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Managing our R&D strategically

Accelerating the delivery of products and services

AWI refocused its business during the year to accelerate the delivery of products and services to the Australian woolgrower and global apparel business.

The most significant changes were to the former AWI portfolios of *Textile Technology* and *Trade Development* as AWI moves to an apparel product delivery model. The two portfolios were refocused and renamed under the titles of *Product Development* and *Product Marketing*.

We have been progressively changing the business/commercial culture of the off-farm part of the company from "R&D" to "Australian Merino apparel development and marketing". This has been done by working closely with the retail industry, recruiting experienced staff from that sector and aligning our activity with the apparel development calendar. This change is being driven through our global network in China, United States, Italy, Hong Kong and India.

A brief description of the new business model is as follows:

- We work with the apparel industry to develop innovative Merino wool products that they would not otherwise easily obtain.
- The products we develop add value to the apparel industry because they capitalise on the unique characteristics of Australian Merino wool.

- We provide support for product development and product marketing.
- We will establish a business-to-business brand that conveys AWI's value proposition and the value of Australian Merino to the apparel industry.

The *Wool Production* portfolio is the most mature of the portfolios and has largely been unchanged. It has continued to drive innovation into the woolgrower business through genetic improvements, business tools, management programs such as Land Water and Wool and the ever important mulesing and wool harvesting alternatives.

Revised set of programs:

The following programs will guide AWI investment into the future:

Product Development:

Knitwear

Wovens

Non-apparel

Wool Science, Processing and Education

Product Marketing:

B2B Product Marketing

Supply Chain and Trade Development

Wool Production:

Sustainable Production Systems

Animal Health and Welfare

Sheep Productivity

Special Project: Wool Harvesting

Corporate Affairs:

Stakeholder Communications

Marketing Communications

Fashion Communications

Industry and Government Relations

Collaboration with other R&D organisations

On-farm

Forming relationships and collaborating (financially and intellectually) with other R&D organisations on projects continued this year to ensure we deliver the best return for Australian woolgrowers.

During 2005/06, AWI was involved in collaborations with research bodies including rural research and development corporations (RDCs), government departments of agriculture, CSIRO, universities and commercial partners.

AWI partnered with MLA during the year to conduct a 'Making more from Merinos' forums in Broken Hill – attended by over 60 sheep producers and woolgrowers.

Collaborations in which AWI made a significant co-investment during the year included:

- the Sheep Genomics program, with MLA and nine other partners aiming to discover sheep genes and their functions, and to provide new tools to producers;
- Sheep Genetics Australia with MLA which will allow breeders to achieve higher rates of genetic gain in their flocks;
- the Land, Water & Wool natural resource management program with LWA;
- the Invasive Animal CRC to continue R&D on a new toxin for the control of feral dogs and foxes, and to keep the number of rabbits low with MLA;

- the Meat and Wool New Zealand financial contribution towards Australia's push to make shearing and wool handling easier, safer and more efficient;
- Pasture Australia, a new investment in pastures with MLA, Dairy Australia, GRDC and the Rural Industries Research and Development Corporation;
- the EverGraze project to help producers in the high rainfall zone develop new farming systems, with MLA;
- the development of new pasture legumes through National Annual Pasture Legume Improvement Program (NAPLIP), with the GRDC, CSIRO, five state departments of agriculture (Qld, NSW, Vic, SA and WA), and the Universities of Adelaide and WA; and
- Grain & Graze, a research and extension program for mixed farms in southern Australia with MLA, GRDC and LWA.

AWI is collaborating with numerous organisations on projects to combat flystrike, such as the injectable replacement to mulesing project with organisations including Medical International Technologies (Canada) and the University of Adelaide. Other projects include the blowfly genome project with the University of Melbourne and Massey University (NZ), biocontrol methods for blowfly control with the Department of Primary Industries and Fisheries Queensland, and integrated parasite management with the University of New England, Department of Agriculture and Food Western Australia, the

University of Melbourne and the Department of Primary Industries and Fisheries Queensland. For further details, see AWI's *Battling the blowfly* Insight factsheet.

Off-farm

As has been outlined throughout this annual report, a key strategy of AWI has been to work directly with key apparel companies around the world to increase the demand for Australian Merino wool. AWI has the textile technology and market know-how to help apparel companies get an edge in the marketplace with Australian Merino wool.

We are targeting leading and influential companies in the key markets – in the processing and manufacturing powerhouse of China, in the influential trend setting centres of Europe, in the global retail brand and sportswear hub of the US, in emerging markets such as India, and in the world knitwear centre of Hong Kong.

We are building partnerships with these companies, the decision-makers in world apparel, and encouraging them to take-up new Australian Merino fabrics, yarns and products that will give their business an edge, which can only be good for Australian Merino producers.

The Woolmark Company (TWC) is often a key participant in AWI projects and received funding from AWI during 2005/06 on a range of projects to help get wool to the world. TWC also provided market intelligence services to AWI such as the Review and Outlook for Fine Wool and Mid-Micron and Broader Wool, which are available free to AWI shareholders.

AWI also collaborated in 2005/06 with scientists, researchers and companies in fundamental wool science and new wool processing technologies to improve efficiency and the quality of the end product. These organisations included CSIRO, Canesis in New Zealand and the German wool research institute Deutsches Wollforschungsinstitut (DWI). Research in fundamental wool science underpins a whole range of technical developments in wool processing and textile design.

The China Australian Wool Innovation Network (CAWIN) initiative established by AWI and Deakin University to build wool textile technical expertise in China continued. The annual enrolment on wool programs at the five CAWIN universities by undergraduate students increased from 50 in 2003 to 128 in 2006, and masters students from 18 in 2003 to 52 in 2006.

Intellectual property

Intellectual Property (IP) as generated through AWI-funded research and development is an important company asset, and AWI's primary objective is to apply its IP for the maximum benefit of Australian woolgrowers, which requires its rapid and widespread adoption and/or commercialisation.

Revenue from IP is not a priority for AWI, but when projects do generate revenue, AWI expects to receive royalties in proportion to its investment. Royalty income contributed \$585,450 to AWI in 2005/06.

During 2005/06, AWI acting solely or jointly with various research partners, lodged or acquired five patents, seven trademarks and abandoned two patents. A table of registered IP which is owned by AWI or in which AWI has an interest is included as Appendix C on page 108.

It is at the point where AWI's IP is delivered to the market that Australian woolgrowers' get the most benefit. AWI signed during 2005/06 the following 10 commercial contracts relating to industry partnership/licensing of research outcomes:

- Chlorine-free continuous shrink-resist treatment for wool loose stock and tops
- Novel self twist yarns using modified false twist spinning techniques to develop a range of knitted and woven apparel products
- Performance-plus protective clothing made from mid-micron Australian Merino fibre
- Commercial application for transfer of easy care oven bake technology for wool blend trousers
- Light weight, low pilling woollen knitwear by using PVA (polyvinyl alcohol) and compact yarn
- Australian Merino range of products that caters for the leisure/travel market in conjunction with Purely Merino
- A software package for an integrated web based wool supply chain management system that links all segments from woolgrower to brand managers
- The exploitation of rota-shear for the production of spare parts and consumables
- Novel knit fabric development and commercialisation – the development and commercialisation of a range of novel, low cost, wool-rich fabrics based on patented technology
- Performance-plus introducing new finished, fibre blends and chemical applications to wool to add value and exceed the requirements of the military, corporate, institutional and industrial sectors.

Responding to Australian Government priorities

Addressing Government challenges

The Australian Government is a major investor in the wool industry by providing statutory levy collection power plus taxpayer funds. The Australian Government has put the following six challenges to all R&D Corporations (RDCs) including AWI:

Is the RDC maximising R&D benefits to the industry?

Despite AWI being a relatively young RDC, during the past year we have delivered significant R&D results to woolgrowers by providing them with new products and practices to improve their on-farm productivity and profitability. Equally, we have been working with over 50 leading global apparel manufacturers, retailers and fashion designers to get more wool products into global markets to increase the demand for wool.

Is the RDC maximising adoption of R&D by the industry?

During the past year, as R&D projects started two to three years ago increasingly began to reach commercialisation stage, AWI refocused its business to accelerate the delivery of products and services to the Australian woolgrower and global apparel business. We continued to facilitate the adoption of R&D outcomes by woolgrowers through initiatives such as the national network of state grower extension programs.

Is the RDC working closely with other RDCs?

We continued our relationships and collaboration, financially and intellectually, with other R&D organisations during the year, including other RDCs such as Meat and Livestock Australia, Land and Water Australia and the Grains Research & Development Corporation – see the *Collaboration with other R&D organisations* section on page 36.

Is the RDC improving its current practices?

A major focus of the year for AWI was the continued refocusing of our programs to help ensure that the products and outputs from our textile related R&D projects get to market and increase the demand for wool. In the wool production area, we continually sought ways to create new on-farm solutions for woolgrowers to use on their enterprises. We also put in place a range of measures to improve our internal practices during the year such as improved project management.

Is the RDC communicating effectively with Government and industry?

We continued our positive relationships with those in Government and industry that influence wool industry policy, by meeting face-to-face, attendance at events and timely distribution of newsletters and other communications – see the report on the Corporate Affairs program on page 28.

Is the RDC the best model for Government and industry investment?

AWI is delivering significant outcomes for the wool industry. This is recognised by Australian woolgrowers who delivered a clear mandate for the continuance of wool R&D at WoolPoll 2003 in November 2003. Woolgrowers voted by a strong majority for continuation of the two per cent wool levy. This result has provided for a solid investment in the future of the Australian wool industry and we are confident that woolgrowers will continue to provide a firm endorsement of wool R&D at this year's WoolPoll.

Programs undertaken by AWI during 2005/06 aligned to the NRPs and RRDPs

National Research Priorities (NRP)	An Environmentally Sustainable Australia	Promoting and Maintaining Good Health (strengthening Australia's social & economic fabric)		
Rural Research & Development Priorities (RRDP)	Sustainable Natural Resource Management	Improving Competitiveness through a Whole of Industry Approach	Maintaining & Improving Confidence in the Integrity of Australian Agricultural, Food, Fish and Forestry Products	Improved Trade and Market Access
Textile Technology portfolio (now known as Product Development portfolio)				
Fundamental Wool Science				
Processing of Merino Fibre				
Merino Fibre in Fashion Markets				√
Merino as a Performance Fibre				√
Trade Development portfolio (now known as Product Marketing portfolio)				
Market Information		√		√
Market Development		√		√
Trade Access		√		√
Wool Production portfolio				
Profitable Grazing for Wool Sheep	√	√	√	
Natural Resource Management	√			
Animal Health and Welfare			√	
Molecular Genetics				
Applied Genetics and Wool Quality		√		
Wool Harvesting				
Education and Adoption		√		
Corporate Affairs portfolio				
Communications – Corporate		√	√	
Communications – Fashion/Retail/Trade		√	√	√
Industry Affairs		√	√	

Frontier Technologies for Building and Transforming Australian Industries		Safeguarding Australia
Use of Frontier Technologies	Creating an Innovative Culture	Protecting Australia from Invasive Diseases and Pests
√		
√		
√		
√		
	√	
		√
√		√
√		
√		
√		
	√	
	√	
	√	

Alignment to research priorities

The Rural R&D priorities (RRDPs) assist Research and Development Corporations to achieve the objectives of the *Primary Industries and Energy Research and Development Act 1989*.

These priorities provide specific guidance on issues of strategic significance to rural industries.

These priorities are consistent with and reflect the Government's National Research Priorities (NRPs) that were announced by the Prime Minister on 5 December 2002.

This table summarises how the programs undertaken by AWI during 2005/06 align to the RRDPs and the NRPs. Some AWI programs are aligned to more than one NRP and RRDP.

Corporate review

Corporate governance

The AWI Board believes that a strong corporate governance culture throughout AWI enhances performance and maximises the Company's ability to achieve its primary mission of increasing the long-term profitability of Australian woolgrowers.

Where appropriate, the Board has adopted the Australian Stock Exchange (ASX) Corporate Governance Council's Principles of Good Corporate Governance and Best Practice Recommendations. While these ASX Corporate Governance Principles are not binding on AWI as an un-listed public company, the AWI Board is committed to adopting them in broad terms as befitting a not-for-profit company.

The Board approved 30 June 2005 a Corporate Governance Statement which details AWI's, position in relation to the following 10 core principles contained within the ASX Corporate Governance Principles:

- **Principle 1:** Lay solid foundations for management of oversight
- **Principle 2:** Structure – The Board to add value
- **Principle 3:** Promote ethical and responsible decision making
- **Principle 4:** Safeguard integrity in financial reporting
- **Principle 5:** Make timely and balanced disclosure
- **Principle 6:** Respect the rights of shareholders
- **Principle 7:** Recognise and manage risk
- **Principle 8:** Encourage enhanced performance
- **Principle 9:** Remunerate fairly and responsibly
- **Principle 10:** Recognise the legitimate interests of stakeholders

AWI's Corporate Governance Statement is available on the Company's website www.wool.com.au.

AWI's corporate governance obligations are found in:

- AWI's Constitution, approved by shareholders, 21 November 2003
- Statutory Funding Agreement, 31 August 2004
- Corporate Governance Policy, approved by the Board, 17 June 2004
- Code of Conduct – Obligations to Stakeholders, approved by the Board 17 June 2004, amended 24 May 2006
- Board Charter, approved by the Board, 17 March 2005
- Code of Conduct – Directors and Officers, approved by the Board, 17 March 2005
- Charters of the Committees of the Board, approved by the Board, 17 March 2005
- Communications Strategy, approved by the Board, 16 February 2006
- Rules and Procedures governing election of Directors, approved by the Board 17 February 2005, amended 24 May 2006
- Financial Authorities, approved by the Board, April 2005.

Corporate governance documents are available on the AWI website at www.wool.com.au/CorporatePublications

The Company has not provided any director with an indemnity in the past 12 months. As approved by the shareholders, Directors and Officers insurance has been arranged and the premium paid.

The Board

The Board continued to meet regularly during 2005/06, concentrating on core functions including:

- enhancing corporate governance systems, managing risk and threats to the industry and providing transparent, balanced reporting of Company operations to shareholders; and
- building a portfolio of research, development, innovation and marketing programs and projects aimed at enhancing the long-term profitability of woolgrowers.

A number of AWI Board committees continue to monitor and guide specific activities. These committees assist the Board to effectively implement, monitor and enforce the Corporate Governance Principles throughout the Company.

Board Committees

At 30 June 2006, there were five Board committees:

Finance and Audit Committee *chaired by Brian van Rooyen*

The Committee's main role is to:

- assist the Board in managing its responsibilities relating to all financial and legal matters;
- ensure the Company's financial controls are working effectively; and
- monitor and guide the Company's approach to corporate governance and risk management.

Remuneration and Appointments Committee *chaired by Brian van Rooyen*

The Committee sets executive remuneration, terms of employment and conditions, staffing policies and staffing levels as well as reviewing Board and management performance.

Intellectual Property and Commercialisation Committee *chaired by Hugh Nivison*

The Committee's major role is to provide policy direction for the management of AWI's Intellectual Property (IP) portfolio; see the schedule of IP in Appendix C.

Falkiner Memorial Field Station Committee *chaired by Chris Abell*

The Committee's role is to provide oversight and guidance of the major capital redevelopment at the Falkiner Memorial Field Station. This Committee was disbanded as at 30 June 2006, its objectives satisfactorily completed.

Integration Committee *chaired by Ian McLachlan*

This Committee, has been appointed for a limited purpose and time to advise the Board on possible options to form an alliance between AWI and Australian Wool Services Limited.

Statutory Funding Agreement

AWI is obliged to contract with the Federal Government on the use of levy monies. This contract is called the Statutory Funding Agreement (SFA). The current SFA is operative 2004 to 2007 and requires AWI to allocate funds to authorised research, development, innovation and marketing activities to ensure that projects AWI invests in are to the benefit of Australian woolgrowers, and that projects are efficient, effective and ethical.

The SFA is available on the AWI website.

Audit and risk

AWI has continued to strengthen its internal controls and level of accountability, and engages the services of three of Australia's leading professional services firms. **PricewaterhouseCoopers** is engaged to conduct the external audit and report to shareholders. **Deloitte Touche Tohmatsu** conducts internal audits on a regular basis, reporting on internal controls and processes and the day-to-day management of AWI to the Finance and Audit Committee. **Ernst & Young** provides advice on taxation and other related matters to AWI management.

AWI has also conducted a number of risk assessments in conjunction with the internal auditors and its insurance broker, Jardine Lloyd Thompson. Appropriate insurances have been effected and AWI has developed a risk management plan.

AWI staff

During 2005/06, the Company continued with the development and implementation of an integrated human resources strategy. The purpose of the strategy is to ensure that the Company has the right people with the skill sets required for AWI to meet its Strategic Plan. With the pool of skilled people contracting into the future, AWI is expanding its staff training programs. As a result, several new policies were implemented, including:

Training Courses

- Project management training
- Negotiation skills training
- Time management training
- Occupational health and safety (OHS) committee training
- Presentation skills training.

Policies

- Internet & email policy
- Workplace surveillance policy
- Overseas travel and vaccination policy.

During 2005/06, AWI also continued with various established human resource initiatives including:

- OHS, with the OHS Committee conducting OHS audits and discussing relevant OHS topics. This is to ensure the health and safety of all employees in AWI designated workplaces, which is particularly relevant for AWI's Falkiner Memorial Field Station; employees, contractors and visitors;
- regular performance reviews and the establishment of a new performance management system, including new performance appraisal forms and employee development plan form used to gather information on the training and development needs of employees;
- new induction program which includes a comprehensive introduction to employees, company policies, OHS and IT systems; and
- recruitment and selection of the best available staff.

AWI staff statistics

- At 30 June 2006 AWI had a total of 85 staff members.
- Eighty five per cent have tertiary qualifications of various disciplines.
- Fifty seven per cent of AWI staff are female.
- AWI employees are located in AWI offices in Sydney, Melbourne, Geelong, Deniliquin, Gosford and overseas in Shanghai, Hong Kong, New York, New Delhi and Italy.

Chief Executive Officer:

DR LEN STEPHENS

Dip Agr Sci, BVSc, MSc, PhD

Len Stephens was appointed as CEO in April 2003, with the responsibility to lead the Company in the delivery and commercialisation of its research, development, innovation and marketing on behalf of Australian woolgrowers. Len has an extensive background in rural research and development and came to AWI after five years as General Manager for Livestock Production Innovation at Meat and Livestock Australia. Previously he held senior positions with the then Meat Research Corporation and Agriculture Victoria, including as foundation Director of the Victorian Institute of Animal Science. Len holds Australian tertiary qualifications in both Agricultural and Veterinary Sciences and was awarded Master of Science and Doctorate of Philosophy degrees from the University of Guelph, Canada.

Deputy Chief Executive Officer and Company Secretary:

LES TARG

Les Targ is responsible for developing and implementing the AWI corporate services of legal, contracting, IP management, company secretarial and human resources. Les is also responsible for the wool harvesting program and crisis management. Les has 25 years of senior management experience as a company director, CEO and senior executive. Prior to joining AWI, Les held senior executive positions in the Australian defence and aerospace industries,

including ten years with ADI Limited, a high technology defence systems and engineering company. He is currently a Director of Recoiless Technologies International Limited.

**General Manager
Corporate Affairs:**

MATTHEW FLUGGE

BBus, Grad Cert Sust Ag

Matthew Flugge manages the Corporate Affairs portfolio, responsible for communications and industry and government relations. Prior to his appointment in February 2005, Matthew was with AWI for two years undertaking the role of Industry and Government Relations Manager. Before joining AWI, Matthew was Executive Director of the Victorian Farmers Federation (VFF) Pastoral Group, with responsibility for industry and government matters relating to the wool, cattle, sheepmeat and goat industries across Victoria and Australia. Matthew has also had extensive experience in agricultural policy and industry initiatives and has held senior positions with the WA Minister for Agriculture and the WA Department of Agriculture.

**General Manager Wool
Production:**

IAN ROGAN

B Rural Science (Hons)

Ian Rogan oversees the Wool Production portfolio which includes the Falkiner Memorial Field Station, managing AWI's investments in the key on-farm areas of genetic improvement technologies, pasture development, fibre specification, animal health and natural resource management. Ian has significant experience in both agricultural research and commercial agriculture.

He was previously a director and senior consultant of agricultural consultancy Hassall and Associates for 12 years. Prior to this, Ian was a regional director of research with NSW Agriculture and also principal research scientist with the South Australian Department of Agriculture where he headed the state's centre of excellence for sheep and wool research.

**General Manager
Product Marketing:**

PASCAL SENKOFF

Pascal Senkoff is responsible for AWI's Product Marketing portfolio, which aims to commercialise wool innovations and work with Government and industry to help reduce trade barriers. Pascal has 16 years experience in the wool textile trade and prior to joining AWI was Greater China General Manager for Chargeurs wool. He was responsible for industrial and trading activities for a region that included Greater China, Japan, Korea, Indonesia, India and Australia. Prior to working in China, Pascal was based at Chargeurs in Japan, where he was responsible for starting up the Chargeurs Interlining business.

General Manager Finance:

DAVID SMULLEN

BA, CA, ACA

David Smullen manages the company's Finance division and is also responsible for developing and implementing the AWI corporate services of audit, risk management, IT systems and office services. David has extensive experience in financial management, having worked in senior financial roles over the past 15 years in a number of industries including publishing,

property, telecommunications and medical research. Prior to joining AWI, David was Chief Financial Officer of Ventracor Limited, a listed research company.

**General Manager
Product Development:**

GRAHAM STEWART

(Until August 2006)

Graham Stewart has responsibility for managing the operations of the Product Development team, including the development of new wool products and processes, fundamental wool science and the marketing of wool innovations to designers, manufacturers and retailers. Prior to joining AWI in June 2005, Graham had his own consultancy company working with a number of leading international textile businesses. He previously worked for Michell Australia, managing operations in Europe before heading up the company's marketing from Adelaide. Graham began his career in the UK with the Brook Group, Europe's largest dyer, and as a divisional director for the textile consumer brand house Dawson International PLC in the UK, Europe and United States.

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Directors' report

Your directors present their report on the consolidated entity (referred to hereafter as the Group) consisting of Australian Wool Innovation Limited and the entities it controlled at the end of, or during, the year ended 30 June 2006.

Directors

The following persons were directors of Australian Wool Innovation Limited during the whole of the financial year and continue to hold office at the date of this report.

The Hon I M McLachlan AO

Mr B P van Rooyen

Dr C J Abell

Dr K J Bell

Mr W B Merriman

Mr H P Nivison

Mr P S Sykes

Information on directors and their experience can be found on page 2.

Principal activities

The principal activity of Australian Wool Innovation Limited as recorded in its adopted strategic plan is to drive research, development, innovation and marketing that will increase the long term profitability of Australian wool growers. To achieve that mission, the Group receives funding from the Commonwealth Government of Australia by way of both a statutory levy imposed upon Australian wool growers and a capped matching contribution from the Government on behalf of Australian taxpayers.

Significant changes in the state of affairs

There have been no significant changes in the state of affairs of the Group during the financial year.

Review of operations and results

	2006	2005
	\$'000	\$'000
Revenue	57,035	64,999
(Deficit)/Surplus from ordinary activities	(25,643)	(13,498)

Matters subsequent to the end of the financial year

Australian Wool Innovation Limited and Australian Wool Services Limited have signed a Memorandum of Understanding on 27 July 2006, outlining their resolve to integrate the two companies. Both Boards will work to get shareholder and Federal Government approval to integrate by the end of 2006.

Likely developments and expected results of operations

Information on likely developments in the Group's operations and the expected results of operations have not been included in this report because the directors believe it would be likely to result in unreasonable prejudice to the Group.

Company secretary

The company secretaries are Mr L Targ (former CEO and senior executive in the defence and aerospace industries with particular experience in strategic business development, finance and audit) and Mr C Chapman (Barrister and Solicitor, Dip Law, Dip CM, Dip CD, FCIS, FICD, MBA).

Meetings of directors

The number of meetings of the company's board of directors and each board committee held during the year ended 30 June 2006, and the number of meetings attended by each director were:

Director	Committees											
	Full meeting of directors		Finance & Audit		Remuneration & Appointments		Intellectual Property & Commercialisation		Falkiner Memorial Field Station		Integration	
	A	B	A	B	A	B	A	B	A	B	A	B
I M McLachlan	12	11 ^{1*}	–	–	5	4 ¹	2	1 ¹	–	–	3	3*
B P van Rooyen	12	12	12	12*	5	5*	–	–	–	–	3	3
C J Abell	12	11 ¹	12	11 ¹	–	–	2	1 ¹	2	2*	3	3
K J Bell	12	12	–	–	–	–	–	–	2	2	–	–
W B Merriman	12	12	–	–	5	5	–	–	–	–	–	–
H P Nivison	12	12	12	12	–	–	2	2*	2	2	–	–
P S Sykes	12	12	–	–	–	–	2	2	–	–	3	3

A = Number of meetings held

B = Number of meetings attended

¹ = leave of absence granted

* = indicates chairman

Remuneration report

The objective of the Group's executive reward framework is to ensure reward for performance is competitive and appropriate for the results delivered. The framework aligns executive reward with achievement of strategic objectives and the innovation of value for shareholders, and conforms with market best practice for delivery of reward. The Board ensures that executive reward satisfies the following key criteria for good reward governance practices:

- competitiveness and reasonableness
- acceptability to shareholders
- transparency.

In consultation with external remuneration consultants, the Group has structured an executive remuneration framework that is market competitive, attracts and retains high calibre executives and is complimentary to the reward strategy of the organisation.

Directors' fees

All directors are non-executive, and fees and payments to directors reflect the demands which are made on, and the responsibilities of, the directors. All directors' fee payments are reviewed annually by the Board. The Board also has agreed to the advice of independent remuneration consultants to ensure directors' fees and payments are appropriate and in line with the market. The Chairman's fees are determined independently to the fees of directors based on comparative roles in the external market. The Chairman and other non-executive directors receive additional fees for their membership on committees.

Superannuation payments are made in accordance with the Superannuation Guarantee legislation to the director's choice of superannuation fund.

The Board undertakes an annual review of its performance and the performance of the Board committees against goals set at the start of the year. Bonuses are not payable to non-executive directors.

Details of the nature and amount of each element of the emoluments of each director of Australian Wool Innovation Limited are set out in the following table.

Directors' report (continued)

Non-executive directors of Australian Wool Innovation Limited

Name	Primary		Post-employment		Total
	Directors' base fee	Committee fees	Superannuation	Separation	
	\$	\$	\$	\$	
I M McLachlan, Chairman	103,000	15,450	10,661	–	129,111
B P van Rooyen	51,500	15,450	6,025	–	72,975
C J Abell	51,500	20,600	6,489	–	78,589
K J Bell	51,500	5,150	5,099 ⁽¹⁾	–	61,749
W B Merriman	51,500	5,150	5,099	–	61,749
H P Nivison	51,500	15,450	6,025	–	72,975
P S Sykes	51,500	10,300	5,562	–	67,362
Total	412,000	87,550	44,960	–	544,510

⁽¹⁾ Payment made to a related body corporate of the director as provision for superannuation benefits.

Executive pay

The executive pay consists of base pay, benefits and superannuation. These are structured at the executives' discretion as a total employment cost package, which may be delivered as a mix of cash and prescribed non-financial benefits. The value of non-financial benefits is calculated on the basis of the "total cost to the Group", so that the total expense to the Group is no more than it would have been had the Group paid cash salary plus statutory superannuation contributions.

Superannuation payments are made in accordance with the Superannuation Guarantee legislation to the executive's choice of superannuation fund. Australian Wool Innovation Limited does not offer a defined benefits retirement plan.

There are no guaranteed pay increases in any senior executive contracts.

Key management personnel compensation for the years ended 30 June 2006 and 2005 for executives is set out below. The key management personnel of Australian Wool Innovation Limited includes those executives who have the authority and responsibility for planning, directing and controlling the activities of the company, either directly or indirectly.

Directors are also classed as key management personnel. However the total remuneration of directors is separately disclosed above in greater detail and according excluded from the table below.

	2006	2005
	\$	\$
Short-term employee benefits	1,810,093	1,671,527
Post-employee benefits	138,138	143,552
	<u>1,948,231</u>	<u>1,815,079</u>

Executive Service Agreements

Remuneration and other terms of employment for the Executive Management Team are formalised in service agreements. These service agreements state a salary package (which is calculated on a total cost to the Group basis). None of these service agreements include bonus, share options or termination conditions in excess of six months.

Insurance of officers

During the year, Australian Wool Innovation Limited paid an insurance premium of \$32,753 to insure the directors and officers of the entity against liability and professional indemnity.

Non-audit services

The Group may decide to appoint the auditor on assignments additional to their statutory audit duties where the auditor's experience with the Group and/or the consolidated entity are important.

Details of the amounts paid to the auditor (PricewaterhouseCoopers) for audit and non-audit services provided during the year are set out in Note 19 to the Financial Statements.

Auditors' independence declaration

A copy of the auditors' independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 52.

Rounding of amounts

The company is of a kind referred to in Class Order 98/0100, issued by the Australian Securities & Investments Commission, relating to the 'rounding off' of amounts in the directors' report. Amounts in the directors' report have been rounded off in accordance with that Class Order to the nearest thousand dollars, or in certain cases, to the nearest dollar.

Dividends Paid

There have been no dividends paid or recommended for the 2006 financial year (2005: Nil)

Share options

There have been no share options granted to any directors or executives of the Group.

Environmental regulation

The entity's operations are not subject to any particular or significant environmental regulations under either Commonwealth or State legislation.

Proceedings on behalf of the company

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the company, or to intervene in any proceedings to which the company is a party for the purpose of taking responsibility on behalf of the company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the company with leave of the Court under section 237 of the *Corporations Act 2001*.

Statutory funding agreement obligations

In addition to usual annual reporting requirements, there are additional reporting requirements imposed upon the company under Schedule 3 of the Statutory Funding Agreement between Australian Wool Innovation Limited and the Commonwealth of Australia. These are all dealt with in this annual report with the exception of a listing of the projects for which Commonwealth Matching Funds have been claimed. This will be provided separately to the Government.

A number of the matters identified in this report contain commercial in confidence information and the company has elected to exercise its prerogative to provide that report separately to the Commonwealth on an 'in confidence' basis.

This report is made in accordance with a resolution of directors.



I M McLachlan
Chairman

Sydney
21 September 2006

Auditors' Independence Declaration

As lead auditor for the audit of Australian Wool Innovation Limited for the year ended 30 June 2006, I declare that to the best of my knowledge and belief, there have been:

- (a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
- (b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Australian Wool Innovation Limited and the entities it controlled during the period.



Peter Buchholz
Partner
PricewaterhouseCoopers

Sydney
21 September, 2006

Financial report – 30 June 2006

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The financial report covers both Australian Wool Innovation Limited as an individual entity and the consolidated entity consisting of Australian Wool Innovation Limited and its controlled entities (as listed in Note 23 to the financial report). The financial report is presented in the Australian currency.

Australian Wool Innovation Limited is a company limited by shares, incorporated and domiciled in Australia. Its registered office and principal place of business is:

Level 5
16-20 Barrack Street
SYDNEY NSW 2000

A description of the nature of the consolidated entity's operations and principal activities is included in the review of operations and activities in the directors' report on pages 48–51, which is not part of this financial report.

The financial report was authorised for issue by the directors on 21 September 2006. The company has the power to amend and reissue the financial report.

Through the use of the internet, we have ensured that our corporate reporting is timely, complete, and available globally at minimum cost to the company. All press releases, financial reports and other information are available on our website: www.wool.com.au.

Income Statement

For the year ended 30 June 2006

	Notes	Consolidated		Parent entity	
		2006	2005	2006	2005
		\$'000	\$'000	\$'000	\$'000
Revenue from ordinary activities	3	57,035	64,999	57,035	64,999
Research, development and innovation program expenditure	5	(70,421)	(65,721)	(70,385)	(65,721)
RDI support services expenditure					
• Employee expenses		(4,727)	(4,832)	(4,727)	(4,832)
• Legal and professional expenses	5	(1,615)	(2,856)	(1,615)	(2,856)
• Travel expenses		(809)	(738)	(809)	(738)
• Depreciation and amortisation expenses		(1,399)	(784)	(1,399)	(784)
• Other expenses from ordinary activities		(3,707)	(3,566)	(3,707)	(3,566)
(Deficit) / Surplus from ordinary activities	17	(25,643)	(13,498)	(25,607)	(13,498)
Profit / (Loss) attributable to members of Australian Wool Innovation Limited		(25,643)	(13,498)	(25,607)	(13,498)

The above income statement should be read in conjunction with the accompanying notes.

Balance Sheet

As at 30 June 2006

	Notes	Consolidated		Parent entity	
		2006	2005	2006	2005
		\$'000	\$'000	\$'000	\$'000
Current assets					
Cash assets	6	77,114	101,079	77,102	101,079
Receivables	7	4,054	4,232	4,089	4,232
Other	8	970	836	970	836
Total current assets		82,138	106,147	82,161	106,147
Non-current assets					
Receivables	9	–	–	–	–
Investment in controlled entities	23	–	–	13	–
Property, plant and equipment	10	4,260	4,547	4,260	4,547
Livestock	11	326	584	326	584
Intangible assets	12	–	–	–	–
Total non-current assets		4,586	5,131	4,599	5,131
Total assets		86,724	111,278	86,760	111,278
Current liabilities					
Payables	13	8,857	7,585	8,857	7,585
Provisions	14	518	615	518	615
Total current liabilities		9,375	8,200	9,375	8,200
Non-current liabilities					
Provisions	15	–	86	–	86
Total non-current liabilities		–	86	–	86
Total liabilities		9,375	8,286	9,375	8,286
Net assets		77,349	102,992	77,385	102,992
Equity					
Contributed equity *	16	–	–	–	–
Retained surplus	17	77,349	102,992	77,385	102,992
Total equity		77,349	102,992	77,385	102,992

* At 30 June 2005 and 2006 contributed equity in the parent entity was \$100.

The above balance sheet should be read in conjunction with the accompanying notes.

Statement of Changes in Equity

For the year ended 30 June 2006

		Consolidated		Parent entity	
	Note	2006	2005	2006	2005
		\$'000	\$'000	\$'000	\$'000
Total equity at the beginning of the financial year	17	102,992	116,490	102,992	116,490
Total recognised income and expense for the year		(25,643)	(13,498)	(25,607)	(13,498)
Total equity at the end of the financial year		77,349	102,992	77,385	102,992

The above statement of changes in equity should be read in conjunction with the accompanying notes.

Cash Flow Statement

For the year ended 30 June 2006

	Notes	Consolidated		Parent entity	
		2006	2005	2006	2005
		\$'000	\$'000	\$'000	\$'000
Cash flows from operating activities					
Receipts from customers (inclusive of goods and services tax)		56,004	63,344	56,004	63,344
Payments to suppliers and employees (inclusive of goods and services tax)		(84,469)	(82,079)	(84,481)	(82,079)
		(28,465)	(18,735)	(28,477)	(18,735)
Interest received		5,433	6,507	5,433	6,507
Other revenue		22	1,543	22	1,543
Net cash inflow/(outflow) from operating activities	25	(23,010)	(10,685)	(23,022)	(10,685)
Cash flows from investing activities					
Payments for property, plant and equipment		(1,282)	(1,698)	(971)	(1,698)
Proceeds from sale of property, plant and equipment		327	328	16	328
Net cash inflow/(outflow) from investing activities		(955)	(1,370)	(955)	(1,370)
Net decrease in cash held		(23,965)	(12,055)	(23,977)	(12,055)
Cash at the beginning of the financial year		101,079	113,134	101,079	113,134
Cash at the end of the financial year	6	77,114	101,079	77,102	101,079

The above cash flow statement should be read in conjunction with the accompanying notes.

Notes to the Financial Report

30 June 2006

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Notes to the Financial Report (continued)

30 June 2006

Note 1. Summary of significant accounting policies

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

This general purpose financial report has been prepared in accordance with Australian equivalents to International Financial Reporting Standards (AIFRSs), other authoritative pronouncements of Australian Accounting Standards Board, Urgent Issues Group Interpretations and the *Corporation Act 2001*.

Application of AASB 1 First time Adoption of Australian Equivalents to International Financial Reporting Standards

These financial statements are the first Australian Wool Innovation Limited financial statements to be prepared in accordance with AIFRSs. AASB 1 First time Adoption of Australian Equivalents to International Financial Reporting Standards has been applied in preparing these financial statements.

Financial statements of Australian Wool Innovation Limited until 30 June 2005 had been prepared in accordance with previous Australian Generally Accepted Accounting Principles (AGAAP). AGAAP differs in certain respects from AIFRS. When preparing Australian Wool Innovation Limited financial statements, management has amended certain accounting, valuation and consolidation methods applied in the AGAAP financial statements to comply with AIFRS. With the exception of financial instruments, the comparative figures in respect of 2005 were restated to reflect these adjustments.

The description of the effect of transition from previous AGAAP to AIFRSs on the company's and consolidated entity's equity and net income are given in note 27.

The preparation of financial statements in conformity with AIFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the entity's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 1.

This financial report has been prepared under the historical cost convention, except for certain assets which, as stated, are at valuation. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year. Comparative information is reclassified where appropriate to enhance comparability.

Critical accounting estimates and judgements

Estimates and judgement are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances..

A General

A(1) Principles of consolidation

The consolidated financial statements incorporate the assets and liabilities of all entities controlled by Australian Wool Innovation Limited as at 30 June 2006 and the results of all controlled entities for the year then ended. Australian Wool Innovation Limited and its controlled entities together are referred to in this financial report as the consolidated entity. The effects of all transactions between entities in the consolidated entity are eliminated in full. Outside equity interests in the results and equity of controlled entities are shown separately in the consolidated statement of financial performance and statement of financial position respectively.

Where control of an entity is obtained during a financial year, its results are included in the consolidated statement of financial performance from the date on which control commences. Where control of an entity ceases during a financial year its results are included for that part of the year during which control existed.

A(2) Income tax

Australian Wool Innovation Limited is exempt from income tax in Australia under Section 50-40 of the Income Tax Assessment Act 1997.

A(3) Foreign currency translation

Transactions

(i) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Australian dollars, which is Australian Wool Innovation Limited's functional and presentation currency.

Notes to the Financial Report (continued)

30 June 2006

Note 1. Summary of significant accounting policies (continued)

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges and qualifying net investment hedges.

Translation differences on non-monetary financial assets and liabilities are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognised in profit or loss as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale financial assets are included in the fair value reserve in equity.

(iii) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

A(4) Rounding of amounts

The company is of a kind referred to in Class Order 98/0100, issued by the Australian Securities and Investments Commission, relating to the "rounding off" of amounts in the financial report. Amounts in the financial report have been rounded off in accordance with that Class Order to the nearest thousand dollars, or in certain cases, to the nearest dollar.

B Revenue and expenditure

B(1) Revenue recognition

Revenue for the sale of goods is recognised upon the delivery of the goods to the customers.

Revenue for the disposal of non-current assets is recognised when control of the asset has passed to the buyer.

Revenue from the rendering of a service is recognised by reference to the stage of completion of contracts or other agreements to provide services.

Interest revenue is recognised on a proportional basis taking into account the interest rates applicable to the financial assets.

B(2) Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

B(3) 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, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- for receivables and payables which are recognised inclusive of GST.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

B(4) Acquisition of assets

Purchases of property, plant and equipment are recognised initially at cost in the statement of financial position, except for purchases costing less than \$2,000, which are expensed in the year of acquisition.

Note 1. Summary of significant accounting policies (continued)

C Assets

C(1) Cash

For the purpose of the statement of cash flows, cash includes deposits held at call with a bank, funds under management and investment securities. There were no standby credit facilities in place at 30 June 2006.

C(2) Receivables

Collectibility of trade debtors is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off. A provision for doubtful debts is raised when some doubt as to collection exists.

C(3) Recoverable amount of non-current assets

The recoverable amount of an asset is the net amount expected to be recovered through the cash inflows and outflows arising from its continued use and subsequent disposal.

Where the carrying amount of a non-current asset is greater than its recoverable amount, the asset is written down to its recoverable amount. Where net cash inflows are derived from a group of assets working together, the recoverable amount is determined on the basis of the relevant group of assets. The decrement in the carrying amount is recognised as an expense in net surplus or deficit in the reporting period in which the recoverable amount write-down occurs.

C(4) Impairment of assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

C(5) Intangible Assets

(i) Research, development and innovation

Costs incurred on research, development and innovation projects and in-process research and development acquired in the acquisition of an entity or operation are expensed as incurred.

(ii) Intellectual property

Costs associated with intellectual property, either developed or acquired by the Group, are expensed as incurred, except to the extent that they are expected beyond a reasonable doubt to be recoverable.

In the event that the future economic benefit attributable to an individual research, development and innovation project or piece of intellectual property can be determined and it becomes probable such benefit will exceed the future cumulative expenditure relating to that item, all future costs relating to that item are deferred and amortised on a straight line basis over the period of their expected benefit.

C(6) Investments

Investments are stated at cost less amounts written off for permanent diminution in their value. Investment income is recognised in the statement of financial performance when receivable.

C(7) Depreciation of property, plant and equipment

Depreciation is calculated on a straight line basis to write off the net cost or re-valued amount of each item of property, plant and equipment (excluding land) over its expected useful life to the economic entity. Estimates of remaining useful lives are made on a regular basis for all assets, with annual reassessments for major items. The expected useful lives are as follows:

Category	Useful life	Depreciation basis
Buildings	40 years	straight line
Plant and equipment	2-6 years	straight line

Notes to the Financial Report (continued)

30 June 2006

Note 1. Summary of significant accounting policies (continued)

C(8) Leasehold improvements

The cost of improvements to or on leasehold properties is amortised over the unexpired period of the lease or the estimated useful life of the improvement to the consolidated entity, whichever is the shorter.

D Liabilities

D(1) Trade and other creditors

These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

D(2) Employee entitlements

(i) Wages, salaries and annual leave

Liabilities for wages, salaries and annual leave expected to be settled within 12 months of the reporting date are measured at the amounts expected to be paid when liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and measured at the rates paid or payable.

(ii) Long service leave

The liability for long service leave expected to be settled within 12 months of the reporting date is recognised in the provision for employee benefits and is measured in accordance with (i) above. The liability for long service leave expected to be settled more than 12 months from the reporting date is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date.

Note 2. Segment information

Business Segments

Australian Wool Innovation Limited operates predominately in research, development and innovation in the wool industry.

Geographical segments

Australian Wool Innovation Limited operates primarily in one geographic segment, that being Australia. The Group has opened offices in Shanghai and Hongkong, China, New York, USA, New Delhi, India, and Treviso, Italy which are responsible for growing domestic demand for Australian Merino wool in key international markets through strategic engagements with manufacturing and retail brand partners. They do this by building business relationships which facilitate innovative wool based product development and its commercialisation into the consumer market. However, these offices do not enter into research, development and innovation contracts or conduct business in their own right and accordingly no geographic segment split is considered appropriate.

Note 3. Revenue

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Revenue from operating activities				
Government Contributions	11,048	13,513	11,048	13,513
Sale of goods and services	606	350	606	350
Royalties	574	569	574	569
Wool levy	38,359	42,835	38,359	42,835
Other	1,011	1,207	1,011	1,207
	51,598	58,474	51,598	58,474
Revenue from outside the operating activities				
Interest	5,437	6,525	5,437	6,525
Revenue from ordinary activities	57,035	64,999	57,035	64,999

Note 4. Expenses

Surplus from ordinary activities includes the following specific net gains and expenses:

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Expenses				
Depreciation				
Buildings	269	70	269	70
Plant and equipment	1,130	714	1,130	714
Total depreciation	1,399	784	1,399	784
Other Provisions				
Employee entitlements	(183)	41	(183)	41
Rental expense relating to operating leases	750	614	750	614

Notes to the Financial Report (continued)

30 June 2006

Note 5. Research, development and innovation expenditure

Consolidated:	2006			2005		
	\$'000			\$'000		
	External costs	Internal costs	Total	External costs	Internal costs	Total
Product Development						
Fundamental Wool Science	3,206			2,187		
The Processing of Merino Fibre	7,119			1,474		
Merino Fibre in Fashion Markets	5,975			6,099		
Merino as a Performance Fibre	3,000			3,746		
	19,300	2,449	21,749	13,506	1,836	15,342
Wool Production						
Profitable Grazing for Wool Sheep	4,471			5,957		
Natural Resource Management	2,912			4,880		
Animal Health and Welfare	7,078			9,087		
Molecular Genetics	4,270			2,803		
Applied Genetics	1,933			2,134		
Wool Quality and Logistics				1,013		
Education and Adoption	3,508			6,889		
Wool Harvesting	3,172			3,040		
	27,344	1,959	29,303	35,803	2,055	37,858
Product Marketing						
Market Information	3,287			1,365		
Market Access and Trade Development	5,115			676		
	8,402	3,439	11,841	2,041	1,080	3,121
Corporate Affairs *						
	6,743	785	7,528	8,509	891	9,400
Total RDI expenditure	61,789	8,632	70,421	59,859	5,862	65,721

"External costs" represents payment to suppliers directly related to individual projects and programs.

"Internal costs" are the cost of staff who manage those projects and programs and their related expenses.

This amount does not include executives or any allocations of support services, rent and similar items, and consists of the following items of expenditure:

Consolidated:	2006			2005		
	\$'000			\$'000		
	RDI Program	RDI Support	Total cost	RDI Program	RDI Support	Total cost
Employee expenses	5,391	4,727	10,118	3,674	4,832	8,506
Legal and professional expenses **	303	1,615	1,918	104	2,856	2,960
Travel expenses	1,393	809	2,202	936	738	1,674
Depreciation and amortisation expenses	–	1,399	1,399	–	784	784
Other expenses from ordinary activities	1,545	3,707	5,252	1,148	3,566	4,714
	8,632			5,862		

Note 5. Research, development and innovation expenditure (continued)

Parent entity:	2006			2005		
	\$'000			\$'000		
	External costs	Internal costs	Total	External costs	Internal costs	Total
Product Development						
Fundamental Wool Science	3,206			2,187		
The Processing of Merino Fibre	7,119			1,474		
Merino Fibre in Fashion Markets	5,975			6,099		
Merino as a Performance Fibre	3,000			3,746		
	19,300	2,449	21,749	13,506	1,836	15,342
Wool Production						
Profitable Grazing for Wool Sheep	4,471			5,957		
Natural Resource Management	2,912			4,880		
Animal Health and Welfare	7,078			9,087		
Molecular Genetics	4,270			2,803		
Applied Genetics	1,933			2,134		
Wool Quality and Logistics				1,013		
Education and Adoption	3,508			6,889		
Wool Harvesting	3,172			3,040		
	27,344	1,959	29,303	35,803	2,055	37,858
Product Marketing						
Market Information	3,287			1,365		
Market Access and Trade Development	5,115			676		
	8,402	3,403	11,805	2,041	1,080	3,121
Corporate Affairs *						
	6,743	785	7,528	8,509	891	9,400
Total RDI expenditure	61,789	8,596	70,385	59,859	5,862	65,721
Parent entity:						
	2006			2005		
	\$'000			\$'000		
	RDI Program	RDI Support	Total cost	RDI Program	RDI Support	Total cost
Employee expenses	5,366	4,727	10,093	3,674	4,832	8,506
Legal and professional expenses **	294	1,615	1,909	104	2,856	2,960
Travel expenses	1,392	809	2,201	936	738	1,674
Depreciation and amortisation expenses	–	1,399	1,399	–	784	784
Other expenses from ordinary activities	1,544	3,707	5,251	1,148	3,566	4,714
	8,596			5,862		

* Corporate Affairs includes costs associated with defending against actions by animal rights groups.

** Legal and professional expenses include Nil (2005:\$1.4m) settlement of a claim against AWI relating to a 2002 contract, including cost and interest.

Notes to the Financial Report (continued)

30 June 2006

Note 6. Current assets - Cash assets

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Cash on hand and at bank	687	256	675	256
Funds under management	76,427	100,823	76,427	100,823
	<u>77,114</u>	<u>101,079</u>	<u>77,102</u>	<u>101,079</u>

	2006	2005
	\$'000	\$'000
Representing:		
Unrestricted cash and cash investments	43,876	65,337
Restricted as security against guarantees issued by the company's bankers ^(a)	327	326
Restricted by the directors in respect of:		
• Capital reserve ^(b)	20,606	20,606
• Emergency reserve ^(c)	5,000	5,000
• Operating reserve ^(c)	7,305	9,810
	<u>77,114</u>	<u>101,079</u>

(a) Bank guarantees have been issued to a number of parties in respect of the company's liabilities. The company has given its primary bankers security over term deposits in respect of those amounts, such deposits attracting commercial interest rates.

(b) The directors resolved in July 2003 to set aside funds received from the sale of the company's interest in CSIRO properties as a capital sum for special purposes. Subsequently an amount was released as payment to the Australian Wool Education Trust.

(c) The directors resolved in May 2003 to set aside \$5,000,000 as an emergency reserve to cover any unforeseeable expenditure and 15% of annual budgeted revenue as an operating reserve in respect of future liabilities.

Note 7. Current assets – Receivables

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Trade debtors	595	269	595	269
Provision for doubtful debts	–	–	–	–
	595	269	595	269
Accrued wool levy	2,992	3,498	2,992	3,498
Other debtors	467	465	502	465
	4,054	4,232	4,089	4,232

Note 8. Current assets – Other

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Goods and services tax receivable	628	701	628	701
Prepayments	169	135	169	135
Others	173	–	173	–
	970	836	970	836

Note 9. Non-current assets – Receivables

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Loan to textile manufacturer	–	1,141	–	1,141
Provision for doubtful debts	–	(1,141)	–	(1,141)
	–	–	–	–

During the year ended 30 June 2006, an agreement was signed to reduce the loan to 50% of the principal, with the balance payable in July 2006. The loan balance is included as part of the trade debtors.

Notes to the Financial Report (continued)

30 June 2006

Note 10. Non-current assets – Property, plant & equipment

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Land & buildings				
Freehold land – at cost	425	425	425	425
Buildings				
At cost	2,639	2,550	2,639	2,550
Less: Accumulated depreciation	(474)	(205)	(474)	(205)
	2,165	2,345	2,165	2,345
Total land and buildings	2,590	2,770	2,590	2,770
Plant and equipment				
Plant & equipment				
At cost	4,079	3,250	4,079	3,250
Less: Accumulated depreciation	(2,409)	(1,473)	(2,409)	(1,473)
Total plant and equipment	1,670	1,777	1,670	1,777
	4,260	4,547	4,260	4,547

Reconciliations

Reconciliation of the carrying amounts of each class of property, plant and equipment at the beginning and end of the current financial year is set out below:

	Land and Buildings	Plant and equipment	Total
	\$'000	\$'000	\$'000
Carrying amount at 1 July 2005	2,770	1,777	4,547
Additions	89	1,193	1,282
Disposals	–	(172)	(172)
Depreciation/amortisation expense	(269)	(1,128)	(1,397)
Carrying amount at 30 June 2006	2,590	1,670	4,260

Note 11. Livestock

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Number of livestock	7,569	11,721	7,569	11,721
Value	326	584	326	584

Livestock are carried on the balance sheet at cost, with adjustment made to reflect net market value as appropriate.

Note 12. Non-current assets – Intangible assets

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Patents and trademarks	–	–	–	–

The Group owns or has an interest in a number of items of registered intellectual property, as shown in Appendix C of this Annual Report. The Group's current policy is to expense all intellectual property costs as incurred unless Generally Accepted Accounting Practice requires treatment otherwise. At the date of this report, no costs relating to these intangible assets have been deferred; all costs have been expensed as incurred.

Note 13. Current liabilities – Payables

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Unsecured				
Trade creditors	4,066	631	4,066	631
Other payables – RDI contract payments accrued	4,094	4,722	4,094	4,722
Other creditors	697	2,232	697	2,232
	8,857	7,585	8,857	7,585

Note 14. Current liabilities – Provisions

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Annual leave	518	597	518	597
Other employee entitlements	–	18	–	18
	518	615	518	615

Note 15. Non-current liabilities – Provisions

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Long service leave	–	86	–	86
	–	86	–	86

Notes to the Financial Report (continued)

30 June 2006

Note 16. Contributed equity

	Consolidated		Parent entity	
	2006	2005	2006	2005
	Shares	Shares	Shares	Shares

(a) Share capital

Ordinary shares – fully paid	37,462	37,462	37,462	37,462
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(b) Ordinary shares

The \$100 represents the initial capital contribution on the establishment of the company. Each wool grower has a right to one vote for every \$100 of wool levy or wool tax contributed during the 3 previous financial years, as defined in the Wool Services Privatisation Act 2000 (Cth). These shares do not entitle wool growers to participate in any profit distributions or in any proceeds on the winding up of the entity.

(c) Movements in ordinary share capital

Date	Details	Number of shares	Issue price	\$
1 July 2004	Opening balance	37,462	–	100
30 June 2005	Balance	37,462	–	100
30 June 2006	Balance	37,462	–	100

The actual number of shareholders at 30 June 2006 was 31,989.

Note 17. Retained surplus

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Retained surplus at the beginning of the financial year	102,992	116,490	102,992	116,490
Net surplus attributable to shareholders of Australian Wool Innovation Limited	(25,643)	(13,498)	(25,607)	(13,498)
Retained surplus at the end of the financial year	77,349	102,992	77,385	102,992

Note 18. Financial instruments**(a) Credit risk exposures**

The consolidated entity's maximum exposures to credit risk at reporting date in relation to each class of recognised financial asset is the carrying amount of those assets as indicated in the statement of financial position.

The consolidated entity has no significant exposures to any concentrations of credit risk.

According to Australian Wool Innovation Limited's Treasury Policy, counterparties for Financial Instruments must have a minimum credit rating A (long term) and A1 (short term) as rated by S&P's Australian Standards. The company manages all risks by only approving investments in Australian dollars with a fixed exchange rate set at the rate prevailing at 4pm the day before any contract is signed.

(b) Interest rate risk exposures

The consolidated entity's exposure to interest rate risk and effective weighted average interest rate by maturity periods is set out in the following table.

		Weighted average interest rate	Floating interest rate	Non interest bearing	Total
2006	Notes	%	\$'000	\$'000	\$'000
Financial assets					
Cash and deposits	6	5.25	687	6	693
Funds under management	6	5.97	76,427	–	76,427
Receivables	7		–	4,054	4,054
Receivables (non-current)	9		–	–	–
			77,114	4,060	81,174
Financial liabilities					
Trade and other creditors	13		–	(8,857)	(8,857)
Net financial assets / (liabilities)			77,114	(4,797)	72,317
2005					
Financial assets					
Cash and deposits	6	5.00	252	4	256
Funds under management	6	5.58	100,823	–	100,823
Receivables	7		–	4,232	4,232
Receivables (non-current)	9	6.79	–	–	–
			101,075	4,236	105,311
Financial liabilities					
Trade and other creditors	13		–	(7,585)	(7,585)
Net financial assets / (liabilities)			101,075	(3,349)	97,726

(c) Net fair value of financial assets and liabilities**On-balance sheet**

The net fair value of cash and cash equivalents and non-interest bearing monetary financial assets and financial liabilities of the economic entity approximates their carrying amounts.

Notes to the Financial Report (continued)

30 June 2006

Note 19. Remuneration of auditors

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$	\$	\$	\$
During the year the auditor of the parent entity and its related practices earned the following remuneration:				
Audit of financial reports of the entity or any entity in the consolidated entity	105,000	75,000	105,000	75,000
Other audit-related work	–	–	–	–
Other assurance services	19,580	17,500	19,580	17,500
Total audit and other assurance services	124,580	92,500	124,580	92,500
Advisory services	54,071	11,902	54,071	11,902
Total remuneration	178,651	104,402	178,651	104,402

As part of the review of Corporate Governance practices, the consolidated entity segregated its taxation, internal audit and advisory services from statutory audit within Australia.

Note 20. Commitments for expenditure

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000

Other Commitments

Commitments in relation to research and development, technical proving and transfer and, the cost of various goods and services contracted for at the end of the reporting date but not recognised as liabilities, payable:

Within one year	33,690	38,739	33,690	38,739
Later than one year but not later than 5 years	20,332	27,271	20,332	27,271
	54,022	66,010	54,022	66,010

Lease commitments

Commitments in relation to leases contracted for at the reporting date but not recognised as liabilities, payable:

Within one year	845	733	789	733
Later than one year but not later than 5 years	647	877	647	877
	1,492	1,610	1,436	1,610
Representing:				
Non-cancellable operating leases	1,492	1,610	1,436	1,610

A small number of commitments are denominated in currencies other than Australian dollars. It is currently the company's policy to translate those commitments at the exchange rate at 30 June 2006, and to subsequently meet those commitments as they fall due by purchasing foreign currency at spot rates. This policy is reviewed by the Board from time to time.

Note 21. Employee benefits

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Employee benefit and related on-costs liabilities				
Provision for employee benefits – current (Note 14)	518	615	518	615
Provision for employee benefits – non-current (Note 15)	–	86	–	86
Aggregate employee benefit and related on-costs liabilities	518	701	518	701
Employee Numbers	Number	Number	Number	Number
Number of employees at 30 June	85	73	83	73
Number of permanent full time contractors at 30 June	0	1	0	1
	85	74	83	74

Note 22. Related parties**Directors**

The names of persons who were directors of Australian Wool Innovation Limited at any time during the financial year are as follows: I M McLachlan, B P van Rooyen, C J Abell, K J Bell, W B Merriman, H P Nivison, P S Sykes. All of these persons were also directors during the year ended 30 June 2005.

Remuneration

Information on remuneration of directors is disclosed in the Directors' Report.

Directors' Interests in Contracts

During the year ended 30 June 2006 no director, or director-related entity entered into a contract or had any transactions on other than normal terms and conditions with Australian Wool Innovation Limited.

Other transactions with directors and director related parties

There were no other transactions with directors or director related parties during the year ended 30 June 2006.

Note 23. Investment in controlled entities

Name of entity	Country of incorporation	Cost of Investment		Equity holding	
		2006	2005	2006	2005
		\$	\$	%	%
Australian Wool Innovation LLC	USA	13,000	0	100	–

Australian Wool Innovation LLC was formed on 13th September 2005 with initial capital contribution of USD10,000.

Note 24. Economic dependency

Australian Wool Innovation Limited is dependent upon receipt of Wool Levy through the Commonwealth Government who collect the levy and provide the funds in accordance with the Statutory Funding Agreement.

Note 25. Events occurring after reporting date

Australian Wool Innovation Limited and Australian Wool Services Limited have signed a Memorandum of Understanding on 27 July 2006, outlining their resolve to integrate the two companies. Both Boards will work to get shareholder and Federal Government approval to integrate by the end of 2006.

Notes to the Financial Report (continued)

30 June 2006

Note 26. Reconciliation of surplus from ordinary activities to net cash inflow from operating activities

	Consolidated		Parent entity	
	2006	2005	2006	2005
	\$'000	\$'000	\$'000	\$'000
Surplus from ordinary activities	(25,643)	(13,498)	(25,607)	(13,498)
Depreciation and amortisation	1,399	784	1,399	784
(Profit)/Loss on sale of property, plant and equipment	(157)	67	(157)	67
Change in operating assets and liabilities				
Decrease (increase) in trade debtors	(326)	759	(326)	759
Decrease (increase) in prepayments	(34)	121	(34)	121
Decrease (increase) in other operating assets	(100)	(984)	(100)	(984)
Decrease (increase) in accrued wool levy	506	664	506	664
Decrease (increase) in other debtors	256	(19)	221	(19)
Increase (decrease) in creditors	1,272	1,380	1,272	1,380
Increase (decrease) in provisions	(183)	41	(183)	41
Net cash inflow from operating activities	(23,010)	(10,685)	(23,009)	(10,685)

Note 27. Explanation of transition to Australian equivalents to IFRSs

(1) Reconciliation of equity reported under previous Australian Generally Accepted Accounting Principles (AGAAP) to equity under Australian equivalents to IFRSs (AIFRS)

(a) At the end of the last reporting period under previous AGAAP: 1 July 2004

	Consolidated			Parent entity		
	Previous AGAAP	Effect of transition to AIFRS	AIFRS	Previous AGAAP	Effect of transition to AIFRS	AIFRS
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
ASSETS						
Current assets						
Cash assets	113,134	–	113,134	113,134	–	113,134
Receivables	5,634	–	5,634	5,634	–	5,634
Other	557	–	557	557	–	557
Total current assets	119,325	–	119,325	119,325	–	119,325
Non-current assets						
Receivables	–	–	–	–	–	–
Property, plant and equipment	4,030	–	4,030	4,030	–	4,030
Livestock	–	–	–	–	–	–
Intangible assets	–	–	–	–	–	–
Total non-current assets	4,030	–	4,030	4,030	–	4,030
Total assets	123,355	–	123,355	123,355	–	123,355

Note 27. Explanation of transition to Australian equivalents to IFRSs (continued)

	Consolidated			Parent entity		
	Previous AGAAP	Effect of transition to AIFRS	AIFRS	Previous AGAAP	Effect of transition to AIFRS	AIFRS
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
LIABILITIES						
Current liabilities						
Payables	6,205	–	6,205	6,205	–	6,205
Provisions	555	–	555	555	–	555
Total current liabilities	6,760	–	6,760	6,760	–	6,760
Non-current liabilities						
Provisions	105	–	105	105	–	105
Total non-current liabilities	105	–	105	105	–	105
Total liabilities	6,865	–	6,865	6,865	–	6,865
Net assets	116,490	–	116,490	116,490	–	116,490
EQUITY						
Contributed equity	–	–	–	–	–	–
Retained surplus	116,490	–	116,490	116,490	–	116,490
Total equity	116,490	–	116,490	116,490	–	116,490
(b) At the end of the last reporting period under previous AGAAP: 30 June 2005						
ASSETS						
Current assets						
Cash assets	101,079	–	101,079	101,079	–	101,079
Receivables	4,232	–	4,232	4,232	–	4,232
Other	836	–	836	836	–	836
Total current assets	106,147	–	106,147	106,147	–	106,147
Non-current assets						
Receivables	–	–	–	–	–	–
Property, plant and equipment	4,547	–	4,547	4,547	–	4,547
Livestock	584	–	584	584	–	584
Intangible assets	–	–	–	–	–	–
Total non-current assets	5,131	–	5,131	5,131	–	5,131
Total assets	111,278	–	111,278	111,278	–	111,278

Notes to the Financial Report (continued)

30 June 2006

Note 27. Explanation of transition to Australian equivalents to IFRSs (continued)

	Consolidated			Parent entity		
	Previous AGAAP	Effect of transition to AIFRS	AIFRS	Previous AGAAP	Effect of transition to AIFRS	AIFRS
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
LIABILITIES						
Current liabilities						
Payables	7,585	–	7,585	7,585	–	7,585
Provisions	615	–	615	615	–	615
Total current liabilities	8,200	–	8,200	8,200	–	8,200
Non-current liabilities						
Provisions	86	–	86	86	–	86
Total non-current liabilities	86	–	86	86	–	86
Total liabilities	8,286	–	8,286	8,286	–	8,286
Net assets	102,992	–	102,992	102,992	–	102,992
EQUITY						
Contributed equity	–	–	–	–	–	–
Retained surplus	102,992	–	102,992	102,992	–	102,992
Total equity	102,992	–	102,992	102,992	–	102,992
(2) Reconciliation of loss for the year ended 30 June 2005						
Revenue from ordinary activities	64,999	–	64,999	64,999	–	64,999
Research, development and innovation program expenditure	(65,721)	–	(65,721)	(65,721)	–	(65,721)
RDI support services expenditure						
• Employee expenses	(4,832)	–	(4,832)	(4,832)	–	(4,832)
• Legal and professional expenses	(2,856)	–	(2,856)	(2,856)	–	(2,856)
• Travel expenses	(738)	–	(738)	(738)	–	(738)
• Depreciation expenses	(784)	–	(784)	(784)	–	(784)
• Other expenses	(3,566)	–	(3,566)	(3,566)	–	(3,566)
(Deficit) / Surplus from ordinary activities	(13,498)	–	(13,498)	(13,498)	–	(13,498)
Total changes in equity attributable to members of Australian Wool Innovation Limited other than those resulting from transactions with owners as owners	(13,498)	–	(13,498)	(13,498)	–	(13,498)

Directors' declaration

30 June 2006

In the directors' opinion:

- (a) the financial statements and notes set out on pages 46 to 79 are in accordance with the *Corporations Act 2001*, including:
 - (i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; and
 - (ii) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2006 and of its performance, as represented by the results of their operations, changes in equity and their cash flows, for the financial year ended on that date; and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable;

The directors have been given the declarations by the chief executive officer and general manager – finance required by section 295A of the *Corporations Act 2001*.

This declaration is made in accordance with a resolution of the directors.



I M McLachlan
Chairman

Sydney
21 September 2006

Independent audit report to the members of Australian Wool Innovation Limited

Matters relating to the electronic presentation of the audited financial report

This audit report relates to the financial report of Australian Wool Innovation Limited (the Company) and the Australian Wool Innovation Limited Group (defined below) for the financial year ended 30 June 2006 included on Australian Wool Innovation Limited's web site. The Company's directors are responsible for the integrity of the Australian Wool Innovation Limited web site. We have not been engaged to report on the integrity of this web site. The audit report refers only to the financial report identified below. It does not provide an opinion on any other information which may have been hyperlinked to/from the financial report. If users of this report are concerned with the inherent risks arising from electronic data communications they are advised to refer to the hard copy of the audited financial report to confirm the information included in the audited financial report presented on this web site.

Audit opinion

In our opinion, the financial report of Australian Wool Innovation Limited:

- gives a true and fair view, as required by the *Corporations Act 2001* in Australia, of the financial position of Australian Wool Innovation Limited and the Australian Wool Innovation Limited Group (defined below) as at 30 June 2006, and of their performance for the year ended on that date, and
- is presented in accordance with the *Corporations Act 2001*, Accounting Standards and other mandatory financial reporting requirements in Australia, and the *Corporations Regulations 2001*.

This opinion must be read in conjunction with the rest of our audit report.

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, cash flow statements, statement of changes in equity, accompanying notes to the financial statements, and the directors' declaration for both Australian Wool Innovation Limited (the company) and the Australian Wool Innovation Limited Group (the consolidated entity), for the year ended 30 June 2006. 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. For further explanation of an audit, visit our website <http://www.pwc.com/au/financialstatementaudit>.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001*, 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, changes in equity 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.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

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.

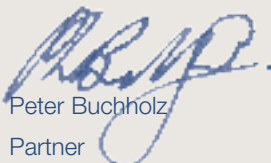
Our audit did not involve an analysis of the prudence of business decisions made by directors or management.

Independence

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



PricewaterhouseCoopers



Peter Buchholz
Partner

Sydney

21 September 2006