

**COMPUMEDICS LIMITED**  
**ACN 006 854 897**

**NOTICE OF GENERAL MEETING**  
**PROXY FORM**  
**AND**  
**EXPLANATORY MEMORANDUM**

**Date of Meeting**  
Tuesday, 28 November 2006

**Time of Meeting**  
10.30 am

**Place of Meeting**  
30-40 Flockhart Street, Abbotsford Victoria 3067

**COMPUMEDICS LIMITED**  
**ACN 006 854 897**

**NOTICE OF ANNUAL GENERAL MEETING**

**NOTICE** is given that the Annual General Meeting of Compumedics Limited (ACN 006 854 897) ("**the Company**") will be held at 30-40 Flockhart Street, Abbotsford Victoria 3067 Australia on Tuesday 28 November, 2006 at 10.30am.

The accompanying Explanatory Memorandum ("Explanatory Memorandum") provides additional information relating to the matters to be considered at the Annual General Meeting and forms part of this Notice of Annual General Meeting ("Notice"). Certain terms and abbreviations used in this Notice and the Explanatory Memorandum have defined meanings, which are explained in the Explanatory Memorandum.

**Business**

**1. Financial Statements and Reports**

To receive and consider the financial report of the Company and the reports of the Directors and the Company's auditor for the year ended 30 June 2006.

**2. Election of Professor Graham Mitchell as Director**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

"That Professor Graham Mitchell, who retires by rotation, be re-elected as a director of the Company."

**3. Adoption of Remuneration Report**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

"That the section of the report of the Directors entitled "Directors' Remuneration" dealing with the remuneration of the Company's Directors be adopted".

Under s 250R(3) of the Corporations Act, the vote on this item is advisory only and does not bind the Directors or the Company.

**4. Options issued to Director, Mr Bruce Rathie**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

"That for the purposes of Listing Rule 10.11, Chapter 2E of the Corporations Act and all other purposes, the Shareholders approve the issue of 20,000 Options to Mr Bruce Rathie, on the terms outlined in the Explanatory Memorandum."

Note: if approval is given under Listing Rule 10.11, approval is not required under Listing Rule 7.1.

**5. Redeemable Convertible Notes issued to D & DJ Burton Holdings Pty Ltd**

To consider and, if thought fit, pass the following resolutions as ordinary resolutions:

- (a) "That for the purposes of Listing Rule 10.11 and all other relevant purposes, the Shareholders approve the Redeemable Convertible Notes Agreement made between the

Company and D & DJ Burton Holdings Pty Ltd, being the agreement described in the Explanatory Memorandum."

- (b) "That for the purposes of Listing Rule 10.11, section 611 and Chapter 2E of the Corporations Act and all other relevant purposes, the Board be authorised to issue to D & DJ Burton Holdings Pty Ltd ordinary shares of the Company in accordance with the terms of the Redeemable Convertible Notes Agreement. As described in the Explanatory Memorandum, such terms provide for an interest rate of 20% per annum on the Redeemable Convertible Notes from the day of issue to the earlier of the date of conversion or the date of redemption."

Note: if approval is given under Listing Rule 10.11, approval is not required under Listing Rule 7.1.

BY ORDER OF THE BOARD

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**David Lawson, Secretary**  
**23 October, 2006**

## **VOTING AND PROXIES**

### *Eligibility*

You will be eligible to vote at the meeting if you are registered as a holder of shares of the Company at 5pm Melbourne time on 26 November 2006.

### *Appointing a proxy*

If you are entitled to attend and vote at the meeting, you can appoint a proxy to attend and vote on your behalf. A proxy need not be a Shareholder of the Company and may be an individual or a body corporate.

If you are a Shareholder, and you are unable or do not wish to attend and vote at the meeting, and you wish to appoint a proxy, please complete and return the enclosed proxy form. If you are entitled to cast two or more votes, you may appoint two proxies and specify the proportion or number of votes each proxy is appointed to exercise. If you do not specify a proportion or number, each proxy may exercise half of the votes. If you require a second proxy form, please contact the Company on (03) 8420 7300.

### *Lodging your proxy form*

You can lodge your proxy form by:

- Mailing it to the Company at 30-40 Flockhart Street, Abbotsford Victoria 3067
- Faxing it to the Company on (03) 8420 7399 or to + 61 3 8420 7399 (from outside Australia)
- Hand delivering it to the Company at 30-40 Flockhart Street, Abbotsford Victoria 3067

Your completed proxy form (and any necessary supporting documentation) must be received by the Company no later than 10.30am on 26 November 2006.

If the proxy form is signed by an attorney, the original power of attorney under which the proxy form was signed (or a certified copy) must also be received by the Company by 10.30am on 26 November 2006 unless it has been previously provided to the Company. If the proxy is signed under power of attorney, the signatory must also declare that they have had no notice of revocation of the power of attorney.

If you appoint a proxy, you may still attend the meeting. However, if you vote on a resolution your proxy is not entitled to also vote on that resolution.

### *Voting at the meeting*

At the meeting, on a show of hands each Shareholder present may cast one vote. For these purposes a Shareholder being 'present' includes a person present as a proxy, attorney or body corporate representative.

The Chair of the meeting will vote any undirected proxies in favour of all of the resolutions unless he or she has a personal interest in the relevant resolution. The Company encourages all Shareholders who submit proxies to direct their proxy how to vote on each resolution.

### **Voting exclusion statement**

The Company will disregard any vote cast:

- (a) on Resolution 4 by Mr Bruce Rathie or any of his associates;
- (b) on Resolutions 5(a) and 5(b) by D & DJ Burton Holdings Pty Ltd or any of its associates,

unless the vote is cast by:

- a person as a proxy for a person who is entitled to vote, in accordance with the directions in the proxy form; or
- the Chair of the meeting as proxy for a person who is entitled to vote, in accordance with the directions in the proxy form.

## **EXPLANATORY MEMORANDUM**

### **Defined Terms**

The following terms, which are used in this Notice (including this Explanatory Memorandum), have the meanings set out below:

'ASX' means Australian Stock Exchange Limited ABN 98 008 624 691;

'Board' means the board of directors of the Company;

'Company' means Compumedics Limited ACN 006 854 897;

'Corporations Act' means the Corporations Act (Cth) 2001;

'Listing Rules' means the Listing Rules of the ASX;

'RCNs' means the Redeemable Convertible Notes issued to D & DJ Burton Holdings Pty Ltd under the RCN Agreement with an issue date of 15 March 2006;

'RCN Agreement' means the Redeemable Convertible Notes Agreement made between the Company and D & DJ Burton Holdings Pty Ltd pursuant to which the Company issued the RCNs to D & DJ Burton Holdings Pty Ltd; and

'Shareholder' means a person who is registered as a holder of shares of the Company.

### **Item 1:**

#### **Financial Statements and Reports**

During this item there will be an opportunity for Shareholders at the meeting to ask questions and comment on the Director's Report, Financial Statements and Independent Audit Report for the financial year ended 30 June 2006. No resolution will be required to be passed on this matter.

### **Item 2:**

#### **Re-election of Professor Graham Mitchell as Director**

Professor Mitchell retires by rotation in accordance with the Constitution and being eligible offers himself for re-election.

A brief summary of Professor Mitchell's experience and qualifications appears below.

#### *Professor Graham Mitchell*

Professor Graham Mitchell is one of the 3 non-executive directors on the Board of the Company. He was first elected as a director in December 2000. He is recognized as one of Australia's leading biological scientists. His expertise extends over a wide range of science and technology fields. He has a detailed knowledge of the academia and industry interface, has authored more than 350 publications, and received numerous awards for scientific achievement. In 1993, he was appointed an Officer of the Order of Australia for services to science, in particular immunoparasitology. Professor Mitchell is a principal of Foursight Associates Pty Ltd and non-executive director of Antisense Therapeutics Limited, the Geoffrey Gardner Dairy Foundation and AVS Pty Ltd. He acts as a principal adviser to the Victorian Government through the Council for Knowledge, Innovation, Science and Engineering. He is joint Chief Scientist for the Department of Primary Industries. He is also a member of the World Health Organisation committee for special programs in tropical diseases.

### *Recommendation*

The Directors, other than Professor Graham Mitchell, unanimously support the re-election of Professor Graham Mitchell.

#### **Item 3:**

##### **Adoption of Remuneration Report**

The Corporations Act requires that the section of the Directors' report relating to director and executive remuneration (the "Remuneration Report") be put to a vote of Shareholders for its adoption. The vote is advisory only and does not bind the directors of the Company.

The Remuneration Report can be found at pages 32 to 38 of the Financial Statements in the Company's 2006 Annual Report. Following consideration of the Remuneration Report, Shareholders will be given a reasonable opportunity to ask questions or comment on the Remuneration Report.

#### **Item 4:**

##### **Options for Mr Bruce Rathie, Director**

The information relating to this Item is intended to meet the legal requirements imposed on the Company to provide sufficient information to Shareholders to allow them to properly consider and make an informed decision concerning the resolution seeking approval of the issue of options to Mr Bruce Rathie, who is a director of the Company. The approval is sought for the purposes of:

- (a) Chapter 2E of the Corporations Act, dealing with the provision of financial benefits to related parties; and
- (b) Listing Rule 10.11, dealing with the issue of securities and the issue of securities to related parties respectively. If approval for the issue of the options to Mr Rathie is obtained under Listing Rule 10.11 it is not required under Listing Rule 7.1.

### *Introduction*

Mr Bruce Rathie was elected to the Board in 2004 as a non-executive director. Subject to approval by the Shareholders, the Company agreed to issue Mr Rathie 20,000 options on the following terms:

- (a) the grant date for the options will be the date of the meeting at which the Shareholders approve the grant of the options ("Grant Date");
- (b) each option grants Mr Rathie a right to acquire one ordinary share in the capital of the Company and hence the maximum number of shares that may be issued to Mr Rathie pursuant to the options is 20,000;
- (c) the right to exercise the options is staggered over a three year period. On the first anniversary of the Grant Date, which will be 28 November 2007 if Shareholders approve the issue, Mr Rathie will have the right to exercise 20% of the options (4000 options); on the second anniversary of the Grant Date, which will be 28 November 2008 if Shareholders approve the issue, Mr Rathie will have the right to exercise 30% of the Options (6000 options); on the third anniversary of the Grant Date, which will be 28 November 2009 if Shareholders approve the issue, Mr Rathie will have the right to exercise the remaining 50% of the options (10,000 options);
- (d) subject to the above, the options must be exercised within 5 years of the Grant Date; and
- (e) the exercise price for each option is the average price for Shares in the 5 days prior to 21 October 2004. This average price was 35.1 cents.

The purpose of the issue of the options to Mr Rathie is to provide an incentive to him for future services and a reward for past services. The issue of options as part of the remuneration offered to non-Executive Directors is an established practice of listed public companies.

### *Potential benefits*

If the options are issued to Mr Rathie pursuant to Resolution 4, the Board considers the following benefits will arise:

- (a) Mr Rathie will have an interest in the affairs of the Company as the holder of the options and as shareholder upon exercise of the options;
- (b) the options are a non-cash form of remuneration, thus conserving the cash reserves of the Company while providing an incentive for future performance and a reward for past services;
- (c) exercise of the options will provide working capital for the Company.

### *Potential costs*

If the options are exercised at a time when the market price of the Company's shares is greater than the exercise price of the options, there will be a detriment insofar as the Company will be required to issue shares at a price lower than it might otherwise have been able to, with the result that less funds will be raised.

In this regard, the price of the Company's shares quoted on the ASX in the 12 month period from 23 October 2005 to 23 October 2006 has ranged from between 7 cents per share (lowest price reached 11 May 2006) to 22.5 cents per share (highest price reached 25 October 2005). The share price at close of trading on 23 October 2006 was 11 cents per share.

As there are currently 140 million issued shares in the Company, the Board considers that the potential detrimental effect on the Company as a result of the issue of the options to Mr Rathie is negligible. If all the options are exercised, then assuming no further shares are issued during the relevant period, the number of issued shares in the Company will increase to 140,020,000.

### *Valuation of the options*

The options to be granted to Mr Rathie after approval by Shareholders are not traded on the ASX and as such have no market value. Each option grants the holder the right to obtain one ordinary share in the Company upon exercise of the option and payment of the exercise price of the option. Accordingly, the options may have a present value at the date of their grant. The options may acquire future value depending upon the extent to which the share prices(s) exceed the exercise price during the term of the options.

Various factors will affect the value of the options including:

- the period outstanding before the expiry date of the options;
- the exercise price of the options relative to the underlying price or value of the shares into which they may be converted;
- the proportion of the issued capital as expanded upon exercise of the options;
- the value of the shares into which the options may be converted; and
- whether or not the options are listed (and therefore capable of being sold).

There are various formulae which can be applied to value options. The Board has estimated the value of the options using the Black-Scholes Model option valuation formula, which is probably the most widely used and recognised model for pricing options. The value of an option calculated under the Black-Scholes Model is a function of the relationship between a number of variables, being the share price, the exercise price, the time to expiry, the risk-free interest rate and the volatility of the Company's underlying share price.

To apply the Black-Scholes Model, it is necessary to assume certain inputs. The data relied upon in applying the Black-Scholes Model to the options were as follows:

- (a) an exercise price of 35.1 cents per option;
- (b) the period of time prior to conversion being 5 years (28 November 2006 to 28 November 2011). For this purpose it was assumed that none of the options would be exercised earlier than the expiration date of the options (28 November 2011) however it is noted in this respect that the options may be exercised earlier than this date (see above);
- (c) the Company has not forecast any future dividend payments. For the purpose of the analysis, it was assumed that the Company's share price is "ex-dividend";
- (d) the risk free rate used for the purposes of the analysis was the rate on current Treasury Bond yields with a maturity date approximating the expiry date of the options being 5.92%;
- (e) a volatility measure of 39%. This volatility factor was based on the variations in the share price of the Company's share in the two year period ended 23 October 2006;
- (f) the value of the Company's share price at 23 October 2006 which was 11 cents per share.

Using the Black-Scholes Model and the assumed data outlined above, the Board has valued the options as at 23 October 2006 at 2 cents each. As 20,000 options are proposed to be issued to Mr Rathie, then assuming this value is correct, the options granted to Mr Rathie will have a value of \$400.00.

The Board draws Shareholders attention to the fact that the stated valuation does not constitute and should not be taken as audited financial information.

#### *Identifying the Related party*

The related party to whom Resolution 4 would permit financial benefits to be given is Bruce Rathie, a director of the Company.

#### *Financial benefit*

The nature of the financial benefit is the grant of the 20,000 options to Mr Rathie for no consideration.

#### *Related party's existing interest and possible consequence of issuing options*

Excluding the options, neither Mr Rathie nor his associates have any interests in the securities of the Company.

If all of the options are exercised, Mr Rathie will obtain 20,000 ordinary shares in the capital of the Company at a cost of \$7020.

#### *Current emoluments*

Mr Rathie's current remuneration from the Company is \$35,000 per annum in director's fees.

#### *Taxation consequences*

The taxation consequences of the issue of the options are not considered to be material to the Company.

#### *Recommendation*

The Directors, other than Mr Bruce Rathie, recommend that Shareholders approve the resolution. They believe that the issue of the options is fair and reasonable having regard to their terms. No director, other than Mr Rathie, has an interest in the outcome of Resolution 4.

Other than the information above and otherwise set out in this Explanatory Memorandum, the Directors believe that there is no other information known to the Company or its Directors that will be reasonably required by Shareholders to make a decision in relation to Resolution 4.



**Item 5:****Redeemable Convertible Notes issued to D & DJ Burton Holdings Pty Ltd**

The information relating to this Item is intended to meet the legal requirements imposed on the Company to provide sufficient information to Shareholders to allow them to properly consider and make informed decisions on Resolution 5(a) and 5(b) for the purposes of (as required):

- (c) Chapter 2E of the Corporations Act, dealing with the provision of financial benefits to related parties;
- (d) Listing Rule 10.11, dealing with the issue of securities to related parties; and
- (e) Section 611 of the Corporations Act, dealing with takeover approvals.

*Introduction*

During the financial year ended 30 June 2006, and continuing into the current financial year, the Company's financial success has depended on the contribution of additional financial resources by its major shareholder, D & DJ Burton Holdings Pty Ltd.

In the period ended 30 June 2006, D & DJ Burton Holdings Pty Ltd agreed to advance A\$1m cash to the Company. In consideration for the agreement to advance the cash, the Company issued Redeemable Convertible Notes ("RCNs") to D & DJ Burton Holdings Pty Ltd under a Redeemable Convertible Notes Agreement ("RCN Agreement") whose terms can be summarised as follows:

1. The A\$1m was payable by D & DJ Burton Holdings Pty Ltd ( in the following numbered paragraphs, "Noteholder") within 30 days of the issue date of the RCNs which was 15 March 2006. The terms of the RCN issue were subsequently amended to allow 45 days from the issue date for the money to be paid. The \$1m was paid within this time frame and has been used as working capital by the Company.
2. 1000 RCNs were issued with a face value of A\$1000 each.
3. The term of the RCNs is 2 years from the issue date. All or some of the RCNs are convertible into ordinary shares of the company on the 1<sup>st</sup> or 2<sup>nd</sup> anniversary of the issue date, being 15 March 2007 and 15 March 2008 respectively.
4. The conversion of the RCNs to ordinary shares is at the discretion of the Noteholder. However, all issues of shares to the Noteholder pursuant to the RCN Agreement must be approved by the Shareholders in general meeting in accordance with the Listing Rules and the Corporations Act.
5. If the Shareholders approve the conversion of the RCNs to shares, the rate of interest payable on the face value of the RCNs is 20% per annum. However, if the conversion of the RCNs into shares is not approved by shareholders, the face value of the RCNs is immediately repayable on request by the Noteholder and the rate of interest payable on the face value of the RCNs is 14.5% per annum.
6. The conversion factor to be used if the Noteholder elects to convert the RCNs into ordinary shares of the Company and the conversion is approved in general meeting is the average price for the Company's Shares 5 days immediately prior to the date of issue of the RCNs which has been calculated to be 8.2 cents per share. The Company's shares have traded as low as 6 cents since the issue of the RCNs. By way of comparison, the closing price for the ordinary shares in the Company on 23 October 2006 was 11 cents.
7. If conversion is approved by Shareholders but no conversion occurs, the Noteholder may redeem the face value of the RCNs for cash, plus receive interest at the rate of 20 per cent per annum calculated on the face value of the RCNs for the relevant period.

With the exception of David Burton, who was an associate of the related party advancing the funds, the Board unanimously agreed to the terms of the RCN Agreement in the belief that it was, taken as a whole, in the best interests of the Company having regard to the then financial position of the Company.

Before entering into the RCN Agreement, the Directors sought alternate arm's-length financing options that might have been available to the Company and the terms upon which such finance might be made available. Alternative sources of finance were not generally available within the extremely short time-frame in which cash was needed. The Directors considered, having regard to that information and other relevant market information generally available, that the terms of the RCN Agreement were appropriate.

As a consequence of the RCN Agreement, D & DJ Burton Holdings Pty Ltd advanced \$1m cash into the Company at short notice at a time of critical importance to the Company's prospects. Had those funds not been provided, the Company's operations may have been severely impacted

The Board seeks Shareholder approval of the RCN Agreement and approval for the issue of ordinary shares to D & DJ Burton Holdings Pty Ltd pursuant to the terms of the RCN Agreement if D & DJ Burton Holdings Pty Ltd seeks to convert all or any of its RCNs to ordinary shares in accordance with the terms of the RCN Agreement.

#### *The related party and its interests*

D & DJ Burton Holdings Pty Ltd is the major Shareholder of the Company. It currently holds 87,761,608 ordinary shares in the capital of the Company which represents 62.69% of the issued ordinary shares in the Company. As the major Shareholder of the Company, D & DJ Burton Holdings Pty Ltd is a related party to the Company. A further 2,041,500 shares are owned by Electro Molecular Pty Ltd, a company owned and controlled by David Burton. Accordingly, D & DJ Burton Holdings Pty Ltd and its associates hold 89,803,108 ordinary shares in the Company, which represent 64.15% of the issued ordinary shares of the Company.

Because D & DJ Burton Holdings Pty Ltd is a related party, neither it nor its associates may vote on the relevant resolutions. The associates of D & DJ Burton Holdings Pty Ltd include Mr David Burton, the Chairman and Chief Executive Officer of the Company, his wife, and Electro Molecular Pty Ltd.

#### *Financial benefit to related party*

The financial benefit provided to the related party D & DJ Burton Holdings Pty Ltd consists of the rights granted to it under the RCN Agreement. These rights principally comprise:

- (a) the right to have the sum advanced by it repaid, together with interest at the rates described above; and
- (b) subject to Shareholder approval, the rights to convert the RCNs to ordinary shares in the Company in the manner specified.

#### *Consequences of approval of RCN Agreement and conversion*

If Shareholders pass Resolutions 5(a) and 5(b) then:

1. If D & DJ Burton Holdings Pty Ltd seeks to convert its RCNs, the Company shall issue to it ordinary shares in Company in accordance with the formula set out in the RCN Agreement.
2. The formula in the RCN Agreement entitles D & DJ Burton Holdings Pty Ltd to obtain:
  - (a) 12,195,121 ordinary shares in respect of (in effect) the advance of \$1m (representing the face value of the RCNs); and
  - (b) 2,439,024 ordinary shares in respect of interest payable on the RCNs if all RCNs are converted on 15 March 2007 (the interest being calculated at 20% per annum for one year) or alternatively 5,365,853 ordinary shares if all RCNs are converted on 15 March 2008 (the interest being calculated at 20% per annum with interest payable annually).
3. If conversion of all the RCNs becomes effective at 15 March 2008, D & DJ Burton Holdings Pty Ltd would therefore receive its maximum number of new shares being a further 17,560,974 ordinary shares. If this occurred, D & DJ Burton Holdings Pty Ltd and

its associates would increase their shareholdings to 107,364,082 ordinary shares. On this basis, assuming no further shares were issued in the Company, D & DJ Burton Holdings Pty Ltd and its associates would hold 107,364,082 ordinary shares out of a total issued 157,560,974 ordinary shares. This would represent 68.14% of issued shares. Accordingly, the maximum increase in the percentage of issued shares in the Company held by D & DJ Burton Holdings Pty Ltd as a result of passing resolutions 5(a) and 5(b) is 3.99%.

#### *Consequences of non-approval of RCN Agreement and conversion*

If Shareholders do not pass both Resolutions 5(a) and 5(b) and consequently no conversion occurs, then D & DJ Burton Holdings Pty Ltd would be entitled to repayment of the face value of the RCNs immediately together with interest calculated at the rate of 14.5% per annum from the issue date up to the date of redemption. Hence if redemption of the RCNs occurs on 15 March 2007, an amount of \$1,145,000 will be payable by the Company. If redemption occurs on 15 March 2008, an amount of \$1,311,025 will be payable by the Company.

#### *Valuation of the conversion rights*

As noted above, the approval of the conversion will give D & DJ Burton Holdings Pty Ltd the right to convert its debt (at the relevant conversion date) into:

- (a) a further 14,634,145 ordinary shares if conversion of all the relevant debt occurs on 15 March 2007; or
- (b) a further 17,560,974 ordinary shares if conversion of all the relevant debt occurs on 15 March 2008.

The conversion rights to be obtained by the Noteholder on approval by Shareholders are not traded on the ASX and as such have no market value. However, the Noteholder will have a right to acquire shares (up to the maximum number specified above) at the exercise price of 8.2 cents per share and accordingly the conversion rights will have a present value at the date they are approved. The rights may acquire future value depending upon the extent to which the share prices(s) exceed the exercise price during the term in which conversion may occur.

Various factors will affect the value of conversion rights including:

- the period during which the conversion rights may be exercised;
- the exercise price at which the relevant debt may be converted to equity;
- the proportion of the issued capital as expanded upon exercise of the conversion rights;
- the value of the shares into which the debt may be converted;
- whether or not the rights in question are listed (and therefore capable of being sold), and;
- the ability of the Noteholder to sell the ordinary shares in the Company post conversion.

There are various formulae which can be applied to value conversion rights. The Board has estimated the value of the conversion rights using the Black-Scholes Model formula for valuing options (see above). This basis was used because, once the conversion rights are obtained, the Noteholder will be in some respects in a similar economic position to a holder of options over shares in the Company. To apply the Black-Scholes Model, it is necessary to assume certain inputs. The data relied upon in applying the Black-Scholes Model to the options were as follows:

- (a) an exercise price on conversion is 8.2 cents per share;
- (b) the period of time up to conversion being respectively 105 days (from the date of approval until 15 March 2007) or 470 days (from the date of approval until 15 March 2008);
- (c) the Company has not forecast any future dividend payments. For the purpose of the analysis, it was assumed that the Company's share price is "ex-dividend";

- (d) the risk free rate used for the purposes of the analysis was the rate on current Treasury Bond yields with a maturity date approximating the expiry date of the options being 5.92%;
- (e) a volatility measure of 39%. This volatility factor was based on the variations in the share price of the Company's share in the two year period ended 23 October 2006;
- (f) the Company's share price based on a range of values namely:
  - i. the Company's share price at 23 October 2006 which was 11 cents per share;
  - ii. an average share price value over the 12 month period ended 23 October 2006 namely 11.3 cents per share;
  - iii. a share price of 16 cents at each of the relevant conversion dates;
  - iv. a share price of 25 cents at each of the relevant conversion dates.

Based on this valuation method and the assumed data outlined above, the Board has valued the conversion rights as at 23 October 2006 by providing a range of values depending primarily on the assumptions referred to above and in particular the assumptions relating to the value of the Company's shares.

Implicit in the range of values below is the ability of the Noteholder to trade the quantity of ordinary shares in the Company that the Noteholder would be entitled to at March 2007 and/or March 2008, without unduly effecting the then share price of those ordinary shares. Given that the average daily volume of ordinary shares in the Company traded on the Australian Stock Exchange over the last 12 months was approximately 90,000 ordinary shares in the Company per day it would take the Noteholder in excess of 160 or 200 trading days respectively to sell either 14,634,145 ordinary shares in the Company post March 2007 or 17,560,974 ordinary shares in the Company post March 2008. In both scenarios the Noteholder is only entitled, pursuant to the Company's security trading policy, to trade ordinary shares in the Company up to a maximum of 60 trading days per year unless the Board agree to any additional trading period. Given the uncertainty in predicting the likelihood of the Noteholder to be able to sell the ordinary shares in the Company that it will be entitled to either on market or in any approved off-market transaction and to do so without effecting the share price at that time, the board has not discounted the valuations given below to reflect this uncertainty:

Conversion assumed 15 March 2007	Share price assumed on conversion				
	11 cents per share	11.3 cents per share (average share price)	16 cents per share	25 cents per share	
Value of conversion right based on valuation method	\$468,000	\$498,000	\$1,171,000	\$2,487,000	

Conversion assumed 15 March 2008	Share price assumed on conversion				
	11 cents per share	11.3 cents per share (average share price)	16 cents per share	25 cents per share	
Value of conversion right based on valuation method	\$632,000	\$667,000	\$1,458,000	\$3,020,000	

### *Recommendation*

The Board, other than Mr Burton, unanimously recommends that the Shareholders pass the resolutions proposed relating to the RCNs for the following reasons:

- 1 The Board, other than Mr Burton, unanimously agreed to the terms of the RCN Agreement in the belief that it was in the best interests of the Company. The result of entry into the RCN Agreement was that \$1m of capital was injected into the Company at a critical juncture.
- 2 If both relevant resolutions are not passed, D & DJ Burton Holdings Pty Ltd may redeem the RCNs at face value plus accrued interest at any point in time following the failure to pass the resolutions. Should the Noteholder elect to withdraw its funds from the Company, this would reduce the working capital of the Company by over \$1million. This would severely impact the Company's working capital at a time when the Company's business is beginning to demonstrate improved operating performance.
- 3 When announcing the Preliminary Final Results of the Company to the ASX on 11 September 2006, the Company indicated that the current estimates of future cash flow forecasts of the business allowed for the repayment of the RCNs should convertibility of the RCNs into ordinary equity in the Company not be approved by shareholders. In the situation where the approval to convert the RCNs to ordinary equity of the Company is not achieved (or the Noteholder seeks to exercise its right not to convert the RCNs to ordinary equity) and the current cash flows of the business at that time do not allow for the repayment of the principal and interest of the RCNs, the non-executive directors will enter into good faith discussions/negotiations with the Noteholder on a "best efforts" basis to retain the RCN funds in the Company to minimise the impact on the cash flow of the business. Shareholders should be aware that the outcome of such negotiations is not guaranteed.
- 4 If the resolutions are passed and D & DJ Burton Holdings Pty Ltd converts its debt to equity, the Balance Sheet of the Company will in the view of the Board be substantially improved by the removal of the relevant debt from the Company's Balance Sheet. At 30 June 2006 the \$1m received pursuant to the RCN was classified as current borrowings. If the resolution allowing convertibility is approved and the RCN holder elects to convert the RCNs to ordinary shares in the Company the RCNs classified as current borrowings will be re-classified as contributed equity at that point in time.

Mr Burton is an associate of D & DJ Burton Holdings Pty Ltd and therefore has an interest in the outcome of the resolution.

Other than the information above and otherwise set out in this Explanatory Memorandum, the Directors believe that there is no other information known to the Company or its Directors that will be reasonably required by Shareholders to make a decision in relation to the benefits contemplated by Resolutions 5(a) and 5(b).