

Koala Corporation Australia Ltd

**A.C.N 010 679 633**

General Meeting - 20 May 2005

Explanatory Memorandum

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## 1. INTRODUCTION

This Explanatory Memorandum is being sent to shareholders in advance of the General Meeting of Shareholders to be held on 20 May 2005. The resolutions to be considered are as follows:

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| Resolution 1 | Selective Buy-Back of Shares                                |
| Resolution 2 | Issue of Options to Non-Executive Director – Howard Stack   |
| Resolution 3 | Issue of Options to Non-Executive Director – Phillip Dubois |
| Resolution 4 | Issue of Options to Non-Executive Director – Peter Grogan   |
| Resolution 5 | Issue of Options to Non-Executive Director – Charles Ho     |
| Resolution 6 | Approval of Executive Share Option Plan                     |
| Resolution 7 | Approval of Issue of Options to Managing Director           |
| Resolution 8 | Change of Name to Magnetica Limited                         |

Further information regarding the recent activities of Koala Corporation Australia Limited and the resolutions to be considered are set out in this Explanatory Memorandum.

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## 2. RECENT ACTIVITIES OF THE COMPANY

Koala Corporation Australia Limited (**Koala** or the **Company**) has over the last 12 months been actively engaged in a process of restructuring its assets and shareholdings. The Company's objective has been to strengthen its balance sheet sufficiently to enable it to develop and commercialise its technology interests and to reinstate the shares of the Company to trading on the Australian Stock Exchange Limited (**ASX**).

The Company has now made significant progress towards commercialising its technology assets and exploiting its rights under various agreements with UniQuest Pty Limited (**UniQuest**), the University of Queensland's major technology transfer company.

In January 2005 the Company successfully completed a \$4,000,000 capital raising with the assistance of InterFinancial Limited. The Company also obtained shareholder approval for a re-structure of the Company, which has now been completed, and most significantly involved:

- the acquisition of a 100% interest in the Asymmetric Magnet Technology;
- UniQuest becoming a major shareholder in the Company;
- the discharge of significant liability involved in the financing of the original acquisition of the technologies and the research programmes conducted on the technologies;
- the unwinding of a series of complex research and commercialisation arrangements with UniQuest Limited;
- the consolidation of the Company's shares; and

- arrangements being entered into with the liquidators of two of the Companies former major shareholders to Buy-Back a significant portion of their shares.

These events have effected a re-organisation of the share register, clarified ownership of the technology assets and re-structured commercialisation arrangements to allow a smoother path forward for the commercialisation of the Company's key assets and access, via fresh agreements with UniQuest Ltd, to a quality product pipeline.

Significantly, the Company has also appointed a new Board. The Board now has a highly experienced Chairman and a mix of Directors including respected radiologists from Australia and the USA and other Directors conversant with the core technologies owned by the Company.

It has also appointed Dr David Evans as its Managing Director and has moved to appoint a small but experienced team of staff.

The Company has now commenced to make rapid strides and discussions with a number of international manufacturers on the conducting of feasibilities and preliminary designs for the construction of prototype magnets.

At the Annual General Meeting of the Company held in December 2004 shareholders approved the proposed issue by the Company of up to 50,000,000 shares at an issue price of a minimum of 40 cents by way of a public capital raising. Pursuant to the Listing Rules of the ASX, and a waiver of those rules granted by the ASX, this approval allowed the company to proceed with this raising providing shares are issued by the Company within time limits imposed by the ASX pursuant to the Listing Rules.

Currently the Company is progressing due diligence and prospectus preparation with the view to the issuing of a prospectus for a public capital raising (the Capital Raising) in or about June 2005. The precise size of this raising has not as yet been determined but it is likely to be in the range of 25,000,000 to 35,000,000 shares issued at an issue price of 40 cents per share. For the purposes of this Explanatory Memorandum unless otherwise specified a reference to the Capital Raising is a reference to a raising of \$12,000,000 by way of the issue of 30,000,000 shares at an issue price of 40 cents per share. The successful completion of the Capital Raising will facilitate the quotation of the Company's shares on the ASX.

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### **3. THE RESOLUTIONS TO BE CONSIDERED**

#### **RESOLUTION 1 – SELECTIVE BUY-BACK OF SHARES**

##### **Background**

Prior to the consolidation of the Company's shares and the completion of the recent seed capital raising, 80% of the shares in the Company were held by Bradley Keeling Management Pty Ltd (In Liquidation) (**BKM**) and Bradley Keeling Hospitality Pty Ltd (In Liquidation) (**BKH**). Both of these companies had been placed in liquidation in 2002. The liquidation placed significant obstacles in the course of the Company attempting to advance its business.

As was outlined in the material forwarded to shareholders prior to the Annual General Meeting held in December 2004, it was part of the re-structuring proposal agreed to between the Company and the liquidators that a portion of the liquidators' shares would be bought back by the Company. One tranche of shares, equal to 25% of the liquidators' post-consolidation holding of shares, was to be bought back following the completion of the seed capital raising. This Buy-Back was effected in January 2005. As a consequence of

that Buy-Back 2,162,329 shares were bought back from the liquidators by the Company and subsequently cancelled in return for a payment to the liquidators of \$576,628.

It was further agreed between the Company and the liquidators that a further Buy-Back of shares is to be effected upon the Company conducting the Capital Raising.

This resolution seeks approval for this further proposed Buy-Back (the Buy-Back). The terms of the Buy- Back are detailed below.

#### **Particulars of the terms of the Buy-Back**

Under the Buy-Back, the Company proposes to effect a Buy-Back of the following shares:

BKH	1,616,859 Shares
BKM	1,623,376 Shares
<b>Total</b>	<b>3,240,235 Shares</b>

The shares to be bought back from BKH represent all of the remaining shareholding of BKH in the Company. BKM will retain 3,246,754 shares in the Company after the Buy-Back.

The Buy-Back will be effected following the completion of the Capital Raising and the price per share offered under the Buy-Back will be the price at which shares are issued to the public under the Capital Raising.

#### **Capital Structure**

The following table sets out the current shareholding in the Company.

<b>Shareholder</b>	<b>Number of shares</b>	<b>%</b>
BKH	1,616,859	3.32
BKM	4,870,130	10.04
UniQuest	25,000,000	51.52
Other Shareholders	17,041,961	35.12
<b>Total</b>	<b>48,528,950</b>	<b>100.00%</b>

Following the completion of the Buy-Back and the Capital Raising the capital structure of the Company will be as follows:-

<b>Shareholder</b>	<b>Number of shares</b>	<b>%</b>
BKH	Nil	0
BKM	3,246,754	4.31
UniQuest	25,000,000	33.21
Other Shareholders	47,041,961	62.48
<b>Total</b>	<b>75,288,715</b>	<b>100.00%</b>

### **The number and percentage of shares to be bought back**

The total number of shares to be brought back will be 3,240,235 shares. Currently this represents 6.7% of the Company. The precise number of shares to be issued pursuant to the capital raising has yet to be finalised. However, it is likely to be in the range of 25,000,000 shares to 35,000,000 shares. If 30,000,000 shares are issued under the Capital Raising then the percentage of shares to be bought back from the liquidators will amount to 4.1% of the shares in the Company.

### **Offer price or formula for the calculation of the offer price**

The offer price under the Buy-Back will be that price at which shares are issued to the public pursuant to the Capital Raising. Pursuant to the approvals obtained from the shareholders of the Company at the general meeting held in December 2004, the shares issued under the Capital Raising will be issued at not less than 40 cents per share. Therefore, 40 cents per share is the minimum amount per share that will be paid to BKH and BKM under the Buy-Back. If the shares are issued under the Capital Raising at a higher price then, similarly, the offer under the Buy-Back to purchase shares from BKH and BKM will be made at that higher price.

### **The reasons for the Buy-Back**

The Company has undertaken the Buy-Back as part of the overall re-structuring of the Company to facilitate a re-quotations of the Company's shares on the ASX. The liquidators of BKH and BKM are required, in the capacity of liquidators, to realise assets under their control for the benefit of creditors in a timely fashion. The Company considers that it was in the best interests of an efficient re-structuring that they negotiate a commercial agreement with the liquidators to achieve this end and as a consequence the Buy-Back arrangements were agreed to between the parties.

### **The interests of any directors who may participate in the Buy-Back**

No directors have any interest in the Buy-Back. No directors are participating either directly or indirectly in the Buy-Back.

### **The financial effect of the Buy-Back on the Company**

If the Buy-Back is undertaken at a price of 40 cents per share, the total cost of the Buy-Back to the Company will be \$1,296,094. If the Buy-Back were undertaken at 50 cents per share, the total cost of the Buy-Back to the Company will be \$1,620,118. The Buy-Back will only be effected if the Company has successfully completed the Capital Raising.

### **The source of funds for the Buy-Back**

The funds for the Buy-Back will be provided from the Capital Raising.

### **The effect the Buy-Back will have on the control of the Company**

The Buy-Back will not have any significant effect on the control of the Company. Prior to the consolidation of shares undertaken by the Company in December 2004, BKH and BKM together controlled 80% of the shares of the Company. Following the consolidation and the seed capital raising, BKH and BKM held 13.4% of the Company. Following the further proposed Buy-Back, BKH will not hold any shares in the Company and BKM will hold 3,246,754 shares in the Company equating to between 4.3% if 30,000,000 shares are issued pursuant to the Capital Raising.

## **The advantages and disadvantages of the Buy-Back**

The principal advantage of the Buy-Back is that it rationalises the interest of the liquidators in the Company and provides an orderly exit for them from their shareholding position in the Company at a price which the Company considers to be reasonable in all the circumstances. The principal disadvantage of the Buy-Back is the cost to the Company of effecting same.

## **Financial statements**

A copy of the Company's financial statements for the half-year ended 31 December 2004 are attached to this meeting material.

## **Directors recommendations**

Each of the directors of the Company recommends the Buy-Back to the shareholders.

## **RESOLUTIONS 2, 3, 4 and 5 – ISSUE OF OPTIONS TO NON – EXECUTIVE DIRECTORS**

### **Background**

Resolutions 2 through to 5 inclusive seek shareholder approval for the grant of an aggregate total of 1,400,000 options by the Company to Mr Howard Stack, Dr Phillip Dubois, Mr Peter Grogan, and Dr Charles Ho (the **Recipient Directors**).

The grant of the options to the Recipient Directors is intended to act as a strong incentive to align with the Company's strategic plan focusing on seeking improved performance, the growth of the Company and better returns for shareholders.

## Key Details of Options

Key details of the options to be granted by the Company to the Recipient Directors are set out below:

Recipient Director	Number	Offer Price	Exercise Details	Vesting date	Expiry Date
Howard Stack	500,000	No consideration is payable by the Recipient Director	<p>166,666 options at an exercise price equivalent to the issue price of shares under the Capital Raising (the <b>Issue Price</b>) plus 25%;</p> <p>166,667 options at an exercise price equivalent to the Issue Price plus 50%; and</p> <p>166,667 options at an exercise price equivalent to the Issue Price plus 100%.</p>	Within 30 days of shareholder approval	5 years from date of issue
Phillip Dubois Peter Grogan Charles Ho	300,000 per director	No consideration is payable by the Recipient Directors	<p>100,000 options to each director at an exercise price equivalent to the Issue Price plus 25%;</p> <p>100,000 options to each director at an exercise price equivalent to the Issue Price plus 50%; and</p> <p>100,000 options to each director at an exercise price equivalent to the Issue Price plus 100%.</p>	Within 30 days of shareholder approval	5 years from date of issue

A summary of the terms and conditions of the options is set out in Schedule 1 to this Explanatory Memorandum.

## Chapter 2E of the Corporations Act

Chapter 2E of the Corporations Act prohibits the Company from giving a financial benefit to a related party of the Company unless either:

- (a) the giving of the financial benefit falls within one of the nominated exceptions to the provisions; or
- (b) prior shareholder approval is obtained to the giving of the financial benefit.

For the purposes of Chapter 2E, the Recipient Directors are related parties by virtue of the fact that they are directors of the Company and the grant of options by the Company constitutes the giving of a financial benefit.

In accordance with the requirements of Chapter 2E, and in particular with section 219 of the Corporations Act, the following information is provided to shareholders to allow them to assess the proposed grant of options by the Company to the Recipient Directors:

- (a) The Recipient Directors are related parties of the Company to whom the proposed Resolutions would permit the financial benefits to be given.
- (b) The nature of the financial benefit to be given to Howard Stack is the grant of 500,000 options.
- (c) The nature of the financial benefit to be given Phillip Dubois, Peter Grogan and Charles Ho is the grant of 300,000 options each.
- (d) As at the date of this Explanatory Memorandum, the issued capital of the Company is 48,528,950 Shares. The following table sets out the capital structure of the Company as at the date of this Explanatory Memorandum and after the proposed offers to be undertaken pursuant to the Prospectus. The table also sets out the issued capital of the Company should:-
  - (i) the Recipient Directors exercise all of their options;
  - (ii) Dr David Evans exercises all of the options proposed to be granted to him pursuant to Resolution 7; and
  - (iii) no other securities are issued by the Company in the meantime.

<b>Description</b>	<b>Shares</b>
Existing Shares on issue	48,528,950
Shares subject to the Buy-Back	(3,240,235)
Shares offered under the Capital Raising	30,000,000
Total maximum number of Shares on issue after completion of the Buy-Back and Capital Raising	75,288,715
<i>Options proposed to be issued to Recipient Directors</i>	<i>1,400,000</i>
<i>Options proposed to be offered to Dr David Evans (see Resolution 7)</i>	<i>3,000,000</i>
Maximum number of shares on issue following exercise of all options by Recipient Directors and Dr Evans	79,688,715

- (e) If shareholders approve the grant of options to the Recipient Directors, the exercise of the options by the Recipient Directors will result in a dilution of all other shareholders' holdings in the Company of approximately 2%, subject to the completion of the Capital Raising and the and options the subject of Resolution 7 being granted and subsequently exercised.
- (f) Assuming Resolutions 2, 3, 4 and 5 are approved by shareholders, the Recipient Directors will be entitled to the following securities in the Company, subject to satisfaction of the conditions relating to the exercise of the options and subsequent exercise of the options by the Recipient Directors:

<b>Recipient Director</b>	<b>Number of Shares issued following exercise of all options</b>	<b>Shares currently held by Recipient Directors</b>	<b>Total Shares held after exercise of all options</b>
Howard Stack	500,000	375,000	875,000
Phillip Dubois	300,000	375,000	675,000
Peter Grogan	300,000	3,247	303,247
Charles Ho	300,000	333,305	633,305

- (g) Details of the proposed remuneration of the Recipient Directors are as follows:

<b>Recipient Director</b>	<b>Directors' Fees</b>
Howard Stack	\$30,000
Dr Phillip Dubois	\$20,000
Peter Grogan	\$20,000
Dr Charles Ho	\$20,000

- (h) The Recipient Directors do not wish to make a recommendation in relation to Resolutions 2, 3, 4 and 5 as each has an interest in the outcome of those Resolutions. David Evans, the Managing Director of the Company, is in favour of the grant of options to the Recipient Directors and recommends in favour of resolutions 2, 3, 4 and 5.
- (i) The options will be granted by the Recipient Directors for no consideration and therefore no funds will be raised by the grant of the options to the Recipient Directors. Any funds raised from time to time due to the exercise of any options will be used as the Board sees fit.
- (j) Other than the information set out in this Explanatory Memorandum the Company believes there is no other information that would be reasonably required by shareholders in order to decide whether it is in the best interests of the Company to pass Resolutions 2, 3, 4 and 5.

## Details Concerning Valuation of Executive options

The options to be granted to the Recipient Directors will not be quoted on the ASX and as such have no actual market value.

BDO Kendalls Securities Ltd has provided an indicative valuation for the options to be granted to the Recipient Directors.

Recipient Director	Exercise Price	Value per options	Number of options	Total Value
Howard Stack	The issue price of shares under the Capital Raising (the <b>Issue Price</b> ) plus 25%	\$0.187	166,666	\$31,166.54
	Issue Price plus 50%	\$0.178	166,667	\$29,666.73
	Issue Price plus 100%.	\$0.161	166,667	\$26,833.39
<b>TOTAL</b>			<b>500,000</b>	<b>\$87,666.66</b>
Dr Phillip Dubois	Issue Price plus 25%	\$0.187	100,000	\$18,700.00
	Issue Price plus 50%	\$0.178	100,000	\$17,800.00
	Issue Price plus 100%	\$0.161	100,000	\$16,100.00
<b>TOTAL</b>			<b>300,000</b>	<b>\$52,600.00</b>
Peter Grogan	Issue Price plus 25%	\$0.187	100,000	\$18,700.00
	Issue Price plus 50%	\$0.178	100,000	\$17,800.00
	Issue Price plus 100%	\$0.161	100,000	\$16,100.00
<b>TOTAL</b>			<b>300,000</b>	<b>\$52,600.00</b>
Dr Charles Ho	Issue Price plus 25%	\$0.187	100,000	\$18,700.00
	Issue Price plus 50%	\$0.178	100,000	\$17,800.00
	Issue Price plus 100%	\$0.161	100,000	\$16,100.00
<b>TOTAL</b>			<b>300,000</b>	<b>\$52,600.00</b>

The valuation was made using the Black-Scholes options Pricing Model on the basis of the following assumptions regarding the various inputs that comprise the valuation model:

- (a) The Capital Raising is successfully completed and the shares of the Company are quoted and remain quoted on the ASX for the life of the options.
- (b) The underlying spot price of \$0.40 used for the purposes of this valuation is based on the proposed issue price of shares pursuant to the Capital Raising.
- (c) As at the date of this Explanatory Memorandum, the Company has not forecast any future dividend payments. For the purposes of this valuation it has been assumed that the Company's projected annual dividend yield is nil.
- (d) A volatility factor of 78% was assumed based on the volatility of a basket of comparable companies shares over the last 12 months.
- (e) A risk free rate of 5.37% which is the 5 year Commonwealth Treasury Bond as at 15 April 2005.
- (f) An expiry date of the options of 20 May 2010.

### **ASX Listing Rules**

ASX Listing Rule 10.11 prohibits the issue of securities to a director of a company unless the approval of the shareholders of the company is obtained. Listing Rule 7 broadly prohibits a company from issue more than 15% of its shares in any one year. Pursuant to Listing Rule 7.2 (Exception 14), if shareholder approval is given under Listing Rule 10.11, further approval is not required for the purposes of Listing Rule 7.1.

Listing Rule 10.13 sets out a number of matters which must be included in a notice of meeting requesting shareholder approval under Listing Rule 10.11. In accordance with Listing Rule 10.13, the following information is provided to shareholders in relation to Resolutions 2, 3, 4 and 5:

- (a) The Company will grant up to 1,400,000 options to the Recipient Directors. If all options are exercised by the Recipient Directors, the Recipient Directors will be entitled to 1,400,000 Shares.
- (b) The options are granted to each of the Recipient Directors for no consideration and, therefore, no funds will be raised by the grant of the options to the Recipient Directors. Any funds raised from time to time due to the exercise of any options will be used as the Board sees fit.
- (c) The Company acknowledges that the issue of options to non-executive directors is not in accordance with recommendation 9.3 of the ASX Principles of Good Corporate Governance and Best Practice Recommendations. Despite the Recommendations the Company considers it appropriate to issue these options given the relatively low level of remuneration that the Company proposes to pay the non-executive directors for their services.
- (d) For details of the exercise prices and expiry dates of the options please refer to above.

- (e) The options will be granted to the Recipient Directors on a date which is not more than one month after the date of the General Meeting the subject of this Explanatory Memorandum.
- (f) For details of the indicative valuations of the options, please refer above.
- (g) The terms and conditions of the options to be issued to the Recipient Directors are set out in Schedule 1 to this Explanatory Memorandum.

### **Section 195 of the Corporations Act**

Section 195 of the Corporations Act provides, in essence, that a director of a public company may not vote or be present during meetings of directors when matters in which that director holds a “material personal interest” are being considered. Resolutions 2, 3, 4 and 5 seek approval to grant options to subscribe for shares in the capital of the Company to five out of six of the directors of the Company.

As four out of the six directors are considered to hold a material personal interest in the consideration of the matter, a quorum cannot be formed to consider the matter at board level. However, by reason of section 195(4), the directors are permitted in such instances to put the matter before the shareholders to consider and resolve.

The directors have accordingly exercised their right under section 195(4) of the Corporations Act and have resolved to place the proposed grant of options to the Recipient Directors to shareholders to consider and resolve upon.

### **RESOLUTION 6 – APPROVAL OF EXECUTIVE SHARE OPTION PLAN**

The directors of the Company propose to implement an executive share option plan called the Magnetica Limited Executive Share Options Plan (**Plan**). Although the Company is not required to obtain shareholder approval for the introduction of the Plan if approval is obtained then securities issued pursuant to the plan will be considered as an exception to ASX Listing Rule 7.1. ASX Listing Rule 7 broadly provides, subject to certain exceptions, that a company may not issue or agree to issue securities which represent more than 15% of the nominal value of the company’s issued capital at the beginning of any 12 month period without obtaining shareholder approval.

#### **Objectives of the Plan**

The major objectives of the Plan are:-

- (a) to provide an appropriate method to provide long term incentives for participation in the Company’s future growth;
- (b) to act as an incentive to motivate directors of the Company;
- (c) to generate loyalty from senior executives;
- (d) to provide the Company with the ability to attract executives of a higher calibre; and
- (e) to form a valuable tool to be used as part of remuneration planning for executives.

Once shareholder approval is obtained, the Company intends to grant 3,000,000 options in accordance with Resolution 7 to Dr David Evans and may issue further shares and options to executives of the Company in accordance with the terms of the Plan. However all further grants of options under the Plan to any director of the Company will require the specific approval by shareholders.

### **Summary of the terms and conditions of the Plan**

- (a) Participants in the Plan may be executives of the Company or executive directors of the Company.
- (b) The Company may in its absolute discretion offer options to eligible executives on terms and conditions as determined by the Company.
- (c) The Company will meet the costs of establishing, managing and administering the Plan.
- (d) Participants in the Plan may not transfer, assign or otherwise encumber options granted under the Plan other than with the consent of the Board and in accordance with the terms of the Plan.
- (e) If a participant ceases to be a senior executive by reason of resignation, retirement, or termination for cause, that participant shall, subject to the Rules of the Plan, forfeit all entitlement to exercise options granted under the Plan.
- (f) If a participant ceases to be a executive by reason of retirement, death or permanent disability (the "ceasing event") the participant or the participant's personal representative shall retain their entitlement to exercise their options granted under the Plan for six months after the ceasing event or such later time period permitted by the board of directors of the Company.
- (g) Shares which are issued as a result of the exercise of options granted under the Plan will rank equally in all respects with fully paid shares on issue and the Company will apply for quotation of the shares on ASX.
- (h) In the event of any reconstruction (including consolidation, subdivision, reduction or return) of the issued capital of the Company, all terms of the options will be changed to the extent necessary to comply with the ASX Listing Rules applying to a reorganisation of capital at the time of the reorganisation.
- (i) In the event that there is a publicly announced proposal which the board of directors of the Company reasonably believes may lead to another party legally owning more than 50% of the Company's issued share capital, or if another party owns more than 50% of the Company's issued share capital, the board may by notice to all participants, permit options to be exercised early.
- (j) The options shall be issued on the terms and conditions set out in the Rules of the Plan any other terms that are required by the Corporations Act, ASX Listing Rules and the Company's constitution.

A copy of the full Rules of the Plan will be sent to any member of the Company upon request.

## RESOLUTION 7 – APPROVAL OF ISSUE OF OPTIONS TO MANAGING DIRECTOR

The Company proposes to make a grant of 3,000,000 options to the managing director of the Company, Dr David Evans.

The proposed issue of options is intended to provide an appropriate and adequate incentive to Dr Evans to retain his services and reinforce his commitment to the Company for its future development.

### Terms and Conditions of the options

Number	Offer Price	Exercise Details	Vesting Date	Expiry Date
1,000,000	No consideration is payable for the grant of options	Capital Raising Issue Price plus 25%	The date of the requotation of the shares of the Company on the ASX following the completion of the Capital Raising (the <b>Relisting Date</b> ).	3 years after the Relisting Date.
1,000,000	No consideration is payable for the grant of options	Capital Raising Issue Price plus 35%	The completion of the Year 2 Milestones but in any event no earlier than 1 year after the Relisting Date.	4 years after the Relisting Date.
1,000,000	No consideration is payable for the grant of options	Capital Raising Issue Price plus 50%	The completion of the Year 3 Milestone but in any event no earlier than 2 years after the Relisting Date.	5 years after the Relisting Date.

A summary the terms and conditions of the options, including the Milestones, are set out in Schedule 2.

### Chapter 2E of the Corporations Act

Chapter 2E of the Corporations Act prohibits the Company from giving a financial benefit to a related party of the Company unless either:

- (a) the giving of the financial benefit falls within one of the nominated exceptions to the provisions; or
- (b) prior shareholder approval is obtained to the giving of the financial benefit.

For the purposes of Chapter 2E, Dr Evans is a related party by virtue of the fact that he is a Director of the Company and the grant of options by the Company constitutes the giving of a financial benefit.

In accordance with the requirements of Chapter 2E, and in particular with section 219 of the Corporations Act, the following information is provided to shareholders to allow them to assess the proposed grant of options to Dr Evans:

- (a) Dr Evans is a related party of the Company to whom the proposed Resolution would permit the financial benefits to be given;
- (b) the nature of the financial benefit to be given to Dr Evans is the grant of 3,000,000 options;
- (c) as at the date of this Explanatory Memorandum, the issued capital of the Company is 48,528,950 Shares. The following table sets out the capital structure of the Company as at the date of this Explanatory Memorandum and after the proposed offers to be undertaken pursuant to the Prospectus. The table also sets out the issued capital of the Company should:-
  - (i) the Recipient Directors exercise all of their options proposed to be granted to them under Resolutions 2, 3, 4 and 5;
  - (ii) Dr David Evans exercises all of the options proposed to be granted to him pursuant to Resolution 7; and
  - (iii) no other securities are issued by the Company in the meantime.

<b>Description</b>	<b>Shares</b>
Existing Shares on issue	48,528,950
Shares subject to the Buy-Back	(3,240,235)
Shares offered under the Capital Raising	30,000,000
Total maximum number of Shares on issue after completion of the Buy-Back and Capital Raising	75,288,715
<i>Options proposed to be issued to Recipient Directors</i>	<i>1,400,000</i>
<i>Options proposed to be offered to Dr David Evans (see Resolution 7)</i>	<i>3,000,000</i>
Maximum number of shares on issue following exercise of all options by Recipient Directors and Dr Evans	79,688,715

- (d) If shareholders approve the grant of options to Dr Evans, the exercise of the options by Dr Evans will result in a dilution of all other shareholders' holdings in the Company of approximately 3.8%, assuming that the Capital Raising is fully subscribed and the options the subject of Resolutions 2, 3, 4 and 5 are granted and subsequently exercised.

- (e) Assuming this resolution is approved by shareholders, Dr Evans will be entitled to the following securities in the Company, subject to satisfaction of the conditions to the exercise of the options, and the exercise of those options:

<b>Number of shares issued following exercise of all options</b>	<b>Shares currently held by Dr Evans</b>	<b>Shares held after exercise of all options</b>
3,000,000	150,000	3,150,000

- (f) The proposed remuneration for Dr Evans, other than the grant of options consists of an annual salary of \$325,000 plus statutory superannuation of \$11,584. This salary will commence upon the completion of the Capital Raising. Until that time Dr Evans salary will be \$200,000 plus statutory superannuation entitlements.
- (g) Dr Evans does not wish to make a recommendation in relation to Resolution 7 as he has an interest in the outcome of that resolution. All other directors of the Company are in favour of the grant of options to Dr Evans and recommend in favour of Resolution 7.
- (h) The options will be granted to Dr Evans for no consideration and therefore no funds will be raised by the grant of the options to Dr Evans. Any funds raised from time to time due to the exercise of any options will be used as the Board sees fit.
- (i) Other than the information set out in this Explanatory Memorandum the Company believes there is no other information that would be reasonably required by shareholders in order to decide whether it is in the best interests of the Company to pass Resolution 7.

### **Details Concerning Valuation Options**

The options to be granted to Dr Evans will not to be quoted on ASX and as such have no actual market value.

BDO Kendalls Securities Ltd has provided an indicative valuation for the options to be granted to Dr Evans.

<b>Exercise Price</b>	<b>Value per option</b>	<b>Number of options</b>	<b>Total Value</b>
Capital Raising Issue Price plus 25%	\$0.112	1,000,000	\$112,000
Capital Raising Issue Price plus 35%	\$0.097	1,000,000	\$97,000
Capital Raising Issue Price plus 50%	\$0.072	1,000,000	\$72,000
<b>Total</b>		<b>3,000,000</b>	<b>\$281,000</b>

The valuation was made using the Black-Scholes options Pricing Model on the basis of the following assumptions regarding the various inputs that comprise the valuation model:

- (a) The Capital Raising is successfully completed and the shares of the Company are quoted and remain quoted on the ASX for the life of the options.
- (b) The underlying spot price of \$0.40 used for the purposes of this valuation is based on the proposed issue price of shares pursuant to the Capital Raising.
- (c) As at the date of this Explanatory Memorandum, the Company has not forecast any future dividend payments. For the purposes of this valuation it has been assumed that the Company's projected annual dividend yield is nil.
- (d) A volatility factor of 78% was assumed based on the volatility of a basket of comparable companies shares over the last 12 months.
- (e) Commonwealth Bond rates of 5.37%, 5.39%, and 5.37%, which best match the option terms, have been used as a proxy for the risk free rate in each calculation.
- (f) The exercise periods of the options are as set out in the relevant table in this Explanatory Memorandum. For the purposes of this valuation it has been assumed that the options will not be exercised any earlier than the relevant expiry date.

### **ASX Listing Rules**

ASX Listing Rule 7 broadly prohibits a company from issuing more than 15% of its shares in any one year. Pursuant to Listing Rule 7.2 (Exception 9), if securities are issued under an employee incentive scheme, such as that proposed in Resolution 7, no further shareholder approval is not required for the purposes of Listing Rule 7.1.

Listing Rule 10.11 prohibits the issue of securities to a director of a company unless the approval of the shareholders of the company is obtained. Listing Rule 10.14 further prohibits the issue of securities under an employee incentive scheme to directors without first obtaining the approval of shareholders. Listing rule 10.15A sets out a number of matters which must be included in a notice of meeting requesting shareholder approval under Listing Rule 10.14.

In accordance with Listing Rule 10.15A, the following information is provided to shareholders in relation to Resolution 7.

- (a) The Company will grant up to 3,000,000 options to Dr Evans. If all options are exercised by the Dr Evans he will be entitled to 3,000,000 shares.
- (b) The options are granted to Dr Evans for no consideration and, therefore, no funds will be raised by the grant of the options to Dr Evans. Any funds raised from time to time due to the exercise of any options will be used as the Board sees fit.
- (c) Other than the options proposed to be issued to Dr Evans no other securities have or are currently proposed to be issued under the Company's Executive Share Option Plan.

- (d) For details of the exercise prices and expiry dates of the options please refer above.
- (e) The options will be granted to Dr Evans on a date which is not more than one month after the date of the General Meeting the subject of this Explanatory Memorandum.
- (f) For details of the indicative valuations of the options, please refer above.
- (g) The terms and conditions of the options to be issued to Dr Evans are set out in Schedule 2 to this Explanatory Memorandum.
- (h) Details of any securities issued under the Executive Share Option Plan will be published in each annual report of the Company. The fact that approval has been obtained for any such issues will also be noted in the annual report.
- (i) Any additional person who becomes entitled to participate in the Executive Share Option Plan after that resolution has been passed and who has not been named in this notice of meeting will not participate in any issue of securities under the Executive Share Option Plan until approval is obtained under Listing Rule 10.14.

## **RESOLUTION 8 – CHANGE OF NAME TO MAGNETICA LIMITED**

It is proposed that the name of the Company be changed from "Koala Corporation Australia Limited" to "Magnetica Limited", to reflect and the focus of the Company on the bio-medical sector and, in particular, the magnetic resonance imaging business of the Company.

Resolution 8 is proposed as a special resolution and requires a 75% majority of the shareholders present and voting at the General Meeting.

---

## VOTING EXCLUSION STATEMENTS

The following voting exclusion statement applies to the resolutions listed below under the ASX Listing Rules to the following persons (Excluded Persons). The Company will disregard any votes cast on these resolutions by the following Excluded Persons:

<b>Resolution Number</b>	<b>Voting Exclusion</b>
Resolutions 2, 3, 4 and 5.	In accordance with Listing Rules 7.1, 10.11, 14.11 and section 224 of the Corporations Act, the Company will disregard any votes cast on Resolutions 2, 3, 4 and 5 by Howard Stack, Dr Phillip Dubois, Peter Grogan, and Dr Charles Ho and by any Associate of them. However, the Company need not disregard a vote if it is cast by any of the above named as a proxy for a person who is entitled to vote, in accordance with the directions on the Proxy Form, or it is cast by any of the above named chairing the Meeting as a proxy for a person who is entitled to vote, in accordance with a direction on the proxy form to vote as the proxy decides.
Resolution 6	In accordance with Listing Rules 7.2 Exception 9 and Listing Rule 14.11 the Company will disregard any votes cast on Resolution 6 by Dr David Evans and by any Associate of Dr Evans. However, the Company need not disregard a vote if it is cast by Dr Evans as a proxy for a person who is entitled to vote, in accordance with the directions on the Proxy Form, or it is cast by Dr Evans chairing the Meeting as a proxy for a person who is entitled to vote, in accordance with a direction on the proxy form to vote as the proxy decides.
Resolution 7	In accordance with Listing Rules 7.1, 10.11 and 14.11 the Company will disregard any votes cast on Resolution 7 by Dr David Evans and by any Associate of Dr Evans. However, the Company need not disregard a vote if it is cast by Dr Evans as a proxy for a person who is entitled to vote, in accordance with the directions on the Proxy Form, or it is cast by Dr Evans chairing the Meeting as a proxy for a person who is entitled to vote, in accordance with a direction on the proxy form to vote as the proxy decides.

## **SCHEDULE 1 - TERMS AND CONDITIONS OF OPTIONS (NON EXECUTIVE DIRECTORS)**

The options to be granted by the Company to the Recipient Directors (**optionholders**), in accordance with Resolutions 2, 3, 4 and 5 are to be issued on the following terms and conditions:

1. Each option entitles the optionholders to subscribe for one Share in the capital of the Company.
2. The Company will issue to the optionholders those options details of which are set out in the discussion of Resolutions 2, 3, 4 and 5 in this Explanatory Memorandum.
3. The options are exercisable after the date of grant until any time up to 5.00 pm Brisbane time on Expiry Date by completing an option exercise form and delivering it together with the payment for the number of Shares in respect of which the options are exercised to the registered office of the Company. Options will lapse if the optionholder ceases to be a Director of the Company within 12 months of the date of grant other than as a result of not being re-elected by shareholders at the Company's next annual general meeting, or if any options are not exercised prior to the Expiry Date.
4. An optionholder may exercise some only of that optionholder's options, which does not affect that optionholder's right to exercise the remainder of their options by the deadline in paragraph 3 above. Options must be exercised in multiples of 1,000 at a time, unless the optionholder exercises all options able to be exercised at that time.
5. Subject to the Corporations Act, the Listing Rules of the ASX and the Company's constitution, the options are not transferable.
6. All Shares issued upon exercise of the options will, from the date they are issued, rank pari passu in all respects with the Company's then issued Shares.
7. Optionholders cannot participate in new issues of capital offered to shareholders of the Company (in respect to unexercised options) during the currency of the options without exercising the options. However, the Company will ensure that for the purpose of determining entitlements to any such issue, the record date will be at least 10 business days after the issue is announced. This will give optionholders the opportunity to exercise their options prior to the date for determining entitlements to participate in any such issue.
8. Subject to paragraph 9, if the Company makes a bonus share issue, a rights issue or any other similar issue of rights or entitlements, there will be no adjustment to the exercise price, the number of Shares per option or any other terms of those options.
9. In the event of any reorganisation (including consolidation, subdivision, reduction or return) of the issued capital of the Company the rights of optionholders, including the number of options or the exercise price of the options or both will be changed to the extent necessary to comply with the Listing Rules of the ASX applying to a reorganisation of capital at the time of the reorganisation.

10. Optionholders will be sent all communications sent to shareholders of the Company, but options do not confer any rights to attend or vote at meetings of shareholders of the Company. Notice may be given by the Company to optionholders in the manner provided by the Company's constitution for the giving of notices to shareholders, and the relevant provisions of the Company's constitution apply with all necessary modification to notices to optionholders.

## SCHEDULE 2 - TERMS AND CONDITIONS OF OPTIONS (MANAGING DIRECTOR)

The options to be granted by the Company to the Dr David Evans (the **Optionholder**), in accordance with Resolution 7 are to be issued on the following terms and conditions:

1. Each option entitles the Optionholder to subscribe for one Share in the capital of the Company.
2. The Company will issue to the Optionholder 3,000,000 options details of which are set out below.
3. Subject to clause 4 the options will vest upon the meeting of the following milestones (the **Milestones**):-
  - (a) 1,000,000 options (**Tranche 1**)
    - Preparation of Business Plan including progress made towards commercialisation of technology.
    - Completion of Capital Raising and Relisting.(the **Year 1 Milestone**)
  - (b) 1,000,000 options (**Tranche 2**)
    - Effective management of the existing option agreement for Ultra-Short Compact Magnet with UniQuest Pty Ltd in such a manner as to produce a commercial outcome for the Company.
    - Completion of construction of a proto-type or achievement of licence, distribution or other types of agreement that advance the commercialisation process of the Company's technologies and capabilities.(the **Year 2 Milestones**)
  - (c) 1,000,000 options (**Tranche 3**)
    - Commencement of a substantive revenue stream to Company from commercialisation of technology.(the **Year 3 Milestone**)
4. Irrespective of the date on which the Milestones are met the options will not vest any earlier than as follows:-
  - (a) Tranche 1 – the Relisting Date;
  - (b) Tranche 2 – 1 year after the Relisting Date;
  - (c) Tranche 3 – 2 years after the Relisting Date.

5. The options will expire on the following dates (the **Expiry Date**):-
  - (a) Tranche 1 – 3 years after the Relisting Date;
  - (b) Tranche 2 – 4 years after the Relisting Date;
  - (c) Tranche 3 – 5 years after the Relisting Date.
6. The exercise price of the options is:-
  - (a) Tranche 1 – 125% of the issue price of the Company's shares pursuant to the Capital Raising undertaken for the purposes of Relisting;
  - (b) Tranche 2 – 135% of the issue price of the Company's shares pursuant to the public Capital Raising undertaken for the purposes of Relisting;
  - (c) Tranche 3 – 150% of the issue price of the Company's shares pursuant to the Capital Raising undertaken for the purposes of Relisting.
7. The options are exercisable from after their vesting date until any time up to 5.00 pm Brisbane time on their Expiry Date by completing an option exercise form and delivering it together with the payment for the number of Shares in respect of which the options are exercised to the registered office of the Company. Options will lapse if the Optionholder ceases to be a Director of the Company within 12 months of the date of grant other than as a result of not being re-elected by shareholders at the Company's next annual general meeting, or if any options are not exercised prior to the Expiry Date.
8. The Optionholder may exercise some only of the Optionholder's options, which does not affect the Optionholder's right to exercise the remainder of their options by the deadline in paragraph 3 above. Options must be exercised in multiples of 1,000 at a time, unless the Optionholder exercises all options able to be exercised at that time.
9. Subject to the Corporations Act, the Listing Rules of ASX and the Company's constitution, the options only transferable in accordance with the provisions of the Company's Executive Share Option Plan pursuant to which the Options are issued.
10. All Shares issued upon exercise of the options will, from the date they are issued, rank pari passu in all respects with the Company's then issued Shares.
11. The Optionholder cannot participate in new issues of capital offered to shareholders of the Company (in respect to unexercised options) during the currency of the options without exercising the options. However, the Company will ensure that for the purpose of determining entitlements to any such issue, the books closing date will be at least 10 business days after the issue is announced. This will give the Optionholder the opportunity to exercise their options prior to the date for determining entitlements to participate in any such issue.
12. Subject to paragraph 9, if the Company makes a bonus share issue, a rights issue or any other similar issue of rights or entitlements, there will be no adjustment to the exercise price, the number of Shares per option or any other terms of those options.

13. In the event of any reorganisation (including consolidation, subdivision, reduction or return) of the issued capital of the Company the rights of the Optionholder, including the number of options or the exercise price of the options or both will be changed to the extent necessary to comply with the Listing Rules of the ASX applying to a reorganisation of capital at the time of the reorganisation.
14. The Optionholder will be sent all communications sent to shareholders of the Company, but options do not confer any rights to attend or vote at meetings of shareholders of the Company. Notice may be given by the Company to the Optionholder in the manner provided by the Company's constitution for the giving of notices to shareholders, and the relevant provisions of the Company's constitution apply with all necessary modification to notices to the Optionholder.



**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**ACN 010 679 633**

**31 DECEMBER 2004**

**HALF YEAR REPORT**

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Level 2  
307 Queen Street  
BRISBANE QLD 4000

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**DIRECTORS' REPORT**

Your directors present their report on the consolidated financial statements for the half-year ended 31 December 2004.

**DIRECTORS**

The following persons were directors of Koala Corporation Australia Limited during the period and up to the date of this report:

Peter Grogan	
Peter Marshall	(resigned 23 December 2004)
Richard Anthon	(resigned 23 December 2004)
David Evans	(appointed 23 December 2004)
Howard Stack	(appointed 23 December 2004)
Philip Dubois	(appointed 23 December 2004)
Andrew Davis	(appointed 23 December 2004)
Charles Ho	(appointed 23 December 2004)

**REVIEW OF OPERATIONS**

The company continues to hold patents relating to research results in medical resonance technologies. The technologies are yet to be commercialised.

The principal activity of the company during the half-year was to progress negotiations for a restructure of the company, resolve the shareholder issues facing the company and to raise further capital.

To assist with this process the company has engaged InterFinancial Limited, a Brisbane based corporate advisory and merchant banking firm with significant experience in the radiology market in Queensland. The engagement includes a small monthly retainer plus expenses and market range fees for raising capital for the Company.

Since 30 June 2004 the company has taken a number of major steps to progress the restructure. On 2 July 2004 Koala entered into a conditional agreement for the restructure of Koala and resolutions to effect the restructure were put to members and passed at the Annual General Meeting held on 23 December 2004.

The other parties to the agreement are UniQuest Pty Limited (Koala's partner in the technology assets), InterFinancial Limited (Koala's adviser on the restructure and related capital raisings) and the liquidators of Bradley Keeling Management Pty Limited and BK Hospitality Pty Limited, (Koala's two largest shareholders).

The key achievements during the period were:

- On or about 25 October 2004 Koala Corporation Australia agreed to the appointment of Dr David Evans as managing director-elect and chief executive officer.
- The company announced on 25 October 2004 that it had made substantial progress with its \$4 million capital raising.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

- On or about 25 October 2004 Koala reached preliminary agreement with Bell Potter and ABN Amro Morgans to the proposed capital raising by prospectus in 2005, subject to due diligence, market conditions and final written agreement.

Following the resolutions to effect the restructure being passed by members at the Annual General Meeting held on 23 December 2004, and prior to 31 December 2004:

- On 23 December 2004 Messrs Howard Stack and Andrew Davis and Doctors David Evans, Charles Ho and Philip Dubois were appointed Non-Executive Directors of the company. Mr Stack was appointed Chairman of the Board and Dr Evans appointed Managing Director. Messrs Anthon and Marshall resigned as directors of the company on the same day, 23 December 2004.
- Koala acquired 100% of the Intellectual Property in the Asymmetric Magnets;
- Koala acquired an option to acquire the IP in the Compact Magnets from UniQuest (who will own the Compact Magnets) by 30 June 2006 for \$6 million in cash or shares; and
- The pre-existing option agreement with UniQuest and the loan agreement with National Australia Bank Limited were wound up and discharged.

The following events have taken place since the reporting date. Many of these transactions were approved by the shareholders at the Annual General Meeting held on 23 December 2004:

- The existing share capital of the company was consolidated on a 15.4:1 basis;
- 15,000,000 shares were issued to seed capital investors at 26.667 cents per share;
- 25,000,000 shares were issued at 40 cents per share to Flux Industries Pty Ltd/UniQuest Pty Ltd as settlement of the acquisition of NMR 2 as disclosed in Note 4;
- 2,186,264 shares were bought back from shareholders at 26.667 cents per share under a share buy-back offer; and
- Koala have been granted a 'right of first look' at any research proposals or intellectual property developed by the University's Centre for Magnetic Resonance and Biomedical Engineering group in the field of MRI magnet designs for human medical imaging.

The likely developments for the company include:

- Research and development will continue at the University in this field of MRI technology under a research contract for Koala;
- Subject to possible ASX restrictions, the liquidators BKM and BKH may dispose of their holdings in Koala in stages, gives certainty on their exit from the register and maximises the effects of the company's restructure and future plans; and
- The company plans to issue a prospectus for an issue of up to 50 million ordinary shares at a minimum of 40 cents per share and re-list the company on the Australian Stock Exchange Ltd.

These are substantial steps in clearing the way to progress the planned restructuring of the Company and the reinstatement of the shares of the Company to trading on the Australian Stock Exchange Ltd.

**DIRECTORS' REPORT (continued)**

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**RESULTS OF OPERATIONS**

Results for the half-year may be summarised as follows:

	<b>2004</b>	<b>2003</b>
	<b>\$</b>	<b>\$</b>
Operating loss before income tax	(346,294)	(2,085,356)
Income tax attributable to operating loss	-	-
	<hr/>	<hr/>
Operating loss after income tax	(346,294)	(2,085,356)
	<hr/>	<hr/>

Signed this 28<sup>th</sup> day of February 2005 in accordance with a resolution of the directors

Peter Grogan  
Director

The Board of Directors  
Koala Corporation Australia Limited  
Level 2  
307 Queen Street  
BRISBANE QLD 4000

28 February 2005

Dear Board Members

**KOALA CORPORATION AUSTRALIA LIMITED**

In accordance with section 307C of the Corporations Act 2001, I am pleased to provide the following declaration of independence to the directors of Koala Corporation Australia Limited.

As lead audit partner for the review of the financial statements of Koala Corporation Australia Limited for the half-year ended 31 December 2004, I declare that to the best of my knowledge and belief, there have been no contraventions of:

- (i) the auditor independence requirements of the Corporations Act 2001 in relation to the review; and
- (ii) any applicable code of professional conduct in relation to the review.

Yours faithfully

CRANSTOUN & HUSSEIN  
Chartered Accountants

M Ayoob  
Principal

# INDEPENDENT REVIEW REPORT TO THE MEMBERS OF KOALA CORPORATION AUSTRALIA LIMITED

## Scope

### *The financial report and directors' responsibility*

The financial report comprises the directors' declaration, the condensed consolidated statements of financial performance, financial position, cash flows and notes to the financial statements for Koala Corporation Australia Limited and Controlled Entities (the consolidated entity) for the half-year ended 31 December 2004. The consolidated entity comprises both the company (Koala Corporation Australia Limited) and the entities it controlled at the end of, or during, the half-year.

The preparation of the financial report for the half-year ended 31 December 2004 is the responsibility of the directors of the company.

### *Review approach*

We conducted an independent review of the financial report in order for the company to lodge the financial report with the Australian Securities and Investments Commission. Our role was to conduct the review in accordance with Australian Auditing Standards applicable to review engagements.

This review was performed in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that the financial report is not presented fairly in accordance with the Corporations Act 2001, Accounting Standard 1029: Interim Financial Reporting and other mandatory professional reporting requirements in Australia, and the Corporations Regulations 2001, so as to present a view which is consistent with our understanding of the consolidated entity's financial position, and its performance as represented by the results of its operations and cash flows.

The review procedures performed were limited primarily to:

- inquiries of company personnel of certain internal controls, transactions and individual items; and
- analytical procedures applied to financial data.

These procedures do not provide all the evidence that would be required in an audit, thus the level of assurance provided is less than given in an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

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

## **Independence**

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

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**Statement**

Based on our review, which is not an audit, we have not become aware of any matter that causes us to believe that the half year financial report of Koala Corporation Australia Limited, set out on pages 9 to 17 is not in accordance with:

- (a) the Corporations Act 2001, including:
  - (i) giving a true and fair view of the consolidated entity's financial position as at 31 December 2004 and of its performance for the half-year ended on that date; and
  - (ii) complying with Accounting Standard AASB 1029: Interim Financial Reporting and the Corporations Regulations 2001; and
- (b) other mandatory professional reporting requirements.

**Inherent uncertainty regarding intangibles**

As detailed in Note 4 the consolidated entity has recorded intangibles of \$10,000,000 representing the fair value attributed to the intellectual property based on a director's valuation. This valuation assumes future events, which may not occur as anticipated. Accordingly, we are unable to determine whether the carrying value of this asset exceeds its recoverable amount.

CRANSTOUN & HUSSEIN  
Chartered Accountants

M AYOOB  
A Member of the Firm

Signed in Brisbane this 28<sup>th</sup> day of February 2005

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**DIRECTORS' DECLARATION**

The directors declare that the financial statements and notes set out on pages 10 to 17:

- (a) comply with Accounting Standard AASB 1029: Interim Financial Reporting and the Corporations Regulations; and
- (b) give a true and fair view of the consolidated entity's financial position as at 31 December 2004 and of its performance, as represented by the results of its operations and its cash flows, for the half-year ended on that date.

In the directors' opinion, there are reasonable grounds to believe that Koala Corporation Australia Limited will be able to pay its debts as and when they become due and payable.

Signed this 28<sup>th</sup> day of February 2005 in accordance with a resolution of the directors

Peter Grogan  
Director

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL  
PERFORMANCE  
FOR THE HALF-YEAR ENDED 31 DECEMBER 2004**

	Note	31 December 2004 \$	31 December 2003 \$
Loss from ordinary activities before income tax expense	2	(346294)	(2085356)
Income tax expense relating to ordinary activities		-	-
Net loss attributable to members of Koala Corporation Australia Limited		(346294)	(2085356)
Basic and diluted earnings per share (cents per share)	3	(0.21)	(1.26)

This condensed consolidated statement of financial performance should be read in conjunction with the accompanying notes.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS  
AT 31 DECEMBER 2004**

	Note	31 December 2004 \$	30 June 2004 \$
<b>CURRENT ASSETS</b>			
Cash assets		2,896,283	260,469
Receivables		315,446	358,240
Intangibles	4	-	22,540,677
Other		9,128	-
		-----	-----
<b>Total Current Assets</b>		3,220,857	23,159,386
		-----	-----
<b>NON-CURRENT ASSETS</b>			
Property, plant and equipment		2,139	3,095
Intangibles	4	10,000,000	-
		-----	-----
<b>Total Non-Current Assets</b>		10,002,139	3,095
		-----	-----
<b>Total Assets</b>		13,222,996	23,162,481
		-----	-----
<b>CURRENT LIABILITIES</b>			
Payables	5	13,077,307	106,874
Interest bearing liabilities	6	164,280	22,727,904
		-----	-----
<b>Total Liabilities</b>		13,241,587	22,834,778
		-----	-----
<b>Net (Liabilities) Assets</b>		(18,591)	327,703
		-----	-----
<b>SHAREHOLDERS' EQUITY</b>			
Contributed equity		32,837,591	32,837,591
Accumulated losses		(32,856,182)	(32,509,888)
		-----	-----
<b>Total Equity</b>		(18,591)	327,703
		-----	-----

This condensed consolidated statement of financial position should be read in conjunction with the accompanying notes.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS  
FOR THE HALF-YEAR ENDED 31 DECEMBER 2004**

	<b>31 December 2004</b>	<b>31 December 2003</b>
	\$	\$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from customers (inclusive of GST)	-	46,436
Payments to suppliers and employees (inclusive of GST)	(203,435)	(322,455)
Interest received	24,935	36,621
Borrowing costs	(7,166)	(5,054)
	<hr/>	<hr/>
Net cash outflow from operating activities	(185,666)	(244,452)
	<hr/>	<hr/>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Payment for property, plant and equipment	-	(2,844)
Proceeds from vendor finance facility	63,424	319,310
	<hr/>	<hr/>
Net cash inflow from investing activities	63,424	316,466
	<hr/>	<hr/>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from share application	2,781,003	-
Decrease in shareholders loans	(22,947)	(37,150)
	<hr/>	<hr/>
Net cash inflow (outflow) from financing activities	2,758,056	(37,150)
	<hr/>	<hr/>
Net increase in cash held	2,635,814	34,864
Cash at the beginning of the reporting period	260,469	369,228
	<hr/>	<hr/>
Cash at the end of the reporting period	2,896,283	404,092
	<hr/>	<hr/>

**Non-cash financing and investing activities**

Refer note 4.

This condensed consolidated statement of cash flows should be read in conjunction with the accompanying notes.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE HALF-YEAR ENDED 31 DECEMBER 2004**

**Note 1 - Basis of preparation of half-year financial report**

The half-year condensed consolidated financial statements are a general purpose financial report prepared in accordance with the requirements of Corporations Act 2001, Accounting Standard AASB 1029: Interim Financial Reporting and other mandatory professional reporting requirements.

It is recommended that this financial report be read in conjunction with the annual financial report for the year ended 30 June 2004 and any public announcements made by Koala Corporation Australia Limited and its controlled entities during and since the half-year in accordance with continuous disclosure requirements arising under the Corporations Act 2001.

The accounting policies have been consistently applied by the entities in the economic entity and are consistent with those applied in the annual report for the year ended 30 June 2004.

The half-year report does not include full disclosures of the type normally included in an annual financial report.

***Adoption of Australian Equivalents to International Financial Reporting Standards***

Australia is currently preparing for the introduction of International Financial Reporting Standards (IFRS).

The consolidated entity's management has assessed the significance of these changes and has prepared for their implementation.

The directors are of the opinion that the key differences in the consolidated entity's accounting policies which will arise from the adoption of IFRS are:

**Impairment of Assets**

The consolidated entity currently determines the recoverable amount of an asset on the basis of undiscounted net cash flows that will be received from the asset's use and subsequent disposal. In terms of AASB136: Impairment of Assets, the recoverable amount of an asset will be determined as the higher of fair value less costs to sell and value in use.

**Income Tax**

Currently, the consolidated entity adopts the liability method of tax effect accounting whereby the income tax expense is based on the accounting profit adjusted for any permanent differences. Timing differences are currently brought to account either as a provision for deferred income tax or future income tax benefit. Under AASB 112 the economic entity will be required to adopt a balance sheet approach under which temporary differences are identified for each asset and liability rather than the effects of the timing and permanent differences between taxable income and accounting profits.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE HALF-YEAR ENDED 31 DECEMBER 2004**

**Note 1 - Basis of preparation of half-year financial report**

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

Equity-based Compensation Benefits

Under AASB2: Share-based Payment, equity-based compensation to employees will be recognised as an expense in respect of the services received. This will result in a change to the current accounting policy, under which no expense is recognised for equity-based compensation.

Intangible Assets

Under AASB 138: Intangible Assets, costs associated with research must be expensed in the period in which they are incurred.

**Note 2 – Loss from ordinary activities**

	<b>31 December 2004 \$</b>	<b>31 December 2003 \$</b>
The following revenue and expense items are relevant in explaining the financial performance for the interim period:		
Borrowing costs	7,166	765,681
	_____	_____
Depreciation and amortisation	957	1,172,385
	_____	_____

**Note 3 – Earnings per share**

	<b>No. of Shares</b>	<b>No. of Shares</b>
(a) Weighted average number of ordinary shares outstanding during the period used in calculation of basic and diluted EPS (refer note 10)	165,013,804	165,013,804
	_____	_____
	<b>\$</b>	<b>\$</b>
Earnings used in the calculation of basic and diluted EPS	(346,294)	(2,085,356)
	_____	_____

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE HALF-YEAR ENDED 31 DECEMBER 2004**

	<b>31 December 2004 \$</b>	<b>30 June 2004 \$</b>
<b>Note 4 – Intangibles</b>		
Intellectual property at director’s valuation	10,000,000	22,540,677
	_____	_____
Disclosed as - current	-	22,540,677
- non-current	10,000,000	-
	_____	_____
	10,000,000	22,540,677
	_____	_____

On 24 December 2004 the consolidated entity entered into various agreements to unwind the complex arrangements in place over the magnetic resonance intellectual property.

In accordance with the Deed of Put Option dated 15 September 1999, NMR Holdings No1 Pty Ltd (NMR1), a wholly owned subsidiary of Koala Corporation Australia Limited (Koala), exercised a Put Option, at a cost of \$100, and required Flux Industries Pty Ltd (Flux) to subscribe for \$21,748,368 (the subscription amount) in shares in NMR Holdings No2 Pty Ltd (NMR2). The proceeds of the subscription amount were used to settle, in full, the debt owed to National Australia Bank Limited by NMR1. (Refer Note 6)

The result of exercising the Put Option was that NMR1 lost control of NMR2 and hence the intellectual property.

On the same date the consolidated entity entered into the “Koala Share Issuance Agreement” in which Koala acquired all the share capital in NMR2 from Flux for a purchase consideration of \$10,000,000 (reflected in payables in Note 5). This liability was settled by way of issue of 25,000,000 shares at 40 cents each on 5 January 2005. As a result NMR2 now owns 100% of the Asymmetric Magnet Technology and has an option to acquire the rights to the Compact Magnet Technology from Flux.

**KOALA CORPORATION AUSTRALIA LIMITED  
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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
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	Note	31 December 2004 \$	30 June 2004 \$
<b>Note 5 – Payables</b>			
Trade creditors and accruals		616,304	106,874
Other	4	10,000,000	-
Share application monies received		2,461,003	-
		<hr/>	<hr/>
		13,077,307	106,874
		<hr/>	<hr/>

Share application monies received represent proceeds in advance (net of share issue costs) for 10,428,750 shares which were issued on 5 January 2005.

**Note 6 – Interest bearing liabilities**

Shareholder loan (unsecured)		164,280	187,227
Bank loan (secured)	4	-	22,540,677
		<hr/>	<hr/>
		164,280	22,727,904
		<hr/>	<hr/>

**Note 7 – Dividends**

No dividends were paid or provided for during the period.

**Note 8 – Contingent liabilities**

There has been no change in contingent liabilities since the last annual reporting date.

**Note 9 – Segment information**

The consolidated entity operates in one geographical segment and one business segment being that of research in magnetic resonance technologies. The consolidated entity's operations during the period were carried out primarily in Queensland, Australia.

**KOALA CORPORATION AUSTRALIA LIMITED  
AND CONTROLLED ENTITIES**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
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**Note 10 – Events subsequent to balance date**

The following transactions have taken place since the reporting date. These transactions were approved by the shareholders at the annual general meeting held on 23 December 2004.

- The existing share capital of the company was consolidated on a 15.4:1 basis;
- 15,000,000 shares were issued to seed capital investors at 26.667 cents per share. Proceeds of this issue received prior to 31 December 2004 are disclosed in Note 5;
- 25,000,000 shares were issued at 40 cents per share to Flux Industries Pty Ltd as settlement of the acquisition of NMR 2 as disclosed in Note 4; and
- 2,186,264 shares were bought back from shareholders at 26.667 cents per share under a share buy-back offer.

As a result the number of shares on issue is as follows: -

	<b>Shares on Issue</b>
Balance at 31 December 2004	165,013,804
Share capital consolidation	(154,298,590)
Issue to seed investors	15,000,000
Issue to Flux Industries Pty Ltd	25,000,000
Shares bought under share buy-back offer	(2,186,264)
	<hr/>
Balance at 28 February 2005	48,528,950
	<hr/>