such as occupational health and safety, employment opportunity, the level and structure of remuneration, and conflict resolution;
- responsibilities to the community, such as environmental protection policies, supporting the community activities and sponsorships and donations;
- responsibilities to the individual, such as privacy, use of privileged or confidential information, and conflict resolution;
- conflicts of interest;

## Directors' report (cont'd)

## Corporate governance statement (cont'd)

- corporate opportunities such as preventing directors and key management member from taking advantage of property, information or position for personal gain;
- confidentiality of corporate information;
- fair dealing;
- protection and proper use of the Company's assets;
- compliance with law; and
- reporting of unethical behaviour.

**Trading in general company securities by director and employees**

Directors may acquire shares in the Company, but are prohibited from dealing in Company shares or exercising options:

- except between three and 30 days after either the release of the Company's half-year and annual results to the Australian Stock Exchange ("ASX"), the annual general meeting or any major announcement; and
- whilst in possession of price sensitive information.

### *Communication with shareholders*

The Board provides shareholders with information which includes matters that may have a material effect on the price of the company's securities, notifying them to the ASX and issuing media releases.

In summary, the process operates as follows:

- The Managing Director and the Company Secretary are responsible for interpreting the company's policy and where necessary informing the Board. The Company Secretary is responsible for all communications with the ASX. Such matters are advised to the ASX on the day they are discovered.
- The full annual financial report is available to all shareholders.
- The half-yearly report contains summarised financial information and a review of the operations of the consolidated entity during the period. The half-year reviewed financial report is lodged with the Australian Securities and Investments Commission and the ASX, and sent to any shareholder who requests it.
- Proposed major changes in the consolidated entity which may impact on share ownership rights are submitted to a vote of shareholders.
- The external auditor is requested to attend the annual general meetings to answer any questions concerning the audit and the content of the auditor's report.

## Directors' report (cont'd)

The Board encourages full participation of shareholders at the Annual General Meeting to ensure a high level of accountability and identification with the consolidated entity's strategy and goals. Important issues are presented to the shareholders as single resolutions.

The shareholders are requested to vote on the appointment of directors, the granting of options and shares to directors and change of the Constitution. Copies of the Constitution are available to any shareholder who requests it.

## Principal activities

The principal activities of the consolidated entity during the course of the financial year were:

- the processing of industrial residues and the manufacture of value added products therefrom;
- the manufacture of chemicals and resource recovery; and
- the development of environmental, remediation and mineral processing technologies.

There were no significant changes in the nature of the activities of the consolidated entity during the year.

## Review and results of operations

### *Company overview*

The consolidated loss from ordinary operations for the year attributable to members of the Company was $989,655 (2003: loss $4,452,966). The loss of $1,446,000 in the first half of the financial year was reduced by the profit of $456,345 earned in the second half.

The 2004 financial year produced solid sustainable progress in both revenue improvement and project development. The profit earned in the six months to June 2004 indicates continued growth and profit into the 2005 financial year and onwards.

With additional EAF dust contracts with Comsteel and Smorgon Steel signed for our Unanderra plant and expected continuing strong selenium pricing, we are confident of positive performance in the year ending June 2005.

Key achievements realised during the year included:

- Completion of a 9,300 tonne waste immobilisation project for Port Kembla Copper Pty Limited which commenced in October 2003 and concluded in June 2004, generating $2.05 million in revenue for the year.
- Commencement of a 4,000 tonne lead slag immobilisation project in September 2003 on behalf of Exide Technologies in Wellington New Zealand, generating $1.0 Million in revenue for the year.
- Completion of an onsite immobilisation project for Australian Magnesium in Queensland in November 2003.
- Completion of a pilot plant trial on behalf of two Western Australian gold miners to immobilise arsenic waste.
- Signed a four year EAF dust treatment contract with Smorgon Steel in May 2004 covering up to 15,000 tonnes per annum of dust from its Comsteel Newcastle and Laverton Victoria steel mills.

## Directors' report (cont'd)

## Review and results of operations (cont'd)

- Record production of selenium recovered from smelter residues.
- Signed a three year agreement with Falconbridge Norway for up to 100 tonnes per annum of selenium bearing residue to support our highly profitable selenium recovery process at our Newcastle plant.
- Conducted successful trial recovery processing of selenium bearing residue for a US based copper smelter and are negotiating a long term agreement for ongoing feed for the Newcastle plant.
- Commissioned a waste acid recovery pilot plant at our Unanderra NSW plant in February 2004.
- Prepared and lodged an Environment Impact Statement (EIS) with both EPA and Wollongong Council in support of our development application for a used lead acid battery crushing and recycling operation at our Unanderra facility. Approval was granted during August 2004.
- Prepared and lodged a Statement of Environmental Effects (SEE) for our waste acid recovery project, currently under an AusIndustry Grant, at the Unanderra facility. Approval was granted during August 2004.
- Commencement of a mercury immobilisation project at our Hobart Tasmania plant on behalf of Zinifex Limited.
- Commencement of Zinc Sulphate production at Unanderra in April 2004.
- Development work undertaken to produce other zinc based products to optimise zinc recovery from the EAF dust.
- In July 2004 concluded an option agreement to sell the Stanton Prospect (Cobalt reserve) in the Northern Territory.
- Continued to gain specific immobilisation approvals from New South Wales Department of Environment and Conservation (formerly known as Environment Protection Authority).
- Entered into a strategic alliance with Tennant (2000) Pty Limited in November 2003. Tennant, a highly respected chemical trading company subscribed for $1 Million convertible notes issued by the Company.
- The issue of $1.1 Million in Debentures.

Total revenue earned for the year was $9.7 Million and represented an increase of 104% over 2003.

## Hydromet Corporation Limited and its controlled entities
## for the year ended 30 June 2004

## Directors' report (cont'd)

## Review and results of operations (cont'd)

The consolidated entity's business elements and relevant revenue contributions for the year included:

| | 2004 | | 2003 | |
|---|---|---|---|---|
| | $'000 | % | $'000 | % |
| Treatment fees earned | 6,257 | 64.5 | 3,154 | 66.3 |
| Finished product sales | 3,207 | 33.1 | 1,261 | 26.5 |
| Total operating revenue | 9,464 | 97.6 | 4,415 | 92.8 |
| Research grant | 112 | 1.2 | - | - |
| Other incomes | 121 | 1.2 | 342 | 7.2 |
| Total revenue | 9,697 | 100.0 | 4,757 | 100.0 |

Contribution of revenue from individual sites was as follows:

| | 2004 | | 2003 | |
|---|---|---|---|---|
| | $'000 | % | $'000 | % |
| Unanderra | 4,417 | 45.5 | 1,697 | 35.7 |
| Minmet | 3,766 | 38.8 | 2,523 | 53.0 |
| Tasmania | 38 | 0.4 | 360 | 7.6 |
| Exide – New Zealand | 1,192 | 12.3 | - | - |
| Australian Magnesium | 132 | 1.4 | - | - |
| Corporate | 152 | 1.6 | 177 | 3.7 |
| | 9,697 | 100.0 | 4,757 | 100.0 |

### *Significant changes in the state of affairs*

During the year the consolidated entity issued $1,100,000 (2003: $700,000) debentures to several holders. The face value of each debenture is $1. The debentures have a term of three years from the date of issue, and attract an interest rate of 12% per annum, to be paid in arrears, semi-annually on 31 March and 30 September, respectively. The debenture holders have a fixed and floating charge over the assets of the Company and its controlled entities.

1,000,000 convertible notes (2003: nil) were issued on 19 December 2003 and have a face value of $1 each. Within 365 days from the date of issue, the notes can be converted into ordinary shares of the Company at the conversion rate of $0.04 per ordinary share. The notes can also be converted into ordinary shares of the Company during the second 365 days from date of issue. The conversion rate during this period is $0.043 per ordinary share. The unconverted notes will be redeemed 912 days after the issue date.

Other then the matters above, in the opinion of the Directors there were no significant changes in the state of affairs of the consolidated entity that occurred during the financial year under review.

## Directors' report (cont'd)

## Review and results of operations (cont'd)

### *Review of principal businesses*

### Hydromet Operations (Southern) Limited – Unanderra NSW.

- Treated 19,352 tonnes of wastes including Onesteel and Comsteel electric arc furnace dusts, Port Kembla Copper water treatment sludge, and tin sludge.
- Commenced the waste acid recycling pilot plant project.
- Signed a four year agreement with Smorgon Steel to receive up to 15,000 tonnes per annum of electric arc furnace (EAF) dust for zinc recovery.
- Conducted development work on zinc product alternatives to utilise the zinc contained in the EAF dust residues processed.
- Obtained council and EPA approval for a used lead acid battery crushing and recycling process at the site.
- Obtained council and EPA approval for a waste acid recycling process.

**Minmet Operations Pty Limited –Tomago NSW.**

- Processed 294 tonnes of precious metal/selenium bearing smelter residue from Norway and the United States recovering 144 tonnes of high grade selenium which was sold to customers in the United Kingdom, China and the Philippines. Copper sulphate solution (approximately 200 tonnes) also recovered from the selenium process was sold to the mining industry.
- Improved selenium output was achieved over the year with a three year agreement reached with Falconbridge to secure up to 100 tonnes per annum of selenium bearing residue from their smelter in Kristiansand Norway.
- Finalised an ongoing agreement with a US copper smelter to supply selenium bearing residue for upgrade at Minmet.
- Selenium pricing escalated over the year taking the price from $20 per kg to $60 per kg in June 2004. It is expected the price will remain strong for the next 12 to 24 months. Demand is being fuelled by China's increased requirement for building and industrial applications. Selenium is used in metal alloys, glass manufacture and agricultural applications.

**Hydromet Operations limited – Hobart Tasmania**.

- Commenced the Mercury immobilisation project in January 2004. Delays in landfill disposal preparation which was outside our control have prevented continuous processing to date. This is expected to be rectified in the December quarter of 2004.
- The Cobalt recovery process proposal was not taken up by Zinifex limited.

## Directors' report (cont'd)

## Review and results of operations (cont'd)

**Stanton Project – Northern Territory.**

- Negotiated an option agreement to sell Stanton Prospect in July 2004.
- The option agreement enables the purchaser, Conico Limited to conduct due diligence in preparation for listing and will remain in force until July 2005.
- Hydromet will receive \$500,000 in cash and 12.5 Million ordinary shares (\$0.20 each) in the purchaser, subject to the option agreement being exercised, and successful listing of the purchaser on the ASX after its due diligence work on the Stanton Prospect.
- As part of the agreement, Hydromet has the right to enter into an off take agreement with the purchaser allowing first right of refusal to purchase its mine cobalt concentrates. This would allow Hydromet to establish a long-term sustainable cobalt chemical business at the company's Minmet operation in Tomago, NSW.
- On completion of the sale, Hydromet intends to distribute some or all of the purchaser's shares to existing Hydromet shareholders in the form of a dividend paid on a pro rata basis, subject to approval from the ASX.

**Exide Project – Wellington New Zealand.**

- The lead slag immobilisation project commenced in September 2004 with a small purpose built plant on the Exide smelter site. The project involves the treatment of an estimated 4,000 tonne stockpile at the smelter.
- Full scale processing began in January 2004 with 2,714 tonnes treated to June 2004.
- The stockpile processing is expected to be completed by September 2004.
- Negotiations are underway for Hydromet to continue processing the smelter arising once the stockpile processing is completed.

## Other operations

Ongoing research and development work led to a number of prospective and completed projects during the year which including:

- Further enhancement of our selenium recovery process at Minmet to produce a higher quality product capable of increasing revenue by up to 50%. We expect to produce the upgraded selenium in the December quarter 2004.
- A small immobilisation project carried in November 2004 onsite at Australian Magnesium in Queensland.
- Trial immobilisation of Arsenic wastes on behalf of two gold mining operations in Western Australia.
- Immobilisation of catalyst waste on behalf of an oil refiner.

## Directors' report (cont'd)

## Review of operations (cont'd)

With achievements outlined above and projects under negotiation we are making strong progress to increased turnover and profit potential. The progress is pleasing and rewarding with recognition of our capabilities across a range of industrial companies around Australia and overseas. We expect strong performance in next financial year with contribution from continued selenium sales, increased quantity throughput of EAF dust at Unanderra and ongoing processing of lead slag in New Zealand. Prospects for arsenic trioxide immobilisation in Western Australia are also promising with expected commencement in the June quarter of 2005.

## Dividends

There were no dividends paid or declared by the Company to members since the end of the previous financial year.

## Events subsequent to reporting date

The Company signed an Option Agreement with Conico Limited on 20 July 2004 for the potential sale of Hydromet's Stanton prospect cobalt mine lease situated in the Gulf of Carpentaria in the Northern Territory.

The option agreement which remains in place until July 2005 will enable Conico Limited to conduct required due diligence obligations in assessing the lease for an intended listing by the company. Conico will pay Hydromet an option fee of $20,000 per every four month period of the option.

Hydromet will receive $500,000 in cash and 12.5 Million ordinary shares ($0.20 each) in the new listed entity, subject to the option agreement being exercised, and successful listing of the purchaser on the ASX after its due diligence work on the Stanton Prospect.

As part of the agreement, Hydromet has the right to enter into an off take agreement with the purchaser allowing first right of refusal to purchase its mine cobalt concentrates. This would allow Hydromet to establish a long-term sustainable cobalt chemical business at the company's Minmet operation in Tomago, NSW.

On completion of the sale, Hydromet intends to distribute some or all of the purchaser's shares to existing Hydromet shareholders in the form of a dividend paid on a pro rata basis, subject to approval from the ASX.

The Government has announced that it plans to amend the tax consolidation legislation. Details of the proposal changes are not yet available. The effect of any change will be brought to account when the legislation is substantively enacted and the entity can assess the impact.

For financial years starting on or after 1 July 2005, the consolidated entity must comply with International Financial Reporting Standards (IFRS) as issued by the Australian Accounting Standards Board. At balance date, it was not possible to quantify the effect of the convergence to IFRS as key IASs and AASBs are currently under development.

Other than matters discussed above, 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 and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity, in the future financial years.

## Directors' report (cont'd)

## Likely developments

With strong long term contracts in place across the electric arc furnace dust project, ongoing immobilisation projects and other new opportunities the potential for Hydromet's turnover to grow strongly in 2005 is expected.

Further enhancement of our selenium recovery process in the December quarter of 2004 should see increases in sales revenue and profit on the project.

The waste acid recycling research and development project underway at Unanderra is important to the zinc sulphate business in that the acid recovered will be used to extract the zinc from the EAF dust substituting the high cost acid currently used. The acid saving would be substantial and combined with the treatment fee receivable for waste acid processing could improve savings and revenue by up to $2.1 Million per year. This will be confirmed at the completion of our pilot trial programme and would come into effect in the 2006 financial year.

The used lead acid battery project will be progressed during the 2005 financial year to confirm process details, customer commitment, capital funding and timing for entry to this unique recycling process developed by Hydromet. We will utilise a chemical process to recover lead waste from the crushing and separation stage to produce an attractive feed for a secondary lead smelter. We expect to finalise details on this project by December 2004.

Although lead times on prospective projects remains long, often in excess of 1 to 1.5 years, we are confident that with sufficient prospects in progress we will always be in a position to bring new business to the group and expand accordingly.

## Directors' interests

The relevant interest of each director in the shares issued by the Company, as notified by the directors to the Australian Stock Exchange in accordance with S205G(1) of the Corporations Act 2001, at the date of this report is as follows:

| | Hydromet Corporation Limited | | |
|---|---|---|---|
| **Directors** | **Options over ordinary shares** | **Ordinary shares** | **Redeemable convertible notes (i)** |
| Mr TR Allen | 2,000,000 | 2,300,000 | - |
| Dr LD Jayaweera | 2,000,000 | 13,608,250 | - |
| Mr SH Kwan | 2,000,000 | 46,000 | - |
| Mr PS Tang | 2,000,000 | 80,000 | - |
| Mr GW Wrightson | 2,000,000 | 578,300 | - |
| Mr SB Wolfe | - | - | 1,000,000 |

(i) Detail of redeemable convertible notes is set out on note 28(d).

## Directors' report (cont'd)

### Indemnification and insurance of officers

Since the end of the previous financial year the Company has paid insurance premiums in respect of directors' and officers' liability and legal expenses insurance contracts, for current and former directors and officers, including executive officers of the Company and Directors, executive officers and secretaries of its controlled entities. The insurance premiums relate to:

- costs and expenses incurred by the relevant officers in defending proceedings, whether civil or criminal and whatever their outcome; and
- other liabilities that may arise from their position, with the exception of conduct involving a wilful breach of duty or improper use of information or position to gain a personal advantage.

The Directors have not included details of amount of the premium paid in respect of the directors' and officers' liability and legal expenses insurance contracts, as such disclosure is prohibited under the terms of the contracts.

Other than the insurance matter discussed above, the Company has not, during or since the financial year, in respect of any person who is or has been an officer of the Company or a related body corporate indemnified or made any relevant agreement for indemnifying against a liability incurred as an officer, including costs and expenses in successfully defending legal proceedings.

Signed in accordance with a resolution of the Directors:

Dr Lakshman Jayaweera
*Chairman*

Dated at Wollongong this 27th day of August 2004.

## Hydromet Corporation Limited and its controlled entities

## Statements of financial performance
## for the year ended 30 June 2004

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| Revenue from rendering of services | | 6,257,493 | 3,153,927 | 1,323,463 | - |
| Revenue from sale of goods | | 3,207,166 | 1,260,928 | - | - |
| Other revenues from ordinary activities | | 231,977 | 342,187 | 158,733 | 171,168 |
| Total revenue from ordinary activities | 2 | 9,696,636 | 4,757,042 | 1,482,196 | 171,168 |
| Raw materials and consumables used | | (1,291,196) | (1,422,668) | (218,542) | - |
| Direct production costs | | (3,589,579) | (2,031,780) | (732,873) | - |
| Employee expenses | | (2,897,468) | (2,929,188) | (911,224) | (1,109,374) |
| Depreciation and amortisation expenses | 3 | (1,491,990) | (1,352,153) | (51,075) | (35,002) |
| Write back/(diminution) of intercompany loans and investments | | - | - | 627,750 | (3,248,864) |
| Borrowing costs | 3 | (259,691) | (64,313) | (66,116) | (24,213) |
| Consultants and professional services | | (220,464) | (304,387) | (157,386) | (267,070) |
| Insurance expenses | | (202,139) | (225,254) | (86,589) | (143,519) |
| Property rental and site costs | | (30,480) | (407,720) | (15,304) | (28,975) |
| Other expenses from ordinary activities | | (670,102) | (472,545) | (345,003) | (319,637) |
| Total expenses | | (10,653,109) | (9,210,008) | (1,956,362) | (5,176,654) |
| Loss from ordinary activities before related income tax expense | 3 | (956,473) | (4,452,966) | (474,166) | (5,005,486) |
| Income tax expense relating to ordinary activities | 5(a) | (33,182) | - | (33,182) | - |
| Net loss attributable to members of the parent entity | | (989,655) | (4,452,966) | (507,348) | (5,005,486) |
| Net increase in accumulated losses on initial adoption of revised AASB 1028 "Employee Benefits" | | - | (13,000) | - | - |
| Total changes in equity from non-owner related transactions attributable to members of the parent entity | | (989,655) | (4,465,966) | (507,348) | (5,005,486) |
| Basic and diluted (loss) per ordinary share | 7 | (0.37) cents | (1.651) cents | | |

The statements of financial performance are to be read in conjunction with the notes to the financial statements set out on pages 26 to 69.

## Hydromet Corporation Limited and its controlled entities

## Statements of financial position
## as at 30 June 2004

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| **Current assets** | | | | | |
| Cash assets | 8 | 1,262,046 | 1,261,173 | 708,073 | 1,027,780 |
| Receivables | 9 | 3,315,141 | 1,368,666 | 1,020,522 | 21,964 |
| Inventories | 11 | 200,187 | 334,808 | 4,309 | - |
| **Total current assets** | | 4,777,374 | 2,964,647 | 1,732,904 | 1,049,744 |
| **Non-current assets** | | | | | |
| Receivables | 9 | - | - | 7,022,654 | 7,449,027 |
| Other financial assets | 10 | - | - | 3,525,019 | 1,413,538 |
| Property, plant and equipment | 12 | 8,363,390 | 9,139,713 | 263,397 | 199,427 |
| Exploration, evaluation and development expenditure | 13 | 302,199 | 302,199 | - | - |
| Intangible assets | 14 | 663,390 | 908,034 | - | - |
| **Total non-current assets** | | 9,328,979 | 10,349,946 | 10,811,070 | 9,061,992 |
| **Total assets** | | 14,106,353 | 13,314,593 | 12,543,974 | 10,111,736 |
| **Current liabilities** | | | | | |
| Payables | 15 | 1,698,346 | 1,581,487 | 572,823 | 84,510 |
| Interest-bearing liabilities | 16 | 72,801 | 74,384 | 60,476 | 63,544 |
| Provisions | 17 | 903,111 | 1,302,321 | 165,205 | 261,979 |
| **Total current liabilities** | | 2,674,258 | 2,958,192 | 798,504 | 410,033 |
| **Non-current liabilities** | | | | | |
| Interest-bearing liabilities | 16 | 2,680,623 | 855,536 | 854,857 | 117,446 |
| Provisions | 17 | 678,563 | 638,301 | 61,632 | 46,188 |
| Loans from controlled entities | 29(b) | - | - | 6,047,769 | 4,449,509 |
| **Total non-current liabilities** | | 3,359,186 | 1,493,837 | 6,964,258 | 4,613,143 |
| **Total liabilities** | | 6,033,444 | 4,452,029 | 7,762,762 | 5,023,176 |
| **Net assets** | | 8,072,909 | 8,862,564 | 4,781,212 | 5,088,560 |
| **Equity** | | | | | |
| Contributed equity | 18 | 63,200,126 | 63,000,126 | 63,200,126 | 63,000,126 |
| Reserves | 19 | 505,688 | 505,688 | 150,000 | 150,000 |
| Accumulated losses | 20 | (55,632,905) | (54,643,250) | (58,568,914) | (58,061,566) |
| **Total equity** | | 8,072,909 | 8,862,564 | 4,781,212 | 5,088,560 |

The statements of financial position are to be read in conjunction with the notes to the financial statements set out on pages 26 to 69.

**Hydromet Corporation Limited and its controlled entities**

**Statements of cash flows**
**for the year ended 30 June 2004**

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| **Cash flows from operating activities** | | | | | |
| Cash receipts in the course of operations | | 7,674,869 | 4,996,723 | 443,891 | 30 |
| Cash payments in the course of operations | | (8,895,313) | (8,771,189) | (2,056,004) | (1,748,905) |
| Interest received | | 54,688 | 151,598 | 39,747 | 142,665 |
| Borrowing costs paid | | (243,757) | (52,209) | (55,868) | (24,213) |
| **Net cash used in operating activities** | 31(b) | (1,409,513) | (3,675,077) | (1,628,234) | (1,630,423) |
| **Cash flows from investing activities** | | | | | |
| Proceeds (to)/from loans to controlled entities | | - | - | 540,902 | (3,357,226) |
| Proceeds from sale of non-current assets | | - | 49,878 | - | 28,473 |
| Payments for property, plant and equipment | | (546,133) | (2,326,600) | (117,637) | (157,818) |
| **Net cash (used in)/provided by investing activities** | | (546,133) | (2,276,722) | 423,265 | (3,486,571) |
| **Cash flows from financing activities** | | | | | |
| Lease payments | | (66,985) | (102,302) | (49,081) | (34,494) |
| Proceeds from share placements | | - | 53,206 | - | 53,206 |
| Proceeds from borrowings: | | | | | |
| Convertible notes | | 1,000,000 | - | 1,000,000 | - |
| Debentures | | 1,100,000 | 700,000 | - | - |
| Other | | - | 188,728 | | 143,880 |
| Repayment of borrowings | | (76,496) | - | (65,657) | - |
| Dividends Paid | | - | (403,441) | - | (403,441) |
| **Net cash provided by/(used in) financing activities** | | 1,956,519 | 436,191 | 885,262 | (240,849) |
| Net increase/(decrease) in cash held | | 873 | (5,515,608) | (319,707) | (5,357,843) |
| Cash at the beginning of the financial year | | 1,261,173 | 6,776,781 | 1,027,780 | 6,385,623 |
| Cash at the end of the financial year | 31(a) | 1,262,046 | 1,261,173 | 708,073 | 1,027,780 |

The statements of cash flows are to be read in conjunction with the notes to the financial statements set out on pages 26 to 69.

## 1 Statement of significant accounting policies

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

### *(a) 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 costs and except where stated, does not take into account changing money values or fair values of assets.

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

Where necessary, comparative information has been reclassified to achieve consistency in disclosure with current financial year amounts and other disclosures.

The consolidated annual financial report has been prepared on the going concern basis, which contemplates continuity of normal business activities and the realisation of assets and liabilities in the ordinary course of business.

***Financial position – going concern***

The consolidated entity incurred a loss from ordinary activities of $989,655 for the financial year ended 30 June 2004. The result was impacted by the loss of $1,463,000 incurred in the first half of the financial year. The consolidated entity made a profit of $456,345 in the second half of the financial year.

The loss in the December half was primarily the result of the high cost of bringing the Electric Arc Furnace (EAF) dust/zinc sulphate production processes online and overcoming EAF dust variability issues which were affecting final zinc sulphate produced. The issues have been addressed in the second half of the financial year and the consolidated entity has operated profitably in the June half.

The consolidated entity held cash as at 30 June 2004 of $1,262,046 (2003: $1,261,173). In addition, the consolidated entity had net assets of $8,072,909 (2003: $8,862,564) and positive working capital of $2,103,116 (2003: $6,455) at year end.

The net cash used in operating activities during the year was $1,409,513 (2003: $3,675,077). The net cash used in operating activities was mainly the result of the increase in receivables of $1,946,475. The revenue from ordinary activities increased by 104% to $9.7 million in the year and as a result, the receivables level increased significantly in the year.

The directors consider the consolidated entity had produced a solid sustainable progress in both revenue improvement and project development in the second half of the year. The Directors expect the consolidated entity to continue to grow and be profitable in the 2005 financial year.

## 1 Statement of significant accounting policies (cont'd)

### *(a) Basis of preparation (cont'd)*

In light of the EAF dust processing difficulties being addressed; successfully concluded long term contracts for EAF dust and immobilisation projects; continuing strong selenium price; the emerging new projects in hand and the improved cash and working capital position of the consolidated entity, the consolidated financial report has been prepared on a going concern basis which contemplates continuity of normal business activities and the realisation of assets and liabilities in the ordinary course of business.

### *(b) Principles of consolidation*

***Controlled entities***

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

***Associates***

Associates are those entities, other than partnerships, over which the consolidated entity exercises significant influence and which are not intended for sale in the near future.

In the consolidated financial statements, investments in associates are accounted for using equity accounting principles. Investments in associates are carried at the lower of the equity accounted amount and recoverable amount. The consolidated entity's equity accounted share of the associates' net profit or loss is recognised in the consolidated statement of financial performance from the date significant influence commences until the date significant influence ceases. Other movements in reserves are recognised directly in consolidated reserves.

***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 associates, including those relating to contributions of non-monetary assets on establishment, are eliminated to the extent of the consolidated entity's interest. Unrealised gains relating to associates are eliminated against the carrying amount of the investment. Unrealised losses are eliminated in the same way as unrealised gains, unless they evidence a recoverable amount impairment.

### *(c) Revenue recognition*

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

***Rendering of services***

Revenue from rendering services is recognised when the treated material reaches a condition specified in the contract and/or the licence issued by the state Department of Environment and Conservation.

## 1 Statement of significant accounting policies (cont'd)

### *(c) Revenue recognition (cont'd)*

***Unearned income***

Income received in advance is deferred until the services are performed.

***Sale of goods***

Revenue from the sale of goods is recognised (net of returns, discounts and allowances) when control of the goods passes to the customer.

***Interest revenue***

Interest revenue is recognised as it accrues, taking into account the effective yield on the financial asset.

***Sale of non-current assets***

The gross proceeds of non-current asset sales are included as revenue at the date control of the asset passes to the buyer, usually when 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.

Any related balance in the asset revaluation reserve is transferred to the general reserve on disposal.

***Research and development grants***

Where a grant is received relating to research and development costs that have been expensed, the grant is recognised as revenue. Where a grant is received relating to research and development costs that have been deferred, the grant is deducted from the carrying amount of the deferred research and development costs.

### *(d) 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, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included.

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.

## *1 Statement of significant accounting policies (cont'd)*

### *(e) Foreign currency*

***Transactions***

Foreign currency transactions are translated to Australian currency at the rates of exchange ruling at the dates of the transactions. Amounts receivable and payable in foreign currencies at balance date are translated at the rates of exchange ruling on that date.

Exchange differences relating to amounts payable and receivable in foreign currencies are brought to account as exchange gains or losses in the statement of financial performance in the financial year in which the exchange rates change.

### *(f) Borrowing costs*

Borrowing costs include interest, amortisation of discounts or premiums relating to borrowings, amortisation of ancillary costs incurred in connection with arrangement of borrowings, including trade creditors and lease finance charges.

Ancillary costs incurred in connection with the arrangement of borrowings are capitalised and amortised over the life of the borrowings.

Borrowing costs are expensed as incurred.

### *(g) Earnings per share*

Basic earnings per share ("EPS") is calculated by dividing the net profit/(loss) attributable to members of the parent entity for the financial year, after excluding any costs of servicing equity, by the weighted average number of ordinary shares of the Company.

Dilute 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 weighted average number of ordinary shares and dilutive potential ordinary shares adjusted for any bonus issue.

### *(h) Taxation*

The consolidated entity adopts the income statement liability method of tax effect accounting.

Income tax expense is calculated on operating profit 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 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 a reasonable doubt, or if relating to tax losses when realisation is virtually certain.

## 1 Statement of significant accounting policies (cont'd)

### *(h) Taxation (cont'd)*

***Tax consolidation***

The company is the head entity in the tax-consolidated group comprising all the Australian wholly-owned subsidiaries. The group intends to consolidate from 1 July 2003.

Subject to meeting the above requirements, the head entity recognises all of the current and deferred tax assets and liabilities of the tax-consolidated group (after elimination of intra-group transactions).

At 30 June 2004, no tax funding agreement has been entered into.

### *(i) Acquisitions of assets*

All assets acquired including property, plant and equipment and intangibles other than goodwill are initially recorded at their cost of acquisition at the date of acquisition, being the fair value of the consideration provided plus incidental costs directly attributable to the acquisition. When equity instruments are issued as consideration, their market price at the date of acquisition is used as fair value. Transaction costs arising on the issue of equity instruments are recognised directly in equity subject to the extent of proceeds received, otherwise expensed.

The costs of assets constructed or internally generated by the consolidated entity, other than goodwill, include the cost of materials and direct labour.

Expenditure, including that on internally generated assets other than research and development costs, is only recognised as an asset when the entity controls future economic benefits as a result of the costs incurred, it is probable that those future economic benefits will eventuate, and the costs can be measured reliably. Costs attributable to feasibility and alternative approach assessments are expensed as incurred.

***Research and development costs***

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 deferred.

***Subsequent additional costs***

Costs incurred on assets subsequent to initial acquisition are capitalised when it is probable that future economic benefits in excess of the originally assessed performance of the asset will flow to the consolidated entity in future years.

Costs that do not meet the criteria for capitalisation are expensed as incurred.

## 1 Statement of significant accounting policies (cont'd)

### *(j) Revisions 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 affect both current and future periods.

### *(k) Receivables*

The collectibility of debts is assessed at balance date and specific provision is made for any doubtful accounts.

### *(l) Inventories*

Raw materials and stores, work in progress and finished goods are carried at the lower of cost and net realisable value.

Cost includes direct materials, direct labour, other direct variable costs and allocated production overheads necessary to bring inventories to their present location and condition, based on normal operating capacity of the production facilities.

***Manufacturing activities***

The cost of manufacturing inventories and work-in-progress are assigned on a first-in, first-out basis. Costs arising from exceptional wastage are expensed as incurred.

***Net realisable value***

Net realisable value is determined on the basis of each inventory line's normal selling pattern. Expenses of marketing, selling and distribution to customers are estimated and are deducted to establish net realisable value.

### *(m) Investments*

***Controlled entities***

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

***Associates***

In the Company's financial statements investments in unlisted shares of associates are carried at the lower of cost and recoverable amount.

***Other entities***

Investments in other listed entities are measured at fair value, being quoted market prices at reporting date.

Investments in other unlisted entities are carried at the lower of cost and recoverable amount.

## 1 Statement of significant accounting policies (cont'd)

### *(n) Leased assets*

Leases under which the consolidated entity 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. Contingent rentals are expensed as incurred.

***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.

### *(o) 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 either 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.

### *(p) Intangibles*

The cost of the intangible is amortised over the period in which the related benefits are expected to be realised. The carrying amount of the intangible is reviewed at each reporting date. Where the balance exceeds the value of expected future benefits, the difference is charged to the statement of financial performance. The amortisation rate applied is 11.0% on original cost.

## 1 Statement of significant accounting policies (cont'd)

### *(q) Recoverable amount of non-current assets valued on cost basis*

The carrying amounts of non-current assets valued on the cost basis, other than exploration and evaluation expenditure carried forward (refer Note 1(o)) 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 financial year in which it occurs.

Current valuations for land and buildings valued on the cost basis are carried out at least once every three years.

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

In assessing recoverable amounts of non-current assets the relevant cash flows have been discounted to their present value, except where specifically stated.

### *(r) Depreciation and amortisation*

***Complex assets***

The components of major assets that have materially different useful lives, are effectively accounted for as separate assets, and are separately depreciated.

***Useful lives***

All assets, including intangibles, have limited useful lives and are depreciated/amortised using the straight line method over their estimated useful lives, taking into account estimated residual values, with the exception of finance lease assets which are amortised over the term of the relevant lease, or where it is likely the consolidated entity will obtain ownership of the asset, the life of the asset.

Assets are depreciated or amortised from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

Amortisation is not charged on costs carried forward in respect of areas of interest in the development phase until commercial production commences.

Depreciation and amortisation rates and methods are reviewed annually for appropriateness. When changes are made, adjustments are reflected prospectively in current and future periods only. Depreciation and amortisation are expensed, except to the extent that they are included in the carrying amount of another asset as an allocation of production overheads.

## 1 Statement of significant accounting policies (cont'd)

### *(r) Depreciation and amortisation (cont'd)*

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

| | 2004<br>% | 2003<br>% |
|---|---|---|
| **Property, plant and equipment** | | |
| Buildings and freehold improvements | 2.5 | 2.5 |
| Plant and equipment | 13-25 | 13-25 |
| Office equipment and fixtures | 13-27 | 13-27 |
| Motor vehicles | 15-25 | 15-25 |
| Leased vehicles and machinery | 15-25 | 15-25 |
| **Intangibles** | | |
| Hydroproc process | 11 | 11 |

### *(s) Payables*

Liabilities are recognised for amounts to be paid in the future for goods or services received. Trade accounts payables are normally settled within 30 days.

### *(t) Interest bearing liabilities*

Debentures and notes payable are recognised when issued at the net proceeds received. Interest expense is accrued at the contracted rate and included in "Other creditors and accruals".

### *(u) Employee benefits*

***Wages, salaries, annual leave, sick leave and non-monetary benefits***

Liabilities for employee benefits for wages, salaries, annual leave and sick leave represent present obligations resulting from employees' services provided to reporting date, calculated at undiscounted amounts based on remuneration wage and salary rates that the consolidated entity expects to pay as at reporting date including related on-costs, such as, workers compensation insurance and payroll tax.

Non-accumulating non-monetary benefits, such as company car provided, are expensed based on the net marginal cost to the consolidated entity as the benefits are taken by the employees.

## 1 Statement of significant accounting policies (cont'd)

### *(u) Employee benefits (cont'd)*

***Long service leave***

The provision for employee benefits 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 bonds at reporting 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 option plans***

Where shares or options are issued to employees, including directors, as remuneration for past services, the difference between fair value of the shares or options issued and the consideration received, if any, from the employee is expensed. The fair value of the shares or options issued is recorded in the contributed equity. Shares or options issued to employees, including directors, pursuant to the Employee Share Option Plan are recorded in contributed equity at the fair value of consideration received, if any.

Transaction costs associated with issuing shares and options are recognised in equity subject to the extent of the proceeds received, otherwise expensed. Other administrative costs are expensed.

***Superannuation plan***

The Company and other controlled entities contribute to employee nominated superannuation funds. Contributions are recognised as an expense as they are made. The Company and its controlled entities have no legal or constructive obligation to fund any deficit.

### *(v) Provisions*

A provision is recognised when there is a legal, equitable or constructive obligation as a result of a past event and it is probable that a future sacrifice of economic benefits will be required to settle the obligation, the timing or amount of which is uncertain.

***Dividends***

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

***Provisions for disposal of residues and site clean up***

Provisions are made for estimated costs relating to the remediation of soil, groundwater and untreated waste as soon as the need is identified.

Provisions are determined on an undiscounted basis on the basis of current costs, current legal requirements and current technology. Changes in estimates are dealt with on a prospective basis.

## 1 Statement of significant accounting policies (cont'd)

### *(w) Financial instruments issued*

***Convertible financial instruments***

Where financial instruments, such as convertible notes issued by the Company, give rise to a contractual obligation to deliver cash to the holder, they are classified as liabilities to the extent of the obligation.
Where financial instruments are redeemable at the option of the holder, redeemable at a fixed date or perpetual instruments with cumulative interest obligations, the proceeds received are classified as liabilities and related distributions as interest expense.

Where financial instruments are redeemable but either the holder or the Company has an option to convert them into ordinary shares of the Company, 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 accretes 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.

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | **2004** | **2003** | **2004** | **2003** |
| | **$** | **$** | **$** | **$** |
| **2 Revenue from ordinary activities** | | | | |
| Rendering of services revenue from operating activities | 6,257,493 | 3,153,927 | 1,323,463 | |
| Sale of goods revenue from operating activities | 3,207,166 | 1,260,928 | - | |
| **Other revenue:** | | | | |
| *From operating activities* | | | | |
| ■ Interest received from unrelated parties | 54,688 | 151,598 | 39,747 | 142,66 |
| *From outside operating activities* | | | | |
| ■ Gross proceeds on sales of property, plant and equipment | - | 49,878 | - | 28,47 |
| ■ Freight subsidy | 55,554 | 39,375 | | - |
| ■ Research and development grant | 111,835 | - | 111,835 | - |
| ■ Other | 9,900 | 101,336 | 7,151 | |
| Total other revenue | 231,977 | 342,187 | 158,733 | 171,168 |
| **Total revenue from ordinary activities** | 9,696,636 | 4,757,042 | 1,482,196 | 171,168 |

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | 2004 $ | 2003 $ | 2004 $ | 2003 $ |

## 3 Loss from ordinary activities before income tax expense

Loss from ordinary activities before income tax expense has been arrived at after charging/(crediting) the following items:

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| Cost of goods sold | 971,933 | 624, | - | - |
| Borrowing costs paid or payable in respect to: | | | | |
| ■ finance leases | 15,934 | 19,702 | 10,248 | 12,711 |
| ■ debenture costs | 179,671 | 12,104 | - | - |
| ■ financial institutions | 12,767 | 28,697 | 4,549 | - |
| ■ convertible notes classified as liabilities | 51,319 | - | 51,319 | - |
| ■ others | - | 3,810 | - | 11,502 |
| | 259,691 | 64,313 | 66,116 | 24,213 |
| Depreciation of: | | | | |
| ■ buildings and freehold improvements | 83,536 | 81,950 | - | - |
| ■ plant and equipment | 1,112,185 | 972,847 | 15,056 | 329 |
| ■ office equipment and fixtures | 10,562 | 10,401 | 6,501 | 6,491 |
| ■ motor vehicles | 18,856 | 22,057 | 7,311 | 6,714 |
| Amortisation of: | | | | |
| ■ intangibles | 244,644 | 244,643 | - | - |
| ■ leased vehicles and machinery | 22,207 | 20,255 | 22,207 | 21,468 |
| | 1,491,990 | 1,352,153 | 51,075 | 35,002 |
| Net expense/(credit) from movements in provision for: | | | | |
| ■ employee entitlements | 141,096 | 61,057 | (19,574) | 19,251 |
| ■ disposal of residues | (315,155) | (880,908) | - | - |
| ■ (Write back)/diminution in loans to controlled entities and investments | | - | (627,750) | 3,248,864 |
| Operating lease rental expense | 30,480 | 113,321 | 15,304 | 17,381 |
| Research and development expenses | - | 860 | - | - |
| Net foreign exchange loss/(gain) | 20,603 | 15,493 | (6,666) | 27,449 |
| Net gain on sales of property, plant and equipment | - | (13,218) | - | (8,804) |

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | 2004 | 2003 | 2004 | 2003 |
| | $ | $ | $ | $ |
| **4 Auditor's remuneration** | | | | |
| ***Audit services*** | | | | |
| Auditors of the Company - KPMG | | | | |
| ■ Audit and review of the financial reports | 70,128 | 69,355 | 70,128 | 9,765 |
| ■ Other regulatory audit services | 2,000 | 1,611 | 2,000 | 1,611 |
| | 72,128 | 70,966 | 72,128 | 11,376 |
| ***Other services*** | | | | |
| Auditors of the Company – KPMG | | | | |
| ■ Taxation services | 10,650 | 20,866 | 10,650 | 7,725 |
| ■ Advisory services | 329 | 11,772 | - | 11,772 |
| KPMG related practices | | | | |
| ■ KPMG New Zealand tax services | 16,035 | - | 16,035 | - |
| | 99,142 | 103,604 | 98,813 | 30,873 |

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | 2004 $ | 2003 $ | 2004 $ | 2003 $ |

## 5 Taxation

### (a) *Income tax expense*

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| Prima-facie income tax revenue at 30% (2003: 30%) on the loss from ordinary activities | (286,943) | (1,335,890) | (142,250) | (1,501,646) |
| Increase in income tax expense due to: | | | | |
| ■ Non deductible depreciation and amortisation | 97,660 | 97,414 | - | - |
| ■ Non deductible diminution in value of investments/loans | - | - | 445,119 | 974,659 |
| ■ Non deductible items | 3,830 | 4,756 | 946 | 4,670 |
| ■ Provision for tax payable by New Zealand operation | 33,182 | - | 33,182 | - |
| | (152,271) | (1,233,720) | 336,997 | (522,317) |
| Decrease in income tax expense due to: | | | | |
| ■ Non assessable adjustment to diminution in value of investments/loans | - | - | (633,444) | - |
| ■ Non assessable items | (30,165) | - | (30,165) | - |
| ■ Other deductible items | (1,571) | - | (32) | - |
| | (184,007) | (1,233,720) | (326,644) | (522,317) |
| Tax effect of losses not taken to account | 328,068 | 1,481,097 | 400,705 | 477,479 |
| Tax effect of timing differences not taken to account | (110,879) | (247,377) | (40,879) | 36,142 |
| Tax losses transferred for nil consideration | - | - | - | 8,696 |
| Income tax expenses on the profit from ordinary activities | 33,182 | - | 33,182 | - |

## 5. Taxation (cont'd)

### *(b) Current tax liabilities/(receivables)*

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| Movement during the year: | | | | | |
| Balance at beginning of year | | - | - | - | - |
| Income tax paid – current year operating activities Australia | | - | - | - | - |
| Income tax paid – current year operating activities New Zealand | | (155,689) | - | (155,689) | - |
| Current year income tax expense on profit from ordinary activities of Australia | | - | - | - | - |
| Current year income tax expense on profit from ordinary activities of New Zealand | | 33,182 | - | 33,182 | - |
| Current tax receivable | | (122,507) | - | (122,507) | - |

This amount represents excess withholding tax paid to the New Zealand which is refundable on the lodgement of the Company's income tax return in New Zealand. This balance is included in other receivables.

***Future income tax benefit not taken to account***

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| The potential future income tax benefit in controlled entities, which are companies, arising from tax losses and timing differences has not been recognised as an asset because recovery of tax losses is not virtually certain and recovery of timing differences is not assured beyond reasonable doubt | 1(h) | 2,607,706 | 2,390,421 | 2,607,706 | 1,042,703 |

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

- the relevant company derives future assessable income of a nature and an amount sufficient to enable the benefit to be realised;
- the relevant company continues to comply with the conditions for deductibility imposed by the law; and
- no changes in tax legislation adversely affect the relevant company in realising the benefit.

## 6 Dividends

No dividends paid or declared by the Company to members since the end of the previous financial year.

| | The Company | |
|---|---|---|
| | **2004** **$** | **2003** **$** |
| ***Dividend franking account*** | | |
| 30% franking credits available to shareholders of HydroMet Corporation Limited for subsequent financial years | 3,216,850 | 3,216,850 |

The above available amounts are based on the balance of the dividend franking account at year end adjusted for:

- franking credits that will arise from the payment of the current tax liability;
- franking debits that will arise from the payment of dividends recognised as a liability at the year end;
- franking credits that will arise from the receipt of dividends recognised as receivables by the tax consolidated group at the year end; and
- franking credits that the entity may be prevented from distributing in subsequent years.

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

***Tax Consolidation legislation***

On 1 July 2003, Hydromet Corporation Limited and its wholly-owned subsidiaries adopted the Tax Consolidation legislation which requires a tax-consolidated group to keep a single franking account. The amount of franking credits available to shareholders of the parent entity (being the head entity in the tax-consolidated group) disclosed at 30 June 2004 has been measured under the new legislation as those available from the tax-consolidated group.

## 7 Earnings per share

Ordinary shares on issue during the year are the only classification of securities included in the basic and diluted earnings per share calculation.

Further details of these securities are contained in Note 18.

## 7 Earnings per share (cont'd)

### *Earnings reconciliation*

| | Consolidated 2004 $ | Consolidated 2003 $ |
|---|---|---|
| Net loss | (989,655) | (4,452,966) |
| Basic loss | (989,655) | (4,452,966) |
| | **No.** | **No.** |
| Weighted average number of ordinary shares used as the denominator in the calculation of basic earnings per share | 270,131,585 | 269,737,780 |
| The following securities have not been included in the calculation of diluted EPS as they are not dilutive: | | |
| Employees share options issued on 8 March 2004 | 5,315,000 | - |
| Directors' share options issued on 19 December 2002 | 10,000,000 | 10,000,000 |
| Options held by Chemmet Pty limited issued on 29 September 2000. | - | 6,000,000 |
| Convertible notes issued on 19 December 2003 | 1,000,000 | - |

Full details of these options are set out in Note 18.

## 8 Cash assets

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| Cash at bank and on hand | 1,262,046 | 1,261,173 | 708,073 | 1,027,780 |

| | | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|---|
| **9** | **Receivables** | | | | | |
| | **Current** | | | | | |
| | Trade debtors | | 2,699,464 | 447,178 | 866,599 | - |
| | Provision for doubtful trade debtors | | - | (173) | - | - |
| | | | 2,699,464 | 447,005 | 866,599 | - |
| | Sundry debtors | | 615,677 | 921,661 | 153,923 | 21,964 |
| | | | 3,315,141 | 1,368,666 | 1,020,522 | 21,964 |
| | **Non-current** | | | | | |
| | Loans to controlled entities | | - | - | 36,927,964 | 35,870,606 |
| | Provision for doubtful debts | | - | - | (29,905,310) | (28,421,579) |
| | | 29 | - | - | 7,022,654 | 7,449,027 |
| | Loans to associated company | 23 | 194,510 | 194,510 | 194,510 | 194,510 |
| | Provision for doubtful debts | | (194,510) | (194,510) | (194,510) | (194,510) |
| | | | - | - | - | - |
| **10** | **Other financial assets** | | | | | |
| | **Non-current** | | | | | |
| | Investments in controlled entities – unlisted shares at cost | 21 | - | - | 13,287,558 | 13,287,558 |
| | Provision for diminution in investments | | - | - | (9,762,539) | (11,874,020) |
| | | | - | - | 3,525,019 | 1,413,538 |
| | Investment in associate – unlisted shares at cost | 23 | 1,108,852 | 1,108,852 | - | - |
| | Provision for diminution in investments | | (1,108,852) | (1,108,852) | - | - |
| | | | - | - | - | - |
| | | | - | - | 3,525,019 | 1,413,538 |

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| **11 Inventories** | | | | |
| **Current** | | | | |
| ■ Raw materials and stores - at cost | 151,112 | 124,210 | 4,309 | - |
| ■ Work in progress - at cost | 37,556 | 93,818 | - | - |
| ■ Finished goods - at cost | 11,519 | 116,780 | - | - |
| | 200,187 | 334,808 | 4,309 | - |
| **12 Property, plant and equipment** | | | | |
| Freehold land – at cost | 1,794,580 | 1,794,580 | - | - |
| Buildings and freehold improvements – at cost | 3,304,923 | 3,299,227 | - | - |
| Accumulated depreciation | (691,083) | (607,545) | - | - |
| | 2,613,840 | 2,691,682 | - | - |
| Plant and equipment - at cost | 17,282,566 | 16,824,859 | 114,377 | 3,100 |
| Accumulated depreciation | (13,531,349) | (12,421,284) | (14,876) | (329) |
| | 3,751,217 | 4,403,575 | 99,501 | 2,771 |
| Office equipment and fixtures - at cost | 219,678 | 214,176 | 146,641 | 143,382 |
| Accumulated depreciation | (196,011) | (185,448) | (130,437) | (123,936) |
| | 23,667 | 28,728 | 16,204 | 19,446 |
| Motor vehicles - at cost | 131,426 | 132,641 | 48,744 | 48,744 |
| Accumulated depreciation | (75,976) | (58,336) | (25,688) | (18,377) |
| | 55,450 | 74,305 | 23,056 | 30,367 |
| Leased vehicles and machinery - at cost | 172,062 | 172,062 | 172,062 | 172,062 |
| Accumulated amortisation | (47,426) | (25,219) | (47,426) | (25,219) |
| | 124,636 | 146,843 | 124,636 | 146,843 |
| Total property, plant and equipment - net book value | 8,363,390 | 9,139,713 | 263,397 | 199,427 |

| | Consolidated | The Company |
|---|---|---|
| | 2004<br>$ | 2004<br>$ |

## 12 Property, plant and equipment (cont'd)

### Reconciliations

Reconciliations of the carrying amounts for each class of property, plant and equipment are set out below:

| | Consolidated 2004 $ | The Company 2004 $ |
|---|---|---|
| *Freehold land* | | |
| Carrying amount at beginning and end of year | 1,794,580 | - |
| *Buildings and freehold improvements* | | |
| Carrying amount at beginning of year | 2,691,682 | - |
| Additions | 5,697 | - |
| Depreciation | (83,539) | - |
| Carrying amount at end of year | 2,613,840 | - |
| *Plant and equipment* | | |
| Carrying amount at beginning of year | 4,403,575 | 2,771 |
| Additions | 534,933 | 114,377 |
| Disposals/retirements | (76,713) | (2,591) |
| Depreciation | (1,110,578) | (15,056) |
| Carrying amount at end of year | 3,751,217 | 99,501 |
| *Office equipment and fixtures* | | |
| Carrying amount at beginning of year | 28,728 | 19,446 |
| Additions | 5,503 | 3,259 |
| Depreciation | (10,564) | (6,501) |
| Carrying amount at end of year | 23,667 | 16,204 |
| *Motor vehicles* | | |
| Carrying amount at beginning of year | 74,305 | 30,367 |
| Depreciation | (18,855) | (7,311) |
| Carrying amount at end of year | 55,450 | 23,056 |
| *Leased vehicles and machinery* | | |
| Carrying amount at beginning of year | 146,843 | 146,843 |
| Amortisation | (22,207) | (22,207) |
| Carrying amount at end of year | 124,636 | 124,636 |

## 12 Property, plant and equipment (cont'd)

*Current valuations – land and buildings*

An independent valuation was carried out on 15 August 2003 by Mr JR Harrington AAPI Certified Practising Valuer on the land and buildings located at Tomago, NSW. The valuation was made on "market value" basis. The directors are of the opinion that this basis provides a reasonable estimate of recoverable amount. The property was valued at $1,300,000, $316,389 above its net book value.

An independent valuation was carried out on 30 June 2002 by Mr WG Bramall, FAPI, AREI on the land and buildings located at Unanderra, NSW. The valuation was made on "specialised assets" basis. Specialised assets are those not normally traded in any market except as part of a total enterprise by reason of this specific design, size, location or other factors. The assessment of specialised owner-occupied assets controlled by the consolidated entity is made on the assumption that the consolidated entity will continue in operation or existence for the foreseeable future. The property was valued at $4,100,000, $675,191 above its net book value.

Capital gains tax has not been recognised in determining the valuation of land and buildings. Capital gains tax would not be payable if the assets were sold at reporting date.

The valuation is in accordance with Hydromet's policy of obtaining an independent valuation of land and buildings every three years. As land and buildings are recorded at cost, the valuation has not been brought to account.

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | 2004 $ | 2003 $ | 2004 $ | 2003 $ |
| **13 Exploration, evaluation and development expenditure** | | | | |
| Costs carried forward in respect of an area of interest in the exploration stage: | | | | |
| Purchase consideration | 240,000 | 240,000 | - | - |
| Exploration and evaluation expenditure capitalised | 62,199 | 62,199 | - | - |
| | 302,199 | 302,199 | - | - |
| **14 Intangible assets** | | | | |
| Hydroproc process - at cost | 2,217,323 | 2,217,323 | - | - |
| Accumulated amortisation | (1,553,933) | (1,309,289) | - | - |
| | 663,390 | 908,034 | - | - |

The Hydroproc process is the technology applied by the consolidated entity in its operations.

| | | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|---|
| **15** | **Payables** | | | | | |
| | **Current** | | | | | |
| | Trade creditors | | 1,029,781 | 663,298 | 296,231 | 39,057 |
| | Other creditors and accruals | | 414,543 | 311,396 | 276,592 | 45,453 |
| | Unearned income | | 254,022 | 606,793 | - | - |
| | | | 1,698,346 | 1,581,487 | 572,823 | 84,510 |
| **16** | **Interest bearing liabilities** | | | | | |
| | **Current** | | | | | |
| | Lease liabilities | 22 | 72,801 | 74,384 | 60,476 | 63,544 |
| | **Non-current** | | | | | |
| | Debentures | | 1,800,000 | 700,000 | - | - |
| | Convertible notes | 18 | 800,000 | - | 800,000 | - |
| | Lease liabilities | 22 | 80,623 | 155,536 | 54,857 | 117,446 |
| | | | 2,680,623 | 855,536 | 854,857 | 117,446 |

***Finance lease facility***

The consolidated entity's lease liabilities are secured by the leased assets of $146,843 (2003: $146,843), as in the event of default, the assets revert to the lessor.

***Debentures***

The debentures were issued on 26 March 2003 ($500,000), 30 May 2003 ($100,000) 18 June 2003 ($100,000), 20 August 2003 ($500,000), 22 September 2003 ($100,000), 24 October 2003 ($300,000) and 3 February 2004 ($200,000). The face value of each debenture is $1. The debentures have a term of three years from the date of issue, and attract an interest rate of 12% per annum, to be paid in arrears, semi-annually on 31 March and 30 September, respectively. The debenture holders have a fixed and floating charge over the assets of the company and its controlled entities.

## 17 Provisions

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| **Current** | | | | | |
| Employee benefits | 24 | 367,578 | 451,633 | 165,205 | 261,979 |
| Disposal of residues | 25(a) | 535,533 | 850,688 | - | - |
| | | 903,111 | 1,302,321 | 165,205 | 261,979 |
| **Non-current** | | | | | |
| Employee benefits | 24 | 118,563 | 78,301 | 61,632 | 46,188 |
| Site clean up | 25(a) | 560,000 | 560,000 | - | - |
| | | 678,563 | 638,301 | 61,632 | 46,188 |

### *Reconciliations*

Reconciliations of the carrying amounts of each class of provision, except for employee benefits are set out below:

| | Consolidated 2004 $ | The Company 2004 $ |
|---|---|---|
| **Disposal of residues – current** | | |
| Carrying amount at beginning of year | 850,688 | - |
| Payments made during the period | (315,155) | - |
| Carrying amount at end of year | 535,533 | - |
| **Site clean up – non current** | | |
| Carrying amount at beginning of year | 560,000 | - |
| Payments made during the year | - | - |
| Carrying amount at end of year | 560,000 | - |

## 18 Contributed equity

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | **2004** **$** | **2003** **$** | **2004** **$** | **2003** **$** |
| ***Share capital*** | | | | |
| 270,131,585 (2003: 270,131,585) ordinary shares, fully paid | 63,000,126 | 63,000,126 | 63,000,126 | 63,000,126 |
| 1,000,000 (2003:nil) redeemable convertible notes | 200,000 | - | 200,000 | - |
| | 63,200,126 | 63,000,126 | 63,200,126 | 63,000,126 |
| ***Movements during the year*** | | | | |
| **Ordinary shares** | | | | |
| Balance at the beginning of year | 63,000,126 | 62,946,920 | 63,000,126 | 62,946,920 |
| Shares issued | | | | |
| ■ 1,159,183 for cash issued under dividend reinvestment plan | - | 53,206 | - | 53,206 |
| Balance at end of year | 63,000,126 | 63,000,126 | 63,000,126 | 63,000,126 |
| **Redeemable convertible notes** | | | | |
| Balance at the beginning of year | - | - | - | - |
| Convertible notes issued | | | | |
| ■ 1,000,000 redeemable convertible notes issued on 19 November 2003 | 200,000 | - | 200,000 | - |
| Balance at end of year | 200,000 | - | 200,000 | - |

***Terms and conditions***

*Ordinary shares*

The voting rights attaching to the ordinary shares are set out in Rule 11.15 of the Company's Constitution.

Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings.

In the event of winding up the Company, ordinary shareholders rank after convertible note holders and creditors and are fully entitled to any proceeds of liquidation.

No ordinary shares were issued during the year. In the prior year 1,159,183 ordinary shares were issued at a price of 4.59 cents per share under the Company's approved dividend reinvestment plan.

## 18 Contributed equity (cont'd)

*Options*

On 19 December 2002 the Company issued a total of 10,000,000 ordinary share options to directors pursuant to approval of shareholders at the annual general meeting held on 29 November 2002. These options have an exercise price of 8 cents and expire on 31 March 2007. There are differing vesting dates in four parcels of 2,500,000 vesting annually for four years commencing on 31 December 2003.

During the year 6,000,000 options fully vested, with an exercise price of 15 cents per option expired.

On 8 March 2004, the Company provided 30 (2003: nil) employees to receive 5,315,000 options over ordinary shares for no consideration. Each option is convertible to one ordinary share at the exercise price of $0.08 per share. The options cannot be exercised before 16 February 2005 and expire on 16 February 2007.

On allotment the shares will be fully paid up to the exercise price and will rank equally with all other fully paid ordinary shares.

No options were exercised during the year.

*Convertible notes*

On 19 November 2003 the Company issued 1,000,000 convertible notes at a principal value of $1. Interest is payable quarterly in arrear at the coupon rate of 9.25% until the notes are either converted or redeemed. Interest is accumulative in the event that an interest payment is not made.

The notes may be converted to ordinary shares in the Company at the option of the note holder under the following terms:

- At the rate of $0.04 per share at the first conversion date being any day in the first 365 days after the issue of the last note; and
- At the rate of $0.043 per share at the second conversion date being any day in the second 365 days after the issue of the last note.

If the subscriber fails to convert the notes by either of the conversion dates, then the Company must on or before the redemption date being 912 days after the issue of the last note, redeem all the notes at the redemption price, being the principal value of $1, plus any accrued interest. The notes have been accounted for as compound financial instruments. A market discount rate has been used to determine the value of the liability component of the notes.

Prior to conversion, the notes do not entitle the note holder to any voting rights in the Company. Following conversion, the shares have the same voting rights as any other ordinary shares in the Company.

| | | Consolidated | | The Company | |
|---|---|---|---|---|---|
| | | 2004 | 2003 | 2004 | 2003 |
| | | $ | $ | $ | $ |

## 18 Contributed equity (cont'd)

*Convertible notes*

The proceeds received have been accounted for as follows:

| | | | | | |
|---|---|---|---|---|---|
| Non-current interest bearing liabilities | 16 | 800,000 | - | 800,000 | - |
| Contributed equity | | 200,000 | - | 200,000 | - |
| Total | | 1,000,000 | - | 1,000,000 | - |

## 19 Reserves

| | | | | |
|---|---|---|---|---|
| General reserve | 150,000 | 150,000 | 150,000 | 150,000 |
| Asset revaluation reserve | 355,688 | 355,688 | - | - |
| Total reserves | 505,688 | 505,688 | 150,000 | 150,000 |

There has been no movement in reserves during the past financial year.

***Nature and purpose of reserves***

*General*

The amount standing to the credit of the general reserve resulted from prior period allocations of retained profits for non-specific purposes.

*Asset revaluation*

The asset revaluation reserve includes the increment arising from the revaluation of freehold land and buildings in the financial year ended 30 June 1996. The asset revaluation reserve is not available for future asset write-downs as a result of using the deemed cost election for land and buildings when adopting the revised AASB 1041.

## 20 Accumulated losses

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| Accumulated losses at beginning of year | (54,643,250) | (49,773,843) | (58,061,566) | (52,652,639) |
| Net (loss) attributable to members of the parent entity | (989,655) | (4,452,966) | (507,348) | (5,005,486) |
| Net effect of initial adoption of revised AASB 1028 "Employee Benefits" | - | (13,000) | - | - |
| Net effect from dividends recognised during the year | - | (403,441) | - | (403,441) |
| Accumulated losses at end of year | (55,632,905) | (54,643,250) | (58,568,914) | (58,061,566) |

## 21 Particulars in relation to controlled entities

| Name | Note | Consolidated entity interest 2004 % | Consolidated entity interest 2003 % |
|---|---|---|---|
| ***Parent entity*** | | | |
| HydroMet Corporation Limited | | | |
| *Controlled entities* | | | |
| ■ HydroMet Operations (Southern) Limited | (i) | 100 | 100 |
| ■ HydroMet Technologies Pty Limited | | 100 | 100 |
| ■ HydroMet Operations (NT) Pty Limited | (i) | 100 | 100 |
| ■ HydroMet Operations (Tasmania) Pty Limited | (i) | 100 | 100 |
| ■ Mineral Estates Pty Limited | | 100 | 100 |
| Subsidiaries of which are: | | | |
| - MinMet Operations Pty Limited | | 100 | 100 |
| - Kia Pacific Gold Pty Limited | | 100 | 100 |
| ■ HydroMet Operations Limited | (i) | 100 | 100 |
| Subsidiary of which is: | | | |
| - Enviromet Operations Pty Limited | (i) | 100 | 100 |
| ■ MinMet Unit Trust | (ii) | 100 | 100 |
| ■ Hydromet Corporation Debenture Nominees Pty Limited | (i) (iii) | 100 | 100 |

*Notes*

(i) refer to note 32 for details of Deed of Cross Guarantee.

(ii) Mineral Estates Pty Limited owns 51% of the units of the MinMet Unit Trust. The balance of 49% is owned by HydroMet Operations Limited. MinMet Unit Trust is the beneficial owner of the consolidated entity's operating site in Tomago, NSW.

(iii) Hydromet Corporation Debenture Nominees Pty Limited has been issued debentures to the value of $1,800,000 as at 30 June 2004.

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| **22 Commitments** | | | | | |
| **Finance lease payment commitments** | | | | | |
| Finance lease commitments are payable: | | | | | |
| ■ within one year | | 84,548 | 90,855 | 68,021 | 74,327 |
| ■ one year or later and no later than five years | | 82,871 | 196,420 | 53,949 | 128,361 |
| | | 167,419 | 287,275 | 121,970 | 202,688 |
| Less: Future lease finance charges | | (13,995) | (57,355) | (6,637) | (21,698) |
| | | 153,424 | 229,920 | 115,333 | 180,990 |
| Lease liabilities provided for in the financial statements: | | | | | |
| ■ Current | 16 | 72,801 | 74,384 | 60,476 | 63,544 |
| ■ Non-current | 16 | 80,623 | 155,536 | 54,857 | 117,446 |
| Total lease liability | | 153,424 | 229,920 | 115,333 | 180,990 |

The consolidated entity leases vehicles and plant and equipment under various leases expiring from one to five years. At the end of the lease terms, the consolidated entity will purchase the assets at fixed percentages of original cost. The end of term residual values are included in the total finance lease payment commitments.

## 23 Investment in associated companies

Interest is held in the following associated company:

| Name | Principal activities | Balance date | Ownership interest 2004 % | Ownership interest 2003 % | Investment carrying amount 2004 $ | Investment carrying amount 2003 $ |
|---|---|---|---|---|---|---|
| HydroMet (India) Limited | Chemical manufacturer | 31 March | 23 | 23 | - | - |

The equity method has not been applied in respect of the consolidated entity's interest in HydroMet (India) Limited. The company incurred losses in previous years and the carrying amount of this investment has been written down to zero.

The aggregate amount receivable from HydroMet (India) Limited by the consolidated entity at balance date was $194,510 (2003: $194,510). A doubtful debt provision on the loan of $194,510 (2003: $194,510) has been made.

| | Note | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|---|
| **24 Employee benefits** | | | | | |
| Aggregate liability for employee entitlements, including on-costs | | | | | |
| Employee benefits provision | | | | | |
| ■ Current | 17 | 367,578 | 451,633 | 165,205 | 261,979 |
| ■ Non-current | 17 | 118,563 | 78,301 | 61,632 | 46,188 |
| | | 486,141 | 529,934 | 226,837 | 308,167 |
| The present values of employee entitlements not expected to be settled within twelve months of balance date have been calculated using the following weighted averages: | | | | | |
| Assumed rate of increase in wage and salary rates | | 4% | 3.5% | 4% | 3.5% |
| Discount rate | | 5.95% | 5.4% | 5.95% | 5.4% |
| Settlement term (years) | | 10 | 10 | 10 | 10 |
| Number of employees at year end | | 58 | 37 | 14 | 10 |

### *Superannuation commitments*

The Consolidated Entity contributes to several defined contribution plans for the purpose of superannuation guarantee payments and payment of other superannuation benefits on behalf of employees. The plans are administered by independent corporate trustees.

The Consolidated Entity has no interest in these superannuation plans (other than as a contributor) and is not liable for the performance of the plans, nor the obligations of the plans.

### *Employee share options plan*

The Company has an Employee Share Option Plan (ESOP) approved by the shareholders at the Company's annual general meeting on 29 September 2000.

The ESOP is available to all eligible employees to receive options over ordinary shares for no consideration. Each option is convertible to one ordinary share. The exercise price of the option is determined in accordance with the rules of the plan. The entitlement of each employee was determined by the Board.

To be eligible, employees must be employed by any entity in the consolidated entity at the time of grant. Share options are issued in the name of the participating employee.

## 24 Employee benefits (cont'd)

On 8 March 2004, the Company provided 30 (2003: nil) employees to receive 5,315,000 options over ordinary shares for no consideration. None of these options were issued to the Directors. Each option is convertible to one ordinary share at the exercise price of $0.08 per share. The options cannot be exercised before 16 February 2005 and expire on 16 February 2007.

There are no voting or dividend rights attached to the options. There are no voting rights attached to the unissued ordinary shares. Voting rights will be attached to the ordinary shares issued when the options are exercised.

Summary of options over unissued ordinary shares:

| Grant dates | Opening balance | Granted during the year | Closing balance | Vested and exercisable at 30 June 2004 |
|---|---|---|---|---|
| 8 March 2004 | - | 5,315,000 | 5,315,000 | - |

## 25 Contingent liabilities

### (a) *Environmental contingent liabilities*

Hazardous by-products are produced during the manufacturing processes carried on by HydroMet Operations (Southern) Limited, MinMet Operations Pty Limited and HydroMet Operations Limited. The controlled entities have established strict procedures to ensure that all such hazardous by-products are disposed of safely.

Provisions have been made for the estimated costs of disposal of these by-products on hand at 30 June 2004. Refer Note 17 for provision details. These provisions are sufficient to meet the disposal requirements of current environmental legislation. However, these operations are subject to rapidly changing environmental legislation in various jurisdictions and future obligations to meet changing environmental legislation could involve the consolidated entity in costly work. The directors are not aware of any impending changes to the requirements or of any current breaches of legislation which are material in nature.

### (b) *Deed of Cross Guarantee*

Under the terms of a Deed of Cross Guarantee, described in Note 32, the Company has guaranteed the repayment of all current and future creditors in the event any of the entities party to the Deed are wound up.

## 26 Segment information

Inter-segment pricing is determined on arm's-length basis.

Segments 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, interest-bearing loans, borrowings and expenses, and corporate assets and expenses.

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.

## 26 Segment information (cont'd)

### Business segment

The consolidated entity operates in one business segment which is the treatment of industrial residues using hydrometallurgical processing technology.

### Geographical segments

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of the processing plant where the services are provided to customers. Segment assets are based on the geographical location of the assets:

The consolidated entity's business segments operate geographically in Australia and New Zealand and involve in the treatment of industrial residues.

| Geographical segments | Australia | | New Zealand | | Consolidated | |
|---|---|---|---|---|---|---|
| | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 |
| | $ | $ | $ | $ | $ | $ |
| External segment revenue by location of processing plant | 8,550,805 | 4,757,042 | 1,145,831 | - | 9,696,636 | 4,757,042 |
| Segment assets by location of assets | 14,106,353 | 13,314,593 | 1,087,339 | - | 14,106,353 | 13,314,593 |
| Acquisitions of non-current assets | 431,756 | 2,326,600 | 114,377 | - | 546,133 | 2,326,600 |

## 27 Events subsequent to reporting date

***Option Agreement to sell Stanton Prospect***

The Company signed an Option Agreement with Conico Limited on 20 July 2004 for the potential sale of Hydromet's Stanton Prospect Cobalt mine lease situated in the Gulf of Carpentaria in the Northern Territory. The option agreement which remains in place until July 2005 will enable Conico Limited to conduct required due diligence obligations in assessing the lease for an intended listing by the company. Conico will pay Hydromet an option fee of $20,000 per every four month period of the option.

Hydromet will receive $500,000 in cash and 12.5 Million ordinary shares ($0.20 each) in a newly listed entity, subject to the option agreement being exercised, and successful listing of the purchaser on the ASX after its due diligence work on the Stanton Prospect. As part of the agreement, Hydromet has the right to enter into an off take agreement with the purchaser allowing first right of refusal to purchase its mine cobalt concentrates. This would allow Hydromet to establish a long-term sustainable cobalt chemical business at the company's Minmet operation in Tomago, NSW.

On completion of the sale, Hydromet intends to distribute some or all of the purchaser's shares to existing Hydromet shareholders in the form of a dividend paid on a pro rata basis, subject to approval from the ASX.

## 27 Events subsequent to reporting date (cont'd)

***International Financial Reporting Standards***

For financial years beginning on or after 1 January 2005, the consolidated entity must comply with International Financial Reporting Standards (IFRS) as issued by the Australian Accounting Standards Board.

This financial report has been prepared in accordance with Australian accounting standards and other financial reporting requirements (Australian GAAP). The differences between Australian GAAP and IFRS identified to date as potentially having a significant effect on the consolidated entity's financial performance and financial position are summarised below. The summary should not be taken as an exhaustive list of all the differences between Australian GAAP and IFRS. No attempt has been made to identify all disclosure, presentation or classification differences that would affect the manner in which transactions or events are presented.

The consolidated entity has not quantified the effects of the differences discussed below. Accordingly, there can be no assurances that the consolidated financial performance and financial position as disclosed in this financial report would not be significantly different if determined in accordance with IFRS.

Regulatory bodies that promulgate Australian GAAP and IFRS have significant ongoing projects that could affect the differences between Australian GAAP and IFRS described below and the impact of these differences relative to the consolidated entity's financial reports in the future. The potential impacts on the consolidated entity's financial performance and financial position of the adoption of IFRS, including system upgrades and other implementation costs which may be incurred, have not been quantified as at the transition date of 1 July 2004 due to the short timeframe between finalisation of the IFRS standards and the date of preparing this report. The impact on future years will depend on the particular circumstances prevailing in those years.

The board will establish a project to achieve transition to IFRS reporting, beginning with the half-year ended 31 December 2005 being the first financial year under IFRS. The Company's implementation project will consist of three phases as described below.

**Assessment and planning phase**

The assessment and planning phase aims to produce a high level overview of the impacts of conversion to IFRS reporting on existing accounting and reporting policies and procedures, systems and processes, business structures and staff.

This phase includes:

- high level identification of the key differences in accounting policies and disclosures that are expected to arise from adopting IFRS;
- assessment of new information requirements affecting management information systems, as well as the impact on the business and its key processes;
- evaluation of the implications for staff, for example training requirements; and
- preparation of a conversion plan for expected changes to accounting policies, reporting structures, systems, accounting and business processes and staff training.

It is planned that this phase will be completed in most respects by 30 September 2004.

## 27 Events subsequent to balance date (cont'd)

***International Financial Reporting Standards (cont'd)***

**Design phase**

The design phase aims to formulate the changes required to existing accounting policies and procedures and systems and processes in order to transition to IFRS. The design phase will incorporate:

- Formulating revised accounting policies and procedures for compliance with IFRS requirements.
- Identifying potential financial impacts as at the transition date and for subsequent financial years prior to adoption of IFRS.
- Developing revised IFRS disclosures.
- Designing accounting and business processes to support IFRS reporting obligations.
- Identifying and planning required changes to financial reporting and business source systems.
- Developing training programs for staff.

The Company will commence its design phase as soon as the assessment and planning phase is completed. It is expected to be completed by 31 December 2004.

**Implementation phase**

The implementation phase will include implementation of identified changes to accounting and business procedures, processes and systems and operational training for staff. It will enable the company to generate the required disclosures of AASB 1 as it progresses through its transition to IFRS.

Except for certain training that has been given to operational staff, the Company has not yet commenced the implementation phase.

The key potential implications of the conversion to IFRS on the consolidated entity are as follows:

- Financial instruments must be recognised in the statement of financial position and all derivatives and most financial assets must be carried at fair value.
- Income tax will be calculated based on the "balance sheet" approach, which will result in more deferred tax assets and liabilities and, as tax effects follow the underlying transaction, some tax effects will be recognised in equity.
- Revaluation increments and decrements relating to revalued property, plant and equipment and intangible assets will be recognised on an individual asset basis, not a class of assets basis.
- Goodwill and intangible assets with indefinite useful lives will be tested for impairment annually and will not be amortised.

## 28 Director and executive disclosures

### *(a) Remuneration of specified directors and specified executives by the consolidated entity*

Remuneration levels are competitively set to attract and retain appropriately qualified and experienced directors and senior executives. The Audit and Remuneration Committee considers the appropriateness of remuneration packages, given trends in comparative companies both locally and internationally. Remuneration packages include a mix of fixed remuneration and equity-based remuneration. There was no performance-based remuneration paid to Directors during the year.

The remuneration structures explained below are designed to attract suitably qualified candidates, and to effect the broader outcome of increasing the consolidated entity's net profit attributable to members of the parent entity. The remuneration structures took into account:

- The overall level of remuneration for each director and executive; and
- The executives' ability to control performance.

The Company has no redundancy arrangements and schemes for retirement benefits, other than statutory superannuation, for directors.

Non-executive directors' base fees are presently $25,000 per annum. The Chairperson and committee members receive no extra fees. Directors' fees cover all main board activities and membership of committee. Non-executive directors may receive additional payments for services required by the Company which are outside normal board and committee activities. Details of these services are set out on note 28(c).

## 28 Director and executive disclosures (cont'd)

### *(a) Remuneration of specified directors and specified executives by the consolidated entity (cont'd)*

The following table provides the details of all directors of the Company ("specified directors") and the nature and amount of the elements of their remuneration for the year ended 30 June 2004. The consolidated entity has no specified executives who are not also directors of the Company.

| | | Primary | | Post-employment | Equity compensation | Other compensation | |
|---|---|---|---|---|---|---|---|
| | | Salary & fees $ | Non-monetary benefits $ | Super-annuation benefits $ | Value of options $ (i) | Insurance premium $ | Total $ |
| **Specified directors** | | | | | | | |
| **Non-executive** | | | | | | | |
| Mr SH Kwan | 2004 | 25,000 | - | 2,250 | - | 13,225 | 40,475 |
| | 2003 | 25,000 | - | 2,250 | - | 14,619 | 41,869 |
| Mr PS Tang | 2004 | 25,000 | - | 2,250 | - | 13,225 | 40,475 |
| | 2003 | 25,000 | - | 2,250 | - | 14,619 | 41,869 |
| Mr TR Allen | 2004 | 25,000 | - | 4,979 | - | 13,225 | 43,204 |
| | 2003 | 25,000 | - | - | - | 14,619 | 39,619 |
| Mr SB Wolfe | 2004 | 10,417 | - | 938 | - | 4,935 | 16,290 |
| (Appointed 2 February 2004) | 2003 | - | - | - | - | - | - |
| **Executive** | | | | | | | |
| Mr GW Wrightson | 2004 | 188,460 | 21,647 | 15,162 | - | 13,225 | 238,494 |
| (Managing Director) | 2003 | 174,994 | 20,416 | 13,950 | - | 14,619 | 223,979 |
| Dr LD Jayaweera | 2004 | 159,998 | 33,951 | 12,000 | - | 13,225 | 219,174 |
| (Chairperson) | 2003 | 159,998 | 37,022 | 9,600 | - | 14,619 | 221,239 |
| Total, all specified directors | 2004 | 433,875 | 55,598 | 37,579 | - | 71,060 | 598,112 |
| | 2003 | 409,992 | 57,438 | 28,050 | - | 73,095 | 568,575 |

(i) 2,000,000 options were issued to each of Mr. G Wrightson, Dr. L Jayaweera, Mr. S Kwan, Mr. P Tang and Mr. T Allen on 19 December 2002 in which 500,000 out of the 2,000,000 options were vested and exercisable at the reporting date. The value of the options have been independently valued at a fair value of $Nil at the date of grant using Black-Scholes Option Pricing model.

## 28 Director and executive disclosures (cont'd)

### *(b) Equity instruments*

All options refer to options over ordinary shares of Hydromet Corporation Limited, which are exercisable on a one-for-one basis under the terms of the options issued.

**Options and rights over equity instruments granted as remuneration**

During the financial year, no options were issued to Directors and executives as remuneration. The following options over ordinary shares were vested during the current year under the terms of the options issued:

| | Number of options granted during the year | Number of options vested during the year |
|---|---|---|
| **Specified directors** | | |
| Mr SH Kwan | - | 500,000 |
| Mr PS Tang | - | 500,000 |
| Mr TR Allen | - | 500,000 |
| Mr. GW Wrightson | - | 500,000 |
| Dr LD Jayaweera | - | 500,000 |

Further details, including grant dates and exercise dates regarding options granted to directors are in note 18. No options were exercised during the financial year.

**Options holdings**

The movement during the financial year in the number of options over ordinary shares in Hydromet Corporation Limited held, directly, indirectly or beneficially, by each specified director, including their personally-related entities, is as follows:

| | Held at 1July 2003 | Expired during the year | Held at 30 June 2004 | Vested and exercisable at 30 June 2004 |
|---|---|---|---|---|
| Specified directors | | | | |
| Mr SH Kwan | 2,000,000 | - | 2,000,000 | 500,000 |
| Mr PS Tang | 2,000,000 | - | 2,000,000 | 500,000 |
| Mr TR Allen | 2,000,000 | - | 2,000,000 | 500,000 |
| Mr GW Wrightson | 2,000,000 | - | 2,000,000 | 500,000 |
| Dr LD Jayaweera | 8,000,000 | 6,000,000 | 2,000,000 | 500,000 |

No options held by specified directors are vested but not exercisable. The expiry date for all options exercisable at 30 June 2004 is 31 March 2007.

## 28 Director and executive disclosures (cont'd)

### *(b) Equity instruments (cont'd)*

**Equity holdings and transactions**

The movement during the financial year in the number of ordinary shares of Hydromet Corporation Limited held, directly, indirectly or beneficially, by each specified director, including their personally-related entities is as follows:

| | Held at 1July 2003 | Sales | Held at 30 June 2004 |
|---|---|---|---|
| Specified directors | | | |
| Mr SH Kwan | 46,000 | - | 46,000 |
| Mr PS Tang | 80,000 | - | 80,000 |
| Mr TR Allen | 2,300,000 | - | 2,300,000 |
| Mr GW Wrightson | 578,300 | - | 578,300 |
| Dr LD Jayaweera | 15,308,250 | 1,700,000 | 13,608,250 |

### *(c) 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 financial year. 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 $68,913. Details of the transactions are as follows:

| | Transaction | Note | $ |
|---|---|---|---|
| Specified directors | | | |
| Mr PS Tang | Secretarial and consulting fees | (i) | 10,500 |
| Mr TR Allen | Consulting fees | (ii) | 32,101 |
| Mr SB Wolfe | Inventory purchases | (iii) | 26,312 |

(i) The Company used the secretarial and consulting services of a related entity to Mr PS Tang to provide company secretarial services, advice over the sale of Stanton Prospect and tax consolidation matters. Amounts were billed based on normal market rates for such services and were due and payable under normal payment terms.

(ii) The Company used the consulting services of a related entity to Mr TR Allen advice over the issue of debentures and convertible notes. Amounts were billed based on normal market rates for such services and were due and payable under normal payment terms.

(iii) The Company purchased various chemicals from Tennant Limited, a company of which Mr SB Wolfe is a director. Amounts were billed based on normal market rates for such supplies and were due and payable under normal payment terms.

There were no assets and liabilities arising from the above transactions as at 30 June 2004.

## 28 Director and executive disclosures (cont'd)

### *(d) Directors' transactions in convertible notes*

On 14 November 2003 ($200,000), 17 December 2003 ($700,000) and 18 December 2003 ($100,000) Tennant (2000) Pty Limited, a director related entity of Mr. SB Wolfe, subscribed $1,000,000 convertible notes issued by the Company. Within 365 days from the date of issue, the notes can be converted into ordinary shares of the Company at the conversion rate of $0.04 per ordinary share. The notes can also be converted into ordinary shares of the Company during the second 365 days from date of issue. The conversion rate during this period is $0.043 per ordinary share. The unconverted notes will be redeemed 912 days after the issue date. The interest paid and payable to Tennant (2000) Pty Limited during the financial year was $64,243 (2003: $nil). The notes issued are classified as compound financial instruments. For details refer note 1(w).

Liabilities arising from the above transactions as at 30 June 2004:

| | 30 June 2004 $ |
|---|---|
| Non-current liabilities | |
| Interest bearing liabilities | |
| Convertible notes | 800,000 |
| | |
| Contributed equity | |
| Redeemable convertible notes | 200,000 |
| | 1,000,000 |

### *(e) Directors' transactions in loan*

On 20 August 2003 Chemmet Pty Limited, a director related entity of Dr. LD Jayaweera, subscribed $500,000 debentures issued by the Company. The face value of each debenture is $1. The debentures have a term of three years from the date of issue, and attract an interest rate of 12% per annum, to be paid in arrears, semi-annually on 31 March and 30 September, respectively. The debenture holders have a fixed and floating charge over the assets of the company and its controlled entities. The interest paid and payable to Chemmet Pty Limited during the financial year was $51,780 (2003: $nil).

On 3 February 2003 Lenvat Pty Limited, a director related entity of Mr. TR Allen, subscribed $200,000 debentures issued by the Company. The face value of each debenture is $1. The debentures have a term of three years from the date of issue, and attract an interest rate of 12% per annum, to be paid in arrears, semi-annually on 31 March and 30 September, respectively. The debenture holders have a fixed and floating charge over the assets of the company and its controlled entities. The interest paid and payable to Lenvat Pty Limited during the financial year was $9,732 (2003: $nil).

Liabilities arising from the above transactions as at 30 June 2004:

| | 30 June 2004 $ |
|---|---|
| Non-current liabilities | |
| Interest bearing liabilities | |
| Debenture | 700,000 |

## 29 Non-director related parties

The classes of non-director related parties are:

- wholly owned controlled entities (refer Notes 21); and
- associates (refer Notes 10 and 23).

***Transactions***

All transactions with non-director related parties are on normal terms and conditions.

***Wholly-owned group***

Details of interests in wholly-owned controlled entities are set out at Note 21. Details of dealings with these entities are set out below:

### *Loans*

Loans between entities in the wholly-owned group are interest free and repayable on demand. The aggregate amounts receivable from/payable to wholly-owned controlled entities of the Company at reporting date are:

| | The Company | |
|---|---|---|
| | **2004** **$** | **2003** **$** |
| **Non-current** | | |
| Loans receivable | 7,022,654 | 7,449,027 |
| Loans payable | 6,047,769 | 4,449,509 |

### *Loans receivable*

| | 2004 $ | 2003 $ |
|---|---|---|
| Balance at the beginning of the year | 7,449,027 | 5,837,692 |
| Increase/(decrease) in loans to controlled entities | (426,373) | 1,611,335 |
| Balance at the end of year | 7,022,654 | 7,449,027 |

### *Loans payable*

| | 2004 $ | 2003 $ |
|---|---|---|
| Balance at the beginning of the year | 4,449,509 | 3,510,969 |
| Increase in loans from controlled entities | 1,598,260 | 938,540 |
| Balance at the end of year | 6,047,769 | 4,449,509 |

## 30 Additional financial instruments disclosure

### *(a) Interest rate risk*

The consolidated entity's exposure to interest rate risk and the effective weighted average interest rates on classes of financial assets and financial liabilities is set out below:

| | Note | Weighted avg interest rate | Floating interest rate | Fixed interest maturing in: | | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| | | | | 1 year or less | 1 to 5 years | | |
| **2004** | | | $ | $ | $ | $ | $ |
| *Financial assets* | | | | | | | |
| Cash | 31(a) | 3.8% | 1,262,046 | - | - | - | 1,262,046 |
| Receivables | 9 | - | - | - | - | 3,315,141 | 3,315,141 |
| | | | 1,262,046 | - | - | 3,315,141 | 4,577,187 |
| *Financial liabilities* | | | | | | | |
| Payables | 15 | - | - | - | - | 1,444,324 | 1,444,324 |
| Lease liabilities | 16,22 | 8.7% | - | 72,801 | 80,623 | - | 153,424 |
| Debentures | 16 | 12% | - | - | 1,800,000 | - | 1,800,000 |
| Convertible Notes | | 9.25% | - | - | 1,000,000 | - | 1,000,000 |
| Employee benefits | 24 | 5.95% | 576,141 | - | - | - | 576,141 |
| | | | 576,141 | 72,801 | 2,880,623 | 1,444,324 | 4,973,889 |
| **2003** | | | | | | | |
| *Financial assets* | | | | | | | |
| Cash | 31(a) | 4.4% | 1,261,173 | - | - | - | 1,261,173 |
| Receivables | 9 | - | - | - | - | 1,368,666 | 1,368,666 |
| | | | 1,261,173 | - | - | 1,368,666 | 2,629,839 |
| *Financial liabilities* | | | | | | | |
| Payables | 15 | - | - | - | - | 974,694 | 974,694 |
| Lease liabilities | 16,22 | 8.7% | - | 74,384 | 155,536 | - | 229,920 |
| Debentures | 16 | 12% | - | - | 700,000 | - | 700,000 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Employee benefits | 24 | 5.4% | 529,934 | - | - | - | 529,934 |
| | | | 529,934 | 74,384 | 855,536 | 974,694 | 2,434,548 |

## 30 Additional financial instruments disclosure (cont'd)

### *(b) Credit risk*

Credit risk represents the loss that would be recognised if counterparties failed to perform as contracted. The credit risk of financial assets, excluding investments, of the consolidated entity which have been recognised on the statement of financial position, is the carrying amount, net of any provision for doubtful debts.

The consolidated entity was materially exposed to four customers at balance date. The exposure as a percentage of trade debtors:

- Exide Technologies 31.9%
- Mining & Chemical Products Ltd 18.3%
- Lewer Corporation 15.8%
- One Steel NSW Pty Ltd 13.4%

### *(c) Net fair values of financial assets and liabilities*

The net fair values of financial assets and liabilities approximate their carrying amounts.

## 31 Notes to the statements of cash flows

### *(a) Reconciliation of cash*

For the purposes of the statements of cash flows, cash includes cash on hand and at bank and short term deposits at call. Cash as at the end of the financial year as shown in the statements of cash flows is reconciled to the statements of financial position as follows:

| | Consolidated | | The Company | |
|---|---|---|---|---|
| | 2004 $ | 2003 $ | 2004 $ | 2003 $ |
| Short term deposits | 1,262,046 | 1,261,173 | 708,073 | 1,027,780 |
| Total cash held | 1,262,046 | 1,261,173 | 708,073 | 1,027,780 |

*Security over cash*

A term deposit for $250,000 has been issued as security in respect of a bank guarantee issued to a customer and not available to be used by the consolidated entity.

## 31 Notes to the statements of cash flows (cont'd)

### *(b) Reconciliation of profit/(loss) from ordinary activities after income tax to net cash provided by/(used in) operating activities*

| | Consolidated 2004 $ | Consolidated 2003 $ | The Company 2004 $ | The Company 2003 $ |
|---|---|---|---|---|
| Loss from ordinary activities after income tax | (989,655) | (4,452,966) | (507,348) | (5,005,486) |
| Add/(less) non-cash items: | | | | |
| ■ Amortisation | 244,644 | 264,898 | - | 21,468 |
| ■ Depreciation | 1,245,738 | 1,087,255 | 51,075 | 13,534 |
| ■ Retirement of fixed assets | 76,718 | - | 2,592 | - |
| ■ Write back provision for investment | - | - | (2,111,481) | - |
| ■ Diminution in value of investments | - | - | - | 3,248,864 |
| ■ Provision for loans to controlled entities | - | - | 1,483,731 | - |
| ■ Transfer of assets | - | (186,752) | - | (1,512) |
| Add/(less) items classified as investing/financing activities: | | | | |
| ■ Lease payments | 66,985 | - | 49,081 | - |
| ■ Loss/(profit) on sales of property, plant and equipment | - | (13,218) | - | (8,804) |
| Net cash provided by/(used in) operating activities before changes in assets and liabilities | 644,430 | (3,300,783) | (1,032,350) | (1,731,936) |
| Changes in assets and liabilities adjusted for effects of purchase and disposal of controlled entities during the financial year: | | | | |
| ■ Decrease/(increase) in inventories | 134,621 | (100,875) | (4,309) | - |
| ■ (Increase)/decrease in receivables | (1,946,476) | 600,283 | (998,558) | 267,891 |
| ■ Increase/(decrease) in payables | 116,860 | (53,851) | 488,313 | (185,629) |
| ■ (Decrease)/increase in provisions | (358,948) | (819,851) | (81,330) | 19,251 |
| Net cash used in operating activities | (1,409,513) | (3,675,077) | (1,628,234) | (1,630,423) |

## 32 Deed of cross guarantee

Pursuant to ASIC Class Order 98/1418 (as amended) dated 13 August 1998 the wholly owned subsidiaries listed below are relieved from the Corporations Act 2001 requirements for preparation, audit and lodgement of financial reports, and directors' report.

It is a condition of the Class Order that the Company and each of the subsidiaries enter into a Deed of Cross Guarantee. The effect of the Deed is that the Company guarantees to each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the Corporations Act 2001. If a winding up occurs under other provisions of the Act 2001, the Company will only be liable in the event that after six months any creditor has not been paid in full. The subsidiaries have also given similar guarantees in the event that the Company is wound up.

The subsidiaries subject to the Deed are:

- Hydromet Operations Limited;
- Hydromet Operations (Southern) Limited;
- Hydromet Operations (Tasmania) Pty Limited;
- Hydromet Operation (NT) Pty Limited;
- Enviromet Operations Pty Limited; and
- Hyrdomet Corporation Debenture Nominees Pty Limited.

A consolidated statement of financial performance and consolidated statement of financial position, comprising the Company and subsidiaries which are a party to the Deed, after eliminating all transactions between parties to the Deed of Cross Guarantee, at 30 June 2004 is set out on the following page.

## 32 Deed of cross guarantee (cont'd)

| | Consolidated 2004 $ | Consolidated 2003 $ |
|---|---|---|
| **Statement of financial performance** | | |
| Loss from ordinary activities before related income tax expense | (307,491) | (4,267,426) |
| Income tax expense relating to ordinary activities | (33,182) | - |
| Loss from ordinary activities after related income tax expense | (340,673) | (4,267,426) |
| Accumulated losses at beginning of the year | (55,624,626) | (50,953,759) |
| Dividends recognised during the year | - | (403,441) |
| Accumulated loss at the end of the year | (55,965,299) | (55,624,626) |
| | | |
| **Statement of financial position** | | |
| Cash assets | 999,332 | 1,203,301 |
| Receivables | 1,845,385 | 400,432 |
| Inventories | 117,492 | 117,104 |
| **Total current assets** | 2,962,209 | 1,720,837 |
| | | |
| Receivables | 831,480 | 1,402,242 |
| Investments | 3,808,526 | 1,662,277 |
| Property, plant and equipment | 6,689,714 | 7,358,668 |
| Intangibles | 663,390 | 908,034 |
| **Total non-current assets** | 11,993,110 | 11,331,221 |
| **Total assets** | 14,955,319 | 13,052,058 |
| | | |
| Accounts payable | 1,240,814 | 664,196 |
| Interest bearing liabilities | 72,801 | 74,384 |
| Provisions | 530,474 | 907,789 |
| **Total current liabilities** | 1,844,089 | 1,646,369 |
| | | |
| Interest bearing liabilities | 2,880,623 | 855,536 |
| Provisions | 104,228 | 78,301 |
| Other liabilities | 2,585,864 | 2,590,664 |
| **Total non-current liabilities** | 5,570,715 | 3,524,501 |
| **Total liabilities** | 7,414,804 | 5,170,870 |
| **Net assets** | 7,540,515 | 7,881,188 |
| | | |
| Contributed equity | 63,000,127 | 63,000,127 |
| Reserves | 505,687 | 505,687 |
| Accumulated losses | (55,965,299) | (55,624,626) |
| **Total equity** | 7,540,515 | 7,881,188 |

## Directors' declaration

1 In the opinion of the directors of HydroMet Corporation Limited ("the Company"):

(a) the financial statements and notes, set out on page 19 to 65, 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 2004 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date; and

(ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

(iii) 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 There are reasonable grounds to believe that the Company and the subsidiaries identified in Note 32 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those controlled entities pursuant to ASIC Class Order 98/1418.

Signed in accordance with a resolution of the directors:

Dr Lakshman Jayaweera
Director

Dated at Wollongong this 27th day of August 2004.

## Independent audit report to members of Hydromet Corporation Limited

## Scope

### *The financial report and directors' responsibility*

The financial report comprises the statements of financial position, statements of financial performance, statements of cash flows, accompanying notes to the financial statements, and the directors' declaration set out on pages 23 to 70 for both Hydromet Corporation Limited (the "Company") and Hydromet Corporation Limited and its controlled Entities (the Consolidated Entity"), for the year ended 30 June 2004. The Consolidated Entity comprises both the company and the entities it controlled during that 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.

### *Independence*

In conducting our audit, we followed applicable independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001.

### *Audit opinion*

In our opinion, the financial report of Hydromet Corporation Limited is in accordance with:

a) the Corporations Act 2001, including:

   (i) giving a true and fair view of the Company's and Consolidated Entity's financial position as at 30 June 2004 and of their performance for the financial year ended on that date; and

   (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

b) other mandatory professional reporting requirements in Australia.

KPMG

KPMG

C Hollis

Chris Hollis
*Partner*

Sydney
Dated the 27th day of August 2004

## ASX additional information

Additional information required by the Australian Stock Exchange Limited Listing Rules and not disclosed elsewhere in this report is set out below.

## Shareholdings (as at 19 August 2004)

### *Substantial shareholders*

The number of shares held by the substantial shareholders are set out below:

| Shareholder | Ordinary |
|---|---|
| National Nominees Limited | 19,421,292 |

### *Voting rights*

*Ordinary shares*

As at 19 August 2004 there were 2,458 holders of the ordinary shares of the Company. Refer to Note 18.

*Options*

Refer to Note 18.

*Redeemable convertible notes*

Refer to Note 18.

### *Distribution of equity security holders*

| | Number of equity security holders | | |
|---|---|---|---|
| **Category** | **Ordinary shares** | **Options** | **Convertible Notes** |
| 1 - 1,000 | 316 | - | - |
| 1,001 - 5,000 | 383 | - | - |
| 5,001 - 10,000 | 209 | - | - |
| 10,001 - 100,000 | 1,135 | - | - |
| 100,001 and over | 415 | 5 | 1 |
| | 2,458 | 5 | 1 |

The number of shareholders holding less than a marketable parcel is 1,033.

*On-market buy-back*

There is no current on-market buy-back.

### *Twenty largest shareholders*

| Name | | Number of ordinary shares held | Percentage of capital held |
|---|---|---|---|
| 1 | National Nominees Limited | 19,421,292 | 7.19 |
| 2 | Chemmet Pty Limited | 10,355,965 | 3.83 |
| 3 | Picasso Holdings International Limited | 8,500,000 | 3.15 |
| 4 | Twynam Commodities Pty Limited | 7,500,000 | 2.78 |
| 5 | Leet Investments Pty Limited | 6,600,000 | 2.44 |
| 6 | Mrs Selina Wu | 5,910,859 | 2.19 |
| 7 | Leet Investments Pty Limited (Superannuation Fund A/C) | 4,200,000 | 1.55 |
| 8 | Linkenholt Pty Limited (Grant Austin Family A/C) | 3,995,736 | 1.48 |
| 9 | Merrill Lynch (Australia) Nominees Ltd | 3,723,782 | 1.38 |
| 10 | Chemmet Pty Limited (Super Fund A/C) | 3,510,000 | 1.30 |
| 11 | Mr Gordon Menzies Wilson | 3,078,815 | 1.14 |
| 12 | Citicorp Nominees Pty Limited | 3,050,377 | 1.13 |
| 13 | Igera Pty Limited (Ash A/C) | 2,800,000 | 1.04 |
| 14 | International Investments Enterprises Limited | 2,357,683 | 0.87 |
| 15 | TSN Pty Ltd | 2,250,000 | 0.83 |
| 16 | Lenvat Pty Ltd | 2,200,000 | 0.81 |
| 17 | Jodeen Securities Pty Limited | 2,097,642 | 0.78 |
| 18 | Mr John Raymond McDonald & Mrs Anna Margaret McDonald | 2,000,000 | 0.74 |
| 19 | Wightholme Nominees Pty Ltd (P F Burke Group S/F A/C) | 2,000,000 | 0.74 |
| 20 | Ms Therese Mary Nichols | 1,950,000 | 0.72 |
| | | 97,502,151 | 36.09 |

### *Unquoted equity securities*

*Options*

As at 18 August 2004, options over ordinary shares were held by:

| | Options over ordinary shares | Exercise price | Expiry date |
|---|---|---|---|
| Mr TR Allen | 2,000,000 | $0.08 | 31 March 2007 |
| Dr LD Jayaweera | 2,000,000 | $0.08 | 31 March 2007 |
| Mr SH Kwan | 2,000,000 | $0.08 | 31 March 2007 |
| Mr PS Tang | 2,000,000 | $0.08 | 31 March 2007 |
| Mr GW Wrightson | 2,000,000 | $0.08 | 31 March 2007 |

*Redeemable convertible notes*

Tennant (2000) Pty Limited holds 1,000,000 redeemable convertible notes. This holding represents 100% of the total number on issue. Tennant (2000) Pty Limited is a director related entity of Mr SB Wolfe, a director of Hydromet Corporation Limited.