



Arasor International Limited

ABN 29 119 999 441

Annual Financial Report

for the year ended 31 December 2009

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Appendix 4E Requirements

| Results for announcement to the market | 2009 \$A | 2008 \$A | | Percentage change |
|---|-------------|---------------|-----------|----------------------|
| Revenues from continuing activities (i) | - | 18,187,472 | down | 100% |
| Loss from ordinary activities after tax attributable to the members (including discontinued operations) | (5,385,783) | (144,334,160) | loss down | 96% |
| Loss for the period attributable to members (including discontinued operations) | (5,385,783) | (144,334,160) | down | 96% |

Dividends (distributions)

No dividend have been paid during the financial year ended 31 December 2009

The directors have not proposed a dividend for the year end 31 December 2009

| | | |
|---|----------|----------|
| Net Tangible Assets Per Security - cents | (\$0.22) | (\$0.28) |
|---|----------|----------|

(i) Please note the revenues listed above include only continued operations. Due to the fact the Company's US operations have continued to be classified as discontinued from December 2008 and due to the abandonment of the Company's operations in China, the comparative revenue numbers have been modified to exclude the Company's US and Chinese operations. Please refer to note 32 for more details.

Corporate Information

This annual report covers both Arasor International Ltd (ABN 29 119 999 441) as an individual entity and the consolidated entity comprising Arasor International Ltd and its subsidiaries.

A description of the Group's operations and of its principal activities is included in the review of operations and activities in the directors' report.

Directors

| | |
|---|--------------------------|
| Dr Simon Cao, Ex-Chairman | (Resigned 23 April 2010) |
| Mr George SyCip, Non-Executive Director | |
| Mr Edward Li, Non-Executive Director | |
| Mr Reginald Bancroft, Chairman | |

Company Secretary

Mr Reginald Bancroft

Registered Office

C/- HLB Mann Judd (SA) Pty Ltd
82 Fullarton Road
NORWOOD SA 5067

Principal place of business

C/- HLB Mann Judd (SA) Pty Ltd
82 Fullarton Road
NORWOOD SA 5067

Share Register

Computershare Investor Services Pty Ltd
Level 5, 115 Grenfell Street
ADELAIDE SA 5000

Legal Advisors

O'loughlins Lawyers
Level 2, 99 Frome Street
ADELAIDE SA 5000

Auditors

Grant Thornton South Australian Partnership
Chartered Accountants
Level 1, 67 Greenhill Road
WAYVILLE SA 5034

Directors' report

Your directors submit their report for the year ended 31 December 2009.

DIRECTORS

The names and details of the company's directors in office during the financial year and until the date of this report are as follows. Directors were in office for this entire period unless otherwise stated.

Names, qualifications, experience and special responsibilities

Simon Cao, PhD (Chairman and Chief Executive Officer) Resigned 23 April 2010

Simon Cao is the Executive Chairman of Arasor and has more than 20 years experience in optics, communications and signal processing. Prior to co-founding Arasor, Simon was a founder of Avanex Corporation and served as Chief Technology Officer, Senior Vice President of Business Development and a member of the board of directors. Prior to Avanex Corporation, Simon was a founder of Oplink Communications Inc. and served as Vice President of Sales and Marketing and established the company's wavelength division multiplexing (WDM) product line. Over the span of his career, Simon has been directly responsible for the invention and commercialisation of fibre-optic products such as the fiber amplifier, WDM transmission and >10Gb/s high-speed optical transmission. In 1999, Forbes named Dr Cao the "Godfather" of WDM technology. Simon is also the author of 'Cao's Law', the optical corollary of Moore's Law in electronics, which states that WDM will spread more and more finer and finer channels of light, each using less and less power, across an optical fibre. Earlier in his career, Simon was also one of the first employees of E-Tek Dynamics Inc. Dr Cao holds PhD and M.S. degrees in both electrical engineering and physics from the University of Southern California ("USC"). He also chairs the research committee on the board of USC's engineering school and holds various U.S. and international patents.

George SyCip, MBA (Non-Executive Director)

George SyCip is President of Halanna Management Corporation and a founder and principal in Galaxaco China Group LLC. Mr SyCip advises a variety of companies in their cross-border endeavours between the US/Europe and Asia. He also sits on several corporate boards including: Bank of the Orient in San Francisco; Beneficial-PNB Life Insurance Company in the Philippines; MacroAsia Corporation; Medtecs International Corporation Limited, Paxys, Inc. in the Philippines; and is a board member of the International Institute for Rural Reconstruction. Prior to setting up his own offices, Mr SyCip had a career in banking and currently serves as a board member of the Stanford Institute for International Studies, Give2Asia and the California Asia Business Council. He has also served as Commissioner for the City and County of San Francisco's Social Services Department. Mr SyCip was born in the Philippines and received his A.B. in International Relations/Economics in 1978 from Stanford University and his MBA from Harvard.

Directors' report

Mr Edward Li CA (Non-Executive Director)

Edward Li is a Chartered Accountant with over 30 years experience in senior positions of both private and public companies, including Red Earth, Lincraft, the Sussan Group and more recently with Go Connect Ltd and Sino Strategic International Limited. Mr Li has been Chief Financial Officer and joint Company Secretary of Go Connect Ltd since March 2000. He has been a Chartered Accountant for over 35 years and holds a Bachelor of Economics.

Mr Reginald Bancroft (Non-Executive Director and Company Secretary)

Reg Bancroft had a 37 year career with UK based Royal and Sun Alliance Insurance (RSA). After 17 years in the UK, he moved to Australia in 1984 taking on roles including Director of commercial insurance across the Asia Pacific region. Retiring from RSA in Korea in 2002, he took up an assignment as Executive Vice Chairman with Green Hwajae, a listed Korean non-life insurer. He presently is Australian Managing Partner of Doran Capital Partners, a privately held, diversified real estate investment management and advisory Company that conducts business throughout Asia.

INTERESTS IN THE SHARES AND OPTIONS OF THE COMPANY AND RELATED BODIES CORPORATE

As at the date of this report, the interests of the directors in the shares and options of Arasor International Ltd were:

| | Number of Ordinary Shares | Number of Options over Ordinary Shares |
|----------------------|------------------------------|---|
| Dr Simon Cao | 4,423,717 | 1,000,000 |
| Mr George SyCip | 469,742 | 1,040,000 |
| Mr Edward Li | - | 1,000,000 |
| Mr Reginald Bancroft | 5,000 | 1,000,000 |

In addition to the above listed interests, the following directors have an indirect interest in the shares of Arasor International Ltd:

- New Commerce Investment Co. Ltd, an entity in which Simon Cao is a director, holds 12,468,726 Ordinary Fully Paid Shares in Arasor International Ltd.

DIVIDENDS

No dividends were paid or declared since the start of the financial year. No recommendation for payment of dividends has been made at the date of this report.

PRINCIPAL ACTIVITIES

During the year the Group:

- continued to pursue the possibility of making its ZTEI joint venture with ZTEI in Tianjin in China operational; and
- collection from outstanding Indian receivables and funding these principal pursuits by the sale of non-core assets.

Directors' report

REVIEW OF OPERATIONS

The Group's reported net loss attributable to Arasor International Limited, excluding discontinued operations, amounted to \$1.36 Million (2008: \$5.87 Million).

This result was driven by the disposal of its loss making subsidiaries AOFR Pty Ltd and Bandwidth Foundry Pty Ltd which brought in working capital to the Group.

The Company continued to focus its efforts on removing the loss from its manufacturing facility located in Nansha, Guangdong Province, China and exploring the possibility of making its Joint Venture with ZTE International Ltd (ZAT) operational, as well as the disposal of the Group's remaining subsidiary in Japan.

RISK MANAGEMENT

The Board is responsible for ensuring that risks, and also opportunities, are identified on a timely basis and that the group's objectives and activities are aligned with the risks and opportunities identified by the Board.

The Board has mechanisms in place to ensure that management's objectives and activities are aligned with the risks identified by the Board. These include the strategies laid down at the last two Annual General Meetings.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

As detailed in the review of operations, Arasor International Limited has made several changes throughout the year which have impacted the size and performance of the group. These include the disposal of two subsidiaries, AOFR Pty Ltd and Bandwidth Foundry International Pty Ltd and the abandonment of the Company's Chinese operations, which have significantly affected the Company's operating results.

SIGNIFICANT EVENTS AFTER THE REPORTING DATE

As disclosed within the 31 December 2008 financial statements, on 5 February 2010, the Company announced the payment of the secured term loan in place in China with the Agricultural Bank of China. The resolution involved the payment of \$18 Million (RMB 116 Million) to the bank (representing both principal and accrued interest) made by the Company's minority JV partner Guangzhou Nan Sha Assets Operation Co., Ltd ('NGAO'). In exchange for the payment, the NGAO has assumed ownership of the Company's land and buildings in Guangzhou. Arasor maintains an ability to lease the land off the NGAO in order to continue to service its client base. Post this resolution, the board has formally reached the decision to abandon its operations in China, which have been reflected in the financial statements for the year ended 31 December 2009.

On 1 April 2010, the Company announced it had entered into an agreement to sell its Japan optical wafer production fabrication facility and assets to a US based multinational Company. The transaction provides for a consideration of US \$1.17 Million (AUD \$1.3 Million).

On 25 November 2010, the Company announced that due to the lack of development of the Company's Joint Venture with ZTEI, it would be seeking remedies from its former Executive Chairman, Dr Simon Cao, for the amount of USD \$10 Million.

Directors' report

LIKELY DEVELOPMENTS AND EXPECTED RESULTS

Information as to the likely developments in the operations of the Group and the expected results of those operations in future years has not been included in the Annual Report because disclosure of the information would be likely to result in unreasonable prejudice to the Group.

ENVIRONMENTAL REGULATION AND PERFORMANCE

The Group is not subject to any specific environmental regulation in its operations under the law of a state/territory or Commonwealth of Australia.

SHARE OPTIONS

Unissued Shares

At the date of this report, the following options to acquire ordinary shares in the company were on issue:

| Issue Date | Expiry Date | Exercise Price | Balance at the date of this report |
|------------|-------------|----------------|--|
| 11/10/2006 | 23/01/2013 | \$1.00 | 40,107 |
| 11/10/2006 | 24/10/2011 | \$1.50 | 240,000 |
| 05/11/2007 | 4/11/2012 | \$1.48 | 1,050,000 |
| 09/01/2008 | 8/01/2013 | \$1.59 | 643,788 |
| 08/07/2009 | 7/07/2014 | \$0.05 | 3,000,000 |
| 16/07/2010 | 15/07/2015 | \$0.05 | 4,000,000 |
| | | | <u>8,973,895</u> |

The above list of options differs from the number of options listed at note 15 to the financial statements due to option lapses that occurred post reporting date. Refer to an announcement in relation to these lapses lodged on 21 July 2010.

Shares issued as a result of the exercise of options

During and subsequent to the end of the financial year, no options have been exercised by option holders into fully paid ordinary shares.

INDEMNIFICATION AND INSURANCE OF DIRECTORS, AUDITORS AND OFFICERS

The Parent Entity maintains a directors' and officers' indemnity insurance policy for the benefit of the Directors and executive officers of the Consolidated Group. The insurance policy grants indemnity against liabilities permitted to be indemnified by the Consolidated Group under section 199B of the Corporations Act 2001. The policy prohibits disclosure of the premium payable.

Directors' report

REMUNERATION REPORT – AUDITED

This report outlines the remuneration arrangements in place for directors and key management personnel of Arasor International Ltd.

Summary of positions held by executive key management personnel

Mr William Mackenzie, Chief Executive Officer

Mr Mackenzie was appointed as the group's Chief Executive Officer on 1 June 2008. Mr Mackenzie is responsible for the overall management of the group's operations and communication with the board.

Remuneration philosophy

The board is responsible for determining remuneration policies applicable to directors and key management personnel of the entity. The broad policy is to ensure that remuneration properly reflects the individuals' duties and responsibilities and that remuneration is competitive in attracting, retaining and motivating people with appropriate skills and experience. At the time of determining remuneration consideration is given by the Board to the entity's financial performance.

All remuneration paid to directors and executives is expensed as incurred. Executives are also entitled to participate in the company share option scheme. Options issued under the plan are valued using the Black-Scholes methodology.

The board policy is to remunerate non-executive directors at market rates based on comparable companies for time, commitment and responsibilities. The board determines payments to non-executive directors and reviews their remuneration annually, based on market practice, duties and accountability. Independent external advice is sought when required. The maximum aggregate remuneration of the Non-executive Directors is presently fixed at \$500,000.

Employment contracts

Chairman

The employment conditions of Chairman, Dr Simon Cao, are formalised in a contract of employment. Dr Cao commenced his employment on 1 June 2006 and his gross base salary is US\$304,192, which is subject to an annual review. All travel expenses of Dr Cao in the course of his employment are reimbursed by the Company.

Dr Cao may resign on six months' notice and the Company may terminate Dr Cao's employment without cause by providing one months' notice or immediately, with the payment of six months' base salary. Termination payments are generally not payable on resignation or dismissal for serious misconduct. In the instance of serious misconduct, the Company can terminate employment at any time.

Chief Executive Officer

The employment conditions of the Chief Executive Officer, Mr. William Mackenzie, are formalised in a contract of employment. Mr. Mackenzie commenced his employment on 15 May 2008 and his gross salary was US \$360,000. Mr. Mackenzie entered into a new contract of employment in June 2009 with an annual gross salary of US \$125,000. This contract ends in December 2nd, 2010.

Directors' report

Other Key Management Personnel

The employment contracts in place for all other key management personnel contain provisions whereby the employment relationship can be terminated by either party at any time, with or without notice and with or without cause.

Remuneration Report

Table 1: Director remuneration for the year ended 31 December 2009

| | Primary Benefits | Post Employment | Equity | Total |
|-------------------|---------------------|-----------------|---------|----------------|
| | Salary & Fees | Superannuation | Options | \$ |
| Dr Simon Cao | | | | |
| 2009 | 304,192 | - | - | 304,192 |
| 2008 | 304,192 | - | - | 304,192 |
| Mr George SyCip | | | | |
| 2009 | 40,000 | - | - | 40,000 |
| 2008 | 40,000 | - | - | 40,000 |
| Edward Li | | | | |
| 2009 | 40,000 | - | - | 40,000 |
| 2008 | 11,616 | - | - | 11,616 |
| Reginald Bancroft | | | | |
| 2009 | 40,000 | - | - | 40,000 |
| 2008 | 11,507 | - | - | 11,507 |
| Total | | | | |
| 2009 | 424,192 | - | - | 424,192 |
| 2008 | 367,315 | - | - | 367,315 |

No remuneration for Directors for the year ended 31 December 2009 or 31 December 2008 was performance based.

The directors note the above listed remuneration report reflects the Company's accrued fees and the actual cash paid during the period does not necessarily relate to the above listed numbers.

Directors' report

Table 2: Remuneration of other management personnel for the year ended 31 December 2009

| | Primary Benefits | Post Employment | Equity | Total |
|-------------------|------------------|-----------------|---------|----------------|
| | Salary & Fees | Superannuation | Options | \$ |
| William Mackenzie | | | | |
| 2009 | 309,057 | - | 35,096 | 344,153 |
| 2008 | 457,460 | - | - | 457,460 |
| Mike Hong | | | | |
| 2008 | 257,742 | - | - | 257,742 |
| Total | | | | |
| 2009 | 309,057 | - | 35,096 | 344,153 |
| 2008 | 715,202 | - | - | 715,202 |

The directors note the above listed remuneration report reflects the Company's accrued fees and the actual cash paid during the period does not necessarily relate to the above listed numbers.

Table 3: Options granted as part of remuneration 2010

| 31 December 2009 | Grant date | Grant number | Vesting date | Value per option at grant date | Exercise Price | Total fair value | % of Remuneration |
|----------------------|------------|--------------|--------------|--------------------------------|----------------|------------------|-------------------|
| Mr William Mackenzie | 08/07/09 | 3,000,000 | 08/07/09 | \$ 0.012 | 0.05 | 35,096 | 10.20% |

DIRECTORS' MEETINGS

The number of meetings of directors (including meetings of committees of directors) held during the year and the number of meetings attended by each director were as follows:

| Directors' Meetings | Attended | Eligible |
|----------------------|----------|----------|
| Dr Simon Cao | 7 | 11 |
| Mr George SyCip | 8 | 11 |
| Mr Edward Li | 9 | 11 |
| Mr Reginald Bancroft | 11 | 11 |

Directors' report

| Audit Committee | Attended | Eligible |
|-----------------|----------|----------|
| Mr Edward Li | - | - |
| Mr George SyCip | - | - |

During the year, no meetings were held for audit committee due to the length of time taken in preparing the Group's 2009 accounts.

PROCEEDINGS ON BEHALF OF THE COMPANY

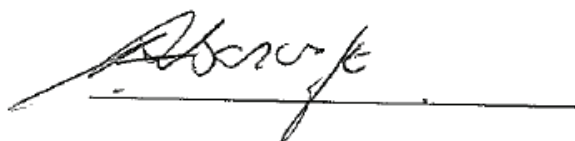
No person has applied for leave of Court to bring proceedings on behalf of the Company or intervene in any proceedings to which the Company is a party for the purpose of taking responsibility on behalf of the Company for all or any part of those proceedings.

The Company was not a party to any such proceedings during the year.

NON-AUDIT SERVICES

Details of amounts paid or payable to the auditor for non-audit services are contained with note 27 to the financial statements. The auditor's independence declaration for the year ended 31 December 2009 has been received and can be found on page 13 which forms a part of this report.

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



Mr Reginald Bancroft
Director

29 December 2010



Grant Thornton

Level 1,
67 Greenhill Rd
Wayville SA 5034
GPO Box 1270
Adelaide SA 5001

T 61 8 8372 6666
F 61 8 8372 6677
E info@gtlsa.com.au
W www.grantthornton.com.au

**AUDITOR'S INDEPENDENCE DECLARATION
TO THE DIRECTORS OF ARASOR INTERNATIONAL LIMITED**

In accordance with the requirements of section 307C of the Corporations Act 2001, as lead auditor for the audit of Arasor International Limited for the year ended 31 December 2009, I declare that, to the best of my knowledge and belief, there have been:

- a no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- b no contraventions of any applicable code of professional conduct in relation to the audit.

GRANT THORNTON SOUTH AUSTRALIAN PARTNERSHIP
Chartered Accountants

S J Gray
Partner

Adelaide, 29 December 2010

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Corporate Governance Statement

The board of directors is responsible for the corporate governance of Arasor International Ltd (the Company) and its controlled entities (the Group). The Group operates in accordance with the corporate governance principles as set out by the ASX corporate governance council and required under ASX listing rules.

The Group details below the corporate governance practices in place at the end of the financial year, all of which comply with the principles and recommendations of the ASX corporate governance council unless otherwise stated.

Principle 1: Lay solid foundations for management and oversight Board Responsibilities

The Board is accountable to the Shareholders for the performance of the Group and has overall responsibility for its operations. Day to day management of the Group's affairs and the implementation of the corporate strategy and policy initiatives, are formally delegated by the Board to the Chief Executive Officer.

The key responsibilities of the board include:

- Approving the strategic direction and related objectives of the Group and monitoring management performance in the achievement of these objectives;
- Adopting budgets and monitoring the financial performance of the Group;
- Reviewing annually the performance of the Chief Executive Officer and Senior Executives against the objectives and performance indicators established by the Board;
- Overseeing the establishment and maintenance of adequate internal controls and effective monitoring systems;
- Overseeing the implementation and management of effective safety and environmental performance systems;
- Ensuring all major business risks are identified and effectively managed; and
- Ensuring that the Group meets its legal and statutory obligations.

For the purposes of the proper performance of their duties, the Directors are entitled to seek independent professional advice at the Group's expense, unless the Board determines otherwise. The Board schedules meetings on a regular basis and other meetings as and when required.

The Board has not publicly disclosed a statement of matters reserved for the board, or the board charter and therefore the Group has not complied with recommendation 1.3 of the Corporate Governance Council. Given the experience and skills of the board of directors, the Group has not considered it necessary to formulate a board charter.

Principle 2: Structure the board to add value

Size and composition of the Board

At the date of this statement the Board consists of three non-executive directors. Directors are expected to bring independent views and judgement to the Board's deliberations.

| | |
|----------------------|------------------------|
| Mr Regianld Bancroft | Non-Executive Chairman |
| Mr George SyCip | Non-Executive Director |
| Mr Edward Li | Non-Executive Director |

The Board considers this to be an appropriate composition given the size and development of the Group at the present time. The names of directors including details of their qualifications and experience are set out in the Directors' Report of this Annual Report.

Independence

The Board is conscious of the need for independence and ensures that where a conflict of interest may arise, the relevant Director(s) leave the meeting to ensure a full and frank discussion of the matter(s) under consideration by the rest of the Board. Those Directors who have interests in specific transactions or potential transactions do not receive Board papers related to those transactions or potential transactions, do not participate in any part of a Directors' meeting which considers those transactions or potential transactions, are not involved in the decision making process in respect of those transactions or potential transactions, and are asked not to discuss those transactions or potential transactions with other Directors.

At the date of this statement the Board consists of three non-executive directors, Mr Reginald Bancroft, who is also chairman and secretary of the Board, Mr George SyCip and Mr Edward Li who all have no other material relationship with the Group or its subsidiary other than their directorships. The Company therefore has three independent directors as that relationship is currently defined and therefore has complied with recommendation 2.1 of the Corporate Governance Council which recommends that the Board consist of a majority of independent directors.

Nomination, retirement and appointment of Directors

The Board has from 2008 disbanded its remuneration and nomination committee and therefore the Group has not complied with recommendation 2.4 of the Corporate Governance Council. Given the size of the Group, the Board made the decision in 2008 that the Company does not require a separate committee in light of the size and composition of the Company. The Board takes ultimate responsibility for these matters.

The composition/membership of the Board is subject to review in a number of ways, as outlined below:

- The Group's constitution provides that at every Annual General Meeting, one third of the directors shall retire from office but may stand for re-election.
- Board composition is also reviewed periodically either when a vacancy arises or if it is considered that the Board would benefit from the services of a new director, given the existing mix of skills and experience of the board which should match the strategic demands of the Group. Once it has been agreed that a new director is to be appointed, a search would be undertaken, sometimes using the services of external consultants. Nominations are subsequently received and reviewed by the Board.

Evaluation of Board performance

The Board continues to review performance and identify ways to improve performance. The Chairman is responsible for reviewing the Board performance on an annual basis.

Board Committees

It is the role of the Board to oversee the management of the Group and it may establish appropriate committees to assist in this role. The Board presently has only one committee, an audit, risk and compliance committee. At the present time no other committees have been established because of the size of the Group and the involvement of the Board in the operations of the Group. The Board takes ultimate responsibility for the operations of the Group including remuneration of Directors and executives and nominations to the Board.

The Board has not publicly disclosed the process for evaluating the performance of the Board, its committees and individual directors. Therefore, the Group has not complied with recommendation 2.5 of the Corporate Governance Council. Given the size of the Group, the Board does not consider disclosure of the performance evaluation process necessary. The Board takes ultimate responsibility for these matters.

Principle 3: Promote ethical and responsible decision making

Code of Conduct

The Board recognises the need for Directors and employees to observe the highest standards of behaviour and business ethics when engaging in corporate activity. The Group intends to maintain a reputation for integrity. The Group's officers and employees are required to act in accordance with the law and with the highest ethical standards. The Board has adopted a formal code of conduct applying to the Board and all Employees. However, the Group has not publicly disclosed the code of conduct and therefore the Group has not complied with recommendation 3.1 of the Corporate Governance Council. Given the size of the Group, the Board does not consider disclosure of the code of conduct to be necessary. The Board takes ultimate responsibility for these matters.

Securities Trading Policy

The Group's constitution permits designated persons to acquire securities in the Group, however Group policy prohibits designated persons from dealing in the Group's securities at any time whilst in possession of price sensitive information and for 24 hours after:

- Any major announcements;
- The release of the Group's quarterly, half yearly and annual financial results to the Australian Securities Exchange; and
- The Annual General Meeting.

Directors must advise the chairman of the board before buying or selling securities in the Group. All such transactions are reported to the Board. In accordance with the provisions of the Corporations Act and the Listing Rules of the Australian Securities Exchange, the Group advises the Exchange of any transaction conducted by directors in securities in the Group.

The Group has not established and publicly disclosed a policy concerning trading in Group securities by directors, senior executives and employees other than as disclosed above, and therefore has not complied with recommendation 3.2 of the Corporate Governance Council. Given the size of the Group, the Board does not consider establishment or disclosure of a trading policy to be appropriate. The Board takes ultimate responsibility for these matters.

Principle 4: Safeguard integrity in financial reporting

The Group has structured financial management to independently verify and safeguard the integrity of their financial reporting. The structure established by the Group includes:

- Review and consideration of the financial statements by the audit committee;
- A process to ensure the independence and competence of the Group's external auditors.

Audit Committee

The audit, risk and compliance committee comprises Mr Edward Li (Chairman) and Mr George SyCip. . Due to the size of the board, it is not possible to meet recommendation 4.3 of the Corporate Governance Council of having at least three non-executive directors as members, the majority of which are independent. The Board will annually confirm the membership of the committee.

The committee's primary responsibilities are to:

- oversee the existence and maintenance of internal controls and accounting systems;
- oversee the management of risk within the Group;
- oversee the financial reporting process;
- review the annual and half-year financial reports and recommend them for approval by the Board of Directors;
- nominate external auditors;
- review the performance of the external auditors and existing audit arrangements; and

- ensure compliance with laws, regulations and other statutory or professional requirements, and the Group's governance policies.

Given the experience and skills of the members of the committee, the Board has not documented a formal committee charter and therefore the Group has not complied with recommendation 4.3 of the Corporate Governance Council. Given the size of the Group the members of the audit committee have been chosen for their relevant skills and experience. The Board continues to monitor the composition of the committee and the roles and responsibilities of the members.

Principle 5: Make timely and balanced disclosure

The Group has a policy that all shareholders and investors have equal access to the Group's information. The Board ensures that all price sensitive information is disclosed to the ASX in accordance with the continuous disclosure requirements of the Corporation's Act and ASX Listing Rules. The company secretary has primary responsibility for all communications with the ASX and is accountable to the Board for all governance matters.

The Group has not publicly disclosed a formal disclosure policy and therefore has not complied with recommendation 5.1 of the Corporate Governance Council. Given the size of the Group, the Board does not consider a public disclosure policy to be appropriate. The Board takes ultimate responsibility for these matters.

Principle 6: Respect the rights of shareholders

The Board strives to ensure that Shareholders are provided with sufficient information to assess the performance of the Group and its Directors and to make well-informed investment decisions.

Information is communicated to Shareholders through:

- annual, half-yearly and quarterly financial reports;
- annual and other general meetings convened for Shareholder review and approval of Board proposals; and
- continuous disclosure of material changes to ASX for open access to the public.

The auditor is invited to attend the annual general meeting of Shareholders. The Chairman will permit Shareholders to ask questions about the conduct of the audit and the preparation and content of the audit report.

The Group has not designed or publicly disclosed a communications policy and therefore has not complied with recommendation 6.1 of the Corporate Governance Council. Given the size of the Group, the Board does not consider the disclosure of a communications policy to be appropriate. The Board takes ultimate responsibility for these matters.

Principle 7: Recognise and manage risk

The Board has identified the significant areas of potential business and legal risk of Arasor International Ltd. The identification, monitoring and, where appropriate, the reduction of significant risk to the Group is the responsibility of the Chief Executive Officer and the Board. The Board has also established the audit, risk and compliance committee which addresses the risk of the Group.

The Board reviews and monitors the parameters under which such risks will be managed. Management accounts are prepared and reviewed with the Chief Executive Officer at subsequent Board meetings. Management and the Board monitor the Group's material business risks and reports are considered at regular meetings.

Chief Executive Officer and Company Secretary declaration to the Board of Directors

The Chief Executive Officer and the Company Secretary will be required to state in writing to the Board that the Group's financial reports present a true and fair view, in all material respects, of the Group's financial condition and operational results are in accordance with relevant accounting standards.

The Group has not established or publicly disclosed a policy for the oversight and management of material business risks and therefore has not complied with recommendation 7.1 of the Corporate Governance Council. Given the size of the Group, the Board does not consider establishment or disclosure of a risk management policy to be appropriate. The Board takes ultimate responsibility for these matters.

Principle 8: Remunerate fairly and responsibly

The Chairman and the non-executive Directors are entitled to draw Directors fees and receive reimbursement of reasonable expenses for attendance at meetings. The Group is required to disclose in its annual report details of remuneration to Directors. The maximum aggregate annual remuneration which may be paid to non-executive Directors is \$500,000. This amount cannot be increased without the approval of the Group's shareholders. Please refer to the remuneration report within the directors' report for details regarding the remuneration structure of the Chief Executive Officer and senior management.

The Board has not established a remuneration committee or disclosed a remuneration committee charter and therefore the Group has not complied with recommendation 8.1 and 8.3 respectively of the Corporate Governance Council. Given the size of the Group, the Board does not consider a separate committee appropriate. The Board takes ultimate responsibility for these matters. Refer to the Directors Report of the Annual Report for details regarding the remuneration of non-executive directors, executive directors and senior executives.

Statement of Comprehensive Income

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009

| | Note | Consolidated | | Parent | |
|---|-------|--------------------|----------------------|--------------------|----------------------|
| | | 2009 \$ | 2008 \$ | 2009 \$ | 2008 \$ |
| Other income | 3 (b) | 3,108 | 432 | 3,108 | 432 |
| Employee benefits expense | 3 (d) | (850,323) | (3,953,207) | (850,323) | (3,953,207) |
| Professional fees | | (195,195) | (246,041) | (195,195) | (246,041) |
| Insurance expense | | (94,842) | (433,471) | (94,842) | (433,471) |
| Impairment expense | 3 (h) | - | (701,162) | (1,170,341) | (109,764,784) |
| Share of loss of joint venture | | (166,702) | (315,280) | - | - |
| Other expenses | | (61,028) | (223,740) | (61,216) | (133,261) |
| Loss before income tax | | (1,364,982) | (5,872,469) | (2,368,809) | (114,530,332) |
| Income tax expense | | - | - | - | - |
| Loss for the year from continuing operations | | (1,364,982) | (5,872,469) | (2,368,809) | (114,530,332) |
| Loss for the year from discontinued operations | 32 | (4,020,801) | (141,592,492) | - | - |
| Loss for the year attributable to members of the parent entity | | (5,385,783) | (147,464,961) | (2,368,809) | (114,530,332) |
| Other comprehensive income | | | | | |
| Exchange differences arising on translation of foreign operations | | 13,987,627 | (4,628,632) | - | - |
| Total comprehensive income for the year | | 8,601,844 | (152,093,593) | (2,368,809) | (114,530,332) |
| Loss attributable to: | | | | | |
| Owners of the parent | | (5,385,783) | (144,334,160) | | |
| Non-controlling interests | | - | (3,130,801) | | |
| | | (5,385,783) | (147,464,961) | | |
| Earnings/(loss) per share: | | <i>Cents</i> | <i>Cents</i> | | |
| From continuing and discontinued operations: | | | | | |
| Basic earnings per share | 5 | (4.19) | (113.17) | | |
| From continuing operations: | | | | | |
| Basic earnings per share | 5 | (1.06) | (4.60) | | |
| From discontinued operations: | | | | | |
| Basic earnings per share | 5 | (3.13) | (108.56) | | |

The above statement of comprehensive income should be read in conjunction with the accompanying notes

Statement of Financial Position

AS AT 31 DECEMBER 2009

| | Note | Consolidated | | Parent | |
|---|-------|---------------|---------------|---------------|---------------|
| | | 2009 \$ | 2008 \$ | 2009 \$ | 2008 \$ |
| CURRENT ASSETS | | | | | |
| Cash and cash equivalents | 6 | 144,610 | 1,790,038 | 144,610 | 1,834 |
| Trade and other receivables | 7 | 1,636 | 4,088,091 | 1,636 | 8,080 |
| Inventories | 8 | - | 378,969 | - | - |
| Other current assets | 9 | 5,105 | 142,412 | 5,105 | 96,491 |
| Discontinued operations | 32(b) | - | 1,134,747 | - | - |
| | | 151,351 | 7,534,257 | 151,351 | 106,405 |
| Assets classified as held for sale | 34 | 208,258 | - | - | - |
| TOTAL CURRENT ASSETS | | 359,609 | 7,534,257 | 151,351 | 106,405 |
| NON-CURRENT ASSETS | | | | | |
| Available-for-sale investments | 10 | - | 46,455 | - | - |
| Property, plant and equipment | 11 | - | 18,249,057 | - | - |
| Other financial assets | 13 | 119,069 | 344,894 | - | 2,364,730 |
| Intangible assets | 14 | - | 1,085,389 | - | - |
| TOTAL NON-CURRENT ASSETS | | 119,069 | 19,725,795 | - | 2,364,730 |
| TOTAL ASSETS | | 478,678 | 27,260,052 | 151,351 | 2,471,135 |
| CURRENT LIABILITIES | | | | | |
| Trade and other payables | 16 | 549,585 | 8,779,951 | 549,585 | 417,401 |
| Short-term borrowings | 17 | - | 17,380,883 | - | 87,277 |
| Other current liabilities | 18 | - | 1,402,133 | - | - |
| Discontinued operations | 32(b) | 26,891,343 | 35,477,684 | - | - |
| | | 27,440,928 | 63,040,651 | 549,585 | 504,678 |
| Liabilities directly associated with assets classified as held for sale | 34 | 30,358 | - | - | - |
| TOTAL CURRENT LIABILITIES | | 27,471,286 | 63,040,651 | 549,585 | 504,678 |
| NON-CURRENT LIABILITIES | | | | | |
| Long-term provisions | 19 | - | 305,081 | - | - |
| Other non-current liabilities | 18 | - | 136,667 | - | 623,777 |
| Financial liabilities | 20 | 1,403,326 | 1,403,326 | 1,403,326 | 1,403,326 |
| TOTAL NON-CURRENT LIABILITIES | | 1,403,326 | 1,845,074 | 1,403,326 | 2,027,103 |
| TOTAL LIABILITIES | | 28,874,612 | 64,885,725 | 1,952,911 | 2,531,781 |
| NET ASSETS | | (28,395,934) | (37,625,673) | (1,801,560) | (60,646) |
| EQUITY | | | | | |
| Issued capital | 21 | 157,066,028 | 157,066,028 | 157,066,028 | 157,066,028 |
| Reserves | 22 | 5,160,475 | (9,455,047) | 6,657,176 | 6,029,281 |
| Retained losses | 23 | (190,622,437) | (185,236,654) | (165,524,764) | (163,155,955) |
| Parent interests | | (28,395,934) | (37,625,673) | (1,801,560) | (60,646) |
| Non-controlling interest | 24 | - | - | - | - |
| TOTAL EQUITY | | (28,395,934) | (37,625,673) | (1,801,560) | (60,646) |

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

Statement of Changes in Equity

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009

| | Consolidated | | | | | |
|--|------------------------------------|--------------------------|---|----------------------------------|---------------------------------------|---------------|
| | Share Capital Ordinary \$ | Retained Losses \$ | Foreign Currency Translation Reserve \$ | Share Option Reserve \$ | Non- Controlling Interest \$ | Total \$ |
| Balance at 1 January 2008 | 146,842,064 | (40,902,494) | (10,855,696) | 1,997,421 | 3,130,801 | 100,212,096 |
| Shares and options issued upon acquisition of the assets of Novalux Inc. | | | | | | |
| 21/22 | 8,007,005 | - | | 417,605 | - | 8,424,610 |
| Shares issued in relation to acquisition of Verrillon Holdings Pty Ltd (deferred consideration) | | | | | | |
| 21 | 2,224,893 | - | - | - | - | 2,224,893 |
| Total comprehensive income from continuing and discontinued operations for the year | | | | | | |
| 21 | - (7,934) | (144,334,160) | (4,628,632) | - | (3,130,801) | (152,093,593) |
| Transaction costs | | | | | | |
| 21 | (7,934) | - | - | - | - | (7,934) |
| Share-based payments | | | | | | |
| 15/22 | - | - | - | 3,614,255 | - | 3,614,255 |
| Balance at 31 December 2008 | 157,066,028 | (185,236,654) | (15,484,328) | 6,029,281 | - | (37,625,673) |
| Balance at 1 January 2009 | 157,066,028 | (185,236,654) | (15,484,328) | 6,029,281 | - | (37,625,673) |
| Total comprehensive income for the year from continuing and discontinued operations for the year | | | | | | |
| 15/22 | - | (5,385,783) | 13,987,627 | - | - | 8,601,844 |
| Share-based payments | | | | | | |
| 15/22 | - | - | - | 627,895 | - | 627,895 |
| Balance at 31 December 2009 | 157,066,028 | (190,622,437) | (1,496,701) | 6,657,176 | - | (28,395,934) |

The above statement of changes in equity should be read in conjunction with the accompanying notes

Statement of Changes in Equity (continued) FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009

| | Parent | | | |
|--|------------------------------------|--------------------------|----------------------------------|--------------------|
| | Share Capital Ordinary \$ | Retained Losses \$ | Share Option Reserve \$ | Total \$ |
| Balance at 1 January 2008 | 146,842,064 | (48,625,623) | 1,997,421 | 100,213,862 |
| Shares and options issued upon acquisition of the assets of Novalux Inc. | | | | |
| 21/22 | 8,007,005 | - | 417,605 | 8,424,610 |
| Shares issued in relation to acquisition of Verrillon Holdings Pty Ltd (deferred consideration) | | | | |
| 21 | 2,224,893 | - | - | 2,224,893 |
| Total comprehensive income from continuing and discontinued operations for the year | | | | |
| 21 | - | (114,530,332) | - | (114,530,332) |
| Transaction costs | (7,934) | - | - | (7,934) |
| Share-based payments | - | - | 3,614,255 | 3,614,255 |
| Balance at 31 December 2008 | 157,066,028 | (163,155,955) | 6,029,281 | (60,646) |
| Balance at 1 January 2009 | 157,066,028 | (163,155,955) | 6,029,281 | (60,646) |
| Total comprehensive income for the year from continuing and discontinued operations for the year | | | | |
| 15/22 | - | (2,368,809) | - | (2,368,809) |
| Share-based payments | - | - | 627,895 | 627,895 |
| Balance at 31 December 2009 | 157,066,028 | (165,524,764) | 6,657,176 | (1,801,560) |

The above statement of changes in equity should be read in conjunction with the accompanying notes

Statement of Cash Flows

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009

| | | Consolidated | | Parent | |
|--|--------------|--------------------|--------------------|------------------|------------------|
| | | 2009 | 2008 | 2009 | 2008 |
| | | \$ | \$ | \$ | \$ |
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | | |
| Receipts from customers | | 2,352,883 | 35,323,000 | - | - |
| Payments to suppliers and employees | | (4,271,585) | (40,953,000) | (300,215) | (608,986) |
| Finance costs | | - | (2,577,000) | - | - |
| Interest received | | 3,108 | 92,000 | 3,108 | - |
| NET CASH USED IN OPERATING ACTIVITIES | 6 (b) | (1,915,594) | (8,115,000) | (297,107) | (608,986) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | | |
| Net proceeds from the sale/abandonment of subsidiaries | | 304,926 | - | 2,371,168 | - |
| Purchase of property, plant and equipment | | - | (1,513,000) | - | - |
| Proceeds from sale of property, plant and equipment | | 504,583 | 4,518,000 | - | - |
| Payments on amounts due to related parties | | - | (547,000) | - | - |
| Amounts received from related parties | | - | 161,000 | - | - |
| Loan to wholly-owned subsidiaries | | - | - | (1,844,008) | (250,000) |
| Repayment of loans from wholly owned subsidiaries | | - | - | - | 460,774 |
| Loan from wholly-owned subsidiary | | - | - | - | 623,773 |
| NET CASH PROVIDED BY/(USED IN) INVESTING ACTIVITIES | | 809,509 | 2,619,000 | 527,160 | 834,547 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | | | |
| Proceeds from borrowings | | - | 4,658,000 | - | 95,211 |
| Repayment of borrowings | | (591,860) | (4,245,000) | (87,277) | (364,561) |
| NET CASH PROVIDED BY/(USED IN) FINANCING ACTIVITIES | | (591,860) | 413,000 | (87,277) | (269,350) |
| Net (decrease)/increase in cash and cash equivalents | | (1,697,945) | (5,083,000) | 142,776 | (43,789) |
| Net foreign exchange differences | | 30,003 | (544,995) | - | - |
| Cash at the beginning of the year | | 1,839,005 | 7,467,000 | 1,834 | 45,623 |
| CASH AT THE END OF THE YEAR | 6 (a) | 171,063 | 1,839,005 | 144,610 | 1,834 |

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

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009

NOTES TO THE FINANCIAL STATEMENTS

This financial report includes the consolidated financial statements and notes of Arasor International Limited and controlled entities ('Group') and the separate financial statements and notes of Arasor International Limited as an individual parent entity ('Parent Entity').

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Basis of Preparation

The financial report is a general-purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001 and Australian Accounting Standards (and other pronouncements of the AASB). The financial report has been prepared on a historical cost basis using Australian dollars, which is the presentation currency. Arasor International Ltd is a company limited by shares incorporated and domiciled in Australia whose shares are publicly traded on the Australian Securities Exchange.

b. Statement of compliance

The financial report complies with Australian Accounting Standards, which include Australian equivalents to International Financial Reporting Standards (AIFRS). Australian Accounting Standards and Interpretations that have recently been issued or amended but are not yet effective have not been adopted by the Group for the annual reporting period ended 31 December 2009.

The financial statements were authorised for issue by the directors on 29 December 2010.

c. Basis of consolidation

The consolidated financial statements comprise the financial statements of Arasor International Ltd and its subsidiaries as at 31 December each year (the Group).

The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

In preparing the Group financial statements, all intercompany balances and transactions, income and expenses and profit and losses resulting from intra-group transactions have been eliminated in full.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group.

Minority interests represent the portion of profit or loss and net assets in Arasor GuangZhou Co., Limited not held by the Group and are presented separately in the statement of comprehensive income and within equity in the consolidated statement of financial performance.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

d. Business combinations

The purchase method of accounting is used to account for all business combinations regardless of whether equity instruments or other assets are acquired. Cost is measured as the fair value of the assets given, shares issued or liabilities incurred or assumed at the date of exchange plus costs directly attributable to the combination. Where equity instruments are issued in a business combination, the fair value of the instruments is their published market price as at the date of exchange unless, in rare circumstances, it can be demonstrated that the published price at the date of exchange is an unreliable indicator of fair value and that other evidence and valuation methods provide a more reliable measure of fair value. Transaction costs arising on the issue of equity instruments are recognised directly in equity.

Except for non-current assets or disposal groups classified as held for sale (which are measured at fair value less costs to sell), all identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of the business combination over the net fair value of the Group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the Group's share of the net fair value of the identifiable net assets of the subsidiary, the difference is recognised as a gain in the statement of comprehensive income, but only after a reassessment of the identification and measurement of the net assets acquired.

e. Joint Venture Arrangements

Jointly controlled entities

Interests in jointly controlled entities in which the Group is a venturer (and so has joint control) are accounted for under the equity method in the consolidated financial statements and the cost method in the company financial statements.

f. Revenue Recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods

Revenue is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Risks and rewards of ownership are considered passed to the buyer at the time of delivery of the goods to the customer.

Interest income

Interest revenue is recognised on a proportional basis taking into account the interest rates applicable to the financial asset.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

g. Government grants

Government grants are recognised when there is reasonable assurance that the grant will be received and all attaching conditions will be complied with.

When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

When the grant relates to an asset, the fair value is credited to a deferred income account and is released to the statement of comprehensive income over the expected useful life of the relevant asset by equal annual instalments to match the depreciation charge.

h. Borrowing costs

Borrowing costs are recognised as an expense when incurred.

i. Leases

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are recognised as an expense in profit or loss.

Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term. Lease incentives are recognised in the income statement as an integral part of the total lease expense.

j. Cash and cash equivalents

Cash and short-term deposits in the statement of financial position comprise cash at bank and in hand and short term deposits with an original maturity of 3 months or less.

For the purposes of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above.

k. Trade and other receivables

All debtors are recognised at cost less provision for doubtful debts, which in practice will equal the amounts receivable upon settlement. Collectability of trade debtors is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off. A provision for doubtful receivables is established when there is objective evidence that the Group will not be able to collect on all amounts due according to the original terms of receivables. The amount of the provision is recognised in the statement of comprehensive income.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

l. Inventories

Inventories are valued at the lower of cost or net realisable value.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

Raw materials - purchase cost on a first-in, first-out basis; and

Finished goods and work-in-progress - cost of direct materials and labour and a proportion of manufacturing overheads based on normal operating capacity but excluding borrowing costs.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

m. Foreign currency translation

The functional currency for the Group is US dollars and presentation currency is Australian dollars. The Group determines each entity's functional currency and items included in the financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are initially recorded in the local currency by applying the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are restated at the rate of exchange ruling at the reporting date.

All exchange differences in relation to the translation from local currency to functional currency are taken to profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

As at the reporting date the assets and liabilities of all of the Groups subsidiaries are translated into the presentation currency of Arasor International Ltd at the rate of exchange ruling at the reporting date and items in the statement of comprehensive income are translated at the weighted average exchange rate for the year where this approximates the rate at the date of the transaction.

The exchange differences arising on the translation of functional currency to presentation currency are taken directly to a separate component of equity.

On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in profit or loss.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

n. Income tax

Income tax expense or benefit for the period is the tax payable on the current period's taxable income based on the notional income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and to unused tax losses. Current and deferred tax expense attributable to amounts recognised directly in equity is also recognised directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences except:

- when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and that, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the taxable temporary difference is associated with investments in subsidiaries, associates or interests in joint ventures, and the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; or
- when the deductible temporary difference is associated with investments in subsidiaries, associates or interests in joint ventures, in which case a deferred tax asset is only recognised to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and deferred tax liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority.

o. Other taxes

Revenues, expenses and assets are recognised net of the amount of Goods and Services Tax (GST) and Value Added Tax (VAT) except:

- when the GST or VAT incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST or VAT is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables, which are stated with the amount of GST/VAT included.

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

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

Commitments and contingencies are disclosed net of the amount of GST and VAT recoverable from, or payable to, the taxation authority.

p. Property, plant and equipment

Plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Such cost includes the cost of replacing parts that are eligible for capitalisation when the cost of replacing the parts is incurred. Similarly, when each major inspection is performed, its cost is recognised in the carrying amount of the plant and equipment as a replacement only if it is eligible for capitalisation.

Depreciation is calculated on a straight-line over the estimated useful life of the assets as follows:

| | |
|------------------------|-------------|
| Buildings | 20 years |
| Machinery | 10 years |
| Vehicles | 5 years |
| Furniture and fittings | 3 - 5 years |
| Electronic equipment | 3 - 5 years |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

The assets' residual values, useful lives and amortisation methods are reviewed, and adjusted if appropriate, at each financial year end.

q. Intangible assets

Intangible assets acquired separately or in a business combination are initially measured at cost. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are expensed against profits in the year in which the expenditure is incurred.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, which is a change in accounting estimate. The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed each reporting period to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate and is thus accounted for on a prospective basis.

Research and development costs

All research costs are expensed as incurred.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

r. Financial Instruments

Recognition

Financial instruments are initially measured at cost on trade date, which includes transaction costs, when the related contractual rights or obligations exist. Subsequent to initial recognition these instruments are measured as set out below.

Financial liabilities

Non-derivative financial liabilities are recognised at amortised cost, comprising original debt less principal payments and amortisation.

Available-for-sale financial assets

Available-for-sale financial assets are reflected at fair value. Unrealised gains and losses arising from changes in fair value are taken directly to equity.

Fair value

Fair value is determined based on current bid prices for all quoted investments. Valuation techniques are applied to determine the fair value for all unlisted securities, including recent arm's length transactions, reference to similar instruments and option pricing models.

Impairment

At each reporting date, the Group assess whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a significant or prolonged decline in the value of the instrument is considered to determine whether an impairment has arisen. Impairment losses are recognised in the statement of comprehensive income.

s. Impairment of non-financial assets

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of its fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or Groups of assets and the asset's value in use cannot be estimated to be close to its fair value. In such cases the asset is tested for impairment as part of the cash-generating unit to which it belongs. When the carrying amount of an asset or cash-generating unit exceeds its recoverable amount, the asset or cash-generating unit is considered impaired and is written down to its recoverable amount. Impairment losses are recognised in the statement of comprehensive income.

t. Trade and other payables

Trade payables and other payables are carried at cost and represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

u. Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost.

v. Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the risks specific to the liability.

w. Employee leave benefits

Wages, salaries, annual leave and sick leave

Liabilities for wages and salaries, including non-monetary benefits and annual leave, are expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and are measured at the rates paid or payable. Amounts after 12 months have been recognised as non-current liabilities at their present value.

x. Share-based payment transactions

The Group provides benefits to employees and consultants of the Group in the form of share-based payments, whereby employees or consultants receive option incentives (equity-settled transactions).

There is currently one plan in place to provide these benefits, the Employee Share Option Plan (ESOP) which provides benefits to directors and employees.

The cost of these equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The cost is recognised as an expense in the statement of comprehensive income, together with a corresponding increase in the share option reserve, when the options are issued. The fair value is determined using the Black Scholes option pricing model.

Upon the exercise of options, the balance of share based payments reserve relating to those options is transferred to share capital.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

y. **Non-current assets (or disposal groups) and discontinued operations**

Non-current assets (or disposal groups) are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing their use. They are measured at the lower of their carrying amount and fair value less costs to sell.

An impairment loss is recognised for any initial or subsequent write down of the asset (or discontinued operation) to fair value less costs to sell. A gain is recognized for any subsequent increases in fair value less costs to sell of an asset, but not in excess of any cumulative impairment loss previously recognized. A gain or loss not previously recognised by the date of the sale of the non-current asset is recognised at the date of derecognition.

Assets of a disposal group are presented separately from the other assets in the statement of financial position. The liabilities of a disposal group are present separately from the other liabilities in the statement of financial position.

A discontinued operation that is a component of the entity that has been disposed of or abandoned is classified as held for sale and that represents a separate major line of business or geographical area of operations, is part of a single coordinated plan to dispose of such a line of business or area of operations, or is a subsidiary acquired exclusively with a view to resale. The results of discontinued operations are presented separately on the face of the statement of comprehensive income.

z. **Contributed equity**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

aa. **Earnings per share**

Basic earnings per share is calculated as net profit attributable to members of the parent, adjusted to exclude any costs of servicing equity (other than dividends), divided by the weighted average number of ordinary shares, adjusted for any bonus element.

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

ab. **Comparatives**

When required by accounting standards, comparative figures have been adjusted to conform to changes in presentation for the current financial year. The financial statements of Arasor have been adjusted in light of the Group's discontinued operations in accordance with AASB 5 'Non-current Assets Held for Sale and Discontinued Operations'.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

ac. Significant accounting judgements, estimates and assumptions

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to assets, liabilities, contingent liabilities, revenue and expenses. Management bases its judgements and estimates on historical experience and on other various factors it believes to be reasonable under the circumstances, the result of which form the basis of the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions and conditions.

Management has identified the following critical accounting policies for which significant judgements, estimates and assumptions are made. Actual results may differ from these estimates under different assumptions and conditions and may materially affect financial results or the financial position reported in future periods.

Further details of the nature of these assumptions and conditions may be found in the relevant notes to the financial statements.

Significant accounting estimates and assumptions

Share-based payment transactions

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by an using the Black-Scholes model, with the assumptions detailed in note15. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities within the next annual reporting period but may impact expenses and equity.

Intangible assets – impairment

The group tests annually whether the intangible assets held have suffered any impairment in accordance with its accounting policies. The recoverable amounts of cash generating units have been determined with reference to value in use calculations.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

ad. Adoption of new and revised accounting standards

During the current year the group adopted all of the new and revised Australian Accounting Standards and Interpretations applicable to its operations that became mandatory.

The adoption of these standards has impacted the recognition, measurement and disclosure of certain transactions. The following is an explanation of the impact that adoption of these standards and interpretations has had on the financial statements.

AASB 3: Business Combinations

In March 2008 the Australian Accounting Standards Board revised AASB 3 and as a result, some aspects of business combination accounting have changed. The changes only apply to business combinations first recognised after 1 July 2009.

Recognition and measurement impact

Recognition of acquisition costs - The revised standard requires that all acquisition costs are expensed in the period in which they occur. Previously these costs were capitalised as part of the cost of the business combination.

Measurement of contingent consideration - The revised standard requires that contingent consideration associated with a business combination be included as part of the cost of the business combination. They are recognised at the fair value of expected payment. Any subsequent changes in the fair value or probability of settlement are recognised in the statement of comprehensive income, except to the extent that they relate to conditions that existed at the date of acquisition and that are identified during any "Measurement period." In this case the cost of acquisition is adjusted. The previous version of the standard allowed such changes to be recognised as a cost of the combination impacting goodwill.

AASB 8: Operating Segments

In February 2007, the Australian Accounting Standards Board issued AASB 8 which replaced AASB 114: Segment Reporting. Consequently, some of the required operating segment disclosures have changed. In addition, there is a possible impact on the impairment testing of goodwill allocated to cash generating units (CGUs) of the entity. Set out below is an overview of the key changes and the impact on the Consolidated group's financial statements.

Identification and measurement of segments - AASB 8 requires a "management approach" to the identification, measurement and disclosure of operating segments. This approach requires that segments are identified on the basis of internal reports that are regularly reviewed by management, for the purpose of allocating resources and assessing performance.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

Unlike AASB 114 this could identify segments that primarily or exclusively sell to other internal operating segments. Under AASB 114, segments were identified by business and geographical areas, and only segments deriving revenue from external sources were considered. The adoption of the management approach to segment reporting has identified reportable segments largely consistent with the prior year.

AASB 101: Presentation of Financial Statements

In September 2007, the Australian Accounting Standards Board revised AASB 101 and as a result, there have been changes to the presentation and disclosure of certain information within the financial statements. An overview of the key impacts on the Consolidated group's financial statements is set out below.

Terminology changes - The revised version of AASB 101 contains a number of terminology changes, including the amendment of the names of the primary financial statements and the change of the term "minority interests" to "non-controlling interests."

Reporting changes in equity - The revised AASB 101 requires all changes in equity arising from transactions with owners, in their capacity as owners, to be recognised in the statement of changes in equity, with all other changes in equity to be recognised in a new statement of comprehensive income. Previously, all changes in equity were recognised in the statement of changes in equity.

Statement of comprehensive income - The revised standard requires that all income and expenses are presented in either a single statement of comprehensive income or in two statements, one being a separate income statement as well as a new statement of comprehensive income. Previously, only an income statement was required. The Consolidated group has adopted the single statement approach and the financial statements now include a statement of comprehensive income that replaces the previously reported income statement.

Other comprehensive income - The revised standard introduces the concept of "other comprehensive income" which comprises income and expenses that are not recognised in profit or loss as required by Australian Accounting Standards. Items of other comprehensive income are to be disclosed in the statement of comprehensive income. Entities are required to disclose the income tax relating to each component of other comprehensive income. The previous version of AASB 101 did not contain an equivalent concept.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

ae. New Accounting Standards for Application in Future Periods

The AASB has issued new and amended accounting standards and interpretations that have mandatory application dates for future reporting periods. The Group has decided against early adoption of these standards. A discussion of those future requirements and their impact on the Group follows:

AASB 9: Financial Instruments and AASB 2009-11: Amendments to Australian Accounting Standards arising from AASB 9 [AASB 1, 3, 4, 5, 7, 101, 102, 108, 112, 118, 121, 127, 128, 131, 132, 136, 139, 1023 & 1038 and Interpretations 10 & 12] (applicable for annual reporting periods commencing on or after 1 January 2013).

These standards are applicable retrospectively and amend the classification and measurement of financial assets. The Group has not yet determined the potential impact on the financial statements.

The changes made to accounting requirements include:

- simplifying the classifications of financial assets into those carried at amortised cost and those carried at fair value;
- simplifying the requirements for embedded derivatives;
- removing the tainting rules associated with held-to-maturity assets;
- removing the requirements to separate and fair value embedded derivatives for financial assets carried at amortised cost;
- allowing an irrevocable election on initial recognition to present gains and losses on investments in equity instruments that are not held for trading in other comprehensive income. Dividends in respect of these investments that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument; and
- reclassifying financial assets where there is a change in an entity's business model as they are initially classified based on:
 - a) the objective of the entity's business model for managing the financial assets; and
 - b) the characteristics of the contractual cash flows.

AASB 124: Related Party Disclosures (applicable for annual reporting periods commencing on or after 1 January 2011).

This standard removes the requirement for government related entities to disclose details of all transactions with the government and other government related entities and clarifies the definition of a related party to remove inconsistencies and simplify the structure of the standard. No changes are expected to materially affect the Group.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

AASB 2009-4: Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 2 and AASB 138 and AASB Interpretations 9 & 16] (applicable for annual reporting periods commencing from 1 July 2009) and AASB 2009-5: Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 5, 8, 101, 107, 117, 118, 136 & 139] (applicable for annual reporting periods commencing from 1 January 2010).

These standards detail numerous non-urgent but necessary changes to accounting standards arising from the IASB's annual improvements project. No changes are expected to materially affect the Group.

AASB 2009-8: Amendments to Australian Accounting Standards – Group Cash-settled Share-based Payment Transactions [AASB 2] (applicable for annual reporting periods commencing on or after 1 January 2010).

These amendments clarify the accounting for group cash-settled share-based payment transactions in the separate or individual financial statements of the entity receiving the goods or services when the entity has no obligation to settle the share-based payment transaction. The amendments incorporate the requirements previously included in Interpretation 8 and Interpretation 11 and as a consequence, these two Interpretations are superseded by the amendments. These amendments are not expected to impact the Group.

AASB 2009-9: Amendments to Australian Accounting Standards – Additional Exemptions for First-time Adopters [AASB 1] (applicable for annual reporting periods commencing on or after 1 January 2010).

These amendments specify requirements for entities using the full cost method in place of the retrospective application of Australian Accounting Standards for oil and gas assets, and exempt entities with existing leasing contracts from reassessing the classification of those contracts in accordance with Interpretation 4 when the application of their previous accounting policies would have given the same outcome. These amendments are not expected to impact the Group.

AASB 2009-10: Amendments to Australian Accounting Standards – Classification of Rights Issues [AASB 132] (applicable for annual reporting periods commencing on or after 1 February 2010).

These amendments clarify that rights, options or warrants to acquire a fixed number of an entity's own equity instruments for a fixed amount in any currency are equity instruments if the entity offers the rights, options or warrants pro-rata to all existing owners of the same class of its own non-derivative equity instruments. These amendments are not expected to impact the Group.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

AASB 2009-12: Amendments to Australian Accounting Standards [AASBs 5, 8, 108, 110, 112, 119, 133, 137, 139, 1023 & 1031 and Interpretations 2, 4, 16, 1039 & 1052] (applicable for annual reporting periods commencing on or after 1 January 2011).

This standard makes a number of editorial amendments to a range of Australian Accounting Standards and Interpretations, including amendments to reflect changes made to the text of International Financial Reporting Standards by the IASB. The standard also amends AASB 8 to require entities to exercise judgment in assessing whether a government and entities known to be under the control of that government are considered a single customer for the purposes of certain operating segment disclosures. These amendments are not expected to impact the Group.

AASB 2009-13: Amendments to Australian Accounting Standards arising from Interpretation 19 [AASB 1] (applicable for annual reporting periods commencing on or after 1 July 2010).

This standard makes amendments to AASB 1 arising from the issue of Interpretation 19. The amendments allow a first-time adopter to apply the transitional provisions in Interpretation 19. This standard is not expected to impact the Group.

AASB 2009-14: Amendments to Australian Interpretation – Prepayments of a Minimum Funding Requirement [AASB Interpretation 14] (applicable for annual reporting periods commencing on or after 1 January 2011).

This standard amends Interpretation 14 to address unintended consequences that can arise from the previous accounting requirements when an entity prepays future contributions into a defined benefit pension plan.

AASB Interpretation 19: Extinguishing Financial Liabilities with Equity Instruments (applicable for annual reporting periods commencing on or after 1 July 2010).

This Interpretation deals with how a debtor would account for the extinguishment of a liability through the issue of equity instruments. The Interpretation states that the issue of equity should be treated as the consideration paid to extinguish the liability, and the equity instruments issued should be recognised at their fair value unless fair value cannot be measured reliably in which case they shall be measured at the fair value of the liability extinguished. The Interpretation deals with situations where either partial or full settlement of the liability has occurred. This Interpretation is not expected to impact the Group.

The Group does not anticipate the early adoption of any of the above Australian Accounting Standards.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

2. SEGMENT INFORMATION

The directors have considered the requirements of AASB 8 Operating Segments and the internal reports that are reviewed by the chief operating decision maker (the Board) in allocating resources and have concluded at this time that there are no separately identifiable segments. This decision has been made specifically in light of the reduced size and scope of the Group's operations given the restructure of the Group including its abandoned and discontinued operations as disclosed throughout the report.

| | Consolidated | | Parent | |
|--|--------------|------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |

3. REVENUE AND EXPENSES

(a) Revenue

From discontinued operations:

Sale of goods

| | | | | |
|--|-----------|------------|---|---|
| | | | | |
| | 1,800,725 | 20,677,977 | - | - |
| | 1,800,725 | 20,677,977 | - | - |

(b) Other income

From continuing operations:

Interest income

| | | | | |
|--|-------|-----|-------|-----|
| | 3,108 | 432 | 3,108 | 432 |
| | 3,108 | 432 | 3,108 | 432 |

From discontinued operations:

Interest income

| | | | | |
|--|-------|--------|-------|-----|
| | 741 | 91,774 | - | - |
| | 3,849 | 92,206 | 3,108 | 432 |

(c) Expenses

Depreciation of non-current assets

From discontinued operations:

Plant and equipment

Buildings

| | | | | |
|--|---------|-----------|---|---|
| | 171,877 | 3,097,592 | - | - |
| | - | 563,283 | - | - |
| | 171,877 | 3,660,875 | - | - |

Amortisation of intangibles

From discontinued operations:

Customer lists

Patents and trademarks

| | | | | |
|--|---|-----------|---|---|
| | - | 1,267,919 | - | - |
| | - | 3,548,409 | - | - |
| | - | 4,816,328 | - | - |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|--|--------------|------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |

3. REVENUE AND EXPENSES (Continued)

(d) Employees benefits expense

From continuing operations:

Wages, salaries, directors fees and other remuneration expenses

Share-based payments expense

| | | | |
|---------|-----------|---------|-----------|
| 222,427 | 338,952 | 222,427 | 338,952 |
| 627,895 | 3,614,255 | 627,895 | 3,614,255 |
| 850,322 | 3,953,207 | 850,322 | 3,953,207 |

From discontinued operations:

Wages, salaries, directors fees and other remuneration expenses

| | | | |
|-----------|------------|---------|-----------|
| 664,307 | 7,564,504 | - | - |
| 1,514,629 | 11,517,711 | 850,322 | 3,953,207 |

(e) Net foreign exchange gain / (loss)

Total foreign exchange gain/(loss)

| | | | |
|---|---------|---|---|
| - | 332,702 | - | - |
|---|---------|---|---|

(f) Finance costs

From discontinued operations:

Term loan

Notes payables

Other facilities (see note 17)

| | | | |
|-----------|-----------|---|---|
| - | 949,888 | - | - |
| 1,054,169 | 1,570,473 | - | - |
| - | 140,546 | - | - |
| 1,054,169 | 2,660,907 | - | - |

(g) Bad debts

From discontinued operations:

Bad and doubtful debts - trade debtors

| | | | |
|---|------------|---|---|
| - | 59,474,074 | - | - |
|---|------------|---|---|

(h) Impairment expense

From continuing operations:

Intercompany loans and investments to wholly owned subsidiaries

Intangible assets

Other

| | | | |
|---|-----------|-----------|-------------|
| - | - | 1,170,341 | 109,764,784 |
| - | 701,162 | - | - |
| - | 315,280 | - | - |
| - | 1,016,442 | 1,170,341 | 109,764,784 |

From discontinued operations:

Intangible assets

Property, plant and equipment

Prepayments

Pledged deposits

Other

| | | | |
|---------|------------|-----------|-------------|
| - | 47,770,224 | - | - |
| - | 2,847,398 | - | - |
| - | 1,352,822 | - | - |
| - | 1,084,410 | - | - |
| 134,711 | 893,007 | - | - |
| 134,711 | 53,947,861 | - | - |
| 134,711 | 54,964,303 | 1,170,341 | 109,764,784 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

4. INCOME TAX

| | Consolidated | | Parent | |
|--|--------------|------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| Statement of comprehensive income | | | | |
| Current income tax charge/(benefit) | - | - | - | - |
| Income tax expense/(benefit) reported in the statement of comprehensive income | - | - | - | - |

A reconciliation between tax expense and the product of accounting profit before income tax multiplied by the Group's applicable income tax rate is as follows:

| | | | | |
|---|-------------|---------------|-------------|---------------|
| Loss before income tax from continuing operations | (1,364,982) | (5,872,469) | (2,368,809) | (114,530,332) |
| Loss before income tax from discontinued operations | (4,020,801) | (141,592,492) | - | - |
| | (5,385,783) | (147,464,961) | (2,368,809) | (114,530,332) |

| | | | | |
|---|-------------|--------------|-----------|--------------|
| At the Group's statutory income tax rate of 30% (2008: 30%) | (1,615,735) | (44,239,488) | (710,643) | (34,359,100) |
| Non deductible loss on disposal/abandonment of subsidiaries | 509,878 | - | - | - |
| Non deductible share of joint venture loss | 50,011 | - | - | - |
| Share based payments | 188,369 | 1,084,277 | 188,369 | 1,084,277 |
| Loan impairment | - | - | - | 32,929,435 |
| Difference in overseas tax rates | (120,624) | 520,264 | - | - |
| Impairment of assets | - | 17,340,102 | - | - |
| Tax losses not recognised | 988,101 | 25,294,845 | 522,274 | 345,388 |
| | - | - | - | - |

The Group has tax losses arising in the following jurisdictions:

Australia AUD 13,542,749

Australian tax losses are available indefinitely for offset against future taxable profits of Arasor International Ltd. No Chinese or North American losses have been listed as the tax returns have not been prepared and the Group has abandoned or are to abandon the entities to which the losses related (refer to note 32).

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

5. EARNINGS/(LOSS) PER SHARE

Basic earnings/(loss) per share amounts are calculated by dividing net profit/(loss) for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit/(loss) attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The following reflects the income and share data used in the basic and diluted earnings/(loss) per share computations:

| | Consolidated | |
|--|--------------|---------------|
| | 2009 \$ | 2008 \$ |
| Loss for the year attributable to members of the parent entity | (5,385,783) | (144,334,160) |
| | 2009 No. | 2008 No. |
| | | |
| Weighted average number of ordinary shares for basic earnings per share | 128,559,267 | 127,541,270 |
| Effect of dilution | | |
| Share options | N/A | N/A |
| Weighted average number of ordinary shares adjusted for the effect of dilution | 128,559,267 | 127,541,270 |

In accordance with AASB 133 'Earnings per Share', as potential ordinary shares may only result in a situation where their conversion results in an increase in loss per share or decrease in profit per share from continuing operations, no dilutive effect has been taken into account.

| | Consolidated | | Parent | |
|--|--------------|------------|------------|------------|
| | 2009 \$ | 2008 \$ | 2009 \$ | 2008 \$ |

6. CASH AND CASH EQUIVALENTS

| | | | | |
|---|---------|-----------|---------|-------|
| Cash in bank and on hand | 144,610 | 744,952 | 144,610 | 1,834 |
| Short-term deposits | - | 1,045,086 | - | - |
| | 144,610 | 1,790,038 | 144,610 | 1,834 |
| Cash from operations held for sale or discontinued (refer to note 34) | 26,453 | 48,967 | - | - |
| | 171,063 | 1,839,005 | 144,610 | 1,834 |

6(a) Reconciliation to Statement of Cash Flows

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprise the following at 31 December:

| | | | | |
|---------------------------|---------|-----------|---------|-------|
| Cash at banks and in hand | 171,063 | 1,839,005 | 144,610 | 1,834 |
| | 171,063 | 1,839,005 | 144,610 | 1,834 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|--|--------------|---------------|-------------|---------------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 6. CASH AND CASH EQUIVALENTS (Continued) | | | | |
| 6(b) Reconciliation of net loss after tax to net cash flows from operations | | | | |
| Net loss | (5,385,783) | (144,334,160) | (2,368,809) | (114,530,332) |
| <i>Adjustments for non-cash items:</i> | | | | |
| Depreciation (discontinued operations) | 171,877 | 3,660,875 | - | - |
| Amortisation | - | 4,816,328 | - | - |
| Share-based payments | 627,895 | 3,614,255 | 627,895 | 3,614,255 |
| Non cash tax expense/(benefit) | - | - | - | - |
| Minority interest in loss of subsidiaries | - | (3,130,801) | - | - |
| Impairment expense | - | 54,964,303 | 1,170,341 | 109,764,784 |
| Loss on sale/abandonment of subsidiaries | 1,699,592 | - | - | - |
| <i>Changes in assets and liabilities:</i> | | | | |
| (Increase)/decrease in inventories | - | 2,656,000 | - | - |
| (Increase)/decrease in trade and other receivables | 558,602 | 74,452,000 | 6,444 | (4,000) |
| (Increase)/decrease in prepayments | 91,386 | 2,571,000 | 91,386 | 326,000 |
| (Increase)/decrease in other receivables | - | 1,084,000 | - | - |
| Increase/(decrease) in deferred income | - | 989,000 | - | - |
| (Decrease)/increase in trade and other payables | 320,837 | (9,715,800) | 175,636 | 220,307 |
| (Decrease)/increase in provisions | - | 258,000 | - | - |
| Net cash from operating activities | (1,915,594) | (8,115,000) | (297,107) | (608,986) |

6(c) Non-cash transactions

The group abandoned its operations in China, which resulted in a net loss of 1,924,685. Refer to note 32 in relation to this non-cash transaction.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|---|--------------|-------------|--------|-------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 7. TRADE AND OTHER RECEIVABLES (CURRENT) | | | | |
| Trade receivables (i) | - | 11,964,737 | - | - |
| Allowance for doubtful debts | - | (8,100,828) | - | - |
| | - | 3,863,909 | - | - |
| Sundry receivables | 1,636 | 224,182 | 1,636 | 8,080 |
| | 1,636 | 4,088,091 | 1,636 | 8,080 |

Trade receivables are non-interest bearing and are generally on 30-90 day terms. An allowance for doubtful debts is made when there is objective evidence that a trade receivable is impaired. No such allowance has been recognised as an expense for the current year (2008: \$34,933,000). The amount of the allowance/impairment loss has been measured as the difference between the carrying amount of the trade receivables and the estimated future cash flows expected to be received from the relevant debtors.

8. INVENTORIES

| | Consolidated | | Parent | |
|---|--------------|---------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| Finished goods (at net realisable value) | - | 378,969 | - | - |
| Total inventories at the lower of cost and net realisable value | - | 378,969 | - | - |

9. OTHER CURRENT ASSETS

| | | | | |
|-------------|-------|---------|-------|--------|
| Prepayments | 5,105 | 142,412 | 5,105 | 96,491 |
| | 5,105 | 142,412 | 5,105 | 96,491 |

10. AVAILABLE FOR SALE INVESTMENTS

| | | | | |
|-----------------------------|---|--------|---|---|
| At cost: | | | | |
| Shares in unlisted entities | - | 46,455 | - | - |
| | - | 46,455 | - | - |

The available-for-sale investment is an investment in ordinary shares, and therefore has no fixed maturity date or coupon rate.

As the unlisted available-for-sale investment has no readily available quoted market price, the investment is carried at cost which is the best estimate of its fair value. Movements in the carrying value is impacted by changes in the relevant exchange rates.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|---|--------------|-------------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 11. PROPERTY, PLANT AND EQUIPMENT | | | | |
| Plant and equipment | | | | |
| Opening balance | 16,724,983 | 13,910,255 | - | - |
| Additions | - | 701,074 | - | - |
| Acquisitions through business combinations | - | 5,976,475 | - | - |
| Disposals | - | (4,293,640) | - | - |
| Currency translation differences | - | 4,056,685 | - | - |
| Classified within discontinued operations or abandoned | (16,724,983) | (3,625,866) | - | - |
| | - | 16,724,983 | - | - |
| Accumulated depreciation | | | | |
| Opening balance | 9,215,239 | 6,252,267 | - | - |
| Depreciation for the year | - | 3,029,955 | - | - |
| Disposals | - | (882,996) | - | - |
| Currency translation differences | - | 2,474,500 | - | - |
| Classified within discontinued operations or abandoned | (9,215,239) | (1,658,487) | - | - |
| | - | 9,215,239 | - | - |
| Provision for impairment | | | | |
| Opening balance | 1,377,342 | - | - | - |
| Impairment expense | - | 2,742,445 | - | - |
| Currency translation differences | - | 314,500 | - | - |
| Classified within discontinued operations or abandoned | (1,377,342) | (1,679,603) | - | - |
| Closing balance | - | 1,377,342 | - | - |
| Net book value of plant and equipment | - | 6,132,401 | - | - |
| Plant and equipment under finance lease | | | | |
| Opening balance | - | 602,950 | - | - |
| Additions | - | - | - | - |
| Currency translation differences | - | 159,892 | - | - |
| Classified within discontinued operations | - | (762,842) | - | - |
| | - | - | - | - |
| Accumulated depreciation | | | | |
| Opening balance | - | 435,117 | - | - |
| Depreciation for the year | - | 67,637 | - | - |
| Currency translation differences | - | 131,094 | - | - |
| Classified within discontinued operations | - | (633,848) | - | - |
| | - | - | - | - |
| Provision for impairment | | | | |
| Opening balance | - | - | - | - |
| Impairment expense | - | 104,953 | - | - |
| Currency translation differences | - | 24,198 | - | - |
| Classified within discontinued operations | - | (129,151) | - | - |
| Closing balance | - | - | - | - |
| Net book value of plant and equipment under finance lease | - | - | - | - |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|--|--------------|------------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 11. PROPERTY, PLANT AND EQUIPMENT (Continued) | | | | |
| Buildings | | | | |
| Opening balance | 13,418,080 | 10,363,676 | - | - |
| Additions | - | - | - | - |
| Transfer from capital works in progress | - | 242,310 | - | - |
| Currency translation differences | - | 2,812,094 | - | - |
| Classified within discontinued operations or abandoned | (13,418,080) | - | - | - |
| | - | 13,418,080 | - | - |
| Accumulated depreciation | | | | |
| Opening balance | 1,473,401 | 679,900 | - | - |
| Depreciation for the year | - | 563,283 | - | - |
| Currency translation differences | - | 230,218 | - | - |
| Classified within discontinued operations or abandoned | (1,473,401) | - | - | - |
| | - | 1,473,401 | - | - |
| Net book value of buildings | - | 11,944,679 | - | - |
| Capital Work in progress | | | | |
| Opening balance | 171,977 | - | - | - |
| Other additions | - | 401,027 | - | - |
| Transfer to Buildings | - | (242,310) | - | - |
| Currency translation differences | - | 13,260 | - | - |
| Classified within discontinued operations or abandoned | (171,977) | - | - | - |
| Net book value of capital work in progress | - | 171,977 | - | - |
| Total net book value of property, plant and equipment | - | 18,249,057 | - | - |

12. OTHER RECEIVABLES (NON-CURRENT)

| | Consolidated | | Parent | |
|-----------------------------------|--------------|------|--------------|--------------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| Loan to wholly-owned subsidiary | - | - | 93,597,016 | 92,463,260 |
| Provision for impairment of loans | - | - | (93,597,016) | (92,463,260) |
| | - | - | - | - |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|-----------------------------------|--------------|---------|--------|-----------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 13. OTHER FINANCIAL ASSETS | | | | |
| Investment in subsidiaries | - | - | - | 2,364,730 |
| Investment in ZTEI Joint Venture | 119,068 | 344,894 | - | - |
| | 119,068 | 344,894 | - | 2,364,730 |

The ZTEI joint venture was entered into with ZTEI Corporation to develop and manufacture laser display applications. Arasor's beneficial ownership in the joint venture is 49%. The value of the investment has been written down to Arasor's share of capital assets and cash reserves at each balance date.

14. INTANGIBLE ASSETS

Customer lists

| | | | | |
|-----------------------------------|------------|------------|---|---|
| Opening balance | 21,241,818 | 18,366,408 | - | - |
| Currency translation differences | - | 2,875,410 | - | - |
| | 21,241,818 | 21,241,818 | - | - |
| Accumulated amortisation | | | | |
| Opening balance | 3,687,270 | 1,836,035 | - | - |
| Amortisation charge for the year | - | 1,267,919 | - | - |
| Currency translation differences | - | 583,316 | - | - |
| | 3,687,270 | 3,687,270 | - | - |
| Provision for impairment | | | | |
| Opening balance | 17,554,548 | - | - | - |
| Impairment expense | - | 16,193,606 | - | - |
| Currency translation differences | - | 1,360,942 | - | - |
| Closing balance | 17,554,548 | 17,554,548 | - | - |
| Carrying amount of customer lists | - | - | - | - |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

14. INTANGIBLE ASSETS (CONTINUED)

| | Consolidated | | Parent | |
|--|--------------|--------------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| Patents and trademarks | | | | |
| Opening balance | 22,934,471 | 22,779,331 | - | - |
| Other additions | - | 359,859 | - | - |
| Acquisitions through business combinations | - | 14,773,605 | - | - |
| Currency translation differences | - | 6,484,500 | - | - |
| Classified within discontinued operations or abandoned | (22,934,471) | (21,462,824) | - | - |
| | - | 22,934,471 | - | - |
| Accumulated amortisation | | | | |
| Opening balance | 4,275,710 | 2,767,055 | - | - |
| Amortisation charge for the year | - | 3,548,409 | - | - |
| Currency translation differences | - | 1,164,667 | - | - |
| Classified within discontinued operations or abandoned | (4,275,710) | (3,204,421) | - | - |
| | - | 4,275,710 | - | - |
| Provision for impairment | | | | |
| Opening balance | 17,573,372 | - | - | - |
| Impairment expense | - | 32,278,085 | - | - |
| Currency translation differences | - | 3,265,007 | - | - |
| Classified within discontinued operations or abandoned | (17,573,372) | (17,969,720) | - | - |
| | - | 17,573,372 | - | - |
| Closing balance | - | 17,573,372 | - | - |
| Carrying amount of patents and trademarks | - | 1,085,389 | - | - |
| | | - | | |
| Total carrying amount of intangible assets | - | 1,085,389 | - | - |

The estimated useful life of all intangible assets listed above for 2009 and 2008 is 10 years. The amortisation rate applied is 10% per annum on a straight line basis.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

15. SHARE BASED PAYMENTS

Employee Share Option Plan

The Company has established the Arasor International Ltd Employee Share Option Plan ('ESOP') and a summary of the Rules of the Plan are set out below:

- All employees (full time and part time) will be eligible to participate in the Plan.
- Options are granted under the Plan at the discretion of the board and if permitted by the board, may be issued to an employee's nominee.
- Each option is to subscribe for one fully paid ordinary share in the Company and will expire 5 years from its date of issue. An option is exercisable at any time from its date of issue (provided all relevant vesting conditions, if applicable, have been met. Options will be issued free. The exercise price of options will be determined by the board. The total number of shares the subject of options issued under the Plan, when aggregated with issues during the previous 5 years pursuant to the Plan and any other employee share plan, must not exceed 5% of the Company's issued share capital.
- If, prior to the expiry date of options, a person ceases to be an employee of a Group company for any reason other than retirement at age 60 or more (or such earlier age as the board permits), permanent disability, redundancy or death, the options held by that person (or that person's nominee) automatically lapse on the first to occur of a) the expiry of the period of 30 days from the date of such occurrence, and b) the expiry date. If a person dies, the options held by that person will be exercisable by that person's legal personal representative.
- Options cannot be transferred other than to the legal personal representative of a deceased option holder.
- The Company will not apply for official quotation of any options.
- Shares issued as a result of the exercise of options will rank equally with the Company's previously issued shares.
- Option holders may only participate in new issues of securities by first exercising their options.

The board may amend the Plan Rules subject to the requirements of the Listing Rules.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

15. SHARE BASED PAYMENTS (CONTINUED)

The following table illustrates the weighted average exercise prices (WAEP) and movements in share options issued during the year (including those issues outside of the ESOP plan):

| | 2009 No. | 2009 WAEP | 2008 No. | 2008 WAEP |
|--|-------------|--------------|-------------|--------------|
| Outstanding at the beginning of the year | 10,037,594 | 1.66 | 9,393,806 | 1.67 |
| Granted during the year | 3,000,000 | 0.05 | 643,788 | 1.59 |
| Forfeited during the year | (6,786,250) | 1.80 | - | - |
| Outstanding at the end of the year | 6,251,344 | 0.73 | 10,037,594 | 1.66 |
| Exercisable at the end of the year | 6,251,344 | 0.73 | 10,037,594 | 1.66 |

Refer to page 8 for a complete list of the Company's options outstanding by class.

The weighted average remaining contractual life for the share options outstanding as at 31 December 2009 was 1.44 years (2008: 3.40 years).

The range of exercise prices for options outstanding at the end of the year was \$1.00 - \$3.10 (2008: \$1.00 - \$3.90).

The Company's share price at the year end (31 December 2009) was \$0.022 (2008: \$0.03).

The weighted average fair value of options granted during the year was \$0.012 (2008: No options were granted), which related to the issue of options to the Company's CEO.

The fair value of all share options are measured at the reporting date using the Black-Scholes option pricing model taking into account the terms and conditions upon which the instruments were granted. The following table lists the inputs to the model used for the year ended 31 December 2009.

Options issued to CEO

| | 2009 |
|---------------------------------|--------|
| Share price | 0.024 |
| Exercise price | 0.050 |
| Volatility | 73.71% |
| Risk-free interest rate (%) | 4.93% |
| Expected life of option (years) | 5.00 |
| Dividend rate | 0% |

The volatility used in the above assumptions has been estimated based on Arasor's previous trading history up to mid 2008. As the Company has been in voluntary suspension since February 2009, the Company has no empirical evidence on which to formulate historical volatility. The rate used is therefore the best estimate of expected volatility in the value of Arasor's securities.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|--|--------------|------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |

16. TRADE AND OTHER PAYABLES

| | | | | |
|--------------------|---------|-----------|---------|---------|
| Trade payables (i) | 61,931 | 7,142,964 | 61,931 | 146,154 |
| Accrued expenses | 487,654 | 652,382 | 487,654 | 266,247 |
| Other payables | - | 984,605 | - | 5,000 |
| | 549,585 | 8,779,951 | 549,585 | 417,401 |

- (i) Trade payables are non-interest bearing and are normally settled on 60-day terms.

17. BORROWINGS

Current

| | | | | |
|--|---|------------|---|--------|
| Term loan (i) | - | 16,362,753 | - | - |
| Insurance funding (ii) | - | 87,277 | - | 87,277 |
| Unsecured loans from related parties (iii) | - | 930,853 | - | - |
| | - | 17,380,883 | - | 87,277 |

All borrowings relate to balances in 2008, with (i) and (iii) being extinguished through abandonment.

- (i) The Agriculture Bank of China, Nansha Branch, had granted Arasor Guangzhou Co. Ltd a loan facility. The total amount available under this facility was RMB 80 Million, of which RMB 77.7 Million (approximately AUD \$16.3 Million) are used at 31 December 2008. The loan was repayable in 5 years from 1 July 2007 and a total of RMB 15 Million was required to be repaid prior to 30 June 2008. On 5 February 2010, as announced to the ASX, the term loan was settled by way of an asset swap with the Companies JV partner Guangzhou Nan Sha Assets Operation Co., Ltd. The facility incurred interest at an annual rate of 8.613%
- (ii) The Company has received funding for the payment of its directors and offices insurance. The funds were repayable monthly and were fully repaid in November 2009.
- (iii) A party related to Dr S Cao has temporarily granted Arasor Guangzhou Co. Ltd the amount of RMB 8.89 Million as a short term loan (of which, RMB 4.42 million was outstanding at the balance date), with the loan period being 1 year at the rate of Libor +1%.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|------------------------------------|--------------|-----------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 18. OTHER LIABILITIES | | | | |
| Current | | | | |
| Deferred income - Government Grant | - | 1,402,133 | - | - |
| | - | 1,402,133 | - | - |
| Non-current | | | | |
| Deferred income - Government Grant | - | 136,667 | - | - |
| | - | 136,667 | - | - |

All other liabilities relate to balances in 2008 which have been extinguished through discontinuation.

In accordance with an equipment and service agreement between Bandwidth Foundry International Pty Ltd ('BFI') and Macquarie University ('Macquarie'), BFI has agreed to provide Macquarie a licence to access its fabrication facility in exchange for \$3 million in grants over 5 years, in accordance with an agreed contribution schedule. This agreement in substance is a government grant and in accordance with AASB 120 'Accounting for Government Grants and Disclosure of Government Assistance', the revenue is required to be deferred and amortised over the period the grant is intended to cover, or the life of the asset it is intended to reimburse. For further details of this accounting policy, refer to note 1 (h).

| | Consolidated | | Parent | |
|---|--------------|---------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 19. PROVISIONS | | | | |
| Long service leave | | | | |
| Opening balance | 305,081 | 47,101 | - | - |
| Net increase in provision during financial year | - | 257,980 | - | - |
| Classified as discontinued through disposal | (305,081) | - | - | - |
| | - | 305,081 | - | - |

20. FINANCIAL LIABILITIES

1,351,351 convertible notes
(2008: 1,351,351)

| | | | |
|-----------|-----------|-----------|-----------|
| 1,403,326 | 1,403,326 | 1,403,326 | 1,403,326 |
| 1,403,326 | 1,403,326 | 1,403,326 | 1,403,326 |

| | 2009 | | 2008 | |
|--|-----------|-----------|-----------|-----------|
| | Number | \$ | Number | \$ |
| Convertible Notes | | | | |
| Balance at beginning of year | 1,351,351 | 1,403,326 | - | - |
| Partial proceeds , at a value of \$1.00 per note | - | - | 1,351,351 | 1,351,351 |
| Proceeds received, but not yet allotted | - | - | - | 51,975 |
| Balance at end of financial year | 1,351,351 | 1,403,326 | 1,351,351 | 1,403,326 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

The convertible notes listed above have a zero percent interest rate and mature 3 years from the date of issue (unless otherwise requested to be matured at an earlier date by the holder, being not less than one year after the issue date). The notes can be converted into cash or shares at Arasor's discretion. In the event the notes are converted to shares, they will be converted at a rate of \$0.30 per share.

21. ISSUED CAPITAL

| | Consolidated | | Parent | |
|---|--------------|-------------|-------------|-------------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 128,559,267 fully paid ordinary shares (2008: 128,559,267) | 157,066,028 | 157,066,028 | 157,066,028 | 157,066,028 |
| | 157,066,028 | 157,066,028 | 157,066,028 | 157,066,028 |
| | 2009 | | 2008 | |
| | Number | \$ | Number | \$ |
| Ordinary shares | | | | |
| Balance at beginning of year | 128,559,267 | 157,066,028 | 122,392,760 | 146,842,064 |
| Shares issued in relation to acquisition of Verrillon Holdings Pty Ltd | - | - | 1,130,655 | 2,224,893 |
| Shares issued pursuant to private placements | - | - | | |
| Issued upon acquisition of the assets of Novalux | - | - | 5,035,852 | 8,007,005 |
| Transaction costs on shares issued | - | - | - | (7,934) |
| Balance at end of financial year | 128,559,267 | 157,066,028 | 128,559,267 | 157,066,028 |

Fully paid ordinary shares carry one vote per share and carry the right to dividends. Fully paid ordinary shares participate in the winding up of the parent entity in proportion to the number of securities held.

Capital Management

The targets of management include controls of the capital and borrowings of the Group in order to maintain a good debt to equity ratio, provide the shareholders with adequate returns and ensure that the Group can fund its operations and continued as a going concern.

The Group's debt and capital includes ordinary fully paid shares, convertible notes and financial liabilities, supported by financial assets.

There are no externally imposed capital requirements.

Management effectively manages the Group's capital by assessing the Group's financial risks and adjusting its capital structure in response to changes in these risks and in the market. These responses include the management of debt levels, distributions to share holders and share issues.

There have been no changes in the strategy adopted by management to control the capital of the Group since the prior year.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|---|--------------|--------------|-----------|-----------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| 22. RESERVES | | | | |
| Reserves | | | | |
| Share-option reserve (a) | 6,657,176 | 6,029,281 | 6,657,176 | 6,029,281 |
| Foreign currency translation reserve (b) | (1,496,701) | (15,484,328) | - | - |
| | 5,160,475 | (9,455,047) | 6,657,176 | 6,029,281 |
| (a) Share-option reserve | | | | |
| Balance at beginning of financial year | 6,029,281 | 1,997,421 | 6,029,281 | 1,997,421 |
| Issue of options to employees and officers under Employee Share Option Plan | 627,895 | 3,614,255 | 627,895 | 3,614,255 |
| Issued to debt holders upon acquisition of Novalux assets | - | 417,605 | - | 417,605 |
| Balance at end of financial year | 6,657,176 | 6,029,281 | 6,657,176 | 6,029,281 |
| (b) Foreign currency translation reserve | | | | |
| Balance at beginning of financial year | (15,484,328) | (10,855,696) | - | - |
| Net exchange differences on translation of foreign controlled entities | 13,987,627 | (4,628,632) | - | - |
| Balance at end of financial year | (1,496,701) | (15,484,328) | - | - |

Nature and purpose of reserves

Share-option reserve

This reserve is used to record the value of equity benefits provided to employees and directors as part of their remuneration. Refer to note 15 for further details of these plans. In addition, it is used to record the value of options issued as part of the consideration given for business combinations.

Foreign currency translation reserve

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

| | Consolidated | | Parent | |
|--|--------------|------|--------|------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |

23. RETAINED EARNINGS

Retained Earnings

| | | | | |
|---|---------------|---------------|---------------|---------------|
| Balance at beginning of financial year | (185,236,654) | (40,902,494) | (163,155,955) | (48,625,623) |
| Net loss attributable to members of the parent entity | (5,385,783) | (144,334,160) | (2,368,809) | (114,530,332) |
| Balance at end of financial year | (190,622,437) | (185,236,654) | (165,524,764) | (163,155,955) |

24. MINORITY INTEREST

| | | | | |
|--|---|-------------|---|---|
| Balance at beginning of financial year | - | 3,130,801 | - | - |
| Contributions of equity | - | - | - | - |
| Share of net loss | - | (3,130,801) | - | - |
| Balance at end of financial year | - | - | - | - |

25. COMMITMENTS FOR EXPENDITURE

Operating leases

| | | | | |
|---|---|---------|---|---|
| Not longer than 1 year | - | 56,286 | - | - |
| Between 1 and 2 years | - | 7,581 | - | - |
| Longer than 2 years and not longer than 5 years | - | 74,000 | - | - |
| | - | 137,867 | - | - |

Capital commitments

| | | | | |
|---|---|-----------|---|---|
| Not longer than 1 year | - | 1,644,743 | - | - |
| Between 1 and 2 years | - | - | - | - |
| Longer than 2 years and not longer than 5 years | - | - | - | - |
| | - | 1,644,743 | - | - |

26. CONTINGENT LIABILITIES AND CONTINGENT ASSETS

The Group notes an action initiated by OEMSquared against the Company to recover USD \$12 Million (AUD \$16.2 Million) in commissions allegedly owed by Arasor Corporation Inc. arising from a written commission agreement. The Group continues to defend the claim and at the date of this report are confident that the likelihood of an unfavorable outcome is remote.

The Company is in default of its debt agreement with Sand Hill Capital Inc ('Sand Hill'). in relation to the US \$9.0 Million (AUD \$12.2 Million) debt assumed upon acquisition of Novalux Inc's assets. Under the terms of the agreement, Sand Hill can elect to become an unsecured creditor of Arasor International Ltd. At the date of signing this report, Sand Hill have not yet elected to do so.

At the date of this report, with the exception of the above, the Group is not aware of any Contingent Asset or Liability that should be disclosed in accordance with AASB 137.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

27. AUDITORS REMUNERATION

| | Consolidated | | Parent | |
|---|--------------|---------|--------|-------|
| | 2009 | 2008 | 2009 | 2008 |
| | \$ | \$ | \$ | \$ |
| Remuneration of the auditor for the parent entity for: | | | | |
| Auditing or reviewing the financial report | 89,651 | 90,698 | 89,651 | 7,500 |
| Other services | - | 5,500 | - | - |
| Audit services provided by related practices of the parent entity auditor | - | 105,523 | - | - |
| | 89,651 | 201,721 | 89,651 | 7,500 |

28. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES AND FINANCIAL INSTRUMENTS

Credit risk

There are no significant concentrations of credit risk within the Group.

With respect to credit risk arising from the other financial assets of the Group, which comprise cash and cash equivalents the Group's exposure to credit risk arises from default of the counter party, with a maximum exposure equal to the carrying amount of these instruments.

Liquidity risk

The Group's objective since May 2008 has been to de-leverage the Group's statement of financial position by way of sale of non core assets and other initiatives. Excluding the US operations, at the date of signing this report, the Group now has no secured debt, minimal cash burn and small cash reserves. It is however noted that the Group's debt owed to Sand Hill must be dealt with in order to negate its current liquidity risk.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

CONSOLIDATED

| | < 1year \$ | > 1 - < 3 years \$ | > 3 - < 5 years \$ | Total \$ |
|--|---------------|-----------------------|-----------------------|-------------|
| Year ended 31 December 2009 | | | | |
| <i>FINANCIAL ASSETS</i> | | | | |
| <i>Non interest bearing</i> | | | | |
| Investment in joint venture | 119,069 | - | - | 119,069 |
| Weighted average effective interest rate | - | - | - | |
| <i>Floating rate</i> | | | | |
| Cash assets | 144,610 | - | - | 144,610 |
| Weighted average effective interest rate | 3.57% | - | - | |
| <i>FINANCIAL LIABILITIES</i> | | | | |
| <i>Fixed rate</i> | | | | |
| Convertible note | - | 1,403,326 | - | 1,403,326 |
| Weighted average effective interest rate | - | 0.00% | - | |
| <i>Non interest bearing</i> | | | | |
| Trade and other payables | 549,585 | | | 549,585 |
| Weighted average effective interest rate | 0.00% | - | - | |

CONSOLIDATED

| | < 1year \$ | > 1 - < 3 years \$ | > 3 - < 5 years \$ | Total \$ |
|--|---------------|-----------------------|-----------------------|-------------|
| Year ended 31 December 2008 | | | | |
| <i>FINANCIAL ASSETS</i> | | | | |
| <i>Non interest bearing</i> | | | | |
| Investment in joint venture | 344,894 | - | - | 344,894 |
| Weighted average effective interest rate | - | - | - | |
| <i>Floating rate</i> | | | | |
| Cash assets | 1,790,038 | - | - | 1,790,038 |
| Weighted average effective interest rate | 3.36% | - | - | |
| <i>FINANCIAL LIABILITIES</i> | | | | |
| Convertible note | | 1,403,326 | | 1,403,326 |
| Weighted average effective interest rate | - | 0.00% | - | |
| <i>Non interest bearing</i> | | | | |
| Trade and other payables | 8,779,951 | | | 8,779,951 |
| Weighted average effective interest rate | 0.00% | - | - | |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

28. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES AND FINANCIAL INSTRUMENTS (Continued)

The parent entities financial liability obligations are the same as the consolidated entity.

Presently, the groups income and cash flows are not materially exposed to changes in interest rates.

Fair value measurements

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement purposes.

As of 1 July 2009, the Group has adopted the amendment to AASB 7 *Financial Instruments: Disclosures* which requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

- Quoted prices (unadjusted) in active markets for identical assets (level 1)
- Inputs other than quoted prices included within level 1 that are observable for the asset, either directly (as prices) or indirectly (derived from prices)(level 2); and
- Inputs for the asset that are not based on observable market data (unobservable inputs)(level 3).

The following table presents the Group's assets recognized at fair value at 31 December 2009. Comparative information has not been provided as permitted by the transitional provisions of the new rules:

| | Level 1 \$ | Level 2 \$ | Level 3 \$ | Total \$ |
|---------------------------------------|---------------|---------------|---------------|-------------|
| FINANCIAL ASSETS AT FAIR VALUE | | | | |
| Investments in joint ventures | | | | |
| - Investment in ZTEI JV - 49% | - | - | 119,069 | 119,069 |
| | - | - | 119,069 | 119,069 |

29. INTEREST IN SUBSIDIARIES

| Name of entity | Country of incorporation | Ownership interest | |
|--|--------------------------|--------------------|-----------|
| | | 2009 % | 2008 % |
| <u>Parent entity</u> | | | |
| Arasor International Ltd | Australia | | |
| <u>Subsidiaries</u> | | | |
| Arasor International Group Holding Limited | | | |
| Company (AIG) | Cayman Islands | 100 | 100 |
| Arasor Cayman Acquisition Company Ltd | Cayman Islands | 100 | 100 |
| Arasor Acquisition Company Inc. | United States of America | 100 | 100 |
| Arasor Corporation, Inc | United States of America | 100 | 100 |
| Arasor GuangZhou Co., Limited | China | - | 80 |
| Arasor Shanghai Co., Limited | China | - | 100 |
| Bandwidth Foundry International Pty Ltd | Australia | - | 100 |
| Verrillon Holdings Pty Ltd | Australia | 100 | 100 |
| AOFR Pty Ltd | Australia | - | 100 |

Refer to note 33 in relation to the disposal of interest in subsidiaries that occurred during the year.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

30. RELATED PARTY DISCLOSURE AND KEY MANAGEMENT PERSONNEL REMUNERATION

The following individuals are classified as key management personnel ("KMP") in accordance with AASB 124 'Related Party Disclosures':

Dr Simon Cao, Chairman (Resigned 23 April 2010)
 Mr George SyCip, Non-Executive Director
 Mr Edward Li, Non-Executive Director
 Mr Reginald Bancroft, Non-Executive Director and Company Secretary
 Mr William Mackenzie, Chief Executive Officer

The remuneration details of the above personnel can be found in remuneration report of the director's report. The totals of remuneration paid to KMP of the Group during the year are as follows:

| | 2009 | 2008 |
|------------------------------|----------------|------------------|
| | \$ | \$ |
| Consolidated group | | |
| Short-term employee benefits | 733,249 | 1,082,517 |
| Post employment benefits | - | - |
| Share-based payments | 35,096 | - |
| | 768,345 | 1,082,517 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

30. RELATED PARTY DISCLOSURE (CONTINUED)

(a) Option holdings of Key Management Personnel

| 31 December 2009 | Balance at beginning of period | Granted as remuneration | Options Exercised | Net change other | Balance at end of period | Expiry Date | First Exercise Date | Last Exercise Date |
|-------------------|--------------------------------|-------------------------|-------------------|------------------|--------------------------|-------------|---------------------|--------------------|
| Directors | | | | | | | | |
| Simon Cao | - | - | - | - | - | N/A | N/A | N/A |
| Edward Li | - | - | - | - | - | N/A | N/A | N/A |
| Reginald Bancroft | - | - | - | - | - | N/A | N/A | N/A |
| George SyCip | 40,000 | - | - | - | 40,000 | 23/10/11 | 11/10/06 | 23/10/11 |

Executives

| | | | | | | | | |
|-------------------|---|-----------|---|---|-----------|---------|---------|---------|
| William Mackenzie | - | 1,000,000 | - | - | 1,000,000 | 7/07/14 | 8/07/09 | 7/07/14 |
|-------------------|---|-----------|---|---|-----------|---------|---------|---------|

| 31 December 2008 | Balance at beginning of period | Granted as remuneration | Options Exercised | Net change other | Balance at end of period | Expiry Date | First Exercise Date | Last Exercise Date |
|-------------------|--------------------------------|-------------------------|-------------------|------------------|--------------------------|-------------|---------------------|--------------------|
| Directors | | | | | | | | |
| Simon Cao | - | - | - | - | - | N/A | N/A | N/A |
| George SyCip | 40,000 | - | - | - | 40,000 | 23/10/11 | 11/10/06 | 23/10/11 |
| Edward Li | - | - | - | - | - | N/A | N/A | N/A |
| Reginald Bancroft | - | - | - | - | - | N/A | N/A | N/A |

Executives

| | | | | | | | | |
|-------------------|-----------|---|---|---|-----------|----------|----------|----------|
| William Mackenzie | - | - | - | - | - | N/A | N/A | N/A |
| Mike Hong | 1,000,000 | - | - | - | 1,000,000 | 07/07/14 | 08/07/09 | 07/07/14 |
| Younglin Huang | 250,000 | - | - | - | 250,000 | 04/11/12 | 02/02/08 | 04/11/12 |
| Jeffrey Cheng | 700,000 | - | - | - | 700,000 | 04/11/12 | 05/07/08 | 04/11/12 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

30. RELATED PARTY DISCLOSURE (CONTINUED)

(b) Shareholdings of Key Management Personnel (Consolidated)

| 31 December 2009 | Balance at 1 Jan 09 | On Exercise of Options | Net Change Other | Balance 31 Dec 09 |
|-------------------|--------------------------------------|---------------------------|---------------------|----------------------|
| Directors | | | | |
| Simon Cao | 4,423,717 | - | - | 4,423,717 |
| George SyCip | 469,742 | - | - | 469,742 |
| Edward Li | - | - | - | - |
| Reginald Bancroft | 5,000 | - | - | 5,000 |
| Executives | | | | |
| William Mackenzie | - | - | - | - |
| 31 December 2008 | Balance at beginning of period | On Exercise of Options | Net Change Other | Balance 31 Dec 08 |
| Directors | | | | |
| Simon Cao | 4,423,717 | - | - | 4,423,717 |
| George SyCip | 469,742 | - | - | 469,742 |
| Edward Li | - | - | - | - |
| Reginald Bancroft | 5,000 | - | - | 5,000 |
| Executives | | | | |
| William Mackenzie | - | - | - | - |
| Mike Hong | - | - | - | - |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

30. RELATED PARTY DISCLOSURE (CONTINUED)

In addition to the above listed interests, New Commerce Investment Co. Ltd, an entity in which Simon Cao is a director, holds 12,468,726 Ordinary Fully Paid Shares in Arasor International Ltd.

(c) Other related party disclosures – director related transactions

Chairman's guarantee

In accordance with a personal guarantee, Dr Simon Cao (*who was the Chairman of the Company until April 2010) has provided Arasor Corporation Inc. with a loan of \$2.09 Million (USD \$1.877 Million). The loan has no fixed repayments and the funds provided at the reporting date are part of Dr. Cao's \$4.5 Million (US \$4.0 Million) solvency guarantee. Dr. Cao has also guaranteed the Hao Lasertech investment, up to US \$10.0 Million (AUD \$11.15 Million).

31. SUBSEQUENT EVENTS

As disclosed within the 31 December 2008 financial statements, on 5 February 2010, the Company announced the payment of the secured term loan in place in China with the Agricultural Bank of China. The resolution involved the payment of \$18 Million (RMB 116 Million) to the bank (representing both principal and accrued interest) made by the Company's minority JV partner Guangzhou Nan Sha Assets Operation Co., Ltd ('NGAO'). In exchange for the payment, the NGAO has assumed ownership of the Company's land and buildings in Guangzhou. Arasor maintains an ability to lease the land off the NGAO in order to continue to service its client base. Post this resolution, the board has formally reached the decision to abandon its operations in China, which have been reflected in the financial statements for the year ended 31 December 2009.

On 1 April 2010, the Company announced it had entered into an agreement to sell its Japan optical wafer production fabrication facility and assets to a US based multinational Company. The transaction provides for a consideration of US \$1.17 Million (AUD \$1.3 Million).

On 25 November 2010, the Company announced that due to the lack of development of the Company's Joint Venture with ZTEI, it would be seeking remedies from its former Executive Chairman, Dr Simon Cao, for the amount of USD \$10 Million.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

32. DISCONTINUED OPERATIONS

| | Consolidated | |
|--|-------------------------------|-------------------------------|
| | Year ended 31 Dec 09 \$ | Year ended 31 Dec 08 \$ |
| DISCONTINUED OPERATIONS | | |
| Net profit/loss | | |
| Arasor, Japan Branch (refer to note 34) | (563,187) | (1,018,122) |
| AOFR Pty Ltd (refer to note 33 (a)) | (230,636) | (18,441,165) |
| Bandwidth Foundry International Pty Ltd (refer to note 33 (b)) | (313,265) | (803,997) |
| Arasor Corporation Inc. (refer to note 32 (b)) | (1,214,121) | (98,419,026) |
| China based entities (refer to note 32 (a)) | - | (22,910,182) |
| Gain/(loss) on disposal/abandonment | | |
| AOFR Pty Ltd (refer to note 33 (a)) | 76,828 | - |
| Bandwidth Foundry International Pty Ltd (refer to note 33 (b)) | 148,265 | - |
| Abandonment of Chinese entities (refer to note 32 (a)) | (1,924,685) | - |
| | (4,020,801) | (141,592,492) |

(a) China based subsidiaries and branches

On the 1 January 2009, due to insufficient working capital Arasor International Ltd abandoned its investments in its Chinese subsidiaries and branches, comprising of Arasor Beijing (a branch of Arasor Corporation Inc.), Arasor GuangZhou Co., Limited and Arasor Shanghai Co., Limited. Whilst the board continued to pursue opportunities in these entities up until mid 2010 in substance Arasor lost control of these investments for accounting purposes at the beginning of 2009. The loss represents the book value of net assets that the entities contributed to the Arasor Group at the date of the decision and is reconciled as follows:

| | Year ended 31 Dec 09 \$ |
|--|-------------------------------|
| Abandonment of Chinese entities | |
| Net asset deficiency derecognised relating to Arasor GuangZhou Co., Limited and Arasor Shanghai Co., Limited | (1,839,827) |
| Net assets abandoned in Arasor Beijing | (84,858) |
| | (1,924,685) |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

32. DISCONTINUED OPERATIONS (CONTINUED)

The loss attributable to the Chinese entities in the year ended 31 December 2008 is summarised as follows:

| | Year ended 31 Dec 09 \$ | Year ended 31 Dec 2008 |
|--|-------------------------------|---------------------------|
| Revenue from operating activities | - | 6,999,250 |
| Cost of revenue from operating activities | - | (6,787,851) |
| Gross Profit | - | 211,399 |
| Other income | - | 133,718 |
| Impairment expense | - | (6,217,626) |
| Bad and doubtful debts expense | - | (12,626,977) |
| Research expenses | - | (1,776,480) |
| Sales and marketing costs | - | (638,328) |
| General and administration costs | - | (1,011,705) |
| Finance costs | - | (984,183) |
| Loss before income tax | - | (22,910,182) |
| Income tax expense | - | - |
| Loss for the year from Arasor, Chinese entities | - | (22,910,182) |

(b) Arasor Corporation Inc.

As previously disclosed in the Group's annual financial statements for 2008, the board formally made the decision to discontinue its operations in the United States ('US').

The business has been classified as discontinued in the Group's financials, as the directors believe this is the most appropriate way of presenting the Company's financials.

As the financial records for the entity were not accurately kept beyond 31 December 2008, the amounts recorded in the Group's statement of financial position at the reporting date are the amounts booked to 31 December, modified for certain events. These events included:

- The payment US\$0.2 Million paid by Necsel Intellectual Property Inc. (an entity not controlled by the Arasor Group, but associated with the Group's CEO Mr William Mackenzie) as consideration for certain IP to the value of US \$0.2 Million;
- The acquisition of the Company's remaining plant equipment for the consideration of US \$0.2 Million; and
- The payment of certain statutory liabilities owed by the group (principally unpaid salaries and wages) with a portion of the proceeds from AOFR Pty Ltd.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

32. DISCONTINUED OPERATIONS (CONTINUED)

After accounting for these transactions, the net liability booked as discontinued in the Company's estimated liabilities are detailed as follows:

| | Estimated at 31 Dec 2009 \$ | Estimated at 31 Dec 2008 \$ |
|--|-----------------------------------|-----------------------------------|
| Cash and cash equivalents | - | 48,967 |
| Other receivables | - | 508,412 |
| Property, plant and equipment (net) | - | 288,684 |
| Intangible assets (net) | - | 288,684 |
| Total assets | - | 1,134,747 |
| Trade and other payables | (14,740,992) | (20,567,055) |
| Interest bearing liabilities | (10,057,709) | (12,391,865) |
| Ex-chairmans guarantee (Dr. Simon Cao) | (2,092,642) | (2,518,764) |
| Total liabilities | (26,891,343) | (35,477,684) |
| Net liabilities | (26,891,343) | (34,342,937) |

The entities net loss incurred for the period 31 December 2009 (noting the above assumptions) is detailed as follows:

| | Year ended 31 Dec 09 \$ | Year ended 31 Dec 2008 |
|---|-------------------------------|---------------------------|
| Revenue from operating activities | - | 2,909,046 |
| Cost of revenue from operating activities | - | (2,512,034) |
| Gross Profit | - | 397,012 |
| Other income | - | 122,788 |
| Impairment expense | (134,711) | (18,820,446) |
| Bad and doubtful debts expense | - | (58,289,265) |
| Research expenses | - | (10,343,242) |
| Sales and marketing costs | - | (4,030,999) |
| General and administration costs | (25,241) | (5,778,531) |
| Finance costs | (1,054,169) | (1,676,343) |
| Loss before income tax | (1,214,121) | (98,419,026) |
| Income tax expense | - | - |
| Loss for the year from Arasor US | (1,214,121) | (98,419,026) |

As discussed in note 35, Sand Hill Capital Inc. has the ability to become an unsecured creditor of Arasor International Ltd (as Arasor Corporation Inc. has defaulted on the terms of the note). As no notice of intent has been received at the date of this report, the US \$8.915 Million (AUD \$10.058 Million) owed on the notes has been included in Group's discontinued operations.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

33. DISPOSAL OF SUBSIDIARIES

(a) Sale of AOFR Pty Ltd

On 3 March 2009, the Group disposed of 100% of its beneficial interest in AOFR Pty Ltd. Proceeds of \$2,371,167 were received in cash in relation to the sale.

The loss for the year ended 31 December 2009 related to AOFR Pty Ltd is analysed as follows:

| | 2 months ended 3 Mar 2009 \$ | Year ended 31 Dec 2008 \$ |
|--|------------------------------------|---------------------------------|
| Revenue from operating activities | 1,209,523 | 11,700,702 |
| Cost of revenue from operating activities | (879,951) | (9,164,146) |
| Gross Profit | 329,572 | 2,536,556 |
| Impairment expense | - | (17,192,970) |
| Other income | 106,507 | 64,887 |
| Research expenses | (272,981) | (1,955,902) |
| Sales and marketing costs | (101,767) | (576,875) |
| General and administration costs | (291,967) | (1,316,861) |
| Loss before income tax | (230,636) | (18,441,165) |
| Income tax expense | - | - |
| Loss for the period from AOFR Pty Ltd | (230,636) | (18,441,165) |

The net assets of AOFR Pty Ltd at the date of disposal was as follows:

| | 3 Mar 2009 \$ |
|----------------------------|------------------|
| Net assets disposed of | 2,294,339 |
| Gain on disposal | 76,828 |
| Total consideration | 2,371,167 |

(b) Bandwidth Foundry International Pty Ltd

During the reporting period, the board resolved to formally enter into arrangements to dispose of Bandwidth Foundry International Pty Ltd. As announced to the ASX on 5 November 2009, the Group successfully completed the sale transaction for the notional consideration of \$1.00.

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

33. DISPOSAL OF SUBSIDIARIES (Continued)

The loss for the year ended 31 December 2009 related to Bandwidth Foundry International Pty Ltd is as follows:

| | Period ended 1 Nov 2009 \$ | Year ended 31 Dec 2008 |
|---|----------------------------------|---------------------------|
| Revenue from operating activities | 566,535 | 332,747 |
| Cost of revenue from operating activities | (12,215) | (278,035) |
| Gross Profit | 554,320 | 54,712 |
| Other income | - | 1,074,820 |
| Research expenses | (867,585) | (1,643,626) |
| Impairment expense | - | (289,903) |
| Loss before income tax | (313,265) | (803,997) |
| Income tax expense | - | - |
| Loss for the period from Bandwidth Foundry International Pty Ltd | (313,265) | (803,997) |

The net assets of Bandwidth Foundry International Pty Ltd at the date of disposal was as follows:

| | 1 Nov 2009 \$ |
|-----------------------------------|------------------|
| Net asset deficiency derecognised | (148,264) |
| Gain on disposal | 148,265 |
| Total consideration | 1 |

34. NON-CURRENT ASSETS HELD FOR SALE

Arasor, Japan Branch

During the reporting period, the board resolved to enter into arrangements to dispose of its operations in Japan. Accordingly, the business group's results have been classified as discontinued in the statement of comprehensive income. The entities assets and liabilities have been classified as held for sale.

The loss for the year ended 31 December 2009 in relation to Arasor Japan is analysed as follows:

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

34. NON-CURRENT ASSETS HELD FOR SALE (Continued)

| | Year ended 31 Dec 09 \$ | Year ended 31 Dec 2008 |
|--|-------------------------------|---------------------------|
| Revenue from operating activities | 24,667 | 187,307 |
| Cost of revenue from operating activities | - | (48,006) |
| Gross Profit | 24,667 | 139,301 |
| Research expenses | (587,854) | (1,157,423) |
| Loss before income tax | (563,187) | (1,018,122) |
| Income tax expense | - | - |
| Loss for the year from Arasor, Japan Branch | (563,187) | (1,018,122) |

The summarised statement of financial position of the disposal group is detailed as follows:

| | 31 Dec 2009 \$ |
|--|-------------------|
| Cash and cash equivalents | 26,453 |
| Property, plant and equipment at fair value to sell | 181,805 |
| Total assets classified as held for sale | 208,258 |
| Trade and other payables | (30,358) |
| Total liabilities classified as being associated with assets held for sale | (30,358) |
| Net assets | 177,900 |

Notes to the Financial Statements

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2009 continued

35. GOING CONCERN

The annual report for the Parent Entity and Consolidated Entity has been prepared on a going concern basis. Notwithstanding this method of preparation, it is noted that the parent and group incurred a net loss of \$2,368,809 and \$5,385,783 respectively during the year ended 31 December 2009, and, as of that date, the parent and group's current liabilities exceeded its current assets by \$398,234 and \$26,992,608 respectively. The directors believe that the group continues to be a going concern, noting the following key issues:

- The directors intend to place the Company's beneficially owned US subsidiary, Arasor Corporation Inc., into administration when sufficient working capital is available. Arasor Corporation is the only entity within the group at the date of signing this report that no longer trades as a going concern and is largely the reason for the group's net asset deficiency.
- Dr. Simon Cao, ex-chairman of the Consolidated Entity had provided a personal guarantee in favour of Arasor Corporation Inc. to the remaining value of USD \$12 Million. The Consolidated Entity has commenced proceedings to call on the balance of this guarantee.
- The Consolidated Entity is in an advanced stage of legal action in India to recover trade receivables of Arasor Corporation Inc. to the value of USD\$6.4 Million, and other Indian receivables in excess of USD\$20M which were fully provided for as doubtful debts in the financial statements for the year ended 30 December 2008.
- The debt holders in the US ('Sand Hill Capital') continue to work with the Company in relation to its secured debt. Whilst Sand Hill Capital's secured claim is limited to the assets of Arasor Corporation Inc., it has the ability to become an unsecured creditor in Arasor International Ltd. Notwithstanding that the proceeds from the call on Dr. Cao's personal guarantee and ongoing legal action with respect to Indian receivables cannot be ascertained at this stage, the directors believe that the Group would be able to reach a satisfactory outcome with Sand Hill Capital.
- As announced on 5 February 2010, the term loan in place with the Agricultural Bank of China has been settled by way of an asset swap, which involved the Nansha JV's minority partner Guangzhou Nan Sha Assets Operation Co., Ltd ('NGAO') taking back the land and buildings located in the Company's Guangzhou Manufacturing Facility. At the same time, the NGAO repaid the loan owed to the bank in cash of \$18 Million (RMB 116 Million) including principal and accrued interest.

The Board recognises that the company's cash position is low and has taken all commercially reasonable actions to reduce expenses. The board will continue to monitor the situation of collecting monies from receivables and/or the guarantee from Dr. Cao. If at any time the board determines that the Company's cash position falls to a level where the Company is going into insolvency, then the Company would seek an administrator and declare voluntary insolvency.

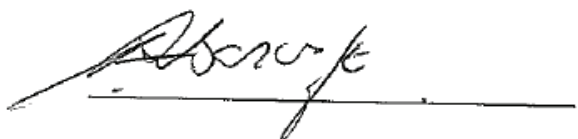
No adjustments have been made to the financial report relating to recoverability and classification of recorded asset amounts and classification of liabilities that might be reclassified if the entity does not continue as a going concern.

Directors' Declaration

In accordance with a resolution of the directors of Arasor International Ltd, I state that:

1. In the opinion of the directors:
 - a. the financial statements and notes of the company and of the consolidated entity are 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 31 December 2009 and of their performance for the year ended on that date; and
 - ii. complying with Accounting Standards and Corporations Regulations 2001; and
 - b. there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.
2. This declaration has been made after receiving the declarations required to be made to the directors in accordance with section 295A of the Corporations Act 2001 for the financial period ending 31 December 2009.

On behalf of the board

A handwritten signature in black ink, appearing to read 'R. Bancroft', is written over a horizontal line.

Mr Reginald Bancroft
Director

29 December 2010

Level 1,
67 Greenhill Rd
Wayville SA 5034
GPO Box 1270
Adelaide SA 5001

T 61 8 8372 6666
F 61 8 8372 6677
E info.sa@au.gt.com
W www.grantthornton.com.au

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF ARASOR INTERNATIONAL LIMITED

Report on the financial report

We have audited the accompanying financial report of Arasor International Limited (the "Company"), which comprises the statement of financial position as at 31 December 2009, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes to the financial report and the directors' declaration of the company the consolidated entity comprising the Company and the entities it controlled at the year's end or from time to time during the financial year.

Directors responsibility for the financial report

The Directors of the Company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards and the Corporations Act 2001. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. The Directors also state, in the notes to the financial report, in accordance with Accounting Standard AASB 101 Presentation of Financial Statements, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards which require us to comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error.

In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit, we have complied with the independence requirements of the Corporations Act 2001.

Basis for disclaimer of auditor's opinion

As stated in Note 32(b) of the financial statements, the United States operations were closed in March 2009 and the employees were terminated at that time. The financial records of the United States operations were incomplete at the time the employees were terminated and have not been maintained from that date. As a consequence, there is no further financial information available for this company. The incomplete United States accounting records may also have the implication of affecting the completeness of transactions in the parent entity.

The discontinuation of the United States operations occurred prior to the completion of our audit and the directors of the parent entity are not aware if the current financial position of the United States operations has changed. As the accounting records are not adequate to permit the application of necessary auditing procedures, we are unable to obtain all the information and explanations we require in order to form an opinion on the financial report.

Disclaimer of auditor's opinion

In our opinion, because of the existence of the limitation on the scope of our work, as described in the preceding paragraphs, and the effects of such adjustments, if any, as might have been determined to be necessary had the limitation not existed, we are unable to and do not express an opinion as to whether:

- a the financial report of Arasor International 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 31 December 2009 and of their performance for the year ended on that date; and
 - ii complying with Australian Accounting Standards and the Corporations Regulations 2001; and
- b the financial report also complies with International Financial Reporting Standards as disclosed in the notes to the financial statements.

Material uncertainty regarding continuation as a going concern

Without further qualifying our opinion, we draw attention to Note 35 in the financial report which indicates that the company and consolidated entity incurred a net loss of \$2,368,809 and \$5,385,783 respectively during the year ended 31 December 2009 and, as of that date, the company's and consolidated entity's current liabilities exceeded its total assets by \$398,234 and \$26,992,608 respectively. In addition, the parent entity has guaranteed the unsecured debt from Sand Hill Capital Inc. which was assumed upon the acquisition of the assets of Novalux Inc. Should this be called upon the parent entity may not be able to pay its debts as and when they fall due.

These conditions, along with other matters as set forth in Note 35, indicate the existence of a material uncertainty which may cast significant doubt about the company's and consolidated entity's ability to continue as a going concern and therefore the company and consolidated entity may be unable to realise its assets and discharge its liabilities in the normal course of business, and at the amounts stated in the financial report.

Report on the remuneration report

We have audited the remuneration report included in the directors' report for the year ended 31 December 2009. The Directors of the Company are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the Corporations Act 2001. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

Basis for disclaimer of auditor's opinion on the remuneration report

As noted in the Basis for Disclaimer of auditor's opinion above, the United States operations were discontinued in March 2009 and the accounting records remain incomplete. As a consequence, there is no reliable financial information available for this company to be able to form an opinion on the amount of remuneration paid during the year ended 31 December 2009.



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Disclaimer of auditor's opinion on the remuneration report

In our opinion, because of the existence of the limitation on the scope of our work, as described in the preceding paragraph, and the effects of such adjustments, if any, as might have been determined to be necessary had the limitation not existed, we are unable to and do not express an opinion as to whether the Remuneration Report of Arasor International Limited for the year end 31 December 2009, complies with section 300A of the Corporations Act 2001.

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GRANT THORNTON SOUTH AUSTRALIAN PARTNERSHIP
Chartered Accountants



S.J. Gray
Partner

Adelaide, *29 December 2010*