QrxPharma Pty Limited
ACN 102 254 151

Annual report – 30 June 2005

Contents

Directors' report

Your directors present their report on the consolidated entity consisting of QrxPharma Pty Limited (the company) and the entities it controlled at the end of, or during, the year ended 30 June 2005.

Directors
The following persons were directors of QrxPharma Pty Limited during the whole of the financial year and up to the date of this report:

M Quinn
GW Pace
MS Hirshorn
G Savage
DA Henderson

R Creswell was appointed a director on 19 October 2004 and remains in office at the date of this report.

D Stack was appointed a director on 18 May 2005 and remains in office at the date of this report.

Principal activities
The principal activity of the consolidated entity during the course of the financial year was the development and commercialisation of biopharmaceutical products based on Australian research and targeting the US market.

Dividends
No dividends were paid or declared since the start of the financial year.

Review of operations
The consolidated entity has made a loss from ordinary activities after income tax for the period of $ 4,673,208 (2004: loss of $4,219,967).

Significant changes in the state of affairs
There were no significant changes in the state of affairs of the consolidated entity that occurred during the financial year under review.

Matters subsequent to the end of the financial year
Since balance date, the consolidated entity has entered into a contract with an investment adviser to act as exclusive placement agent for the issue of new shares to private investors.

No other matter or circumstance has arisen since 30 June 2005 that has significantly affected, or may significantly affect:
- the consolidated entity's operations in future financial years, or
- the results of those operations in future financial years, or
- the consolidated entity's state of affairs in future financial years.

Likely developments and expected results of operations
Information about likely developments in the operations of the consolidated entity and the expected results of those operations has not been included in this report because the directors believe would be likely to result in unreasonable prejudice to the consolidated entity.

Environmental regulation
There are no particular and significant environmental regulations under a law of the Commonwealth or of a State or Territory affecting the consolidated entity.

Share options granted to directors
Options over unissued ordinary shares of QrxPharma Pty Limited granted during or since the end of the financial year to any of the directors of the Company and consolidated entity were as follows:

Directors	*Options granted*
R Creswell	100,000
D Stack	240,000

Directors' report (continued)

Shares under option
Unissued ordinary shares of QrxPharma Pty Limited under option at the date of this report are as follows:

Date options granted	Expiry date	Issue price of shares	Number
19 December 2002	19 December 2012	$1.50	40,000
19 February 2003	19 February 2006	$0.15	40,000
21 November 2003	21 November 2005	$0.15	5,000
1 December 2003	1 December 2006	$0.15	20,000
15 December 2003	15 December 2013	$0.15	50,000
24 February 2004	24 February 2014	$0.15	15,000
24 February 2004	24 February 2007	$0.15	10,000
24 February 2004	24 February 2014	$1.50	20,000
25 February 2004	24 February 2014	$0.15	5,000
16 March 2004	16 March 2014	$0.15	10,000
19 May 2004	19 May 2014	$0.15	25,000
24 June 2004	24 June 2014	$0.15	20,000
13 July 2004	13 July 2014	$0.15	50,000
14 July 2004	14 July 2014	$0.15	40,000
17 August 2004	17 August 2014	$0.15	20,000
19 October 2004	19 October 2014	$0.15	100,000
19 February 2005	19 February 2015	$0.15	150,000
18 May 2005	18 May 2015	$0.15	240,000

Shares issued on the exercise of options
The following ordinary shares of QrxPharma Pty Limited were issued during the year ended 30 June 2005 on the exercise of options granted under the QrxPharma Employee Option Plan. No further shares have been issued since that date. No amounts are unpaid on any of the shares.

Date options granted	Issue price of shares	Number of shares issued
19 February 2003	$0.15	45,000
7 June 2004	$0.15	30,000

Insurance of officers
During the financial year, the Company made, in respect of the directors and officers of the Company an agreement for indemnifying against a liability incurred as an officer, including costs and expenses in successfully defending legal proceedings. Insurance premiums have been paid in respect of Directors' and Officers Liability insuring against a liability incurred as an officer for the costs or expenses to defend legal proceedings.

Proceedings on behalf of 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*.

Auditor
PricewaterhouseCoopers continues in office in accordance with section 327 of the *Corporations Act 2001*.

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

M A Quinn
Director

Sydney
25 October 2005

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Auditors' Independence Declaration

As lead auditor for the audit of QrxPharma Pty Limited for the year ended 30 June 2005, 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 QrxPharma Pty Limited and the entities it controlled during the period.

Andrew Sneddon
Partner
PricewaterhouseCoopers

Sydney
25 October 2005

QrxPharma Pty Limited
ACN 102 254 151

Financial report

30 June 2005

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This financial report covers QrxPharma Pty Limited as an individual entity and the consolidated entity consisting of QrxPharma Pty Limited and its controlled entities.

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

QrxPharma Pty Limited
Suite 401, 35 Lime St,
Sydney NSW 2000

A description of the nature of the consolidated entity's operations and its principal activities is included in the directors' report on pages 1 to 2.

Statements of financial performance

For the year ended 30 June 2005

		Consolidated		Parent	
		2005	2004	**2005**	2004
	Notes	**$**	$	**$**	$
Revenue from ordinary activities	2	**72,287**	102,503	**72,287**	101,349
Expenses from ordinary activities					
Research and development	3	**(3,422,847)**	(3,041,454)	**(3,422,847)**	(3,041,454)
Marketing		**(617,841)**	(206,261)	**(617,841)**	(206,361)
General & administration		**(621,940)**	(1,074,660)	**(621,940)**	(1,075,352)
Borrowing costs expense	3	**(82,867)**	-	**(82,867)**	-
Loss from ordinary activities before income tax expense	3	**(4,673,208)**	(4,219,967)	**(4,673,208)**	(4,221,818)
Income tax expense	4	-	-	-	-
Net loss		**(4,673,208)**	(4,219,967)	**(4,673,208)**	(4,221,818)

The above statements of financial performance should be read in conjunction with the accompanying notes.

Statements of financial position

As at 30 June 2005

		Consolidated		Parent	
		2005	2004	**2005**	2004
	Notes	**$**	$	**$**	$
Current assets					
Cash assets	5	**1,412,133**	3,654,256	**1,412,133**	3,654,256
Receivables	6	**-**	12,752	**-**	12,752
Total current assets		**1,412,133**	3,667,008	**1,412,133**	3,667,008
Non-current assets					
Plant and equipment	7	**48,330**	65,421	**48,330**	65,421
Other financial assets	8	**-**	-	**-**	-
Total non-current assets		**48,330**	65,421	**48,330**	65,421
Total assets		**1,460,463**	3,732,429	**1,460,463**	3,732,429
Current liabilities					
Payables	9	**831,213**	526,706	**858,913**	554,406
Provisions	10	**17,000**	17,971	**17,000**	17,971
Interest bearing liabilities	11	**2,139,325**	-	**2,139,325**	-
Total current liabilities		**2,978,538**	544,677	**3,015,238**	572,377
Non-current liabilities					
Provisions	12	**2,244,891**	1,199,547	**2,244,891**	1,199,547
Total non-current liabilities		**2,244,891**	1,199,547	**2,244,891**	1,199,547
Total liabilities		**5,232,429**	1,744,224	**5,260,129**	1,771,924
Net assets / (liabilities)		**(3,771,966)**	1,988,205	**(3,799,666)**	1,960,505
Equity					
Contributed equity	13	**10,527,652**	10,569,271	**10,527,652**	10,569,271
Accumulated losses	14	**(14,299,618)**	(8,581,066)	**(14,327,318)**	(8,608,766)
Total equity / (deficiency in capital)		**(3,771,966)**	1,988,205	**(3,799,666)**	1,960,505

The above statements of financial position should be read in conjunction with the accompanying notes.

Statements of cash flows
For the year ended 30 June 2005

		Consolidated		Parent	
		2005	2004	**2005**	2004
		$	$	**$**	$
	Notes				
Cash flows from operating activities					
Payments to suppliers and employees (inclusive of goods and services tax)		**(4,637,169)**	(4,380,612)	**(4,637,169)**	(4,381,309)
Interest received		**72,287**	102,503	**72,287**	101,349
R&D grant received		**227,326**	175,895	**227,326**	175,895
GST tax refund		**9,752**	171,219	**9,752**	171,219
Net cash (outflow) from operating activities	20	**(4,327,804)**	(3,930,995)	**(4,327,804)**	(3,932,846)
Cash flows from investing activities					
Payments for property, plant and equipment		**(12,025)**	(17,210)	**(12,025)**	(17,210)
Net cash (outflow) from investing activities		**(12,025)**	(17,210)	**(12,025)**	(17,210)
Cash flows from financing activities					
Proceeds from intercompany loan		**-**	-	**-**	27,700
Proceeds from borrowings		**2,139,325**	-	**2,139,325**	-
Proceeds from issues of shares		**11,250**	4,607,948	**11,250**	4,607,948
Share issue transaction costs		**(52,869)**	(51,358)	**(52,869)**	(51,358)
Net cash inflow from financing activities		**2,097,706**	4,556,590	**2,097,706**	4,584,290
Net (decrease)/increase in cash held		**(2,242,133)**	608,385	**(2,242,123)**	634,234
Cash at the beginning of the financial year		**3,654,256**	3,045,871	**3,654,256**	3,020,022
Cash at the end of the financial year	5	**1,412,133**	3,654,256	**1,412,133**	3,654,256

The above statements of cash flows should be read in conjunction with the accompanying notes.

Notes to the financial statements
30 June 2005

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Note 1 Summary of significant accounting policies

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

It is prepared in accordance with the historical cost convention, except for certain assets which, as noted, are at valuation. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year.

The Australian Accounting Standards Board (AASB) is adopting International Financial Reporting Standards (IFRS) for application to reporting periods beginning on or after 1 January 2005. The AASB has issued Australian equivalents to IFRS (AIFRS), and the Urgent Issues Group has issued interpretations corresponding to IASB interpretations originated by the International Financial Reporting Interpretations Committee or the former Standing Interpretations Committee. The adoption of AIFRS will be first reflected in the consolidated entity's financial statements for year ending 30 June 2006. Information about how the transition to AIFRS is being managed, and the key differences in accounting policies that are expected to arise, is set out in note 25.

(a) Going concern

The consolidated entity has continued to experience operating losses of $4,673,208 and operating cash outflows of $4,327,804 during the year ending 30 June 2005 as the consolidated entity continues to focus on the achievement of key milestones set out in the funding of its R&D program and operating plan. As of balance date, the consolidated entity had a deficiency in capital of $3,771,966 and cash balances of $1,412,133. The continuing viability of the company and its controlled entities and their ability to continue as a going concern and meet their debts and commitments as they fall due is dependent upon:

(i) the consolidated entity being successful in negotiating and obtaining additional funding, including securing equity financing and government research and development grants based on continued achievement of key milestones in the R&D program; and
(ii) The consolidated entity successfully implementing its business strategy and operating plan.

The consolidated entity's short operating history and reliance on future funding and successfully executing its business strategy result in there being significant uncertainty whether the consolidated entity will continue as a going concern and, therefore, whether it will realise its assets and settle its liabilities and commitments in the normal course of business and at the amounts stated in the financial report.

However, subsequent to year end, the consolidated entity has negotiated a contract with an investment adviser to seek funding through private equity placements. Up to $25 million is sought through this round of funding. Hence, the directors believe that the consolidated entity will be successful in the above matters, and accordingly, have prepared the financial report on a going concern basis. The directors regularly monitor the consolidated entity's cash position and on an on-going basis consider a number of strategic and operational plans and initiatives to ensure that adequate funding continues to be available for the consolidated entity to meet its business objectives.

At this time, the directors are of the opinion that no asset is likely to be realised for an amount less than the amount at which it is recorded in the financial report at 30 June 2005. No adjustments have been made to the financial report relating to recoverability and classification of the asset carrying amounts or the amounts and classification of liabilities that might be necessary should the Company not continue as a going concern.

(b) Principles of consolidation

The consolidated financial statements incorporate the assets and liabilities of all entities controlled by QrxPharma Pty Limited as at 30 June 2005 and the results of all controlled entities for the year then ended. QrxPharma Pty 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.

Note 1 Summary of significant accounting policies (continued)

(c) Income tax

Tax effect accounting procedures are followed whereby the income tax expense in the statement of financial performance is matched with the accounting profit after allowing for permanent differences. The future tax benefit relating to tax losses or cumulative timing differences is not carried forward as an asset unless the benefit is virtually certain of realisation.

(d) Foreign currency translation

Transactions

Foreign currency transactions are initially translated into Australian currency at the rate of exchange at the date of the transaction. At balance date amounts payable and receivable in foreign currencies are translated to Australian currency at rates of exchange current at that date. Resulting exchange differences are recognised in determining the profit or loss for the year.

(e) Acquisitions of assets

The purchase method of accounting is used for all acquisitions of assets regardless of whether equity instruments or other assets are acquired. Cost is measured as the fair value of the assets given up, shares issued or liabilities undertaken at the date of acquisition plus incidental costs directly attributable to the acquisition. Where equity instruments are issued in an acquisition, the value of the instruments is determined by reference to the fair value of the assets acquired, including goodwill where applicable. Transaction costs arising on the issue of equity instruments are recognised directly in equity.

(f) 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, 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 profit or loss in the reporting period in which the recoverable amount write-down occurs.

The expected net cash flows included in determining recoverable amounts of non-current assets are not discounted.

(g) Depreciation of property, plant and equipment

Depreciation is calculated on a straight line basis to write off the net cost of each item of plant and equipment over its expected useful life to the consolidated 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:

Plant & equipment	4 years

(h) Trade and other creditors

These amounts represent liabilities for goods and services provided to the consolidated entity 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.

(i) Grant income

Grant income is recognised during the year in which the income is received and is disclosed in the results for the period against related R&D expenditure incurred in the period.

Note 1 Summary of significant accounting policies (continued)

(j) Employee benefits

(i) Wages and salaries and annual leave

Liabilities for wages and salaries and annual leave expected to be settled within 12 months of the reporting date are recognised in other creditors in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled.

(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.

(iii) Employee benefit on-costs

Employee benefit on-costs, including payroll tax, are recognised and included in employee benefit liabilities and costs when the employee benefits to which they relate are recognised as liabilities.

(iv) Equity-based compensation benefits

Equity-based compensation benefits are provided to employees via the QrxPharma Employee Share Option Plan. Information relating to these schemes is set out in note 23.

No accounting entries are made in relation to the QrxPharma Employee Share Option Plan until options are exercised, at which time the amounts receivable from employees are recognised in the statement of financial position as share capital.

(k) Interest bearing liabilities

Convertible notes are included as a liability based upon the principle value of the notes. The liability is included in borrowings until conversion or maturity of the notes. Interest on the convertible notes is accrued at a rate of 10% p.a. and is included in other creditors.

(l) Borrowing costs

Borrowing costs are recognised as expenses in the period in which they are incurred. Borrowing costs include interest paid or payable on convertible notes.

(m) Cash

For purposes of the statement of cash flows, cash includes deposits at call with financial institutions and other highly liquid investments with short periods to maturity which are readily convertible to cash on hand and are subject to an insignificant risk of changes in value, net of outstanding bank overdrafts.

Note 2 Revenue

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Revenue from outside the operating activities				
Interest	**72,287**	102,503	**72,287**	101,349
Revenue from ordinary activities	**72,287**	102,503	**72,287**	101,349

Note 3 Loss from ordinary activities

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Net expenses				
Loss from ordinary activities before income tax expense includes the following specific net expenses:				
Expenses				
Depreciation				
Plant and equipment	**29,116**	26,955	**29,116**	26,955
Net foreign exchange loss	**26,258**	33,814	**26,258**	33,814
Borrowing costs				
Interest payable on convertible notes	**82,867**	-	**82,867**	-
Research and development expensed	**3,547,722**	3,157,256	**3,422,847**	2,835,884
Research and development grant	**(124,875)**	(115,802)	**(124,875)**	(115,802)
Net research and development	**3,422,847**	3,041,454	**3,422,847**	3,041,454

Note 4 Income tax

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
(a) Income tax expense				
The income tax expense for the financial period differs from the amount calculated on the operating loss. The differences are reconciled as follows:				
Operating loss before income tax	**(4,673,209)**	(4,219,967)	**(4,673,209)**	(4,221,818)
Income tax calculated at 30%	**(1,401,963)**	(1,265,990)	**(1,401,963)**	(1,266,545)
Tax effect of permanent differences				
Sundry	**-**	-	**-**	-
Income tax adjusted for permanent differences	**(1,401,963)**	(1,265,990)	**(1,401,963)**	(1,266,545)
Benefit of tax losses not recognised	**1,401,963**	1,265,990	**1,401,963**	1,266,545
Income tax expense	**-**	-	**-**	-
(b) The directors estimate that the potential future income tax benefit at 30 June 2005 in respect of tax losses and cumulative timing differences not brought to account is	**4,031,072**	2,629,109	**4,031,072**	2,629,109

This benefit for tax losses will only be obtained if:

(i) the consolidated entity derives future assessable income of a nature and of an amount sufficient to enable the benefit from the deductions for the losses to be realised, or

(ii) the consolidated entity continues to comply with the conditions for deductibility imposed by tax legislation, and

(iii) no changes in tax legislation adversely affect the consolidated entity in realising the benefit from the deduction for the losses

Note 4 Income tax (continued)

Tax consolidation legislation
QrxPharma Pty Limited and its wholly-owned Australian subsidiaries have implemented the tax consolidation legislation as of 7 December 2002. The Australian Taxation Office has been notified of this decision. The wholly owned controlled entities in the QrxPharma Pty Limited group are dormant companies and no current or deferred tax amounts are expected to arise. As a consequence, QrxPharma Pty Limited will recognise current and deferred tax amounts relating to its own transactions, events and balances.

Note 5 Current assets – Cash assets

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Cash at bank and on hand	**1,412,133**	3,654,256	**1,412,133**	3,654,256

Note 6 Current assets - Receivables

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
GST Receivable	-	9,752	-	9,752
Other assets	-	3,000	-	3,000
	-	12,752	-	12,752

Note 7 Non-current assets – Property, plant and equipment

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Plant and equipment				
Plant and equipment- at cost	**109,277**	97,252	**109,277**	97,252
Less: Accumulated depreciation	**(60,947)**	(31,831)	**(60,947)**	(31,831)
Total plant and equipment	**48,330**	65,421	**48,330**	65,421

Reconciliations
Reconciliations of the carrying amounts of each class of plant and equipment at the beginning and end of the current financial period are set out below.

	Plant & equipment
	$
Consolidated	
Carrying amount at 1 July 2004	65,421
Additions	12,025
Depreciation expense (note 3)	(29,116)
Carrying amount at 30 June 2005	48,330
Parent entity	
Carrying amount at 1 July 2004	65,421
Additions	12,025
Depreciation expense (note 3)	(29,116)
Carrying amount at 30 June 2005	48,330

Note 8 Non-current assets - Other financial assets

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Shares in controlled entities	-	-	**500,570**	500,570
Less: provision for write down to recoverable amount	-	-	**(500,570)**	(500,750)
	-	-	-	-

Note 9 Current liabilities – Payables

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Trade creditors	**587,366**	400,774	**587,366**	400,774
Other creditors	**243,847**	125,932	**243,847**	125,932
Payable to controlled entities	-	-	**27,700**	27,700
	831,213	526,706	**858,913**	554,406

Note 10 Current liabilities – Provisions

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Employee entitlements (note 23)	**17,000**	17,971	**17,000**	17,971

Note 11 Current liabilities – Interest bearing liabilities

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Convertible notes	**2,139,325**	-	**2,139,325**	-

The parent entity issued 2,500,000 convertible notes in two tranches. The notes are convertible into Series B preference shares at the option of the holder, or mandatorily on occurrence of qualified financing, being the raising of greater than $15 million of funds. The conversion price of each convertible note is to be determined by the issue price of the Series B preference shares.

The notes are repayable on 31st December 2005 or rolled-over for a further 12 month period, subject to the approval of the note-holders. As at balance date, management are of the opinion that the notes will be rolled-over.

Interest accrues daily at rate of 10% per annum. Any unpaid interest will be capitalised annually into the underlying note balance. The unpaid interest will be convertible into Series B preference shares.

Note 12 Non-current liabilities – Provisions

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Dividends on preference shares	**2,244,891**	1,199,547	**2,244,891**	1,199,547

Dividends on preference shares
Provision is made for the dividend payable on preference shares. Dividends are accrued daily at a rate of 10% p.a. Any unpaid dividends are compounded on an annual basis on the anniversary of the preference share issue. Dividends are paid when declared by the board of directors.

Movement in provision for dividends

Consolidated and parent 2005	**$**
Carrying amount at start of the year	1,199,547
Additional provision recognised	1,045,344
Carrying amount at end of the year	2,244,891

Note 13 Contributed equity

	Parent 2005 Shares	Parent 2004 Shares	**Parent 2005 $**	Parent 2004 $
(a) Share capital				
Ordinary shares – fully paid (d)	**7,318,500**	7,243,500	**629,435**	671,054
Series A preference shares – fully paid (e)	**10,249,142**	10,249,142	**9,898,217**	9,898,217
	17,567,642	17,492,642	**10,527,652**	10,569,271

(b) Movements in ordinary share capital:

Date	**Details**	**Shares**	**Issue Price**	**$**
1 July 2003 and 30 June 2004	Balance	7,243,500		671,054
19 July 2004	Exercise of 2003 options – Note (f)	10,000	$0.15	1,500
18 September 2004	Exercise of 2003 options – Note (f)	10,000	$0.15	1,500
28 September 2004	Exercise of 2003 options – Note (f)	20,000	$0.15	3,000
29 September 2004	Exercise of 2003 options – Note (f)	5,000	$0.15	750
30 March 2005	Exercise of 2004 options – Note (f)	30,000	$0.15	4,500
				682,304
	Less: Transaction costs arising on share issue			(52,869)
30 June 2005	Balance	7,318,500		629,435

(c) Movements in non-redeemable, convertible preference shares:

Date	**Details**	**Shares**	**Issue Price**	**$**
1 July 2003	Opening balance	5,641,194		5,341,627
1 October 2003	Series A preferred share issuance – Note (e)	4,607,948	$1.00	4,607,948
	Less: Transaction costs arising on issue of shares			(51,358)
30 June 2004 and 30 June 2005	Balance	10,249,142		9,898,217

Note 13 Contributed equity (continued)

(d) Ordinary shares

Each ordinary shareholder maintains the right, when present in person or by proxy or by attorney at any general meeting of the Company the right to cast one vote for each ordinary share held (subject to any agreement between the Company and a Member affecting the voting rights attaching to any share).

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number and amounts paid on the shares held, subsequent to the satisfaction of preferred shareholder rights as included in the shareholder deed dated 6 December 2002.

(e) Series A preferred shares

Non-redeemable, convertible preferred shares entitle the holder to have priority over ordinary shareholders upon liquidation of the company or in the event of an initial public offering, and each preferred shareholder maintains the right to receive cumulative dividends if the Company declares and pays discretionary dividends in respect of ordinary shares. Upon liquidation of the company, preferred shareholders are entitled to a liquidation preference equal to 10% of the issue price per annum plus all accrued but unpaid dividends.

On 1 October 2003, 4,607,948 Series A preferred shares ($1.00 per share) were issued for a total consideration of $4,607,948.

(f) Options

Each option granted to founding shareholders on 19 September 2002 is exercisable immediately on issue. When exercisable, each option is convertible into one ordinary share and entitles the holder to the same ordinary share rights as noted above.

Information related to the QRxPharma Employee Option Plan, including details of options issued, exercised and lapsed during the financial year and options outstanding at the end of the financial year are set out in note 23.

Each Series A Preferred Share carries the right to receive any document or information an Ordinary Share carries the right to receive, and has the same right to attend and speak at the general meeting of the Company and the same number of votes as if each preferred share were converted into Ordinary Shares, as per terms included in the shareholder deed dated 6 December 2002.

Note 14 Accumulated losses

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Accumulated losses at the beginning of the financial year	**(8,581,066)**	(3,161,552)	**(8,608,766)**	(3,187,401)
Net loss for the year	**(4,673,208)**	(4,219,967)	**(4,673,208)**	(4,221,818)
Dividends provided for	**(1,045,344)**	(1,199,547)	**(1,045,344)**	(1,199,547)
Accumulated losses at the end of the financial year	**(14,299,618)**	(8,581,066)	**(14,327,318)**	(8,608,766)

Note 15 Financial instruments

(a) Credit risk exposures
The credit risk on financial assets of the consolidated entity which have been recognised on the statement of financial position, other than investment in shares, is generally the carrying amount, net of any provisions for doubtful debts.

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

Exposures arise predominantly from assets and liabilities bearing variable interest rates as the company intends to hold fixed rate assets and liabilities to maturity.

2005	Notes	Floating Interest Rate $	Fixed interest rate maturing in > 1 year $	Non-interest bearing $	Total $
Financial assets					
Cash	5	1,412,133	-	-	1,412,133
		1,412,133	-	-	1,412,133
Weighted average interest rate		5.1%			
Financial liabilities					
Trade and other payables	9	-	-	831,213	831,213
Convertible notes	11	-	2,139,325	-	2,139,325
		-	2,139,125	831,213	2,970,538
Weighted average interest rate			10%		
Net financial assets (liabilities)		1,412,133	(2,139,325)	(831,213)	(1,558,405)

2004	Notes	Floating Interest Rate $	Fixed interest rate maturing in > 1 year $	Non-interest bearing $	Total $
Financial assets					
Cash	5	3,654,256	-	-	3,654,256
Receivables	6		-	12,752	12,752
		3,654,256	-	12,752	3,667,008
Weighted average interest rate		4.65%			
Financial liabilities					
Trade and other payables	9	-	-	526,706	526,706
		-	-	526,706	526,706
Net financial assets (liabilities)		3,654,256	-	(513,954)	3,140,302

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

Note 16 Remuneration of directors

	Directors of parent entity 2005 $	Directors of parent entity 2004 $
Income paid or payable, or otherwise made available, to directors by entities in the consolidated entity and related parties in connection with the management of affairs of the parent entity or its controlled entities.	**358,553**	324,430

	2005 Number	2004 Number
The number of parent entity directors whose total income from the parent entity or related parties was within the specified bands are as follows:		
$0-$9,999	**6**	4
$320,000-$329,999	**-**	1
$350,000-$359,999	**1**	-

Options are granted over ordinary shares to certain directors pursuant to the Company's Employee Share Option Plan, details of which are set out in note 23.

Four directors of the parent entity received remuneration of nil (2004: nil).

Note 17 Remuneration of auditors

	Consolidated		Parent	
	2005 $	2004 $	**2005 $**	2004 $
During the year, the following amounts were paid to the auditor of the parent entity:				
Assurance services				
1. Audit services				
Fees paid to PricewaterhouseCoopers Australian firm				
Audit of the financial report	**16,000**	14,000	**16,000**	14,000
2. Other assurance services				
Fees paid to PricewaterhouseCoopers Australian firm				
Preparation of financial statements	**6,000**	6,000	**6,000**	6,000
IFRS accounting services	**2,000**	-	**2,000**	-
	24,000	20,000	**24,000**	20,000
Taxation services				
Fees paid to PricewaterhouseCoopers Australian firm				
Tax compliance and consulting services, including preparation of company tax returns	**43,400**	17,800	**43,400**	17,800
	67,400	37,800	**67,400**	37,800

Note 18 Related parties

Directors
The names of persons who were directors of the company at any time during the financial year are as follows:

M Quinn
GW Pace
MS Hirshorn
G Savage
DA Henderson
R Creswell
D Stack

All of these persons were also directors during the year ended 30 June 2004, with the exception of R Cresswell and D Stack.

Remuneration
Information on remuneration of directors is disclosed in note 16.

Transactions of directors and director related entities concerning shares

Aggregate numbers of shares and share options of QrxPharma Pty Limited acquired by directors or their director-related entities from the company during the financial year:

	2005 Number	2004 Number
Acquisitions		
Series A preferred shares	-	3,293,907
QRx Employee Option Plan options over ordinary shares	**340,000**	-

The establishment of the QrxPharma Pty Limited Employee Share Option Plan was approved by shareholders and the terms and conditions of the plan are described in note 23. All other transactions relating to shares and options of the company were on the same basis as similar transactions with other shareholders.

The directors and their related parties had the following interests in the share capital and options at the end of the financial year:

	2005 Number	2004 Number
Ordinary shares – vested	**1,092,400**	1,092,400
Ordinary shares - non-vested	**888,600**	888,600
Series A preferred shares	**7,319,792**	7,319,792
Options over ordinary shares	**340,000**	-

Other transactions with directors and director related entities
During the year, the consolidated entity issued 2,500,000 convertible notes in two tranches. These convertible notes were taken up by the directors or their director related entities. These notes were issued on normal commercial terms and conditions.

A director, Mr D Stack, is the owner of the firm Stack Pharmaceuticals. Stack Pharmaceuticals has provided research and development services to QrxPharma Pty Limited for several years on normal commercial terms and conditions.

A director, Mr D Henderson, is a director of Uniquest Pty Limited. UniQuest Pty Limited is a significant shareholder of the company, owning 3,612,500 vested ordinary shares as at 30 June 2005. During the year, the company paid fees to UniQuest Pty Limited for the research, development and commercialisation of patented technology. Total fees paid to UniQuest Pty Limited during the year was approximately $133,500 (2004: $507,000).

Note 18 Related parties (continued)

A director, Mr G Savage, is a director and shareholder of ST Management Pty Limited. ST Management provided ad-hoc consulting services to the consolidated entity throughout the year. The consulting services were provided on normal commercial terms and conditions:

Aggregate amounts of each of the above types of other transactions with directors and their director-related entities:

	2005	2004
	$	$
Interest expense	**50,644**	-
Research and development	**195,872**	507,000

Aggregate amounts payable to directors and their director-related entities at balance date relating to the above types of other transactions:

	2005	2004
	$	$
Current liabilities	**1,362,605**	-

Wholly- owned group
The wholly- owned group consists of QrxPharma Pty Limited and its wholly- owned controlled entities, Lynx Pty Limited and Haempatch Pty Limited. Ownership interests in these controlled entities are set out in note 19.

Aggregate amounts payable to entities in the wholly owned group at balance date

	2005	2004
	$	$
Current payable	**27,700**	27,700

Other related parties
During the year, the company directly engaged and contracted the services of certain shareholders in relation to the ongoing normal course of business operations. Total amounts paid to shareholders for contracted services rendered during the year amounted to $368,116 (2004: $348,668).

Note 19 Investment in controlled entities

Name of entity	Country of incorporation	Class of shares	Equity holding	
			2005	2004
			%	%
Lynx Pty Limited	Australia	Ordinary	100	100
Haempatch Pty Limited	Australia	Ordinary / Preferred	100	100

Note 20 Reconciliation of loss from ordinary activities after income tax to net cash outflow from operating activities

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Loss from ordinary activities after income tax	**(4,673,208)**	(4,219,967)	**(4,673,208)**	(4,221,818)
Depreciation and amortisation	**29,116**	26,955	**29,116**	26,955
Decrease in other operating assets	**12,752**	46,495	**12,752**	46,495
Increase in trade creditors and accruals	**304,507**	204,056	**304,507**	204,056
(Decrease)/ increase in other operating liabilities	**(971)**	11,466	**(971)**	11,466
Net outflow from operating activities	**(4,327,804)**	(3,930,995)	**(4,327,804)**	(3,932,846)

Note 21 Segment information

The company's operations during the year were predominantly in Australia. The company operates in only one market segment, that of the research and development of biopharmaceutical products for commercial sale.

Note 22 Commitments for expenditure

On 25 January 2005, the Company entered into a contract with Bresagen for services in connection with securing government grants to fund the research and development activities being undertaken by the company. The total committed future fees as at 30 June 2005 are approximately $97,945.

On 21 February 2005, the consolidated entity entered into a development agreement with CIT to conduct a toxicity study. The committed future development fee as at 30 June 2005 was $213,782. The term of this contract is such that these committed funds are expected to be paid in the next 12 months.

Note 23 Employee benefits

	Consolidated		Parent	
	2005	2004	**2005**	2004
	$	$	**$**	$
Employee benefits and related on-costs liabilities				
Provision for employee benefits – current (note 10)	**17,000**	17,971	**17,000**	17,971
	Numbers		**Numbers**	
Employee numbers				
Average number of employees during the financial year	3	4	3	4

QrxPharma Pty Limited Employee Share Option Plan (ESOP)
The ESOP was established to enable QrxPharma to grant options over shares to employees and consultants of the economic entity, subject to local regulations. Under the ESOP, the Board may invite applications for options from directors, full time or part time employees and consultants of QRxPharma having regard to the employee's position, services provided by employee, record of employment or service, potential contributions and any other matters which indicate the employee's merit. The exercise price in respect of an option granted shall be the market price for a share prevailing at the time of grant unless the Board decides otherwise. Options will lapse if they are not exercised before the expiration date or if the option holder leaves the employment of QRxPharma. The Board reserves discretion to waive the latter provision.

Note 23 Employee benefits (continued)

Options granted under plan carry no dividend or voting rights. The vesting period for each option is 4 years, 25% vesting after 12 months from date of grant and the balance vesting monthly over the remaining 36 month period. When exercisable, each option is convertible into one ordinary share and entitle the holder to the same ordinary share rights as set out in Note 13.

Set out below are summaries of options granted under the plan.

Grant date	Expiry date	Exercise price	Balance at start of the year	Issued during the year	Exercised during the year	Cancelled during the year	Balance at end of the year
			Number	Number	Number	Number	Number
Consolidated and parent entity – 2005							
19 December 2002	19 December 2012	$1.50	100,000	-	-	(60,000)	40,000
19 February 2003	19 February 2006	$0.15	40,000	-	-	-	40,000
19 February 2003	30 September 2004	$0.15	45,000		(45,000)	-	-
21 November 2003	21 November 2005	$0.15	5,000	-	-	-	5,000
1 December 2003	1 December 2006	$0.15	20,000	-	-	-	20,000
15 December 2003	15 December 2013	$0.15	50,000	-	-	-	50,000
24 February 2004	24 February 2014	$0.15	15,000	-	-	(10,000)	5,000
24 February 2004	24 February 2007	$0.15	10,000	-	-	-	10,000
24 February 2004	24 February 2014	$1.50	20,000	-	-	-	20,000
25 February 2004	24 February 2014	$0.15	5,000	-	-	-	5,000
19 May 2004	19 May 2014	$0.15	25,000	-	-	-	25,000
7 June 2004	7 June 2014	$0.15	200,000	-	(30,000)	(170,000)	-
24 June 2004	24 June 2014	$0.15	20,000	-	-	-	20,000
13 July 2004	13 July 2014	$0.15	-	50,000	-	-	50,000
14 July 2004	14 July 2014	$0.15	-	40,000	-	-	40,000
16 March 2004	16 March 2014	$0.15	-	10,000	-	-	10,000
17 August 2004	17 August 2014	$0.15	-	20,000	-	-	20,000
19 October 2004	19 October 2014	$0.15	-	100,000	-	-	100,000
18 May 2005	18 May 2015	$0.15	-	240,000	-	-	240,000
19 February 2005	19 February 2015	$0.15	-	150,000	-	-	150,000
			555,000	610,000	(75,000)	(240,000)	850,000
Consolidated and parent entity – 2004							
19 December 2002	19 December 2012	$1.50	100,000	-	-	-	100,000
19 February 2003	19 February 2006	$0.15	40,000	-	-	-	40,000
19 February 2003	30 September 2004	$0.15	45,000		-	-	45,000
21 November 2003	21 November 2005	$0.15	-	5,000	-	-	5,000
1 December 2003	1 December 2006	$0.15	-	20,000	-	-	20,000
15 December 2003	15 December 2013	$0.15	-	50,000	-	-	50,000
24 February 2004	24 February 2014	$0.15	-	15,000	-	-	15,000
24 February 2004	24 February 2007	$0.15	-	10,000	-	-	10,000
24 February 2004	24 February 2014	$1.50	-	20,000	-	-	20,000
25 February 2004	24 February 2014	$0.15	-	5,000	-	-	5,000
19 May 2004	19 May 2014	$0.15	-	25,000	-	-	25,000
7 June 2004	7 June 2014	$0.15	-	200,000	-	-	200,000
24 June 2004	24 June 2014	$0.15	-	20,000	-	-	20,000
			185,000	370,000	-	-	555,000

Note 24 Events occurring after reporting date

Since balance date, the consolidated entity has entered into a contract with an investment adviser to act as exclusive placement agent for the sale of the entity's shares to private investors. Up to $25 million is sought through this round of funding and is expected to be secured prior to December 2005. The financial effect of the above has not been brought to account at 30 June 2004.

Note 25 Impacts of adopting Australian equivalents to IFRS

The Australian Accounting Standards Board (AASB) is adopting International Financial Reporting Standards (IFRS) for application to reporting periods beginning on or after 1 January 2005. The AASB has issued Australian equivalents to IFRS (AIFRS), and the Urgent Issues Group has issued interpretations corresponding to IASB interpretations originated by the International Financial Reporting Interpretations Committee or the former Standing Interpretations Committee. The adoption of AIFRS will be first reflected in the consolidated entity's financial statements for the year ending 30 June 2006.

Entities complying with AIFRS for the first time will be required to restate their comparative financial statements to amounts reflecting the application of AIFRS to that comparative period. Most adjustments required on transition to AIFRS will be made, retrospectively, against opening retained earnings as at 1 July 2004.

Management have analysed all of the AIFRS and have identified the accounting policy changes that will be required. In some cases choices of accounting policies are available, including elective exemptions under Accounting Standard AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards*. These choices have been analysed to determine the most appropriate accounting policy for the consolidated entity.

The known or reliably estimable impacts on the financial report for the year ended 30 June 2005 had it been prepared using AIFRS are set out below.

Although the adjustments disclosed in this note are based on management's best knowledge of expected standards and interpretations, and current facts and circumstances, these may change. For example, amended or additional standards or interpretations may be issued by the AASB and the IASB. Therefore, until the company prepares its first full AIFRS financial statements, the possibility cannot be excluded that the accompanying disclosures may have to be adjusted.

(a) Equity based compensation benefits

Under AASB 2 *Share-based Payment*, from 1 July 2004 the group is required to recognise an expense for those options that were issued to employees under the QrxPharma Employee Option Plan after 7 November 2002 but that had not vested by 1 January 2005.

This will result in a change to the current accounting policy under which no expense is recognised for equity-based compensation. If the policy required by AASB 2 had been applied during the year ended 30 June 2005, the consolidated and parent entity accumulated losses at 30 June 2005 would have been $3,334 higher with a corresponding increase in the share-based payment reserve. For the year ended 30 June 2005, the consolidated entity's employee benefits expense would have been $18,934 higher with a corresponding increase in the net movement in the share-based payment reserve.

(b) Financial instruments

The group will be taking advantage of the exemption available under AASB 1 to apply AASB 132 *Financial Instruments: Disclosure and Presentation* and AASB 139 *Financial Instruments: Recognition and Measurement* only from 1 July 2005. This allows the group to apply previous Australian generally accepted accounting principles (Australian GAAP) to the comparative information of financial instruments within the scope of AASB 132 and AASB 139 for the 30 June 2006 financial report.

Under AASB 132, the current classification of the preference shares will change from equity to debt. The current classification of the remaining financial instruments issued by the company would not change.

Under AASB 139, investments in loans and receivables and financial liabilities classifications will remain unchanged. Measurement of these instruments will initially be at fair value with subsequent measurement at amortised cost, using the effective interest rate method.

Note 25 Impacts of adopting Australian equivalents to IFRS (continued)

This will result in a change to the current accounting policy, under which financial assets are carried at the lower of cost and recoverable amount, with changes recognised in profit or loss.

As a result of the application of the exemption referred to above, there would have been no adjustment to classification or measurement of financial assets or liabilities from the application of AIFRS during the year ended 30 June 2005. Changes in classification and measurement will be recognised from 1 July 2005.

(c) Reclassification of other income

Under AIFRS, foreign exchange gains, government grants and gains on debt defeasance are classified as other income. This is in contrast to the current Australian GAAP treatment under which such items are classified as revenue or as a deduction to expenses.

If the policy required under AIFRS had been applied during the year ended 30 June 2005, the research and development expenses and the general and administration expenses in both the consolidated entity and parent entity would have been $124,875 and $102,451 higher respectively and consolidated and parent other income would have been $227,326 higher.

Directors' declaration

In the directors' opinion:

(a) the financial statements and notes set out on pages 4 to 24 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 consolidated entity's financial position as at 30 June 2005 and of their performance, as represented by the results of their operations and their cash flows, for the financial year ended on that date.

(b) having regard to the matters set out in note 1(a) to the financial statements, there are reasonable grounds to believe that the consolidated entity will be able to pay its debts as and when they become due and payable.

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

MA Quinn
Director

Sydney
25 October 2005

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Independent audit report to the members of QrxPharma Pty Limited and controlled entities

Audit opinion

In our opinion, the financial report of QrxPharma Pty Limited:

- gives a true and fair view, as required by the *Corporations Act 2001* in Australia, of the financial position of QrxPharma Pty Limited and the QrxPharma Pty Limited Group (defined below) as at 30 June 2005, 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.

Inherent uncertainty regarding continuation as a going concern

Without qualification to the opinion expressed above, attention is drawn to the following matter. As a result of the matters described in Note 1(a), there is significant uncertainty whether QrxPharma Pty Limited and the QrxPharma Group will be able to continue as going concerns and therefore whether they will realise their assets and extinguish their liabilities in the normal course of business and at the amounts stated in the financial report.

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 both QrxPharma Pty Limited (the company) and the QrxPharma Pty Limited Group (the consolidated entity), for the year ended 30 June 2005. 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 and cash flows.

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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

PricewaterhouseCoopers

Andrew Sneddon

Andrew Sneddon
Partner

Sydney
25 October 2005