

# EAST KIMBERLEY SANDALWOOD PROJECT NO. 1

ANNUAL FINANCIAL REPORT  
FOR YEAR ENDED 30 JUNE 2004

# CONTENTS

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	<b>PAGE</b>
MANAGER'S REPORT	1
AUDITOR'S REPORT	4
STATEMENT OF FINANCIAL PERFORMANCE	6
STATEMENT OF FINANCIAL POSITION	7
STATEMENT OF CASH FLOWS	8
NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS	9
TRUSTEE'S DECLARATION	17

## MANAGER'S REPORT

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The Directors of Tropical Forestry Services Ltd (ACN 081 046 353), Manager of East Kimberley Sandalwood Project No. 1 ("EKS 1"), present their report together with the financial statements of the East Kimberley Sandalwood Project No. 1 ("the Project") for the year ended 30 June 2004, to the Growers in EKS1.

### **Directors**

The names of Directors of Tropical Forestry Services Ltd ("the Company") during the half year 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 year the principal activity of the Project continued to be the management of a Sandalwood plantation.

### **Change of State of Affairs**

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

### **Operations and Likely Developments**

The Project made a profit for the financial year ended 30 June 2004 of \$736,750.

This is due to an increase in the valuation of the plantation.

The EKS 1 plantation was originally established in 1999, and trees are now 5 years old.

In our report to you of 31 December 2003 we mentioned that efforts were being made by the Company to improve stocking rates for this Project. As we previously reported, stocking levels of Indian Sandalwood have been well below desired levels resulting in some replacement plantings in 2000. 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. We are now able to report that this block has been re-planted in August this year and preliminary indications are promising in relation to it.

We also note that our expert forester's report is to the effect that a total of 10 trees in the EKS 1 Project were bored with a small diameter drill and at the age of 5 each showed the development of heartwood and 4 out of 5 showed detectable traces of Sandalwood oil.

It was also encouraging to note that an earlier problem previously reported on relating to Phytophthora root rot had not re-occurred.

The price of Sandalwood continues to rise at the Indian auctions in Tamil Nadu and at the latest auction in September 2004, on a relatively thin trade, the price had risen to \$US45,000 per tonne on average.

## MANAGER'S REPORT (CONTINUED)

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This compares with an average price per tonne of \$US35,000 at the same auctions in January 2003.

### **Maintenance Works Done in the Past Year**

The following is an extract from a report prepared by our expert forester, Mr Peter Kimber, who reviewed the plantation on a monthly basis:

Management activities included irrigation and also access tubes were placed on block 83C to allow the measurement of soil moisture using a 'Diviner 2000' moisture probe. Moisture probing allows data collection for the purposes of providing guidelines as to the optimal time to irrigate the plantation.

Other activities included the pruning of Sandalwood trees to a height of 2.5 metres above the bole and the removing of the branches of mahogany trees which were overtopping the Sandalwood.

Tractor access rows were mechanically slashed to break down woody debris and to control weeds. Irrigation furrows were also maintained throughout the year using a 'go-devil' – a set of opposed plough discs which cultivates to create a mound of soil with a furrow on either side, through which irrigation water can travel.

### **Present State of the Plantation**

The host species *Cassia siamea* continue to thrive together with the other host species *Cathormium umbellatum* and *Sesbania formosa*. The latter two are growing well but in lower numbers than the *Cassia*.

The Sandalwood trees from the original planting continue to exceed their expected growth rate and their size at 5 years of age. Measurement of sample trees in the plantation has commenced which will provide a more objective indicator of their development.

### **Conclusion**

The East Kimberley Sandalwood plantation has developed to the point where it is flourishing with the Sandalwood trees growing quickly. Poor stocking levels are likely to be compensated for both by the larger size of the original trees and by the fact that the Company has re-planted 8 hectares for EKS 1 Growers as noted above and holds an additional 25 hectares on trust for EKS 1 Growers in the Company's Packsaddle plantation as noted in our report for the period to 31 December 2003.

### **Balance of Interests**

As at 30 June 2004, the balance of lease interests held by growers is 440 (30 June 2003: 440).

### **Interests Held by Manager and Related Parties**

As at 30 June 2004, 185 lease interests are held by the Manager (30 June 2003: 185) and 47 lease interests are held by related parties (30 June 2003: 47).

The lease interest held by the Manager are as a result of the termination of Grower agreements due to the failure to pay Lease and Management Fees when they were due despite repeated requests since the inception of the Project.

## MANAGER'S REPORT (CONTINUED)

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### **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 \$367,583 were paid to Tropical Forestry Services Ltd the Manager of East Kimberley Sandalwood Project No. 1 for provision of its services during the period ended 30 June 2004 (period ending 30 June 2003: \$268,810).

### **Insurance of Officers of the Company or Auditors**

Neither the Project nor Tropical Forestry Services Ltd has during or since the end of the financial year in respect of any person who is or has been an officer of Tropical Forestry Services Ltd or a related body corporate or auditor of the Project:

- indemnified or made any relevant agreement for indemnifying against a liability, including costs and expenses in successfully defending legal proceedings; or
- paid or agreed to pay a premium in respect of a contract insuring against a liability for the costs or expenses to defend legal proceedings.

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



**Graeme Eric Scott**

Perth, 21 December 2004



# Rix Levy Fowler

CHARTERED BUSINESS ADVISORS

## Independent Audit Report to the Trustee of East Kimberley Sandalwood Project No. 1

**Partners:**

Phillip Rix FCA  
Ranko Matic CA  
George Lazarou CA  
Jon Carcich CA

**Services:**

Accounting  
Audit & Assurance  
Business Financing  
Business Reviews  
Corporate Secretarial  
Financial Planning  
IT Solutions  
Superannuation  
Taxation Planning

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### Scope

*The financial report and trustees' 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 trustee's declaration for East Kimberley Sandalwood Project No. 1 (the project), for the financial year ended 30 June 2004.

The trustee is responsible for the preparation and true and fair presentation of the project's 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 form an opinion whether, in all material respects, the financial report is presented fairly in accordance with the Corporations Act 2001 and Accounting Standards and other mandatory professional reporting requirements in Australia so as to present a view which is consistent with our understanding of the project's financial position, and performance as represented by the results of its operations and its cash flows.

Our procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial report, and the evaluation of accounting policies and significant accounting estimates made by the directors of the responsible entity.

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.

The audit opinion expressed in this report has been formed on the above basis.

### Independence

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

# Independent Auditor's Report

to the Trustee of East Kimberley Sandalwood Project No. 1 (continued)

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## 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 2004 and of their performance for the year ended on that date; and
  - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and
- (b) other mandatory professional reporting requirements in Australia.



**RIX LEVY FOWLER**  
Chartered Business Advisors



**PHILLIP RIX**  
Partner

DATED at PERTH this 22<sup>nd</sup> day of December 2004

**STATEMENT OF FINANCIAL PERFORMANCE  
FOR THE YEAR ENDED 30 JUNE 2004**

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	Notes	2004 \$	2003 \$
<b>REVENUE FROM ORDINARY ACTIVITIES</b>			
Lease and Management Fees		367,583	268,810
Interest income		55	25
Net increment in net market value of Sandalwood trees	1 (d)	<u>736,750</u>	<u>734,934</u>
		1,104,388	1,003,769
<b>EXPENSES FROM ORDINARY ACTIVITIES</b>			
Accountancy fees		2,775	-
Auditor's remuneration		4,125	4,950
Doubtful debts expense		3,510	-
Filing fees		1,033	-
Bank charges		196	184
Trustee's fees		415	13,648
Contractor services		367,583	268,810
Reimbursement of expenses by Manager		<u>(11,999)</u>	<u>(18,756)</u>
		<u>367,638</u>	<u>268,836</u>
<b>PROFIT/(LOSS) FROM ORDINARY ACTIVITIES</b>		<b><u>736,750</u></b>	<b><u>734,933</u></b>

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

STATEMENT OF FINANCIAL POSITION  
AT 30 JUNE 2004

	Notes	2004 \$	2003 \$
<b>CURRENT ASSETS</b>			
Cash	2	36,480	36,298
Receivables	3	47,702	19,532
Prepayments	4	186,302	186,302
<b>TOTAL CURRENT ASSETS</b>		<b>270,484</b>	<b>242,132</b>
<b>NON CURRENT ASSETS</b>			
Sandalwood trees	5	6,973,095	6,236,345
Prepayments	6	1,490,417	1,676,719
<b>TOTAL NON CURRENT ASSETS</b>		<b>8,463,512</b>	<b>7,913,064</b>
<b>TOTAL ASSETS</b>		<b>8,733,996</b>	<b>8,155,196</b>
<b>CURRENT LIABILITIES</b>			
Payables	7	74,182	45,830
Unearned income	8	186,302	186,302
<b>TOTAL CURRENT LIABILITIES</b>		<b>260,484</b>	<b>232,132</b>
<b>NON-CURRENT LIABILITIES</b>			
Unearned income	9	1,490,417	1,676,719
<b>TOTAL NON-CURRENT LIABILITIES</b>		<b>1,490,417</b>	<b>1,676,719</b>
<b>TOTAL LIABILITIES</b>		<b>1,750,901</b>	<b>1,908,851</b>
<b>NET ASSETS</b>		<b>6,983,095</b>	<b>6,246,345</b>
<b>TRUST FUNDS</b>			
Trustee's Reserve Fund	10	10,000	10,000
Undistributed Income Reserve	10	6,973,095	6,236,345
<b>TOTAL TRUST FUNDS</b>		<b>6,983,095</b>	<b>6,246,345</b>

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

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED 30 JUNE 2004**

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	Notes	2004 \$	2003 \$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Lease and Management Fees received		153,111	268,810
Interest received		55	26
Other monies received		-	-
Payments to suppliers		(152,788)	(279,913)
Refunds to Growers		-	-
Bank charges		(196)	(184)
<b>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>	12	<u>182</u>	<u>(11,261)</u>
<b>NET INCREASE (DECREASE) IN CASH HELD</b>		<b>182</b>	<b>(11,261)</b>
Add opening cash brought forward		<u>36,298</u>	<u>47,559</u>
<b>CLOSING CASH CARRIED FORWARD</b>	12	<u><b>36,480</b></u>	<u><b>36,298</b></u>

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 ENDED 30 JUNE 2004 (CONTINUED)

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## 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 Trust Deed 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) Changes in Accounting Policies

The accounting policies adopted are consistent with those of the preceding corresponding reporting period.

### (d) Sandalwood Trees

The Project has adopted Accounting Standard AASB 1037 "Self-Generating and Regenerating Assets". Sandalwood trees are measured at their net 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 of 17%).

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 the 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.

## NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

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### **(e) 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.

### **(f) 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.

### **(g) Receivables**

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

### **(h) 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.

### **(i) 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.

### **(j) 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.

### **(k) Adoption of Australian Equivalents to International Financial Reporting Standards**

Australia is currently preparing for the introduction of International Financial Reporting Standards (IFRS) effective for financial years commencing 1 January 2005. This requires the production of accounting data for future comparative purposes at the beginning of the next financial year.

The economic entity's management, along with its auditors, are assessing the significance of these changes and preparing for their implementation. Stakeholders will be kept informed as to the impact of these new standards on the financial statements as they are finalised.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

	2004 \$	2003 \$
<b>2. CASH</b>		
Cash at bank	<u>36,480</u>	<u>36,298</u>
<b>3. RECEIVABLES</b>		
Outstanding Lease & Management Fees (i)	63,252	31,916
Less: Provision for doubtful debts	<u>(16,562)</u>	<u>(13,052)</u>
	<u>46,690</u>	<u>18,864</u>
Other (ii)	<u>1,012</u>	<u>668</u>
	<u>47,702</u>	<u>19,532</u>
(i) Outstanding Establishment Fees represent moneys receivable from Growers in accordance with the Lease and Management Agreement. No interest has been charged on amounts due.		
(ii) Other represents GST receivable from Manager.		
<b>4. OTHER ASSETS</b>		
Prepayments (i)	<u>186,302</u>	<u>186,302</u>
(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.		
<b>5. SANDALWOOD TREES</b>		
<i>at net market value</i>	<u>6,973,095</u>	<u>6,236,345</u>
<b>(a) Physical Quantity of Sandalwood Trees Owned</b>		
Number of Sandalwood trees	23,549	25,810
Area under lease (Ha)	<u>73</u>	<u>73</u>

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

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2004  
\$

2003  
\$

**(b) Nature of Asset**

Investors in the East Kimberley Sandalwood Project No. 1 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 254, 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 to 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.

**(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 real 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. OTHER ASSETS**

Prepayments (i)	<u>1,490,417</u>	<u>1,676,719</u>
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- (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.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

	2004 \$	2003 \$
<b>7. PAYABLES</b>		
Trust funds payable to the Manager (i)	64,837	38,482
Other (ii)	<u>9,345</u>	<u>7,348</u>
	<u>74,182</u>	<u>45,830</u>

(i) Trust funds payable to the Manager represent the sum of monies payable by Growers to the Manager under the Lease and Management Agreement yet to be paid across to the Manager. No interest is payable on outstanding amounts.

(ii) Other represents Trustee Funds Payable.

**8. UNEARNED INCOME (CURRENT)**

Prepaid Lease & Management Fees (i)	<u>186,302</u>	<u>186,302</u>
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(i) Represents Lease and Management Fees received upfront for services to be provided over the next twelve months.

**9. UNEARNED INCOME (NON-CURRENT)**

Prepaid Lease & Management Fees (i)	<u>1,490,417</u>	<u>1,676,719</u>
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(i) Represents Lease and Management Fees received upfront for services to be provided beyond the next twelve months.

**10. TRUST FUNDS**

**Trustee's Reserve Fund**

Nature and purpose of reserve

Represents monies 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	<u>-</u>	<u>-</u>
Closing balance	<u>10,000</u>	<u>10,000</u>



NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

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2004  
\$

2003  
\$

**13. RELATED PARTY DISCLOSURES**

**(a) Manager**

The Manager of the Project is Tropical Forestry Services Ltd.

**(b) Directors**

The Directors of the Manager during the year 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 received all of the Lease and Management Fees, which have been deducted from 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 and holder of a dealer's license.

**(i) Manager**

Total fees paid for provision of its services during the year.

367,583

268,810

**(d) Directors' Holdings**

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.

**14. TRUSTEE**

**(a) Trustee**

The Trustee during the year was Professional Funds Management Pty Ltd.

**(b) Trustee's Remuneration**

\$415 was paid to the Trustee, by the Manager, for provision of its services during the year ended 30 June 2004 (year ended 30 June 2003: \$13,648).

## NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2004 (CONTINUED)

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### 15. AUDIT

#### (a) Auditors

The auditors of the Project are Rix Levy Fowler.

#### (b) Auditors' Remuneration

\$4,125 is payable to the auditors, by the Manager, for provision of their services during the year ended 30 June 2004 (year ended 30 June 2003: \$4,950).

### 16. FINANCIAL INSTRUMENTS

#### (a) 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 2004. A provision for doubtful accounts is recognised when collection of the full nominal amount is uncertain.

#### (b) Net Fair Value

The Project's financial assets and liabilities included in the Statement of Financial Position are carried at their net fair value.

### 17. SEGMENT INFORMATION

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

### 18. SUBSEQUENT EVENTS

Since 30 June 2004, 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.

## TRUSTEE'S DECLARATION FOR THE YEAR ENDED 30 JUNE 2004

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The financial statements for the year ended 30 June 2004 have been prepared by us and audited and audited by Rix Levy Fowler, the auditors appointed by us in accordance with the Trust Deed.

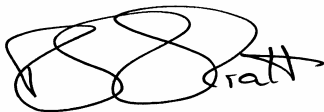
Based upon our ongoing programme of monitoring the Trust and the Manager, we believe that:

- (i) the Trust has been conducted in accordance with its stated investment policies, 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 on pages 6 to 16 are drawn up so as to present fairly the operations and results of the Trust for the year ended 30 June 2004.



R. M. Pratt  
Director  
**Professional Funds Management Pty Ltd**