



**Advanced
Magnesium**
Limited

25 August 2006

Company Announcements Office
Australian Stock Exchange Limited
Level 4, 20 Bridge Street
SYDNEY NSW 2000

Dear Sirs,

RE: AML RESULTS

Please find attached an announcement package in relation to AML's results for the year ended 30 June 2006:

- **2006 Review of Operations**
- **Appendix 4E – Preliminary Final Report**
- **Corporate Governance Statement & Directors' Report**
- **Audited Financial Statements**

Yours sincerely,

P.K. Nair
COMPANY SECRETARY



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ASX ANNOUNCEMENT - 25 August 2006

2006 Review of Operations

Advanced Magnesium Limited, through its wholly owned subsidiary, Advanced Magnesium Technologies (AMT), has undertaken a wide range of commercialisation activities, particularly for its AM-lite[®] alloy, over the past twelve months. The purpose of this campaign was to maximise the exposure of AM-lite[®] to potential customers as a cost effective replacement for existing materials used in the die casting industry.

This report marks the first anniversary of the inception of AMT's international marketing campaign for AM-lite. While the overwhelming focus of the Company's efforts has been the development of markets for AM-lite[®], there has also been considerable activity supporting the market entry of other products.

Activities Undertaken

- AMT's international marketing team has given detailed technical presentations on AM-lite[®] to over 150 major Original Equipment Manufacturers (OEMs), Tier One suppliers and diecasters; and 42 production trials of the alloy have been completed with diecasters.
- The Company has concentrated its marketing activities for AM-lite[®] in four market sectors: hardware; electronics; motorcycles; and automotive. Some applications require extended development and testing periods before they achieve production-ready status. Others, particularly in the hardware and sanitary ware sectors, are expected to go into production more rapidly.
- The Company has received expressions of interest from many more diecasters wishing to conduct trials. The results of trials have confirmed the outstanding properties and cost advantages achievable from AM-lite[®], but before OEMs will release new parts made from AM-lite[®] for commercial production, they need to ensure that any new product can meet certain minimum property and performance criteria, including surface coating.
- The Company is working with its alliance partner, MacDermid Inc, to install MacDermid's new Bondal[®] Mg electroplating technology that has been specially developed for AM-lite[®], in existing commercial production facilities. The aim is to have two electroplating facilities operating in each of the three major regions of Europe, North America and Asia by the end of 2006.

A number of diecasting trials have led to more focussed product development programs with a number of large key end-users seeking to qualify new parts for commercial production.

As a result of this work, Management and the Board confirm that the Company expects to be able to successfully commercialise AM-lite[®] and its wider suite of proprietary magnesium alloys and metal handling technologies.

Marketing Plan to Focus on Selected customers

Whereas the initial phase of the marketing plan was to give a wide exposure of AM-lite[®] to as many potential customers as possible, the Company has decided it is now appropriate to focus its resources on a select number of high quality customers with a large initial sales potential and who have demonstrated a willingness to include AM-lite[®] in their near term production plans.

ASX ANNOUNCEMENT

- The criteria used to select these key customers include their:
 - (a) technical capabilities;
 - (b) engagement in installation of new equipment (if required) and technologies;
 - (c) eagerness to put new AM-lite[®] diecasting capacity in place; and
 - (d) strategic importance for the growth of AM-lite sales in a particular manufacturing sector

Successful sales into these customers will remove production uncertainty for other customers who have expressed interest, but do not wish to be the initial users of the product. The focussed sales plan is intended to underpin the future growth of the AM-lite[®] business.

- Detailed programs of work are currently being finalised with the selected customers with the aim of bringing a number of new products to the market before the end of calendar year 2006.
- By focussing on these selected customers and concentrating internal resources, the Company expects to be able to reduce the sales tonnage required for breakeven and maintain cash reserves at higher levels for a longer period.

The operating costs over the next 12 months and are not expected to change significantly from 2006.

Company's 2006 Financial Position & Performance

- The company has a debt free balance sheet;
- As at 30 June, 2006 cash reserves were \$12.1 million.
- Cash operating costs for the 12 month period just ended were \$7.8 million.
- The Company's consolidated loss for the year was \$0.4 million.

Way Forward

- Progress has been made in each of the hardware, sanitary ware, electronics, motor cycle and automotive sectors. Diecasters in Asia, North America and Europe are at various stages in their development programs to use AM-lite[®] either as a replacement material for the current benchmark magnesium alloy AZ91, or as a replacement for zinc, aluminium or plastic. AM-lite[®] offers significant cost, performance and weight advantages over these other materials in key applications.
- A Memorandum of Understanding that provides a commercial framework for ongoing development work has recently been agreed with a major electronics manufacturer in Asia. Further MoUs are currently under negotiation with the Company's key customers and AMT expects to be able to make announcements of significant sales tonnage in the coming months.
- The Company expects orders from these and new customers to continue to grow. Then once product development programs are successfully implemented an annualised total AM-lite[®] sales of around 5,000 tonnes by June 2007 is forecast.

APPENDIX 4E

Preliminary Final Report For the financial year ended 30 June 2006

Advanced Magnesium Limited
ABN 51 010 441 666

Current reporting period: 30 June 2006
Previous corresponding period: 30 June 2005

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This Preliminary Final Report is provided to the Australian Stock Exchange under ASX Listing Rule 4.3A

Results for announcement to the market

Revenue and net profit

		Percentage change		Amount \$
Revenue from ordinary activities	Up	325.32%	to	363,140
Loss from ordinary activities after tax attributable to members	Up	N/A % (a)	to	(426,459)
Net loss for the period attributable to members	Up	N/A % (a)	to	(426,459)

(a) The percentage change in loss from ordinary activities after tax and net loss for the period attributable to members cannot be calculated as the results have changed from a net profit of \$55,999 in the previous year to a net loss of \$426,459 in the current year.

Dividends

		Amount per security	Franked amount per security
Final dividend		Nil	Nil
Previous corresponding period		Nil	Nil
Record date		n/a	

Commentary on results for the year

<p>Revenue</p> <p>The Company has embarked on its Advanced Magnesium Technology business and essentially focussed on taking the AM-lite product through to the commercialisation phase. A significant number of customer trials have occurred, a pre-cursor for commercial sales.</p> <p>Sales revenue from the Advanced Magnesium Technologies operations continues to grow, albeit slowly, with sales of six AM-converters during the year and initial sales of its flagship AM-lite product.</p>
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Commentary on results for the year (cont'd)

Results

The overall loss for the year is a result of continuing operating expenditure on the Advanced Magnesium Technologies business, offset by specific non-recurring credits. Two significant credits include the reversal of a licence payable in relation to the terminated Stanwell Project for \$4.8m and the cash received from Magtrust Pty Ltd on its sale of Advanced Magnesium Limited shares in October 2005 of \$2.1m.

Operating expenditure of \$3.0m on the Advanced Magnesium Technologies business was supported by \$1.5m of research and development costs and \$1.1m of marketing and promotional expenditure. Other operating overhead and corporate infrastructure costs were \$2.1m.

The balance sheet of Advanced Magnesium Limited now relates solely to its Advanced Magnesium Technologies operating business. No significant impacts from terminated or sold divisions are expected on the income statement after this financial year.

Net tangible assets per share

Net tangible assets per ordinary share at 30 June 2006 are 14.77 cents (30 June 2005: 6.18 cents). These numbers are adjusted for the 1 for 20 share consolidation approved by shareholders at the Extraordinary General Meeting on 4 October 2005.

Information on audit or review

The Financial Statements have been audited by Deloitte.

CORPORATE GOVERNANCE STATEMENT

A summary of the Company's main corporate governance practices, as well as any disclosures required by the Australian Stock Exchange's "Principles of Good Corporate Governance and Best Practice Recommendations", is set out below.

Composition of the board

The Board reviews the mix of experience, expertise and other qualities of the Directors. If a vacancy occurs on the Board, or if the Board is to be increased, the Board will identify the experience, expertise and other qualities sought and identify appropriate candidates. The Remuneration and Appointments (REM) Committee considers these matters in concert with the Board.

Directors retiring by rotation do not seek re-election at an Annual General Meeting if they have reached 69 years of age on or before the date of that meeting. In any event, Directors retire from the Board on reaching 70 years of age.

Board responsibilities

The Directors are responsible for protecting the rights and interests of the Shareholders through the development of sound strategies, ensuring their implementation, and by the development of an integrated framework of controls over the Company's resources, functions and assets.

The Board's responsibilities include:

- Steering strategic directions and establishing goals for management;
- Monitoring performance against these goals and objectives;
- Ensuring there are adequate business controls and ethical standards of behaviour;
- Appointing the Chief Executive Officer, evaluating performance and determining the remuneration of the Chief Executive Officer and senior executives;
- Ensuring the significant risks facing the business have been identified and the appropriate and adequate control monitoring and reporting mechanisms are in place; and
- Ensuring there are policies and procedures for recruitment, training, remuneration and succession planning.

Committees of the board

The Board of AML has established and continues to operate the following committees:

- Finance, Audit and Compliance Committee; and
- Remuneration and Appointments Committee.

Each Committee is chaired by a Non-Executive Director and is comprised of Non-Executive members. The committee terms of reference outline committee responsibilities and are available on request.

Membership and attendance at Board Committees is detailed in the Directors' Report.

Independence of directors

It is important to have a board of an effective composition, size and commitment to adequately discharge its responsibilities and duties. During the year, the Board comprised of a Non-Executive Chairman, three Non-Executive Directors and a Managing Director (who is the only executive on the Board).

Mr Creagh O'Connor, Non-Executive Director resigned as Director on 20 April 2006 due to other business commitments. Mr O'Connor had been a Director of the Company since October 1996.

Dr Rawlings, Mr Byrne and Mr Williams are Non-Executive Directors and are independent, acting in the Company's best interests, notwithstanding the following:

- Dr Rawlings, was previously appointed acting Chief Executive Officer on 16 June 2003, was appointed as Executive Chairman on 24 November 2003. This was due to the challenges facing the Group. With the finalisation of the QMAG sale and termination of the Heads of Agreement, Dr Rawlings resigned this position on 8 November 2004, and became Non-Executive Chairman; and
- Mr Williams was a consultant to Newmont Australia, recently a major shareholder, and was also their previous Group Executive - Finance and Business Management until March 2003.

The Non-Executive Directors meet whenever necessary without the Managing Director. The Managing Director is not a member of the FAC or REM Committees and is invited to these meetings where appropriate.

The Company will engage further independent directors (as required).

Internal controls framework and risk management

The Board is responsible for the overall business control framework, but recognises that cost-effective control systems will not necessarily preclude all errors and irregularities. To assist in discharging this responsibility, the Board has instigated a Business Control Framework designed to safeguard the Group's assets and interests and to ensure the integrity of reporting. In addition, the Board constantly monitors the operational and financial aspects of the Company's activities. Through the audit committee, the Board considers the recommendations and advice of external auditors and other external advisors on the operational and financial risks that face the Company.

The Business Control Framework identifies risk management as a key area which is subject to regular reporting to the Board. In addition, the Board investigates ways of enhancing existing risk management strategies, including appropriate segregation of duties, and the employment and training of suitably qualified and experienced personnel.

CORPORATE GOVERNANCE STATEMENT

Remuneration

The overall role of the REM Committee is to ensure that Company remuneration policies and practices are consistent with the Company's goals and objectives. Written detailed terms of reference have been completed.

Directors' and executives' remuneration is presented in the Directors' Report and in note 4 to the financial statements.

Independent professional advice

When Board members require advice, it is sought as advice for the full Board and each member has unrestricted access to that advice and may suggest issues on which such advice should be sought.

However, if an individual Director requires separate advice then, with the prior approval of the Chairman, which must not be unreasonably withheld, that Director may seek that advice at the Company's expense.

Performance assessment

The Board reviews Key Performance Indicators (KPIs) for the Managing Director and the Management Team set on an annual basis. These annual KPIs are mutually agreed by the employee and his/her supervisor. The KPIs reflect the employee's ability to add value to the entity by ensuring productive gains such as increasing efficiencies, reduction in costs and increased profitability by maximising sales volumes and margins on sale revenues. Variable and long term incentives will only be paid if set objectives are achieved.

A Board evaluation process is undertaken by the Directors to define the areas in which the Board excels and, of equal importance, those areas which need focused attention for improvement. Non-Executive Directors do not receive any performance incentive payments.

External auditor

The appointment of the external auditor, the audit fee, and any questions of resignation or dismissal are considered first by the FAC Committee. The FAC Committee then conveys its recommendation to the full board. Our current external auditor, Deloitte, was first appointed in late 1999. It is Deloitte policy to rotate audit engagement partners on listed companies at least every five years. In practice, however, our audit engagement partner was changed for the 2001 and again for the 2004 financial year audit.

Ethical standards

AML has adopted the following Statement of General Principles that applies to all of AML's business affairs and describes the behaviour expected of every employee. The principles are founded in the core values of honesty, integrity and respect for people.

All directors, managers and staff are expected to act with the utmost integrity and objectivity, in their dealings with each other, competitors, suppliers, customers and the community, striving at all times to enhance the reputation and performance of the business. Every employee has a nominated supervisor to whom they may refer any issues arising from their employment.

The requirement to comply with these ethical standards is taken as a matter of course and is emphasised to all employees.

Continuous disclosure and shareholder communication

The Company has a written continuous disclosure policy.

The Company Secretary is responsible for communications with the Australian Stock Exchange (ASX), including compliance with the ASX continuous disclosure requirements. These responsibilities are specified in the Company Secretary's written position description. The charter of the Finance, Audit and Compliance Committee also specifically includes the review of compliance with ASX and legal requirements.

Through regular shareholder communications such as the Annual Report, Quarterly Reports, and periodic Stock Exchange Reports, the Board informs shareholders of significant developments affecting the Company. All company announcements are immediately posted on the company website. Shareholders are explicitly encouraged to attend general meetings in notices of meeting.

Dealing in shares

The Company has a formal share dealing policy for all employees. This policy reinforces the restrictions in the Corporations Act 2001 with respect to inside trading and use of price sensitive information.

Under the terms of the policy applicable to company staff, AML securities may only be sold or purchased outside the restricted period. The restricted period occurs during the following times:

- Two weeks prior to a Board Meeting.
- One month prior to the release of the half yearly results or the annual results.
- One week prior to the release of the quarterly reports.

If a special need arises for employees to deal outside the window period they are required to contact the Company Secretary prior to entering into the transaction so that Management can determine whether the dealing would be prohibited under the Corporations Law.

DIRECTORS' REPORT

The Directors of Advanced Magnesium Limited (formerly Australian Magnesium Corporation Limited) submit herewith the annual financial report of the Company for the financial year ended 30 June 2006. In order to comply with the provisions of the Corporations Act 2001, the Directors report as follows:

The names and particulars of the Directors of the Company during or since the end of the financial year are:

Board of Directors

DR CHRIS RAWLINGS
PhD, B Sc (Hons), FAICD.

Non-Executive Chairman

Dr Rawlings (55) is a former Managing Director of QCT Resources Ltd and was appointed to the AML Board on 3 October 2002. On 6 June 2003 he was appointed Acting Chief Executive Officer. He was appointed Executive Chairman on 22 November 2003 and resigned from his executive roles on 8 November 2004 and since then has been the Non-Executive Chairman of AML. He is the Chairman of Renison Consolidated Mines NL, Northern Energy Corporation Limited and D'Aguiar Gold Pty Limited and a non-Executive Director of Uniquest Pty Ltd and JKTech Pty Ltd.

Shareholding at 30 June 2006: 5,000 Ordinary Shares.

MR DENIS BYRNE
LL.B.

Non-Executive Director

Mr Byrne (59) practised commercial law for 27 years with wide experience in the corporate, infrastructure and resources areas. He was President of the Queensland Law Society in 1985/1986 and the Law Council of Australia in 1988/1989. He was formerly the Managing Partner of Freehill Hollingdale & Page, Brisbane.

Mr Byrne is currently a member of the Australian and the New Zealand Takeovers Panel and Chairman of the Fisheries Research & Development Corporation. His other directorships include Stanwell Corporation Ltd and the Ball Solutions Group of Companies Australia – subsidiaries of Ball Corporation (US).

Shareholding at 30 June 2006: 100,000 Ordinary Shares.

MR IAN HARTNELL
B. Eng. (Chem. Eng.), MBA.

Managing Director

Mr Hartnell (58) joined the Company in 1987 and has over 30 years history in new project development, international marketing of metals and merchant banking. He was previously the General Manager of QMC and subsequently became Vice President Sales & Marketing of AML. He was appointed the Managing Director of the Company in November 2004.

Shareholding at 30 June 2006: 9,100 Ordinary Shares and 656,000 Options.

MR CREAGH O'CONNOR
B.Ec., LL.B., ACA.

Non-Executive Director

Mr O'Connor (45) is a Director and Principal of merchant bank advisory group Gryphon Partners. Mr O'Connor resigned from the Board of Directors on 20 April, 2006.

Shareholding at 30 June 2006: not applicable.

MR KEN WILLIAMS
B.Ec (Hons), M App Fin, MAICD, CFTP.

Non-Executive Director

Mr Williams (45) joined the AML Board as a Newmont appointee in April 2002 and became an independent non-executive director in December 2003. Mr Williams has over 20 years experience in corporate finance and treasury related roles and is a non-executive director of Havilah Resources NL, Curnamona Energy Limited, Geothermal Resources Limited and Queensland Cotton Limited.

Shareholding at 30 June 2006: 15,000 Ordinary Shares.

DIRECTORS' REPORT

The above directors held office during and since the end of the financial year except for:

- Mr Creagh O'Connor – resigned 20 April 2006

Directorships of other listed companies

Directorships of other listed companies held by directors in the three years immediately before the end of the financial year are as follows:

Director and Company	Period of Directorship
Dr CD Rawlings	
Renison Consolidated Mines NL	Since 2002
D'Aguilar Gold Limited	Since 2003
Northern Energy Corporation Limited	Since 2005
Mr FCH O'Connor	
Hindmarsh Resources Ltd	Since 2003 Resigned April 2006
Mr KG Williams	
Havilah Resources NL	Since December 2003
Curnamona Energy Limited	Since January 2005
Geothermal Resources Ltd	Since July 2005
Queensland Cotton Ltd	Since January 2006
Mr DM Byrne	
Ball Solutions Group of Companies Australia (subsidiaries of Ball Corporation (US))	Since May 2005

Company Secretary

MR PK NAIR

B Bus (Acctg), MBA, FCA, FCPA, FCIS, FTIA, MAICD

Mr Nair (49) joined AML in 1988. He was previously a tax manager for a chartered accounting firm and has over 30 years experience in commercial business.

Principal activities

The principal activities of the consolidated entity during the course of the financial year consisted of:

- Researching and developing new proprietary magnesium alloys and technologies which will be required to support the future needs of automotive and other downstream users;
- Creating markets for these new alloys and technologies by supporting in-house demonstration trials and programs for developing new applications in alliance with these customers; and
- Manufacturing and selling these new alloys and technologies to its customers for a profit.

Directors meetings

The following table sets out the number of directors meetings (including meetings of committees of directors) held during the financial year and the number of meetings attended by each director (while they were a director or committee member). During the financial year, ten board meetings, one nomination and remuneration committee meeting and five finance and audit committee meetings were held.

Director	Board Meetings		Committee Meetings*	
	Attended	Held	FAC	REM
Mr CD Rawlings	10	10	5/5	1/1
Mr DM Byrne	10	10	5/5	1/1
Mr ID Hartnell	10	10	5/5	1/1
Mr FCH O'Connor	8	9	4/4	0/0
Mr KG Williams	10	10	5/5	1/1

* Attendance reflects tenure of member, e.g. attended four of five (4/5) meetings while a committee appointee.

Directors' shareholdings

The following table sets out each director's relevant interest in shares, debentures, and rights or options in shares or debentures of the Company or a related body corporate as at the date of this report.

Director	Security Type	Amount of shares
Dr CD Rawlings	Ordinary	5,000
Mr KG Williams	Ordinary	15,000
Mr DM Byrne	Ordinary	100,000
Mr ID Hartnell	Ordinary	9,100

Director	Options	Amount of Options*
Mr ID Hartnell	31 cent options	656,000

* These options expire in October 2010.

DIRECTORS' REPORT

Remuneration report

(a) Key management personnel - audited

The key management personnel of Advanced Magnesium Limited during the year were:

- **Dr CD Rawlings** – Chairman of the Board
- **Mr ID Hartnell** – Managing Director
- **Mr DM Byrne** – Non-Executive Director and Chairman of REM committee
- **Mr FCH O'Connor** – Non-Executive Director (resigned 20 April 2006)
- **Mr KG Williams** – Non-Executive Director and Chairman of FAC committee
- **Mr G Dunlop** – General Manager Technology Development
- **Mr G Fotheringham** – General Manager East Asia
- **Mr C Kettler** – General Manager Europe
- **Mr PK Nair** – General Manager Corporate
- **Mr T Sweder** – General Manager North America

(b) Key management personnel compensation policy - audited

The aggregate amount of Non-Executive Directors' fees is approved by Shareholders and is currently limited to \$600,000 per annum. Any increase must be approved by Shareholders. The Board decides how that aggregate or a lesser amount is divided between the Directors.

For 2005-06, the directorship fees for Non-Executive Directors were set at \$40,000 per annum and \$60,000 per annum for the Non-executive Chairman. These amounts remain unchanged from the previous financial year. Fees paid to the Chairman of the Finance, Audit and Compliance Committee amounted to \$6,250 and fees paid to each Non-Executive member of the FAC Committee amounted to \$2,500. Mercer HR Consulting have advised that the Non-Executive Directors and Committee fees reflect current market practice for comparable companies. No fees were paid to members of the REM Committee.

Remuneration and other terms of employment for the Managing Director and executives are formalised in employment agreements. Each agreement provides the ability to salary sacrifice benefits and an eligible bonus scheme and are open ended. Personnel are entitled to annual, long service and sick leave as prescribed by local or Queensland legislation. Entitlements under foreign jurisdiction laws in relation to pensions are also reflected in the specified remuneration details, where applicable. Termination of the employment may be effected by either the company or the executive at any time with either four weeks or one month written notice.

Employees are subject to annual salary reviews. Salaries of AML and AMT employees are adjusted annually for inflationary effects. AML employee salaries are also adjusted to average market rate if appropriate.

(c) Elements of remuneration related to performance - audited

The Board of Directors' policy on remuneration is as follows:

- Each Director, Executive or employee has an individual written contract outlining the terms and conditions under which that person is engaged;
- Each non-executive director has executed an indemnity, insurance & access deed with the Company;
- When an executive or an employee is recruited, the Group's aim is to reward its staff at market rates within the manufacturing technology industry as determined and in consultation with the employment agency;
- Employee's fixed remuneration packages are indexed annually in accordance with movement in the Consumer Price Index (All Groups Index) as published by the Australian Government Statistician;
- The individual's package is flexible and can incorporate salary sacrifice components making the individual's package tax effective;
- The aim of the remuneration policy is to retain key employees and to align employee interests with Company performance and Shareholders' interests; and
- An Employee Share Option Plan (ESOP) has been established comprised of two components:
 - (i) An initial issue of options was made in October 2005 which was approved by Shareholders and amongst other things was based on the position held by the employee, their length of service and the contribution made by the employee to the Company; and
 - (ii) Subsequent issues of options will be based on the achievement of specific performance criteria to be approved by the Board on an annual basis. Non-executive directors are not entitled to participate in the ESOP. The ESOP is designed to provide personnel with options, which links their rewards to the future success of the Company and to shareholders' objectives. In the current year there were no issue of options under this form.
- Staff remuneration has three components:
 - (i) Base or fixed remuneration;
 - (ii) Variable (at risk) performance (there were no bonuses awarded under this criterion during the year); and
 - (iii) A long-term incentive in the form of options.
- Each employee has a set of key performance indicators (KPIs) mutually agreed by the employee and his/her supervisor established on an annual basis. The KPIs reflect the employee's ability to add value to the entity and increase shareholder wealth by ensuring productive gains such as increasing efficiencies, reduction in costs and increased profitability by maximising sales volumes and margins on sale revenues. Variable and long term incentives will only be paid if set objectives are achieved.

This Board Policy will be reviewed by the Remuneration & Appointments Committee as required and, where appropriate make recommendations to the Board if any amendment is required.

DIRECTORS' REPORT

(d) Key management personnel – audited

The following tables disclose the remuneration of the key management personnel of the Company for the financial year with comparatives for the prior year:

Financial Year ended 30 June 2006:

	Short-term employee benefits			Post-employment benefits		Share based payments	Total
	Salary & fees	Bonus	Non-monetary	Super-annuation	Other	Equity Options (2)	
	\$	\$	\$	\$	\$	\$	
Dr CD Rawlings	62,500	-	-	5,625	-	-	68,125
Mr ID Hartnell	217,397	-	2,051	90,853	-	121,360	431,661
Mr DM Byrne	42,500	-	-	3,825	-	-	46,325
Mr KG Williams	46,250	-	-	4,163	-	-	50,412
Mr FCH O'Connor(1)	33,750	-	-	-	-	-	33,750
Mr G Dunlop	181,665	-	2,051	76,290	-	73,006	333,012
Mr G Fotheringham(3)	127,450	-	-	41,471	-	30,409	199,330
Mr C Kettler	196,938	-	25,000	-	-	52,147	274,085
Mr PK Nair	169,700	-	2,051	42,057	-	69,148	282,956
Mr T Sweder(3)	200,000	-	-	-	-	27,750	227,750
Total	1,278,150	-	31,153	264,284	-	373,820	1,947,406

(1) Mr O'Connor retired from the Board on 20 April 2006.

(2) The Equity Options have been valued at a theoretical cost of 18.5 cents each with a volatility of 67.5%. The Options have each an exercise price of 31 cents were granted in October 2005 and at 30 June 2006 were "well out of the money". The Shareholders approved the allocation of the Equity Options to the Managing Director.

(3) Mr G Fotheringham and Mr T Sweder are considered key management personnel from 1 July 2005 due to a change in responsibilities.

Financial Year ended 30 June 2005:

	Short-term employee benefits			Post-employment benefits		Share based payments	Total
	Salary & fees	Bonus	Non-monetary	Super-annuation	Other	Ordinary Shares	
	\$	\$	\$	\$	\$	\$	
Dr CD Rawlings(1)	172,615	-	1,180	15,535	-	-	189,330
Mr ID Hartnell(2)	261,267	-	21,996	19,861	-	4,423	307,547
Mr DM Byrne(3)	6,410	-	-	577	-	-	6,987
Mr FCH O'Connor	40,000	-	-	-	-	-	40,000
Mr KG Williams	40,000	-	-	3,600	-	-	43,600
Mr JD Story(4)	33,795	-	-	3,042	-	-	36,837
Mr G Dunlop	217,890	-	3,124	19,610	-	-	240,624
Mr C Kettler	177,966	-	25,424	19,171	-	-	222,561
Mr PK Nair	192,601	-	3,124	16,600	-	-	212,325
Mr G Sheehan(5)	182,575	-	3,124	14,649	-	-	200,348
Mr A Roughead(6)	69,994	21,500	16,437	7,656	-	1,301	116,888
Total	1,395,113	21,500	74,409	120,301	-	5,724	1,617,047

(1) Dr Rawlings reverted to non-executive Chairman on 8 November 2004.

(2) Mr Hartnell was employed as an Executive from 1 July 2004 to 17 November 2004 and from thereon served as Managing Director. Mr Hartnell was granted 8,500 (post consolidated) ordinary shares in October 2004 when he was an executive and before he became a director and the market value of those shares amounted to \$4,423. The remuneration received before Mr Hartnell became a director was \$120,690.

(3) Mr Byrne joined the Board on 4 May 2005.

(4) Mr Story retired from the Board on 4 May 2005.

(5) Mr Sheehan was made redundant on 31 October 2005 and ceased to be key management at 30 June 2005.

DIRECTORS' REPORT

- (6) Mr Roughead's employment with AML Group terminated with the sale of the QMAG business to RCF on 1 December 2004. He was granted in December 2004 his allocation of 2,500 (post consolidated) ordinary shares from the Executive Share Plan and the market value of those shares amounted to \$1,301. The Executive Share Plan is otherwise suspended. Mr Roughead received a cash bonus of \$21,500 based on safety, profitability and productivity KPIs for the QMAG business for the year ended 6 July 2004 (paid in September 2004). These KPIs were for the QMAG business and not individually based. The bonus was awarded on a sliding scale based on the criteria met. Mr Roughead forfeited a certain component of his available bonus due to the QMAG business not achieving its maximum possible KPIs.

(e) Value of options issued to key management personnel

The following table discloses the value of options granted, exercised or lapsed during the year.

	Options Granted Value at grant date	Options Exercised Value at exercise date	Options Lapsed Value at time of lapse	Total value of options granted, exercised and lapsed	Value of options included in remuneration for the year	Percentage of total remuneration for the year that consists of options
	\$	\$	\$	\$	\$	%
Mr ID Hartnell(1)	121,360	–	–	121,360	121,360	28.11
Mr G Dunlop	73,006	–	–	73,006	73,006	21.92
Mr G Fotheringham	30,409	–	–	30,409	30,409	15.26
Mr C Kettler	52,147	–	–	52,147	52,147	19.03
Mr PK Nair(2)	69,148	–	–	69,148	69,148	24.44
Mr T Sweder	27,750	–	–	27,750	27,750	12.18

(1) Mr Hartnell had 50 share options which had nil value and lapsed during the year.

(2) Mr Nair had 32 share options which had nil value and lapsed during the year.

(f) Value of options – basis of calculation

Under the Employee Share Option Plan approved on 4 October 2005, options allowing subscription of up to 5% of the issued share capital of AML are available for issue to employees, with options over a further 5% of the issued share capital in the future based on performance.

For the options granted to employees in October 2005, these are unlisted options exercisable at any time upon payment of the exercise price of \$0.31 and expire 5 years from issue on 13 October 2010. A binomial model was used to value these options at a theoretical cost of 18.5 cents each based on a volatility of 67.5%. At 30 June 2006 the options were "well out of the money".

DIRECTORS' REPORT

Review of Income Statement and operations

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
Sales revenue	363,140	85,381
Cost of sales	(209,004)	-
Gross profit	154,136	85,381
Other income	3,012,458	1,567,349
Recoverable amount write downs	(45,016)	(493,740)
Loss on sale of assets	(7,058)	-
Marketing	(1,087,269)	(229,497)
Research, development, licensing and patent costs	(1,479,646)	(878,949)
Redundancy costs	(169,631)	(1,063,901)
AMT operating costs	(3,048,134)	(3,794,094)
Corporate, administration and other expenses	(2,075,111)	(2,566,676)
Loss before income tax expense	(4,745,271)	(7,374,127)
Income tax expense	(97,028)	(51,321)
Loss from continuing operations	(4,842,299)	(7,425,448)
Profit from discontinued operations	4,415,840	7,481,447
Profit/(loss) attributable to members of the parent entity	(426,459)	55,999

Revenue

Sales of AMT's alloys and metal handling technologies continue to grow, albeit slowly. Included in revenue is sales of six AM-converters totalling approximately \$170,000 and AM-lite revenues from trials of \$160,000. Other income during the year consists of cash received from Magtrust on sale of its shareholding of AML shares of \$2.1m and interest on cash balances of \$700,000.

Operating costs relating to the Advanced Magnesium Technologies business continues to be supported by expenditure on research and development into AMT's unique proprietary alloys and the corporate infrastructure expenses of a listed company. As AMT transitions from trials of its flagship AM-lite product into commercial sales, marketing and promotional expenditure has become a greater component of overall expenditure.

The finalisation of the Stanwell Project comprises the accounting profit outlined under discontinued operations. The potential liability of \$4.8m was successfully settled (resulting in a credit) by providing Alcan with an exclusive licence for the Stanwell Engineering Package, offset by a final write down of the remaining assets at Stanwell of \$400,000.

DIRECTORS' REPORT

Review of Balance Sheet

	CONSOLIDATED	
	30 June 2006 \$	30 June 2005 \$
Assets		
Cash	12,109,140	7,152,374
Receivables	880,233	457,301
Inventories	292,005	–
Property, plant & equipment	379,775	449,672
Non-current assets classified as held for sale	–	937,800
Prepayments and other	119,562	139,369
Total	13,780,715	9,136,516
Liabilities		
Payables and Other Liabilities	759,447	5,510,122
Provisions	310,503	354,464
Other	79,000	–
Total	1,148,950	5,864,586
Net Assets	12,631,765	3,271,930

The net asset position of the Group has strengthened during the year due to inflows of cash from the issue of ordinary shares and receipt of cash from Magtrust Pty Ltd for the sale of its shareholding of AML ordinary shares in October 2005.

The balance of Stanwell assets has been classified as assets held for sale under the new accounting standards. The 30 June 2005 balance has been partially converted to cash, during the current year with the remainder written off to nil value.

The reduction in payables includes the settlement of a licence payable to Alcan of \$4.8m in relation to the Stanwell Project.

As a result the 30 June 2006 balance sheet solely comprises the AML Group and its Advanced Magnesium Technologies operating business.

DIRECTORS' REPORT

Review of Cashflow

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
Opening Cash Balance	7,152,374	12,460,000
Inflows		
Proceeds from issue of securities	9,765,900	-
Proceeds from sale of QMAG business	-	65,037,248
Receipt from Magtrust Pty Ltd	2,077,690	-
Proceeds from sale of non-current and project assets	463,825	1,596,100
Recovery of insurance premiums	-	1,145,590
Outflows		
Operating activity outflows and other (net)	(6,332,406)	(3,113,800)
Redundancies	(169,631)	(1,123,184)
Payment to Government Stakeholders re: DOTR	-	(3,000,000)
Repayment of Department of Natural Resources security	-	(1,850,081)
Property, plant & equipment purchased and mine development	(284,600)	(1,583,131)
Net Interest & borrowing costs paid	-	(1,089,439)
Repayment of Borrowings and Leases	-	(61,326,929)
Share issue costs	(564,004)	-
Net Cash Inflows/ (Outflows)	4,956,766	(5,307,626)
Closing Cash Balance	12,109,140	7,152,374

The AML Group had a closing balance of \$12,109,140 at 30 June 2006 representing a net increase in cash of \$4,956,766 over the year.

Total net fundraising in October 2005 comprising issue of ordinary shares, receipt of cash from Magtrust on sale of its AML ordinary shareholding less share issue costs was \$11.3m. This was offset by usage of cash in the Advanced Magnesium Technologies business and supporting corporate and administration activities of \$6.3m.

DIRECTORS' REPORT

Dividends

The Directors have not recommended payment of a dividend and no dividends have been paid or declared since the end of the previous financial year.

Changes in state of affairs

Significant changes in the state of affairs of the consolidated entity during the financial year were as follows:

- An Extraordinary General Meeting was held on 4 October 2005. At this meeting, the following proposals were put to the shareholders and passed:
 - that the Company's name be changed from Australian Magnesium Corporation Limited to Advanced Magnesium Limited;
 - that the Company's share capital be consolidated on a 1 for 20 basis;
 - that an Employee Share Option Plan be implemented;
 - that Mr ID Hartnell be provided options in his capacity as Managing Director; and
 - that up to 50 million ordinary shares be issued via a placement to new shareholders.
- On 4 October 2005, AML undertook a major capital restructuring to prepare itself for the commercialisation phase of its AM-lite technology. This included raising \$13m in new equity capital from 23 institutional and private investors, the sell-down of AML shares by Magtrust, and the consolidation of the share structure on a 1:20 basis.

Subsequent events

There has not been any matter or circumstance that has arisen since the end of the financial year that has significantly affected, or may significantly affect, the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in future financial years.

Share options on issue at the date of this report or exercised during the year

Details of unissued shares or interests under option are:

Issuing entity	Number of shares under option	Class of shares	Exercise price of option	Expiry date of options
AML	150,000	ORD	\$12.00	28 Feb 07
AML	3,313,273	ORD	\$0.70	29 Nov 07
AML	2,645,650	ORD	\$0.31	13 Oct 10
AML	400,000	ORD	\$0.25	7 Oct 08

The holders of such options do not have the right, by virtue of the option, to participate in any share issue or interest issue of any other body corporate or registered scheme.

No shares or interests were issued during the financial year as a result of exercise of an option.

During and since the end of the financial year an aggregate of 2,020,650 share options were granted to the following directors and executives of the Company:

Directors and executives	Number of options granted	Issuing entity	Number of ordinary shares under option
Mr ID Hartnell	656,000	AML	656,000
Mr G Dunlop	394,625	AML	394,625
Mr G Fotheringham	164,375	AML	164,375
Mr C Kettler	281,875	AML	281,875
Mr PK Nair	373,775	AML	373,775
Mr T Sweder	150,000	AML	150,000

Future developments

Disclosure of information regarding likely developments in the operations of the consolidated entity in future financial years and the expected results of those operations are likely to result in unreasonable prejudice to the consolidated entity. Accordingly, this information has not been disclosed in this report.

Environment regulations

The Consolidated Entity's operations were subject to various environmental laws and regulations relating to the QMAG business. These ceased being applicable on the sale of QMAG on 1 December 2004.

Non-audit services

There were no non-audit services provided by the auditors in this year or the prior year.

Auditor's independence declaration

The auditor's independence declaration is included on page 12 of the financial report.

Indemnification of officers and auditors

The Company paid a premium to insure certain officers of the Company and related bodies corporate in relation to performance of their duties as officers of the Company. The officers of the Company covered by the insurance policy include directors or secretaries of controlled entities who are not also directors of the Company. A confidentiality clause in the insurance contract does not permit further details to be disclosed.

The Company has not otherwise, during or since the financial year, indemnified or agreed to indemnify an officer or auditor of the Company or of any related body corporate against a liability incurred as such an officer or auditor.

On behalf of the Directors



DR CD RAWLINGS
NON-EXECUTIVE
CHAIRMAN



MR KG WILLIAMS
NON-EXECUTIVE
DIRECTOR

Signed on the 25 August 2006 in accordance with a resolution of the Directors made pursuant to Section 298(2) of the Corporations Act 2001.

INDEPENDENT AUDIT DECLARATION



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The Board of Directors
Advanced Magnesium Limited
Level 9, 303 Coronation Drive
Milton 4064 QLD

25 August 2006

Dear Board Members

Advanced Magnesium 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 Advanced Magnesium Limited.

As lead audit partner for the audit of the financial statements of Advanced Magnesium Limited for the financial year ended 30 June 2006, 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 audit; and
- (ii) any applicable code of professional conduct in relation to the audit.

Yours sincerely

DELOITTE TOUCHE TOHMATSU

Timothy Biggs
Partner
Chartered Accountant

Liability limited by a scheme approved under Professional Standards Legislation.

FINANCIAL REPORT FOR THE YEAR ENDED 30 JUNE 2006

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DIRECTORS' DECLARATION

AUDIT REPORT

FINANCIAL REPORT GLOSSARY

AASB	Australian Accounting Standards Board
AGAAP	Australian Generally Accepted Accounting Principles
A-IFRS	Australian equivalent to International Financial Reporting Standards
AMC	Australian Magnesium Corporation Limited
AMO	Australian Magnesium Operations Pty Ltd
AML	Advanced Magnesium Limited (formerly AMC)
AMI	Australian Magnesium Investments Pty Ltd
AMT	Advanced Magnesium Technologies Pty Ltd (formerly AMO)
ANZ	Australian and New Zealand Banking Group Limited
ASX	Australian Stock Exchange
AUD	Australian Dollars
CAST	CRC for Cast Metals Manufacturing
CRC	Co-operative Research Centre
CSIRO	Commonwealth Scientific and Industrial Research Organisation
DES	Distribution Entitled Securities
EDC	Export Development Canada
EPM	Exploration Permit Mining
ESOP	Employee Share Option Plan
ESP	Executive Share Plan
EUR	Euro
FBT	Fringe Benefit Tax
FEC	Forward Exchange Contracts
GESP	General Employee Share Plan
GST	Goods and Services Tax
IFRS	International Financial Reporting Standards
IMC	Icelandic Magnesium Corporation Limited
IMS	IMS Expert-Conseils Inc
JLM	Joint Lead Manager
Magtrust	Magtrust Pty Ltd
Newmont	Newmont Australia Limited
QMAG	Queensland Magnesia Pty Ltd
QMAG JV	Queensland Magnesia Joint Venture
QMC	Queensland Metals Corporation Pty Ltd
QMO	Queensland Magnesia Operations Pty Ltd
QTH	Queensland Treasury Holdings
RCF	Resource Capital Fund III L.P.
SMP	Stanwell Magnesium Project
USD	United States Dollars
WANOS	Weighted Average Number of Ordinary Shares

INCOME STATEMENT
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2006

	NOTE	CONSOLIDATED		PARENT ENTITY	
		30 June	30 June	30 June	30 June
		2006	2005	2006	2005
		\$	\$	\$	\$
Sales revenue	2(a)	363,140	85,381	—	—
Cost of sales		(209,004)	—	—	—
Gross profit		154,136	85,381	—	—
Other income	2(b)	3,012,458	1,567,349	2,768,357	397,587
Recoverable amount write downs		(45,016)	(493,740)	(3,107,910)	(458,544)
Loss on sale of assets		(7,058)	—	—	—
Doubtful debts intercompany		—	—	—	(1,650,951)
Marketing		(1,087,269)	(229,497)	—	—
Research, development, licensing and patent costs		(1,479,646)	(878,949)	—	—
Redundancy costs		(169,631)	(1,063,901)	—	(480,842)
AMT operating costs		(3,048,134)	(3,794,094)	—	—
Corporate, administration and other expenses		(2,075,111)	(2,566,676)	(1,754,941)	(1,992,355)
Loss before income tax expense		(4,745,271)	(7,374,127)	(2,094,494)	(4,185,105)
Income tax expense	3(a)	(97,028)	(51,321)	—	—
Loss from continuing operations		(4,842,299)	(7,425,448)	(2,094,494)	(4,185,105)
Profit from discontinued operations	28	4,415,840	7,481,447	—	5,259,228
Profit/(loss) attributable to members of the parent entity		(426,459)	55,999	(2,094,494)	1,074,123
Earnings/(loss) per share:					
Basic (cents per share)	22	(0.555)	0.105		
Diluted (cents per share)	22	(0.555)	0.026		
Loss per share from continuing operations					
Basic (cents per share)	22	(6.304)	(14.024)		
Diluted (cents per share)	22	(6.304)	(14.024)		

Notes to the financial statements are included on pages 19 to 54.

The above Income Statement should be read in conjunction with the accompanying notes.

BALANCE SHEET
AS AT 30 JUNE 2006

	NOTE	CONSOLIDATED		PARENT ENTITY	
		30 June	30 June	30 June	30 June
		2006	2005	2006	2005
		\$	\$	\$	\$
Current assets					
Cash and cash equivalents	30(a)	12,109,140	7,152,374	9,372,913	4,427,045
Trade and other receivables	7	880,233	457,301	187,919	363,892
Inventories	8	292,005	—	—	—
Other	9	119,562	139,369	—	535
		13,400,940	7,749,044	9,560,832	4,791,472
Non-current assets classified as held for sale	10	—	937,800	—	—
Total current assets		13,400,940	8,686,844	9,560,832	4,791,472
Non-current assets					
Other financial assets	11	—	—	2,892,090	—
Property, plant & equipment	12	379,775	449,672	87,939	134,906
Total non-current assets		379,775	449,672	2,980,029	134,906
Total assets		13,780,715	9,136,516	12,540,861	4,926,378
Current liabilities					
Trade and other payables	13	759,447	671,752	96,212	145,055
Provisions	14	136,965	166,233	42,001	40,877
Other	15	15,800	—	—	—
Total current liabilities		912,212	837,985	138,213	185,932
Non-current liabilities					
Trade and other payables	16	—	4,838,370	—	—
Provisions	17	173,538	188,231	170,528	169,806
Other	18	63,200	—	—	—
Total non-current liabilities		236,738	5,026,601	170,528	169,806
Total liabilities		1,148,950	5,864,586	308,741	355,738
Net assets		12,631,765	3,271,930	12,232,120	4,570,640
Equity					
Share capital	19	894,244,184	884,488,210	894,244,184	884,488,210
Reserves	20	2,780,300	2,749,980	—	—
Accumulated losses	21	(884,392,719)	(883,966,260)	(882,012,064)	(879,917,570)
Total equity		12,631,765	3,271,930	12,232,120	4,570,640

Notes to the financial statements are included on pages 19 to 54.

The above Balance Sheet should be read in conjunction with the accompanying notes.

**STATEMENT OF RECOGNISED INCOME & EXPENSE
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2006**

	NOTE	CONSOLIDATED		PARENT ENTITY	
		30 June	30 June	30 June	30 June
		2006	2005	2006	2005
		\$	\$	\$	\$
Translation of foreign operations:					
Exchange differences taken to reserves in equity	20	30,320	—	—	—
Net income recognised directly in equity		30,320	—	—	—
Profit/(Loss) for the year		(426,459)	55,999	(2,094,494)	1,074,123
Total recognised income and expense for the year		(396,139)	55,999	(2,094,494)	1,074,123
Attributable to equity holders of the parent		(396,139)	55,999	(2,094,494)	1,074,123

Notes to the financial statements are included on pages 19 to 54.

The above Statement of Recognised Income and Expense should be read in conjunction with the accompanying notes.

CASHFLOW STATEMENT
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2006

	NOTE	CONSOLIDATED		PARENT ENTITY	
		30 June	30 June	30 June	30 June
		2006	2005	2006	2005
		\$	\$	\$	\$
		Inflows/ (Outflows)	Inflows/ (Outflows)	Inflows/ (Outflows)	Inflows/ (Outflows)
Cash flows from operating activities					
		230,141	29,958,942	—	15,229,431
		(7,755,955)	(34,135,868)	(1,209,792)	(13,447,521)
		543,270	606,930	419,696	283,879
		(2,205)	(1,696,369)	(1,729)	(893,132)
		—	1,145,590	—	—
		482,712	273,407	368,556	166,446
		Net cash provided by/(used in) operating activities			
	30(e)	(6,502,037)	(3,847,368)	(423,269)	1,339,103
Cash flows from investing activities					
		—	65,037,248	—	28,555,996
	30(b)	—	—	(6,000,000)	—
		—	(333,465)	—	—
	30(b)	(284,608)	(1,583,131)	—	(748,293)
		463,825	1,596,100	89,551	10,004
		Net cash (used in)/provided by investing activities			
		179,217	64,716,752	(5,910,449)	27,817,707
Cash flows from financing activities					
		9,765,900	—	9,765,900	—
		(564,004)	—	(564,004)	—
		2,077,690	—	2,077,690	—
		—	(3,000,000)	—	—
		—	(1,850,081)	—	(1,850,081)
		—	(400,929)	—	(148,684)
		—	(60,926,000)	—	(30,463,000)
		Net cash provided by/(used in) financing activities			
		11,279,586	(66,177,010)	11,279,586	(32,461,765)
		Net increase/(decrease) in cash and cash equivalents			
		4,956,766	(5,307,626)	4,945,868	(3,304,955)
		Cash and cash equivalents at the beginning of the financial year			
		7,152,374	12,460,000	4,427,045	7,732,000
		Cash and cash equivalents at the end of the financial year			
	30(a)	12,109,140	7,152,374	9,372,913	4,427,045

Notes to the financial statements are included on pages 19 to 54.

The above Cash Flow should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES

Statement of Compliance

The financial report is a general purpose financial report which has been prepared in accordance with the Corporations Act 2001, Accounting Standards and Urgent Issues Group Interpretations, and complies with other requirements of the law. Accounting Standards include Australian equivalents to International Financial Reporting Standards ('A-IFRS'). Compliance with the A-IFRS ensures that the consolidated financial statements and notes of the consolidated entity comply with International Financial Reporting Standards ('IFRS'). The parent entity financial statements and notes also comply with IFRS except for the disclosure requirements in IAS 32 'Financial Instruments: Disclosure and Presentation' as the Australian equivalent Accounting Standard, AASB 132 'Financial Instruments: Disclosure and Presentation' does not require such disclosures to be presented by the parent entity where its separate financial statements are presented together with the consolidated financial statements of the consolidated entity.

The financial statements were authorised for issue by the directors on 25 August 2006.

Basis of Preparation

The financial report has been prepared on the basis of historical cost. Cost is based on the fair values of the consideration given in exchange for assets.

In the application of A-IFRS management is required to make judgments, estimates and assumptions about carrying values of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstance, the results of which form the basis of making the judgments. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of A-IFRS that have significant effects on the financial statements and estimates with a significant risk of material adjustments in the next year are disclosed, where applicable, in the relevant notes to the financial statements.

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The consolidated entity changed its accounting policies on 1 July 2005 to comply with A-IFRS. Advanced Magnesium Limited (formerly Australian Magnesium Corporation Limited) has adopted all the new and revised Accounting Standards and Interpretations issued by the AASB that are relevant to its operations and effective for annual reporting periods beginning on 1 July 2005. The transition to A-IFRS is accounted for in accordance with Accounting Standard AASB 1 'First-time Adoption of Australian Equivalents to International Financial Reporting Standards', with 7 July 2004 as the date of transition. An explanation of how the transition from superseded policies to A-IFRS has affected the company's and consolidated entity's financial position, financial performance and cash flows is discussed in note 32.

The directors have also elected under s.334(5) of the Corporations Act 2001 to apply Accounting Standard AASB 119 'Employee Benefits' (December 2004), even though the Standard is not required to be applied until annual reporting periods beginning on or after 1 January 2006. The Directors have given due consideration to all other new and revised Standards and Interpretations issued by the AASB that are not yet effective and do not believe that they will have any material financial impact on the financial statements of the Company or the consolidated entity.

The accounting policies set out below have been applied in preparing the financial statements for the year ended 30 June 2006, the comparative information presented in these financial statements for the year ended 30 June 2005, and in the preparation of the opening A-IFRS balance sheet at 7 July 2004 (as disclosed in note 32), the consolidated entity's date of transition, except for the accounting policies in respect of financial instruments. The consolidated entity has not restated comparative information for financial instruments, including derivatives, as permitted under the first-time adoption transitional provisions. The accounting policies for financial instruments applicable to the comparative information and the impact of changes in these accounting policies on 1 July 2005, the date of transition for financial instruments, is discussed further in note 1(t).

The prior year comparatives are for the financial period from 7 July 2004 to 30 June 2005.

Going Concern

In preparing these financial statements on a going concern basis, the Directors of Advanced Magnesium Limited are required to satisfy the going concern criteria set out by both legislation and legislative enforced professional standards.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

The reader's attention is drawn to the Corporations Act requirement that the Directors must opine that reasonable grounds exist that support the ability of the Company to pay its debts as and when they become due and payable. The Directors' belief that such reasonable grounds do exist as at the date of signing this financial report is set out in the Directors' Declaration on page 55.

In preparing its support for this going concern conclusion, the Directors considered many factors, including a cash flow forecast for twelve months from the reporting date which included management's estimates of cash inflows and outflows for the coming year. The Directors also considered other internal and external factors that may impact the operations of the business.

While the Directors have come to the conclusion that AML is a going concern and that the financial statements should be prepared on that basis, the Directors are unable to predict with certainty the impact of various factors that could, in isolation or in conjunction, alter this conclusion.

A significant factor to bring to the reader's attention is the impact that a delay of sales revenue from the commercialisation of AM-lite could have on cash flows. A change to the timing or the quantum of such revenues could have a considerable impact on the operations of the AML Group.

However, taking this matter into consideration and based on Management's estimates of cash inflows and outflows over the next twelve months, noting that these are not guaranteed, the Directors believe that whilst uncertainty exists beyond twelve months with respect to the Company and consolidated entity being able to continue as going concerns, the going concern basis of preparation of the Financial Report is appropriate.

Significant Accounting Policies

The following significant accounting policies have been adopted in the preparation and presentation of the financial report:

(a) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, cash in banks at call and on deposit.

(b) Employee benefits

Provision is made for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave, and sick leave when it is probable that settlement will be required and they are capable of being measured reliably.

Provisions made in respect of employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of employee benefits which are not expected to be settled within 12 months are measured as the present value of the estimated future cash outflows to be made by the consolidated entity in respect of services provided by employees up to reporting date.

Contributions to defined contribution superannuation plans are expensed when incurred.

(c) Financial assets

Subsequent to initial recognition, investments in subsidiaries are measured at cost. Subsequent to initial recognition, investments in associates are accounted for under the equity method in the consolidated financial statements and the cost method in the company financial statements.

Other financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss', 'held-to-maturity' investments, 'available-for-sale' financial assets, and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Receivables

Trade receivables and other receivables are recognised initially at their fair values and subsequently at amortised cost less impairment.

(d) Financial instruments issued by the company

Debt and equity instruments

Debt and equity instruments are classified as either liabilities or as equity in accordance with the substance of the contractual arrangement.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

Transaction costs on the issue of equity instruments

Transaction costs arising on the issue of equity instruments are recognised directly in equity as a reduction of the proceeds of the equity instruments to which the costs relate. Transaction costs are the costs that are incurred directly in connection with the issue of those equity instruments and which would not have been incurred had those instruments not been issued.

(e) **Foreign currency**

Foreign Currency Transactions

All foreign currency transactions during the financial year are brought to account using the exchange rate in effect at the date of the transaction. Foreign currency monetary items at reporting date are translated at the exchange rate existing at reporting date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined.

Exchange differences are recognised in profit or loss in the period in which they arise except that exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned or likely to occur, which form part of the net investment in a foreign operation, are recognised in the foreign currency translation reserve and recognised in profit or loss on disposal of the net investment.

Foreign Operations

On consolidation, the assets and liabilities of the consolidated entity's overseas operations are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are recognised in the foreign currency translation reserve, and recognised in profit or loss on disposal of the foreign operation.

(f) **Goods and Services Tax and Value Added Tax**

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST) or value added tax (VAT) for certain foreign jurisdictions, except for receivables and payables which are recognised inclusive of GST or VAT.

The net amount of GST or VAT recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Cash flows are included in the cash flow statement on a gross basis. The GST or VAT component of cash flows arising from investing and financing activities which is recoverable from, or payable to, the taxation authority is classified as operating cash flows.

(g) **Impairment of assets**

At each reporting date, the consolidated entity reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the consolidated entity estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

(h) Income tax

Current Tax

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by reporting date. Current tax for current and prior periods is recognised as a liability to the extent that it is unpaid.

Deferred Tax

Deferred tax is accounted for using the comprehensive balance sheet liability method in respect of temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax base of those items.

In principle, deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary differences or unused tax losses and tax offsets can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities (other than as a result of a business combination) which affects neither taxable income nor accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries, branches, associates and joint ventures except where the consolidated entity is able to control the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with these investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period(s) when the asset and liability giving rise to them are realised or settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the consolidated entity expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the company/consolidated entity intends to settle its current tax assets and liabilities on a net basis.

Current and Deferred Tax for the Period

Current and deferred tax is recognised as an expense or income in the income statement, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity, or where it arises from the initial accounting for a business combination, in which case it is taken into account in the determination of goodwill or excess.

Tax Consolidation

The company and all its wholly-owned Australian resident entities are part of a tax-consolidated group under Australian taxation law. Advanced Magnesium Limited is the head entity in the tax-consolidated group. Tax expense/income, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'stand-alone taxpayer' approach. Current tax liabilities and assets and deferred tax assets arising from unused tax losses and tax credits of the members of the tax-consolidated group are recognised by the company (as head entity in the tax-consolidated group).

Due to the existence of a tax funding arrangement between the entities in the tax-consolidated group, amounts are recognised as payable to or receivable by the company and each member of the group in relation to the tax contribution amounts paid or payable between the parent entity and the other members of the tax-consolidated group in accordance with the arrangement. Further information about the tax funding arrangement is detailed in note 3 to the financial statements. Where the tax contribution amount recognised by each member of the tax-consolidated group for a particular period is different to the aggregate of the current tax liability or asset and any deferred tax asset arising from unused tax losses and tax credits in respect of that period, the difference is recognised as a contribution from (or distribution to) equity participants.

(i) Intangible assets

Patents, Trademarks and Licences

Patents, trademarks and licences are recorded at cost less accumulated amortisation and impairment.

Research and Development Costs

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period as incurred.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

(j) Inventories

Inventories are valued at the lower of cost and net realisable value. Costs are assigned to inventory on hand by the method most appropriate to each particular class of inventory, with the majority being valued on a first in first out basis. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

(k) Leased assets

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Lease incentives

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefits of incentives are recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

(l) Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. The sale of the asset (or disposal group) is expected to be completed within one year from the date of classification.

(m) Payables

Trade payables and other accounts payable are recognised when the consolidated entity becomes obliged to make future payments resulting from the purchase of goods and services.

(n) Presentation currency

The presentation and functional currency of the AML Group is Australian dollars.

(o) Principles of consolidation and investments in subsidiaries

The consolidated financial statements are prepared by combining the financial statements of all the entities that comprise the consolidated entity, being the company (the parent entity) and its subsidiaries as defined in Accounting Standard AASB 127 'Consolidated and Separate Financial Statements'. A list of subsidiaries appears in note 26 to the financial statements. Consistent accounting policies are employed in the preparation and presentation of the consolidated financial statements.

On acquisition, the assets, liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. If, after reassessment, the fair values of the identifiable net assets acquired exceeds the cost of acquisition, the deficiency is credited to profit and loss in the period of acquisition.

The interest of minority shareholders is stated at the minority's proportion of the fair values of the assets and liabilities recognised.

The consolidated financial statements include the information and results of each subsidiary from the date on which the company obtains control and until such time as the company ceases to control such entity.

In preparing the consolidated financial statements, all intercompany balances and transactions, and unrealised profits arising within the consolidated entity are eliminated in full.

(p) Plant and equipment

Plant and equipment, leasehold improvements and equipment under finance lease are stated at cost less accumulated depreciation and impairment. Cost includes expenditure that is directly attributable to the acquisition of the item. In the event that settlement of all or part of the purchase consideration is deferred, cost is determined by discounting the amounts payable in the future to their present value as at the date of acquisition.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

Depreciation is provided on property, plant and equipment, including freehold buildings but excluding land. Depreciation is calculated on a straight line basis so as to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter, using the straight line method. The estimated useful lives, residual values and depreciation method is reviewed at the end of each annual reporting period.

The following estimated useful lives are used in the calculation of depreciation:

- Plant and equipment 2.5 – 13.33 years

(q) Provisions

Provisions are recognised when the consolidated entity has a present obligation, the future sacrifice of economic benefits is probable, and the amount of the provision can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cashflows estimated to settle the present obligation, its carrying amount is the present value of those cashflows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that recovery will be received and the amount of the receivable can be measured reliably.

(r) Revenue recognition

Sale of goods

Revenue from the sale of goods is recognised when the consolidated entity has transferred to the buyer the significant risks and rewards of ownership of the goods.

Rendering of services

Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract.

Interest revenue

Interest revenue is recognised on a time proportionate basis that takes into account the effective yield on the financial asset.

(s) Share-based payments

Equity-settled share-based payments granted after 7 November 2002 that were unvested as of 1 July 2005, are measured at fair value at the date of grant. Fair value is measured by use of a binomial model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the consolidated entity's estimate of shares that will eventually vest.

For cash-settled share-based payments, a liability equal to the portion of the goods or services received is recognised at the current fair value determined at each reporting date.

(t) Comparative information – financial instruments

The consolidated entity has elected not to restate comparative information for financial instruments within the scope of Accounting Standards AASB 132 'Financial Instruments: Disclosure and Presentation' and AASB 139 'Financial Instruments: Recognition and Measurement', as permitted on the first-time adoption of A-IFRS.

The effect of changes in the accounting policies for financial instruments on the balance sheet at 1 July 2005 are not material.

The accounting policies applied to accounting for financial instruments in the current financial year are detailed in notes 1(a) to (s). The following accounting policies were applied to accounting for financial instruments in the comparative financial year:

- Accounts payable
Trade payables and other accounts payable are recognised when the consolidated entity becomes obliged to make future payments resulting from the purchase of goods and services.
- Receivables
Trade receivables and other receivables are recorded at amounts due less any allowance for doubtful debts.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (cont...)

- Financial instruments issued by the company:

Debt and equity instruments

Debt and equity instruments are classified as either liabilities or as equity in accordance with the substance of the contractual arrangement.

Transaction costs on the issue of equity instruments

Transaction costs arising on the issue of equity instruments are recognised directly in equity as a reduction of the proceeds of the equity instruments to which the costs relate. Transaction costs are the costs that are incurred directly in connection with the issue of those equity instruments and which would not have been incurred had those instruments not been issued.

(u) Extraordinary General Meeting

The Company announced its capital raising exercise and received shareholders approval on a number of initiatives at its Extraordinary General Meeting on 4 October 2005 which were as follows:

- The Company's share capital was consolidated on a 1 for 20 basis.
- The Australian Securities and Investments Commission registered the Company's new name, Advanced Magnesium Limited.
- AML's shareholders approved a placement of up to 50,000,000 new ordinary shares in the company. The Company allotted a total of 32,552,999 shares. In addition, 10,496,996 shares held by Magtrust Pty Ltd were sold to institutional or sophisticated investors. The net proceeds from this sale were distributed to AML.
- The shareholders approved an Employee Share Option Plan and pursuant to this arrangement, AML granted 2,645,650 options to 21 employees including consultants. The exercise price of each option is \$0.31 and has a term of 60 months from the date of issue.
- The shareholders approved the granting of Options to the Managing Director.

The main terms of the options are set out below:

1. Each option will entitle employee to subscribe for one fully paid ordinary share in the capital of Advanced Magnesium Limited upon payment of the exercise price;
2. Each share issued pursuant to the exercise of an option will rank equally in all respects with the shares then on issue; and
3. If the Company goes through a capital reconstruction, the options would be adjusted in accordance with the Listing Rules.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2 RESULTS FROM OPERATIONS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
(a) Revenue				
Revenue from continuing and discontinued operations consisted of the following items:				
Sales Revenue – continuing operations:				
Sale of goods	356,136	74,124	—	—
Rendering of services	7,004	11,257	—	—
	363,140	85,381	—	—
Sales Revenue – discontinuing operations:				
Sale of goods	—	29,093,117	—	14,546,559
Total Sales Revenue	363,140	29,178,498	—	14,546,559
(b) Other income – continuing operations:				
Interest revenue	711,478	400,974	587,320	279,180
Magtrust Pty Ltd proceeds on sale of AML shares	2,077,690	—	2,077,690	—
Foreign exchange gain	106,082	572,626	—	66,053
Gain on sale of assets	69,048	458,542	69,048	3,601
Other	48,160	135,207	34,299	48,753
	3,012,458	1,567,349	2,768,357	397,587
Other income – discontinuing operations:				
Debt forgiveness revenue	—	7,543,377	—	10,638,059
Foreign exchange gain on QMAG sales	—	890,374	—	445,187
	—	8,433,751	—	11,083,246
Total other income	3,012,458	10,001,101	2,768,357	11,480,833
(c) Profit/(loss) before income tax				
Profit/(loss) before income tax has been arrived at after crediting/(charging) the following gains and losses from continuing and discontinued operations:				
Net gain/(loss) on disposal of property, plant and equipment	61,990	366,828	69,048	(104,899)
Gain/(loss) on sale of business	—	5,948,218	—	(3,291,067)
	61,990	6,315,046	69,048	(3,395,966)
Net foreign exchange gains	106,082	1,463,000	—	511,240
Other	—	—	—	—
	168,072	7,778,046	69,048	(2,884,726)
Gains attributable to:				
Continuing operations	175,130	1,031,167	69,048	66,053
Discontinued operations	—	6,838,593	—	445,187
	175,130	7,869,760	69,048	511,240
Losses attributed to:				
Continuing operations	(7,058)	—	—	—
Discontinued operations	—	(91,714)	—	(3,395,966)
	(7,058)	(91,714)	—	(3,395,966)
	168,072	7,778,046	69,048	(2,884,726)
Profit/(loss) before income tax has been arrived at after charging the following expenses. The line items below combine amounts attributable to both continuing operations and discontinued operations:				
Cost of sales	(209,004)	(30,209,433)	—	(15,329,418)
Write-down of inventory to net realisable value	—	(326,000)	—	(163,000)

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2 RESULTS FROM OPERATIONS (cont...)

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Finance costs:				
Interest on loans	—	(1,483,369)	—	(741,632)
Interest on payables	(2,205)	—	(1,729)	—
Finance lease interest expense	—	(213,000)	—	(151,500)
Total interest expenses	(2,205)	(1,696,369)	(1,729)	(893,132)
Borrowing costs amortised	—	(357,736)	—	(178,868)
	(2,205)	(2,054,105)	(1,729)	(1,072,000)
Impairment of non-current asset charge	(467,546)	(3,710,112)	—	(458,544)
Depreciation of non-current assets	(171,616)	(3,205,255)	(26,464)	(1,834,805)
	(639,162)	(6,915,367)	(26,464)	(2,293,349)
Operating lease rental minimum lease payments	(134,186)	(261,242)	—	(87,622)
Employee benefit expense:				
Post employee benefits – defined contribution plans:	(179,944)	(186,615)	(56,549)	(87,128)
Equity settled share-based payments	(490,028)	(5,724)	(490,028)	(5,074)
Retrenchments and termination benefits	(169,631)	(1,063,901)	—	(480,842)
Wages and salaries	(1,884,019)	(2,381,489)	(1,028,398)	(1,124,467)
	(2,723,622)	(3,637,729)	(1,574,975)	(1,697,511)

NOTES TO THE FINANCIAL STATEMENTS

NOTE 3 INCOME TAXES

The aggregate amount of income tax attributable to the financial year differs from the amount calculated on the profit.

	CONSOLIDATED		PARENT ENTITY	
	30 June	30 June	30 June	30 June
	2006	2005	2006	2005
	\$	\$	\$	\$
(a) Income tax recognised in profit and loss				
Tax expense comprises:				
Current tax expense – Australian entities	—	—	—	—
Current tax expense – foreign subsidiaries	97,028	51,321	—	—
Total tax expense	97,028	51,321	—	—
Attributable to:				
Continuing operations	97,028	51,321	—	—
Discontinued operations	—	—	—	—
	97,028	51,321	—	—
The prima facie income tax expense on pre-tax accounting profit from operations reconciles to the income tax expense in the financial statements as follows:				
Loss from continuing operations	(4,745,271)	(7,374,126)	(2,094,494)	(4,185,105)
Profit from discontinued operations (note 28)	4,415,840	7,481,447	—	5,259,228
Profit/(loss) from operations	(329,431)	107,321	(2,094,494)	1,074,123
Income tax benefit/(expense) calculated at 30%	98,829	(32,196)	628,228	(322,237)
Non-deductible expenses	(1,110,529)	(44,456)	(1,079,381)	(501,969)
Deferred tax assets arising from tax losses of the consolidated entity not brought to account as at balance date because realisation is not considered probable	1,108,728	127,973	451,153	824,206
Total tax expense	97,028	51,321	—	—

The tax rate used in the above reconciliation is the corporate tax rate of 30% payable by Australian corporate entities on taxable profits under Australian tax law. There has been no change in the corporate tax rate when compared with the previous reporting period.

	CONSOLIDATED		PARENT ENTITY	
	30 June	30 June	30 June	30 June
	2006	2005	2006	2005
	\$	\$	\$	\$
(b) Current Tax Assets & Liabilities				
Income tax payable by foreign entities	13,859	48,200	—	—
	13,859	48,200	—	—

These amounts are included in note 13 "Current Trade and Other Payables".

Tax Consolidation

Relevance of tax consolidation to the consolidated entity

The company and its wholly-owned Australian resident entities have formed a tax-consolidated group with effect from 1 February 2003 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated group is Advanced Magnesium Limited. The members of the tax-consolidated group are identified at note 26.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 3 INCOME TAXES (cont...)

Nature of tax funding arrangements and tax sharing agreements

Entities within the tax-consolidated group have entered into a tax funding arrangement and a tax-sharing agreement with the head entity. Under the terms of the tax funding arrangement, Advanced Magnesium Limited and each of the entities in the tax-consolidated group has agreed to pay a tax equivalent payment to or from the head entity, based on the current tax liability or current tax asset of the entity. Such amounts are reflected in amounts receivable from or payable to other entities in the tax-consolidated group.

The tax sharing agreement entered into between members of the tax-consolidated group provides for the determination of the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement as payment of any amounts under the tax sharing agreement is considered remote.

Non-recognition of deferred tax assets

Unrecognised deferred tax balances

The following deferred tax assets have not been brought to account as assets:

	CONSOLIDATED/PARENT ENTITY	
	30 June 2006	30 June 2005
	\$	\$
DTA on pre-tax consolidation revenue losses	81,580,882	81,580,882
DTA on post-tax consolidation revenue losses	31,903,944	27,925,849
DTA on capital losses	29,037,675	29,037,675
	142,522,501	138,544,406
These are based on the following tax losses:		
Tax losses – revenue pre-tax consolidation	271,936,272	271,936,272
Tax losses – revenue post-tax consolidation	106,346,481	93,086,163
Tax losses – capital	96,792,251	96,792,251
	475,075,004	461,814,686

The benefit from the deferred tax asset in respect of unused tax losses will only be obtained if:

- (a) The tax consolidated group derives future assessable income of a nature and amount sufficient to enable the benefits to be realised.
- (b) the consolidated group continues to comply with the conditions for deductibility imposed by the tax law; and
- (c) no changes in tax legislation adversely affect the consolidated group in realising the benefit of the losses.

No deferred tax asset has been brought to account as an asset because it is not probable that taxable profit will be available against which such an asset could be utilised.

Unused tax losses incurred after the formation of the AML consolidated group (\$106,346,481) will be fully available to offset future taxable income to the extent AML continues to satisfy the loss integrity rules (i.e. Continuity of Ownership Test and Same Business Test). Based on testing performed by AML and its advisors, these losses should satisfy the loss integrity rules as at 30 June 2006.

Unused tax losses incurred prior to the formation of the AML consolidated group (\$271,936,272) will be subject to restricted use (Available Fraction rules). These restrictions on use are in addition to the loss integrity rules. Broadly, the Available Fraction rules limit the amount of losses that can be used each year by applying the following formula:

$$\text{Available Fraction} \times \text{Taxable income for year} = \text{Pre consolidation losses available for use for year}$$

Based on testing performed by AML and its advisors, AML's pre consolidation losses should satisfy the loss integrity rules at 30 June 2006 subject to further testing and continued compliance with loss integrity rules. No detailed Available Fraction calculations have been performed as at 30 June 2006, however it is unlikely that the Available Fraction applying to pre consolidation tax losses will be greater than 0.2.

The Australian tax consolidated entity has not paid income tax up to 30 June 2006 and no income tax is expected to be paid prior to 30 June 2007. Accordingly, there are no material franking credits available for distribution in the year ending 30 June 2006.

Deferred tax assets and deferred tax liabilities attributable to temporary differences not brought to account are not material.

Tax outside of Australian tax consolidation regime

The Group has several overseas entities which are not subject to Australian tax consolidation and are therefore not sheltered by Australian tax losses. Those entities may incur income tax based on local corporate tax law and are subject to local jurisdiction.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 4 KEY MANAGEMENT PERSONNEL REMUNERATION

The key management personnel of Advanced Magnesium Limited during the year were:

- Dr CD Rawlings (Non-executive Chairman)
- Mr ID Hartnell (Managing Director)
- Mr DM Byrne (Non-executive Director)
- Mr FCH O'Connor (Non-executive Director) (resigned 20 April 2006)
- Mr KG Williams (Non-executive Director)
- Mr G Dunlop (General Manager - Technology Development)
- Mr G Fotheringham (General Manager - East Asia)
- Mr C Kettler (General Manager - Europe)
- Mr PK Nair (General Manager - Corporate)
- Mr T Sweder (General Manager - North America)

(a) Key management personnel remuneration

The aggregate compensation of the key management personnel of the consolidated entity and the Company is set out below:

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Short term employee benefits	1,309,303	1,491,022	576,199	772,988
Post-employment benefits	264,284	120,301	146,523	59,215
Share based payment	373,820	5,724	190,508	4,423
	1,947,407	1,617,047	913,230	836,626

In accordance with Corporations Regulations 2001 – Schedule 5B (regulation 2M.6.04), the disclosures required by paragraphs Aus25.4 to Aus25.6 of AASB 124 “Related Party Disclosures” have been set out in the Remuneration Report on pages 5 to 7 and the disclosures required by paragraph Aus 25.7.2 of AASB 124 have been set out in note 29.

NOTE 5 SHARE-BASED PAYMENT SCHEMES

Details of this note (unless otherwise specified) have been adjusted for the 1 for 20 share consolidation in October 2005. The underlying fair value of share-based payments has not been affected by this. The number of options, exercise price and fair value per option have been amended to reflect the impact of consolidation.

5.1 Employee Share Option Plan

Under the Employee Share Option Plan approved on 4 October 2005, options allowing subscription of up to 5% of the issued share capital of AML are available for issue to employees, with options over a further 5% of the issued share capital in the future based on performance. The total options issued to employees, including those issued to the Managing Director, were 2,645,650.

These are unlisted options exercisable at any time upon payment of the exercise price of \$0.31 and expire in 5 years from issue on 13 October 2010. The binomial model was used to value these options at a total of \$490,028.

5.2 Option Compensation to Pegasus

Pegasus Corporate Advisory Pty Ltd (Pegasus) provided advice and assistance to the Company for the capital raising exercise. Pursuant to this arrangement, Pegasus is entitled to 400,000 options on a post-consolidated basis. The exercise price of each option is \$0.25 and has a term of 36 months from the date of issue. Each option will entitle Pegasus to subscribe for one fully paid ordinary share in the capital of Advanced Magnesium Limited upon payment of the exercise price. These unlisted options are exercisable at any time from the first to the third anniversary of their issue on 7 October 2005. The binomial model was used to value these options at a total of \$64,050.

Each share issued pursuant to the exercise of any option above will rank equally in all respects with the shares then on issue. If the Company goes through a capital reconstruction, the options would be adjusted in accordance with the Listing Rules.

5.3 Resource Capital Funds

As part of the QMAG Sale, Resource Capital Funds were granted 3,313,274 post-consolidation options to acquire fully paid ordinary shares in AMC for a period of up to 36 months from 29 November 2004 at an exercise price of \$0.70 per option. The binomial option valuation model was used to calculate the gross value of these options at \$227,896.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 5 SHARE-BASED PAYMENT SCHEMES (cont...)

The following share-based payment arrangements were in existence during the period:

Options series	Number	Grant date	Expiry date	Exercise price \$	Fair value per option at grant date \$
Rights Issue	2,657,695	15 Jan 2002	31 Jul 2005	\$25.00	nil
Nottacar Investments	150,000	28 Feb 2002	28 Feb 2007	\$12.00	\$5.427
Resource Capital Funds	3,313,273	29 Nov 2004	29 Nov 2007	\$0.70	\$0.069
Employee Share Option Plan	2,645,650	13 Oct 2005	13 Oct 2010	\$0.31	\$0.185
Pegasus Corporate Finance	400,000	7 Oct 2005	7 Oct 2008	\$0.25	\$0.160

The weighted average fair value of the share options granted during the financial year is \$554,078 (2005: \$227,896). Expected volatility is based on the history of five peer group companies over a four year period on a monthly basis up to September 2005.

Inputs into the model	2006		2005
	Option series ESOP	Option series Pegasus	Option series RCF
Grant date share price	\$0.31	\$0.30	\$0.48
Exercise price	\$0.31	\$0.25	\$0.70
Expected volatility	67.48%	67.48%	32.30%
Option life	5 years	3 years	3 years
Dividend yield	Nil	Nil	Nil
Risk-free interest rate	5.25%	5.25%	5.25%

The following table reconciles the outstanding share options granted under the share-based payment schemes at the beginning and end of the financial year (on a post-consolidated adjusted basis).

	2006		2005	
	Number of options	Weighted average exercise price \$	Number of options	Weighted average exercise price \$
Balance at beginning of the financial year	6,120,968	\$11.410	2,807,695	\$24.049
Granted during the financial year	3,045,650	\$0.302	3,313,273	\$0.700
Forfeited during the financial year	—	—	—	—
Exercised during the financial year (i)	—	—	—	—
Expired during the financial year	(2,657,695)	\$25.000	—	—
Balance at end of the financial year (ii)	6,508,923	\$0.664	6,120,968	\$11.410
Exercisable at end of the financial year (iii)	6,108,923	\$0.691	6,120,968	\$11.410

(i) **Exercised during the financial year**

No share options granted under any share-based payment scheme were exercised during the financial year (30 June 2005: nil)

(ii) **Balance at end of the financial year**

The share options outstanding at the end of the financial year had a weighted average exercise price of \$0.664, and a weighted average remaining contractual life of 956 days.

(iii) **Exercisable at end of the financial year**

The Pegasus Corporate Finance options outstanding at the end of the financial year, totalling 400,000, do not vest until the first anniversary of the grant date, which is 7 October 2006.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 6 REMUNERATION OF AUDITORS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Auditor of the parent entity				
Audit or review of the financial report	85,000	102,894	42,500	22,429
	85,000	102,894	42,500	22,429

The auditor of Advanced Magnesium Limited is Deloitte Touche Tohmatsu.

NOTE 7 CURRENT TRADE AND OTHER RECEIVABLES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Trade receivables	140,444	7,445	—	—
Allowance for doubtful debts	—	—	—	—
	140,444	7,445	—	—
Intercompany receivable from AMT	—	—	—	577
Goods and services tax (GST) recoverable	18,535	58,056	944	9,707
Security deposits	50	339,802	50	334,307
CAST CRC R&D receivable	352,000	—	—	—
Project asset sales receivable	141,248	—	—	—
Interest receivable	204,251	36,043	186,925	19,301
Other	23,705	15,955	—	—
	739,789	449,856	187,919	363,892
Total receivables	880,233	457,301	187,919	363,892

NOTE 8 CURRENT INVENTORIES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Finished goods at cost	292,005	—	—	—
	292,005	—	—	—

NOTE 9 OTHER CURRENT ASSETS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Prepayments	119,561	137,706	—	535
Other	—	1,663	—	—
	119,561	139,369	—	535

NOTE 10 NON-CURRENT ASSETS HELD FOR SALE

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Discontinued operations (note 28(b))	—	937,800	—	—
	—	937,800	—	—

NOTE 11 OTHER NON-CURRENT FINANCIAL ASSETS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Shares in controlled entities – unlisted, at cost	—	—	71,767,721	128,555,243
Write down to recoverable amount	—	—	(68,875,631)	(128,555,243)
	—	—	2,892,090	—

NOTES TO THE FINANCIAL STATEMENTS

NOTE 12 PROPERTY, PLANT & EQUIPMENT

	CONSOLIDATED					Total
	Freehold land at fair value	Plant and equipment	Equipment under finance lease at cost	Mine properties & buildings	Mine Plant & equipment	
	\$	\$	\$	\$	\$	\$
Gross carrying amount						
Balance at 7 July 2004	203,172	1,761,915	23,184,544	17,690,888	111,271,747	154,112,266
Additions	—	276,697	43,474	15,114	1,460,351	1,795,636
Disposals	(203,172)	(489,080)	(23,228,018)	(17,706,002)	(112,732,098)	(154,358,370)
Impairment losses charged to Income Statement	—	(814,539)	—	—	—	(814,539)
Balance at 1 July 2005	—	734,993	—	—	—	734,993
Additions	—	176,095	—	—	—	176,095
Disposals	—	(100,571)	—	—	—	(100,571)
Net foreign currency exchange differences	—	1,580	—	—	—	1,580
Balance at 30 June 2006	—	812,097	—	—	—	812,097
Accumulated depreciation/ amortisation and impairment						
Balance at 7 July 2004	—	831,940	8,164,430	10,382,328	76,381,568	95,760,266
Disposals	—	(428,057)	(9,012,895)	(10,673,675)	(78,244,774)	(98,359,401)
Impairment losses charged to Income Statement	—	(320,799)	—	—	—	(320,799)
Depreciation expense	—	202,237	848,465	291,347	1,863,206	3,205,255
Balance at 1 July 2005	—	285,321	—	—	—	285,321
Disposals	—	(70,849)	—	—	—	(70,849)
Impairment losses charged to Income Statement (i)	—	45,016	—	—	—	45,016
Depreciation expense	—	171,676	—	—	—	171,676
Net foreign currency exchange differences	—	1,158	—	—	—	1,158
Balance at 30 June 2006	—	432,322	—	—	—	432,322
Net book value						
As at 30 June 2005	—	449,672	—	—	—	449,672
As at 30 June 2006	—	379,775	—	—	—	379,775

- (i) Impairment losses are included in the line item "Impairment of non-current assets charge" in note 2. The impairment losses recognised during the financial year ended 30 June 2005 relate to property, plant and equipment used by the AML Group. This resulted from a periodic review by management of fixed assets during the financial year. The amount of the write down is based on management's assessment of the condition and fair value of assets.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 12 PROPERTY, PLANT & EQUIPMENT (cont...)

	PARENT ENTITY					Total
	Freehold land at fair value	Plant and equipment	Equipment under finance lease at cost	Mine properties & buildings	Mine Plant & equipment	
	\$	\$	\$	\$	\$	\$
Gross carrying amount						
Balance at 7 July 2004	—	1,285,201	21,510,520	8,845,444	55,633,755	87,274,920
Additions	—	787	21,737	7,557	732,295	762,376
Disposals	—	(241,469)	(21,532,257)	(8,853,001)	(56,366,050)	(86,992,777)
Impairment losses charged to Income Statement	—	(747,251)	—	—	—	(747,251)
Balance at 1 July 2005	—	297,268	—	—	—	297,268
Additions	—	—	—	—	—	—
Disposals	—	(61,263)	—	—	—	(61,263)
Balance at 30 June 2006	—	236,005	—	—	—	236,005
Accumulated depreciation/ amortisation and impairment						
Balance at 7 July 2004	—	580,633	7,939,339	5,191,164	38,190,784	51,901,920
Disposals	—	(232,722)	(8,593,709)	(5,336,838)	(39,122,387)	(53,285,656)
Impairment losses charged to Income Statement	—	(288,706)	—	—	—	(288,706)
Depreciation expense	—	103,158	654,370	145,674	931,603	1,834,805
Balance at 1 July 2005	—	162,363	—	—	—	162,363
Disposals	—	(40,761)	—	—	—	(40,761)
Depreciation expense	—	26,464	—	—	—	26,464
Balance at 30 June 2006	—	148,066	—	—	—	148,066
Net book value						
As at 30 June 2005	—	134,906	—	—	—	134,906
As at 30 June 2006	—	87,939	—	—	—	87,939

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Aggregate depreciation allocated, whether recognised as an expense or capitalised as part of the carrying amount of other assets during the year:				
Plant and equipment	171,676	202,237	26,464	103,158
Equipment under finance lease	—	848,465	—	654,370
Mine properties and buildings	—	291,347	—	145,674
Mine plant and equipment	—	1,863,206	—	931,603
	171,676	3,205,255	26,464	1,834,805

NOTES TO THE FINANCIAL STATEMENTS

NOTE 13 CURRENT TRADE AND OTHER PAYABLES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Trade payables and accruals	381,647	671,752	96,212	71,595
Intercompany payable to AMT	—	—	—	73,460
CAST CRC R&D payable	363,000	—	—	—
Other	14,800	—	—	—
	759,447	671,752	96,212	145,055

NOTE 14 CURRENT PROVISIONS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Employee benefits	136,965	166,233	42,001	40,877
	136,965	166,233	42,001	40,877

NOTE 15 OTHER CURRENT LIABILITIES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Unamortised fitout incentive	15,800	—	—	—
	15,800	—	—	—

NOTE 16 NON-CURRENT TRADE AND OTHER PAYABLES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Licence and fees payable	—	4,838,370	—	—
	—	4,838,370	—	—

NOTE 17 NON-CURRENT PROVISIONS

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Employee benefits	173,538	188,231	170,528	169,806
	173,538	188,231	170,528	169,806

NOTE 18 OTHER NON-CURRENT LIABILITIES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006	30 June 2005	30 June 2006	30 June 2005
	\$	\$	\$	\$
Unamortised fitout incentive	63,200	—	—	—
	63,200	—	—	—

NOTES TO THE FINANCIAL STATEMENTS

NOTE 19 SHARE CAPITAL

	CONSOLIDATED		PARENT ENTITY	
	30 June	30 June	30 June	30 June
	2006	2005	2006	2005
	\$	\$	\$	\$
85,506,292 fully paid ordinary shares				
(2005: 1,058,994,616 pre-consolidation) (i)	892,648,210	883,446,314	892,648,210	883,446,314
Rights issue expire 31 July 2005 (ii)	—	—	—	—
Nottacar options expire 28 Feb 2007 (iii)	814,000	814,000	814,000	814,000
RCF options expire 29 Nov 2007 (iv)	227,896	227,896	227,896	227,896
Pegasus options expire 7 Oct 2008 (iv)	64,050	—	64,050	—
ESOP options expire 12 Oct 2010 (iv)	490,028	—	490,028	—
	894,244,184	884,488,210	894,244,184	884,488,210

Changes to the then Corporations Law abolished the authorised capital and par value concept in relation to share capital from 1 July 1998. Therefore, the Company does not have a limited amount of authorised capital and issued shares do not have a par value.

On 4 October 2005, the shareholders approved a 1 for 20 share consolidation of AML's ordinary shares. The details (including comparatives) in this note and elsewhere in this financial report, have been adjusted for this consolidation unless otherwise stated.

In the previous financial year, management determined that deferred Joint Lead Manager (JLM) fees in relation to the November 2001 offer of Distribution Entitled Securities previously classed as a current payable are more appropriately disclosed as equity. Each Joint Lead Manager (JLM) of the November 2001 offer of Distribution Entitled Securities has waived their right to receive their share of a cash payment of \$2,500,000 for fees. However, each JLM may severally elect to receive shares in the Company, calculated at \$12.16 per share, in lieu of their portion of the deferred fees. Based on this information, the total shares issuable by the Company at November 2001 was 205,592. The number of shares issuable increases by a factor of 1.2 for each twelve month period from 31 January 2003 that the fees remain outstanding. At 30 June, 2006, the number of shares issuable by the Company was 355,264 (30 June 2005: 296,053).

- (i) Fully paid ordinary shares carry one vote per share and carry the right to dividends.
- (ii) The exercise price was \$25.00 (on a post-consolidated basis). Each option expired on 31 July 2005. These options were issued for no cash consideration and were listed on the ASX.
- (iii) On 28 February 2002 a loan establishment fee of \$814,000 for the 2001 Facility with Newmont Finance Limited (a Newmont Australia Limited subsidiary) was paid by the issue of 150,000 post-consolidated options to Nottacar Investments Pty Ltd (a Newmont Australia Limited subsidiary) under the 2001 Subscription Deed, approved by shareholders on 28 February 2002. Each option will entitle Nottacar to subscribe for one share. Each option may be exercised up to 28 February 2007. The exercise price of each option is \$12.00 (on a post consolidation basis). These options are not listed on the ASX.
- (iv) Details of these options are located at note 5.

	CONSOLIDATED / PARENT ENTITY			
	2006		2005	
	No.	\$	No.	\$
Fully paid ordinary shares				
Balance at beginning of financial year	1,058,994,616	883,446,314	1,058,994,616	883,446,314
Share consolidation (note 1(u))	(1,006,041,323)	—	—	—
Issue of shares under placement in October 2005 (note 1(u))	32,552,999	9,765,900	—	—
Transaction costs on issue of shares	—	(564,004)	—	—
Balance at end of financial year	85,506,292	892,648,210	1,058,994,616	883,446,314

Fully paid ordinary shares carry one vote per share and carry the right to dividends

Share options

All share options carry no rights to dividends and no voting rights until paid for conversion into ordinary shares. Further details of the share-based payment schemes are contained in note 5 to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 20 RESERVES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Capital reserve	2,749,980	2,749,980	—	—
	2,749,980	2,749,980	—	—
Foreign currency translation reserve				
Balance at beginning of financial year	—	—	—	—
Translation of foreign operations	30,320	—	—	—
Balance at end of financial year	30,320	—	—	—
Total reserves	2,780,300	2,749,980	—	—

The capital reserve is a historical reserve from 2002 that arose after calculation of the outside equity interest in the (as it then was) Advanced Magnesium Investments Pty Ltd consolidated entity.

The foreign currency translation reserve is a result of translating overseas subsidiaries from their functional currency to the presentation currency of Australian dollars.

NOTE 21 ACCUMULATED LOSSES

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Balance at beginning of financial year	(883,966,260)	(884,022,259)	(879,917,570)	(880,991,693)
Net profit/(loss) attributable to members of the parent entity	(426,459)	55,999	(2,094,494)	1,074,123
Balance at end of financial year	(884,392,719)	(883,966,260)	(882,012,064)	(879,917,570)

NOTES TO THE FINANCIAL STATEMENTS

NOTE 22 EARNINGS/(LOSS) PER SHARE

Basic earnings/(loss) per share:

From continuing operations
From discontinued operations
Total basis earnings/(loss) per share

Diluted earnings/(loss) per share:

From continuing operations (i)
From discontinued operations
Total diluted earnings/(loss) per share (i)

CONSOLIDATED ENTITY	
2006	2005
cents per share	cents per share
(6.304)	(14.024)
5.749	14.129
(0.555)	0.105
(6.304)	(14.024)
5.719	14.050
(0.555)	0.026

- (i) As EPS is a loss per share for 2006, any potential ordinary shares would be anti-dilutive. As a result, loss per share is identical for basic and diluted EPS calculations.

Basic earnings/(loss) per share

The earnings and weighted average number of ordinary shares used in the calculation of basic earnings/(loss) per share are as follows:

	NOTE	2006	2005
		\$	\$
Earnings/(losses)	(a)	(426,459)	55,999
Earnings/(losses) from continuing operations	(a)	(4,842,299)	(7,425,448)
Weighted average number of ordinary shares for the purposes of basic earnings/(loss) per share.		76,817,284	52,953,293

- (a) Earnings/(losses) used in the calculation of total basic earnings/(losses) per share and basic earnings/(losses) per share from continuing operations reconciles to net profit/(loss) in the income statement as follows:

CONSOLIDATED ENTITY	
30 June 2006	30 June 2005
\$	\$
Net profit/(loss)	(426,459) 55,999
Earnings/(losses) used in the calculation of basic EPS	(426,459) 55,999
Adjustments to exclude profit for the period from discontinued operations	(4,415,840) (7,481,447)
Losses used in the calculation of basic EPS from continuing operations	(4,842,299) (7,425,448)

Diluted earnings/(losses) per share

The earnings/(losses) and weighted average number of ordinary shares used in the calculation of diluted earnings/(losses) per share are as follows:

	NOTE	2006	2005
		\$	\$
Earnings/(losses)	(a)	(426,459)	55,999
Losses from continuing operations	(a)	(4,842,299)	(7,425,448)
Weighted average number of ordinary shares for the purposes of diluted earnings/(losses) per share	(b),(c),(d)	77,211,694	53,249,346

- (a) Earnings/(losses) used in the calculation of total diluted earnings/(losses) per share and diluted earnings/(losses) per share from continuing operations reconciles to net profit/(loss) in the income statement as follows:

CONSOLIDATED ENTITY	
2006	2005
\$	\$
Net profit/(loss)	(426,459) 55,999
Earnings/(losses) used in the calculation of diluted EPS	(426,459) 55,999
Adjustments to exclude profit for the period from discontinued operations	(4,415,840) (7,481,447)
Losses used in the calculation of diluted EPS from continuing operations	(4,842,299) (7,425,448)

NOTES TO THE FINANCIAL STATEMENTS

NOTE 22 EARNINGS/(LOSS) PER SHARE (cont...)

- (b) The weighted average number of ordinary shares for the purposes of diluted earnings/(losses) per share reconciles to the weighted average number of ordinary shares used in the calculation of basic earnings/(losses) per share as follows:

	CONSOLIDATED	
	2006 No.	2005 No.
Weighted average number of ordinary shares used in the calculation of basic EPS	76,817,284	52,953,293
Shares deemed to be issued for no consideration in respect of:		
Pegasus Corporate Finance options	39,146	—
Share based fees for JLM	355,264	296,053
Weighted average number of ordinary shares used in the calculation of diluted EPS	77,211,694	53,249,346

- (c) The following potential ordinary shares are not dilutive and are therefore excluded from the weighted average number of ordinary shares for the purposes of diluted earnings/(losses) per share:

	2006	2005
	\$	\$
Non-renounceable rights issue	—	2,657,133
Nottacar Investments Pty Ltd options	150,000	150,000
Resource Capital Funds III LP options	3,313,273	3,313,273
Employee Share Option Plan options	2,645,650	—
	6,108,923	6,120,406

- (d) There were no converted, lapsed, or cancelled potential ordinary shares included in the calculation of diluted earnings/(losses) per share.

NOTE 23 COMMITMENTS FOR EXPENDITURE

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Capital expenditure commitments				
<u>Fitout and associated assets</u>				
Not longer than 1 year	—	57,514	—	—
Longer than 1 year and not longer than 5 years	—	—	—	—
Longer than 5 years	—	—	—	—
	—	57,514	—	—

Lease commitments

Non-cancellable operating lease commitments are disclosed in note 25 to the financial statements.

NOTE 24 CONTINGENT LIABILITIES AND CONTINGENT ASSETS

- (i) Under the CSIRO Research Agreement, CSIRO engaged the Company's wholly-owned subsidiary, Advanced Magnesium Technologies Pty Ltd, to conduct further research into production of magnesium from magnesite, and provided AMT with \$50,000,000 of cash funding in two tranches (December 2001 and December 2002).

If commercial production were to commence, AMT would be obliged to pay production royalties of a minimum value of \$75,000,000 over the first twenty years. AMT would recognise a liability for the present value of this amount upon commencement of commercial magnesium metal production, based on production forecasts current at that time.

With the decision to terminate the Stanwell Magnesium Project there is no future royalty obligations at Balance Date.

- (ii) Advanced Magnesium Technologies Pty Ltd, a wholly-owned subsidiary of AML, had entered into a contract with IMS Experts-Conseils, Inc (IMS) a Canadian corporation, for the licensing of technology to AMT for the Stanwell Magnesium Project. IMS claimed licensing fee instalments due on dates after the contract terminated. Export Development Canada

NOTES TO THE FINANCIAL STATEMENTS

NOTE 24 CONTINGENT LIABILITIES AND CONTINGENT ASSETS (cont...)

(EDC) a Canadian Government entity, is a provider of trade credit insurance and insured IMS on accounts receivable under its contract with AMT. EDC has advised it paid an amount of C\$410,000 (A\$439,000) to IMS and now claims that amount from AMT as IMS has assigned its rights to EDC.

This contingent liability was first disclosed in the 31 December 2003 half year report and there has been no further contact since the date of publishing that report. The Directors continue to believe neither IMS, nor EDC as the assignee of IMS' rights, has a valid claim against AMT. AMT will defend any such claim if action is taken against it.

- (iii) As part of the QMAG Sale Agreement, AML has agreed that if it is able to structure a Finance Co-operation Agreement that generates additional value to AML, AML will pay to RCF an amount equal to 25% of that additional value generated as such value is realised. This agreement expires 36 months after the QMAG date of completion on 1 December 2004.

NOTE 25 LEASES

Operating Lease Arrangements

Office Premises – Brisbane, Australia (six year lease from July 2005 with an option to extend for another three years).

Internet – Brisbane, Australia (two year lease from April 2005 for internet services).

Office Premises – Heidelberg, Germany (five year lease from March 2006 with an option to extend for another three years).

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Non-cancellable operating lease payments in respect of premises				
Not longer than 1 year	190,253	106,213	132,217	106,213
Longer than 1 year and no longer than 5 years	379,398	510,073	135,365	510,073
Longer than 5 years	—	152,268	—	152,268
	569,652	768,554	267,582	768,554
In respect of non-cancellable operating leases the following liabilities have been recognised:				
Current: Fitout incentives (note 15)	15,800	—	—	—
Non-current: Fitout incentives (note 18)	63,200	—	—	—
	79,000	—	—	—

NOTE 26 SUBSIDIARIES

Name of entity	Country of Incorporation	Ownership interest 2006 %	Ownership interest 2005 %
<u>Parent entity</u>			
Advanced Magnesium Limited	Australia		
<u>Subsidiaries</u>			
Australian Magnesium Investments Pty Ltd	Australia	100%	100%
Advanced Magnesium Technologies Pty Ltd (a)	Australia	100%	100%
AM Technologies Pty Ltd (b)	Australia	100%	100%
AMC Magmetal Pty Ltd (c)	Australia	—	100%
AMC People Services Pty Ltd	Australia	100%	100%
AMT North America, Inc (d)	USA	100%	100%
Australian Magnesium Europe BV	Netherlands	100%	100%
AMT Europe GmbH (e)	Germany	100%	100%

- (a) Renamed from Australian Magnesium Operations Pty Ltd on 12 January 2005
 (b) Renamed from MG Magnesium Pty Ltd on 12 January 2005
 (c) Deregistered on 7 August 2005
 (d) Renamed from AMC North America, Inc on 20 January 2005 (Delaware) and 31 January 2005 (Kentucky)
 (e) Renamed from Australian Magnesium Europe GmbH on 30 May 2006

NOTES TO THE FINANCIAL STATEMENTS

NOTE 27 SEGMENT INFORMATION

Products and services within each geographical segment

For management purposes, the consolidated entity is organised into three major operating divisions – Europe, North America and Asia Pacific and one corporate division including Australia. These divisions are the basis on which the consolidated entity reports its primary segment information. The principal products and services of each of these divisions comprise the business segments as follows:

- Magnesium alloys including AM-lite, AM-HP2, AM-SC1 and AM-cast;
- Magnesium handling technologies including AM-cover and AM-converter;
- Magnesium consulting activities; and
- Magnesite mining previously with the QMAG operating division (now sold).

The costs of corporate, finance and administration for the Group are managed by the parent entity at the head office in Brisbane, Australia.

Intersegment revenue

The activities of AMT Europe GmbH and AMT North America, Inc. are carried out in their respective regions as agents of Advanced Magnesium Technologies Pty Ltd. These overseas entities charge AMT, an agency fee equivalent to 107.5% of costs incurred.

	Europe		North America		Asia Pacific		Australia		Total	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
<i>Continuing Operations</i>										
Revenue from external customers	268,501	78,802	9,162	—	85,477	6,579	—	—	363,140	85,381
Intersegment revenue	1,560,074	1,471,283	556,570	361,306	—	—	(2,116,644)	(1,832,589)	—	—
Total sales revenue	1,828,575	1,550,085	565,732	361,306	85,477	6,579	(2,116,644)	(1,832,589)	363,140	85,381
Other income	2,059	657	—	1,400	—	—	2,123,791	133,152	2,125,850	135,209
Foreign exchange gain	—	—	—	—	—	—	106,082	572,626	106,082	572,626
Gain on sale of assets	—	—	—	—	—	—	69,048	458,542	69,048	458,542
Interest revenue	1,192	118	—	—	—	—	710,286	400,855	711,478	400,973
Gross expenditure	(1,474,043)	(1,589,645)	(561,460)	(330,854)	(417,363)	—	(5,668,003)	(7,106,359)	(8,120,869)	(9,026,858)
Continuing operations Profit/(Loss) before tax	357,783	(38,785)	4,272	31,852	(331,886)	6,579	(4,775,440)	(7,373,773)	(4,745,271)	(7,374,127)
Income tax	(97,028)	(51,321)	—	—	—	—	—	—	(97,028)	(51,321)
Continuing Operations Profit/(Loss) after tax	260,755	(90,106)	4,272	31,852	(331,886)	6,579	(4,775,440)	(7,373,773)	(4,842,299)	(7,425,448)
<i>Discontinuing Operations</i>										
Discontinuing operations Profit/(Loss) before tax	—	(1,273,939)	—	(212,958)	—	(1,538,149)	4,415,840	10,506,493	4,415,840	7,481,447
Income tax	—	—	—	—	—	—	—	—	—	—
Discontinuing Operations Profit/(Loss) after tax	—	(1,273,939)	—	(212,958)	—	(1,538,149)	4,415,840	10,506,493	4,415,840	7,481,447
Net result	260,755	(1,364,045)	4,272	(181,106)	(331,886)	(1,531,570)	(359,600)	3,132,720	(426,459)	55,999

	Europe		North America		Asia Pacific		Australia		Total	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Segment Assets										
Total assets	481,322	441,507	168,608	130,416	—	—	13,130,785	8,564,593	13,780,715	9,136,516
Segment Liabilities										
Total liabilities	(170,120)	(280,097)	(43,653)	(14,638)	—	—	(935,178)	(5,569,851)	(1,148,951)	(5,864,586)
Segment Disclosures										
Acquisition of segment fixed assets	—	31,694	13,758	—	—	—	86,813	1,763,942	100,571	1,795,636
Depreciation and amortisation	17,232	1,181	4,585	2,702	—	—	149,859	248,354	171,676	252,237
Credit on reversal of licencing liability	—	—	—	—	—	—	(4,838,370)	—	(4,838,370)	—
Impairment losses	—	—	—	—	—	—	467,546	493,740	467,546	493,740
Non-cash share based payments	—	—	—	—	—	—	554,078	227,896	554,078	227,896

Segment disclosures by business segment

	Magnesium alloys		Metal Handling		Consulting		Magnesite		Total	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Revenue from external customers	171,768	6,579	181,875	35,144	9,497	43,658	—	27,642,118	363,140	27,727,499
Segment fixed assets	379,775	449,672	—	—	—	—	—	—	379,775	449,672
Acquisition of segment fixed assets	100,571	—	—	276,697	—	—	—	1,518,939	100,571	1,795,636

NOTES TO THE FINANCIAL STATEMENTS

NOTE 28 DISCONTINUED OPERATIONS

QMAG Joint Venture operations

The magnesia operation produced raw magnesite and calcined, deadburned and electrofused magnesia, and marketed this predominantly to steel refractory, agricultural and general chemical industries. In the previous financial year on 1 December 2004, AML and its related subsidiaries disposed of the QMAG business and associated assets to Resource Capital Fund III L.P. ("RCF").

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
(a) Financial performance information relating to the QMAG operations		
Revenue	—	37,526,868
Expenses	—	(32,356,906)
Profit before income tax	—	5,169,962
Income tax expense	—	—
Profit after income tax	—	5,169,962
Cash flow information relating to the QMAG operations		
Net cash inflow from operating activities	—	922,000
Net cash outflow from investing activities	—	(832,000)
Net cash outflow from financing activities	—	(137,000)
Total cash outflow	—	(47,000)
Other disclosures required regarding discontinuation of the QMAG operations		
Carrying amount/net settling price of assets, including effect of ANZ loan	—	76,000
Gain on sale of QMAG operations	—	5,959,683
Income tax attributable to gain on sale	nil	nil

(b) Stanwell Magnesium Plant

The Magnesium Primary Production business was being pursued through the Stanwell Magnesium Project (SMP) and involved the development and construction of a 97,000 tonne per annum magnesium metal and alloy plant at Stanwell in Central Queensland. The Annual Report for the year ended 6 July 2004 outlined at Note 5 the shareholders' decision to terminate the Stanwell Magnesium Project.

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
Financial performance information for the years ended 30 June 2006 and 30 June 2005		
Revenue	—	—
Expenses	(422,530)	(3,636,735)
Credit on grant of Engineering Technology licence related to settlement of licensing payable	4,838,370	—
Profit/(Loss) before income tax	4,415,840	(3,636,735)
Income tax expense	—	—
Profit/(Loss) after income tax	4,415,840	(3,636,735)
Carrying amount of assets and liabilities at 30 June 2006 and 30 June 2005		
Receivables	—	—
Property, plant and equipment	—	937,800
Total Assets	—	937,800
Payables	—	4,838,370
Provisions	—	—
Total Liabilities	—	4,838,370

NOTES TO THE FINANCIAL STATEMENTS

NOTE 28 DISCONTINUED OPERATIONS (cont...)

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
Net Liabilities	—	(3,900,570)
Cash flow information for the years ended 30 June 2006 and 30 June 2005		
Net cash outflow from operating activities	—	(325,698)
Net cash inflow from investing activities	515,270	1,375,974
Net cash inflow/(outflow) from financing activities	—	—
Total cash inflow	515,270	1,050,276

NB: cash balances subsumed within group and not shown separately as Stanwell Magnesium Project cash.

On 29 September 2005, the Advanced Magnesium Limited Group agreed to grant Alcan International Limited an exclusive licence to use and to sub-licence the Engineering Technology which AML developed for the Stanwell Magnesium Project. This transaction extinguished the last remaining liability related to the SMP. The Group retains access to the technology it has developed over many years.

(c) Icelandic Magnesium Company Limited

On 31 August 2004, the Group sold the entire share capital in Icelandic Magnesium Company Limited. There were no operations in the period to disposal on 31 August 2004.

	CONSOLIDATED	
	30 June	30 June
	2006	2005
	\$	\$
Loss on sale of IMC	—	(11,465)

Further details for this sale are at note 30(b).

NOTES TO THE FINANCIAL STATEMENTS

NOTE 29 RELATED PARTY DISCLOSURES

(a) Equity interests in related parties

Equity interest in subsidiaries

Details of the percentage of ordinary shares held in subsidiaries are disclosed in note 26 to the financial statements.

(b) Key Management Personnel Remuneration

Details of key management personnel remuneration are disclosed in note 4 to the financial statements.

(c) Key Management Personnel Equity Holdings (on a post-consolidated basis)

Fully paid ordinary shares of Advanced Magnesium Limited - 2006

	Balance @ 1/7/05	Granted as remuneration	Received on exercise of options	Net other change	Balance @ 30/6/06	Balance held nominally
	No.	No.	No.	No.	No.	No.
Dr CD Rawlings	5,000	—	—	—	5,000	—
Mr ID Hartnell	9,100	—	—	6,800	15,900	—
Mr DM Byrne	—	—	—	100,000	100,000	100,000
Mr FCH O'Connor * (resigned 20 Apr 06)	9,596	—	—	(9,596)*	—	—
Mr KG Williams	—	—	—	15,000	15,000	—
Mr G Dunlop	320	—	—	—	320	—
Mr G Fotheringham	256	—	—	—	256	—
Mr C Kettler	—	—	—	—	—	—
Mr PK Nair	907	—	—	193	1,100	—
Mr T Sweder	—	—	—	—	—	—
	25,179	—	—	112,397	137,576	100,000

* Balance at date of resignation

Fully paid ordinary shares of Advanced Magnesium Limited - 2005

	Balance @ 7/7/04	Granted as remuneration	Received on exercise of options	Net other change	Balance @ 30/6/05	Balance held nominally
	No.	No.	No.	No.	No.	No.
Dr CD Rawlings *	5,000	—	—	—	5,000	—
Mr ID Hartnell	600	8,500	—	—	9,100	—
Mr FCH O'Connor *	9,596	—	—	—	9,596	—
Mr JD Story * (resigned 4 May 05)	12,794	—	—	(12,794)	—	—
Mr KG Williams *	—	—	—	—	—	—
						10,496,996*
Mr G Dunlop	320	—	—	—	320	—
Mr P Nair	907	—	—	—	907	—
Mr AD Roughead	740	2,500	—	(3,240)	—	—
	29,957	11,000	—	(16,034)	24,923	10,496,996*

* Each of the four Non-Executive Directors held one share with a value of \$1 in Magtrust Pty Ltd at 30 June 2005. The entire balance of shares held by Magtrust Pty Ltd in AML were sold as part of the transaction outlined at note 1(u).

NOTES TO THE FINANCIAL STATEMENTS

NOTE 29 RELATED PARTY DISCLOSURES (cont...)

Share options of Advanced Magnesium Limited - 2006

	Bal @ 1/7/05	Granted as remuneration	Exer- cised	Net other change	Bal @ 30/06/06	Bal vested @ 30/06/06	Vested but not exerci- sable	Vested and exerci- sable	Options vested during year
	No.	No.	No.	No.	No.	No.	No.	No.	No.
Mr ID Hartnell	50	656,000	—	(50)	656,000	656,000	—	656,000	656,000
Mr G Dunlop	—	394,625	—	—	394,625	394,625	—	394,625	394,625
Mr G Fotheringham	—	164,375	—	—	164,375	164,375	—	164,375	164,375
Mr C Kettler	—	281,875	—	—	281,875	281,875	—	281,875	281,875
Mr PK Nair	32	373,775	—	(32)	373,775	373,775	—	373,775	373,775
Mr T Sweder	—	150,000	—	—	150,000	150,000	—	150,000	150,000
	82	2,020,650	—	(82)	2,020,650	2,020,650	—	2,020,650	2,020,650

Share options of Advanced Magnesium Limited - 2005

	Bal @ 7/7/04	Granted as remuneration	Exer- cised	Net other change	Bal @ 30/06/05	Bal vested @ 30/06/05	Vested but not exerci- sable	Vested and exerci- sable	Options vested during year
	No.	No.	No.	No.	No.	No.	No.	No.	No.
Mr ID Hartnell	50	—	—	—	50	—	—	—	—
Mr PK Nair	32	—	—	—	32	—	—	—	—
	82	—	—	—	82	—	—	—	—

All share options issued to key management personnel and executives during the financial year were made in accordance with the provisions of the Employee Share Option Plan.

During the financial year, no options were exercised by key management personnel.

Further details of the Employee Share Option Plan and of share options granted during the financial year is contained in notes 4 and 5 to the financial statements.

(d) Director related party disclosures

	CONSOLIDATED		PARENT ENTITY	
	30 June 2006 \$	30 June 2005 \$	30 June 2006 \$	30 June 2005 \$
Fees paid to Corrs Chambers Westgarth, a firm which provides legal services to the Company and consolidated entity, and of which Mr John Story is a partner, during the period Mr Story has been a director of the Company. Mr Story resigned as Director on 4 May 2005 and therefore the payments captured are to this date only. These transactions were conducted on normal commercial terms and conditions.	—	200,308	—	135,135
Amounts outstanding at balance date:				
Current payable				
- to Gryphon Partners Pty Ltd (as directors' fees for Mr Creagh O'Connor; Mr O'Connor resigned as a Director on 20 April 2006)	—	3,539	—	3,539
- to Corrs Chambers Westgarth	—	17,644	—	—

NOTES TO THE FINANCIAL STATEMENTS

NOTE 29 RELATED PARTY DISCLOSURES (cont...)

(e) Wholly owned group

The parent entity in the wholly-owned group is Advanced Magnesium Limited.

Members of the wholly-owned group are set out in Note 26. Transactions between the parent entity and controlled entities consist of:

	NOTE	PARENT ENTITY	
		30 June	30 June
		2006	2005
		\$	\$
Other amounts receivable from controlled entities:			
Current receivable (net of provision)	7	—	577
Amounts payable to controlled entities:			
Current payable	13	—	73,460

Transactions during the financial year between the parent entity and other entities in the wholly-owned group included:

- Investment in controlled entities;
- Advance of interest free funds to controlled entities;
- Repayment of interest free funds from controlled entities to the parent entity;
- Incurring expenditure on behalf of other entities for office rental and related costs, travel costs, seconded employees and other sundry costs. (The entity is fully reimbursed for these costs on an actual cost basis); and
- Intercompany debt forgiveness in the year ended 30 June 2005

Transactions involving the parent entity

During the financial year, Advanced Magnesium Limited provided accounting and administration services to its subsidiaries for no consideration.

During the financial year, Advanced Magnesium Limited contributed \$56,549 (2005: \$87,128) to its defined contribution plan.

Parent entity

The ultimate Australian parent entity in the consolidated entity is Advanced Magnesium Limited.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 30 NOTES TO THE CASH FLOW STATEMENT

	CONSOLIDATED		PARENT ENTITY	
	2006	2005	2006	2005
	\$	\$	\$	\$
(a) Reconciliation of cash and cash equivalents				
For the purposes of the cash flow statement, cash and cash equivalents includes cash on hand and in banks and investments in money market instruments. Cash and cash equivalents at the end of the financial year as shown in the cash flow statement is reconciled to the related items in the balance sheet as follows:				
Cash and cash equivalents	12,109,140	7,152,374	9,372,913	4,427,045
(b) Business disposed				
During the previous financial year, on 31 August 2004 the consolidated entity sold the entire share capital in Icelandic Magnesium Company Limited. Details of the disposal are as follows:				
Consideration				
Cash and cash equivalents	—	658,775	—	—
	—	658,775	—	—
Book value of net assets sold				
Current assets:				
Cash	—	992,240	—	—
Receivables	—	35,683	—	—
Current liabilities:				
Payables	—	(11,772)	—	—
Net assets disposed	—	1,016,151	—	—
Minority interest	—	(345,911)	—	—
Loss on disposal	—	(11,465)	—	—
	—	658,775	—	—
Net cash inflow/(outflow) on disposal				
Cash and cash equivalents				
Consideration	—	658,775	—	—
Less cash and cash equivalent				
Balances disposed	—	(992,240)	—	—
	—	(333,465)	—	—
During the previous financial year, on 1 December 2004 the consolidated entity disposed of QMAG business. Details of the disposal are as follows:				
Consideration				
Net cash and cash equivalents	—	65,037,248	—	28,555,996
	—	65,037,248	—	28,555,996
Book value of net assets sold				
Current assets:				
Cash	—	2,065,000	—	1,032,511
Receivables	—	10,565,204	—	4,012,320
Inventory	—	25,781,000	—	12,890,542
Other current assets	—	1,513,000	—	741,474
Non-current assets:				
Property, plant and equipment	—	55,721,172	—	33,773,122
Other non-current assets	—	3,239,000	—	1,197,296

NOTES TO THE FINANCIAL STATEMENTS

NOTE 30 NOTES TO THE CASH FLOW STATEMENT (cont...)

	CONSOLIDATED		PARENT ENTITY	
	2006	2005	2006	2005
	\$	\$	\$	\$
Current liabilities:				
Payables	—	(12,474,000)	—	(6,237,229)
Interest-bearing liabilities	—	(3,229,000)	—	(1,614,304)
Provisions	—	(2,829,000)	—	(1,414,368)
Other current liabilities	—	(7,289,000)	—	(3,644,387)
Non-current liabilities:				
Payables	—	(42,000)	—	(20,759)
Interest-bearing liabilities	—	(3,521,000)	—	(3,236,013)
Provisions	—	(4,639,000)	—	(2,319,220)
Other non-current liabilities	—	(3,587,000)	—	(1,793,821)
Net assets disposed	—	61,274,376	—	33,367,164
Other disclosures				
Options granted	—	227,896	—	227,896
Gain/(loss) on disposal	—	5,959,683	—	(3,488,159)
Net cash inflow on disposal				
Cash and cash equivalents	—	67,102,248	—	29,588,507
Less cash and cash equivalent	—	(2,065,000)	—	(1,032,511)
Balances disposed	—	65,037,248	—	28,555,996
(c) Non-cash financing and investing activities				
There were no non-cash financing or investing activities other than those disclosed elsewhere in this financial report.				
(d) Cash balances not available for use				
The AML Group has \$483,228 as cash collateralised guarantees for its premises lease and payroll obligations.				
(e) Reconciliation of profit for the period to net cash flows from operating activities				
Profit/(Loss) after income tax	(426,459)	55,999	(2,094,494)	1,074,123
Depreciation & amortisation expense	171,676	2,931,238	26,464	1,697,796
Depreciation charged to inventory	—	(277,391)	—	(357,977)
Loss/(gain) on disposal of QMAG	—	(5,959,683)	—	3,488,159
Loss/(gain) on disposal of plant & equipment	(61,990)	(458,542)	(69,048)	104,899
Loss/(gain) on disposal of project assets	—	91,714	—	—
Loss/(gain) on disposal of Icelandic Magnesium Corporation	—	11,465	—	—
Net asset recoverable amount write-down	467,546	3,710,112	—	458,544
Amortisation of lease incentive	—	14,929	—	—
Equity settled share-based payments to employees	490,028	—	490,028	—
Equity settled share-based payments to corporate advisors	64,050	—	64,050	—
Increase in FCTR on translation of overseas subsidiaries	30,320	—	—	—
Project asset sales receivable in other current assets	141,248	—	—	—
Debt forgiveness revenue Newmont	—	(7,543,377)	—	(3,161,287)
Debt forgiveness with subsidiaries and related movement in balance sheet caption	—	—	—	(328,232)
Doubtful debts expense intercompany	—	—	—	1,650,951
Recoverability provision against investment	—	—	3,107,910	—
Magtrust revenue (in financing)	(2,077,690)	—	(2,077,690)	—
Repayment to government stakeholders of Department of Natural Resources security (in financing)	—	1,850,081	—	1,850,081

NOTES TO THE FINANCIAL STATEMENTS

NOTE 30 NOTES TO THE CASH FLOW STATEMENT (cont...)

	CONSOLIDATED		PARENT ENTITY	
	2006	2005	2006	2005
	\$	\$	\$	\$
Liability to government stakeholders in current payables (in financing)	—	3,000,000	—	—
Q MAG net balance sheet amounts at 1 December 2004 included in movements below	—	(3,130,000)	—	(1,129,350)
Loss of control of Q MAG cash balances on sale	—	2,065,000	—	1,032,500
Adjustment for RCF bridging loan	—	(2,500,000)	—	—
Q MAG sale non-cash adjustments	—	702,708	—	310,482
Accrued fitout at new AML premises	110,000	(187,210)	—	—
Changes in net assets and liabilities, net of effects from acquisition and disposal of businesses:				
(Increase)/decrease in current receivables	(422,932)	11,276,699	175,973	4,519,108
(Increase)/decrease in non-current receivables	—	1,247,000	—	849,000
(Increase)/decrease in inventories	(292,005)	22,504,000	—	11,252,000
(Increase)/decrease in other current assets	19,807	3,200,631	535	1,688,465
(Increase)/decrease in other non-current assets	—	9,514,522	—	2,030,585
Increase/(decrease) in current payables	87,695	(18,023,248)	(48,843)	(15,405,945)
Increase/(decrease) in non-current payables	(4,838,370)	(7,609,630)	—	(1,236,000)
Increase/(decrease) in current provisions	(29,268)	(3,033,757)	1,124	(303,517)
Increase/(decrease) in non-current provisions	(14,693)	(7,363,628)	722	(3,630,282)
Increase/(decrease) in other current liabilities	15,800	(6,070,000)	—	(3,071,000)
Increase/(decrease) in other non-current liabilities	63,200	(3,867,000)	—	(2,044,000)
Net cash from operating activities	(6,502,037)	(3,847,368)	(423,269)	1,339,103

NOTE 31 FINANCIAL INSTRUMENTS

(a) Financial risk management objectives

The consolidated entity does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes. The use of financial derivatives with respect to Q MAG was governed by the consolidated entity's policies approved by the Board of Directors, which provided written principles on the use of financial derivatives.

In the previous financial year, the Company and certain of its controlled entities were parties to derivative financial instruments in the normal course of business in order to hedge exposure to fluctuations in foreign exchange rates relating to sales by the Q MAG joint venture. All hedges were closed out as part of the sale agreement of the Q MAG joint venture operations to RCF on 1 December 2004.

(b) Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 1 to the financial statements.

(c) Interest rate risk management

The consolidated entity was exposed to interest rate risk as it borrowed funds at both fixed and floating interest rates. This risk ceased on the sale of the Q MAG operations and subsequent repayment of all outstanding loans.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 31 FINANCIAL INSTRUMENTS (cont...)

(d) Maturity profile of financial instruments

The following table details the consolidated entity's exposure to interest rate risk as at 30 June 2006.

	Weighted average effective interest rate	Variable interest rate	Fixed maturity dates					Non interest bearing	Total
			Less than 1 year	1-2 years	2-3 years	3-4 years	4-5 years		
2006	%	\$	\$	\$	\$	\$	\$	\$	
Financial assets:									
Cash and cash equivalents	5.558%	2,519,399	9,588,176	—	—	—	—	1,565	12,109,140
Trade receivables	nil	—	—	—	—	—	—	140,444	140,444
Other receivables	nil	—	—	—	—	—	—	739,789	739,789
	5.181%	2,519,399	9,588,176	—	—	—	—	881,798	12,989,373
Financial liabilities:									
Trade payables	nil	—	—	—	—	—	—	173,904	173,904
Other payables	nil	—	—	—	—	—	—	585,543	585,543
Employee benefits	nil	—	—	—	—	—	—	303,295	303,295
	nil	—	—	—	—	—	—	1,062,742	1,062,742

The following table details the consolidated entity's exposure to interest risk as at 30 June 2005.

	Weighted average effective interest rate	Variable interest rate	Fixed maturity dates					Non interest bearing	Total
			Less than 1 year	1-2 years	2-3 years	3-4 years	4-5 years		
2005	%	\$	\$	\$	\$	\$	\$	\$	
Financial assets:									
Cash and cash equivalents	5.255%	3,684,960	3,465,000	—	—	—	—	2,414	7,152,374
Trade and other receivables	nil	—	—	—	—	—	—	457,301	457,301
	4.939%	3,684,960	3,465,000	—	—	—	—	459,715	7,609,675
Financial liabilities:									
Trade payables	nil	—	—	—	—	—	—	671,752	671,752
Other payables	nil	—	—	—	—	—	—	4,838,370	4,838,370
	nil	—	—	—	—	—	—	5,510,122	5,510,122

(e) Fair value of financial instruments

The directors consider that the carrying amount of financial assets and financial liabilities recorded in the financial statements approximates their fair values (2005: net fair value).

(f) Liquidity risk management

The consolidated entity manages liquidity risk by maintaining adequate cash reserves and banking facilities by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 32 IMPACTS OF THE ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

The consolidated entity changed its accounting policies on 1 July 2005 to comply with Australian equivalents to International Financial Reporting Standards ('A-IFRS'). The transition to A-IFRS is accounted for in accordance with Accounting Standard AASB 1 'First-time Adoption of Australian Equivalents to International Financial Reporting Standards', with 7 July 2004 as the date of transition, except for financial instruments, including derivatives, where the date of transition is 1 July 2005 (refer note 1(t)).

An explanation of how the transition from superseded policies to A-IFRS has affected the company and consolidated entity's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables.

Effect of A-IFRS on the balance sheet as at 7 July 2004

NOTE	CONSOLIDATED			PARENT ENTITY		
	Super-seded policies* \$	Effect of transition to A-IFRS \$	A-IFRS \$	Super-seded policies* \$	Effect of transition to A-IFRS \$	A-IFRS \$
Current assets						
	12,460,000	—	12,460,000	7,732,000	—	7,732,000
	11,734,000	—	11,734,000	4,883,000	—	4,883,000
	22,504,000	—	22,504,000	11,252,000	—	11,252,000
	3,340,000	—	3,340,000	1,689,000	—	1,689,000
	50,038,000	—	50,038,000	25,556,000	—	25,556,000
Non-current assets classified as held for sale	—	5,545,172	5,545,172	—	—	—
Total current assets	—	5,545,172	55,583,172	25,556,000	—	25,556,000
Non-current assets						
Trade & other receivables	1,247,000	—	1,247,000	849,000	—	849,000
Property, plant and equipment	58,352,000	438,390	58,790,390	35,373,000	320,781	35,693,781
Project Assets	5,342,000	(5,342,000)	—	—	—	—
Other	4,909,000	—	4,909,000	2,031,000	—	2,031,000
Total non-current assets	69,850,000	(4,903,610)	64,946,390	38,253,000	320,781	38,573,781
Total assets	119,888,000	641,562	120,529,562	63,809,000	320,781	64,129,781
Current liabilities						
Trade & other payables	18,695,000	—	18,695,000	15,551,000	—	15,551,000
Borrowings	61,953,000	—	61,953,000	30,976,000	—	30,976,000
Provisions	5,345,000	(2,145,163)	3,199,837	1,599,000	(1,254,161)	344,839
Other	6,070,000	—	6,070,000	3,071,000	—	3,071,000
Total current liabilities	92,063,000	(2,145,163)	89,917,837	51,197,000	(1,254,161)	49,942,839
Non-current liabilities						
Trade & other payables	12,448,000	—	12,448,000	1,236,000	—	1,236,000
Borrowings	3,433,000	—	3,433,000	3,838,000	—	3,838,000
Provisions	4,414,000	3,137,064	7,551,064	2,240,000	1,559,906	3,799,906
Other	3,867,000	—	3,867,000	2,044,000	—	2,044,000
Total non-current liabilities	24,162,000	3,137,064	27,299,064	9,358,000	1,559,906	10,917,906
Total liabilities	116,225,000	991,901	117,216,901	60,555,000	305,745	60,860,745
Net assets	3,663,000	(350,339)	3,312,661	3,254,000	15,036	3,269,036
Equity						
Share capital	884,261,000	—	884,261,000	884,261,000	—	884,261,000
Other reserves	2,724,000	—	2,724,000	—	—	—
Outside Equity Interest	348,000	—	348,000	—	—	—
Accumulated Losses	(883,670,000)	(350,339)	(884,020,339)	(881,007,000)	15,036	(880,991,964)
Total equity	3,663,000	(350,339)	3,312,661	3,254,000	15,036	3,269,036

* Reported financial position for the financial year ended 6 July 2004

NOTES TO THE FINANCIAL STATEMENTS

NOTE 32 IMPACTS OF THE ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont...)

Effect of A-IFRS on the income statement for the year ended 30 June 2005

NOTE	CONSOLIDATED			PARENT ENTITY			
	Superseded policies*	Effect of transition to A-IFRS	A-IFRS	Superseded policies*	Effect of transition to A-IFRS	A-IFRS	
	\$	\$	\$	\$	\$	\$	
Operating revenue	(a)	30,469,846	(30,384,465)	85,381	15,336,979	(15,336,979)	—
Debt forgiveness revenue	(a)	7,543,377	(7,543,377)	—	10,638,059	(10,638,059)	—
Proceeds on sale of QMAG	(a), (e)	67,102,248	(67,102,248)	—	29,588,496	(29,588,496)	—
Proceeds on sale of assets	(a), (c)	2,254,875	(2,254,875)	—	10,004	(10,004)	—
Foreign exchange gain	(a)	572,626	(572,626)	—	—	—	—
Other revenue		135,209	(135,209)	—	48,753	(48,753)	—
Revenue		108,078,181	(107,992,800)	85,381	55,622,291	(55,622,291)	—
Other income	(c)	—	1,567,349	1,567,349	—	397,587	397,587
Revenue and Other income		108,078,181	(106,425,451)	1,652,730	55,622,291	(55,224,704)	397,587
QMAG related operating costs	(a)	(30,535,433)	30,535,433	—	(15,492,418)	15,492,418	—
Recoverable amount write downs	(a)	(3,710,112)	3,216,372	(493,740)	(458,544)	—	(458,544)
Net provision writeback/(expense)	(a)	820,041	(820,041)	—	(209,500)	209,500	—
Write down of other investments & loans		—	—	—	(1,650,951)	—	(1,650,951)
Written down value of assets sold	(a), (c)	(63,401,785)	63,401,785	—	(33,176,522)	33,176,522	—
Research, development, licencing and patent costs under contract	(a)	(622,413)	328,648	(293,765)	—	—	—
Insurance premium writeback/(refund)	(a)	(587,410)	587,410	—	—	—	—
Redundancy costs		(1,063,901)	—	(1,063,901)	(480,842)	—	(480,842)
Administration and other costs		(7,188,201)	12,750	(7,175,451)	(2,013,389)	21,034	(1,992,355)
Expenses (excluding finance costs)		(106,289,214)	97,262,357	(9,026,857)	(53,482,166)	48,899,474	(4,582,692)
Finance costs	(a)	(2,054,105)	2,054,105	—	(1,072,000)	1,072,000	—
Profit/(loss) before income tax expense		(265,138)	(7,108,989)	(7,374,127)	1,068,125	(5,253,230)	(4,185,105)
Income tax expense relating to ordinary activities		(51,321)	—	(51,321)	—	—	—
Profit/(loss) from continuing operations after income tax expense		(316,459)	(7,108,989)	(7,425,448)	1,068,125	(5,253,230)	(4,185,105)
Profit from discontinuing operations after income tax expense	(a)	—	7,481,447	7,481,447	—	5,259,228	5,259,228
Net profit/(loss) attributable to members of the parent entity		(316,459)	372,458	55,999	1,068,125	5,998	1,074,123

* Reported financial results for the year ended 30 June 2005.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 32 IMPACTS OF THE ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont...)

Effect of A-IFRS on the balance sheet as at 30 June 2005

NOTE	CONSOLIDATED			PARENT ENTITY		
	Super-seded policies* \$	Effect of transition to A-IFRS \$	A-IFRS \$	Super-seded policies* \$	Effect of transition to A-IFRS \$	A-IFRS \$
Current assets						
	7,152,374	—	7,152,374	4,427,045	—	4,427,045
	457,301	—	457,301	363,892	—	363,892
	139,369	—	139,369	535	—	535
	Non-current assets classified as held for sale					
(d)	—	937,800	937,800	—	—	—
	7,749,044	937,800	8,686,844	4,791,472	—	4,791,472
Non-current assets						
	—	—	—	—	—	—
	—	—	—	—	—	—
	449,672	—	449,672	134,906	—	134,906
(d)	937,800	(937,800)	—	—	—	—
	1,387,472	(937,800)	449,672	134,906	—	134,906
	9,136,516	—	9,136,516	4,926,378	—	4,926,378
Current liabilities						
	671,752	—	671,752	145,055	—	145,055
(b)	251,278	(85,045)	166,233	135,259	(94,382)	40,877
	923,030	(85,045)	837,985	280,314	(94,382)	185,932
Non-current liabilities						
	4,838,370	—	4,838,370	—	—	—
(b)	125,305	62,926	188,231	96,458	73,348	169,806
	4,963,675	62,926	5,026,601	96,458	73,348	169,806
	5,886,705	(22,119)	5,864,586	376,772	(21,034)	355,738
	3,249,811	22,119	3,271,930	4,549,606	21,034	4,570,640
Equity						
	884,488,210	—	884,488,210	884,488,210	—	884,488,210
	2,749,980	—	2,749,980	—	—	—
	(883,988,379)	22,119	(883,966,260)	(879,938,604)	21,034	(879,917,570)
	3,249,811	22,119	3,271,930	4,549,606	21,034	4,570,640

* Reported financial position for the financial year ended 30 June 2005.

Effect of A-IFRS on the cash flow statement for the financial year ended 30 June 2005

There are no material differences between the cash flow statement presented under A-IFRS and the cash flow statement presented under the superseded policies.

Notes to the reconciliations of income and equity

(a) Discontinued Operations

Under A-IFRS, the consolidated entity recognises revenue and expenses, including tax expenses, attributable to discontinued operations as part of a single line item 'profit from discontinued operations' on the income statement. There was no requirement under previous GAAP to split out revenue and expenses attributable to discontinued operations in this manner, and accordingly, amounts are reclassified from the various line items in which they were recognised under previous GAAP to 'profit from discontinued operations' on adoption of A-IFRS.

(b) Employee entitlement provisions

Under A-IFRS, provisions for employee entitlements must be classified as either current or non-current dependent upon whether the entity has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date. Employee benefits not expected to be settled within 12 months of balance date are measured at the present value of the estimated future cash outflows.

(c) Disclosure of asset disposals

AGAAP required the disclosure of asset disposals on a gross basis, with the proceeds on sale itemised as revenue and the written down value of such assets sold presented as expense. A-IFRS requires a net disclosure basis as either a gain or loss on sale. Gain on sale is included in other income.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 32 IMPACTS OF THE ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (cont...)

(d) Assets held for sale

A-IFRS introduces a category of assets described as assets held for sale. Assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. The sale of the asset or disposal group is expected to be completed within one year from the date of classification.

(e) QMAG sale

The impact of A-IFRS on the opening balance sheet position of the consolidated group at 7 July 2004, as described in (d) above), has altered the carrying value of assets sold as part of the QMAG sale on 1 December 2004. The change in carrying value of the QMAG assets and restoration liabilities sold has resulted in a modification to the gain or loss on sale of these operations.

(f) Financial instruments

The directors have elected to adopt AASB139 *Financial Instruments: Recognition and Measurement* with effect from 1 July 2005. Therefore, there is no impact on the 30 June 2005 financial statements from AASB139.

(g) Business combinations

AMC Limited did not acquire any business or entities in the financial year ended 30 June 2005. On initial adoption of A-IFRS the directors have elected not to restate business combinations that occurred before 7 July 2004. Accordingly, there are no impacts of the adoption of A-IFRS on the financial report associated with past business combinations.

(h) Rehabilitation provision

Under AGAAP the provision for rehabilitation of the QMAG mine and the related expense was recognized progressively throughout the mine life such that the full amount is provided when the mine's life is at an end. Under A-IFRS such a provision is recognised in full at the inception of the mine and capitalised into the asset. The provision is discounted and the capitalised amount is depreciated in accordance with the asset.

(i) Accumulated losses

The effect of the above adjustments on the accumulated losses is as follows:

		CONSOLIDATED		PARENT ENTITY	
		7 July 2004 \$	30 June 2005 \$	7 July 2004 \$	30 June 2005 \$
Employee entitlement provisions	(b)	13,773	(12,750)	197,092	21,034
QMAG sale	(e)	—	(359,708)	—	—
Recalculation of QMAG mine rehabilitation provision	(h)	(364,112)	—	(182,056)	—
Total increase/(decrease) to accumulated losses		(350,339)	(372,458)	15,036	21,034

NOTE 33 ADDITIONAL COMPANY INFORMATION

Advanced Magnesium Limited (AML) is a listed public company and is incorporated in Australia. The AML Group operates globally with subsidiaries in Australia, North America and Europe.

Registered Office and Principal place of business

9th Floor
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DIRECTORS' DECLARATION

The Directors declare that the financial statements and notes thereto, set out on pages 15 to 54.

- (a) in the Directors' opinion, there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable;
- (b) in the Directors' opinion, the attached financial statements and notes thereto are in accordance with the Corporations Act 2001, including compliance with accounting standards and giving a true and fair view of the financial position and performance of the Company and consolidated entity; and
- (c) the Directors have been given the declarations required by s.295A of the Corporations Act 2001.

Signed in accordance with a resolution of the Directors made pursuant to s.295(5) of the Corporations Act 2001.

On behalf of the Directors



DR CD RAWLINGS
NON-EXECUTIVE CHAIRMAN



MR KG WILLIAMS
NON-EXECUTIVE DIRECTOR

Brisbane, 25 August 2006



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Independent audit report to the members of Advanced Magnesium Limited

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, cash flow statement, statement of recognised income and expense, a summary of significant accounting policies and other explanatory notes and the directors' declaration for both Advanced Magnesium Limited (the company) and the consolidated entity, for the financial year ended 30 June 2006 as set out on pages 15 to 55. The consolidated entity comprises the company and the entities it controlled at the year's end or from time to time during the financial year.

The company has disclosed information about the compensation of key management personnel ("compensation disclosures"), as required by paragraphs Aus 25.4 to Aus 25.6 of Accounting Standard AASB 124 *Related Party Disclosures* ("AASB 124") under the heading "remuneration report" in paragraphs (a) to (d) of the directors' report and not in the financial report, as permitted by the Corporations Regulations 2001. These compensation disclosures are identified in the directors' report as being subject to audit. The remuneration report also contains information not subject to audit.

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

Audit approach

We have conducted an independent audit of the financial report and compensation disclosures in order to express an opinion on it to the members of the company. Our audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance whether the financial report is free of material misstatement and the compensation disclosures comply with AASB 124. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal controls, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

Liability limited by a scheme approved under Professional Standards Legislation.



We performed procedures to form an opinion whether, in all material respects, the financial report is presented fairly in accordance with Accounting Standards in Australia and the Corporations Act 2001 so as to present a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and performance as represented by the results of their operations, their changes in equity and their cash flows and whether the compensation disclosures comply with AASB 124.

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

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

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

Audit Opinion

In our opinion:

- (1) the financial report of Advanced Magnesium Limited is in accordance with the Corporations Act 2001, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2006 and of their performance for the year ended on that date; and
 - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001.
- (2) the compensation disclosures that are contained in paragraphs (a) to (d), under the heading "remuneration report" of the directors' report comply with paragraphs Aus 25.4 to Aus 25.6 of Accounting Standard AASB 124 Related Party Disclosures.

A handwritten signature in blue ink that reads "Deloitte Touche Tohmatsu".

DELOITTE TOUCHE TOHMATSU

A handwritten signature in blue ink that reads "Timothy Biggs".

Timothy Biggs
Partner
Chartered Accountants
Brisbane, 25 August 2006