QRx Pharma Pty Limited

ACN 102 254 151

Annual report – 30 June 2004

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Directors' report

Your directors present their report on the consolidated entity consisting of QRx Pharma Pty Limited and the entities it controlled at the end of, or during, the year ended 30 June 2004.

Directors
The following persons were directors of QRx Pharma 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

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 operating activities after income tax for the period of $4,219,967 (2003: loss of $3,161,552).

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 board has resolved to proceed with the additional funding through the issue of convertible loan facilities. $2.5m is to be raised in two tranches. $862,529 has to date been received from investors.

No other matter or circumstance has arisen since 30 June 2004 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.

Insurance of officers
During the financial year, no amounts were paid by the company to insure officers of the company or related bodies corporate.

Share options granted to directors
There were no share options over unissued ordinary shares of QRx Pharma Pty Limited granted during or since the end of the financial year to any of the directors of the Company and consolidated entity.

Shares under option
Unissued ordinary shares of QRx Pharma 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	100,000
19 February 2003	19 February 2006	$0.15	40,000
19 February 2003	30 September 2004	$0.15	45,000
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
19 May 2004	19 May 2014	$0.15	25,000
7 June 2004	7 June 2014	$0.15	200,000
24 June 2004	24 June 2014	$0.15	20,000
13 July 2004	13 July 2014	$0.15	70,000
14 July 2004	14 July 2014	$0.15	40,000

Shares issued from options exercised
During the period no ordinary shares were issued as a result of the exercise of options.

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 were appointed during the year and continue in office in accordance with section 327 of the Corporations Act 2001.

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

G. W. Pace

GW Pace
Director

Sydney
23 September 2004

QRx Pharma Pty Limited
ACN 102 254 151

Financial report

30 June 2004

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

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

Cumbrae- Stewart Building
Research Road
St Lucia Qld 4067

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 2004

	Notes	Consolidated		Parent	
		Year ended 30 June 2004	9 months ended 30 June 2003	**Year ended 30 June 2004**	9 months ended 30 June 2003
		$	$	**$**	$
Revenue from ordinary activities	2	**102,503**	58,347	**101,349**	58,316
Expenses from ordinary activities					
Research and development		**(3,041,454)**	(1,212,887)	**(3,041,454)**	(1,212,887)
Marketing		**(206,261)**	(184,757)	**(206,361)**	(184,757)
Depreciation and amortisation	3	**(26,955)**	(152,946)	**(26,955)**	(73,870)
General & administration		**(1,013,891)**	(603,955)	**(1,014,583)**	(603,955)
Foreign exchange loss		**(33,814)**	(324,117)	**(33,814)**	(324,117)
Write down of intellectual property to net realisable amount	3	**-**	(741,237)	**-**	(345,381)
Write down of investments to recoverable amount	3	**-**	-	**-**	(500,750)
Loss from ordinary activities before income tax expense	3	**(4,219,967)**	(3,161,552)	**(4,221,818)**	(3,187,401)
Income tax expense	4	**-**	-	**-**	-
Loss from ordinary activities after income tax expense		**(4,219,967)**	(3,161,552)	**(4,221,818)**	(3,187,401)

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

Statements of financial position

As at 30 June 2004

	Notes	Consolidated 2004 $	Consolidated 2003 $	Parent 2004 $	Parent 2003 $
Current assets					
Cash assets	5	**3,654,256**	3,045,871	**3,654,256**	3,020,022
Other	6	**12,752**	59,247	**12,752**	59,247
Total current assets		**3,667,008**	3,105,118	**3,667,008**	3,079,269
Non-current assets					
Plant and equipment	7	**65,421**	75,166	**65,421**	75,166
Intangible assets	8	**-**	-	**-**	-
Other financial assets	9	**-**	-	**-**	-
Total non-current assets		**65,421**	75,166	**65,421**	75,166
Total assets		**3,732,429**	3,180,284	**3,732,429**	3,154,435
Current liabilities					
Payables	10	**526,706**	322,650	**554,406**	322,650
Provisions	11	**17,971**	6,505	**17,971**	6,505
Total current liabilities		**544,677**	329,155	**572,377**	329,155
Non-current liabilities					
Provisions	12	**1,199,547**	-	**1,199,547**	-
Total non-current liabilities		**1,199,547**	-	**1,199,547**	-
Total liabilities		**1,744,224**	329,155	**1,771,924**	329,155
Net assets		**1,988,205**	2,851,129	**1,960,505**	2,825,280
Equity					
Contributed equity	13	**10,569,271**	6,012,681	**10,569,271**	6,012,681
Accumulated losses	14	**(8,581,066)**	(3,161,552)	**(8,608,766)**	(3,187,401)
Total equity		**1,988,205**	2,851,129	**1,960,505**	2,825,280

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 2004

	Notes	Consolidated		Parent	
		Year ended 30 June 2004 $	9 months ended 30 June 2003 $	**Year ended 30 June 2004 $**	9 months ended 30 June 2003 $
Cash flows from operating activities					
Payments to suppliers and employees (inclusive of goods and services tax)		**(4,380,612)**	(2,303,520)	**(4,381,309)**	(2,280,027)
Interest received		**102,503**	56,360	**101,349**	56,330
R&D grant received		**175,895**	134,198	**175,895**	134,198
GST tax refund		**171,219**	92,007	**171,219**	92,007
Net cash (outflow) from operating activities	20	**(3,930,995)**	(2,020,955)	**(3,932,846)**	(1,997,492)
Cash flows from investing activities					
Payments for property, plant and equipment		**(17,210)**	(80,042)	**(17,210)**	(80,042)
Cash received in acquisition of controlled entities		**-**	49,312	**-**	-
Net cash inflow/ (outflow) from investing activities		**(17,210)**	(30,730)	**(17,210)**	(80,042)
Cash flows from financing activities					
Proceeds from intercompany loan		**-**	-	**27,700**	-
Proceeds from issues of shares		**4,607,948**	5,416,850	**4,607,948**	5,416,850
Share issue transaction costs		**(51,358)**	(319,294)	**(51,358)**	(319,294)
Net cash inflow from financing activities		**4,556,590**	5,097,556	**4,584,290**	5,097,556
Net increase in cash held		**608,385**	3,045,871	**634,234**	3,020,022
Cash at the beginning of the financial year		**3,045,871**	-	**3,020,022**	-
Cash at the end of the financial year	5	**3,654,256**	3,045,871	**3,654,256**	3,020,022

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

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 will issue Australian equivalents to IFRS, and the Urgent Issues Group will issue abstracts corresponding to IASB interpretations originated by the International Financial Reporting Interpretations Committee or the former Standing Interpretations Committee. The adoption of Australian equivalents to IFRS will be first reflected in the consolidated entity's financial statements for year ending 30 June 2006. Information about how the transition to Australian equivalents to IFRS is being managed, and the key differences in accounting policies that are expected to arise, is set out in note 1(l).

(a) Going concern

The consolidated entity has experienced operating losses of $4,219,967 and operating cash outflows of $3,930,995 during the year ending 30 June 2004 as the Company 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 net assets of $1,988,205 and cash balances of $3,654,256. 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 company 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 company successfully implementing its business strategy and operating plan.

The company's short operating history and reliance on future funding and successfully executing its business strategy result in there being some uncertainty whether the Company 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 Company has successfully met the necessary milestones to receive additional funding in the form of convertible loan facilities from its shareholders, resulting in the approval of $2,500,000 to be funded in two tranches. Hence, the directors believe that the Company will be successful in the above matters, and accordingly, have prepared the financial report on a going concern basis. The directors regularly monitor the Company'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 Company 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 2004. Provisions have been made in the financial report relating to the recoverability of the asset carrying amounts, including the write-down of certain intellectual property (refer note 8) and the Company's investments in Lynx Project Pty Limited and Haempatch Pty Limited (refer note 9). No other 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 QRx Pharma Pty Limited as at 30 June 2004 and the results of all controlled entities for the year then ended. QRx Pharma 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 is not carried forward as an asset unless the benefit is virtually certain of realisation. Income tax on cumulative timing differences is set aside to the deferred income tax or the future income tax benefit accounts at the rates which are expected to apply when those timing differences reverse.

(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 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 (excluding land) 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 company 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) 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.

Note 1 Summary of significant accounting policies (continued)

(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 QRx Pharma Employee Option Plan and an employee share scheme. Information relating to these schemes is set out in note 23.

No accounting entries are made in relation to the QRx Pharma Employee 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.

(j) Cash
For purposes of the statement of cash flows, cash includes deposits at call which are readily convertible to cash on hand and are subject to an insignificant risk of changes in value, net of outstanding bank overdrafts.

(k) Intangible assets – Intellectual property
Intellectual property is amortised on a straight line basis over its anticipated useful life. During the previous period, the Directors resolved to write down the intellectual property to a nil value on the basis that the expected future economic benefit of the underlying assets can not be reasonably estimated by management.

(l) 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.

(m) International Financial Reporting Standards (IFRS)
Entities complying with Australian equivalents to IFRS for the first time will be required to restate their comparative financial statements to amounts reflecting the application of IFRS to that comparative period. Most adjustments required on transition to IFRS will be made, retrospectively, against opening retained earnings as at 1 July 2004.

Management have done a preliminary assessment of potential impacts that the transition to IFRS will have on the company. Management are of the view that the main impacts will be in relation to the classification of debt and equity, share options issued to directors and in relation to intangible assets.

Note 2 Revenue

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Revenue from outside the operating activities				
Interest	**102,503**	58,347	**101,349**	58,316
Revenue from ordinary activities	**102,503**	58,347	**101,349**	58,316

Note 3 Loss from ordinary activities

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Net expenses				
Loss from ordinary activities before income tax expense includes the following specific net expenses:				
Expenses				
Depreciation				
Plant and equipment	**26,955**	4,876	**26,955**	4,876
Amortisation				
Intellectual property	-	148,070	-	68,994
Foreign exchange gains and losses				
Net foreign exchange loss	**33,814**	324,117	**33,814**	324,117
Other charges against assets				
Write down of intellectual property to net realisable value	-	741,237	-	345,381
Write down of investments to recoverable amount	-	-	-	500,750

Note 4 Income tax

	Consolidated		Parent	
	2004	2004	**2004**	2003
	$	$	**$**	$
(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	**(4,219,967)**	(3,161,552)	**(4,221,818)**	(3,187,401)
Income tax calculated at 30%	**(1,265,990)**	(948,466)	**(1,266,545)**	(956,220)
Tax effect of permanent differences:				
Amortisation of intellectual property	-	44,421	-	20,698
Write down of intellectual property to net realisable value	-	222,371	-	103,614
Write down of investments to recoverable amount	-	-	-	150,225
Income tax adjusted for permanent differences	**(1,265,990)**	(681,674)	**(1,266,545)**	(681,683)
Benefit of tax losses not recognised	**(1,265,990)**	681,674	**1,266,545**	681,683
Income tax expense	-	-	-	-
(b) The directors estimate that the potential future income tax benefit at 30 June 2004 in respect of tax losses not brought to account is	**1,947,664**	681,674	**1,948,219**	681,674

Note 4 Income tax (continued)

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

Tax consolidation legislation

QRx Pharma Pty Limited and its wholly-owned Australian subsidiaries have decided to implement the tax consolidation legislation as of 7 December 2002. The Australian Taxation Office has not yet been notified of this decision. The entities also intend to enter into a tax sharing agreement, but details of this agreement are yet to be finalised.

As a consequence, QRx Pharma Pty Limited, as the head entity in the tax consolidated group, will recognise current and deferred tax amounts relating to transactions, events and balances of the wholly-owned Australian controlled entities in this group in future financial statements as if those transactions, events and balances were its own, in addition to the current and deferred tax balances arising in relation to its own transactions, events and balances. Amounts receivable or payable under the tax sharing agreement will be recognised separately by QRx Pharma Pty Limited as tax-related amounts receivable or payable. The impact on the income tax expense and results of QRx Pharma Pty Limited is unlikely to be material because of the tax sharing agreement.

The financial effect of the implementation of the legislation has not been recognised in the financial statements for the year ended 30 June 2004.

Note 5 Current assets – Cash assets

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Cash at bank and on hand	**3,654,256**	3,045,871	**3,654,256**	3,020,022

Note 6 Current assets - Other

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
GST Receivable	**9,752**	59,247	**9,752**	59,247
Other assets	**3,000**	-	**3,000**	-
	12,752	59,247	**12,752**	59,247

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

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Plant and equipment				
Plant and equipment- at cost	**97,252**	80,042	**97,252**	80,042
Less: Accumulated depreciation	**(31,831)**	(4,876)	**(31,831)**	(4,876)
Total plant and equipment	**65,421**	75,166	**65,421**	75,166

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

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 2003	75,166
Additions	17,210
Depreciation expense (note 3)	(26,955)
Carrying amount at 30 June 2004	65,421
Parent entity	
Carrying amount at 1 July 2003	75,166
Additions	17,210
Depreciation expense (note 3)	(26,955)
Carrying amount at 30 June 2004	65,421

Note 8 Non-Current assets – Intangibles

	Consolidated		Parent	
	2004 $	2003 $	**2004 $**	2003 $
Licence fees	**414,375**	414,375	**414,375**	414,375
Intellectual property	**474,932**	474,932	**-**	-
Less: accumulated amortisation	**(889,307)**	(889,307)	**(414,375)**	(414,375)
	-	-	**-**	-

Note 9 Non-current assets - Other financial assets

	Consolidated		Parent	
	2004 $	2003 $	**2004 $**	2003 $
Shares in controlled entities	**-**	-	**500,570**	500,570
Less: provision for write down to recoverable amount	**-**	-	**(500,750)**	(500,750)
	-	-	**-**	-

Management is currently in the process of liquidating the wholly owned controlled entities pending the transfer of intellectual property rights to the parent company.

Note 10 Current liabilities – Payables

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Trade creditors	**400,774**	277,613	**400,774**	277,613
Other creditors	**125,932**	45,037	**125,932**	45,037
Payable to controlled entities	-	-	**27,700**	-
	526,706	322,650	**554,406**	322,650

Note 11 Current liabilities – Provisions

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Employee entitlements (note 23)	**17,971**	6,505	**17,971**	6,505

Note 12 Non-current liabilities – Provisions

	Consolidated		Parent	
	2004	2003	**2004**	2003
	$	$	**$**	$
Dividends provided on preference shares	**1,199,547**	-	**1,199,547**	-

Note 13 Contributed equity

	Parent	Parent	**Parent**	Parent
	2004	2003	**2004**	2003
	Shares	Shares	**$**	$
(a) Share capital				
Ordinary shares – fully paid (c)	**7,243,500**	7,243,500	**690,781**	690,781
Series A preference shares – fully paid (d)	**10,249,142**	5,641,194	**10,249,142**	5,641,194
Capital raising expenses	-	-	**(370,652)**	(319,294)
	17,492,642	12,884,694	**10,569,271**	6,012,681

Note 13 Contributed equity (continued)

(b) Movements in ordinary share capital:

Date	Details	Shares	Issue Price	$
19 September 2002	Opening balance	1	1.00	1
19 September 2002	Share issue	2,655,999	$0.001	2,655
6 December 2002	Share issue	4,587,500	$0.15	688,125
	Total ordinary shares	7,243,500		690,781
	Less: Transaction costs arising on issue of shares			(19,727)
30 June 2003	Balance			671,054
1 July 2003 and 30 June 2004	Balance			671,054

(i) On 19 September 2002 (date of incorporation) the company issued one founder share ($1.00 value), 1,385,999 ordinary shares ($0.001 per share) and a further 1,270,000 ordinary shares ($0.001 per share) from options immediately exercised. Total consideration from the shares issued was $2,655.

(ii) On 6 December 2002, QRxPharma Pty Limited acquired all of the issued shares in Lynx Project Pty Limited and Haempatch Pty Limited. Both of the acquisitions were made by means of share for share exchange, which resulted in the issuance of 1,825,000 (975,000 and 850,000, respectively) ordinary shares valued at $0.15 per share.

On the same date, the company issued a further 2,762,500 ordinary shares valued at $0.15 per share.

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

Date	Details	Shares	Issue Price	$
19 September 2002	Opening balance	-	-	-
6 December 2002	Series A preferred share issuance	5,641,194	$1.00	5,641,194
	Less: Transaction costs arising on issue of shares			(299,567)
30 June 2003	Balance	5,641,194		5,341,627
1 October 2003	Series A preferred share issuance	4,607,948	$1.00	4,607,948
	Less: Transaction costs arising on issue of shares			(51,358)
30 June 2004	Balance	10,249,142		9,898,217

(i) On 6 December 2002, QRxPharma Pty Limited acquired all of the issued shares in Haempatch Pty Limited. The acquisition was made by means of share for share exchange resulting in the issuance of 227,000 Series A preferred shares ($1.00 per share).

On the same date a further 5,414,194 Series A preferred shares ($1.00 per share) were issued for a total consideration of $5,414,194.

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.

(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 22.

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	
	2004	2003	**2004**	2003
	$	$	**$**	$
Accumulated losses at the beginning of the financial year	**(3,161,552)**	-	**(3,187,401)**	-
Net loss for the year	**(4,219,967)**	(3,161,552)	**(4,221,818)**	(3,187,401)
Dividends provided for	**(1,199,547)**	-	**(1,199,547)**	-
Accumulated losses at the end of the financial year	**(8,581,066)**	(3,161,552)	**(8,608,766)**	(3,187,401)

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.

Note 15 Financial instruments (continued)

2004	**Notes**	**Floating Interest Rate $**	**Non-interest bearing $**	**Total $**
Financial assets				
Cash	5	3,654,256	-	3,654,256
Other assets - 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	10,11	-	526,706	526,706
		-	526,706	526,706
Net financial assets (liabilities)		3,654,256	(513,954)	3,140,302

2003	**Notes**	**Floating Interest Rate $**	**Non-interest bearing $**	**Total $**
Financial assets				
Cash	5	3,045,871	-	3,045,871
Other assets - receivables	6	-	59,247	59,247
		3,045,871	59,247	3,105,118
Weighted average interest rate		3.95%		
Financial liabilities				
Trade and other payables	10,11	-	322,650	322,650
		-	322,650	322,650
Net financial assets (liabilities)		3,045,871	(263,403)	2,782,468

(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 2004	Directors of parent entity 2003
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.	**324,430**	172,506

	2004 $	2003 $
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	**4**	4
$170,000-$179,999	-	1
$320,000-$329,999	**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 (2003: nil).

Note 17 Remuneration of auditors

	Consolidated		Parent	
	2004 $	20043 $	**2004** $	2003 $
Remuneration for audit of the financial reports of the parent entity or any entity in the consolidated entity:				
Auditor of the company – PricewaterhouseCoopers Australian firm	**20,000**	19,500	**20,000**	19,500
Remuneration for other services:				
Auditor of the company – PricewaterhouseCoopers Australian firm	**17,800**	27,910	**17,800**	27,910
	37,800	47,410	**37,800**	47,410

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

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

Note 18 Related parties (continued)

Transactions of directors and director related entities concerning shares

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

	2004 Number	2003 Number
Acquisitions		
Ordinary shares – vested	-	1,092,400
Ordinary shares - non-vested	-	888,600
Series A preferred shares	**3,293,907**	4,025,885
QRx Employee Option Plan options over ordinary shares	-	1,000,000
Disposals		
QRx Employee Option Plan options exercised	-	1,000,000

The establishment of the QRx Employee 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:

	2004 Number	2003 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**	4,025,885
Options over ordinary shares	-	-

Wholly- owned group

The wholly- owned group consists of QRx Pharma 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

	2004	2003
Current payable	**27,700**	-

Other transactions with directors and related entities

Contracted services
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 $348,668 (2003 $369,670).

Development and patent fees
UniQuest Pty Limited is a significant shareholder of the company, owning 3,612,500 vested ordinary shares as at 30 June 2004. During the year, the company paid quarterly fees to UniQuest Pty Limited for the development and commercialisation of technology transferred from Haempatch Pty Limited to UniQuest Pty Limited. Total development fees paid to UniQuest Pty Limited during the year was approximately $507,000 (2003: $664,000).

During the year, the company paid UniQuest Pty Limited the amount of nil (2003: $33,205) in relation to patent fees.

Controlling entity

The ultimate parent entity in the wholly owned group is QRx Pharma Pty Limited.

Note 19 Investment in controlled entities

Name of entity	Country of incorporation	Class of shares	Equity holding 30 June 2004 %	Equity holding 30 June 2003 %
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	
	2004 $	2003 $	**2004 $**	2003 $
Loss from ordinary activities after income tax	**(4,219,967)**	(3,161,552)	**(4,221,818)**	(3,187,401)
Depreciation and amortisation	**26,955**	4,876	**26,955**	4,876
Amortisation of intangibles	-	889,307	-	414,375
Write down of investment to recoverable amount	-	-	-	500,750
Decrease/ (increase) in other operating assets	**46,495**	(82,740)	**46,495**	(59,247)
Increase in trade creditors and accruals	**204,056**	322,649	**204,056**	322,650
Increase in other operating liabilities	**11,466**	6,505	**11,466**	6,505
Net outflow from operating activities	**(3,930,995)**	(2,020,954)	**3,932,846**	(1,997,492)

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 6th January 2004, the Company entered into a development agreement with Shire Laboratories Inc to evaluate the application of Shire's Control Release technology. The original term of the agreement for stages 1 and 2 is 10 months one year and total committed future development fees as at 30 June 2004 are approximately $264,000

On 2nd March 2004, the Company entered into a development agreement with CIT to conduct a toxicity study. The committed future development fee as at 30 June 2004 was $146,568. As at the date of this report the study has been completed.

On 26th May 2004, the Company entered into a development agreement with The University of Michigan. The original term of the agreement is one year and total committed future development fees as at 30 June 2004 are approximately $143,000

Note 23 Employee Benefits

	Consolidated 2004 $	Consolidated 2003 $	Parent 2004 $	Parent 2003 $
Employee benefits and related on-costs liabilities				
Provision for employee benefits – current (note 11)	**17,971**	6,505	**17,971**	6,505
	Numbers		**Numbers**	
Employee numbers				
Average number of employees during the financial year	**4**	3	**4**	3

QRx Pharma 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 within the relevant period or if the option holder leaves the employment of QRxPharma. The Board reserves a discretion to waive the latter provision.

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	Lapsed during the year	Balance at end of the year
			Number	Number	Number	Number	Number
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 23 Employee Benefits (continued)

Consolidated and parent entity – 2003								
19 December 2002	19 December 2002	$1,50		-	1,000,000	1,000,000	-	-
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
Total				-	1,185,000	1,000,000	-	185,000

Note 24 Events occurring after reporting date

Since balance date, the board has resolved to proceed with the additional funding through the issue of convertible loan facilities. $2.5m is to be raised in two tranches. $862,529 has to date been received from investors. The financial effect of the above has not been brought to account at 30 June 2004.

Directors' declaration

The directors declare that the financial statements and notes set out on pages 3 to 21:

(a) comply with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

(b) give a true and fair view of the company's and consolidated entities financial position as at 30 June 2004 and of their performance, as represented by the results of their operations and its cash flows, for the financial year ended on that date.

In the directors' opinion:

(a) the financial statements and notes are in accordance with the Corporations Act 2001; and

(b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

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

GW Pace
Director

G.W. Pace

Sydney
23 September 2004

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

Audit opinion

In our opinion, the financial report of QRx Pharma Pty Limited:

- gives a true and fair view, as required by the *Corporations Act 2001* in Australia, of the financial position of QRx Pharma Pty Limited and the QRx Pharma Pty Limited Group (defined below) as at 30 June 2004, and of their performance for the year ended on that date, and
- is presented in accordance with the *Corporations Act 2001*, Accounting Standards and other mandatory financial reporting requirements in Australia, and the *Corporations Regulations 2001*.

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

Scope

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for both QRx Pharma Pty Limited (the company) and the QRx Pharma Pty Limited Group (the consolidated entity), for the year ended 30 June 2004. The consolidated entity comprises both the company and the entities it controlled during that year.

The directors of the company are responsible for the preparation and true and fair presentation of the financial report in accordance with the *Corporations Act 2001*. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit approach

We conducted an independent audit in order to express an opinion to the members of the company. Our audit was conducted in accordance with Australian Auditing Standards, in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001*, Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

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When this audit report is included in a document containing the directors' report, our procedures include reading the directors' 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
23 September 2004