

EAST KIMBERLEY SANDALWOOD PROJECT NO.1

ANNUAL FINANCIAL REPORT
FOR THE YEAR TO 30 JUNE 2005

MANAGER'S REPORT

The Directors of Tropical Forestry Services Ltd (ACN 080 139 960), manager of East Kimberley Sandalwood project No.1 ("the Project"), present their report together with the financial statements of the Project for the period ended 30 June 2005.

Directors

The names of the Directors of Tropical Forestry Services Ltd during the period and at the date of this report are:

Frank Cullity WILSON
Graeme Eric SCOTT
Stephen Lee ATKINSON
Ronald Lionel EACOTT
Blaine David KIDD
Julius Luke MATTHYS
Thomas Nash CULLITY

Principal Activities

During the period the principal activity of the Project was the management of a sandalwood plantation.

Change of State of Affairs

There was no significant change in the state of affairs of the Project.

Results of Operations and Likely Developments

The Project made a profit for the financial year ended 30 June 2005 of \$453,914 (2004: \$736,750).

This is due to the increment in the valuation of the sandalwood trees.

The EKS Plantation was originally established in 1999 and the trees are now 6 years old.

In our report to you for the period ended 30 June 2004 we mentioned that efforts were being made by the Company to improve stocking rates for this Project. We also reported that a block of 8 hectares had been laser levelled for re-planting on behalf of growers in the EKS 1 Project. Last years plantings were not successful on this area perhaps due to extremely hot conditions experienced last December. We are now able to report that this block has been re-planted in July this year with quite high quality seedlings and we are hopeful that this year the area will become properly established and that we will get a good survival rate for the first time.

The price of Sandalwood continues to rise at the Indian auctions in Tamil Nadu and at the latest auction in July 2005, the price had risen to \$US68,000 per tonne on average.

This compares with an average price per tonne of \$US60,000 at the same auctions in January 2005.

The following is an extract from a report prepared by our expert forester, Mr Peter Kimber, who reviewed the Plantation on nine occasions throughout the period:

Present State of the Plantation

The relatively low stocking rates of sandalwood trees in this plantation have been commented upon in previous reports and will be compensated for by the larger size of the existing trees and by the replanting program mentioned above.

The expert forester reports that all blocks in this plantation have remained healthy and free of pests and diseases.

Core samples were taken from 31 trees in this plantation which are now six years old.

The cores were sent to India for analysis and the results in summary were as follows:

- 3 trees had yet to start developing heartwood and oil
- 11 trees had detectable traces of oil.
- 9 trees had between 0.4% and 1.0% oil.
- 8 trees had between 1.0% and 2.35% oil.

MANAGER'S REPORT (CONTINUED)

These results are very encouraging, however it needs to be understood that at this early age the heartwood and oil will be confined to a narrow strip at the base of the tree, and the total amount would be very small indeed.

Maintenance Works Done in the Past Year

The smaller sandalwood trees in the plantation, originating from a second planting in the year 2000 to fill gaps, were again pruned to aid the development of a branch-free lower bole.

Climbers, mainly wild passionfruit, were controlled where they were threatening to smother the trees. Infestations of this plant are mainly confined to openings or gaps in the plantation where daylight penetrates to the ground and encourages germination of the seed, which is carried into the plantations by birds.

Irrigation furrows, tractor access lines, water-supply channels drains and access tracks into the plantations were maintained on a regular basis. In plantation blocks where volunteer *Leucena* trees had become dense they were slashed with a mango hedging machine in order to prevent them competing with the sandalwood crop and its host trees.

The plantations were irrigated every 5 to 6 weeks during the dry season. Irrigation was continued until February when there was good rainfall. However due to the short duration of the wet season, irrigation had to be resumed in March, much earlier than usual and as a result the total number of irrigation events over the year was more than is normally required.

Conclusion

These plantations are developing well and the expert forester has commented in relation to the trees which were core bored and analysed for their oil content "some had reached dimensions that would be expected in a tree of twice that age indicating the excellence of the site and the growing conditions."

Balance of Interests

As at 30 June 2005, the balance of lease interests held by Growers is 440 (30 June 2004: 440).

Interests Held by Responsible Entity and Related Parties

At 30 June 2005, 232 lease interests are held by Related Parties.

Of the lease interests held by related parties, 185 are a result of the termination of "Growers Agreements" due to a failure to pay lease and management fees when they are due.

Environmental Regulations

The Project is not subject to any significant environmental regulations under any State, Commonwealth or Territory Law.

Fees Paid to Manager and Associates

Fees of \$373,697 were paid to Tropical Forestry Services Ltd, the manager of EKS, for provision of its services during the period ended 30 June 2005 (period ended 30 June 2004: \$367,583).

Insurance of Officers of the Company or Auditors

No indemnities have been given or insurance premiums paid, during or since the end of the financial year, for any person who is or has been an officer or auditor of the Manager or the Project, other than the following.

The company that is related to the Manager has paid premiums to insure each of the directors against liabilities for costs and expenses incurred by them in defending any legal proceedings arising out of their conduct while acting in the capacity of director of the Manager. The cover included professional indemnity as well as directors and officers insurance. The total amount of the premium paid was \$66,550.

MANAGER'S REPORT (CONTINUED)

Auditor's Independence Declaration

The auditor's independence declaration for the year ended 30 June 2005 has been received and can be found on page 16 of the financial report.

For and on behalf of the Directors of Tropical Forestry Services Ltd:



Graeme Eric Scott

Perth, 30th September 2005



Independent Auditor's Report

To the Trustee of East Kimberley Sandalwood Project No.1

Scope

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for East Kimberley Sandalwood Project No.1 (the Project), for the year ended 30 June 2005.

The directors of the responsible entity 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 have conducted an independent audit of the financial report in order to express an opinion on it to the trustee of the Project. Our audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance 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 controls, 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, including compliance with Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the Project's financial position, and of its performance as represented by the results of its 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

We are independent of the Project, and have met the independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001

In accordance with ASIC Class Order 05/83, we declare to the best of our knowledge and belief that the auditor's declaration set out on page 16 of the financial report has not changed as at the date of providing our audit opinion.

Independent Auditor's Report

To the Trustee of East Kimberley Sandalwood Project No.1 (CONTINUED)

Audit Opinion

In our opinion, the financial report of East Kimberley Sandalwood Project No.1 is in accordance with:

- (a) the Corporations Act 2001, including:
 - (i) giving a true and fair view of the Project's financial position as at 30 June 2005 and of its performance for the year ended on that date; and
 - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and
- (b) other mandatory financial reporting requirements in Australia.



RIX LEVY FOWLER
Chartered Accountants



PHILLIP RIX FCA, A.S.I.A.
Partner

DATED at PERTH this 30th day of September 2005

EAST KIMBERLEY SANDALWOOD PROJECT NO.1
 STATEMENT OF FINANCIAL PERFORMANCE
 FOR THE YEAR TO 30 JUNE 2005

	NOTE	2005 \$	2004 \$
REVENUE FROM ORDINARY ACTIVITIES			
Establishment fees		-	-
Lease & management fees		373,697	367,583
Interest received		80	55
Net increment in net value of sandalwood trees		453,914	736,750
		<u>827,691</u>	<u>1,104,388</u>
EXPENSES FROM ORDINARY ACTIVITIES			
Accounting fees		1,500	2,775
Audit fees		2,000	4,125
Bad / Doubtful debt expense		67,348	3,510
Bank charges		27	196
Trustees Fees		4,485	415
Filing fees		-	1,033
Contractor Services		373,697	367,583
Reimbursement of expenses by Manager		(75,280)	(11,999)
		<u>373,777</u>	<u>367,638</u>
NET OPERATING INCOME FROM ORDINARY ACTIVITIES			
		<u>453,914</u>	<u>736,750</u>

The Statement of Financial Performance should be read in conjunction with the accompanying notes.

EAST KIMBERLEY SANDALWOOD PROJECT NO.1
STATEMENT OF FINANCIAL POSITION
AT 30 JUNE 2005

	NOTE	2005 \$	2004 \$
CURRENT ASSETS			
Cash	2	10,299	36,480
Receivables	3	6,228	46,690
Other	4	186,302	186,302
TOTAL CURRENT ASSETS		202,829	269,472
NON CURRENT ASSETS			
Sandalwood Trees	5	7,427,009	6,973,095
Other	4	1,304,115	1,490,417
TOTAL NON-CURRENT ASSETS		8,731,124	8,463,512
TOTAL ASSETS		8,933,953	8,732,984
CURRENT LIABILITIES			
Payables	6	6,527	73,170
Unearned Income	7	186,302	186,302
TOTAL CURRENT LIABILITIES		192,829	259,472
NON CURRENT LIABILITIES			
Unearned Income	7	1,304,115	1,490,417
TOTAL NON-CURRENT LIABILITIES		1,304,115	1,490,417
TOTAL LIABILITIES		1,496,944	1,749,889
NET ASSETS		7,437,009	6,983,095
GROWERS' FUNDS			
Trustee's reserve fund	8	10,000	10,000
Undistributed income reserve	8	7,427,009	6,973,095
EQUITY		7,437,009	6,983,095

The Statement of Financial Position should be read in conjunction with the accompanying notes.

EAST KIMBERLEY SANDALWOOD PROJECT NO.1
 STATEMENT OF CASH FLOWS
 FOR THE YEAR TO 30 JUNE 2005

	NOTE	2005 \$	2004 \$
CASH FLOWS FROM OPERATING ACTIVITIES			
<u>Inflows</u>			
Receipts from growers		265,227	153,111
Interest received		80	55
<u>(Outflows)</u>			
Payments to suppliers		(291,488)	(152,984)
	10(b)	(26,181)	182
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES			
Payment for establishment of plantations		-	-
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES			
Other		-	-
Net increase / (decrease) in cash held		(26,181)	182
Cash at beginning of financial year		36,480	36,298
Cash at end of financial year	10(a)	10,299	36,480

The Statement of Cash Flows should be read in conjunction with the accompanying notes.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR 30 JUNE 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Accounting

The financial report is a general purpose financial report which has been prepared in accordance with the Project's constitution and the requirements of the Corporations Act 2001, which includes applicable accounting standards. Other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) have also been complied with.

The financial report has been prepared in accordance with the historical cost convention, except for Sandalwood trees (which are self-generating assets), which are recorded at net market value.

(b) Revenue Recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Project and the revenue can be reliably measured. Specific revenues are recognised as follows.

Operations revenue:

- Sandalwood Lot sales (Establishment Fees) are recognised as revenue on acceptance of the application by the Responsible Entity.
- Lease and Management Fees are recognised as revenue in the period to which they relate.

(c) Sandalwood Trees

Sandalwood trees are measured at their market value at each reporting date. The net market value is determined as being the net present value of expected future cash flows (discounted at a risk adjusted rate).

Net increments or decrements in the market value of the Sandalwood trees are recognised as revenues or expenses in the Statement of Financial Performance, determined as:

- (i) the difference between the total net market values of the trees recognised as at the beginning of the period and the total net market values of the trees recognised as at the reporting date; less
- (ii) costs incurred during the reporting period to acquire and plant Sandalwood trees.

Costs incurred in maintaining or enhancing trees are recognised as expenses when incurred. Therefore, those costs are not included in the determination of the net increment in net market values.

(d) Income Tax

Under current legislation, the scheme is not subject to income tax provided the Growers are presently entitled to the income of the Project.

Unrealised gains and losses on investments which are regarded as income, are transferred to Growers' funds and are not distributable and assessable until realised. When income is realised, tax will be paid by the growers at the marginal rates of tax that exist under the relevant tax legislation at the date of realisation.

(e) Cash and Equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents includes cash on hand and in banks, and short-term deposits at call.

(f) Receivables

Receivables are recognised and carried at original invoice amount, or the amount due less a provision for any uncollectible debts. An estimate for doubtful debts is made when collection of the full amount is no longer probable.

(g) Payables

Liabilities for creditors and other amounts are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received. Payables to related parties are carried at the principal amount.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR 30 JUNE 2005 (CONTINUED)

(h) Unearned Income

Prepaid Lease and Management Fees are recognised on a straight line basis over the term of the project as this is considered to closely approximate the value of the service provided. The unearned portion is deferred and recorded as unearned income.

(i) Goods and Services Tax

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Taxation Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the Statement of Financial Position are shown inclusive of GST.

(j) Adoption of Australian Equivalents to International Financial Reporting Standards

The responsible entity is preparing and managing the transition to Australian Equivalents to International Financial Reporting Standards (AIFRS) effective for the financial years commencing from 1 January 2005. The adoption of AIFRS will be reflected in the scheme's financial statements for the year ending 30 June 2006. On first time adoption of AIFRS, comparatives for the financial year ended 30 June 2005 are required to be restated. The majority of the AIFRS transitional adjustments will be made retrospectively against retained earnings at 1 July 2004.

The responsible entity's management are assessing the significance of these changes and preparing for their implementation. The impact of the alternative treatments and elections under AASB 1: First Time Adoption of Australian Equivalents to International Financial Reporting Standards has been considered where applicable.

The directors of the responsible entity are of the opinion that there are no material differences in the accounting policies on conversion to AIFRS. Users of the financial statements should note, however, that the amounts disclosed could change if there are any amendments by standard setters to the current AIFRS or interpretation of the AIFRS requirements changes from the continuing work being performed by the responsible entity.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR TO 30 JUNE 2005 (CONTINUED)

	NOTE	2005 \$	2004 \$
2. CASH			
Cash at bank		10,299	36,480
3. RECEIVABLES			
Outstanding fees (i)		90,138	63,252
Less: Provision for doubtful debts		(83,910)	(16,562)
		6,228	46,690
 (i) Outstanding fees represent moneys receivable from growers for the cost of establishment of the plantation. No interest has been charged on amounts due.			
4. OTHER ASSETS			
Current			
Prepayments (i)		186,302	186,302
Non Current			
Prepayments (i)		1,304,115	1,490,417
 (i) prepayments represent lease and management fees paid to the manager in advance of the period in which the lease and management services are to be provided.			
5. SANDALWOOD TREES			
at cost of establishment (still to be planted at balance date)		-	-
at net market value (planted at balance date)		7,427,009	6,973,095
		7,427,009	6,973,095
(a) Physical quantity of sandalwood trees planted and owned			
Number of sandalwood trees		20,385	23,549
Area under lease (planted)		73.3	73.3
Area under lease (to be planted)		0.0	0.0
Growers in project (units)		440	440
(b) Nature of Asset			

Investors in EKS who are referred to as "Growers" subscribed for Sandalwood Lots of size one-sixth of a hectare each upon which sandalwood trees have been established.

The Sandalwood plantation is situated at King Location 255, approximately 22 kilometres from the Western Australian township of Kununurra.

The land upon which the Sandalwood plantation is located is leased by the Manager and sub-leased by the Growers. Growers lease the land from the Manager for the duration of the Project. The Project will continue in operation until the date on which the last of the Growers has been advised that the produce of the Sandalwood crop from each leased area which is leased by the Grower has been harvested and that the relevant Lease and Management Agreement has been terminated but in any event, not later than 31 December 2014.

The net market value of the Sandalwood trees has been determined in accordance with a Directors' valuation in accordance with the AASB's to reflect the market value of plantation.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR TO 30 JUNE 2005 (CONTINUED)

NOTE	2005 \$	2004 \$
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(c) Significant Assumptions

Significant assumptions made in determining the net market value of the trees are:

- 100% of the trees will be harvested and sold in 2013/2014;
- the price of Sandalwood is constant in real terms, though updated on an annual basis to reflect current market pricing;
- the costs expected to arise on harvest are constant in relative terms; and
- the pre-tax average real rate at which the net cash flows have been discounted is at 17% per annum

Cash flows exclude income taxes and are expressed in real terms.

6. PAYABLES

Trust funds payable to manager (i)	6,527	64,837
GST payable	-	(1,012)
Other	-	9,345
	<u>6,527</u>	<u>73,170</u>

(i) Trust funds payable to the manager represents the sum of monies payable by growers to the responsible entity under the lease and management agreement yet to be paid across. No interest in payable on outstanding amounts.

7. UNEARNED INCOME

Current

Prepaid lease & management fees	<u>186,302</u>	<u>186,302</u>
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Non Current

Prepaid lease & management fees	<u>1,304,115</u>	<u>1,490,417</u>
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8. TRUST FUNDS

Trustee's Reserve Fund

Represents moneys set aside in accordance with clause 14.1 of the trust deed which are to be used to reimburse the Trustee should the manager fail to pay or cause to be paid in full the Trustee for any costs incurred by the Trustee in accordance with clause 34 of the Trust Deed.

Opening balance	10,000	10,000
Net movement	-	-
Closing balance	<u>10,000</u>	<u>10,000</u>

Undistributed Income

The undistributed income reserve contains realised and unrealised income and expenses that are not yet assessable/deductible.

Opening balance	6,973,095	6,236,345
Net operating income	453,914	736,750
Closing balance	<u>7,427,009</u>	<u>6,973,095</u>

9. DISTRIBUTION PAID

No distributions were payable or paid during the period.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR TO 30 JUNE 2005 (CONTINUED)

	NOTE	2005 \$	2004 \$
10. STATEMENT OF CASHFLOWS			
(a) Reconciliation of cash			
Cash balance comprises:			
Cash at bank		10,299	36,480
(b) Reconciliation of net operating income to net cash flows from operating activities			
Net operating income		453,914	736,750
Adjustments:			
(Increase) / decrease in net receivables		40,462	(28,170)
(Increase) / decrease in prepayments		186,302	186,302
(Increase) / decrease in market value of sandalwood trees		(453,914)	(736,750)
Increase / (decrease) in payables		(66,643)	28,352
Increase / (decrease) in unearned income		(186,302)	(186,302)
Net cash inflow / (outflow) from operating activities.		(26,181)	182

11. RELATED PARTY DISCLOSURE

(a) Manager

The Manager of the project is Tropical Forestry Services Ltd, whose immediate and ultimate holding company is TFS Corporation Limited.

(b) Directors

The Directors of the Manager during the period were:

Frank Cullity WILSON
Graeme Eric SCOTT
Stephen Lee ATKINSON
Ronald Lionel EACOTT
Blaine David KIDD
Julius Luke MATTHYS
Thomas Nash CULLITY

(c) Fees

The Manager receives all of the Lease and Management Fees which have been paid by the Project during the period.

The Manager provides sandalwood plantation establishment and management services for the Project and carries out the custodial and administrative functions.

Transactions between the Project and Tropical Forestry Services Ltd result from normal dealings with that company as the Project's Manager.

(d) Holdings of Directors and Director Related Entities

A total of 47 lease interests are held by Directors or parties related to Directors on the same terms and conditions as other Growers. No amount is outstanding at year end.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR TO 30 JUNE 2005 (CONTINUED)

12. TRUSTEE

(a) Trustee

The Trustee during the year was Professional Funds Management Pty Ltd

(b) Trustee's Remuneration

\$4,485 (GST exclusive) was paid to the Trustee by the Trustee for provision of their services during the period ended 30 June 2005.

13. AUDIT

Rix Levy Fowler are the auditors of the Project.

14. SEGMENT INFORMATION

The Project operates in one industry segment, being investment activities and in one geographical segment, being Australia.

15. SUBSEQUENT EVENTS

Since 30 June 2005, there has not been any matter or circumstance not otherwise dealt with in the financial report that has significantly affected or may significantly affect the Project.

16. FINANCIAL INSTRUMENTS

(a) Interest Rate Risk

Interest rate risk is the risk that a financial investment's value will fluctuate as a result of changes in market interest rates. The Project's exposure to interest rate risk is as follows:

Financial Assets

Cash	\$10,299
Weighted average debit interest rate (p.a.)	0%
Weighted average credit interest rate (p.a.)	3.00%
Interest rate type	Variable

The Project had no other financial assets or financial liabilities with exposure to interest rate risk as at balance date.

(b) Credit Risk

Credit risk represents the risk that a counterparty will fail to perform contractual obligations under a contract. The Project's only credit risk exposure relates to debtors who comprise the receivable balance at 30 June 2005. A provision for doubtful accounts is recognised when collection of the full nominal amount is uncertain.

(c) Net Fair Value

The Project's financial assets and liabilities included in the Statement of Financial Position are carried at their net fair value. Refer to Note 1 for the methods and assumptions adopted in determining net fair values for Sandalwood trees.

TRUSTEE'S REPORT FOR THE YEAR TO 30 JUNE 2005

The financial statements for the year ended 30 June 2005 have been prepared by us and audited by Rix Levy Fowler, the auditors appointed by us in accordance with the trust deed.

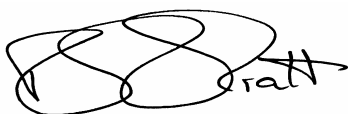
Based upon our ongoing programme of monitoring the Trust and the Manager, we believe that:

- (i) the Trust has been conducted in accordance with its stated investment policies, and the trust deed; and
- (ii) the financial statements have been appropriately prepared and contain all relevant and required disclosures.

We are not aware of any material or significant changes in the state of affairs of the Trust occurring up to the date of this report that require disclosure in the financial statements and the notes thereto that have not already been disclosed.

Review of Operations and Results

Based upon the auditor's report and the Manager's representations, in our opinion the financial statements set out above are drawn up so as to present fairly the operations and results of the Trust for the year ended 30 June 2005.



R. M Pratt
Director
Professional Funds Management Pty Ltd

Dated: this 30th day of September 2005



To the Trustee of East Kimberley Sandalwood Project No.1

Auditor's Independence Declaration

This declaration is made in connection with our audit of the financial report of East Kimberley Sandalwood Project No.1 for the year ended 30 June 2005 and in accordance with the provisions of the Corporations Act 2001.

We declare that, to the best of our knowledge and belief, there have been:

- No contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to this audit;
- No contraventions of the Code of Professional Conduct of the Institute of Chartered Accountants in Australia in relation to this audit.

Yours faithfully

RIX LEVY FOWLER
Chartered Accountants

PHILLIP RIX FCA, A.S.I.A.
Partner

DATED at PERTH this 30th day of September 2005