

KEYCORP LIMITED
ANNUAL REPORT 2007

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DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

The directors present their report together with the financial report of Keycorp Limited ('the Company') and of the consolidated entity, being the Company, its subsidiaries, and the consolidated entity's interest in associates for the financial year ended 30 June 2007 and the auditor's report thereon.

DIRECTORS

The directors of the company in office at any time during or since the end of the financial year are:

Name, qualifications and independence status

Experience, special responsibilities and other directorships

NON-EXECUTIVE CHAIRMAN

Robert Bishop

BEcon, MAICD

Chairman of the Remuneration and Nomination Committee

Robert Bishop joined as a director in January 2006 and was appointed Chairman on 1 June 2007. He has an extensive background in the financial services sector and is considered an authority on cards, payments, retail banking and distribution having held senior executive positions at National Australia Bank, Westpac and Citibank. He has served on numerous boards and advisory groups including MasterCard International, NCR Corporation, Equifax, Mondex International, Bankcard Australia and a number of Australian public and private companies. He is currently chairman of IWL Limited and UK company PSP International plc.

During the last three financial years, Robert has been a director of the following listed companies, apart from Keycorp: IWL Limited (ASX: IWL) from August 2001 (current).

EXECUTIVE DIRECTOR

Ken Carr

DBA, MBA, FAICD, BSc

Member of Remuneration and Nomination Committee

Ken Carr was appointed Managing Director and Chief Executive Officer on 18 May 2007.

Ken was Group Chief Executive Officer of LongReach Group Limited prior to its merger in early November 2006 with Allied Technologies Group Ltd. He has held senior executive roles with organisations such as IBM Global Services Australia, Lucent Technologies, Computer Sciences of Australia and Unisys Australia Limited. He has a depth of experience in the telecommunications industry, having worked for telecommunications carriers such as British Telecom and AT&T and was involved in the second licence bid and creation of Optus.

During the last three financial years, Ken has been a director of the following listed companies, apart from Keycorp: LongReach Group Limited (ASX: LRX) from August 2004 to November 2006 and LongReach Group Limited (ASX: LRG) from November 2006 to July 2007.

NON-EXECUTIVE DIRECTOR

Barry Grisdale

BSc (Elec Eng), BCom, MBA, FAICD

Chairman of the Audit and Risk Committee and Member of the Remuneration and Nomination Committee

Barry Grisdale was appointed a director in January 2001. He has many years of senior executive experience in publicly listed and private technology companies around the globe. Barry is currently the Managing Director of CPS Systems Pty Ltd. Past positions include Executive Director of Telstra Retail, CEO of Bull Information Systems (UK and Ireland) Ltd, and Vice President (Operations) for Groupe Bull based in Paris.

Barry has held no other listed company directorships during the past three financial years.

NON-EXECUTIVE DIRECTOR

Christine Holgate

MBA, PG Dip MKTG, PG Dip MGT ST, PG Dip P&S

Member of Remuneration and Nomination Committee

Christine Holgate joined as a director in January 2006. She has extensive marketing and sales experience in the telecommunications sector, having worked in the industry for the past 18 years. She has held senior management and board level positions in Energis, JP Morgan and Cable & Wireless PLC, and most recently Telstra Corporation Limited, working in Europe, Asia, the Americas and Australia. Christine's prime responsibilities have been leading teams through significant change, growth and start up where she has initiated and executed successful business strategies for both business and consumer customers. Most recently, as Executive Director, Business Sales & Channels at Telstra, Christine leads a team focused on serving Telstra's business customers. Christine is also a board member of Aurora Television.

Christine has held no other listed company directorships during the past three financial years.

DIRECTORS' REPORT continued

FOR THE YEAR ENDED 30 JUNE 2007

DIRECTORS continued**Name, qualifications
and independence status****Experience, special responsibilities and other directorships****NON-EXECUTIVE DIRECTOR**

Michael Ibrahim

BEcon

Member of the Audit and Risk Committee

Michael Ibrahim joined as a director in January 2006. He is a proven strategic international business leader with specific competencies in software and technology development, international foreign exchange, treasury and executive management. He has held senior executive positions at KPMG Consulting, Citibank and Goodman Fielder Limited. Michael is a qualified accountant, having commenced his career as a financial accountant with Chemical Bank. Most recently he has been engaged in a series of managing director level consulting relationships with a range of leading technology companies.

Michael has held no other listed company directorships during the past three financial years.

NON-EXECUTIVE DIRECTOR

Malcolm Irving

AM, BComm, HonDLit, FCPA, FAICD, SF Fin

Malcolm Irving joined the board as Chairman in March 2001. He stepped down as Chairman on 1 June 2007 and retired as a director on 1 July 2007. Prior to retirement Malcolm served as Chairman of the Remuneration and Nomination Committee and a member of the Audit and Risk Committee.

During the last three financial years, Malcolm has been a director of the following listed companies, apart from Keycorp: Abacus Property Group (ASX: ABP) from September 2002 (current).

NON-EXECUTIVE DIRECTOR

Philip Jones

BBs, CPA

Member of the Audit and Risk Committee

Philip Jones was appointed a director in August 2005. He is Telstra's Executive Director of Data, IP and Enterprise Services and is responsible for managing the data and voice products and services used by Telstra's enterprise, government and small business customers. Since joining Telstra in 1994, Philip has held senior operational and commercial roles. His most recent assignment was Managing Director of Operations, BigPond where he was responsible for BigPond's IT, technology, service provision and call centres. Prior to joining Telstra, Philip worked for Exxon Corporation for sixteen years in various commercial, operational and IT roles in Australia and overseas.

Philip has held no other listed company directorships during the past three financial years.

EXECUTIVE DIRECTOR

Bruce Thompson

BEcon, FCPA, FAICD

Bruce Thompson joined the board in March 2001 and was appointed Chief Executive Officer in November 2001. He resigned from the Board on 17 May 2007. Prior to his resignation, he was a member of the Remuneration and Nomination Committee.

During the last three financial years, Bruce has been a director of the following listed companies, apart from Keycorp: SMS Management & Technology Limited (ASX: SMX) from October 2000 (current) and Innovonics Limited (ASX: INO) from December 2000 to December 2004.

COMPANY SECRETARY

Mark Knapman

B Comm, LLB

Mark Knapman joined Keycorp as Company Secretary and General Counsel in March 2001. Previously he held the position of General Counsel, Asia Pacific with US information technology company Silicon Graphics Inc. and was also the Company Secretary of Silicon Graphics' Australian subsidiary. Prior to that role he was a partner at Hunt & Hunt, a national law firm. He is admitted as a solicitor in NSW, Victoria and the ACT.

PRINCIPAL ACTIVITIES

During the year the principal activities of the consolidated entity were:

- research, development and sales of devices and applications and systems to allow secure electronic payments and transactions at the point-of-sale;
- service solutions (including installation, maintenance, help desk support, logistics and asset management services) for point-of-sale terminals and other payments products; and
- research, development and sales of smartcard technology, including licensing of operating systems and applications for smartcards.

REVIEW AND RESULTS OF OPERATIONS

In light of the recent performance of the consolidated entity and the significantly amended business structure during the financial year, the directors have carefully reviewed the consolidated entity's operations and prospects to ensure that the underlying performance is consistent with going concern principles. In doing so, the directors have taken into consideration the forward budgets of the various business entities and have normalised the performance of those entities during the year ended 30 June 2007, including adjusting for a number of non-recurring and specific, additional cost items.

The consolidated entity reported revenue of \$95.578 million for the year to 30 June 2007, compared to \$95.211 million for the prior year. This result was impacted by the decision, taken in May 2007, to structure new managed payments service agreements (MPSA) contracts to give annuity income rather than an up-front revenue on sale of product. Income from the leasing of terminals and devices is recognised on an annuity basis throughout the life of a MPSA contract. Previously, agreements were structured such that income from the resale of terminals and devices had been recognised at the time of sale. This change has the effect of dampening current year revenues but builds greater certainty into future years' revenues.

Two new MPSA transactions commenced in May 2007 will generate \$26.264 million revenue over the next five to six years. In addition an existing MPSA is currently

being re-negotiated and it is anticipated to be extended by up to a further three years, embedding up to a further \$22.6 million of revenue.

The business of the consolidated entity changed significantly during the year to 30 June 2007. The result from operating activities was a loss of \$14.135 million compared to a loss of \$0.600 million for the prior year. The underlying gross margins and embedded cost structures were largely in line with budgeted performance other than in the Australian Payments Solutions business where one major anticipated contract was delayed.

The principal reasons for this loss were threefold: additional costs arising as a result of the acquisition of a new business venture; trading losses incurred as the company repositioned itself from product manufacturing to service provision; and other operating expenses.

During the year the consolidated entity acquired the Optimal Services Group business in Canada (OSG), the largest service provider to the payments and point of sale industry in Canada. This acquisition was in concert with the company's focus on transforming the business from a products-based business to a solutions and services business, offering payment solutions, smartcards and high-level customer service.

The OSG acquisition was expected to be returns dilutive during the first 12 months and this has proven to be the case. OSG recorded a loss before tax of \$3.008 million excluding an accounting gain on acquisition of \$1.174 million. These results were better than forecast at acquisition and include \$1.143 million of restructuring costs, including the reduction in employee numbers by 139. The integration of this business is now complete and while there are expected to be minor rebranding costs to be incurred, at the date of this report the directors are optimistic that the business can exceed expectations for the coming year.

Trading conditions for the consolidated entity's businesses were challenging during the year. Overall, gross margins across all businesses were 30.97% compared to 39.37% for the prior year. There was increased competition in the Smartcards market and in the market for managed payments, and margins in Smartcards fell on average to 27.12% against the previous year's margins of 35.20%.

However, most of the deterioration in overall margin can be attributed to the acquisition of the OSG business which delivered only a 15.63% gross margin, whereas the comparative Australian services business generated a gross margin of 47.49%.

Whilst revenues in the Payment Solutions business fell year on year from \$35.906 million to \$25.218 million, as the company exited terminal product sales in favour of managed payments service contracts, margins were largely retained with only a modest fall in margin of 3%. Write-off and write-down of aged and obsolescent inventory of \$1.176 million contributed to this fall in margin. The transition of this business out of product manufacture and sale was largely completed during the year and the segmental operating loss of \$5.776 million included restructuring costs of \$1.104 million.

For the Smartcards business, revenues rose 9.7% over the prior year though its segment contribution was negatively impacted by a reduction in gross margin, a significant increase in the amortisation of previously capitalised development costs and restructuring expenses of \$0.211 million.

The Australian Services business maintained revenue levels after normalising for the Westpac rollout in 2005/6. With the addition of the OSG business from October 2006 (contributing \$23.572 million revenue over the nine month period post acquisition), overall segment revenues grew strongly from \$35.709 million to \$45.056 million year on year. However, the lower margins in the Canadian business and additional depreciation and restructuring charges produced an operating contribution for the combined services segment of \$2.449 million.

Total group operating expenses increased by \$5.652 million (14.84%) year on year largely attributable to an increase of \$4.683 million being the operating costs of OSG post acquisition, group restructuring charges of \$3.524 million and a further \$4.216 million represented by costs associated with a pro-active rectification program for a systemic fault in a non-Keycorp manufactured component. The rectification program is now largely complete.

DIRECTORS' REPORT continued

FOR THE YEAR ENDED 30 JUNE 2007

REVIEW AND RESULTS OF OPERATIONS continued

These increases were partially offset by increased capitalisation of development costs (\$1.128 million), a \$3.22 million reduction in relation to a prior year taxation settlement, a gain on acquisition of OSG (\$1.174 million) and a favourable insurance claim outcome (\$1.15 million).

Segmental reporting is included in note 4 of the financial report.

The cash position of the consolidated entity was directly impacted during the year by a number of specific cost items which included funding some trading losses and integration costs at OSG; funding the rectification program for the systemic chip fault; restructuring charges in the group businesses; and the costs of renegotiating financing facilities with our principal lenders. In addition, the group paid a \$3.22 million settlement in a dispute relating to a 1994 R&D syndicate, purchased a \$3 million performance bond in accordance with its MPSA with Westpac and purchased a legacy fleet of terminals under a separate MPSA for \$0.978 million. As at 30 June 2007, financing facilities totalling \$15 million were available to the company but only drawn to \$12.7 million. Although these loans are classified as 'current liabilities' in the consolidated balance sheet, subsequent to balance date the company has further renegotiated its financing facilities such that these loans will now mature on 30 September 2008.

The consolidated entity reported a net loss after tax of \$11.517 million compared to a net loss of \$2.887 million in the prior year. At the end of the year, the consolidated entity had cash reserves of \$2.346 million and drawn bank debt of \$11.50 million.

During the year the consolidated entity made a number of key management personnel changes. The directors believe that the recruitment and enhancement of the new management team now strengthens the business allowing for a strong platform upon which to grow. As well as tightening a number of internal business procedures, work has commenced on an assessment and implementation of a group-wide risk review program. This involves understanding and updating all business processes and controls.

This report omits information about business strategies and prospects for future financial years that in the opinion of the directors is likely to unreasonably prejudice the group.

CAPITAL STRUCTURE

The company commenced the year with minimal debt. A variety of events during the year, including the acquisition and funding of OSG and the funding of group inventory holdings and trading losses, determined that additional debt facilities were required. A \$10 million Multi-Option Facility was initially established in November 2006 with Westpac Banking Corporation and this was amended and restated as a \$15 million facility in March 2007. That facility provides for a variety of financing options including fully drawn and revolving cash advances, and a guarantee/performance bond facility.

A \$7.5 million fully drawn cash advance tranche of the facility is supported by a guarantee from Keycorp's principal shareholder, Telstra Corporation Limited, on commercial terms. The company has sought to ensure long term financing is in place to support the future growth of the business. Since balance date the company has agreed revised terms and conditions for the \$15 million Multi-Option facility with the company's bankers. The revised terms include a review date of 30 September 2008.

Management has investigated and considered the streaming of dividends from subsidiary companies to the parent. At this stage, no decision has been made to pay dividends between group companies but the option remains open to the board.

The company continues to investigate growth opportunities, including acquisitions and divestments as appropriate. Any acquisition would most likely require re-capitalisation of the company.

During the year, the company issued no ordinary shares but granted 840,000 options to employees on 26 October 2006. No options were exercised during the year.

TREASURY POLICY

The consolidated entity's treasury function is responsible for managing the finance facilities of the group and the minimisation of risks associated with adverse movements in foreign currencies and interest rates.

The function operates within policies set by the board, through the Audit and Risk Committee, which outline the differing situations in which hedging products are to be utilised.

Hedging of interest rates occurs, where appropriate, through the use of interest rate swap contracts.

The consolidated entity's exposure to adverse foreign currency movements is significantly minimised through the close management of its natural hedge position. In effect, sales to foreign customers and purchases from foreign suppliers (predominantly in US dollars) can offset one another such that foreign currency receipts are used to settle foreign currency payments. Foreign currency bank accounts are available to transact the foreign currency receipts and payments such that it is rarely necessary to convert foreign currency into local currency. Short term foreign currency forward contracts are periodically used to cover periods where temporary mismatches arise between foreign currency receipts and payments.

In the case of significant contractual commitments where the anticipated purchase or sale has a clearly defined delivery timetable, or in the case where timing mismatches are expected to be permanent, a specific foreign currency hedge contract may be acquired to exactly offset the known currency risk of the specific transaction or instance.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

During the year the company acquired Optimal Services Group in Canada, the largest service provider to the payments and point of sale industry in Canada to provide the infrastructure platform to launch managed payment services in the Canadian market. Keycorp did not acquire any cash or debt with the business, but acquired net assets including property, plant and equipment, inventory and receivables which have been recognised at their fair values at acquisition date in accordance with AASB 3.

In March 2007 the company restructured its bank facility with Westpac Banking Corporation. The amount of the facility was increased to \$15 million, \$7.5 million of which was guaranteed by the company's major shareholder Telstra Corporation Limited, and a revised maturity date set at 31 March 2008.

In the opinion of the directors there were no other significant changes in the state of affairs of the consolidated entity during the financial year under review that are not disclosed elsewhere in this report or in the financial report.

SIGNIFICANT EVENTS SINCE THE END OF THE FINANCIAL YEAR

Since balance date the company has negotiated revised terms and conditions for the \$15 million bank facility with Westpac. Those terms include an extended review date of 30 September 2008, on improved terms and conditions.

The directors are unaware of any other matter or circumstance that has occurred since the end of the financial year that has significantly affected or may significantly affect the operations or the state of affairs of the group in future financial years.

LIKELY DEVELOPMENTS AND EXPECTED RESULTS

Details of likely developments in the operations of the consolidated entity in future financial years are referred to in the Review of Results and Operations section above. This report omits information about likely developments and expected future results that in the opinion of the directors is likely to unreasonably prejudice the group.

ENVIRONMENTAL REGULATION AND PERFORMANCE

The choice of materials for the entity's products is constrained by the operational and security requirements with which the products are required to comply. However, subject to those constraints, the company endeavours to use recyclable packaging and componentry and, in the rare instance where corrosive chemicals are used,

to ensure that the handling of those chemicals and their disposal is done in an environmentally responsible way and in compliance with relevant legislation.

DIVIDENDS AND OTHER DISTRIBUTIONS

No dividends or other distributions have been paid or are proposed by the company for the 12 month period under review.

SHARE OPTIONS

The Keycorp Employee Share Option Incentive Plan, initially approved by shareholders on 22 October 1996 and twice amended with shareholder approval since then, was again approved by shareholders on 22 November 2005. The following table sets out the details, as at the date of this report, of options over unissued ordinary shares in Keycorp Limited granted under that plan:

| Date | Options granted | Options on issue ⁽¹⁾ | Exercise price ⁽²⁾ | Exercisable after | Expiry date |
|-------------------|-----------------|---------------------------------|-------------------------------|-------------------|-------------|
| 20 September 2002 | 332 650 | 124 850 | \$0.83 | 20.09.03 | 20.09.07 |
| 20 September 2002 | 332 650 | 129 050 | \$0.83 | 20.09.04 | 20.09.07 |
| 20 September 2002 | 665 300 | 335 900 | \$0.83 | 20.09.05 | 20.09.07 |
| 31 October 2003 | 576 500 | 381 500 | \$0.95 | 31.10.05 | 31.10.08 |
| 31 October 2003 | 576 500 | 429 500 | \$0.95 | 31.10.06 | 31.10.08 |
| 1 July 2004 | 25 000 | 25 000 | \$0.98 | 01.07.06 | 01.07.09 |
| 1 July 2004 | 25 000 | 25 000 | \$0.98 | 01.07.07 | 01.07.09 |
| 23 September 2004 | 13 000 | 7 000 | \$1.39 | 23.09.06 | 23.09.09 |
| 23 September 2004 | 13 000 | 6 000 | \$1.39 | 23.09.07 | 23.09.09 |
| 27 May 2005 | 25 000 | 25 000 | \$1.31 | 01.03.07 | 01.03.10 |
| 27 May 2005 | 25 000 | 25 000 | \$1.31 | 01.03.08 | 01.03.10 |
| 19 December 2005 | 22 500 | 12 500 | \$1.50 | 19.12.07 | 19.12.10 |
| 19 December 2005 | 22 500 | 12 500 | \$1.50 | 19.12.08 | 19.12.10 |
| 15 January 2006 | 243 331 | 109 999 | \$1.48 | 15.01.08 | 15.01.11 |
| 15 January 2006 | 243 332 | 109 999 | \$1.48 | 15.01.09 | 15.01.11 |
| 15 January 2006 | 243 337 | 110 002 | \$1.48 | 15.01.10 | 15.01.11 |
| 26 October 2006 | 279 998 | 183 332 | \$0.80 | 26.10.08 | 26.10.11 |
| 26 October 2006 | 280 001 | 183 334 | \$0.80 | 26.10.09 | 26.10.11 |
| 26 October 2006 | 280 001 | 183 334 | \$0.80 | 26.10.10 | 26.10.11 |

(1) Options on issue are those options that are capable of being exercised after the stated "exercisable after" date and exclude options which have been exercised by the option holder or which have lapsed.

(2) The payment of a capital return of 41 cents per share in September 2005 resulted in a reduction in option exercise prices of the same amount for options issued before that date, which is included above.

The remuneration report that starts on page 9 contains details of options over unissued ordinary shares in Keycorp Limited granted during the year to the directors and the five most highly remunerated officers as part of their remuneration. No options were exercised during the year.

No shares in Keycorp Limited were issued during or since the end of the year as a result of the exercise of options.

DIRECTORS' REPORT continued

FOR THE YEAR ENDED 30 JUNE 2007

INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

Under its constitution, the company indemnifies all past and present officers of the company and its wholly-owned subsidiaries against:

- any liability for costs and expenses incurred by that person in defending any proceedings in connection with an application in relation to any proceedings in which the court grants relief to that person under the *Corporations Act 2001*; and
- any liability incurred by the person as an officer of the company or a wholly-owned subsidiary to another person (other than the company or a related body corporate), unless the liability arises out of conduct involving a lack of good faith.

The company has offered each director of the company and the company secretary holding office since 1 July 1996 a Deed of Access and Indemnity permitting them access, in the event of an action against them, to board papers and reports, indemnifying them in substantially the same terms as provided in the company's constitution (described above) and giving an undertaking by the company to maintain Directors and Officers Liability and Company Reimbursement insurance covers. Directors and officers are to be held covered while in office and for a period of seven years after ceasing to hold that office with the company.

During the financial year, the company paid an insurance premium in respect of a contract insuring the directors, company secretary and executive officers of the company against a liability incurred as a director, company secretary or executive officer of the company to the extent permitted by the *Corporations Act 2001*. The terms of the contract of insurance prohibit disclosure of the amount of premium paid or the nature of liabilities covered.

DIRECTORS' INTERESTS

As at the date of this report, the interests of the directors in the company's ordinary shares or options over ordinary shares as notified by the directors to the Australian Securities Exchange in accordance with Section 205G(1) of the *Corporations Act 2001*, were:

| Name | Ordinary shares |
|------------|-----------------|
| M. Ibrahim | 8 750 |

Other than the above, no shares were acquired by directors during the year and up to the date of this report.

DIRECTORS' MEETINGS

During the financial year there were 26 board meetings, five Audit and Risk Committee meetings and four Remuneration and Nomination Committee meetings. The number of meetings attended by each director is set out in the table below:

| Directors | Notes | Regular board meetings | | Additional board meetings | | Audit & Risk Committee meetings | | Remuneration & Nomination Committee meetings | |
|--------------------------------------|-------|------------------------|----|---------------------------|----|---------------------------------|---|----------------------------------------------|---|
| | | A | B | A | B | A | B | A | B |
| No. of meetings held during the year | | | | | | | | | |
| | | 11 | | 15 | | 5 | | 4 | |
| Robert Bishop | | 11 | 11 | 15 | 12 | — | — | 4 | 4 |
| Kenneth Carr | 1,2 | 2 | 2 | 1 | 1 | 1 | 1 | — | — |
| Barry Grisdale | | 11 | 11 | 15 | 8 | 5 | 5 | 4 | 4 |
| Christine Holgate | | 11 | 11 | 15 | 14 | — | — | — | — |
| Michael Ibrahim | | 11 | 11 | 15 | 11 | 5 | 5 | — | — |
| Malcolm Irving | | 11 | 9 | 15 | 15 | 5 | 4 | 4 | 4 |
| Philip Jones | | 11 | 10 | 15 | 15 | 5 | 4 | — | — |
| Bruce Thompson | 3,4 | 10 | 10 | 14 | 14 | 4 | 4 | 4 | 4 |

Notes:

- Denotes the number of meetings held during the period the director was a member of the board and/or committee.
 - Denotes the number of meetings attended during the period the director was a member of the board and/or committee.
- Ken Carr was appointed as a director on 18 May 2007.
 - Ken Carr is not a member of the Audit & Risk Committee but attends meetings of the committee by invitation.
 - Bruce Thompson resigned as a director on 17 May 2007.
 - Bruce Thompson was not a member of the Audit and Risk Committee but attended meetings of the committee by invitation.

NON-AUDIT SERVICES

During the year Keycorp's auditor, KPMG, provided non-audit services to Keycorp group entities for fees totalling \$13 694. Those non-audit services consisted of:

| | |
|------------------------------------------------------------------------------------|---------|
| • assistance with respect to documentation of billing system (Keycorp Canada Inc.) | \$9 294 |
| • workers' compensation review (Keycorp Limited) | \$2 200 |
| • workers' compensation review (Fox Technology Pty Limited) | \$2 200 |

In accordance with advice from Keycorp's Audit and Risk Committee, directors are satisfied that the provision of the above non-audit services during the year is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. Also, in accordance with advice from the Committee, directors are satisfied that the provision of those non-audit services during the year did not compromise the auditor independence requirements of the *Corporations Act 2001* due to the nature of those services and because the amount of the fees charged for those services is relatively immaterial and furthermore the directors have no reason to question the veracity of the auditor's independence declaration referred to on page 72.

CORPORATE GOVERNANCE

The board of directors of Keycorp Limited is responsible for the corporate governance of the consolidated entity. This section describes the main corporate governance practices in place during the year to 30 June 2007.

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Keycorp support the principles of good corporate governance.

In this section various references are made to the company's website as a source of information on the company's corporate governance practices. The home page for Keycorp's website is www.keycorp.net and, for corporate governance matters, you should follow the links to "Investors Overview" and then "Corporate Governance". If you do not have Web access but wish to read this material, please telephone 1300 855 080 (or +61 3 9415 4000 if phoning from outside Australia) and we will send you a copy of the relevant material.

ASX CORPORATE GOVERNANCE COUNCIL BEST PRACTICE RECOMMENDATIONS

In March 2003 the ASX Corporate Governance Council issued its Principles of Good Corporate Governance and Best Practice Recommendations. The adoption of the Council's best practice recommendations is not compulsory for companies but, if a company considers a recommendation is inappropriate to its particular circumstances, it has the flexibility not to adopt it but it must disclose that it has made that decision and explain why it has done so.

The company has adopted the best practice recommendations in the reporting period except to the extent stated in this corporate governance section.

The board is aware that the ASX Corporate Governance Council issued its revised Corporate Governance Principles and Recommendations in August 2007 and that companies will be required to first report against the revised recommendations for the financial year ended 30 June 2009 (in the case of companies with a June year end). The company will be reviewing that document in the near future.

THE BOARD

The board of directors is accountable to shareholders for the proper management of Keycorp's business and affairs. It operates in accordance with a charter, a copy of which is published on the company's website.

STRUCTURE OF THE BOARD

The board may comprise from three to ten directors and as at the date of this report consists of the six directors whose respective terms of office as a director, and whose qualifications, experience and membership of board committees, are set out on pages 1 to 2.

The composition of the board is determined in accordance with the following principles:

- a majority of the board will be comprised of independent directors;
- the Chairman will be an independent director; and
- a person cannot hold the positions of both Chairman and Chief Executive Officer.

The company's constitution requires one-third of its directors (excluding the managing director) to retire from office at the company's annual general meeting each year. Retiring directors are eligible for re-election. When a vacancy is filled by the board during the year, the new director must stand for election at the next AGM.

INDEPENDENCE OF DIRECTORS

The company's adopted definition of an independent director is a non-executive director who:

- is not a substantial shareholder of the company or an officer of, or otherwise associated directly with, a substantial shareholder of the company;
- within the last three years has not been employed in an executive capacity by the company or another group member, or been a director after ceasing to hold any such employment;
- within the last three years has not been a principal of a material professional adviser or a material consultant to the company or another group member or an employee materially associated with the service provided;

- is not a material supplier or customer of the company or other group member or an officer of or otherwise associated directly or indirectly with a material supplier or customer;
- has no material contractual relationship with the company or another group member other than as a director of the company;
- has not served on the board for a period which could, or could reasonably be perceived to, materially interfere with the director's ability to act in the best interests of the company; and
- is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the director's ability to act in the best interests of the company.

The following materiality thresholds currently apply to that definition of independence:

- a substantial shareholder is a person with a substantial holding as defined in the *Corporations Act 2001* (five per cent or more of the total number of votes attached to voting shares);
- a material professional adviser or consultant is one whose fees to Keycorp in a financial year exceed \$1 000 000;
- a material supplier is one the value of whose sales to Keycorp in a financial year exceeds five per cent of the value of Keycorp's purchases;
- a material customer is one the value of whose purchases from Keycorp in a financial year exceeds five per cent of Keycorp's gross revenue; and
- a material contractual relationship, other than any of those described above, is one in respect of which the consideration payable under the contract exceeds \$1 000 000.

The board has assessed the independence of the non-executive directors and considers Robert Bishop, Barry Grisdale and Michael Ibrahim to be independent.

DIRECTORS' REPORT *continued*

FOR THE YEAR ENDED 30 JUNE 2007

CORPORATE GOVERNANCE *continued*

INDEPENDENCE OF DIRECTORS *continued*

With the retirement of former Chairman Malcolm Irving in July 2007, the board currently comprises six directors of whom three are independent, as noted above. The board is aware that the requirement of the board's charter that a majority of the board be comprised of independent directors – which requirement is consistent with the Principles of Good Corporate Governance and Best Practice Recommendations issued by the ASX Corporate Governance Council – is not currently being met. It is the board's current intention to appoint a further director with appropriate skills and experience to replace Malcolm Irving. If an independent director were to be appointed, a majority of independent directors would be restored. The board also notes in this context that pursuant to the company's constitution, in the case of an equality of votes, the Chairman will have a second or casting vote.

DECLARATION BY CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER

In the course of approving the financial statements for the year, the board considered a written statement by the company's Chief Executive Officer and Chief Financial Officer to the effect that:

- the financial statements give a true and fair view, in all material respects, of the company's financial position at the end of the year and its performance for the year and comply in all material respects with relevant accounting standards; and
- that statement as to the integrity of the financial statements is founded on a sound system of risk management and internal compliance and control.

INDEPENDENT ADVICE

Directors are free to take independent professional advice on matters pertaining to their roles and responsibilities as directors. The company will pay the reasonable legal costs incurred by a director in doing so, provided that before the advice is obtained the director discusses the requirement for the advice with the chairman.

COMMITTEES OF THE BOARD

The board also operates through committees that hold responsibility for particular areas. The committees which operated during the year are the Audit and Risk Committee and the Remuneration and Nomination Committee. Each of those committees operates in accordance with a charter, a copy of which is published on the company's website.

The number of times the committees have met during the year, and the names of the members of the committees and their respective attendances at the meetings, are set out in the directors' report on page 6.

AUDIT AND RISK COMMITTEE

Under its charter, the Committee is required to meet at least four times each year and to be comprised of:

- at least three members;
- only non-executive directors all of whom are to be financially literate and at least one of whom must have financial expertise as a qualified accountant or other financial professional with experience of financial and accounting matters. In this regard, the qualifications of the current committee members are set out on pages 1 to 2;
- a majority of independent directors; and
- an independent chairperson, who is not the chairperson of the board.

The committee provides assistance to the board in fulfilling its corporate governance and oversight responsibilities in relation to the company's financial reporting, internal control structure, risk management systems and the external audit function. In doing so, it is the responsibility of the committee to maintain free and open communication between the committee, the company's external auditors and management of the company.

In discharging the oversight role, the committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities and personnel of the company and the authority to engage independent counsel and other advisers as it determines necessary to carry out its duties.

The committee is also responsible for making recommendations to the board on the appointment, reappointment or replacement (subject, if applicable, to shareholder approval) and remuneration of the company's external auditors. It also monitors the effectiveness and independence of the auditors. The committee's charter sets out some guiding principles governing the company's relationship with its external auditors, the principal purpose of which is to promote the independence of the auditors.

During the year KPMG, the company's auditor, has performed certain other services in addition to their statutory duties.

The board has considered the non-audit services provided during the year by the auditor and is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the *Corporations Act 2001*.

REMUNERATION AND NOMINATION COMMITTEE

The Remuneration and Nomination Committee advises the board on remuneration policies and practices generally and makes recommendations on remuneration packages and other terms of employment for executive and non-executive directors and senior executives and other employees. That role is also referred to in the remuneration report which starts on page 9.

The committee also oversees and advises the board on company share schemes, company superannuation arrangements and replacement and succession planning for key executives.

In its role as a nomination committee the committee assesses the desirable competencies of board members and makes recommendations to the board on succession plans for maintaining the appropriate balance of competencies and the appointment and removal of directors.

BUSINESS STANDARDS

The company recognises that acting with uncompromising integrity and professionalism will protect and enhance its reputation, an invaluable asset of the company. Accordingly, the directors have approved a set of Corporate Business Standards, a summary of which is available on the company's website, and reviews those standards annually.

The Corporate Business Standards include sections on Keycorp's policy on:

- trading by directors and staff in the company's shares
- the company's compliance with its obligation, as a listed public company, to immediately notify the Australian Stock Exchange of any information concerning the company of which it is or becomes aware and which a reasonable person would expect to have a material affect on the price or value of the company's shares.

Summaries of both those policies are available on the company's website.

COMMUNICATION WITH SHAREHOLDERS

The board aims to ensure that shareholders are informed of all significant developments affecting the company's state of affairs. Information is communicated to shareholders by the following means:

- the interim (half yearly) report, the annual report and directors' commentaries on those reports;
- the company's website which has a dedicated investor relations section called Investors Overview (at www.keycorp.net/InvestorOverview/Overview);
- disclosures made to the Australian Stock Exchange, copies of which are posted to the company's website;
- notices and explanatory memoranda of general meetings; and
- the annual general meeting.

It is the company's policy to request the external auditor to attend annual general meetings and to be available to answer shareholders' questions about the conduct of the audit and the preparation and content of the auditor's report.

RISK MANAGEMENT

The board is responsible for approving and reviewing the company's operational risk management strategy and policy. The management of operational risk and implementation of mitigation measures is the responsibility of management.

The board considers significant business risks as part of its annual strategy review and budget planning review. The board has delegated to its Audit and Risk Committee the role of overseeing risk management as more particularly described as follows.

Keycorp's management conducts reviews of significant business risks relating to current operations and new business initiatives and, through that process, identifies and then implements board-approved policies, control procedures and mitigation strategies.

The results of management's reviews are reported semi-annually to the Audit and Risk Committee and the committee provides a report, and where appropriate makes recommendations, to the board on the company's risk profile.

The committee oversees management's processes for and results in identifying, assessing and monitoring risks associated with the company's operations and the implementation and maintenance of board-approved policies, control procedures and mitigation strategies that address significant risks.

In doing so, the committee considers and assesses the appropriateness and effectiveness of management information and systems of internal control, and also reviews reports to management from the company's external auditor and action taken or proposed as a consequence of such reports.

The company publishes on its website a description of its risk management policy and internal compliance and control system.

PERFORMANCE EVALUATION

This year the board has reviewed the process whereby the performance of the board, its committees and individual directors is evaluated. An external consultant has been engaged to collate and review responses from individual directors to a detailed questionnaire on performance issues and that consultant will subsequently facilitate a board discussion of issues requiring attention and the formulation of appropriate action plans. It is expected that this process will be completed in September 2007.

The company's key executives and other employees are subject to a performance management process pursuant to which their performance is reviewed against identified and documented goals. The Chief Executive Officer's performance is reviewed annually by the Remuneration and Nomination Committee.

REMUNERATION REPORT

REMUNERATION POLICIES AND PRACTICES — AUDITED

The Remuneration and Nomination Committee (Committee) is responsible for designing and implementing (upon board approval) the company's remuneration policies and practices. The Committee endorses Principle 9 of the Australian Stock Exchange (ASX) Corporate Governance Council's Principle of Good Governance: "Remuneration fairly and responsibly".

Details of the specific remuneration policies and the remuneration mixes paid by the company are set out in this Remuneration Report which should be read in conjunction with note 37 of the Financial Report.

REMUNERATION AND NOMINATION COMMITTEE

The role of the Committee is to:

- advise the board on remuneration policies and practices generally;
- make recommendations to the board on the remuneration and other terms of employment for executive and non-executive directors, senior executives and other employees; and
- assess, monitor and advise the board on the desirable competencies of board members and on whether the balance of skills, experience and expertise of the board is sufficient to enable it to discharge its mandate effectively.

The Committee has a charter, which is published in the Corporate Governance section of the company's website (www.keycorp.net).

The board performs an evaluation of the Committee's performance on an annual basis.

The experience and qualifications of members of the Committee are detailed on pages 1 to 2. Membership of and attendance at 2006/07 Committee Meetings are detailed on page 6.

Key management personnel have authority and responsibility for planning, directing and controlling the activities of the company and the consolidated entity, including directors of the company and other executives. Key management personnel comprise the directors of the company and executives of the company and consolidated entity including the five most highly remunerated S300A executives.

DIRECTORS' REPORT continued

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued**NON-EXECUTIVE DIRECTORS****Policy**

The policy for remuneration of non-executive directors is set by the board, on recommendation from the Committee and is based on comparable market data.

Non-Executive Director fees

Board members' fees are determined within an aggregate Directors' fee pool limit, which is periodically approved by shareholders. The current limit of \$500 000 was last approved by shareholders at the November 2002 Annual General Meeting (AGM). During the year ended 30 June 2007, \$423 271, excluding retirement benefits of \$94 041, (2006: \$454 528) of the fee pool was used.

For 2006/07 the fees payable to the board remained unchanged from the prior year. In summary, the following fees were paid to directors:

- the Chairman received \$137 158 (full year equivalent of \$141 700. M Irving retired as Chairman effective 1 June 2007);
- non-executive directors each received \$65 000;
- an additional \$10 000 is paid to the Chairman of each Committee; and
- an additional \$5 000 is paid to every member of each Committee.

Equity Participation

No non-executive director has received options as part of their remuneration. Non-executive directors do not receive any performance-related remuneration.

Non-executive directors may participate in the Keycorp Deferred Employee Share Plan (DESP) by way of fee sacrifice. The Chairman and one other non-executive director have participated in the DESP this year.

Retirement Benefits

The board resolved to discontinue the practice of awarding retirement benefits in 2003. The benefits for non-executive directors under the existing plan were determined as at 30 November 2003, based on their service to that date, in the aggregate amount of \$107 885. Those benefits will be preserved, and will be paid to qualifying directors on their retirement. During the year an amount of \$94 041 was paid to M Irving on retirement.

Superannuation

The company pays all non-executive directors the statutory superannuation guarantee contribution with the exception of the former Chairman who, after attaining the age of 70, was no longer eligible to receive pre-tax employer contributions under legislation.

Service Contracts

No non-executive director has a service contract with the company and therefore there are no termination notice periods nor termination payments. There are however, some preserved retirements benefits payable under a former plan as discussed above.

EXECUTIVES**Policy**

Executive remuneration policies are set by the Committee and are reviewed on a regular basis to ensure they remain competitive. The company engages external remuneration consultants to advise on appropriate executive remuneration packages. Selected survey data is also used for benchmarking purposes.

Executive remuneration is determined having regard to the following guiding principles:

- there should be a balance between fixed and variable salary components that is appropriate having regard to both internal and external factors;
- all performance objectives should be appropriately linked to measurable personal and group performance; and
- total compensation – the sum of fixed and variable remuneration components – for each executive should be fair, reasonable and competitive.

The remuneration for the executive director and all senior executive roles is reviewed in September each year following a detailed assessment of achievements in the previous 12 months. Any remuneration adjustment of senior executives is subject to the review and approval of the Chief Executive Officer and is reported to the Remuneration and Nomination Committee.

There are two components of executive remuneration:

- fixed annual remuneration comprising of salary and superannuation; and
- "at risk" remuneration, comprising of both short-term and long-term elements.

Fixed Annual Remuneration

Executives are offered a base salary and benefits. The base salary is reviewed and benchmarked on a regular basis against the market.

Adjustments to base salary are made based on promotion or significant changes to an executive's responsibilities, pay relativities to market and individual performance in relation to agreed performance objectives. Base salary may be increased annually.

Superannuation

The company pays all executives the statutory superannuation guarantee contribution. Executives may also salary sacrifice (pre-tax) into their nominated superannuation fund, up to the statutory age base limit.

"At Risk"/Performance linked remuneration**Short-term incentives**

Short-term incentives in the form of cash bonuses are paid to executives based on a combination of:

- individual performance; and
- company performance.

Company performance is measured against a range of mainly quantitative financial performance measures. These measures include:

- revenue and profit targets;
- generation of new business;
- corporate governance and reporting requirements; and
- integration of infrastructure to create quality improvements and efficiencies.

Specific targets are set for the Chief Executive Officer which are described below.

Performance targets are agreed with each executive at the beginning of each performance period and results are assessed against those targets to determine the value of any payment. With the exception of the Chief Executive Officer, whose bonus may be paid upon the determination of the board, all executive bonuses are payable at the absolute discretion of the Chief Executive Officer.

The proportion of individual and company performance differs amongst executives depending on the nature and responsibilities of their position and market relativities.

“At Risk”/Performance linked remuneration continued

Long-term incentives

Long-term incentives are determined based on a combination of two objectives:

- performance of the company; and
- ensuring the retention of key executives.

Historically, selected executives have received share option allocations under the Keycorp Employee Share Option Incentive Plan (ESOIP). Further awards were made during 2006/07 as approved by shareholders at the 2005 AGM. The performance hurdles for these plans are discussed on page 12. Further details of all equity plans are available on pages 12 to 14.

Other Benefits

Senior executives may also receive additional non-cash benefits as part of their remuneration. Non-cash benefits typically include long-term salary continuance insurance and life insurance, partial contributions towards the executive's private health care plan, and car parking fees. The company pays all fringe benefits tax on insurance items.

No loans have been made to any director or executive of the company, including their personally-related entities during the year.

Service Contracts

With the exception of the Chief Financial Officer, all key management personnel who currently hold executive positions in the company have permanent full-time contracts. At the time of preparing the annual report the Chief Financial Officer was working under a six month contract. From September 2007 the Chief Financial Officer will be employed under a permanent contract, with a minimum three-month termination notice by the employee (six-month by the company) clause. One other executive, R. Ganeson, has a minimum three-month termination notice clause, while all other executives currently have a minimum one-month termination notice, which can be triggered by either party. There are no other contractual termination payments for any executive except for the Chief Executive Officer who has a six month notice period.

Chief Executive Officer

Dr Ken Carr was appointed Chief Executive Officer on the 18 May 2007.

For the year ended 30 June 2007, details of Dr Carr's remuneration package are as follows:

- Base salary (pro-rated accordingly): \$314 000 from 18 May until 30 June;
- Packaged benefits (pro-rated accordingly): \$39 000 from 18 May until 30 June; and
- Short term cash bonus target: \$150 000 with a first payment opportunity after announcement of the 30 June 2008 company performance results.

At the 2007 Annual General Meeting, shareholders will consider a proposal to award the Chief Executive Officer 1 220 000 options at an exercise price of \$0.365 to subscribe for 1 220 000 fully paid ordinary shares in the company, under the Keycorp Employee Share Option Incentive Plan.

The grant of options coinciding with Dr Carr's appointment and subject to shareholder approval was designed to provide both a performance motivation as well as act as a retention incentive.

The proposal is to grant options in three tranches:

- 406 666 options that may vest on 17 May 2009;
- 406 667 options that may vest on 17 May 2010; and
- 406 667 options that may vest on 17 May 2011.

The proposed options to be granted to the Chief Executive Officer will only vest if Keycorp's Total Shareholder Return (TSR) is greater than or equal to the S&P/ASX 200 Information Technology (XIJ) Index for twenty consecutive trading days on or after the first exercise date for each tranche. Growth in TSR is defined as share price growth, any dividends paid and reinvested on the ex-dividend date (adjusted for rights, bonus issues and any capital reconstructions).

In relation to an appropriate award for the Chief Executive Officer, the Directors sought independent advice and then selected a model of simple out-performance against the S&P/ASX 200 Information Technology Index for several reasons:

- this index is the most representative for the company in considering the current strategy and relative size of participants. In previous years the S&P ASX 300 Accumulation Index was deemed most representative considering the company dimensions applicable at the time;
- simple out-performance of the index is a sufficiently demanding test in its own right;
- the board's revised policy to put an amount equivalent to 80-100% of the Chief Executive Officer's fixed annual remuneration at risk in the form of Keycorp options; and
- the desire to balance the dilutive impact of the issue with the need to offer a market competitive incentive to attract, motivate and retain a suitably experienced executive. A more demanding performance hurdle would have resulted in a larger number of options being offered in order to provide the same remuneration value.

Former Chief Executive Officer

After announcing his retirement in March 2007, Mr Thompson resigned as Chief Executive Officer and Executive Director of Keycorp effective 17 May 2007 and left the Company effective 30 June 2007. Mr Thompson received a termination payment as prescribed by his employment contract.

Details of Mr Thompson's remuneration arrangements for the year ended 30 June 2007 and termination payment are set out in the tables on page 14.

RELATIONSHIP BETWEEN POLICY & PERFORMANCE – AUDITED

The company's and consolidated entity's remuneration policies and practices are designed to ensure that remuneration packages are set at a fair and competitive rate, enabling the company and consolidated entity to attract, motivate and retain executives and board members of a high calibre. The nature and levels of remuneration are regularly assessed against relevant market surveys, with input from Human Resources and independent advisors when required.

DIRECTORS' REPORT continued

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued**RELATIONSHIP BETWEEN POLICY & PERFORMANCE — AUDITED** continued

A diverse range of remuneration tools are employed at Keycorp. Remuneration is a mix of fixed and "at-risk" pay and of short, medium and long-term awards. The executives (including the Chief Executive Officer) who are key management personnel are rewarded for both company and individual performance and these rewards are based on the achievement of targets set in prior financial years and measured during the year and targets set in the current financial year to be measured at some future point in time. Non-executive Directors who are key management personnel do not have any "at-risk" remuneration but instead are paid fees within the pool limit as approved by shareholders.

It is noted that some awards have been designed to reward any increase in share price and this is a condition to vesting. Other awards enable participants to enjoy any increase in share price and any returns to shareholders. Cash payments are only made upon the achievement of pre-determined financial targets. Together, these policies attempt to align key management personnel and shareholder interests.

Each plan and its purpose are described below.

Finally, the table below sets out some indices in respect of the company's performance (and the effect on shareholder wealth) in the current financial year and the previous four financial years. The "at-risk" component paid to key management personnel is dependent in part on the company's performance.

| | 2007 ⁽ⁱ⁾ | 2006 ⁽ⁱ⁾ | 2005 ⁽ⁱⁱ⁾ | 2004 ⁽ⁱⁱ⁾ | 2003 ⁽ⁱⁱ⁾ |
|-----------------------------------------------|---------------------|---------------------|----------------------|----------------------|----------------------|
| EBITDA (\$m)* | (8.0) | 9.5 | 31.2 | 18.9 | (31.2) |
| Net (loss)/profit (after tax) (\$m) | (11.5) | (2.9) | (2.0) | 16.5 | (51.0) |
| Dividends paid (\$m) | — | — | — | 2.5 | — |
| Change in share price (\$: at 30 June) | (0.56) | (0.96) | 0.47 | 0.30 | 0.28 |
| Return of capital | — | 0.41 | — | — | — |
| (Loss)/Earnings per share (\$) | (0.140) | (0.035) | (0.024) | 0.202 | (0.620) |

* EBITDA includes interest income.

(i) These indices have been prepared in accordance with Australian equivalents to International Financial Reporting Standards.

(ii) These indices have been prepared in accordance with previous Australian Generally Accepted Accounting Principles

DESCRIPTION**Keycorp Employee Share Option Incentive Plan**

Shareholders approved the introduction of the Keycorp Employee Share Option Incentive Plan (ESOIP) at the 1996 Annual General Meeting.

Each option granted under the ESOIP entitles the employee to acquire one ordinary share of Keycorp Limited. There are no voting or dividend rights attaching to the options until they are exercised by the employee, at which point ordinary shares which rank equally with all other Keycorp shares, are issued and quoted on the ASX. The options cannot be transferred and will not be quoted on the ASX.

The options granted are exercisable between two and four years from grant date providing performance hurdles are attained. The hurdles are twofold and require continuous employment by the employee during the vesting period and for Keycorp's Total Shareholder Return (TSR) to be greater than or equal to the S&P/ASX 300 Accumulation Index for twenty consecutive trading days on or after the first exercise date for each tranche. The S&P/ASX 300 Accumulation Index was deemed the most representative index for options granted through to October 2006. Growth in TSR is defined as share price growth, any dividends paid and reinvested on the ex-dividend date (adjusted for rights, bonus issues and any capital reconstructions).

All options expire on the earlier of their expiry date or termination of the individual's employment. In certain circumstances, at the discretion of management, employees included in an involuntary redundancy program are eligible to retain and exercise share options in accordance with the terms and conditions of the particular options issue.

The price payable by eligible employees for options is determined as the weighted average market price for Keycorp Limited shares traded on the ASX for the five days prior to the date of the offer of options.

RATIONALE

The ESOIP is a long-term equity plan designed to align remuneration with growth in share price (and therefore growth in shareholder value). The ESOIP is a key long-term retention tool for key executives.

DESCRIPTION

Keycorp Deferred Employee Share Plan

Shareholders approved the introduction of the Keycorp Deferred Employee Share Plan (DESP) at the 2006 AGM.

There are two components to the DESP: a company award and a salary sacrifice element.

Company Award

Under this part of the DESP, select key management personnel are offered "deferred shares" to be held subject to a series of holding locks.

Under these awards, shares were allocated in March 2006 and were subject to three separate vesting schedules:

- one-third are "available" to be released from holding lock after 2 years from the date of allocation (being March 2008);
- one-third are "available" to be released from holding lock after 3 years from the date of allocation (being March 2009); and
- one-third are "available" to be released from holding lock after 4 years from the date of allocation (being March 2010);

The following additional performance criteria must also be met prior to any vesting:

- the participant must remain continuously employed with the company to receive those shares which are "available"; and
- the participant must achieve a solid performance rating or better against objectives contained in their individual Performance Agreement. The Performance Condition must be satisfied at any time prior to each tranche of shares becoming "available".

Shares may not be sold or transferred until after they have vested, and prior to vesting a participant has only a conditional entitlement to the shares. Should the relevant conditions not be met, including for reason of cessation of employment, the entitlement will lapse (and shares will be forfeited by the participant).

All shares acquired under the DESP rank equally with all other ordinary shares, and carry full shareholder rights. However, they are not able to participate in any dividend reinvestment plans.

Under this part of the DESP, key management personnel may elect to sacrifice the whole or part of their remuneration to acquire shares in the company at the same time each month when their remuneration is payable. Those shares are acquired on-market by the independent plan manager independent from the company and the participant.

DESCRIPTION

Keycorp Exempt Employee Share Plan

Salary Sacrifice: The Share Save Offer

Shareholders approved the introduction of the Keycorp Exempt Employee Share Plan (EESP) at the 2005 AGM.

The EESP gives eligible Australian employees the opportunity to acquire up to \$1 000 of Keycorp shares per financial year, tax free. The employee nominates to acquire up to \$500 worth of Keycorp shares that will be deducted from their pre-tax salary or wages over the financial year. Keycorp matches this contribution on a dollar for dollar basis by purchasing or issuing an additional \$500 of shares (to total \$1 000 worth of shares for the participant). The invitation to eligible employees to participate in the EESP occurs only once a year, in accordance with the relevant taxation legislation.

Shares acquired under this plan rank equally with all existing ordinary shares of Keycorp Limited and are quoted on the ASX. Shares acquired under the EESP must be held under a trading lock until the earlier of three years from allocation and cessation of employment with the Keycorp Group.

Employee shareholders are entitled to any dividends paid and to vote at general meetings.

There were no issues under this plan during the 2006/07 financial year.

RATIONALE

The DESP is a medium-term incentive and is a key retention tool. Key management personnel are awarded a number of shares which may vest in three tranches from the second anniversary from the date of allotment. Receipt of shares upon the holding lock being removed is dependent on the executive remaining employed with the Keycorp Group. Participants share in benefits enjoyed by shareholders (such as any dividends and the right to vote).

RATIONALE

The EESP is a broad-based incentive designed to give employees an interest in Keycorp's share price and to recognise their individual contributions to the company.

DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued

DESCRIPTION

Keycorp Short Term Incentive Plan

The Keycorp Short Term Incentive Plan (STI) is designed to reward the executives (including the Chief Executive Officer) who are key management personnel when key performance measures are achieved over a 12-month business cycle. The target reward is set on an individual basis in relation to each key management personnel dependant on their level or responsibility and is confirmed to executives in writing separately.

Both financial and non-financial measures determines the amount (if any) of the pool of money available for payment under this Plan. These measures are however mainly financial and include revenue and profit targets and generation of new business.

Where the board approves a pool for the STI payment, the performance of individuals is measured against specific key performance indicators. An executive's contribution relative to other executives (individual performance factors) are taken in to account as well. This results in a differentiated distribution of the incentive pool between executives based on individual performance.

RATIONALE

The purpose of this plan is to measure (and balance) the company's financial performances as well as an executive's individual performance. It is a short-term reward for past performance.

KEY MANAGEMENT PERSONNEL REMUNERATION – AUDITED

Set out in the following tables is the remuneration for the key management personnel of the consolidated entity during the year ended 30 June 2007.

2007

Directors – Company and Consolidated

| | Short term | | | | Post employment | | | | Equity based payments | | Total | Proportion of remuneration performance related | Value of option as proportion of remuneration |
|----------------------------------|-------------------------------|-------------------------------------|--------------------------------------------|---------|--------------------------|--------------------|----------------------|-------------------------|-----------------------|-----------|-------|------------------------------------------------|-----------------------------------------------|
| | Salary & fees ⁽²²⁾ | STI cash bonus ^{(23),(24)} | Non-monetary benefits ^{(25),(26)} | Total | Super-annuation benefits | Long service leave | Termination benefits | Options ⁽²⁷⁾ | Shares | | | | |
| | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | % | % |
| Non Executive Directors | | | | | | | | | | | | | |
| R. Bishop(Chair) ⁽¹⁾ | 74 722 | — | 7 422 | 82 144 | 6 725 | — | — | — | — | 88 869 | — | — | — |
| B. Grisdale | 80 000 | — | 6 553 | 86 553 | 7 200 | — | — | — | — | 93 753 | — | — | — |
| C. Holgate ⁽²⁾ | — | — | 6 553 | 6 553 | — | — | — | — | — | 6 553 | — | — | — |
| M. Ibrahim ⁽³⁾ | 63 566 | — | 6 916 | 70 482 | 6 350 | — | — | — | 7 000 | 83 832 | — | — | — |
| P. Jones ^{(2),(4)} | — | — | 6 553 | 6 553 | — | — | — | — | — | 6 553 | — | — | — |
| Former | | | | | | | | | | | | | |
| M. Irving (Chair) ⁽⁵⁾ | 109 658 | — | 6 553 | 116 211 | 94 041 | — | — | — | 27 500 | 237 752 | — | — | — |
| Executive Director | | | | | | | | | | | | | |
| Current | | | | | | | | | | | | | |
| K. Carr ⁽⁶⁾ | 38 244 | — | 1 100 | 39 344 | 3 982 | 4 | — | 9 747 | — | 53 077 | — | 18.4 | — |
| Former | | | | | | | | | | | | | |
| B. Thompson ⁽⁷⁾ | 575 931 | — | 11 844 | 587 775 | 49 547 | — | 520 000 | (19 296) | — | 1 138 026 | — | — | — |
| Total | 942 121 | — | 53 494 | 995 615 | 167 845 | 4 | 520 000 | (9 549) | 34 500 | 1 708 415 | — | — | — |

2006

Directors — Company and Consolidated

| | Short term | | | | Post employment | | | | Equity based payments | | Total | Proportion of remuneration performance related | Value of option as proportion of remuneration |
|----------------------------------|-------------------------------|-----------------------------------------|--------------------------------------------|----------------|--------------------------|--------------------|----------------------|-------------------------|-----------------------|----------|----------------|------------------------------------------------|-----------------------------------------------|
| | Salary & fees ⁽²²⁾ | Non-STI cash bonus ^{(23),(24)} | Non-monetary benefits ^{(25),(26)} | Total | Super-annuation benefits | Long service leave | Termination benefits | Options ⁽²⁷⁾ | Shares | | | | |
| | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | % | % |
| Non Executive Directors | | | | | | | | | | | | | |
| M. Irving (Chair) ⁽⁵⁾ | 141 700 | — | 7 514 | 149 214 | — | — | — | — | — | — | 149 214 | — | — |
| R. Bishop ⁽¹⁾ | 31 055 | — | 4 026 | 35 081 | 2 796 | — | — | — | — | — | 37 877 | — | — |
| B. Grisdale | 80 000 | — | 7 514 | 87 514 | 7 200 | — | — | — | — | — | 94 714 | — | — |
| C. Holgate ⁽²⁾ | — | — | 3 652 | 3 652 | — | — | — | — | — | — | 3 652 | — | — |
| M. Ibrahim ⁽³⁾ | 31 055 | — | 3 820 | 34 875 | 2 796 | — | — | — | — | — | 37 671 | — | — |
| P. Jones ^{(2),(4)} | — | — | 6 870 | 6 870 | — | — | — | — | — | — | 6 870 | — | — |
| A. Lockwood ⁽⁸⁾ | — | — | 1 287 | 1 287 | — | — | — | — | — | — | 1 287 | — | — |
| D. Standen ⁽⁹⁾ | 41 667 | — | 4 925 | 46 592 | 4 275 | — | 33 846 | — | — | — | 84 713 | — | — |
| J. Wood ⁽¹⁰⁾ | 19 167 | — | 3 490 | 22 657 | 1 725 | — | 14 148 | — | — | — | 38 530 | — | — |
| Executive Director | | | | | | | | | | | | | |
| B. Thompson ⁽⁷⁾ | 403 067 | 55 000 | 10 896 | 468 963 | 36 276 | 494 | — | 19 296 | — | — | 525 029 | 14.2 | 3.7 |
| Total | 747 711 | 55 000 | 53 994 | 856 705 | 55 068 | 494 | 47 994 | 19 296 | — | — | 979 557 | — | — |

2007

Other Key Management Personnel

| | Short term | | | | | Post employment | | | | Equity based payments | | Total | Proportion of remuneration performance related | Value of option as proportion of remuneration |
|-------------------------------------------|-------------------------------|----------------|-------------------------------------|--------------------------------------------|------------------|--------------------------|--------------------|----------------------|-------------------------|-----------------------|------------------|----------|------------------------------------------------|-----------------------------------------------|
| | Salary & fees ⁽²²⁾ | Annual leave | STI cash bonus ^{(23),(24)} | Non-monetary benefits ^{(25),(26)} | Total | Super-annuation benefits | Long service leave | Termination benefits | Options ⁽²⁷⁾ | Shares | | | | |
| | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | % | % |
| Executives | | | | | | | | | | | | | | |
| Current | | | | | | | | | | | | | | |
| J. Bonin ^{(11)*} | 269 985 | 5 531 | 128 516 | 9 407 | 413 439 | 20 506 | 5 213 | — | 32 281 | — | 471 439 | 27.3 | 6.8 | |
| R. Cusson* | 205 473 | 25 345 | 97 553 | 13 354 | 341 725 | 23 325 | 9 435 | — | 10 971 | 7 929 | 393 385 | 24.8 | 2.8 | |
| R. Ganeson* [^] | 232 014 | 15 306 | 32 489 | 15 201 | 295 010 | 22 254 | 112 | — | 38 123 | — | 355 499 | 9.1 | 10.7 | |
| P. Herington ^{(12)*[^]} | 126 394 | — | — | 2 184 | 128 578 | 11 375 | — | — | — | — | 139 953 | — | — | |
| M. Knapman ^{(13)*[^]} | 291 600 | 20 400 | — | 20 884 | 332 884 | 28 080 | 8 611 | — | 21 492 | — | 391 067 | — | 5.5 | |
| M. Ritter ⁽¹⁴⁾ | 89 128 | 846 | 25 618 | 3 612 | 119 204 | 8 098 | 10 | — | — | — | 127 312 | 20.1 | — | |
| J. Stevens [^] | 177 820 | 8 038 | 33 968 | 12 863 | 232 689 | 16 727 | 21 | — | 12 469 | — | 261 906 | 13.0 | 4.8 | |
| Former | | | | | | | | | | | | | | |
| B. Johnson ^{(15)[^]} | 111 776 | 55 585 | — | 6 738 | 174 099 | 10 509 | — | — | (11 908) | — | 172 700 | — | — | |
| P. De Rosse ⁽¹⁶⁾ | 220 142 | 26 765 | — | 12 808 | 259 715 | 32 083 | — | 187 094 | (11 908) | — | 466 984 | — | — | |
| Total | 1 724 332 | 157 816 | 318 144 | 97 051 | 2 297 343 | 172 957 | 23 402 | 187 094 | 91 520 | 7 929 | 2 780 245 | — | — | |
| Total Executives Group | 1 724 332 | 157 816 | 318 144 | 97 051 | 2 297 343 | 172 957 | 23 402 | 187 094 | 91 520 | 7 929 | 2 780 245 | — | — | |
| Total Executives Company | 939 604 | 99 329 | 66 457 | 57 870 | 1 163 260 | 88 945 | 8 744 | — | 60 176 | — | 1 321 125 | — | — | |

* Denotes one of the highest five paid executives of the Group.

[^] Denotes one of the highest five paid executives of the Company.

Company executives include R. Ganeson, P. Herington, M. Knapman, J. Stevens and B. Johnson.

Group executives include the company executives and J. Bonin, R. Cusson, M. Ritter and P. DeRosse.

DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued

KEY MANAGEMENT PERSONNEL REMUNERATION – AUDITED continued

2006

Other Key Management Personnel

| | Short term | | | | | Post employment | | | | Equity based payments | | Total | Proportion of remuneration related | Value of option as proportion of remuneration |
|---------------------------------|-------------------------------|---------------|-------------------------------------|--------------------------------------------|------------------|--------------------------|--------------------|----------------------|-------------------------|-----------------------|------------------|-------|------------------------------------|-----------------------------------------------|
| | Salary & fees ⁽²²⁾ | Annual leave | STI cash bonus ^{(23),(24)} | Non-monetary benefits ^{(25),(26)} | Total | Super-annuation benefits | Long service leave | Termination benefits | Options ⁽²⁷⁾ | Shares | | | | |
| | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ | % | % |
| Executives | | | | | | | | | | | | | | |
| Current | | | | | | | | | | | | | | |
| J. Bonin ⁽¹¹⁾ | 205 691 | 2 373 | 86 580 | 13 479 | 308 123 | 18 512 | 8 281 | — | 11 874 | — | 346 790 | 28.4 | 3.4 | |
| M. Bryant ⁽¹⁷⁾ | 225 196 | — | — | 7 514 | 232 710 | 12 139 | 20 134 | 246 115 | — | — | 511 098 | — | — | |
| R. Cusson | 106 545 | 1 864 | 84 759 | 4 397 | 197 565 | 9 955 | 6 956 | — | 1 246 | 2 433 | 218 155 | 40.5 | 0.6 | |
| P. DeRosse | 293 203 | — | 71 063 | 14 581 | 378 847 | — | — | — | 10 894 | — | 389 741 | 21.0 | 2.8 | |
| J. Esplin ⁽¹⁷⁾ | 66 144 | — | 3 520 | 15 509 | 85 173 | 5 953 | 20 | — | 3 606 | — | 94 752 | 7.5 | 3.8 | |
| R. Ganeson | 247 320 | 5 764 | 30 000 | 16 519 | 299 603 | 22 254 | 15 | — | 17 447 | — | 339 319 | 14.0 | 5.1 | |
| D. Hatton ⁽¹⁷⁾ | 103 662 | — | 20 892 | 16 443 | 140 997 | 8 280 | — | — | 1 246 | 1 622 | 152 145 | 15.6 | 0.8 | |
| B. Johnson | 185 325 | 2 138 | 18 140 | 12 383 | 217 986 | 16 734 | 7 091 | — | 10 894 | — | 252 705 | 11.5 | 4.3 | |
| M. Knapman | 312 000 | 1 200 | 7 540 | 21 817 | 342 557 | 28 170 | 13 502 | — | 11 429 | — | 395 658 | 4.8 | 2.9 | |
| M. Nagy ⁽¹⁷⁾ | 226 084 | 9 308 | — | 7 514 | 242 906 | 12 139 | 3 081 | — | — | — | 258 126 | — | — | |
| J. Smerek ⁽¹⁷⁾ | 70 857 | — | — | 10 908 | 81 765 | 6 070 | — | — | 890 | 1 622 | 90 347 | 2.8 | 1.0 | |
| Former | | | | | | | | | | | | | | |
| A. Bradford ⁽¹⁸⁾ | — | — | — | — | — | — | — | 63 389 | 880 | — | 64 269 | 1.4 | 1.4 | |
| G. Duursma ⁽¹⁹⁾ | 152 869 | — | 59 790 | 12 004 | 224 663 | 13 758 | — | 91 175 | 13 368 | — | 342 964 | 21.3 | 3.9 | |
| T. Fletcher ⁽²⁰⁾ | 116 784 | — | 20 000 | 10 127 | 146 911 | 12 238 | — | — | (1 083) | — | 158 066 | 12.0 | (0.1) | |
| K. Mouton ⁽²¹⁾ | 102 583 | — | 7 540 | 7 822 | 117 945 | 9 232 | — | — | (7 871) | — | 119 306 | 0.0 | (6.6) | |
| Total | 2 414 263 | 22 647 | 409 824 | 171 017 | 3 017 751 | 175 434 | 59 080 | 400 679 | 74 820 | 5 677 | 3 733 441 | | | |
| Total Executives Group | 2 414 263 | 22 647 | 409 824 | 171 017 | 3 017 751 | 175 434 | 59 080 | 400 679 | 74 820 | 5 677 | 3 733 441 | | | |
| Total Executives Company | 1 357 544 | 9 102 | 167 422 | 123 532 | 1 657 600 | 122 689 | 20 628 | 154 564 | 50 806 | 3 244 | 2 009 531 | | | |

Company executives include J. Esplin, R. Ganeson, B. Johnson, D. Hatton, M. Knapman, J. Smerek, A. Bradford, G. Duursma, T. Fletcher and K. Mouton.

Group executives include company executives and J. Bonin, M. Bryant, P. DeRosse, M. Nagy.

(1) Appointed Chairman in June 2007. Chairman's fee of \$4 167 for one month has been included.

(2) These directors are nominated by Telstra. There are no fees payable to either Telstra or these individual directors by Keycorp Limited in relation to these directorships.

(3) During the year, Mr Ibrahim fee sacrificed \$7 000 under the Keycorp Deferred Employee Share Plan (DESP).

(4) Appointed member of the Audit and Risk Committee effective 22 September 2005.

(5) During the year, Mr Irving fee sacrificed \$27 500 under the Keycorp Deferred Employee Share Plan (DESP). Retirement benefits of \$94 041 were paid to Mr Irving.

(6) Appointed Managing Director and Chief Executive Officer on 18 May 2007.

(7) Terminated employment effective 30 June 2007. During the year, Mr Thompson salary sacrificed \$55 566 (2006: \$71 787) into superannuation. Termination benefits of \$520 000 were paid into superannuation. In the prior year Mr Thompson was paid \$83 067 in back pay when terms of his new contract were settled.

(8) Retired 1 August 2005.

(9) Retired 16 January 2006.

(10) Granted leave of absence from the board in August 2005 and resigned as a director on 22 November 2005.

(11) During the year, Mr Bonin salary sacrificed \$20 000 (2006: \$30 000) into superannuation and \$11 611 (2006: \$17 082) for a motor vehicle.

(12) Mr Herington became key management personnel from 12 March 2007. During the year Mr Herington salary sacrificed \$73 125 into superannuation.

(13) During the year Mr Knapman salary sacrificed nil (2006: \$5 000) into superannuation and nil (2006: \$6 200) for a motor vehicle.

(14) Appointed General Manager Keycorp Services on 5 February 2007. Remuneration is disclosed from that date.

(15) Mr Johnson ceased employment on 16 February 2007. Remuneration disclosed is effective to that date.

(16) Mr DeRosse ceased employment on 8 June 2007. Remuneration disclosed is effective to that date.

(17) Ceased to be key management personnel as at 31 December 2005.

(18) Ms Bradford ceased employment in January 2005. Remuneration disclosed is effective to that date.

(19) Mr Duursma ceased employment in February 2006. Remuneration disclosed is effective to that date.

(20) Mr Fletcher ceased employment in January 2006. Remuneration disclosed is effective to that date.

(21) Ms Mouton ceased employment in March 2006. Remuneration disclosed is effective to that date.

(22) Includes any living away from home allowances. Three executives (2006: six executives) salary sacrificed minor amounts during the year for car parking – this is in addition to the above footnotes.

(23) The short term incentives (STI) cash bonus related to performance during the year. In the prior year J Bonin, P DeRosse, D Hatton, B Johnson, M Knapman, G Duursma, K Mouton were paid a discretionary bonus of \$7 540. J Esplin received a payment of \$3 520. While this bonus was based on the performance, it was not measured by reference to pre-determined performance factors.

(24) Some STI bonus amounts may have been accrued at year end and paid subsequent to year end.

(25) The company pays the insurance premium in respect of a directors' and officers' liability insurance policy. The average premium per person has been included in these tables.

(26) Non monetary benefits includes health insurance, car parking, salary continuance insurance and FBT payable by Keycorp on each of these items. These amounts also include D&O insurance paid by Keycorp in respect of each officer.

(27) The fair value of options is calculated at the date of grant using a Black-Scholes Merton "up and in" call barrier pricing model, which takes account of factors such as the option exercise price, the current level and volatility of the underlying share price and the time of maturity of the option. The value of such options is being amortised and disclosed as part of director and executive remuneration on a straight line basis over the option vesting period. In valuing the options, market conditions have been taken into account.

FAIR VALUE OF OPTIONS – FACTORS AND ASSUMPTIONS – AUDITED

The following factors and assumptions were used in determining the fair value of options on grant date.

| Grant date | | Expiry date | Fair value per option | Exercise price ⁽ⁱ⁾ | Prices of shares on grant date | Estimated volatility | Risk free interest rate | Dividend yield |
|-------------|-----------|-------------|-----------------------|-------------------------------|--------------------------------|----------------------|-------------------------|----------------|
| 31 Oct 2003 | Tranche 1 | 31 Oct 2008 | \$0.35 | \$0.95 | \$1.33 | 41% | 5.67% | 0% |
| 31 Oct 2003 | Tranche 2 | 31 Oct 2008 | \$0.44 | \$0.95 | \$1.33 | 41% | 5.67% | 0% |
| 1 Jul 2004 | Tranche 1 | 1 Jul 2009 | \$0.42 | \$0.98 | \$1.48 | 43% | 5.68% | 2% |
| 1 Jul 2004 | Tranche 2 | 1 Jul 2009 | \$0.49 | \$0.98 | \$1.48 | 43% | 5.68% | 2% |
| 15 Jul 2004 | Tranche 1 | 15 Jul 2009 | \$0.36 | \$1.05 | \$1.46 | 42% | 5.53% | 2% |
| 15 Jul 2004 | Tranche 2 | 15 Jul 2009 | \$0.44 | \$1.05 | \$1.46 | 42% | 5.53% | 2% |
| 23 Sep 2004 | Tranche 1 | 23 Sep 2009 | \$0.53 | \$1.39 | \$1.96 | 40% | 5.22% | 2% |
| 23 Sep 2004 | Tranche 2 | 23 Sep 2009 | \$0.62 | \$1.39 | \$1.96 | 40% | 5.22% | 2% |
| 27 May 2005 | Tranche 1 | 1 Mar 2010 | \$0.31 | \$1.31 | \$1.70 | 35% | 5.21% | 2% |
| 27 May 2005 | Tranche 2 | 1 Mar 2010 | \$0.38 | \$1.31 | \$1.70 | 35% | 5.21% | 2% |
| 15 Jan 2006 | Tranche 1 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 15 Jan 2006 | Tranche 2 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 15 Jan 2006 | Tranche 3 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 26 Oct 2006 | Tranche 1 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |
| 26 Oct 2006 | Tranche 2 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |
| 26 Oct 2006 | Tranche 3 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |

(i) The payment of a capital return of 41 cents per share in September 2005 resulted in a reduction of the option exercise price by 41 cents for options outstanding at the date of the capital return, the option hurdle price is a function of the percentage increase in the S&P/ASX 300 index and option exercise price.

FAIR VALUE OF SHARES – FACTORS AND ASSUMPTIONS – AUDITED

Fair value as defined by AASB 2 (Share Based Payments) is amount for which an equity instrument granted could be exchanged between knowledgeable, willing parties in an arm's length transaction.

No deferred shares were allocated during the current year.

The following factors and assumptions were used in determining the fair value of the deferred shares on allocation date in the prior year:

| Executive | Share allocation | Fair value \$ |
|-----------|------------------|---------------|
| R Cusson | 15 000 | 1.47 |
| D Hatton | 10 000 | 1.47 |
| J Smerek | 10 000 | 1.47 |

The fair value of deferred shares is based on the market value of Keycorp shares on the allocation date. The fair value is expensed over the vesting period of the shares.

DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued

ANALYSIS OF BONUSES INCLUDED IN REMUNERATION – UNAUDITED

Details of the vesting profile of the short term incentive cash bonuses awarded as remuneration to the executive director of the company and specific executives are set out below:

| Key Management Personnel | Included in Remuneration \$ ⁽ⁱ⁾ | Incentives bonus % vested in the year | % Forfeited in year ⁽ⁱⁱ⁾ |
|--------------------------|--------------------------------------------|---------------------------------------|-------------------------------------|
| J. Bonin | \$128 516 | 126% | 0% |
| R. Cusson | \$97 553 | 77% | 23% |
| R. Ganeson | \$32 489 | 46% | 54% |
| P. Herington | — | — | — |
| M. Knapman | — | — | — |
| M. Ritter | \$25 618 | 102% | 0% |
| J. Stevens | \$33 968 | 85% | 15% |

(i) Amounts included in remuneration for the financial year represent the amount accrued in the financial year based on achievement of personal goals and satisfaction of specified performance criteria. Any bonus paid is at the absolute discretion of the Chief Executive Officer (CEO) (or the Remuneration and Nomination Committee, in the case of the CEO), who adjudicates as to whether performance criteria have been met. No amounts "vest" in future financial years in respect of the short-term incentive bonus schemes for the 2007 financial year.

(ii) The amounts forfeited are due to the performance or service criteria not being met in relation to the current financial year.

OPTIONS AND RIGHTS OVER EQUITY INSTRUMENTS GRANTED AS COMPENSATION – AUDITED

Details of options over ordinary shares in the company that were granted as compensation to each key management person during the reporting period and details on options that vested during the reporting period are as follows:

| | | Held at beginning of financial year | Granted as remuneration | Exercised | Lapsed | Held at end of financial year | Vested during year | Vested and Exercisable at 30 June 2007 |
|------------------------------------|------|-------------------------------------|-------------------------|-----------|---------|-------------------------------|--------------------|----------------------------------------|
| Executive Director | | | | | | | | |
| Current | | | | | | | | |
| K. Carr | 2007 | — | — ^(v) | — | — | — | — | — |
| Former | | | | | | | | |
| B. Thompson | 2007 | 200 000 | 200 000 ^(vi) | — | 400 000 | — | — | — |
| | 2006 | — | 200 000 ^(vi) | — | — | 200 000 | — | — |
| Executives | | | | | | | | |
| J. Bonin | 2007 | 151 000 | 120 000 ⁽ⁱ⁾ | — | — | 271 000 | 12 500 | 51 000 |
| | 2006 | 51 000 | 100 000 ⁽ⁱ⁾ | — | — | 151 000 | 25 500 | 38 500 |
| R. Cusson | 2007 | 7 000 | 120 000 ⁽ⁱ⁾ | — | — | 127 000 | 7 000 | 7 000 |
| | 2006 | 44 000 | — | 37 000 | — | 7 000 | 22 000 | — |
| R. Ganeson | 2007 | 150 000 | 120 000 | — | — | 270 000 | 25 000 | 25 000 |
| | 2006 | 50 000 | 100 000 ⁽ⁱ⁾ | — | — | 150 000 | — | — |
| M. Knapman | 2007 | 186 000 | — | — | 50 000 | 136 000 | 10 000 | 36 000 |
| | 2006 | 86 000 | 100 000 ⁽ⁱ⁾ | — | — | 186 000 | 18 000 | 76 000 |
| J. Stevens | 2007 | — | 140 000 | — | — | 140 000 | — | — |
| A. Bradford (resigned Jan 2005) | 2007 | — | — | — | — | — | — | — |
| | 2006 | 28 400 | — | — | 10 000 | 18 400 | 9 200 | 14 400 |
| G. Duursma (resigned Feb 2006) | 2007 | — | — | — | — | — | — | — |
| | 2006 | 50 000 | — | — | — | 50 000 | 25 000 | 25 000 |
| T. Fletcher (resigned Jan 2006) | 2007 | — | — | — | — | — | — | — |
| | 2006 | 54 000 | — | 37 000 | 17 000 | — | — | — |
| K. Mouton (resigned Mar 2006) | 2007 | — | — | — | — | — | — | — |
| | 2006 | 50 000 | — | — | 50 000 | — | — | — |
| J. Esplin | 2006 | 8 000 | 30 000 ⁽ⁱⁱ⁾ | — | — | 38 000 | 4 000 | 4 000 |
| D. Hatton | 2006 | 48 000 | — ⁽ⁱⁱⁱ⁾ | — | 10 000 | 38 000 | 19 000 | 31 000 |
| B. Johnson (resigned Feb 2007) | 2007 | 126 000 | 90 000 ⁽ⁱ⁾ | — | 216 000 | — | — | — |
| | 2006 | 40 000 | 100 000 ⁽ⁱ⁾ | — | 14 000 | 126 000 | 13 000 | 19 000 |
| P. DeRosse (resigned June 2007) | 2007 | 147 000 | — | — | 147 000 | — | — | — |
| | 2006 | 84 000 | 100 000 ⁽ⁱ⁾ | 37 000 | — | 147 000 | 22 000 | 40 000 |
| J. Smerek | 2006 | 20 000 | — | — | — | 20 000 | 10 000 | 15 000 |

- (i) Options granted on 26 October 2006 have an expiry date of 26 October 2011. The options were granted in three equal tranches and have exercise dates of 26 October 2008, 26 October 2009 and 26 October 2010 with an exercise price of \$0.80 and a fair value of \$0.36.
- (ii) Options granted on 15 January 2006 have an expiry date of 15 January 2011. The options were granted in three equal tranches and have exercise dates of 15 January 2008, 15 January 2009 and 15 January 2010 with an exercise price of \$1.48 and a fair value of \$0.58.
- (iii) Ceased to be key management personnel on 30 June 2006.
- (iv) Options granted to the former Chief Executive Officer were approved by shareholders at the 2005 Annual General Meeting. 200 000 Options were granted on 26 October 2006 in three equal tranches and have exercise dates of 26 October 2008, 26 October 2009 and 26 October 2010 with an exercise price of \$0.80 and a fair value of \$0.36. In the prior year 200 000 options were granted in three equal tranches and have exercise dates of 15 January 2008, 15 January 2009 and 15 January 2010 with an exercise price of \$1.48 and a fair value of \$0.58.
- (v) 1 220 000 options granted subject to shareholder approval at 2007 Annual General Meeting.

The options were provided at no cost to the recipients. No options have been granted since the end of the financial year.

The option hurdle prices are adjusted to reflect the terms of the issued options to certain key management personnel and the effects of such adjustments are reflected in the option exercise.

The options granted are exercisable between one and three years from grant date providing performance hurdles are attained. The hurdles are twofold and require continuous employment by the employee during the vesting period and for the share price of Keycorp Limited to attain a pre-defined market price for a pre-determined period during the vesting period (and such period varies between each grant).

All options expire on the earlier of their expiry date or termination of the individual's employment. In certain circumstances, at the discretion of management, employees included in an involuntary redundancy program are eligible to retain and exercise share options in accordance with the terms and conditions of the particular option issue.

For options granted to key management personnel in the current year, the earliest exercise is 26 October 2008. No options were exercised during the year.

EXERCISE OF OPTIONS GRANTED AS COMPENSATION – AUDITED

There were no shares issued on exercise of options previously granted as compensation during the reporting period.

During the prior reporting period, the following shares were issued to key management personnel on the exercise of options previously granted as compensation:

| Executive | Number of Shares | Amount paid \$/share |
|-------------|------------------|----------------------|
| R. Cusson | 30 000 | \$1.24 |
| | 7 000 | \$1.36 |
| P. DeRosse | 30 000 | \$1.24 |
| | 7 000 | \$1.36 |
| T. Fletcher | 30 000 | \$1.24 |
| | 7 000 | \$1.36 |

ANALYSIS OF OPTIONS AND RIGHTS OVER EQUITY INSTRUMENTS GRANTED AS COMPENSATION – UNAUDITED

Details of the vesting profile of the options granted as remuneration to each non-executive director of the company (nil), the executive director and each executive (key management personnel) are set out below:

| | Options granted | | Financial year in | | | Value yet to vest | |
|----------------------------------|-----------------|----------|-------------------|---------------------|-------------------|-----------------------|-----------------------|
| | Number | Date | % Vested in year | % Forfeited in year | which grant vests | MIN \$ ⁽ⁱ⁾ | MAX \$ ⁽ⁱ⁾ |
| Executive Director | | | | | | | |
| K. Carr ⁽ⁱ⁾ | — | — | — | — | — | — | — |
| Former Executive Director | | | | | | | |
| B. Thompson | 66 666 | 09/03/06 | 0% | 100% | | | |
| | 66 666 | 09/03/06 | 0% | 100% | | | |
| | 66 667 | 09/03/06 | 0% | 100% | | | |
| | 66 666 | 26/10/06 | 0% | 100% | | | |
| | 66 666 | 26/10/06 | 0% | 100% | | | |
| | 66 667 | 26/10/06 | 0% | 100% | | | |
| Executives | | | | | | | |
| J. Bonin | 12 500 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/08 | Nil | 12 600 |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/09 | Nil | 13 737 |
| | 33 334 | 09/03/06 | 0% | 0% | 30/06/10 | Nil | 17 300 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/09 | Nil | 11 935 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/10 | Nil | 14 195 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/11 | Nil | 16 061 |
| R. Cusson | 7 000 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/09 | Nil | 11 935 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/10 | Nil | 14 195 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/11 | Nil | 16 061 |
| R. Ganeson | 25 000 | 27/05/05 | 100% | 0% | 30/06/07 | — | — |
| | 25 000 | 27/05/05 | 0% | 0% | 30/06/08 | Nil | 9 425 |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/08 | Nil | 12 600 |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/09 | Nil | 13 737 |
| | 33 334 | 09/03/06 | 0% | 0% | 30/06/10 | Nil | 17 300 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/09 | Nil | 11 935 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/10 | Nil | 14 195 |
| | 40 000 | 26/10/06 | 0% | 0% | 30/06/11 | Nil | 16 061 |
| P. Herington | — | — | — | — | — | — | — |
| M. Knapman | 10 000 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/08 | Nil | 12 600 |
| | 33 333 | 09/03/06 | 0% | 0% | 30/06/09 | Nil | 13 737 |
| | 33 334 | 09/03/06 | 0% | 0% | 30/06/10 | Nil | 17 300 |
| M. Ritter | — | — | — | — | — | — | — |
| J. Stevens | 46 666 | 26/10/06 | 0% | 0% | 30/06/09 | Nil | 13 925 |
| | 46 666 | 26/10/06 | 0% | 0% | 30/06/10 | Nil | 16 560 |
| | 46 668 | 26/10/06 | 0% | 0% | 30/06/11 | Nil | 18 738 |

(i) Granted 1 220 000 options which are subject to shareholder approval at 2007 Annual General Meeting

DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

REMUNERATION REPORT continued**ANALYSIS OF OPTIONS AND RIGHTS OVER EQUITY INSTRUMENTS GRANTED AS COMPENSATION – UNAUDITED continued**

| | Options granted | | | | | Value yet to vest | |
|------------------------------------|-----------------|----------|------------------|---------------------|-------------------------------------|-----------------------|-------------------------|
| | Number | Date | % Vested in year | % Forfeited in year | Financial year in which grant vests | MIN \$ ⁽ⁱ⁾ | MAX \$ ⁽ⁱⁱⁱ⁾ |
| Former | | | | | | | |
| A. Bradford (resigned Jan 2005) | 4 000 | 31/10/03 | 100% | 0% | | | |
| G. Duursma (resigned Feb 2006) | 25 000 | 01/07/04 | 100% | 0% | | | |
| | 25 000 | 01/07/04 | 100% | 0% | | | |
| T. Fletcher (resigned Jan 2006) | 7 000 | 31/10/03 | 100% | 100% | | | |
| K. Mouton (resigned Mar 2006) | 25 000 | 15/07/04 | 0% | 100% | | | |
| | 25 000 | 15/07/04 | 0% | 100% | | | |
| P. DeRosse (resigned June 2007) | 7 000 | 31/10/03 | 0% | 100% | | | |
| | 33 333 | 09/03/06 | 0% | 100% | | | |
| | 33 333 | 09/03/06 | 0% | 100% | | | |
| | 33 334 | 09/03/06 | 0% | 100% | | | |
| J. Esplin | 4 000 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |
| | 10 000 | 09/03/06 | 0% | 0% | 30/06/08 | Nil | 3 780 |
| | 10 000 | 09/03/06 | 0% | 0% | 30/06/09 | Nil | 4 121 |
| | 10 000 | 09/03/06 | 0% | 0% | 30/06/10 | Nil | 5 190 |
| D. Hatton | 7 000 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |
| B. Johnson (resigned Feb 2007) | 7 000 | 31/10/03 | 0% | 100% | | | |
| | 33 333 | 09/03/06 | 0% | 100% | | | |
| | 33 333 | 09/03/06 | 0% | 100% | | | |
| | 33 334 | 09/03/06 | 0% | 100% | | | |
| J. Smerek | 5 000 | 31/10/03 | 100% | 0% | 30/06/07 | — | — |

(i) The percentage forfeited in the year represents the reduction from the maximum number of options available to vest due to the highest performance criteria not being achieved.

(ii) The minimum value of options yet to vest is \$nil as the performance criteria may not be met and consequently the option may not vest.

(iii) The maximum value of options yet to vest is not determinable as it depends on the market price of shares of the company on the Australian Stock Exchange at the date the option is exercised. The maximum values presented above are based on the total value of the options over their life calculated at grant date using a Black-Scholes Merton "up and in" call barrier pricing model.

ANALYSIS OF MOVEMENTS IN OPTIONS — UNAUDITED

The movement during the reporting period, by total number, of options over ordinary shares in Keycorp Limited held by key management personnel is detailed below:

| | Year | Granted in year \$ ⁽ⁱ⁾ | Exercised in year \$ ⁽ⁱⁱ⁾ | Lapsed in year \$ ⁽ⁱⁱⁱ⁾ | Total option value in year \$ |
|------------------------------------|------|-----------------------------------|--------------------------------------|------------------------------------|-------------------------------|
| Executive Director | | | | | |
| K. Carr ^(iv) | 2007 | — | — | — | — |
| Former | | | | | |
| B. Thompson | 2007 | 72 679 | — | (189 519) | (116 840) |
| | 2006 | 29 091 | — | — | 29 091 |
| EXECUTIVES | | | | | |
| J. Bonin | 2007 | 43 607 | — | — | 43 607 |
| | 2006 | 14 546 | — | — | 14 546 |
| R. Cusson | 2007 | 43 607 | — | — | 43 607 |
| | 2006 | — | 31 550 | — | (31 550) |
| R. Ganeson | 2007 | 43 607 | — | — | 43 607 |
| | 2006 | 14 546 | — | — | 14 546 |
| P. Herington | 2007 | — | — | — | — |
| M. Knapman | 2007 | — | — | (50 000) | (50 000) |
| | 2006 | 14 546 | — | — | 14 546 |
| M. Ritter | 2007 | — | — | — | — |
| J. Stevens | 2007 | 50 875 | — | — | 50 875 |
| A. Bradford (resigned Jan 2005) | 2007 | — | — | — | — |
| | 2006 | — | — | (81 500) | (81 500) |
| G. Duursma (resigned Feb 2006) | 2007 | — | — | — | — |
| | 2006 | — | — | — | — |
| T. Fletcher (resigned Jan 2006) | 2007 | — | — | — | — |
| | 2006 | — | 31 550 | (84 587) | (53 037) |
| K. Mouton (resigned Mar 2006) | 2007 | — | — | — | — |
| | 2006 | — | — | — | — |
| P. DeRosse (resigned June 2007) | 2007 | — | — | (60 964) | (60 964) |
| | 2006 | 14 546 | 31 550 | — | (17 004) |
| J. Esplin | 2007 | — | — | — | — |
| | 2006 | 4 364 | — | — | 4 364 |
| D. Hatton | 2007 | — | — | — | — |
| | 2006 | — | — | (81 500) | (81 500) |
| B. Johnson (resigned Feb 2007) | 2007 | 32 705 | — | (108 213) | (75 508) |
| | 2006 | 14 546 | — | (114 100) | (99 554) |
| J. Smerek (appointed Jan 2006) | 2007 | — | — | — | — |
| | 2006 | — | — | — | — |

(i) The value of options granted in the year is the fair value of the options calculated at grant date using a Black-Scholes Merton "up and in" call barrier pricing model. The total value of the options granted is included in the table above. This amount is allocated to remuneration over the vesting period.

(ii) The value of options exercised during the year is calculated as the market price of shares of the company on the Australian Stock Exchange as at close of trading on the date the options were exercised after deducting the price paid to exercise the option.

(iii) The value of the options lapsed during the year is calculated as the market price of the shares of the company on the Australian Stock Exchange as at the close of trading on the date the options lapsed, after deducting the price that would have been paid to exercise the option. Where the exercise price of the option. Where the exercise price of the option as at the date of lapse is in excess of the market price of the shares (i.e. the option is "out-of-the-money"), the value of the options lapsed is reported as nil.

(iv) Granted 1 220 000 options which are subject to shareholder approval at 2007 Annual General Meeting.

DIRECTORS' REPORT

FOR THE YEAR ENDED 30 JUNE 2007

LEAD AUDITOR'S INDEPENDENCE DECLARATION

The lead auditor's independence declaration (made under section 307C of the *Corporations Act 2001*) is set out on page 23 and forms part of this report.

NO OFFICERS ARE FORMER AUDITORS

No officer of the Keycorp group has been a partner of an audit firm or a director of an audit company that is or was an auditor of any entity in the group during the year ended 30 June 2007.

ROUNDING OFF

The amounts contained in this directors' report and in the financial report have been rounded to the nearest thousand dollars (where rounding is applicable) under the option available to the company under ASIC Class Order 98/100 dated July 1998. The company is an entity to which the Class Order applies.

Signed in accordance with a resolution of the directors.

A handwritten signature in black ink, appearing to read 'K.M. Carr', written in a cursive style.

K.M. Carr
Director
Sydney, 30 August 2007



Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To: the directors of Keycorp Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

A handwritten signature in black ink, appearing to read 'J Wigglesworth'.

KPMG

A large, stylized handwritten signature in black ink, extending across the page.

John Wigglesworth
Partner

Sydney, 30 August 2007

INCOME STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2007

| | Note | Consolidated | | Company | |
|--------------------------------------------------------------------------------------------------------------------------------|-------|---------------|---------------|---------------|---------------------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| Revenue | 5 | 95 578 | 95 211 | 46 875 | 69 367 |
| Cost of sales | | (65 981) | (57 731) | (32 716) | (43 775) |
| Gross profit | | 29 597 | 37 480 | 14 159 | 25 592 |
| Other income | 6 | 2 608 | — | 1 150 | — |
| Sales and marketing expenses | | (12 093) | (10 815) | (8 285) | (7 506) |
| Administration expenses | 7(a) | (16 711) | (10 733) | (10 043) | (8 785) |
| Manufacturing operations expenses | | (229) | (762) | (34) | (411) |
| Research and development expenses | | (6 183) | (8 865) | (4 474) | (6 751) |
| Rectification costs | 7(b) | (4 216) | — | (758) | — |
| Settlement of contractual dispute | 7(c) | — | (3 220) | — | (3 220) |
| Other expenses | 7(d) | (6 908) | (3 685) | (4 416) | (455) |
| Results from operating activities | | (14 135) | (600) | (12 701) | (1 536) |
| Financial income | 8 | 817 | 1 264 | 778 | 1 293 |
| Financial expenses | 8 | (1 270) | (261) | (1 262) | (15) |
| Net financing (expenses)/income | | (453) | 1 003 | (484) | 1 278 |
| Share of losses of associates | 18 | — | (108) | — | — |
| (Loss)/profit before income tax | | (14 588) | 295 | (13 185) | (258) |
| Income tax benefit/(expense) | 10 | 2 620 | (1 115) | 3 032 | 990 |
| (Loss)/profit after tax but before profit and loss of discontinued operation and loss on sale of discontinued operation | | (11 968) | (820) | (10 153) | 732 |
| Profit/(loss) of discontinued operation and (loss)/gain on sale of discontinued operation, net of tax | 11(c) | 451 | (2 067) | 451 | 52 933 |
| (Loss)/profit for the year attributable to equity holders of the parent entity | | (11 517) | (2 887) | (9 702) | 53 665 |
| Earnings per share for (loss)/profit attributable to the ordinary equity holders of the company | | | | | |
| Basic (loss) per share from continuing operations | 33 | \$(0.1457) | \$(0.010) | | |
| Diluted (loss) per share from continuing operations | 33 | \$(0.1457) | \$(0.010) | | |

The notes on pages 28 to 70 are an integral part of these consolidated financial statements.

STATEMENTS OF RECOGNISED INCOME AND EXPENSE

FOR THE YEAR ENDED 30 JUNE 2007

| | Note | Consolidated | | Company | |
|----------------------------------------------------------------------|---------------|---------------|---------------|---------------|---------------------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| Foreign currency translation differences for foreign operations | 30(a) | 263 | (311) | — | — |
| Income and expense recognised directly in equity | | 263 | (311) | — | — |
| (Loss)/profit for the period | | (11 517) | (2 887) | (9 702) | 53 665 |
| Total recognised income and expense for the period | | (11 254) | (3 198) | (9 702) | 53 665 |
| Impact of change in accounting policy on retained earnings at 1 July | 3(s)(i) 30(b) | — | — | (1 707) | — |

Other movements in equity arising from transactions with owners as owners are set out in note 30.

The amounts recognised directly in equity are disclosed net of tax.

The notes on pages 28 to 70 are an integral part of these consolidated financial statements.

BALANCE SHEETS

FOR THE YEAR ENDED 30 JUNE 2007

| | Note | Consolidated | | Company | |
|---------------------------------------------------|-------|---------------|---------------|---------------|---------------------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| Assets | | | | | |
| Cash and cash equivalents | 34(a) | 2 346 | 15 846 | 809 | 15 056 |
| Trade and other receivables | 14 | 17 816 | 13 285 | 7 665 | 9 076 |
| Inventories | 15 | 6 257 | 5 748 | 4 293 | 2 923 |
| Net investment in finance lease | 16 | 50 | — | 50 | — |
| Other current assets | 17 | 4 426 | 777 | 4 024 | 738 |
| Total current assets | | 30 895 | 35 656 | 16 841 | 27 793 |
| Receivables | 14 | 175 | — | 47 553 | 40 245 |
| Net investment in finance lease | 16 | 305 | — | 305 | — |
| Investments accounted for using the equity method | 18 | — | 114 | — | — |
| Investments | 19 | 8 906 | 8 847 | 10 401 | 10 564 |
| Property, plant and equipment | 20 | 7 363 | 2 893 | 3 952 | 2 007 |
| Deferred tax assets | 21 | 7 627 | 4 558 | 6 343 | 3 104 |
| Intangible assets | 22 | 11 494 | 10 425 | 6 908 | 5 515 |
| Total non-current assets | | 35 870 | 26 837 | 75 462 | 61 435 |
| Total assets | | 66 765 | 62 493 | 92 303 | 89 228 |
| Liabilities | | | | | |
| Trade and other payables | 23 | 14 428 | 13 761 | 26 914 | 26 685 |
| Interest bearing loans and borrowings | 24 | 12 513 | — | 11 772 | — |
| Employee benefits | 25 | 4 029 | 2 781 | 2 265 | 2 579 |
| Provisions | 26 | 3 889 | 5 753 | 3 175 | 5 292 |
| Income tax payable | 27 | 2 007 | 234 | 2 007 | 234 |
| Other current liabilities | 28 | 801 | 2 096 | 402 | 311 |
| Total current liabilities | | 37 667 | 24 625 | 46 535 | 35 101 |
| Deferred tax liability | 21 | 703 | — | — | — |
| Interest bearing loans and borrowings | 24 | 1 982 | — | 1 339 | — |
| Employee benefits | 25 | 203 | 473 | 203 | 402 |
| Provisions | 26 | 268 | 402 | 268 | 268 |
| Total non-current liabilities | | 3 156 | 875 | 1 810 | 670 |
| Total liabilities | | 40 823 | 25 500 | 48 345 | 35 771 |
| Net assets | | 25 942 | 36 993 | 43 958 | 53 457 |
| Equity | | | | | |
| Issued capital | 29 | 61 105 | 61 105 | 61 105 | 61 105 |
| Reserves | 30(a) | (61) | (324) | — | — |
| Accumulated losses | 30(b) | (35 102) | (23 788) | (17 147) | (7 648) |
| Total equity | | 25 942 | 36 993 | 43 958 | 53 457 |

The notes on pages 28 to 70 are an integral part of these consolidated financial statements.

STATEMENTS OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 2007

| | Note | Consolidated | | Company | |
|------------------------------------------------------------------|-------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Cash flows from operating activities | | | | | |
| Cash receipts from customers | | 100 483 | 112 987 | 53 059 | 53 240 |
| Cash paid to suppliers and employees | | (110 907) | (102 951) | (60 252) | (72 604) |
| Cash generated from operations | | (10 424) | (10 036) | (7 193) | (19 364) |
| Net investment in finance leases | | (355) | — | (355) | — |
| Interest received | | 817 | 1 177 | 778 | 1 145 |
| Interest paid | | (747) | (361) | (527) | (318) |
| Income taxes paid | | 1 331 | (3 702) | 1 331 | (3 685) |
| Settlement of R&D syndicate claim | | (3 220) | — | (3 220) | — |
| Restructuring costs | | (2 628) | (691) | (1 026) | (787) |
| Net cash from operating activities | 34(b) | (15 226) | 6 459 | (10 212) | (23 009) |
| Cash flows from investing activities | | | | | |
| Payments for property, plant and equipment | | (3 140) | (927) | (2 926) | (769) |
| Development expenditure | | (3 805) | (2 677) | (3 805) | (2 677) |
| Proceeds from disposal of non-current assets | | 128 | 5 | 50 | 5 |
| Payments for investments | | — | (3 420) | (43) | (3 420) |
| Acquisition of mezzanine note | | (59) | (1 818) | (59) | (1 818) |
| Proceeds from disposal of controlled entity | | — | 55 000 | — | 55 000 |
| Proceeds from disposal of business | | — | 2 256 | — | 2 256 |
| Acquisition of OSG business, including related acquisition costs | 12(i) | (952) | — | — | — |
| Net cash from investing activities | | (7 828) | 48 419 | (6 783) | 48 577 |
| Cash flows from financing activities | | | | | |
| Proceeds from the issue of share capital | | — | 330 | — | 330 |
| Proceeds from borrowings – Bank term loan | | 11 500 | — | 11 500 | — |
| Balance deposited in Escrow pending tax appeal | | — | (4 565) | — | (4 565) |
| Borrowing repayments – government loan | | — | (2 393) | — | (2 393) |
| Borrowing repayments – other | | — | (7 763) | — | (7 763) |
| Finance lease liabilities – new leases in the year | | 1 611 | — | 1 611 | — |
| Finance lease liabilities – payments | | (611) | — | — | — |
| Advances to related parties | | — | — | (19 382) | (8 238) |
| Advances repaid by related parties | | — | — | 12 056 | 37 502 |
| Return of capital | | — | (33 553) | — | (33 553) |
| Security deposit | | (3 000) | — | (3 000) | — |
| Net cash from financing activities | | 9 500 | (47 944) | 2 785 | (18 680) |
| Net (decrease)/increase in cash and cash equivalents | | (13 554) | 6 934 | (14 210) | 6 888 |
| Cash and cash equivalents at 1 July | | 15 846 | 8 831 | 15 056 | 8 157 |
| Effect of exchange rate fluctuations on cash held | | 54 | 81 | (37) | 11 |
| Cash and cash equivalents at 30 June | 34(a) | 2 346 | 15 846 | 809 | 15 056 |

The notes on pages 28 to 70 are an integral part of these consolidated financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. REPORTING ENTITY

Keycorp Limited (the "Company") is a company domiciled in Australia. The consolidated financial statements of the Company as at and for the year ended 30 June 2007 comprise the Company and its subsidiaries (together referred to as the "Consolidated entity") and the Consolidated entity's interest in associates.

2. BASIS OF PREPARATION

(a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AASBs) (including Australian Accounting Interpretations) adopted by the Australian Accounting Standards Board (AASB) and the *Corporations Act 2001*. The consolidated financial report of the Consolidated entity also complies with the IFRSs and interpretations adopted by the International Accounting Standards Board. The Company's financial report does not comply with IFRSs as the Company has elected to apply the relief provided to parent entities by AASB 132 Financial Instruments: Presentation and Disclosure in respect of certain disclosure requirements.

When preparing these financial reports, the board has made an assessment of the company and the consolidated entity's ability to continue as a going concern. These financial reports have been prepared on a going concern basis. In assessing whether a going concern basis is appropriate, the board has taken into account all available information about the future, which is at least, but not limited to, twelve months from the date of this report. As the company and consolidated entity do not demonstrate an immediate history of trading profitably, the board has considered a wide range of factors relating to current and expected profitability and cashflow, the extension, subsequent to balance date, of the consolidated entity's financing facility to 30 September 2008, revised debt repayment schedules (including intercompany balances) and the capacity of certain subsidiaries to pay dividends to the company before satisfying itself that a going concern basis is appropriate.

The financial statements were approved by the Board of Directors on 30 August 2007.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for derivative financial instruments that are measured at fair value.

(c) Functional and presentation currency

These consolidated financial statements are presented in Australian dollars, which is the Company's functional currency and the functional currency of the majority of the Group.

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, all financial information presented in Australian dollars has been rounded to the nearest thousand unless otherwise stated.

(d) Use of estimates and judgements

The preparation of financial report requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in the following notes:

- Note 21 — Utilisation of tax losses;
- Note 22 — Intangible assets; and
- Note 35 — Provisions and contingencies

3. SIGNIFICANT ACCOUNTING POLICIES

Except as described in note 3(s)(i), the accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements, and have been applied consistently by all entities in the consolidated entity.

In the prior financial year the Consolidated entity adopted AASB 132 : *Financial Instruments: Disclosure and Presentation* and AASB 139: *Financial Instruments: Recognition Measurement* in accordance with the transitional rules of AASB 1: *First time Adoption of Australian Equivalents to International Financial Reporting Standards*. The impact on adoption was calculated and found not to be material. Accordingly, there was no adjustment to opening reserves at 1 July 2005.

Certain comparative amounts have been reclassified to conform with the current year's presentation (see note 20).

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the consolidated entity. Control exists when the consolidated entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Investments in subsidiaries are carried at their cost of acquisition in the Company's financial statements.

(ii) Associates

Associates are those entities in which the consolidated entity has significant influence, but not control, over the financial and operating policies. Associates are accounted for using the equity method. The consolidated financial statements include the consolidated entity's share of the income and expenses of associates after adjustments to align the accounting policies with those of the consolidated entity, from the date that significant influence commences until the date that significant influence ceases.

When the consolidated entity's share of losses exceeds its interest in an associate, the carrying amount of that interest is reduced to \$nil and the recognition of further losses is discontinued except to the extent that the consolidated entity has incurred legal or constructive obligations or made payments on behalf of the associate.

In the Company's financial statements, investments in associates are carried at cost, less impairment.

(iii) Transactions eliminated on consolidation

Intra-group balances, and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Unrealised gains arising from transactions with associates are eliminated to the extent of the consolidated entity's interest in the associate.

Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Gains and losses are recognised when the contributed assets are consumed or sold by the associates or, if not consumed or sold by the associate, when the consolidated entity's interest in such entities is disposed of.

(b) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to Australian dollars at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the transaction date.

Non monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Australian dollars at foreign exchange rates ruling at the dates the fair value was determined.

(ii) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to Australian dollars at foreign exchange rates ruling at the balance sheet date. The income and expenses of foreign operations are translated to Australian dollars at rates approximating the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences are recognised in the foreign currency translation reserve (FCTR). When a foreign operation is disposed of, in part or in full, the relevant amount in the FCTR is transferred to profit or loss.

(iii) Net investment in foreign operation

Exchange differences arising from the translation of the net investment in foreign operations, and of related hedges are recognised directly in the FCTR. They are released into the income statement upon disposal.

In respect of all foreign operations, any exchange differences that have arisen after 1 July 2004, the date of transition to AIFRS, are presented as a separate component of equity.

(c) Derivative Financial instruments

The consolidated entity uses derivative financial instruments to hedge its exposure to foreign exchange risks arising from operational activities. In accordance with its treasury policy, the consolidated entity does not hold or issue derivative financial instruments for trading purposes. These derivatives do not qualify for hedge accounting and accordingly are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are measured at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss.

The consolidated entity has not applied hedge accounting in the current period.

(d) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation (see below) and impairment losses (see accounting policy 3(j)).

Cost includes expenditures that are directly attributable to the acquisition of the asset. When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

(ii) Leased assets

Leases in terms of which the consolidated entity assumes substantially all of the risks and rewards of ownership are classified as finance leases.

(iii) Subsequent costs

The consolidated entity recognises in the carrying amount of an item of property, plant and equipment the costs of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied within the item will flow to the consolidated entity and the cost of the item can be measured reliably. The costs of day to day servicing of the property, plant and equipment are recognised in the income statement as incurred.

(iv) Depreciation

Depreciation is charged to the income statement on a straight line basis over the estimated useful lives of each part of an item of property, plant and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives.

The estimated useful lives for the current and comparative periods are as follows:

- plant and equipment — 3 to 6 years
- furniture and fittings — 5 to 8 years
- leasehold improvements — Lease term
- motor vehicles — 4 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

NOTES TO THE FINANCIAL STATEMENTS continued

3. SIGNIFICANT ACCOUNTING POLICIES continued

(e) Intangible assets

(i) Goodwill

Business combinations prior to 1 July 2004

Goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous GAAP. The classification and accounting treatment of business combinations that occurred prior to 1 July 2004 has not been reconsidered in preparing the consolidated entity's opening AIFRS balance sheet at 1 July 2004.

Business combinations since 1 July 2004

All business combinations are accounted for by applying the purchase method. Goodwill represents the excess of the cost of the acquisition over the consolidated entity's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess is negative (negative goodwill) it is recognised immediately in profit or loss.

Subsequent measurement

Goodwill is measured at cost less accumulated impairment losses. In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment.

(ii) Capitalised development expenditure

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the income statement as an expense when incurred.

Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised only if the product or process is technically and commercially feasible, the costs can be measured reliably, future economic benefits are probable and the consolidated entity has sufficient resources to complete development. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads. Other development expenditure is recognised in the income statement as an expense as incurred.

Capitalised development expenditure is stated at cost less accumulated amortisation (see 3(e)(v) below) and impairment losses (see accounting policy 3(j)).

(iii) Other intangible assets

Other intangible assets, including intellectual property, that are acquired by the consolidated entity, which have finite useful lives, are measured at cost less accumulated amortisation (see below) and accumulated impairment losses (see accounting policy 3(j)).

(iv) Capitalised software

Capitalised software is measured at cost less accumulated amortisation and accumulated impairment losses.

(v) Subsequent expenditure

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates.

All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in profit or loss when incurred.

(vi) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Goodwill and intangible assets with an indefinite useful life are systematically tested for impairment at each balance sheet date. Other intangible assets are amortised from the date they are available for use. The estimated useful lives in the current and comparative periods are as follows:

- capitalised development costs — 1 to 3 years
- intellectual property — 3 to 5 years
- Other intangible assets — for the term of the customer contracts (4 to 5 years)
- capitalised software — 3 to 5 years

(f) Non current assets held for sale and discontinued operations

Immediately before classification as held for sale, the measurement of the assets (and all assets and liabilities in a disposal group) is brought up to date in accordance with applicable accounting standards. Then, on initial classification as held for sale, non-current assets and disposal groups are recognised at the lower of carrying amount and fair value less costs to sell.

Impairment losses on initial classification as held for sale are included in profit or loss, even when there is a revaluation. The same applies to gains and losses on subsequent remeasurement.

A discontinued operation is a component of the consolidated entity's business that represents a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to resale.

Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier. A disposal group that is to be abandoned may also qualify.

(g) Trade and other receivables

Trade and other receivables are stated at their amortised cost less impairment losses (see accounting policy 3(j)).

(h) Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

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

- (i) raw materials — purchase costs assigned to individual items of inventory on the basis of weighted average cost.
- (ii) work in progress — cost of direct materials and labour.
- (iii) finished goods — purchase costs assigned to individual items of inventory on the basis of weighted average cost.

(i) Cash and cash equivalents

Cash and cash equivalents comprises cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the consolidated entity's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(j) Impairment

The carrying amounts of the consolidated entity's assets other than inventories and deferred tax assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash generating unit is the smallest identifiable asset group that generates cashflows that are largely independent from other assets and groups. Impairment losses are recognised in the income statement, unless the asset has previously been revalued, in which case the impairment loss is recognised as a reversal to the extent of that previous revaluation with any excess recognised through the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units (group of units) and then, to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

When a decline in the fair value of an available-for-sale financial asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity is recognised in the income statement even though the financial asset has not been derecognised. The amount of the cumulative loss that is recognised in the income statement is the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in the income statement.

(i) Calculation of recoverable amount

The recoverable amount of the consolidated entity's investments in held-to-maturity securities and receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e., the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted.

Impairment of receivables is not recognised until objective evidence is available that a loss event has occurred. Significant receivables are individually assessed for impairment. Impairment testing of significant receivables that are not assessed as impaired individually is performed by placing them into portfolios of significant receivables with similar risk profiles and undertaking a collective assessment of impairment. Non-significant receivables are not individually assessed. Instead, impairment testing is performed by placing non-significant receivables in portfolios of similar risk profiles, based on objective evidence from historical experience adjusted for any effects of conditions existing at each balance date.

The recoverable amount of other assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(ii) Reversal of impairment

Impairment losses, other than in respect of goodwill, are reversed when there is an indication that the impairment loss may no longer exist and there has been a change in the estimate used to determine the recoverable amount.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss in respect of a held-to-maturity security or receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

An impairment loss in respect of an investment in an equity instrument classified as available for sale is not reversed through profit or loss. If the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss shall be reversed, with the amount of the reversal recognised in profit or loss.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(k) Share capital

Ordinary share capital is recognised at the fair value of the consideration received by the company. Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction of the share proceeds received.

When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from total equity.

In the Company's financial statements, the transactions of the Company sponsored employee share plan trust are treated as being executed directly by the Company (as the trust acts as the Company's agent). Accordingly, shares held by the trust are recognised as treasury shares and deducted from equity.

Dividends are recognised as a liability in the period in which they are declared.

NOTES TO THE FINANCIAL STATEMENTS continued

3. SIGNIFICANT ACCOUNTING POLICIES continued

(l) Investments

Financial instruments held for trading are classified as current assets and are stated at fair value, with any resultant gain or loss recognised in the income statement.

Where the consolidated entity has the positive intent and ability to hold debt securities to maturity, they are stated at amortised cost less impairment losses.

Other financial investments are classified as being available for sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity, except for impairment losses, when these investments are derecognised, the cumulative gain or loss previously recognised in equity is recognised in profit or loss.

(m) Interest bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the profit and loss over the period of the borrowings on an effective interest basis.

(n) Employee benefits

(i) Wages, salaries, annual leave, sick leave and non-monetary benefits

Liabilities for employee benefits for wages, salaries, annual leave and sick leave that are expected to be settled within 12 months of the reporting date represent present obligations resulting from employees' services provided to reporting date, are calculated at undiscounted amounts based on remuneration wage and salary rates that the consolidated entity expects to pay as at reporting date including related on-costs, such as workers compensation insurance and payroll tax.

Non-accumulating non-monetary benefits, such as medical care, housing, cars and free or subsidised goods and services, are expensed based on the net marginal cost to the consolidated entity as the benefits are taken by the employees.

A provision is recognised for the amount expected to be paid under short term cash bonus or profit sharing plans if the consolidated entity has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Long-term service benefits

The consolidated entity's net obligation in respect of long-term service benefits is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates, and is discounted using the rates attached to the Commonwealth Government bonds at the balance sheet date which have maturity dates approximating to the terms of the consolidated entity's obligations.

(iii) Share based payment transactions

The share option programme allows consolidated entity employees to acquire shares of the Company. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using a Black-Scholes Merton "up and in" call barrier pricing model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is only due to share prices not achieving the threshold for vesting.

Employees and executives are entitled to shares under the Deferred Employee Share Plan ("DESP") and the Exempt Employee Share Plan ("EESP"). Any shares that the Company contributes under these plans are expensed over the service period. The Company will pay for the costs of administering the plans.

Offers under EESP may be considered on an annual basis. No future offers will be made under EESP without Board approval. The terms of future offers if any, may vary depending, amongst other things, on the profit performance of the Company from year to year.

(iv) Defined contribution superannuation plans

Obligations for contributions to defined contribution superannuation funds are recognised as an expense in the income statement when they are due.

(o) Provisions

A provision is recognised in the balance sheet when the consolidated entity has a present legal or constructive obligation to make a future sacrifice of economic benefits as a result of past transactions or other past events, it is probable that an outflow of 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 is material, provisions are determined by discounting the expected future cash flows required to settle the obligation at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

(i) Warranties

A provision for warranties is recognised for all products under warranty at the reporting date based on sales volume and past experience of the level and cost of repairs and returns.

(ii) Onerous contracts

A provision for onerous contracts is recognised when the expected benefits to be derived by the Consolidated entity from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Consolidated entity recognises any impairment loss on the assets associated with that contract.

(iii) Restructuring

A provision for restructuring is recognised when the consolidated entity has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating costs are not provided for.

(iv) Leasehold restoration

Provision is made for the estimated cost of restoring leasehold premises to their original condition where required by the operating lease agreement. The amount of the provision is capitalised and is depreciated over the term of the lease.

(p) Trade and other payables

Trade and other payables are stated at their amortised cost. Trade payables are non-interest bearing and are normally settled within agreed supplier payment terms.

(q) Revenue**(i) Goods sold and services rendered**

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue from services rendered is recognised in the income statement in proportion to the stage of completion of the transaction at the balance sheet date. The stage of completion is assessed by reference to the labour hours incurred to date as a percentage of total estimated hours for each contract. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the costs incurred or to be incurred cannot be measured reliably, there is a risk of return of goods or there is continuing management involvement with the goods.

Any revenue received for which goods have not been delivered or services have not been rendered is classified as 'income received in advance' in the balance sheet and is recognised as revenue in the income statement only when the goods have been delivered or the services are rendered.

(ii) Lease financing and service

Lease financing revenue is recognised as it accrues, based on the effective interest yield inherent in the underlying leasing contract. Lease service revenue is recognised on a straight line basis over the life of the leasing contract.

(iii) Licence income

Licence income is recognised when the significant risks and rewards of ownership in respect of the intellectual property has passed to the buyer which is normally the date the product is delivered to the customer.

(r) Expenses**(i) Operating lease payments**

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

(ii) Finance lease payments

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent lease payments are accounted for by revising the minimum lease payments over the remaining term of the lease when the lease adjustment is confirmed.

(iii) Net financing costs

Net financing costs comprise interest payable on borrowings calculated using the effective interest method, interest receivable on funds invested, banking fees and the amortisation of ancillary costs incurred in connection with the arrangement of borrowings, dividend income and foreign exchange gains and losses.

Interest income is recognised in the income statement as it accrues, using the effective interest method.

The interest expense component of finance lease payments is recognised in the income statement using the effective interest method. All borrowing costs are recognised in profit or loss using the effective interest method.

(s) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend is recognised.

NOTES TO THE FINANCIAL STATEMENTS continued

3. SIGNIFICANT ACCOUNTING POLICIES continued

(s) Income tax continued

(i) Tax consolidation

The Company is the head entity in a tax consolidated group comprising the Company and all of its Australian wholly owned subsidiaries.

The implementation of the tax consolidations system for the tax consolidated group was 1 July 2003.

The current and deferred tax amounts for the tax consolidated group are allocated among the entities in the group using a 'group allocation method' approach. Deferred tax assets and deferred tax liabilities are measured by reference to the carrying amount of the assets and liabilities in the Company's balance sheet and their tax values applying under tax consolidation.

Any current tax liabilities (or assets) and deferred tax assets arising from unused tax losses assumed by the head entity from the subsidiaries in the tax consolidated group are recognised in conjunction with any tax funding arrangement amounts (refer below). Any difference between these amounts is recognised by the Company as an equity contribution to or distribution from the subsidiary. Distributions firstly reduce the carrying amount of the investment in the subsidiary and are recognised as revenue.

The Company recognises deferred tax assets arising from unused tax losses of the tax-consolidated group only to the extent that it is probable that future taxable profits of the tax-consolidated group will be available against which the asset can be utilised. Any subsequent period adjustments to deferred tax assets arising from unused tax losses assumed from subsidiaries are recognised by the head entity only.

The members of the tax consolidated group have entered into a tax funding agreement which sets out the funding obligations of the members of the tax consolidated group in respect of tax amounts.

The tax funding arrangements require payments to/from the head entity equal to the current tax liability (asset) assumed by the head entity and any tax loss deferred tax asset assumed by the head entity. The members of the tax consolidated group have also entered into a valid Tax Sharing Agreement under the tax consolidation legislation which sets out the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations and the treatment of entities leaving the tax consolidated group.

No amounts have been recognised in the financial statements in respect of this agreement as payment of any amounts under the tax sharing agreement is considered remote.

Change in accounting policy

In the prior year the current and deferred tax amounts for the tax consolidated group were allocated among the entities in the group using a 'stand alone taxpayer approach'. As a result of an increased number of intercompany transactions the company has determined that the group allocation method provides more relevant and meaningful information.

In respect of the company, the impact of the change in accounting policy was to decrease investments in subsidiaries by \$1 707 000 at 1 July 2006, decrease income tax benefit by \$1 166 000 for the year ended 30 June 2006 and increase accumulated losses at 1 July 2005 by \$541 000. The change had no impact on the consolidated entity's net loss or earnings per share.

(t) Goods and services tax

Revenue, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the balance sheet.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

(u) Segment reporting

A segment is a distinguishable component of the Consolidated entity that is engaged either in providing related products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Consolidated entity's primary format for segment reporting is based on business segments.

(v) New standards and interpretations not yet adopted

The following standards, amendments to standards and interpretations have been identified as those which may impact the entity in the period of initial application. They are available for early adoption at 30 June 2007, but have not been applied in preparing this financial report:

- The AASB released Accounting Standard AASB 2007-4 *Amendments to Australian Accounting Standards arising from ED 151 and Other Amendments* in May 2007. AASB 2007-4 makes amendments to a number of Australian Accounting Standards to introduce various accounting policy options, delete various disclosures presently required, and to make a number of editorial amendments. AASB 2007-4 is applicable to annual reporting period beginning on or after 1 July 2007 and must therefore be applied by the Consolidated entity in its financial statements for the year ending 30 June 2008.

Whilst a large number of Accounting Standards are amended by AASB 2007-4, key accounting policy options introduced by AASB 2007-4 relate to:

- the measurement and presentation of government grants;
- the accounting for jointly controlled entities using the proportionate consolidation method; and
- the presentation of the cash flow statement.

At the date of preparation of this financial report, the directors of the company have not decided on which optional accounting treatments may be adopted on initial application of AASB 2007-4. Accordingly, the directors are continuing to evaluate the potential financial impact of AASB 2007-4 on the financial statements.

However in the Consolidated entity's financial statements for the year ended 30 June 2008, certain information may no longer be disclosed, or may be disclosed in an alternative manner, due to amendments made by AASB 2007-4 to the disclosure requirements of various Accounting Standards.

- *AASB 7 Financial Instruments: Disclosures* (August 2005) replaces the presentation requirements of financial instruments in AASB 132. AASB 7 is applicable for annual reporting periods beginning on or after 1 January 2007, and will require extensive additional disclosures with respect to the Consolidated entity's financial instruments and share capital.
- *AASB 2005-10 Amendments to Australian Accounting Standards* (September 2005) makes consequential amendments to *AASB 132 Financial Instruments: Disclosure and Presentation*, *AASB 101 Presentation of Financial Statements*, *AASB 114 Segment Reporting*, *AASB 117 Leases*, *AASB 133 Earnings Per Share*, *AASB 139 Financial Instruments: Recognition and Measurement*, *AASB 1 First time Adoption of*

Australian Equivalents to International Financial Reporting Standards, *AASB 4 Insurance Contracts*, *AASB 1023 General Insurance Contracts* and *AASB 1038 Life Insurance Contracts arising from the release of AASB 7*. AASB 2005-10 is applicable for annual reporting periods beginning on or after 1 January 2007 and is expected to only impact disclosures contained within the consolidated financial report.

- *AASB 8 Operating Segments* replaces the presentation requirements of segment reporting in *AASB 114 Segment Reporting*. AASB 8 is applicable for annual reporting periods beginning on or after 1 January 2009 and is not expected to have an impact on the financial results of the Company and the Consolidated entity as the standard is only concerned with disclosures.
- *AASB 2007-3 Amendments to Australian Accounting Standards* arising from AASB 8 makes amendments to *AASB 5 Non-current Assets Held for Sale and Discontinued Operations*, *AASB 6 Exploration for and Evaluation of Mineral Resources*, *AASB 102 Inventories*, *AASB 107 Cash Flow Statements*, *AASB 119 Employee Benefits*, *AASB 127 Consolidated and Separate Financial Statements*, *AASB 134 Interim Financial Reporting*, *AASB 136 Impairment Assets*, *AASB 1023 General Insurance Contracts* and *AASB 1038 Life Insurance Contracts*. AASB 2007-3 is applicable for annual reporting periods beginning on or after 1 January 2009 and must be adopted in conjunction with *AASB 8 Operating Segments*. This standard is only expected to impact disclosures contained within the financial report.
- *Interpretation 10 Interim Financial Reporting and Impairment* prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, an investment in an equity instrument or a financial

asset carried at cost. Interpretation 10 will become mandatory for the Consolidated entity's 2008 financial statements, and will apply to goodwill, investments in equity instruments, and financial assets carried at cost prospectively from the date that the Consolidated entity first applied the measurement criteria of AASB 136 and AASB 139 respectively (i.e., 1 July 2004 and 1 July 2005, respectively). The potential effect of the Interpretation on the Company's financial report has not yet been determined.

- *Interpretation 11 AASB 2 Share-based Payment — Consolidated entity and Treasury Share Transactions* addresses the classification of a share-based payment transaction (as equity or cash settled), in which equity instruments of the parent or another subsidiary are transferred, in the financial statements of the entity receiving the services. Interpretation 11 will become mandatory for the Consolidated entity's 2008 financial report. Interpretation 11 is not expected to have any impact on the consolidated financial report. The potential effect of the interpretation on the Company's financial report has not yet been determined.
- *AASB 2007-1 Amendments to Australian Accounting Standards* arising from AASB Interpretation II amends *AASB 2 Share-based Payments* to insert the transitional provisions of IFRS 2, previously contained in *AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards*. ASB 2007-1 is applicable for annual reporting periods beginning on or after 1 March 2007 and is not expected to have any impact on the consolidated financial report. The potential impact on the Company has not yet been determined.

NOTES TO THE FINANCIAL STATEMENTS continued

4. SEGMENT REPORTING

Segment information is presented in respect of the Consolidated entity's business and geographical segments. The primary format, business segments, is based on the Consolidated entity's management and internal reporting structure.

The consolidated entity generally values intersegment sales on a fully absorbed cost recovery basis. Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items mainly comprise interest, borrowing costs and corporate costs that cannot be reasonably allocated.

a) Business segments – Primary Segment

The consolidated entity's operations are organised and managed separately according to the nature of the products and services they provide, with each segment offering different products and serving different markets:

Secure transactions – responsible for the marketing and sales of transaction network solutions and secure e-commerce payment gateway services.

Payment solutions – responsible for the development, manufacture and sale of secure electronic payment terminals.

Smartcards – responsible for the design and sale of smartcards and secure smartcard operating systems for payments and identity markets.

Customer services – responsible for the service, installation and maintenance of payment terminals including EFTPOS terminal management services.

4. SEGMENT REPORTING continued

| | Secure transactions (discontinued) | | Payment Solutions | | Smartcards | | Services and other | | Corporate | | Sub total | | Less Secure transactions (Discontinued) | | Total from continuing operations | | |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|--------------|-------------------|----------------|---------------|---------------|--------------------|---------------|-----------------|-----------------|-----------------|----------------|-----------------------------------------|----------------|----------------------------------|----------------|------------|
| | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 | 2006* \$000 | 2007 \$000 |
| Revenue from external customers | | | | | | | | | | | | | | | | | |
| Total external revenues | — | 1 080 | 25 218 | 35 906 | 25 304 | 23 069 | 45 056 | 35 709 | — | — | 95 578 | 95 764 | — | 1 080 | 95 578 | 94 684 | |
| Unallocated revenue | — | — | — | — | — | — | — | — | — | 527 | — | 527 | — | — | — | 527 | |
| Total segment revenue | — | 1 080 | 25 218 | 35 906 | 25 304 | 23 069 | 45 056 | 35 709 | — | 527 | 95 578 | 96 291 | — | 1 080 | 95 578 | 95 211 | |
| Segment result | | | | | | | | | | | | | | | | | |
| Other unallocated costs | — | 491 | (5 776) | (3 819) | 1 340 | 2 251 | 1 275 | 11 190 | — | — | (3 161) | 10 113 | — | 491 | (3 161) | 9 622 | |
| Gain on acquisition of OSG | — | — | — | — | — | — | — | — | (12 148) | (7 002) | (12 148) | (7 002) | — | — | (12 148) | (7 002) | |
| R&D Syndicate settlement | — | — | — | — | — | — | 1 174 | — | — | — | 1 174 | — | — | — | 1 174 | — | |
| | — | — | — | — | — | — | — | — | (3 220) | (3 220) | — | (3 220) | — | — | — | (3 220) | |
| Results from operating activities | — | 491 | (5 776) | (3 819) | 1 340 | 2 251 | 2 449 | 11 190 | (12 148) | (10 222) | (14 135) | (109) | — | 491 | (14 135) | (600) | |
| Net financing (expense)/income | — | — | — | — | — | — | — | — | — | — | (453) | 1 003 | — | — | (453) | 1 003 | |
| Share of losses of associates | — | — | — | — | — | — | — | — | — | — | — | (108) | — | — | — | (108) | |
| (Loss)/profit before tax | — | — | — | — | — | — | — | — | — | — | (14 589) | 786 | — | 491 | (14 589) | 295 | |
| Tax benefit/(expense) | — | — | — | — | — | — | — | — | — | — | 2 620 | (1 262) | — | (147) | 2 620 | (1 115) | |
| Net loss on sale of discontinued operations (net of tax) | — | — | — | — | — | — | — | — | — | — | 451 | (2 411) | 451 | (2 411) | — | — | |
| Net (loss)/profit after tax | — | — | — | — | — | — | — | — | — | — | (11 517) | (2 887) | 451 | (2 067) | (11 968) | (820) | |
| * The 2006 comparative segment note information has been represented to conform with the current year presentation. A reconciliation to the prior year presentation format is set out below. | | | | | | | | | | | | | | | | | |
| Segment results as above | — | 491 | (5 776) | (3 819) | 1 340 | 2 251 | 1 275 | 11 190 | — | — | (3 161) | 10 113 | — | 491 | (3 161) | 9 622 | |
| Add back depreciation and amortisation | — | — | 2 053 | 3 161 | 901 | 299 | 1 252 | 986 | 1 159 | — | 5 365 | 4 446 | — | — | 5 365 | 4 446 | |
| Add back restructuring costs | — | — | 1 104 | 790 | 211 | — | 1 271 | — | 934 | — | 3 520 | 790 | — | — | 3 520 | 790 | |
| EBITDA | — | 491 | (2 619) | 132 | 2 452 | 2 550 | 3 798 | 12 176 | 2 093 | — | 5 724 | 15 349 | — | 491 | 5 724 | 14 858 | |
| Unallocated corporate costs | — | — | — | — | — | — | — | — | (12 149) | (6 708) | (12 149) | (6 708) | — | — | — | — | |
| Share of losses of associates | — | — | — | — | — | — | — | — | — | (108) | — | (108) | — | — | — | — | |
| Interest income | — | — | — | — | — | — | 811 | 970 | — | — | 811 | 970 | — | — | 811 | 970 | |
| Consolidated EBITDA from operations including interest income | — | 491 | (2 619) | 132 | 2 452 | 2 550 | 4 609 | 13 146 | (10 056) | (6 816) | (5 614) | 9 503 | | | | | |
| Segment assets | | | | | | | | | | | | | | | | | |
| Unallocated assets | — | — | 17 208 | 14 825 | 15 383 | 12 206 | 16 923 | 6 148 | — | — | 49 514 | 33 179 | — | — | 49 514 | 33 179 | |
| Total assets | — | — | 17 208 | 14 825 | 15 383 | 12 206 | 16 923 | 6 148 | 17 251 | 29 314 | 66 765 | 62 493 | | | | | |
| Segment liabilities | | | | | | | | | | | | | | | | | |
| Unallocated liabilities | — | — | 6 437 | 4 668 | 3 409 | 2 133 | 11 798 | 5 864 | — | — | 21 644 | 12 665 | — | — | 21 644 | 12 665 | |
| Total liabilities | — | — | 6 437 | 4 668 | 3 409 | 2 133 | 11 798 | 5 864 | 19 179 | 12 835 | 40 823 | 25 500 | | | | | |

Unallocated costs include corporate costs, facilities and IT communication costs which have not been charged to individual businesses.

NOTES TO THE FINANCIAL STATEMENTS continued

4. SEGMENT REPORTING continued

(b) Geographical segments – secondary segment

For geographical segments, segment revenue is based on the geographical location of the customers. Segment assets are based in the geographical location of the assets.

The consolidated entity's business segments operate geographically as follows:

Australia & New Zealand – Sales and service operations supporting Australia and New Zealand markets including sales made from these markets to geographical areas not separately identified below.

North America – Sales office supporting North American customers.

Asia – Sales to Asian customers from Australia.

Europe – UK sales office supporting European customers.

| | Australia & New Zealand | | North America | | Asia | | Europe | | Total | |
|---------------------------------------------------|-------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| External segment revenues by location by customer | 43 278 | 61 797 | 31 596 | 11 305 | 13 940 | 13 861 | 6 764 | 8 801 | 95 578 | 95 764 |
| Segment assets by location of assets | 66 106 | 58 471 | 454 | 3 832 | 205 | 114 | — | 76 | 66 765 | 62 493 |
| Capital expenditure | — | 3 717 | — | — | — | — | — | — | — | 3 717 |

| | Note | Consolidated | | Company | |
|--|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |

5. REVENUE

Revenue includes the following items

| | | | | |
|-------------------|---------------|---------------|---------------|---------------|
| Sales of goods | 50 522 | 58 975 | 46 736 | 69 367 |
| Customer Services | 45 056 | 35 709 | — | — |
| Other revenue | — | 527 | 139 | — |
| | 95 578 | 95 211 | 46 875 | 69 367 |

6. OTHER INCOME

| | | | | |
|-----------------------------------------------------------|--------------|----------|--------------|----------|
| Settlement of insurance claim relating to former director | 1 150 | — | 1 150 | — |
| Gain on acquisition of OSG business | 12(i) | 1 174 | — | — |
| Other | 284 | — | — | — |
| | 2 608 | — | 1 150 | — |

7. EXPENSES EXCLUDING NET FINANCE COST

Expenses, excluding net financing costs, include the following items:

a) Administrative expenses

Costs relating to OSG in the period since acquisition:

| | | | | |
|----------------------------------------|---------------|---------------|---------------|--------------|
| Salaries and associated employee costs | 1 651 | — | — | — |
| Legal and professional fees | 321 | — | — | — |
| Computing and communications | 679 | — | — | — |
| Facilities and premises | 2 032 | — | — | — |
| | 4 683 | | | |
| Operating expenses: | | | | |
| Salaries and associated employee costs | 5 074 | 4 395 | 4 152 | 3 543 |
| Legal and professional fees | 2 457 | 2 658 | 1 847 | 2 160 |
| Computing and communications | 2 086 | 1 643 | 1 691 | 1 230 |
| Facilities and premises | 1 807 | 1 815 | 1 369 | 1 317 |
| Other | 604 | 222 | 984 | 535 |
| | 16 711 | 10 733 | 10 043 | 8 785 |

| | Note | Consolidated | | Company | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 7. EXPENSES EXCLUDING NET FINANCE COST | | | | | |
| continued | | | | | |
| b) Rectification costs | | | | | |
| Costs associated with a proactive rectification program for a systems fault in a non Keycorp manufactured component | | | | | |
| | | 4 216 | — | 758 | — |
| c) Settlement of contractual dispute | | | | | |
| Settlement of dispute with respect to R&D syndicate | | | | | |
| | | — | 3 220 | — | 3 220 |
| d) Other expenses comprise: | | | | | |
| Restructuring costs | | | | | |
| | | 3 524 | 790 | 1 350 | 790 |
| Impairment of investment in associate | | | | | |
| | | 114 | 382 | 266 | 382 |
| Impairment of entity receivables | | | | | |
| | | — | — | 384 | (3 583) |
| Other expenses | | | | | |
| | | 445 | 769 | 1 620 | 2 065 |
| | | 4 083 | 1 941 | 3 620 | (346) |
| Amortisation and impairment of intangible assets: | | | | | |
| Intellectual property | | | | | |
| | | 307 | 260 | — | — |
| Other intangibles assets | | | | | |
| | | 341 | 223 | — | — |
| Capitalised software | | | | | |
| | | 345 | — | 99 | — |
| Total amortisation expense | | | | | |
| | | 993 | 483 | 99 | — |
| Depreciation of non current assets: | | | | | |
| Plant and equipment | | | | | |
| | | 1 073 | 875 | 558 | 549 |
| Motor vehicles | | | | | |
| | | 372 | — | — | — |
| Leasehold improvements | | | | | |
| | | 287 | 313 | 122 | 230 |
| Furniture and fittings | | | | | |
| | | 100 | 73 | 17 | 22 |
| Total depreciation expense | | | | | |
| | | 1 832 | 1 261 | 697 | 801 |
| Total depreciation and amortisation expense | | | | | |
| | | 2 825 | 1 744 | 796 | 801 |
| Total other expenses | | | | | |
| | | 6 908 | 3 685 | 4 416 | 455 |
| Amortisation and impairment of capitalised development costs of \$2 485 000 (2006: \$2 252 000) is included in research and development expenses and is all incurred by Keycorp Limited only. | | | | | |
| e) Operating lease rentals | | | | | |
| | | 2 779 | 2 039 | 1 148 | 998 |
| f) Bad & doubtful debts | | | | | |
| Trade debtors – other persons/bodies corporate | | | | | |
| | | 33 | 72 | 17 | 72 |
| Receivables from controlled entities | | | | | |
| | | — | — | 384 | (3 583) |
| g) Other provisions | | | | | |
| Employee entitlements | | | | | |
| | | 1 595 | 1 342 | 679 | 737 |
| Inventory obsolescence | | | | | |
| | | 1 176 | 1 834 | 497 | 1 229 |
| Warranty expense | | | | | |
| | | 1 046 | 1 027 | 891 | 906 |
| h) Other | | | | | |
| Net loss on disposal of non current assets | | | | | |
| | | 109 | — | 62 | — |

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|----------------------------------------------------------------------------|------|-----------------|----------------|-----------------|---------------------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| 8. NET FINANCING (EXPENSES)/INCOME | | | | | |
| Interest income | | 811 | 970 | 772 | 941 |
| Finance lease interest income | | 6 | — | 6 | — |
| Net gain on foreign exchange | | — | 294 | — | 352 |
| Financial income | | 817 | 1 264 | 778 | 1 293 |
| Interest expense | | 521 | 261 | 318 | 15 |
| Net loss on foreign exchange | | 360 | — | 572 | — |
| Finance lease interest expense | | 17 | — | — | — |
| Refinancing costs | | 372 | — | 372 | — |
| Financial expenses | | 1 270 | 261 | 1 262 | 15 |
| Net financing (expenses)/income | | (453) | 1 003 | (484) | 1 278 |
| 9. PERSONNEL EXPENSES | | | | | |
| Wages and salaries | | 25 889 | 15 283 | 7 720 | 9 155 |
| Other associated personnel expenses | | 3 480 | 2 025 | 1 060 | 1 554 |
| Contributions to defined contribution superannuation funds | | 2 213 | 1 631 | 1 597 | 1 017 |
| Increase/ (decrease) in liability for annual leave | | (90) | 278 | (84) | 82 |
| (Decrease)/increase liability for long-service leave | | (100) | (408) | 51 | (378) |
| Equity-settled share-based payment transactions | 25 | 203 | 266 | 203 | 266 |
| | | 31 595 | 19 075 | 10 547 | 11 696 |
| 10. INCOME TAX EXPENSE | | | | | |
| Recognised in the income statement | | | | | |
| Current tax expense | | | | | |
| Current year | | — | 1 220 | — | (1 316) |
| Adjustments for prior years | | 442 | (329) | 442 | (329) |
| | | 442 | 891 | 442 | (1 645) |
| Deferred tax expense | | | | | |
| Origination and reversal of temporary differences | | (384) | (72) | (552) | 802 |
| Tax losses (brought to account)/derecognised | | (2 678) | 443 | (2 922) | — |
| Total income tax expense in income statement | | (2 620) | 1 262 | (3 472) | (843) |
| Attributable to: | | | | | |
| Continuing operations | | (2 620) | 1 115 | (3 032) | (990) |
| Discontinuing operations | | — | 147 | — | 147 |
| | | (2 620) | 1 262 | (3 032) | (843) |
| Numerical reconciliation between tax expense and pre tax net profit | | | | | |
| (Loss)/profit before tax – continuing operations | | (14 588) | 295 | (13 185) | (258) |
| Profit/(loss) before tax – discontinuing operations | | 451 | (1 920) | 451 | 53 080 |
| (Loss)/profit before tax | | (14 137) | (1 695) | (12 734) | 52 822 |
| Income tax using the domestic corporation tax rate of 30% (2006: 30%) | | (4 241) | (488) | (3 820) | 15 847 |
| Forgiveness intercompany loan | | — | — | 115 | — |
| Effect of tax losses derecognised | | — | 443 | — | — |
| Loss (gain) on disposal of subsidiary | | — | 1 400 | — | (15 100) |
| Other non deductible expenditure | | 354 | 407 | 366 | 54 |
| Effect of tax losses not brought to account | | 960 | 512 | — | — |
| Non assessable profit on intragroup transactions | | — | — | — | (632) |
| Gain on disposal of business | | (135) | (683) | (135) | (683) |
| Under/(over) provided in prior years | | 442 | (329) | 442 | (329) |
| Income tax (benefit)/expense in pre-tax net profit | | (2 620) | 1 262 | (3 032) | (843) |

11. DISCONTINUED OPERATIONS

The consolidated entity sold its entire secure transactions business, a separate business segment, during the 2006 financial year. This segment comprised the Transaction Network Solutions Business and the Camtech e-commerce payment gateway service business.

a) Transactions Network Solutions business

On 28 June 2005, the Board announced the sale of Keycorp Solutions Limited, which owns the Transaction Network Solutions (TNS) business, to Telstra Corporation Limited for \$55 000 000. Of these proceeds \$4 565 000 was paid into an escrow account, pending resolving a disputed tax assessment. Following the Federal Court ruling on 7 February 2007, \$4 114 000 was paid to the ATO with the balance of \$450 628 returned to Keycorp Limited. The sale was approved by shareholders at an Extraordinary General Meeting on 29 August 2005. The TNS sale was effective from 1 July 2005 and a pro-rata return of capital of 41 cents per Keycorp Limited share was paid to shareholders in September 2005.

| | Note | Consolidated | | Company | |
|-----------------------------------------------------------------------------------------------|------|---------------|----------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Financial performance information for the year ended 30 June | | | | | |
| Revenue | | — | — | — | — |
| Amortisation expense | | — | — | — | — |
| Profit before tax | | — | — | — | — |
| Gain/(loss) on sale of discontinued operation | | 451 | (4 667) | 451 | 50 333 |
| Net profit/(loss) | | 451 | (4 667) | 451 | 50 333 |
| Effect of the disposal on individual assets and liabilities of the consolidated entity | | | | | |
| Intangible asset (classified as non current asset held for sale) | | — | 55 000 | — | — |
| Intangible asset sold with subsidiary | | — | 55 000 | — | — |
| Consideration received | | — | (55 000) | — | (55 000) |
| Amount placed in escrow | | — | 4 565 | — | 4 565 |
| Legal fees net of interest received | | — | 102 | — | 102 |
| Net assets | | — | 4 667 | — | (50 333) |
| Cashflow information for the year ended 30 June | | | | | |
| Net cash provided by operating activities | | — | — | — | — |
| Net increase in cash held | | — | — | — | — |

No cash was sold as part of the disposal of this entity.

b) Camtech business

On 23 June 2006, the consolidated entity completed the sale of Camtech e-commerce business to Australian payment services company SecurePay for \$2 256 000. The assets sold comprise intellectual property and fully depreciated property, plant and equipment and had a carrying amount of \$nil.

Financial performance information for the year ended 30 June

| | | | | | |
|--------------------------------------------------------|--|----------|--------------|----------|--------------|
| Revenue | | — | 1 080 | — | 1 080 |
| Other expenses | | — | (589) | — | (589) |
| Profit before tax | | — | 491 | — | 491 |
| Income tax expense | | — | (147) | — | (147) |
| Net profit | | — | 344 | — | 344 |
| Gain on sale of discontinued operation | | — | 2 256 | — | 2 256 |
| Net profit | | — | 2 600 | — | 2 600 |
| Cashflow information for the year ended 30 June | | | | | |
| Net cash provided by operating activities | | — | 344 | — | 344 |
| Net increase in cash held | | — | 344 | — | 344 |

There are no cashflows from investing or financing activities relating to discontinued operations.

c) Total discontinued operations

| | | | | | |
|-----------------------------------------|-----|------------|----------------|------------|---------------|
| Gain on disposal of Camtech business | (b) | — | 2 256 | — | 2 256 |
| Net profit of Camtech business | (b) | — | 344 | — | 344 |
| (Loss)/gain on disposal of TNS business | (a) | 451 | (4 667) | 451 | 50 333 |
| Total net profit/(loss) | | 451 | (2 067) | 451 | 52 933 |

NOTES TO THE FINANCIAL STATEMENTS continued

12.CHANGE IN COMPOSITION OF THE ENTITY

(i) Acquisition of the business and assets of the Optimal Services Group (OSG)

The company acquired 100% of the assets and liabilities of the Optimal Services Group in Canada on 2 October 2006 for a cash consideration of \$240 000. OSG's principal activity is being a service provider of EFTPOS and point of sale solutions in Canada.

The results of the business have been included in consolidated loss from that date.

The acquisition had the following effect on the consolidated entity's assets and liabilities on acquisition date:

| | Pre-Acquisition carrying amounts | Fair value adjustments | Recognised values on acquisition |
|---------------------------------------------------------------------------------------------------------------|----------------------------------------|---------------------------|----------------------------------------|
| | \$000 | \$000 | \$000 |
| Property, plant and equipment | 5 779 | (1 362) | 4 415 |
| Inventories | 2 993 | (2 225) | 768 |
| Trade and other receivables | 6 019 | — | 6 019 |
| Deferred tax liabilities | — | (726) | (726) |
| Trade and other payables | (1 818) | (2 566) | (4 384) |
| Deferred revenue | (530) | — | (530) |
| Employee benefits | (1 013) | — | (1 013) |
| Finance lease liability | (2 306) | — | (2 306) |
| | <u>9 124</u> | <u>(6 880)</u> | 2 243 |
| Cash consideration | | | (240) |
| Legal, professional and other related costs of acquisition | | | (712) |
| Gain on acquisition | | | 1 291 |
| Foreign Exchange difference on closing at year end average taken through foreign currency translation reserve | | | (117) |
| Gain on acquisition | | | 1 174 |

In the nine months to 30 June 2007, OSG contributed an total loss after tax of \$3 008 547. If the acquisition had occurred on 1 July 2006, management estimates that the Keycorp Group consolidated revenue would have been \$103 435 000 and consolidated loss after tax would have been \$12 806 000.

The values of assets, liabilities and contingent liabilities are recognised on acquisition at their estimated fair values. The net gain on acquisition of \$1 174 000 is calculated using the exchange rate at acquisition and is included in other income in the income statement (see note 6).

Pre-acquisition carrying amounts were determined based on applicable AASBs immediately before the acquisition. The values of assets and liabilities recognised on acquisition are their estimated fair values. There is no published market information available in respect of the fair value of the plant and equipment acquired. Accordingly, management has completed a detailed view of the assets acquired and conservatively determined fair value after considering the accounting carrying amount, remaining useful life and the expected realisable value of the respective assets. The fair value of inventory acquired is determined based on its estimated selling price in the ordinary course of business less the estimated costs of completion and sale, and a reasonable profit margin based on the effort required to complete and sell the inventory. The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

(ii) Acquisition of minority interests

During the year the consolidated entity acquired the remaining 30% of shares in Fox Technology Pty Limited for a cash consideration of \$43 000.

| | Note | Consolidated | | Company | |
|-----------------------------------------------------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 13.DIVIDENDS | | | | | |
| No dividends were declared or payable during the year ended 30 June 2007 (30 June 2006: nil) | | | | | |
| Dividend franking account | | | | | |
| 30 per cent franking credits available to shareholders of Keycorp Limited for subsequent financial years. | | | | | |
| | | — | — | 8 483 | 9 883 |

The above available amounts are based on the balance of the dividend franking account at year end adjusted for:

- (a) franking credits that will arise from the payment of the current tax liabilities; and
- (b) franking credits that the entity may be prevented from distributing in subsequent years.

The ability to utilise the franking credits is dependant upon there being sufficient available profits to declare dividends.

In accordance with the tax consolidation legislation, the Company as the head entity in the tax consolidated group has also assumed the benefit of \$8 483 000 (2006: \$9 883 000) franking credits.

14. TRADE AND OTHER RECEIVABLES

| | | | | | |
|--------------------------------------------|----|---------------|---------------|---------------|---------------|
| Trade debtors | | 15 344 | 12 350 | 7 592 | 9 020 |
| Impairment loss | | (195) | (170) | (148) | (142) |
| | | 15 149 | 12 180 | 7 444 | 8 878 |
| Other debtors | | 2 667 | 1 105 | 221 | 198 |
| | | 17 816 | 13 285 | 7 665 | 9 076 |
| Non current receivables | | | | | |
| Long term deposit | | 175 | — | — | — |
| Loans to controlled entities | 37 | — | — | 58 266 | 50 958 |
| Impairment of loans to controlled entities | 37 | — | — | (10 713) | (10 713) |
| | | 175 | — | 47 553 | 40 245 |

15. INVENTORIES

Raw materials

| | | | | | |
|----------------------------|--|-------|---------|-------|---------|
| At cost | | 1 959 | 1 692 | 1 746 | 1 018 |
| Provision for obsolescence | | (784) | (1 086) | (784) | (1 086) |
| | | 1 175 | 606 | 962 | (68) |

Work in progress

| | | | | | |
|----------------------------|--|---|---|---|-----|
| At cost | | — | 7 | — | 7 |
| Provision for obsolescence | | — | — | — | (6) |
| | | — | 7 | — | 1 |

Finished goods

| | | | | | |
|--------------------------------------------------------------------|--|--------------|--------------|--------------|--------------|
| At cost | | 7 164 | 6 485 | 4 495 | 3 781 |
| Provision for obsolescence | | (2 082) | (1 350) | (1 164) | (791) |
| | | 5 082 | 5 135 | 3 331 | 2 990 |
| Total inventories at lower of cost and net realisable value | | 6 257 | 5 748 | 4 293 | 2 923 |

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|----------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 16.NET INVESTMENT IN FINANCE LEASE | | | | | |
| Gross investment in the finance lease | | 457 | — | 457 | — |
| Unearned finance income | | (102) | — | (102) | — |
| Present value of minimum lease payments receivable | | 355 | — | 355 | — |

| | Consolidated & Company | | | |
|----------------------------|----------------------------------|---------------|-----------------------------------------------|---------------|
| | Gross investment in the lease | | Present value of minimum lease payments | |
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Less than one year | 81 | — | 50 | — |
| Between one and five years | 323 | — | 252 | — |
| More than five years | 53 | — | 53 | — |
| | 457 | — | 355 | — |

Keycorp Limited provides terminals and bundled services under managed payment service agreements. These agreements are accounted for as finance leases. Future revenues from these MPS agreements amount to a minimum of \$26.264 million over their contract life. The contracts and lease terms expire in May 2012 and May 2013. After the original lease period, the lessee has the option to purchase the assets at their net book value at that date.

17.OTHER CURRENT ASSETS

| | Note | Consolidated | | Company | |
|------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Prepayments | | 1 411 | 731 | 1 020 | 701 |
| Security deposit | (i) | 3 000 | — | 3 000 | — |
| Other | | 15 | 46 | 4 | 37 |
| | | 4 426 | 777 | 4 024 | 738 |

(i) Cash backed security deposit to support Keycorp Limited's undertaking in respect to the Westpac managed payments services agreement.

18. INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

The consolidated entity accounts for investments in associates using the equity method.

The consolidated entity has the following investment in an associate:

| Name of associate | Principal activity of associate | Country of incorporation or residence | Company and consolidated entity's ownership interest in associate | | Consolidated entity's carrying amounts of investment in associate | | Reporting date of associate | |
|------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------|-------------------------------------------------------------------|-------------|-------------------------------------------------------------------|------------------|-----------------------------|--------------|
| | | | June 2007 % | June 2006 % | June 2007 \$'000 | June 2006 \$'000 | | |
| POSTech Co Ltd (Shenzhen) | Research, develop, produce, sell and export electronic funds transfer point of sales (EFTPOS) terminals to the People's Republic of China. | China | 30% | 30% | — | 114 | 31 December | |
| | | | | | | | Consolidated | |
| | | | | | | | 2007 | 2006 |
| | | | | | | | \$000 | \$000 |
| Result of associate | | | | | | | | |
| Share of associates net loss before and after income tax accounted for using the equity method | | | | | | | — | (108) |
| Movement in the carrying amount of investments in associate: | | | | | | | | |
| Balance at the beginning of the year | | | | | | | 114 | 604 |
| Impairment of investment in POSTech Co. Ltd | | | | | | | (114) | (382) |
| Share of equity accounted losses | | | | | | | — | (108) |
| Balance at the end of the year | | | | | | | — | 114 |

During the year the company wrote off the balance of its investment in POSTech Co Ltd. Accordingly the consolidated entity ceased to equity account its share of the associates result.

The directors are not aware of any capital commitments or contingent liabilities at the end of the year for POSTech Co Ltd.

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|-------------------------------------|-------|---------------|---------------|---------------|---------------------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| 19. INVESTMENTS | | | | | |
| Non Current Investments | | | | | |
| Debt securities held to maturity | 19(a) | 5 355 | 5 296 | 5 355 | 5 295 |
| Investment in controlled entities | | — | — | 1 495 | 1 452 |
| Investment in Associates | | — | — | — | 266 |
| Investment in non-controlled entity | 19(b) | 3 551 | 3 551 | 3 551 | 3 551 |
| | | 8 906 | 8 847 | 10 401 | 10 564 |

- (a) Debt securities – Mezzanine Notes: Pursuant to the sale of the EFTPOS terminal assets and associated rental proceeds related to the Westpac contract to a third party investor in June 2005, the consolidated entity subscribed to Mezzanine Notes maturing on 8 May 2009 (with possible extensions of 12 months at the discretion of both parties), as required under the terms of the Asset & Proceeds Sale Agreement. The consolidated entity subscribed to additional notes during the year ended 30 June 2007. Full entitlement to interest income during that term will accrue in the range of 6.8% to 7.7% per annum.
- (b) Investment in StepNexus Inc: On 30 November 2005 the Board announced the completion of a transaction to form a new company StepNexus Inc to expand MULTOS, one of the world's highest security, open standard card platforms. The agreement involves Keycorp, MasterCard International, Hitachi and venture capital group Oak Hill Venture Partners. The value of Keycorp's investment in this entity is \$3 551 000. In the opinion of the directors cost reflects the current fair value of this investment.
- (c) Investment in controlled entities comprises:

| | Country of incorporation | Ownership interest | | Investment by Keycorp Limited | |
|--------------------------------------|-----------------------------|-----------------------|-----------|----------------------------------|---------------------------|
| | | 2007 % | 2006 % | 2007 \$000 | Restated 2006 \$000 |
| Parent entity | | | | | |
| Keycorp Limited | | | — | | — |
| Subsidiaries | | | | | |
| At cost | | | | | |
| E-Point Pty Limited | Australia ⁽ⁱ⁾ | 100 | 100 | — | — |
| Keycorp Technology Pty Limited | Australia ⁽ⁱ⁾ | 100 | 100 | — | — |
| Fox Technology Pty Limited | Australia ⁽ⁱⁱ⁾ | 100 | 70 | 1 495 | 1 452 |
| Keycorp (Asia) Limited | Hong Kong ⁽ⁱ⁾ | 100 | 100 | — | — |
| Keycorp Systems Limited | UK ⁽ⁱ⁾ | 100 | 100 | — | — |
| Keycorp USA Limited | USA | 100 | 100 | 3* | 3* |
| Tillsmith Systems Inc | USA | 100 | 100 | — | — |
| Keycorp Canada Inc | Canada | 100 | 100 | — | — |
| Keycorp Payment Services Pty Limited | Australia | 100 | 100 | — | — |
| | | | | 1 495 | 1 452 |
| At recoverable amount | | | | | |
| Keycorp Investments Pty Limited | Australia ⁽ⁱ⁾ | 100 | 100 | 3 739 | 3 739 |
| Provision for impairment | | | | (3 739) | (3 739) |
| | | | | 1 495 | 1 452 |

Amounts marked with an asterisk (*) are expressed in whole dollars

- (i) Controlled entities which have been audited by audit firms other than the audit firm of the parent entity
- (ii) Entities subject to ASIC class order relief 98/1418 are relieved from the preparation, audit and lodgement of financial reports and directors' reports
- (iii) During the year the consolidated entity acquired the remaining 30% share in Fox Technology Pty Limited

(d) Deed of Cross Guarantee

Pursuant to Class Order 98/1418 (as amended) dated 13 August 1998, relief has been granted to Keycorp Investments Pty Limited, E-Point Pty Limited and Keycorp Technologies Pty Limited from the Corporations Act 2001 requirements for preparation, audit and lodgement of financial reports and directors reports.

As a condition of the Class Order, Keycorp Limited and the controlled entities identified above (the "Closed Group"), entered into a Deed of Cross Guarantee on 30 December 1999. The effect of the deed is that Keycorp Limited has guaranteed to each creditor to pay any deficiency in the event of winding up of any of the controlled entities in the "Closed Group". All controlled entities in the "Closed Group" have also given a similar guarantee in the event that Keycorp Limited is wound up.

A consolidated income statement and consolidated balance sheet comprising the company and controlled entities which are a party to the Deed of Cross Guarantee (members of the "Closed Group"), after eliminating all transactions between parties to the Deed of Cross Guarantee are as follows:

| | Closed Group | |
|-----------------------------------------------------------|---------------------|-----------------|
| | 2007 | Restated |
| | \$000 | 2006 |
| | | \$000 |
| Summarised income statement and retained profits | | |
| (Loss)/profit before income tax (expense) | (7 880) | 49 299 |
| Income tax benefit/(expense) | 1 526 | (1 811) |
| (Loss)/profit after income tax | (6 354) | 47 488 |
| Accumulated losses at the beginning of the financial year | (7 735) | (55 223) |
| Equity settled transactions | 202 | — |
| Accumulated losses at the end of the financial year | (13 887) | (7 735) |
| Current assets | | |
| Cash and Cash equivalents | 1 175 | 15 513 |
| Trade and other receivables | 10 197 | 10 929 |
| Inventories | 4 506 | 3 050 |
| Net investment in finance lease | 50 | — |
| Other current assets | 4 053 | 752 |
| Total current assets | 19 981 | 30 244 |
| Non current assets | | |
| Receivables | 14 972 | 24 378 |
| Net investment in finance lease | 305 | — |
| Investments | 27 045 | 27 208 |
| Property, plant and equipment | 4 468 | 2 685 |
| Intangible assets | 7 710 | 6 314 |
| Deferred tax assets | 7 544 | 4 303 |
| Total non current assets | 62 044 | 64 888 |
| Total assets | 82 025 | 95 132 |
| Current liabilities | | |
| Trade and other payables | 12 904 | 32 893 |
| Interest bearing loans and borrowings | 11 778 | — |
| Employee benefits | 2 359 | 2 579 |
| Provisions | 3 175 | 5 292 |
| Income tax payable | 2 007 | 234 |
| Other current liabilities | 402 | 313 |
| Total non current assets | 32 625 | 41 311 |
| Non current liabilities | | |
| Interest bearing loans and borrowings | 1 333 | — |
| Employee benefits | 203 | 402 |
| Provisions | 268 | 268 |
| Total non current liabilities | 1 804 | 670 |
| Total liabilities | 34 429 | 41 981 |
| Net assets | 47 596 | 53 151 |
| Shareholders' equity | | |
| Issued capital | 61 105 | 61 105 |
| Reserves | 378 | (219) |
| Accumulated losses | (13 887) | (7 735) |
| Total Shareholders' equity | 47 596 | 53 151 |

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|---------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 20. PROPERTY, PLANT AND EQUIPMENT | | | | | |
| Cost | | | | | |
| Plant and equipment | | | | | |
| Balance at the beginning of year | | 11 300 | 10 291 | 8 184 | 7 321 |
| Additions | | 3 046 | 1 015 | 2 922 | 868 |
| Acquisition through business combinations | | 1 453 | — | — | — |
| Disposals | | (387) | (6) | (197) | (5) |
| Effect of movements in exchange rate | | (93) | — | — | — |
| Reclassification | (i) | (1 024) | — | (863) | — |
| Balance at the end of year | | 14 295 | 11 300 | 10 046 | 8 184 |
| Furniture and Fittings | | | | | |
| Balance at the beginning of year | | 557 | 532 | 258 | 252 |
| Additions | | 33 | 25 | — | 6 |
| Acquisition through business combinations | | 167 | — | — | — |
| Disposals | | (7) | — | — | — |
| Effect of movements in exchange rate | | (13) | — | — | — |
| Reclassification | (i) | (5) | — | (5) | — |
| Balance at the end of year | | 732 | 557 | 253 | 258 |
| Motor Vehicles | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Acquisition through business combinations | | 1 861 | — | — | — |
| Disposals | | (43) | — | — | — |
| Effect of movements in exchange rate | | (110) | — | — | — |
| Balance at the end of year | | 1 708 | — | — | — |
| Leasehold improvements | | | | | |
| Balance at the beginning of year | | 1 551 | 1 551 | 1 000 | 1 000 |
| Additions | | 36 | — | — | — |
| Acquisition through business combinations | | 389 | — | — | — |
| Disposals | | (92) | — | — | — |
| Effect of movements in exchange rate | | (23) | — | — | — |
| Reclassification | (i) | 14 | — | 14 | — |
| Balance at the end of year | | 1 875 | 1 551 | 1 014 | 1 000 |
| Total cost of Property plant and equipment | | 18 610 | 13 407 | 11 313 | 9 442 |
| Depreciation and impairment losses | | | | | |
| Plant and equipment | | | | | |
| Balance at the beginning of year | | 9 366 | 8 491 | 6 724 | 6 175 |
| Disposals | | (290) | — | (121) | — |
| Reclassification | (i) | (770) | — | (645) | — |
| Depreciation expense | | 1 073 | 875 | 558 | 549 |
| Balance at the end of year | | 9 379 | 9 366 | 6 516 | 6 724 |
| Furniture and Fittings | | | | | |
| Balance at the beginning of year | | 315 | 242 | 160 | 138 |
| Disposals | | (3) | — | — | — |
| Reclassification | (i) | (5) | — | (5) | — |
| Depreciation expense | | 100 | 73 | 17 | 22 |
| Balance at the end of year | | 407 | 315 | 172 | 160 |

| | Note | Consolidated | | Company | |
|-------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Motor vehicles | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Disposals | | (6) | — | — | — |
| Depreciation expense | | 372 | — | — | — |
| Balance at the end of year | | 366 | — | — | — |
| Leasehold improvements | | | | | |
| Balance at the beginning of year | | 834 | 521 | 551 | 321 |
| Disposals | | (26) | — | — | — |
| Depreciation expense | | 287 | 313 | 122 | 230 |
| Balance at the end of year | | 1 095 | 834 | 673 | 551 |
| Total Accumulated depreciation | | 11 247 | 10 515 | 7 361 | 7 435 |
| Net written down value | | | | | |
| Plant and equipment | | | | | |
| Balance at the beginning of year | | 1 934 | 1 800 | 1 460 | 1 146 |
| Additions | | 3 046 | 1 015 | 2 922 | 868 |
| Acquisition through business combinations | | 1 453 | — | — | — |
| Disposals | | (93) | (6) | (76) | (5) |
| Effect of movements in exchange rate | | (97) | — | — | — |
| Reclassification | | (254) | — | (218) | — |
| Depreciation expense | | (1 073) | (875) | (558) | (549) |
| Balance at the end of year | | 4 916 | 1 934 | 3 530 | 1 460 |
| Furniture and Fittings | | | | | |
| Balance at the beginning of year | | 242 | 290 | 98 | 114 |
| Additions | | 33 | 25 | — | 6 |
| Acquisition through business combinations | | 167 | — | — | — |
| Disposals | | (4) | — | — | — |
| Effect of movements in exchange rate | | (13) | — | — | — |
| Reclassification | | — | — | — | — |
| Depreciation expense | | (100) | (73) | (17) | (22) |
| Balance at the end of year | | 325 | 242 | 81 | 98 |
| Motor Vehicles | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Acquisition through business combinations | | 1 861 | — | — | — |
| Disposals | | (37) | — | — | — |
| Effect of movements in exchange rate | | (110) | — | — | — |
| Depreciation expense | | (372) | — | — | — |
| Balance at the end of year | | 1 342 | — | — | — |

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|--------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 20.PROPERTY, PLANT AND EQUIPMENT continued | | | | | |
| Leasehold improvements | | | | | |
| Balance at the beginning of year | | 717 | 1 030 | 449 | 679 |
| Additions | | 36 | — | — | — |
| Acquisition through business combinations | | 389 | — | — | — |
| Disposals | | (66) | — | — | — |
| Effect of movements in exchange rate | | (23) | — | — | — |
| Reclassification | | 14 | — | 14 | — |
| Depreciation expense | | (287) | (313) | (122) | (230) |
| Balance at the end of year | | 780 | 717 | 341 | 449 |
| Total carrying amount of Property plant and equipment | | 7 363 | 2 893 | 3 952 | 2 007 |
| Total Property plant and equipment | | | | | |
| Net written down value at the beginning of the year | | 2 893 | 3 120 | 2 007 | 1 939 |
| Net written down value at the end of the year | | 7 363 | 2 893 | 3 952 | 2 007 |

- (i) Following the acquisition of the business and assets of Optimal Services Group the consolidated entity reclassified software assets with a net book value of \$240 000 to intangible assets.

Security

At 30 June 2007, the above property, plant and equipment are subject to a registered charge held by the company's financing bank as outlined in note 24.

Leased assets

Motor vehicles with a net book value of \$1 342 000 (2006: nil) are leased under finance leases.

Other plant and equipment with a net book value of \$2 569 000 (2006: nil) are leased under finance leases.

21. DEFERRED TAX ASSETS AND LIABILITIES

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

| | Assets | | Liabilities | | Net | |
|----------------------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Consolidated | | | | | | |
| Property, plant and equipment | 210 | 236 | — | (48) | 210 | 188 |
| Intangible assets | 534 | 565 | (2 454) | (2 168) | (1 920) | (1 603) |
| Trade debtors | 66 | 8 | — | — | 66 | 8 |
| Inventories | 584 | 565 | — | — | 584 | 565 |
| Income received in advance | 226 | 536 | — | — | 226 | 536 |
| Employee benefits | 392 | 400 | — | — | 392 | 400 |
| Accruals | 807 | 212 | — | — | 807 | 212 |
| Provisions | 1 043 | 1 668 | — | (154) | 1 043 | 1 514 |
| Other items | 961 | 167 | — | — | 961 | 167 |
| Tax value of loss carry forwards recognised | 5 258 | 2 571 | — | — | 5 258 | 2 571 |
| Gain on acquisition of OSG | — | — | (703) | — | (703) | — |
| Tax assets (liabilities) | 10 081 | 6 928 | (3 157) | (2 370) | 6 924 | 4 558 |
| Set off of tax | (2 454) | (2 370) | 2 454 | 2 370 | — | — |
| Net tax assets (liabilities) | 7 627 | 4 558 | (703) | — | 6 924 | 4 558 |
| Company | | | | | | |
| Property, plant and equipment | 112 | 148 | — | (48) | 112 | 100 |
| Intangible assets | — | — | (2 051) | (1 654) | (2 051) | (1 654) |
| Trade debtors | 66 | 8 | — | — | 66 | 8 |
| Inventories | 584 | 565 | — | — | 584 | 565 |
| Employee benefits | 390 | 400 | — | — | 390 | 400 |
| Accruals | 680 | 154 | — | — | 680 | 154 |
| Provisions | 1 033 | 1 668 | — | (154) | 1 033 | 1 514 |
| Other items | 921 | 96 | — | — | 921 | 96 |
| Tax value of loss carry forwards recognised | 2 687 | — | — | — | 2 687 | — |
| Provisions for impairment of intercompany balances | 1 921 | 1 921 | — | — | 1 921 | 1 921 |
| Tax assets (liabilities) | 8 394 | 4 960 | (2 051) | (1 856) | 6 343 | 3 104 |
| Set off of tax | (2 051) | (1 856) | 2 051 | 1 856 | — | — |
| Net tax assets | 6 343 | 3 104 | — | — | 6 343 | 3 104 |

Tax consolidation

In accordance with the tax consolidation legislation, the Company as the head entity of the Australian tax-consolidated group has assumed the current tax (liability) asset and deferred tax assets arising from unused tax losses/credits initially recognised by the members in the tax consolidated group.

Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items

| | Consolidated | | Company | |
|------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Tax losses | 8 485 | 6 572 | — | — |

Tax losses amounting to \$2 967 083 expire in the next 12 months. The remainder will expire between 2009 – 2016. Certain deferred tax assets, which largely relate to the recently acquired OSG business, have not been recognised, as it is not yet sufficiently probable that future taxable profit will be available against which the consolidated entity can utilise the benefits.

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|--------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 22. INTANGIBLE ASSETS | | | | | |
| Cost | | | | | |
| Goodwill | | | | | |
| Balance at the beginning and end of year | | 3 239 | 3 239 | — | — |
| Intellectual property | | | | | |
| Balance at the beginning and end of year | | 4 075 | 4 075 | — | — |
| Capitalised development | | | | | |
| Balance at the beginning of year | | 19 225 | 16 548 | 19 225 | 16 548 |
| Disposals during the year | | (8 692) | — | (8 692) | — |
| Acquisitions – internally developed | | 3 805 | 2 677 | 3 805 | 2 677 |
| Balance at the end of year | | 14 338 | 19 225 | 14 338 | 19 225 |
| Other intangible assets | | | | | |
| Balance at the beginning and end of year | | 1 475 | 1 475 | — | — |
| Computer software | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Reclassifications | (i) | 1 015 | — | 854 | — |
| Additions | | 25 | — | 4 | — |
| Acquisitions through business combinations | | 545 | — | — | — |
| Effect of movements in exchange rate | | (32) | — | — | — |
| Disposals | | (87) | — | (82) | — |
| Balance at the end of year | | 1 466 | — | 776 | — |
| Total cost of Intangible assets | | 24 593 | 28 014 | 15 114 | 19 225 |
| Amortisation and impairment losses | | | | | |
| Goodwill | | | | | |
| Balance at the beginning and end of year | | 325 | 325 | — | — |
| Intellectual property | | | | | |
| Balance at the beginning of year | | 3 068 | 2 808 | — | — |
| Amortisation charge | | 307 | 260 | — | — |
| Balance at the end of year | | 3 375 | 3 068 | — | — |
| Capitalised development | | | | | |
| Balance at the beginning of year | | 13 710 | 11 458 | 13 710 | 11 458 |
| Disposals during the year | | (8 692) | — | (8 692) | — |
| Amortisation for the year | | 2 218 | 1 020 | 2 218 | 1 020 |
| Impairment charge | | 267 | 1 232 | 267 | 1 232 |
| Balance at the end of year | | 7 503 | 13 710 | 7 503 | 13 710 |
| Other intangible assets | | | | | |
| Balance at the beginning of year | | 486 | 263 | — | — |
| Amortisation for the year | | 341 | 223 | — | — |
| Balance at the end of year | | 827 | 486 | — | — |

| | Note | Consolidated | | Company | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 22.INTANGIBLE ASSETS continued | | | | | |
| Computer software | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Reclassifications | (i) | 775 | — | 650 | — |
| Disposals | | (51) | — | (46) | — |
| Amortisation for the year | | 345 | — | 99 | — |
| Balance at the end of year | | 1 069 | — | 703 | — |
| Total accumulated amortisation and impairment losses | | 13 099 | 17 590 | 8 206 | 13 710 |
| Net book value | | | | | |
| Goodwill | | | | | |
| Balance at the beginning and end of year | | 2 914 | 2 914 | — | — |
| Intellectual property | | | | | |
| Balance at the beginning of year | | 1 007 | 1 267 | — | — |
| Amortisation for the year | | (307) | (260) | — | — |
| Balance at the end of year | | 700 | 1 007 | — | — |
| Capitalised development | | | | | |
| Balance at the beginning of year | | 5 515 | 5 090 | 5 515 | 5 090 |
| Acquisitions – internally developed | | 3 805 | 2 677 | 3 805 | 2 677 |
| Amortisation for the year | | (2 218) | (1 020) | (2 218) | (1 020) |
| Impairment charge | | (267) | (1 232) | (267) | (1 232) |
| Balance at the end of year | | 6 835 | 5 515 | 6 835 | 5 515 |
| Other intangible assets | | | | | |
| Balance at the beginning of year | | 989 | 1 212 | — | — |
| Amortisation for the year | | (341) | (223) | — | — |
| Balance at the end of year | | 648 | 989 | — | — |
| Computer software | | | | | |
| Balance at the beginning of year | | — | — | — | — |
| Reclassifications | (i) | 240 | — | 204 | — |
| Additions | | 25 | — | 4 | — |
| Acquisitions through business combinations | | 545 | — | — | — |
| Effect of movements in exchange rate | | (32) | — | — | — |
| Disposals | | (36) | — | (36) | — |
| Amortisation for the year | | (345) | — | (99) | — |
| Balance at the end of year | | 397 | — | 73 | — |
| Net written down value at beginning of year | | 10 425 | 10 483 | 5 515 | 5 090 |
| Net written down value at end of year | | 11 494 | 10 425 | 6 908 | 5 515 |
| (i) Following the acquisition of the business and assets of Optimal Services Group the consolidated entity reclassified software assets with a net book value of \$240 000 to intangible assets. | | | | | |
| Impairment tests for cash generating units containing goodwill | | | | | |
| The following units have the following amounts of goodwill: | | | | | |
| Fox Technology Pty Limited | | 2 114 | 2 114 | — | — |
| E-Point Pty Limited (trading as EFTPOS Engineering) | | 800 | 800 | — | — |
| | | 2 914 | 2 914 | — | — |

NOTES TO THE FINANCIAL STATEMENTS continued

22. INTANGIBLE ASSETS continued

The recoverable amount of the Fox Technologies cash-generating unit is based on future revenue projections over a four year period discounted at 13.24%. These calculations use cash flow projections based on actual operating results and the forecasts of service revenues based on existing managed service agreements in place plus conservative estimates of new agreements likely to be achieved using the Fox software.

The recoverable amount of the EFTPOS Engineering cash-generating unit is based on value in use calculations. Those calculations use cash flow projections based on actual operating results and the forecasts of service revenues based on existing managed service agreements in place. The cash flows are not discounted. The carrying amount is supported by one year of cash flows.

Capitalised development costs

The recoverability of the capitalised development costs is dependent on the successful development and commercial exploitation or sale of the respective area of interest.

The key assumptions and the approach to determining their value in the current and previous period are:

| Assumption | How determined |
|-------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Access devices and Smartcards | Expected cash flows discounted at 15% from existing contracts plus future expectations of growth in market share of new products as a result of development are compared to the carrying value of the asset and any necessary impairment recorded. |

The carrying amount of development costs represents expenditure incurred on labour, materials and other contracted services to develop the technology to the extent that future commercial exploitation is reasonably certain. Any adverse change in assumptions could reduce the recoverable amount below carrying amount.

The impairment analysis for goodwill and other intangible assets, including capitalised development costs, is principally based upon discounted estimated future cash flows from the use and eventual disposal of the assets. Factors such as lower than anticipated sales and resulting decreases in net cash flows and changes in the discount rates used could lead to impairments in future periods.

Impairment loss

During the year, \$267 000 (2006: \$1 232 000), of development costs relating to projects that are no longer expected to generate future economic benefits, were recognised as impaired and expensed to the income statement.

| | Note | Consolidated | | Company | |
|-------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 23. TRADE AND OTHER PAYABLES | | | | | |
| Current | | | | | |
| Trade creditors | | 7 965 | 10 374 | 5 781 | 8 095 |
| Loans to directors of controlled entities | (i) | — | 102 | — | — |
| Other creditors and accruals | | 6 463 | 3 285 | 2 043 | 500 |
| | | 14 428 | 13 761 | 7 824 | 8 595 |
| Amount payable to controlled entities | 37 | — | — | 19 090 | 18 090 |
| | | 14 428 | 13 761 | 26 914 | 26 685 |

(i) In the prior year two directors of Fox Technology Pty Limited loaned Fox Technology Pty Limited \$102 000. The loan was non interest bearing for an undefined term and was repaid during the current year.

24. INTEREST BEARING LIABILITIES

Non-current liabilities

| | | | | |
|---------------------------|--------------|----------|--------------|----------|
| Finance lease liabilities | 1 982 | — | 1 339 | — |
| | 1 982 | — | 1 339 | — |

Current liabilities

| | | | | |
|----------------------------------------------|---------------|----------|---------------|----------|
| Bank term loan | 11 500 | — | 11 500 | — |
| Current portion of finance lease liabilities | 1 013 | — | 272 | — |
| | 12 513 | — | 11 772 | — |

During the year, the company obtained a \$15 000 000 multi option revolving facility with Westpac Banking Corporation, with a maturity date of 31 March 2008. These facilities are secured by a registered charge held by Westpac Banking Corporation over the groups fixed and floating assets. Subsequent to year end the maturity date was revised to 30 September 2008. The amounts drawn down at 30 June 2007 were \$11 500 000. The facility is structured Tranche 1 \$5 500 000 revolving facility which bears interest at 7.5% above BBSY, Tranche 2 \$7 500 000 non revolving facility bearing interest at 1% over BBSY and Tranche 3 \$2 000 000 which is set aside for bank and other guarantees of which \$2 000 000 is undrawn. Interest accrues daily on the outstanding principal drawn and is due for payment on each maturity of the rolling dates. Tranche 2 is supported by a guarantee facility provided by Telstra Corporation Limited.

24.INTEREST BEARING LIABILITIES continued

Terms and debt repayment schedule

Terms and conditions of outstanding loans are as follows:

| Consolidated | | | | | | | |
|------------------------------------|----------|---------------|------------------|------------------|-----------------------|------------------|-----------------------|
| | | | | 30 June 2007 | | 30 June 2006 | |
| | Currency | Interest rate | Year of maturity | Face value \$000 | Carrying amount \$000 | Face value \$000 | Carrying amount \$000 |
| Bank term loan — Tranche 1 | AUD | BBSY+7.5% | 2008 | 4 000 | 4 000 | — | — |
| Bank term loan — Tranche 2 | AUD | BBSY+1% | 2008 | 7 500 | 7 500 | — | — |
| Finance lease liabilities | AUD | 9.12% | 2012 | 1 611 | 1 611 | — | — |
| Finance lease liabilities | CAD | 8.79% | 2008 | 1 384 | 1 384 | — | — |
| | | 10.08% | 2011 | | | | |
| Total interest-bearing liabilities | | | | 14 495 | 14 495 | — | — |

| Company | | | | | | | |
|------------------------------------|----------|---------------|------------------|------------------|-----------------------|------------------|-----------------------|
| | | | | 30 June 2007 | | 30 June 2006 | |
| | Currency | Interest rate | Year of maturity | Face value \$000 | Carrying amount \$000 | Face value \$000 | Carrying amount \$000 |
| Bank term loan — Tranche 1 | AUD | BBSY+7.5% | 2008 | 4 000 | 4 000 | — | — |
| Bank term loan — Tranche 2 | AUD | BBSY+1% | 2008 | 7 500 | 7 500 | — | — |
| Finance lease liabilities | AUD | 9.12% | 2012 | 1 611 | 1 611 | — | — |
| Total interest-bearing liabilities | | | | 13 111 | 13 111 | — | — |

Finance Lease Liabilities

Finance lease liabilities of the group are payable as follows:

| Consolidated | | | | | | | |
|----------------------------|-----------------------------------|---------------------|----------------------|-----------------------------------|---------------------|----------------------|--|
| | Minimum lease payments 2007 \$000 | Interest 2007 \$000 | Principal 2007 \$000 | Minimum lease payments 2006 \$000 | Interest 2006 \$000 | Principal 2006 \$000 | |
| Less than one year | 1 252 | 239 | 1 013 | — | — | — | |
| Between one and five years | 2 319 | 337 | 1 982 | — | — | — | |
| | 3 571 | 576 | 2 995 | — | — | — | |

| Company | | | | | | | |
|----------------------------|-----------------------------------|---------------------|----------------------|-----------------------------------|---------------------|----------------------|--|
| | Minimum lease payments 2007 \$000 | Interest 2007 \$000 | Principal 2007 \$000 | Minimum lease payments 2006 \$000 | Interest 2006 \$000 | Principal 2006 \$000 | |
| Less than one year | 408 | 136 | 272 | — | — | — | |
| Between one and five years | 1 598 | 259 | 1 339 | — | — | — | |
| | 2 006 | 395 | 1 611 | — | — | — | |

Keycorp Limited has obtained a third party financing facility of \$6 000 000 to fund the sale and leaseback of terminal equipment. The facility may be drawn in multiple tranches and is repayable over 60 months commencing 1 May 2007. Keycorp Limited has the right to purchase the equipment under a MPSA at the written down value and may be exercised at any time. At balance sheet date the amount of the facility utilised is \$1 611 000. In addition, a subsidiary has entered into motor vehicle finance leases of \$1 384 000. At balance sheet date the net book value of the motor vehicles under finance lease is \$1 342 000.

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|----------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 25.EMPLOYEE BENEFITS | | | | | |
| Current | | | | | |
| Salaries and wages accrued | | 1 862 | 1 647 | 1 167 | 1 647 |
| Liability for long service leave | | 473 | 303 | 473 | 223 |
| Liability for annual leave | | 1 694 | 831 | 625 | 709 |
| Total employee benefits – current | | 4 029 | 2 781 | 2 265 | 2 579 |
| Non-Current | | | | | |
| Liability for long-service leave | | 203 | 473 | 203 | 402 |
| Total employee benefits – non-current | | 203 | 473 | 203 | 402 |

Share based payments

Shareholders approved the introduction of the Keycorp Employee Share Option Incentive Plan (ESOIP) at the 1996 Annual General Meeting.

Each option granted under the ESOIP entitles the employee to acquire one ordinary share of Keycorp Limited. There are no voting or dividend rights attaching to the options until they are exercised by the employee, at which point ordinary shares which rank equally with all other Keycorp shares are issued and quoted on the ASX. The options cannot be transferred and will not be quoted on the ASX.

All options expire on the earlier of their expiry date. In certain circumstances, at the discretion of management, employees included in an involuntary redundancy program are eligible to retain and exercise share options in accordance with the terms and conditions of the particular options issue.

The recognition and measurement principles in AASB 2 have not been applied to option grants before 7 November 2002 in accordance with the transitional provisions in AASB 1.

The terms and conditions of the grants are as follows, whereby all options are settled by physical delivery of shares.

| Grant date | No of options | Vesting date | Vesting condition | Expiry date | Life of option | Exercise price |
|------------|---------------|--------------|-------------------|-------------|----------------|----------------|
| 20/9/02 | 137 950 | 20/9/03 | Note a | 20/9/07 | 5 years | \$1.24 |
| 20/9/02 | 142 150 | 20/9/04 | Note a | 20/9/07 | 5 years | \$1.24 |
| 20/9/04 | 373 300 | 20/9/05 | Note a | 20/9/07 | 5 years | \$1.24 |
| 31/10/03 | 464 500 | 31/10/05 | Note a | 31/10/08 | 5 years | \$1.36 |
| 31/10/03 | 477 500 | 31/10/06 | Note a | 31/10/08 | 5 years | \$1.36 |
| 1/7/04 | 25 000 | 1/7/06 | Note a | 1/7/09 | 5 years | \$1.39 |
| 1/7/04 | 25 000 | 1/7/07 | Note a | 1/7/09 | 5 years | \$1.39 |
| 23/9/04 | 8 000 | 23/9/06 | Note a | 23/9/09 | 5 years | \$1.80 |
| 23/9/04 | 8 000 | 23/9/09 | Note a | 23/9/09 | 5 years | \$1.80 |
| 27/5/05 | 25 000 | 1/3/07 | Note b | 1/3/10 | 5 years | \$1.72 |
| 27/4/05 | 25 000 | 1/3/08 | Note b | 1/3/10 | 5 years | \$1.72 |
| 19/12/05 | 12 500 | 19/12/07 | Note b | 19/12/10 | 5 years | \$1.50 |
| 19/12/05 | 12 500 | 19/12/08 | Note b | 19/12/10 | 5 years | \$1.50 |
| 15/1/06 | 109 999 | 15/1/08 | Note c | 15/1/11 | 5 years | \$1.48 |
| 15/1/06 | 109 999 | 15/1/09 | Note c | 15/1/11 | 5 years | \$1.48 |
| 15/1/06 | 110 002 | 15/1/10 | Note c | 15/1/11 | 5 years | \$1.48 |
| 26/10/06 | 183 332 | 26/10/08 | Note c | 26/10/11 | 5 years | \$0.80 |
| 26/10/06 | 183 334 | 26/10/09 | Note c | 26/10/11 | 5 years | \$0.80 |
| 26/10/06 | 183 334 | 26/10/10 | Note c | 26/10/11 | 5 years | \$0.80 |

25.EMPLOYEE BENEFITS continued

Note a: The options granted are exercisable between one and three years from grant date providing performance hurdles are attained. The performance hurdles require continuous employment by the employee throughout the vesting period and for Keycorp Limited's share price to attain a pre-defined market price for a period of five consecutive trading days during the vesting period.

Note b: The options granted are exercisable after two years (in respect of 50%) (First Exercise Date) and after three years (in respect of 50%) (Second Exercise Date) until five years from grant date providing performance hurdles are attained. The hurdle is determined by the percentage gain in the S&P/ASX 300 Accumulation Index (Index) for each of the non-exercise periods. The percentage gain in the index over the relevant period is to be applied to the option price (ie the exercise price) to determine the relevant hurdle at each exercise date (Hurdle). At each exercise date, the Hurdle price will be determined by multiplying the option price by the percentage gain in the index, calculated from the date of offer to the First Exercise Date or Second Exercise Date, as the case may be.

The first Hurdle will be determined on the First Exercise Date for 50% of the options offered. The condition will be met when the volume weighted average price for Keycorp shares traded on the ASX on any five consecutive trading days in the three calendar months immediately preceding the First Exercise Date, or any five consecutive trading days after the First Exercise Date, is greater than or equal to the Hurdle price as calculated with reference to the Index.

The second Hurdle will be determined on the Second Exercise Date for the other 50% of the options offered. The condition will be met when the volume-weighted average price for Keycorp shares traded on the ASX on any 5 consecutive trading days in the three calendar months immediately preceding the Second Exercise Date, or any five consecutive trading days after the Second Exercise Date, is greater than or equal to the Hurdle price as calculated with reference to the Index.

Once (and if) the Hurdle set for each of the exercise dates is met, the options are unconditional, vested and exercisable.

Note c: The options granted are exercisable between one and three years (in respect of three equal tranches) from grant date providing performance hurdles are attained. The performance hurdles require continuous employment through the vesting period in respect of each tranche and for the Keycorp Limited total shareholder return (TSR) to be greater than or equal to the S&P/ASX 300 Accumulation Index for twenty consecutive trading days on or after the first exercise date. Growth in the TSR is defined as share price growth and dividends paid and reinvested on the ex-dividend date (adjusted for rights, bonus issues and any capital reconstructions). The hurdle can be satisfied at any time on or after the first exercise date up to the last exercise date.

The number and weighted average exercise prices of share options are as follows:

| | Weighted average exercise price 2007 | No. of options 2007 | Weighted average exercise price 2006 | No. of options 2006 |
|--------------------------------------------|--------------------------------------------------|---------------------------|--------------------------------------------------|---------------------------|
| Outstanding at the beginning of the period | \$1.41 | 2 565 400 | \$2.76 | 3 034 100 |
| Forfeited during the period | \$1.32 | (944 600) | \$6.27 | (877 200) |
| Exercised during the period | — | — | \$1.27 | (366 500) |
| Granted during the period | \$0.80 | 840 000 | \$1.48 | 775 000 |
| Outstanding at the end of the period | \$1.26 | 2 460 800 | \$1.41 | 2 565 400 |
| Exercisable at the end of the period | \$1.32 | 1 497 800 | \$1.29 | 1 078 900 |

The options outstanding at 30 June 2007 have an exercise price in the range of \$0.80 – 1.80 and a weighted average contractual life of 2.10 years.

During the financial year nil options were exercised (2006: 366 500). The weighted average share price at the dates of exercise was nil (2006: \$1.49).

The fair value of services received in return for options granted are measured by reference to the fair value of options granted.

NOTES TO THE FINANCIAL STATEMENTS continued

25.EMPLOYEE BENEFITS continued

| Grant date | | Expiry date | Fair value of option | Exercise price | Share price at grant date | Estimated volatility | Risk free interest free | Dividend yield |
|-------------|-----------|-------------|----------------------|----------------|---------------------------|----------------------|-------------------------|----------------|
| 31 Oct 2003 | Tranche 1 | 31 Oct 2008 | \$0.35 | \$0.95 | \$1.33 | 41% | 5.67% | 0% |
| 31 Oct 2003 | Tranche 2 | 31 Oct 2008 | \$0.44 | \$0.95 | \$1.33 | 41% | 5.67% | 0% |
| 1 Jul 2004 | Tranche 1 | 1 July 2009 | \$0.42 | \$0.98 | \$1.48 | 43% | 5.68% | 2% |
| 1 Jul 2004 | Tranche 2 | 1 July 2009 | \$0.49 | \$0.98 | \$1.48 | 43% | 5.68% | 2% |
| 23 Sep 2004 | Tranche 1 | 23 Sep 2009 | \$0.53 | \$1.39 | \$1.96 | 40% | 5.22% | 2% |
| 23 Sep 2004 | Tranche 2 | 23 Sep 2009 | \$0.62 | \$1.39 | \$1.96 | 40% | 5.22% | 2% |
| 27 May 2005 | Tranche 1 | 1 Mar 2010 | \$0.31 | \$1.31 | \$1.70 | 35% | 5.21% | 2% |
| 27 May 2005 | Tranche 2 | 1 Mar 2010 | \$0.38 | \$1.31 | \$1.70 | 35% | 5.21% | 2% |
| 20 Dec 2005 | Tranche 1 | 19 Dec 2010 | \$0.36 | \$1.50 | \$1.50 | 35% | 5.32% | 0% |
| 20 Dec 2005 | Tranche 2 | 19 Dec 2010 | \$0.45 | \$1.50 | \$1.50 | 35% | 5.32% | 0% |
| 15 Jan 2006 | Tranche 1 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 15 Jan 2006 | Tranche 2 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 15 Jan 2006 | Tranche 3 | 15 Jan 2011 | \$0.58 | \$1.48 | \$1.51 | 36% | 5.12% | 0% |
| 26 Oct 2006 | Tranche 1 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |
| 26 Oct 2006 | Tranche 2 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |
| 26 Oct 2006 | Tranche 3 | 26 Oct 2011 | \$0.36 | \$0.80 | \$0.90 | 44% | 6.03% | 0% |

The estimate of the fair value of the services received is measured based on the Black Scholes Merton "up and in" call barrier pricing model. The contractual life of the options is used as an input into the model.

- (i) The payment of a capital return of 41 cents per share in September 2005 resulted in a reduction of the option exercise price by 41 cents for the options outstanding at that date. The option hurdle price is a function of the percentage increase in the S&P/ASX 300 index and the option exercise price. The exercise price includes the capital return repayment.

The expected volatility is based on the historic volatility (calculated on the weighted average remaining life of the share options), adjusted for any expected changes to volatility due to publicly available information.

Options are granted under service, market and non-market performance conditions. Non-market performance conditions are not taken into account in the grant date fair value measurement of the services rendered.

No shares were granted under the Deferred Employee Share Plan during the year. 255 000 shares were granted in the prior year under the Deferred Employee Share Plan (DESP) to selected employees subject to meeting certain performance criteria. The shares vest over a 3 year period. The fair value of the shares was \$1.47 and is based on the Keycorp Limited share price at grant date. The fair value is recognised as an expense over the vesting period.

1 220 000 options were granted to Chief Executive Officer, subject to shareholder approval at the 2007 Annual General Meeting.

| | Consolidated | | Company | |
|-------------------------------------------------------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| Share options – equity settled | 95 | 225 | 95 | 225 |
| Expense arising from DESP granted in 2006 – equity settled. | 108 | 41 | 108 | 41 |
| Total expense recognised as employee cost | 203 | 266 | 203 | 266 |

| | Consolidated | | Company | |
|--------------------------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 26. PROVISIONS | | | | |
| Current | | | | |
| Warranty | 2 265 | 1 364 | 2 163 | 1 272 |
| Restructuring | 897 | 256 | 324 | — |
| Provision for onerous contract | 39 | 113 | — | — |
| Software development services | 438 | 300 | 438 | 300 |
| Legal provision | 250 | 3 720 | 250 | 3 720 |
| | 3 889 | 5 753 | 3 175 | 5 292 |
| Non current | | | | |
| Lease restoration | 268 | 402 | 268 | 268 |
| | 268 | 402 | 268 | 268 |

Reconciliations

Reconciliations of the carrying amounts of each class of provision as set out below:

Warranty

| | | | | |
|------------------------------------------------|-------|-------|-------|-------|
| Carrying amount at beginning of financial year | 1 364 | 693 | 1 272 | 564 |
| Provided during the year | 1 492 | 1 027 | 1 337 | 906 |
| Amounts utilised during the year | (591) | (356) | (446) | (198) |
| Carrying amount at end of financial year | 2 265 | 1 364 | 2 163 | 1 272 |

The provision for warranty comprises a 1 year product warranty against manufacturer's defects and a deferral of revenue in respect of sales of extended warranty services which have not been delivered at balance date.

Onerous contract

| | | | | |
|------------------------------------------------|------|-----|---|---|
| Carrying amount at beginning of financial year | 113 | — | — | — |
| Provided during the year | — | 113 | — | — |
| Amounts utilised during the year | (74) | — | — | — |
| Carrying amount at end of financial year | 39 | 113 | — | — |

The prior year balance relates to contracted rental payments under an onerous non cancellable lease agreement. During the year the consolidated entity assigned the lease to a third party, and retained a liability in relation to a small portion of the lease.

Restructuring

| | | | | |
|------------------------------------------------|-------|-----|-----|---|
| Carrying amount at beginning of financial year | 256 | — | — | — |
| Provided during the year | 897 | 256 | 324 | — |
| Amounts utilised during the year | (256) | — | — | — |
| Carrying amount at end of financial year | 897 | 256 | 324 | — |

The provision for restructuring primarily includes employee termination benefits as a result of a management program to reorganise the operational structure of the organisation. The current provision relates to a program commenced and publicly announced prior to the end of the financial year. The estimated costs are based on the consolidated entity's published redundancy program which provides the affected employees with all statutory entitlements and outplacement services.

Settlement of a legal action relating to a former director

| | | | | |
|------------------------------------------------|---|-------|---|-------|
| Carrying amount at beginning of financial year | — | 500 | — | 500 |
| Amounts utilised during the year | — | (500) | — | (500) |
| Carrying amount at end of financial year | — | — | — | — |

The prior year provision relates to a settlement of a legal action commenced by a former director claiming alleged unpaid contractual benefits. The case was settled in a court of law with the final settlement paid in July 2005.

NOTES TO THE FINANCIAL STATEMENTS continued

| | Consolidated | | Company | |
|------------------------------------------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 26. PROVISIONS continued | | | | |
| Software development | | | | |
| Current | | | | |
| Carrying amount at beginning of financial year | 300 | 121 | 300 | 121 |
| Transferred from non current | — | 204 | — | 204 |
| Provided during the year | 138 | — | 138 | — |
| Amounts utilised during the year | — | (25) | — | (25) |
| Carrying amount at end of financial year | 438 | 300 | 438 | 300 |
| Non Current | | | | |
| Carrying amount at beginning of financial year | — | 204 | — | 204 |
| Transferred to current | — | (204) | — | (204) |
| Carrying amount at end of financial year | — | — | — | — |

Under the terms of the Westpac terminal services agreement Keycorp has committed to the provision of software development services over the life of the contract. This balance represents the net present value of committed expenditure that Keycorp expects to incur over the five-year contract.

Legal provision

| | | | | |
|------------------------------------------------|---------|-------|---------|-------|
| Carrying amount at beginning of financial year | 3 720 | 500 | 3 720 | 500 |
| Provisions (released)/provided during the year | (250) | 3 220 | (250) | 3 220 |
| Amounts utilised during the year | (3 220) | — | (3 220) | — |
| Carrying amount at end of financial year | 250 | 3 720 | 250 | 3 720 |

A third party has made a claim against a Keycorp distributor claiming that sale of Keycorp product in its market breaches patents that it currently holds. At the date of this report, the company is in the process of evaluating the merits of this claim but considered it prudent to provide an amount of \$250 000 to cover legal costs and a potential settlement in defending the claim.

During the year the company paid \$3 220 000 to settle an outstanding tax matter related to an R&D syndicate that was implemented in 1994.

Lease restoration

| | | | | |
|------------------------------------------------|-------|-----|-----|-----|
| Carrying amount at beginning of financial year | 402 | 402 | 268 | 268 |
| Released during the year | (134) | — | — | — |
| Carrying amount at end of financial year | 268 | 402 | 268 | 268 |

Provision is made for the estimated cost of restoring the consolidated entity's leasehold premises to their original condition as required by the operating lease agreement. The amount provided is based on estimates provided by an external consultant experienced in estimating costs for similar facilities and fit outs.

27. CURRENT TAX LIABILITY

| | | | | |
|--------------------|-------|-----|-------|-----|
| Income tax payable | 2 007 | 234 | 2 007 | 234 |
|--------------------|-------|-----|-------|-----|

The current tax liability represents the amount of income taxes payable in respect of current and prior financial periods. In accordance with the tax consolidation legislation, the Company as the head entity of the Australian tax-consolidated group has assumed the current tax liability initially recognised by the members in the tax-consolidated group.

28. OTHER LIABILITIES

Current

| | | | | |
|----------------------------|-----|-------|-----|-----|
| Income received in advance | 801 | 2 096 | 402 | 311 |
|----------------------------|-----|-------|-----|-----|

| | Consolidated | | Company | |
|-----------------------------------------|---------------|---------------|---------------|---------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 29. ISSUED CAPITAL | | | | |
| Movements in share capital | | | | |
| Balance at beginning of financial year | 61 105 | 94 328 | 61 105 | 94 328 |
| Share options exercised by employees | — | 330 | — | 330 |
| Capital Return | 30(a) | (33 553) | — | (33 553) |
| Balance at end of financial year | 61 105 | 61 105 | 61 105 | 61 105 |

(a) On 28 June 2005, the Board publicly announced the sale of the Transaction Network Solutions (TNS) business to Telstra Corporation Limited. The sale was approved by shareholders at an Extraordinary General Meeting (EGM) on 29 August 2005. Approximately \$33 553 000 of the sale proceeds from the disposal of the TNS business was used as a capital return to investors in August 2005 at the rate of \$0.41 per share.

| | No of shares | |
|-----------------------------------------|-------------------|-------------------|
| | 2007 | 2006 |
| On issue at 1 July | 82 168 938 | 81 802 438 |
| Share options exercised by employees | — | 366 500 |
| On issue at 30 June – fully paid | 82 168 938 | 82 168 938 |

Terms and conditions of issued capital

- (i) Effective 1 July 1998, the Company Law Review Act abolished the concept of par value shares and the concept of authorised capital. Accordingly, the Company does not have authorised capital or par value in respect of its issued shares.
- (ii) Ordinary shares have the right to receive dividends as declared and, in the event of winding up the Company, to participate in the proceeds from the sale of all surplus assets in proportion to the number of and amounts paid up on shares held.
- (iii) Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the company.

| | Consolidated | | Company | |
|-------------|---------------|---------------|---------------|---------------------------|
| | 2007 \$000 | 2006 \$000 | 2007 \$000 | Restated 2006 \$000 |
| Note | \$000 | \$000 | \$000 | \$000 |

30. RESERVES AND ACCUMULATED LOSSES

a) Foreign currency translation reserve

Movements in foreign currency translation reserve

| | | | | |
|-----------------------------------------|-------------|--------------|----------|----------|
| Balance at beginning of financial year | (324) | (13) | — | — |
| Translation of overseas subsidiaries | 263 | (311) | — | — |
| Balance at end of financial year | (61) | (324) | — | — |

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations where their functional currency is different to the presentation of the reporting entity.

b) Accumulated losses

| | | | | |
|--------------------------------------------------------------|-----------------|-----------------|-----------------|----------------|
| Balance at beginning of financial year | (23 788) | (21 167) | (7 648) | (61 037) |
| Impact of change accounting policy | 3(s)(i) | — | — | (542) |
| Balance at beginning of financial year, restated | (23 788) | (21 167) | (7 648) | (61 579) |
| Equity settled transactions | 9 | 266 | 203 | 266 |
| Net (loss)/profit attributable to members of Keycorp Limited | (11 517) | (2 887) | (9 702) | 53 665 |
| Balance at end of financial year | (35 102) | (23 788) | (17 147) | (7 648) |

NOTES TO THE FINANCIAL STATEMENTS continued

| | Note | Consolidated | | Company | |
|-------------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 31.COMMITMENTS | | | | | |
| Operating Leases as lessee | | | | | |
| Non – cancellable operating lease rentals are payable as follows: | | | | | |
| Within one year | | 3 038 | 1 079 | 1 061 | 849 |
| Later than one year but no later than five years | | 4 609 | 2 141 | 999 | 1 549 |
| Balance at end of financial year | | 7 647 | 3 220 | 2 060 | 2 398 |

Capital expenditure commitments

Aggregate expenditure commitments comprise:

Amounts not provided for:

| | | | | | |
|------------------------|--|-------|-------|-------|-------|
| Rental commitments | | 7 541 | 2 981 | 1 968 | 2 178 |
| Plant and equipment | | 106 | 239 | 92 | 220 |
| Total not provided for | | 7 647 | 3 220 | 2 060 | 2 398 |

The consolidated entity leases various properties under non-cancellable operating leases expiring from one to five years. Leases generally provide the consolidated entity with a right of renewal at which time all terms are negotiated.

All other leases relating to equipment are generally arranged with a maximum period of 3 years at which time all terms are renegotiated.

| | Consolidated | | Company | |
|--|--------------|------------|------------|------------|
| | 2007 \$ | 2006 \$ | 2007 \$ | 2006 \$ |

32.AUDITOR'S REMUNERATION

Audit services

Auditors of the Company, KPMG Australia

| | | | | |
|---------------------------------------------------------------------------|---------|---------|---------|---------|
| – audit and review of financial reports (company and consolidated entity) | 294 482 | 317 000 | 294 482 | 317 000 |
| – audit and review of financial reports (other controlled entities) | 5 000 | 8 000 | – | – |
| – Workers compensation review | 4 400 | 2 000 | 2 200 | 2 000 |
| Overseas KPMG firms: | | | | |
| – audit and review of financial reports | 133 919 | – | 24 908 | – |
| | 437 801 | 327 000 | 321 590 | 319 000 |

Other assurance services:

| | | | | |
|---------------------------------------------------------|-------|---|---|---|
| Assistance in documentation of procedures (KPMG Canada) | 9 294 | – | – | – |
| | 9 294 | – | – | – |

33.EARNINGS PER SHARE

Basic and diluted earnings per share

\$ \$

(0.1402) (0.0352)

The calculation of basic and diluted earnings per share at 30 June 2007 was based on the loss attributable to ordinary shareholders of \$11 517 000 (2006 loss: \$2 887 000) and a weighted average number of ordinary shares outstanding during the financial year ended 30 June 2007 of 82 168 938 (2006:81 984 814).

Earnings per share for continuing and discontinued operations

| | | |
|------------------------------|-----------------|-----------------|
| from continuing operations | (0.1457) | (0.0100) |
| from discontinued operations | 0.0055 | (0.0252) |
| | (0.1402) | (0.0352) |

Earnings per share for continuing and discontinued operations has been calculated using the same figures as earnings per share, except that the loss for the period used in the calculation is the loss relating to continuing operations of \$11 968 000 (2006: \$820 000) and the profit relating to discontinued operations of \$451 000 (2006: loss \$2 067 000).

The calculation of diluted earnings per share excludes 2 284 499 (2006: 2 146 195) share options because the effect of these options would have been anti dilutive.

| | Note | Consolidated | | Company | |
|-----------------------------------------------------------------|------|---------------|---------------|---------------|---------------|
| | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| 34(a) CASH AND CASH EQUIVALENTS | | | | | |
| Bank balances | | 2 346 | 5 728 | 809 | 4 938 |
| Call deposits | | — | 10 118 | — | 10 118 |
| Cash and cash equivalents in the statement of cash flows | | 2 346 | 15 846 | 809 | 15 056 |

34(b) RECONCILIATION OF CASH FLOWS FROM OPERATING ACTIVITIES

| | | | | | |
|--------------------------------------------------------------|-------|-----------------|--------------|-----------------|-----------------|
| (Loss)/profit for the period | | (11 517) | (2 887) | (9 702) | 54 831 |
| Adjustments for: | | | | | |
| Depreciation | 7(d) | 1 832 | 1 262 | 697 | 801 |
| Amortisation and impairment of intangible assets | | 3 478 | 2 735 | 2 582 | 2 252 |
| Impairment losses investments | | 114 | 382 | 266 | 382 |
| Impairment/(impairment reversal) of inter entity receivables | | — | — | 384 | (3 583) |
| Share of net loss from Associates | | — | 108 | — | — |
| Unrealised exchange losses | | 251 | — | 870 | — |
| Loss on sale of property, plant and equipment | | 109 | — | 62 | — |
| Gain on acquisition of OSG | 12(i) | (1 174) | — | — | — |
| Gain on disposal of controlled entities | | — | 4 667 | — | (50 333) |
| Gain on disposal of business | | — | (2 256) | — | (2 256) |
| Equity-settled share-based payment transactions | 9, 25 | 203 | — | 203 | — |
| | | (6 704) | 4 011 | (4 638) | 2 094 |
| Change in trade and other receivables | | 756 | 6 411 | 1 411 | (202) |
| Change in inventories | | 215 | 7 499 | (1 370) | 5 091 |
| Change in net investment in finance lease | | (355) | — | (355) | — |
| Change in other current assets | | (451) | — | (286) | (18) |
| Change in trade and other payables | | (4 130) | (11 833) | (771) | (12 139) |
| Change in provisions and employee benefits | | (1 439) | 4 083 | (2 630) | 3 707 |
| Change in other current liabilities | | (1 797) | (1 126) | 91 | (447) |
| Loans to controlled entities | | — | — | — | (19 012) |
| Change in income taxes | | (1 267) | (2 504) | (1 701) | (2 073) |
| Exchange rate changes on opening cash | | (54) | (81) | 37 | (10) |
| Net cash from operating activities | | (15 226) | 6 459 | (10 212) | (23 009) |

35. CONTINGENT LIABILITIES

Claim in respect of patent breaches — A third party has made a claim against a Keycorp distributor claiming that sale of Keycorp product in its market breaches patents that it currently holds. At the date of this report, management is in the process of evaluating the merits of this claim. A provision for legal costs and settlement of \$250 000 has been recorded at 30 June 2007.

36. SUBSEQUENT EVENTS

Since balance date the \$15 million Multi-Option Facility has been extended with the company's bankers, Westpac, to a review date of 30 September 2008, on improved terms and conditions.

The directors are unaware of any other matter or circumstance that has occurred since the end of the financial year that has significantly affected or may significantly affect the operations or the state of affairs of the group in future financial years.

NOTES TO THE FINANCIAL STATEMENTS continued

37. RELATED PARTIES

Key management personnel disclosures

(a) The following were key management personnel of the group at any time during the reporting period and unless otherwise indicated were key management personnel for the entire period:

Non Executive Directors

| | |
|----------------------|-----------------------------------------------------------------------------------------------------------------------|
| R. Bishop (Chairman) | Appointed as Chairman in June 2007. Director since January 2006. |
| M. Irving (Chairman) | Appointed as Chairman and Director in March 2001 (Stepped down as Chairman on 1 June 2007 and retired 1 July 2007) |
| B. Grisdale | Director since January 2001 |
| P. Jones | Director since August 2005 |
| M. Ibrahim | Director since January 2006 |
| C. Holgate | Director since January 2006 |

Executive Director

| | |
|-------------|--------------------------------------------------------------------------------------------------------|
| K. Carr | Appointed a director and Chief Executive Officer on 18 May 2007 |
| B. Thompson | Director since March 2001, appointed Chief Executive Officer in November 2001 (Retired on 17 May 2007) |

Executive Officers

| | |
|--------------|------------------------------------------------------------------------------------------------|
| J. Bonin | Executive Vice President Canada |
| R. Ganeson | General Manager, Strategic Market Development |
| R. Cusson | General Manager, Smartcards (appointed February 2006) |
| P. Herington | Chief Financial Officer (appointed 12 March 2007) |
| M. Knapman | Company Secretary and Legal Counsel |
| M. Ritter | General Manager, Keycorp Services (appointed 5 February 2007) |
| J. Stevens | General Manager, Human Resources (appointed 10 July 2006) |
| B. Johnson | Chief Financial Officer (resigned 16 February 2007) |
| P. DeRosse | General Manager, Keycorp Canada Inc (resigned 18 June 2007) |
| J. Esplin | Quality manager (ceased to be part of key management personnel on 1 July 2006) |
| M. Nagy | Manager Business Developments (ceased to be part of key management personnel on 1 July 2006) |
| M. Bryant | General Manager, Fox Technology (ceased to be part of key management personnel on 1 July 2006) |
| J. Smerek | General Manager, Innovations (ceased to be part of key management personnel on 1 July 2006) |

(b) The key management personnel compensation included in 'personnel expenses' (see note 9) is as follows:

| | Consolidated | | Company | |
|------------------------------|--------------|-----------|-----------|-----------|
| | 2007 | 2006 | 2007 | 2006 |
| | \$ | \$ | \$ | \$ |
| Short-term employee benefits | 3 292 958 | 3 874 456 | 2 158 875 | 2 514 305 |
| Other long term benefits | 23 406 | 59 574 | 8 748 | 21 122 |
| Post-employment benefits | 340 802 | 230 502 | 256 790 | 177 757 |
| Termination benefits | 707 094 | 448 673 | 520 000 | 202 558 |
| Share-based payments | 124 400 | 99 793 | 85 127 | 73 346 |
| | 4 488 660 | 4 712 998 | 3 029 540 | 2 989 088 |

Individual directors and executives compensation disclosures

Information regarding individual directors and executives compensation and some equity instruments disclosures as permitted by Corporations Regulations 2M.3.03 and 2M.6.04 are provided in the Remuneration Report section of the Directors' report on pages 9 to 21.

Apart from the details disclosed in this note, no director has entered into a material contract with the Company or the Group since the end of the previous financial year and there were no material contracts involving directors' interests existing at year-end.

Other key management personnel transactions

A number of key management persons, or their related parties, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities.

Some of these entities transacted with the Company or its subsidiaries in the reporting period. The terms and conditions of the transactions with management persons and their related parties were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to non-director related entities on an arm's length basis.

The aggregate amounts recognised during the year relating to key management personnel and their related parties were as follows:

| Key management person and their related parties | Transaction | Note | Transactions value year ended 30 June | | Balance outstanding as at 30 June | |
|-------------------------------------------------|---------------------|------|---------------------------------------|------------|-----------------------------------|------------|
| | | | 2007 \$000 | 2006 \$000 | 2007 \$000 | 2006 \$000 |
| M. Irving | Insurance | (i) | 831 | 988 | 555 | 988 |
| M. Ibrahim | Consulting Services | (ii) | 32 | — | 32 | — |

(i) During the current and prior year, Keycorp Limited engaged the services of Willis Group, a company in which Mr M Irving is a director of a related entity, providing insurance broking services on terms and conditions consistent with market rates for these types of services and were due and payable under normal payment terms.

(ii) During the year, Keycorp Limited engaged the consulting services of Mr M Ibrahim. The consulting services provided had terms and conditions which are consistent with market rates and were due and payable under normal payment terms.

Options and rights over equity instruments granted as compensation

The movement during the reporting period in the number of options over ordinary shares in Keycorp Limited held, directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

| | | Held at beginning of financial year | Granted as remuneration | Exercised | Lapsed | Held at end of financial year | Vested during year | Vested & Exercisable at 30 June 2007 |
|---------------------------|------|-------------------------------------|-------------------------|-----------|---------|-------------------------------|--------------------|--------------------------------------|
| Executive Director | | | | | | | | |
| Current | | | | | | | | |
| K. Carr | 2007 | — | — | — | — | — | — | — |
| Former | | | | | | | | |
| B. Thompson | 2007 | 200 000 | 200 000 | — | 400 000 | — | — | — |
| | 2006 | — | 200 000 | — | — | 200 000 | — | — |
| Executives | | | | | | | | |
| J. Bonin | 2007 | 151 000 | 120 000 | — | — | 271 000 | 12 500 | 51 000 |
| | 2006 | 51 000 | 100 000 | — | — | 151 000 | 25 500 | 38 500 |
| R. Cusson | 2007 | 7 000 | 120 000 | — | — | 127 000 | 7 000 | 7 000 |
| | 2006 | 44 000 | — | 37 000 | — | 7 000 | 22 000 | — |
| R. Ganeson | 2007 | 150 000 | 120 000 | — | — | 270 000 | 25 000 | 25 000 |
| | 2006 | 50 000 | 100 000 | — | — | 150 000 | — | — |
| M. Knapman | 2007 | 186 000 | — | — | 50 000 | 136 000 | 10 000 | 36 000 |
| | 2006 | 86 000 | 100 000 | — | — | 186 000 | 18 000 | 76 000 |
| J. Stevens | 2007 | — | 140 000 | — | — | 140 000 | — | — |
| A. Bradford | 2007 | — | — | — | — | — | — | — |
| (resigned Jan 2005) | 2006 | 28 400 | — | — | 10 000 | 18 400 | 9 200 | 14 400 |
| G. Duursma | 2007 | — | — | — | — | — | — | — |
| (resigned Feb 2006) | 2006 | 50 000 | — | — | — | 50 000 | 25 000 | 25 000 |
| T. Fletcher | 2007 | — | — | — | — | — | — | — |
| (resigned Jan 2006) | 2006 | 54 000 | — | 37 000 | 17 000 | — | — | — |
| K. Mouton | 2007 | — | — | — | — | — | — | — |
| (resigned Mar 2006) | 2006 | 50 000 | — | — | 50 000 | — | — | — |
| J. Esplin ⁽ⁱ⁾ | 2006 | 8 000 | 30 000 | — | — | 38 000 | 4 000 | 4 000 |
| D. Hatton ⁽ⁱⁱ⁾ | 2006 | 48 000 | — | — | 10 000 | 38 000 | 19 000 | 31 000 |
| B. Johnson | 2007 | 126 000 | 90 000 | — | 216 000 | — | — | — |
| (resigned Feb 2007) | 2006 | 40 000 | 100 000 | — | 14 000 | 126 000 | 13 000 | 19 000 |
| P. DeRosse | 2007 | 147 000 | — | — | 147 000 | — | — | — |
| (resigned June 2007) | 2006 | 84 000 | 100 000 | 37 000 | — | 147 000 | 22 000 | 40 000 |
| J. Smerek ⁽ⁱ⁾ | 2006 | 20 000 | — | — | — | 20 000 | 10 000 | 15 000 |

* Under the relevant plan rules, all options are exercisable once vested. Therefore, there are no vested and unexercisable options on issue.

The options were provided at no cost to the recipients.

(i) Ceased to be key management personnel from 1 July 2006.

(ii) Ceased to be key management personnel from 31 December 2005.

NOTES TO THE FINANCIAL STATEMENTS continued

37. RELATED PARTIES continued

Options and rights over equity instruments granted as compensation continued

The options granted to key management personnel during the current year are exercisable between one and three years (in respect of the three equal tranches) from grant date providing performance hurdles are attained. The performance hurdles require continuous employment through the vesting period in respect of each tranche and for the Keycorp Limited total shareholder return (TSR) to be greater than or equal to the S&P/ASX 300 Accumulation Index for twenty consecutive trading days on or after the first exercise date. Growth in TSR is defined as share price growth and dividends paid and reinvested on the ex-dividend date (adjusted for rights, bonus issues and any capital reconstructions).

The hurdle can be satisfied at any time on or after the first exercise date up to the last exercise date.

All options expire on the earlier their expiry date or termination of the individual's employment. In certain circumstances, at the discretion of management, employees included in an involuntary redundancy program are eligible to retain and exercise share options in accordance with the terms and conditions of the particular option issue.

The option hurdle prices are adjusted to reflect the terms of the issued options to certain specified executives and the effects of such adjustments are reflected in the option expense.

Shareholdings

Details of the movements in the number of ordinary shares in Keycorp Limited held during the financial year by each key management personnel, including their related parties, are set out below:

| | Year | Held at start of year | Purchases during year | Received on exercise of option | Sales | Held at end of year |
|---------------------------------|------|-----------------------|-----------------------|--------------------------------|-------|---------------------|
| Director | | | | | | |
| M. Irving | 2007 | 88 139 | 37 043 | — | — | 125 182 |
| | 2006 | 66 017 | 22 122 | — | — | 88 139 |
| M. Ibrahim | 2007 | — | 8 750 | — | — | 8 750 |
| J. Wood | 2007 | 765 713 | — | — | — | N/A |
| | 2006 | 765 713 | — | — | — | 765 713 |
| Executive Director | | | | | | |
| Current | | | | | | |
| K. Carr | 2007 | — | — | — | — | — |
| Former | | | | | | |
| B. Thompson | 2007 | 34 125 | 64 220 | — | — | 98 345 |
| | 2006 | 34 125 | — | — | — | 34 125 |
| Executives | | | | | | |
| R. Cusson ⁽ⁱ⁾ | 2007 | 62 400 | — | — | — | 62 400 |
| | 2006 | 10 400 | 15 000 | 37 000 | — | 62 400 |
| P. DeRosse | 2007 | 37 000 | — | — | — | N/A |
| | 2006 | — | — | 37 000 | — | — |
| D. Hatton ^{(ii), (iv)} | 2007 | 10 000 | — | — | — | N/A |
| | 2006 | — | 10 000 | — | — | 10 000 |
| B. Johnson ^(iv) | 2007 | 7 500 | — | — | — | N/A |
| | 2006 | 7 500 | — | — | — | 7 500 |
| J. Smerek ^(iv) | 2007 | 10 000 | — | — | — | N/A |
| | 2006 | — | 10 000 | — | — | 10 000 |
| A. Bradford ^(iv) | 2007 | 10 000 | — | — | — | N/A |
| | 2006 | 10 000 | — | — | — | 10 000 |
| T. Fletcher ^(iv) | 2007 | 61 000 | — | — | — | N/A |
| | 2006 | — | 24 000 | 37 000 | — | 61 000 |

(i) On 10 March 2006, 15 000 shares were awarded under the Deferred Employee Share Plan. This award is subject to the participant meeting service conditions and Keycorp attaining performance conditions. One-third of the shares vest in equal tranches on 13 March 2008, 13 March 2009 and 13 March 2010. These shares have an exercise price of \$nil and a fair value of \$1.47.

(ii) On 10 March 2006, 150 000 shares were awarded under the Deferred Employee Share Plan. This award is subject to the participant meeting service conditions and Keycorp attaining performance conditions. One-third of the shares vest in equal tranches on 13 March 2008, 13 March 2009 and 13 March 2010. These shares have an exercise price of \$nil and a fair value of \$1.47.

(iii) On 10 March 2006, 10 000 shares were awarded under the Deferred Employee Share Plan. This award is subject to the participant meeting service conditions and Keycorp attaining performance conditions. One-third of the shares vest in equal tranches on 13 March 2008, 13 March 2009 and 13 March 2010. These shares have an exercise price of \$nil and a fair value of \$1.47.

(iv) Ceased to be key management personnel before the end of the financial year.

Non Key management personnel disclosures**Identity of related parties**

The consolidated entity has a related party relationship with its subsidiaries (see note 19), associate (see note 18), and with its key management personnel (refer to disclosures for Key Management Personnel in this note).

Related party loans

Loans are made between the Company and wholly owned subsidiaries for capital purchases and to fund shortfalls in operating cash requirements. Loans outstanding between the Company and its controlled entities are non-interest bearing and payable on demand. Loans receivable have been recognised in the company's books as non current on the basis that the company does not intend to call the loan within the next 12 months.

| Entity | Note | Net outstanding balance receivable/(payable) at: | |
|---------------------------------------|------|--------------------------------------------------|---------------------|
| | | June 2007 \$ | June 2006 \$ |
| Wholly owned subsidiaries | | | |
| Receivables | | | |
| Keycorp Investments Pty Limited | | 40 359 679 | 40 189 350 |
| Keycorp Canada Inc. | | 11 824 774 | 6 404 941 |
| Keycorp Systems Limited | | 315 518 | 332 491 |
| Fox Technologies Pty Limited | | 5 765 618 | 4 030 953 |
| | | 58 265 589 | 50 957 735 |
| Impairment of Intercompany Receivable | | (10 713 091) | (10 713 091) |
| Net Receivables | 14 | 47 552 498 | 40 244 644 |
| Payables | | | |
| Keycorp USA Limited | | (58 470) | (25 268) |
| Keycorp Technologies Pty Limited | | (60 650) | (60 669) |
| Keycorp Payment Services Pty Limited | | (943 522) | (1 000 684) |
| Tillsmith Systems Inc. | | (142 285) | (142 285) |
| Keycorp (Asia) Limited | | (244 622) | (225 978) |
| E-Point Pty Limited | | (17 641 400) | (16 634 803) |
| | 23 | (19 090 949) | (18 089 687) |
| Other related party | | | |
| Telstra Corporation Limited | | — | — |

On 28 June 2002 Telstra Corporation Limited (previously the ultimate parent entity) notified Keycorp Limited that it no longer held a controlling interest in the company. Telstra Corporation Limited still retains a significant investment in Keycorp Limited and does have representation on the Keycorp Board of Directors and as such is classified as a related party. During the year, Telstra Corporation Limited has provided a guarantee of \$7 500 000 in relation to the Westpac Tranche 2 facility.

NOTES TO THE FINANCIAL STATEMENTS continued

37. RELATED PARTIES continued

Related party transactions

(a) During the financial year the Company has entered into transactions with the following related parties on normal commercial terms and conditions:

| Entity | Amount (paid)/received | | Details of transaction |
|--------------------------------------|------------------------|-----------------|-----------------------------------------------------------------|
| | June 2007 \$ | June 2006 \$ | |
| Wholly owned subsidiaries | | | |
| Keycorp Systems Limited | (556 937) | (865 530) | Management fees |
| Keycorp Canada Inc. | 3 669 139 | 5 423 623 | Sale of EFTPOS Terminal |
| Sale of EFTPOS terminals | — | (897 020) | Product development, materials and employee management services |
| Keycorp Payment Services Pty Limited | — | 15 253 756 | Sale of EFTPOS terminals |
| Keycorp USA Limited | (374 433) | (865 529) | Management fees |
| Keycorp Asia Limited | (205 082) | (472 889) | Management fees |
| Partly owned subsidiaries | | | |
| Fox Technology Pty Limited | — | 1 604 724 | Intercompany loan |
| Other related entity | | | |
| StepNexus | (428 463) | (598 447) | Purchase of product |

No dividends were received from subsidiaries or associates in the 2007 or 2006 financial year.

- (b) E-Point Limited, a wholly owned entity, has provided products and services to a wholly owned entity of Keycorp Limited, Keycorp Payment Services Pty Limited in the amount of \$5 780 547 (2006: \$10 803 000) at normal terms and conditions.
- (c) Keycorp Investments Pty Limited, a wholly owned entity, received interest income from a wholly owned entity of Keycorp Limited, Keycorp Canada Inc., in the amount of \$671 087 (2006: \$583 008). Interest is being charged on the loan at the rate of 10% per annum and is payable on demand.

38. FINANCIAL INSTRUMENTS

Exposure to credit, interest rate and currency risks arises in the normal course of the consolidated entity's business. Derivative financial instruments are used where necessary to hedge exposure to fluctuations in foreign exchange rates and interest rates.

Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The consolidated entity does not require collateral in respect of financial assets.

Investments are allowed only in liquid securities and only with major financial institutions. Similarly transactions involving derivative financial instruments are with the major financial institutions. Given their high credit ratings, management does not expect any counterparty to fail to meet its obligations.

At the balance sheet date there were no significant concentrations of credit risk of concern to management. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet.

Interest rate risk

The consolidated entity may enter into interest rate swaps where necessary to manage cash flow risks associated with interest rates on borrowings that are floating. Interest rate swaps allow the consolidated entity to swap floating rate borrowings into fixed rates. The consolidated entity did not hold any interest rate swaps at 30 June 2007 or at 30 June 2006.

38.FINANCIAL INSTRUMENTS continued

In respect of income earning financial assets and interest bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they reprice.

| Consolidated June 2007 | | | | | | | |
|----------------------------------|---------------------------------|----------------|------------------------------|---------------------------|--------------------|--------------------|----------------------------------|
| | Effective interest rate % | Total \$000 | 6 months or less \$000 | 6 – 12 months \$000 | 1–2 years \$000 | 2–5 years \$000 | More than five years \$000 |
| Financial Assets | | | | | | | |
| Cash and cash equivalents | 6.00% | 2 346 | 2 346 | — | — | — | — |
| Mezzanine note* | 7.25% | 5 355 | — | — | — | 5 355 | — |
| Net investment in finance lease* | 9.30% | 355 | 24 | 26 | 59 | 193 | 53 |
| | | 8 056 | 2 370 | 26 | 59 | 5 548 | 53 |
| Financial Liabilities | | | | | | | |
| Bank term loan | 10.04% | 11 500 | — | — | 11 500 | — | — |
| Finance lease liabilities | 8.79–10.08% | 2 995 | 502 | 512 | 614 | 1 367 | — |
| | | 14 495 | 502 | 512 | 12 114 | 1 367 | — |

| Consolidated June 2006 | | | | | | | |
|---------------------------|---------------------------------|----------------|------------------------------|---------------------------|--------------------|--------------------|----------------------------------|
| | Effective interest rate % | Total \$000 | 6 months or less \$000 | 6 – 12 months \$000 | 1–2 years \$000 | 2–5 years \$000 | More than five years \$000 |
| Financial Assets | | | | | | | |
| Cash and cash equivalents | 5.50% | 15 846 | 15 846 | — | — | — | — |
| Mezzanine note* | 7.03% | 5 296 | — | — | — | 5 296 | — |
| | | 21 142 | 15 846 | — | — | 5 296 | — |

* these assets/liabilities bear interest at a fixed rate

Foreign currency risk

Hedging of fluctuations in foreign currency

The consolidated entity is exposed to foreign currency risk on sales and purchases that are denominated in a currency other than the Australian Dollar (AUD). The currencies giving rise to this risk are primarily US dollars.

The consolidated entity's future cashflows in foreign currencies are predominantly hedged naturally, meaning the inflows of foreign currencies from customer sales are equally matched with outflows of foreign currency purchases. To manage the timing mismatches of these foreign currency movements, the consolidated entity enters into short-term (2 to 6 months) forward exchange contracts.

The consolidated entity does not qualify for hedge accounting on these forward exchange contracts and accordingly these are accounted for as trading instruments. Accordingly, changes in the fair value of forward exchange contracts are recognised in the income statement.

The consolidated entity did not hold any forward exchange contracts at 30 June 2007 or 30 June 2006.

NOTES TO THE FINANCIAL STATEMENTS continued

38.FINANCIAL INSTRUMENTS continued

Fair values

The fair values together with the carrying amounts shown on the balance sheet are as follows:

| | Consolidated | | Consolidated | |
|----------------------------------|-------------------------------------|------------------------------------|-------------------------------------|------------------------------------|
| | Carrying amount 2007 \$000 | Net Fair value 2007 \$000 | Carrying amount 2006 \$000 | Net Fair value 2006 \$000 |
| Financial assets | | | | |
| Cash and cash equivalents | 2 346 | 2 346 | 15 846 | 15 846 |
| Mezzanine notes | 5 355 | 4 713 | 5 295 | 4 340 |
| Net investment in finance lease | 355 | 260 | — | — |
| Trade and Other receivables | 17 816 | 17 816 | 13 285 | 13 285 |
| | 25 872 | 25 135 | 34 426 | 33 471 |
| Financial liabilities | | | | |
| Trade and other payables | 14 428 | 14 428 | 13 761 | 13 761 |
| Bank term loan | 11 500 | 11 500 | — | — |
| Finance lease liabilities | 2 995 | 2 441 | — | — |
| Balance at end of financial year | 28 923 | 28 369 | 13 761 | 13 761 |

The methods and assumptions are used to determine the fair values of financial assets and liabilities

Cash and cash equivalents, short term investments

The carrying amount approximates fair value because of their short term to maturity.

Mezzanine notes

Fair value is calculated based on discounted expected future principal and interest cash flows.

Bank term loan

The carrying amount approximates fair value because of their short term to maturity.

Finance lease liabilities

Fair value is calculated based on a discounted expected future principal and interest cash flows using an effective interest rate of 8.79%–10.03%.

Trade and other receivables/payables

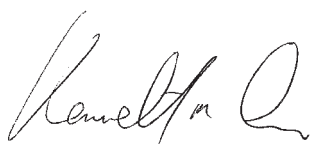
For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value.

All other receivables/payables are discounted to determine the fair value.

DIRECTORS' DECLARATION

- 1 In the opinion of the directors of Keycorp Limited ('the Company'):
 - (a) the financial statements and notes and the remuneration disclosures that are contained in sections marked 'audited' of the Remuneration Report set out on pages 9 to 70 of the Directors' Report, are in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the Company and the consolidated entity's financial position as at 30 June 2007 and of their performance, for the financial year ended on that date; and
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001;
 - (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2(a);
 - (c) the remuneration disclosures that are contained in sections marked 'audited' of the Remuneration Report comply with Australian Accounting Standard AASB 124 Related Party Disclosures; and
 - (d) 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 There are reasonable grounds to believe that the Company and the group entities identified in Note 19 will be able to meet any obligations or liabilities to which they are or may become subject to by virtue of the Deed of Cross Guarantee between the Company and those group entities pursuant to ASIC Class Order 98/1418.
- 3 The directors have been given the declarations required by Section 295A of the *Corporations Act 2001* from the chief executive officer and chief financial officer for the financial year ended 30 June 2007.

Signed in accordance with a resolution of the directors:



K.M. Carr
Director

Sydney 30 August 2007



Independent auditor's report to the members of Keycorp Limited

Report on the financial report and AASB 124 remuneration disclosures contained in the directors' report

We have audited the accompanying financial report of Keycorp Limited (the Company), which comprises the balance sheets as at 30 June 2007, and the income statements, statements of recognised income and expense and cash flow statements for the year ended on that date, a description of significant accounting policies and other explanatory notes 1 to 38 and the directors' declaration of 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.

As permitted by the *Corporations Regulations 2001*, the Company has disclosed information about the remuneration of directors and executives (remuneration disclosures), required by Australian Accounting Standard AASB 124 *Related Party Disclosures*, in sections identified as audited in the "remuneration report" in the directors' report and not in the financial report. We have audited these remuneration disclosures.

Directors' responsibility for the financial report and the AASB 124 remuneration disclosures contained in the directors' report

The directors of the Company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the financial report that is 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. In note 2(a), the directors also state, in accordance with Australian Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial report of the consolidated entity, comprising the financial statements and notes, complies with International Financial Reporting Standards but that the financial report of the Company does not comply.

The directors of the Company are also responsible for the remuneration disclosures contained in the directors' report.

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. These Auditing Standards require that we 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. Our responsibility is also to express an opinion on the remuneration disclosures contained in the directors' report based on our audit.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report and the remuneration disclosures contained in the directors' report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report and the remuneration disclosures contained in the directors' report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report and the remuneration disclosures contained in the directors' 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 entity's internal control.



Auditor's responsibility (continued)

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 and the remuneration disclosures contained in the directors' report.

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001* and Australian Accounting Standards (including the Australian Accounting Interpretations), a view which is consistent with our understanding of the Company's and the consolidated entity's financial position and of their performance and whether the remuneration disclosures are in accordance with Australian Accounting Standard AASB 124.

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

Auditor's opinion on the financial report

In our opinion:

(a) the financial report of Keycorp Limited is in accordance with the *Corporations Act 2001*, including:

- (i) giving a true and fair view of the Company's and the consolidated entity's financial position as at 30 June 2007 and of their performance for the year ended on that date; and
- (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001.

(b) the financial report of the consolidated entity also complies with International Financial Reporting Standards as disclosed in note 2(a).

Auditor's opinion on AASB 124 remuneration disclosures contained in the directors' report

In our opinion the remuneration disclosures that are contained in the sections identified as audited in the "remuneration report" in the directors' report comply with Australian Accounting Standard AASB 124 *Related Party Disclosures*.

KPMG

John Wigglesworth
Partner

Sydney, 30 August 2007

SHAREHOLDERS INFORMATION

FOR THE YEAR ENDED 30 JUNE 2007

Additional information required by the Listing Rules of ASX Limited and not shown elsewhere in this report is as follows. The information is applicable as at 28 August 2007.

20 LARGEST SHAREHOLDERS

| Shareholders | Ordinary shares held | % of issued shares |
|-------------------------------------------------------------------------------|----------------------|--------------------|
| Telstra Corporation Limited | 39,082,000 | 47.42 |
| Bernard Owen Stephens, Mrs Erin Josephine Stephens, Stephens Group S/F A/C | 1,893,000 | 2.30 |
| Mr Anthony Edward Collins, Mrs Andrea Claudia Collins, Collins Family S/F A/C | 1,707,900 | 2.07 |
| Rubicon Nominees Pty Ltd | 1,360,859 | 1.65 |
| HSBC Custody Nominees (Australia) Limited | 1,282,840 | 1.56 |
| Allundy Pty Ltd | 1,107,000 | 1.34 |
| Mr Anthony Edward Collins, Mrs Andrea Claudia Collins, Collins Family S/F A/C | 958,500 | 1.16 |
| Ashabia Pty Ltd Superannuation Fund A/c | 900,000 | 1.09 |
| Jemgum Holdings Pty Ltd | 900,000 | 1.09 |
| Mr John William Wood | 760,486 | 0.92 |
| Citicorp Nominees Pty Limited | 689,839 | 0.84 |
| Stannard Bros Holdings Pty Ltd | 390,016 | 0.47 |
| Condor Capital Pty Ltd, The Masson Family A/C | 324,000 | 0.39 |
| Bridgecall Pty Limited | 323,056 | 0.39 |
| Mr Graham Charles Hook | 300,000 | 0.36 |
| Speliza Investments Pty Ltd, Greysmed P/L Super Fund A/C | 298,494 | 0.36 |
| Davslav Nominees Pty Ltd, Abraham Super Fund A/C | 289,654 | 0.35 |
| UBS Wealth Management Australia Nominees Pty Ltd | 261,000 | 0.32 |
| Mr Sondal Mehmet Bensen | 251,615 | 0.31 |
| Starvor Pty Limited | 250,000 | 0.30 |
| Total | 53,330,259 | 64.69 |

DISTRIBUTION OF ORDINARY SHARES

| Range | No. of holders | Ordinary shares held | % of issued shares |
|------------------|-----------------------|-----------------------------|---------------------------|
| 1 – 1,000 * | 1,339 | 769,554 | 0.93 |
| 1,001 – 5,000 | 1,406 | 3,899,440 | 4.73 |
| 5,001 – 10,000 | 424 | 3,330,492 | 4.04 |
| 10,001 – 100,000 | 492 | 15,161,395 | 18.40 |
| 100,001 and over | 59 | 59,263,057 | 71.90 |
| Total | 3,720 | 82,423,938 | 100.00 |

* 1,655 shareholders hold less than a marketable parcel of shares
(market value less than \$500 or 1,819 shares based on a market price of \$0.275).

SUBSTANTIAL SHAREHOLDERS

The following shareholders have notified that they are substantial shareholders:

| Shareholders | Ordinary shares held | % of issued shares |
|-----------------------------|-----------------------------|---------------------------|
| Telstra Corporation Limited | 39,082,000 | 47.42% |

ON-MARKET BUY-BACK

There is no current on-market buyback.

VOTING RIGHTS

On a shown of hands, each shareholder present in person, each proxy who is not a shareholder and each duly appointed corporate representative who is not a shareholder shall have one vote.

On a poll, each shareholder shall have one vote for each fully paid share held and each person present as a proxy, and each duly appointed corporate representative, shall have one vote for each fully paid share held by the shareholder that the person represents.

CORPORATE DIRECTORY

KEYCORP LIMITED

ABN 61 002 519 986

REGISTERED OFFICE & HEAD OFFICE

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Chatswood NSW 2067
Australia

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Web: www.keycorp.net

AUDITOR

KPMG

KEYCORP SHARE REGISTRY

Computershare Investor Services Pty Limited
Level 2 60 Carrington Street
Sydney NSW 2000

GPO Box 2975
Melbourne Vic 3001
Australia

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Facsimile: +61 3 9473 2500

The notice of annual general meeting and form of proxy are presented separately.

KEYCORP LIMITED
ANNUAL REPORT 2007