SOLBEC
PHARMACEUTICALS LTD

ABN 85 061 289 218

ANNUAL FINANCIAL REPORT 2006

SOLBEC PHARMACEUTICALS LTD

Contents

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Corporate Information

Directors	:	Anthony Kiernan - LL.B, Chairman Graeme Howie - Managing Director Stephen J Carter FAIM, MRACI, Director Michael Grant, Director Professor John Papadimitriou, AM, OStJ, Director
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Bankers	:	National Australia Bank Limited Unit 7, 51 Dowd Street WELSHPOOL WA 6106
Share Registry	:	Computershare Registry Services Pty Ltd Level 2, Reserve Bank Building 45 St George's Terrace PERTH WA 6000 Telephone: (08) 9323 2000 Facsimile: (08) 9323 2033
Australian Stock Exchange	:	Home Branch: Perth Code: SBP
ABN	:	85 061 289 218

Chairman's Report

I am pleased to report to shareholders that Solbec continues to make substantial progress in the development of its lead compound Coramsine®. In particular:

- Solbec has now completed the Phase I/IIA cancer clinical trials;
- Solbec made application for and received Orphan Drug Designation for Coramsine® from the USA Food and Drug Administration (FDA) in both renal cell carcinoma and malignant melanoma;
- Solbec has compiled an Investigational New Drug Application ("IND") data package to pre-IND stage with the FDA;
- Solbec has commenced recruitment of patients for the Phase II cancer clinical trials in Australia.

The Orphan Drug status granted by the FDA allows Solbec to pursue its regulatory strategy of compressing drug development time frames as much as possible.

Completion and evaluation of the Phase I/IIA clinical trials was significant for the Company and led to the decision to move into Phase II clinical trials in renal cell carcinoma and malignant melanoma and for which recruitment for the renal cell trial has commenced.

It is proposed that Solbec will conduct a thorough scientific review of the available data at the mid point of the Australian trials (around 20 patients) as part of the process of selecting the most appropriate cancer indication(s) with which to move forward in trials in the USA.

Solbec continues to place great emphasis on its intellectual property portfolio and amongst other areas now enjoys patent protection for:

- the method of production;
- receptor mediated uptake pathway;
- composition of matter (formulation);
- use patents in cancer and other diseases including synergy with other cytotoxic drugs in combination therapy.

It is also pleasing to report that Solbec's USA based patent counsel has confirmed a clear freedom to operate for Coramsine® in the USA.

A detailed analysis of the year in review and the current status of the clinical development of Coramsine® is set out in the Review of Operations in this Annual Report.

Management at Solbec continues to be dedicated to the task at hand and it is entirely appropriate on behalf of all Directors and shareholders to thank them for their efforts throughout the year.

Stephen Carter stepped down as Managing Director of Solbec after many years and I would like thank him for his contribution. Stephen remains a Director of the Group.

To our shareholders, your continued support is highly valued.

Yours sincerely

Tony Kiernan
Chairman

Review of Operations

Overview

Solbec's primary focus throughout the year has centred on the further clinical development of its lead compound Coramsine®.

In last year's Annual Report, Solbec set out its objectives for 2005/06 which included:

- completion of the Phase I/IIA cancer clinical trial;
- the filing of an Investigational New Drug application (IND) to pre-IND stage;
- applying for Orphan Drug Designation for Coramsine® from the U.S. Food and Drug Administration (FDA); and
- the commencing of Phase II cancer clinical trials in Australia.

Solbec has met these objectives.

The results from the Phase I/IIA dose escalating trial confirmed that Coramsine® was safe for use and well tolerated in patients with advanced cancers. Preliminary efficacy (i.e. the drug actually works) was also noted in the trial in three of the eight patients who received a full 6 cycles of Coramsine® treatment. These results were presented at the 2006 American Society of Clinical Oncologists conference in Atlanta Georgia and published in the Journal of Clinical Oncology June 2006.

In August 2005 the U.S. FDA reviewed Coramsine's® preclinical data package and confirmed that the data supports Solbec's intention to proceed directly to Phase II clinical trials. In addition to this, the FDA granted Coramsine® orphan drug status for both renal cell carcinoma (November 2005) and malignant melanoma (February 2006). These advices from the FDA allow Solbec to pursue its regulatory strategy to compress drug development timeframes as much as practicably possible.

Following completion and evaluation of the Phase I/IIA cancer clinical trials, Solbec resolved to commission the Phase II trials targeting renal cell carcinoma (stage III/IV) and malignant melanoma (stage III/IV). Several Ethics Committee approvals have been received from a number of Australian trial sites and the Australian Phase II clinical trials are set to commence recruitment. At the mid-point of the Australian trials (20 patients), a thorough scientific review of the available data will be undertaken aimed at selecting the best indication(s) with which to move forward in the U.S.

During the year Solbec had a number of patents granted in various jurisdictions (including the USA). Reflecting the further development of Coramsine®, Solbec, in November 2005, filed for further patent protection for the use of Coramsine® in combination with other commonly used chemotherapeutic agents. Using Coramsine® in combination with other chemotherapeutic agents potentially provides substantial scope and opportunity for the commercialisation of the drug.

Patent protection now includes:

- the method of production;
- receptor mediated uptake pathway;
- composition of matter (formulation) and
- "use" patents in cancer and other diseases including synergy with other cytotoxic drugs in combination chemotherapy.

Solbec's USA based patent counsel confirmed the Company's monopoly rights in the glycoalkaloid arena with a clear freedom to operate report for Coramsine® in the USA market.

In December 2005 Solbec was awarded a grant of $2,260,000 under the Australian Government's Commercial Ready Grant Scheme for its Australian Phase II trials and a further $23,000 from the Western Australian Government. These grants provide non-dilutive funding for the Phase II Australian trials on a dollar for dollar basis. In addition to securing grant funding, the Company raised $933,300 from its existing shareholders by way of a share purchase plan and a further $1,298,491 in August 2006 as a private placement.

Review of Operations (Cont.)

Coramsine and Cancer

The pre-clinical studies, compassionate use (through the Therapeutic Goods Administration's Special Access Scheme) and the Phase I clinical trial have shown Coramsine® to have potential activity against a range of cancers in man. Studies have demonstrated that Coramsine® affects cancer cells using a previously undescribed Mode of Action in that it selectively enters the cancer cells causing those cells to burst. This process has been named "Oncotic Cell Death". Solbec considers that this Mode of Action potentially enables the cancer cells to be directly targeted in the body and in the process may overcome the problems associated with cancer therapy resistance commonly seen with other chemotherapeutic agents. As a result of the cancer cell resistance mechanisms, there currently exists no effective chemotherapeutic agent against a number of late stage cancers such as melanoma and kidney cancer. This leads Solbec to believe there is an unmet market for an agent which is able to counter the problem of cancer cell resistance. Coramsine® with its unique Mode of Action has, in the opinion of the Company, the potential to do this for a broad range of cancer types that have poor prognoses.

Studies have also shown that in some cancer patients treated with Coramsine®, tumours which did not completely regress, remained stable for in excess of 2½ years. Further studies demonstrated that administration of Coramsine® increases antigen presentation and, unlike many cancer treatments, Coramsine® has no adverse effect on the immune system. Further animal studies are being undertaken at the University of Western Australia testing for synergy between immune stimulators in arresting further tumour development after the cessation of treatment.

Coramsine - Other Applications

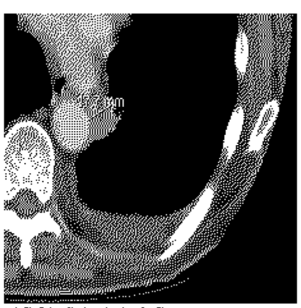
The solasonine/solamargine glycoalkaloids contained in Coramsine® represent one technology platform; however several distinct and independent applications potentially exist and may form the basis of ongoing clinical investigations. Aside from anti-cancer therapy, applications for Coramsine® may include as a possible treatment for certain inflammatory conditions such as psoriasis, palliative care (including in mesothelioma), a cancer diagnostic and certain potential animal health applications.

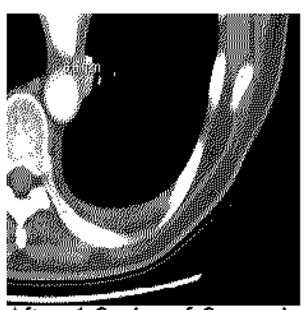
Coramsine Clinical Development

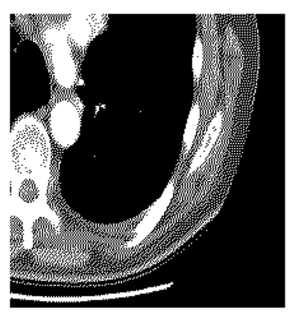
Phase I Cancer Clinical Trials

During the latter half of 2005 Solbec completed an escalating dose Phase I/IIA clinical trial with Coramsine®. Patients were grouped into 2-hour, 4-hour and 24-hour infusion groups. These trials produced data showing Coramsine® is safe for use and well tolerated in patients with advanced cancers. During the trials, three of the eight patients who received a full 6 cycles of Coramsine® treatment showed objective clinical responses (clinically significant reduction in tumour volume as measured by RECIST evaluation criteria, see scans below). These results were presented at ASCO 2006 in Atlanta and published in the Journal of Clinical Oncology June 06.

Phase I/IIa - Non Small Cell Lung Cancer Patient Receiving Coramsine®
These three CT scans were taken from a patient in the Phase I/IIa Coramsine® cancer clinical trial. They show a cancerous mass in the chest cavity adjacent to the aorta (the grey circle). After two courses (12 cycles) of Coramsine® therapy the mass is almost completely eradicated.


NSCLC Initial Scan

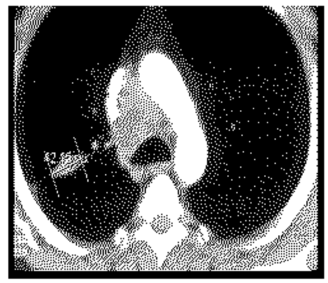

After 6 Cycles of Coramsine®


After 12 Cycles

Review of Operations (Cont.)

Phase I/IIa - Renal Cell Carcinoma Patient Receiving Coramsine®
These two CT scans were from another patient in the Phase I/IIa Coramsine® cancer clinical trial. They show a secondary renal cell carcinoma mass in the lung. After one course (6 cycles) of Coramsine® therapy the mass has greatly reduced in size.


mRCC Initial Scan


After 6 cycles of Coramsine®

Phase II Cancer Clinical Trials

In February 2006 Solbec received a positive written response from the U.S. Food and Drug Administration (FDA) in respect of the pre-IND (Investigational New Drug) submission for Coramsine® in the treatment of advanced solid tumours. The FDA reviewed Coramsine's® pre-clinical and clinical dossier and confirmed that Coramsine® was suitable to move into Phase II cancer clinical trials subject to the FDA's acceptance of Coramsine's® full IND application.

Following on from the successful completion of Coramsine's® Phase I cancer clinical trial and the advice from the FDA, Solbec made the decision to commission Phase II trials in Australia in renal cell carcinoma and malignant melanoma. The clinical trial material for the Phase II trials has been manufactured at Patheon in the United Kingdom. In early 2006 the Company selected the Principal Investigators for the Phase II trials and began identifying suitable trial sites. Solbec, at the date of this Report, has identified 10 hospitals for the renal cell carcinoma trial and 7 hospitals for the malignant melanoma trial.

Several Ethics Committee approvals have now been received from a number of Australian trial sites and the Phase II clinical trials are set to commence recruitment.

At the mid point of the Australian trials (20 patients), a thorough scientific review of the available data will be undertaken aimed at selecting the best indication(s) with which to move forward in the United States.

The Phase II trials will be co-funded on a dollar-for-dollar basis by a $2,260,000 Australian Government Commercial Ready grant awarded to Solbec in December 2005.

Manufacturing/Operations

Under a manufacturing and quality agreement with Patheon, an FDA approved facility in the United Kingdom, the clinical trial material for the Phase II trials has been manufactured to Good Manufacturing Practices (GMP) specifications. Following an audit of Solbec's Perth based facility by the Australian Therapeutic Goods Administration, the facility was given GMP accreditation for precursor compound manufacturing and the GMP testing and release of clinical trial material. As such, Solbec may now use its own facility to test and release the clinical trial material received back from Patheon for the Phase II trials.

Horticultural Operations

Solbec meets its need for glycoalkaloid raw materials from its *Solanum* field growing operation located at Baldivis 40 km south of Perth. Throughout the year a mulching program and other changes to operational aspects of the horticultural facility have resulted in an increased fruit yield and a decreased reliance on chemical spraying. During the peak growing time earlier this year, over 10kg wet weight of fruit was harvested from one plant.

Review of Operations (Cont.)

Intellectual Property

Solbec constantly strives to secure further levels of protection for its glycoalkaloid technology platform. Along with the seven patent families already in various stages of examination or granted, in November 2005 Solbec filed a patent application entitled: "*Glycoalkaloid and Chemotherapeutic agent combinations and various uses thereof*". This filing seeks to protect certain synergies reported with the use of several well accepted cancer chemotherapeutic compounds in combination with Coramsine®.

The current status of Solbec's glycoalkaloid technology patent portfolio is provided in the table below:

Coverage	Application number	Date of filing	Status
Patent family 1: Glycoalkaloids			
Australia	654474	18-Jan-91	Granted
Canada	2,073,855	18-Jan-91	Under examination
France	91901984.4	18-Jan-91	Granted
Germany	91901984.4	18-Jan-91	Granted
Japan	502586/91	18-Jan-91	Granted
South Korea	701699/1992	18-Jan-91	Granted
UK	91901984.4	18-Jan-91	Granted
USA	18/743,671	18-Jan-91	Granted
Patent family 2: Medicinal Compositions and their Method of Preparation			
Australia	779512	4-Oct-00	Granted
Canada	2,369,272	4-Oct-00	Pending awaiting examination
Europe	913972.6	4-Oct-00	Pending under examination
USA	10/752,095	4-Oct-00	Pending under examination
Patent family 3: Rhamnose Binding Protein			
Australia	2003202322	7-Feb-03	Granted
Canada	2,475,066	7-Feb-03	Pending examination requested
China	3805513.9	7-Feb-03	Pending under examination
Europe	3700718.4	7-Feb-03	Pending under examination
Hong Kong	6100115.4	7-Feb-03	Pending
India	2003202322	7-Feb-03	Pending
Japan	2003-566050	7-Feb-03	Pending examination requested
New Zealand	534485	7-Feb-03	Pending under examination
USA	6930171	7-Feb-03	Granted
USA	11/071770	3-Mar-05	Pending yet to be examined
Patent family 4: Method for the Separation of Triglycoalkaloids			
Australia	2003233261	13-Jun-03	Pending awaiting examination
Canada	2489682	13-Jun-03	Pending awaiting examination
Europe	3727026.1	13-Jun-03	Pending awaiting examination
New Zealand	537268	13-Jun-03	Granted
USA	6,984,725	13-Jun-03	Granted
Patent family 5: Glycoalkaloids Compositions & Various Uses Thereof			
Australia	2003238544	24-Jun-03	Pending awaiting examination
Canada	2489675	24-Jun-03	Pending examination requested
Europe	03732115.5	24-Jun-03	Pending awaiting examination
New Zealand	537267	24-Jun-03	Pending under examination
USA	11/143043	2-Jun-05	Pending yet to be examined

Review of Operations (Cont.)

Patent family 6: Methods of Modulating IL-6			
Australia	2004204261	15-Jan-04	Pending awaiting examination
Canada	2516398	15-Jan-04	Pending examination requested
Europe	04702261.1	15-Jan-04	Pending awaiting examination
New Zealand	541774	15-Jan-04	Pending awaiting examination
USA	10/758939	15-Jan-04	Pending awaiting examination
Patent family 7: Glycoalkaloid and TLR agonist combinations and various uses thereof			
All PCT member states	PCT/AU2006/000269	1-Mar-06	Pending awaiting ISR
Patent family 8: Glycoalkaloid and Chemotherapeutic agent combinations and various uses thereof			
Australia	2005906644	29-Nov-05	Pending

Communication and Investor Relations

The results of Solbec's Phase I/IIa cancer clinical trial were presented by Professor Millward the trial's Principal Investigator at ASCO 2006 in Atlanta Gerogia and published in the Journal of Clinical Oncology in 2006. As such, this presentation was an important factor in developing awareness in the world's specialist medical and scientific community of Coramsine's® clinical progress.

Solbec also updated potential licensing partners on the Phase I results at AusBIO in Perth in November 2005, Boston BioRelationships and BIO in Chicago in April 2006. Also throughout the year Solbec has participated in a number of Australian and International roadshows to present the Company to potential investors.

Corporate

In May 2006 Dr Graeme Howie was appointed Managing Director following the resignation of Stephen Carter as Managing Director. Mr Carter continues as a director of the Company and provides consultancy services to Solbec.

Dr Howie brings to Solbec a wealth of experience from his 28 years in executive positions with international pharmaceutical companies including Delta West, Upjohn, Pharmacia and Pfizer.

In July 2006 Dr David Hung resigned as a director to concentrate on his USA medical and drug development activities.

During the year Solbec appointed Dr David Sparling as General Manager. Dr Sparling had been with Solbec since July 2005 in the role of Business Development Manager.

FINANCIAL REVIEW

Operating Results for the Year

Solbec made a net loss of $1,703,301 during the financial year, after taking into account $654,068 received in research and development grants. $1,253,558 was incurred on direct research and development and a further $927,144 was incurred on salaries and consultants fees, substantially associated with research and development. Administration and other expenses amounted to $815,478. Solbec received $290,587 in tax refunds based on research and development expenditure in the previous year.

REVIEW OF FINANCIAL CONDITION

Capital Structure

In an effort to improve the capital structure of the Company, Solbec made an offer during the year to all holders of listed options to cancel those options in consideration for the issue of new shares. The offered ratio was the cancellation of 7 options for every 1 new fully paid share in Solbec. The option cancellation offer closed in December 2005 well subscribed with over 88% take up on the offer. In all, 133,482,631 options were cancelled.

Review of Operations (Cont.)

Treasury Policy

The Group's treasury function is managed by the Managing Director. The majority of the company's funds are invested in National Bank term deposits with an interest rate at the end of the year of 5.8%.

Cash from Operations

Solbec does not generate cash from its operations other than interest. It relies on government grants and on capital raising or debt financing to fund its drug development. Cash during the year was used in operating activities principally in clinical trial costs and payments to employees

In mid November 2005 Solbec announced that it had secured A$ 23,000 in grant funding from the Western Australian Government's Capital Access Scheme. This objective of this funding was such that it was to be utilised to secure further funding for the Company. Solbec used this Capital Access funding to pursue a Commercial Ready grant from the Australian Government. In late November Solbec was pleased to announce that it had secured A$ 2.26M under the Australian Government's Commercial Ready Grant Scheme. This money will provide non-dilutive funding for these Australian trials on a dollar for dollar basis.

In addition to securing A$ 2.28M in grant funding, the Company has throughout the year raised $930,300 from its existing shareholders by way of a share purchase plan which closed in May 2006. In August this year the Company raised $1,298,491 by way of a private placement to sophisticated investors.

Liquidity and Funding

The Company has a $5 million equity standby facility from Cornell Capital Partners in the USA. To utilise the facility, Solbec issues a notice to Cornell Capital pursuant to which Cornell Capital is required to subscribe for shares in amounts of no more than $100,000 at any one time based on the price of Solbec shares trading (on ASX) in the 10 day period following a notice draw down. At balance date the facility was unused.

Segment Performance

The continued strength of the resources sector throughout 2005/06 has overshadowed Australia's biotechnology sector. The June 2006 Intersuisse Biotechnology Index reported that Australian biotechnology stocks rose 10.1 per cent in 2005/06, failing to match the All Ordinaries Index, which rose 19 per cent. This average growth was influenced by a number of extremely strong rises from several individual biotech companies. This must be put into perspective however, since 1 July 2005, 45 biotech companies showed price rises and 34 fell. Looking to Solbec's performance throughout the year, despite making good ground in terms of Coramsine's® clinical development (as detailed herein), the Company's share price remained soft.

Corporate Governance Statement

CORPORATE GOVERNANCE STATEMENT

Corporate Governance is a matter of high importance in the Company and is undertaken with due regard to all of the Company's stakeholders and its role in the community. The key corporate governance practices of the Company are summarised below.

1. Board of Directors

1.1 Role of the Board and Management

The Board represents shareholders' interests in the business and seeks to optimise medium to long-term financial gains for shareholders. The Board believes that this focus will ultimately result in the interests of all stakeholders being appropriately addressed when making business decisions.

The Board is responsible for ensuring that the Company is managed in such a way to best achieve this desired result. Given the current size and operations of the business, the Board currently undertakes an active, not passive role.

The Board is responsible for evaluating and setting the strategic directions for the Company, establishing goals for management and monitoring the achievement of these goals. The Managing Director is responsible to the Board for the day-to-day management of the Company.

The Board has sole responsibility for the following:

- Appointing and removing the Managing Director and approving senior executive remuneration;
- Determining the strategic direction of the Company and measuring performance of management against approved strategies;
- Reviewing the adequacy of resources for management to properly carry out approved strategies and business plans;
- Adopting operating and capital expenditure budgets at the commencement of each financial year and monitoring progress against them;
- Monitoring capital and cash flow requirements;
- Approving and monitoring financial and other reporting to regulatory bodies, shareholders and other organisations;
- Determining that satisfactory arrangements are in place for auditing the Company's financial affairs; and
- Ensuring that policies and compliance systems consistent with the Company's objectives, external best practice and the Company's size and scope of operations are in place and that the Company and its officers act legally, ethically and responsibly on all matters.

The Board's role and the Company's corporate governance practices are reviewed and amended as required.

1.2 Composition of the Board and New Appointments

The Company currently has the following Board members:

Anthony Kiernan	Chairman (Non-executive)
Stephen Carter	Non-executive
Michael Grant	Non- executive
Professor John Papadimitriou	Non-executive
Dr Graeme Howie	Managing Director

The Company's Constitution provides that the number of directors shall not be less than three (3) and not more than nine (9). There is no requirement for any share holding qualification.

Corporate Governance Statement (Cont.)

The membership of the Board and its activities are subject to periodic review. The criteria for determining the identification and appointment of a suitable candidate for the Board shall include quality of the individual, background of experience and achievement, compatibility with other Board members, credibility within the Company's scope of activities, intellectual ability to contribute to the Board's duties and physical ability to undertake Board's duties and responsibilities.

Directors are initially appointed by the full Board subject to election by shareholders at the next annual general meeting. Under the Company's Constitution the tenure of directors (other than the Managing Director) is subject to reappointment by shareholders not later than the third anniversary following his last appointment. Subject to the requirements of the Corporations Act 2001, the Board does not subscribe to the principle of retirement age and there is no maximum period of service as a director. A Managing Director may be appointed for any period and on any terms the directors think fit and, subject to the terms of any agreement entered into, the Board may revoke any appointment.

1.3 Committees of the Board

The Board considers that the Company is not currently of a size, nor are its affairs of such complexity to justify the formation of separate or special committees at this time other than an Audit Committee and a Scientific Review Committee. The Board as a whole is able to address the governance aspects of the full scope of the Company's activities and to ensure that it adheres to appropriate ethical standards.

The Audit committee comprises Messrs Kiernan and Grant who are non- executive.

The Scientific Review Committee has matters referred to it from time to time.

The full Board currently holds meetings at such times as may be necessary to address any general or specific matters as required. The Chairman and Managing Director are in regular contact discussing Company issues and the Chairman has ready and full access at all times to the other directors.

If the Company's activities increase in size, scope and nature, the appointment of separate or special committees will be reviewed by the Board and implemented if appropriate.

1.4 Conflicts of Interest

In accordance with the Corporations Act and the Company's Constitution, directors must keep the Board advised, on an ongoing basis, of any interest that could potentially conflict with those of the Company. Where the Board believes that a significant conflict exists, the director concerned would not receive the relevant board papers and would not be present at the meeting whilst the item is considered or when any appropriate vote was taken.

1.5 Independent Professional Advice

The Board has determined that individual directors have the right in connection with their duties and responsibilities as directors, to seek independent professional advice at the Company's expense. The engagement of an outside adviser is generally subject to prior approval of the Chairman and this will not be withheld unreasonably. If the matter is urgent or the relevant director does not wish to refer the matter to the Chairman prior to seeking outside advice, the director is entitled to do so without prior referral. If appropriate, any advice so received will be made available to all Board members.

2. Ethical Standards

The Board acknowledges the need for continued maintenance of a professional standard of corporate governance practice and ethical conduct by all directors and employees of the Company.

Corporate Governance Statement (Cont.)

2.1 Code of Conduct for Directors

All directors are expected and required to comply with the following code:

The principles of the code are:

- A director must act honestly, in good faith and in the best interests of the company as a whole.
- A director has a duty to use due care and diligence in fulfilling the functions of office and exercising the powers attached to that office.
- A director must use the powers of office for a proper purpose, in the best interests of the company as a whole.
- A director must recognise that the primary responsibility is to the Company's shareholders as a whole but should, where appropriate, have regard for the interest of all stakeholders of the company.
- A director must not make improper use of information acquired as a director.
- A director must not take improper advantage of the position of director.
- A director must not allow personal interests, or the interests of any associated person, to conflict with the interests of the company.
- A director has an obligation to be independent in judgment and actions and to take all reasonable steps to be satisfied as to the soundness of all decisions taken as a Board.
- Confidential information received by a director in the course of the exercise of directorial duties remains the property of the Company and it is improper to disclose it, or allow it to be disclosed, unless that disclosure has been authorised by the Company, or the person from whom the information is provided, or is required by law.
- A director should not engage in conduct likely to bring discredit upon the company.
- A director has an obligation at all times, to comply with the spirit, as well as the letter of the law and with the principles of the Code.

The principles are supported by guidelines as set out by the Australian Institute of Company Directors for their interpretation should that be necessary.

2.2 Code of Ethics and Conduct

All employees and directors are expected to adhere to the following:

- respect the law and act in accordance with it;
- respect confidentiality and not misuse company information, assets or facilities;
- value and maintain professionalism;
- avoid real or perceived conflicts of interest;
- act in the best interests of shareholders;
- by their actions contribute to the company's reputation as a good corporate citizen which seeks the respect of the community and environment in which it operates;
- perform their duties in ways that minimise environmental impacts and maximise workplace safety;
- exercise fairness, courtesy, respect, consideration and sensitivity in all dealings within their workplace and with customers, suppliers and the public generally; and
- act with honesty, integrity decency and responsibility at all times.

An employee that breaches the above may face disciplinary action. If an employee suspects that a breach of the above has occurred or will occur, he or she is to notify that breach to management. No employee will be disadvantaged or prejudiced if he or she reports in good faith a suspected breach. All reports will be acted upon and kept confidential.

2.3 Dealings in Company Securities

The Company's share trading policy imposes basic trading restrictions on all directors of the Company with 'inside information'.

'Inside information' is information that:

- is not generally available; and
- if it were generally available, it would, or would be likely to influence investors in deciding whether to buy or sell the Company's securities.

Corporate Governance Statement (Cont.)

If a director possesses inside information, the person must not:

- trade in the Company's securities;
- advise others or procure others to trade in the Company's securities; or
- pass on the inside information to others – including colleagues, family or friends – knowing (or where the employee or director should have reasonably known) that the other persons will use that information to trade in, or procure someone else to trade in, the Company's securities.

This prohibition applies regardless of how the director learns the information.

Any director considering buying or selling securities is to advise the Chairman (and in his absence the Managing Director) before doing so. If the proposed buyer or seller is the Chairman he is to advise the Managing Director or another director.

In addition to the above, directors must notify the Chairman as soon as practicable, but not later than 2 business days, after they have bought or sold the Company's securities or exercised options. In accordance with the provisions of the Corporations Act and the Listing rules of the ASX, the Company on behalf of the directors must advise the ASX of any transactions conducted by them in the securities of the Company.

Breaches of this policy will be subject to disciplinary action, which may include termination of employment.

2.4 Interests of Other Stakeholders

The Company's objective is to maximise returns to shareholders through continued development of drugs and at the date hereof its lead compound Coramsine.

3. Disclosure of Information

3.1 Continuous Disclosure to ASX

The continuous disclosure policy requires all executives and directors to inform the managing director or in his absence the company secretary of any potentially material information as soon as practicable after they become aware of that information.

Information is material if it is considered likely that the information would influence investors who commonly acquire securities on ASX in deciding whether to buy, sell or hold the Company's securities.

Information is not material and need not be disclosed if:

a) A reasonable person would not expect the information to be disclosed or is material but due to a specific valid commercial reason is not to be disclosed; and

b) The information is confidential; or
c) One of the following applies:

   i) It would breach a law or regulation to disclose the information;
   ii) The information concerns an incomplete proposal or negotiation;
   iii) The information comprises matters of supposition or is insufficiently definite to warrant disclosure;
   iv) The information is generated for internal management purposes;
   v) The information is a trade secret;
   vi) It would breach a material term of an agreement, to which the company is a party, to disclose the information;
   vii) It would harm the company's potential application or possible patent application; or
   viii) The information is scientific data that release of which may benefit the company's potential competitors.

The Chairman and Managing Director are responsible for interpreting and monitoring the Company's disclosure policy and where necessary informing the Board. The Managing Director is primarily responsible for communications with ASX.

Corporate Governance Statement (Cont.)

3.2 Communication with Shareholders

The Company places considerable importance on effective communications with shareholders.

The Company's communication strategy requires communication with shareholders and other stakeholders in an open, regular and timely manner so that the market has sufficient information to make informed investment decisions on the operations and results of the Company. The strategy provides for the use of systems that ensure a regular and timely release of information about the Company is provided to shareholders. Mechanisms employed include:

- Announcements lodged with ASX;
- Half Yearly Report;
- Presentations at the Annual General Meeting/General Meeting's;
- Annual Report;
- Utilisation of a "Contact Us" mechanism on the web site which where a person is registered will see ASX releases emailed to them.

The Board encourages full participation of shareholders at the Annual General Meeting to ensure a high level of accountability and understanding of the Company's strategy and goals.

The Company also posts reports, ASX and media releases and copies of significant business presentations on the Company's website.

4. Risk Management

4.1 Identification of Risk

The Board is responsible for overseeing the Company's risk management and control framework. Responsibility for control and risk management is delegated to the appropriate level of management within the Company with the managing director having ultimate responsibility to the Board for the risk management and control framework.

Arrangements put in place by the Board to monitor risk management include regular reporting to the Board in respect of operations and the financial position of the Company and where possible on a monthly basis.

4.2 Integrity of Financial Reporting

The Company's managing director and chief financial officer (or equivalent) are required to report in writing to the Board that the Company's financial reports are founded on a sound system of risk management and internal compliance and control that implements the policies adopted by the Board.

4.3 Role of Auditor

The Company's practice is to invite the auditor to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report.

5. Remuneration Arrangements

The broad remuneration policy is to ensure that remuneration properly reflects the relevant person's duties and responsibilities, and that the remuneration is competitive in attracting, retaining and motivating people of the highest quality. The Board believes that the best way to achieve this objective is to provide executive directors and executives with a remuneration package consisting of components that reflect the person's responsibilities, duties, personal and corporate performance.

The remuneration of Non-executive directors is determined by the Board as a whole having regard to the level of fees paid to Non-executive directors by other companies of similar size in the industry.

The aggregate amount payable to the Company's Non-executive directors must not exceed the maximum annual amount approved by the Company's shareholders.

The Chairman, subject to Board approval, generally sets remuneration of the Managing Director.

Corporate Governance Statement (Cont.)

ASX Corporate Governance Council : Principles of Good Corporate Governance and Best Practice Recommendations

Council Principle 1:
Lay solid foundations for management and oversight

Council Recommendation 1.1:
Formalise and disclose the functions reserved to the board and those delegated to management.

The Company complies with this recommendation. Refer Section 1.1 of Corporate Governance Statement.

Council Principle 2
Structure the board to add value

Council Recommendation 2.1:
A majority of the board should be independent directors.

The Board considers that Michael Grant and Professor John Papadimitriou are independent directors in accordance with Recommendation 2.1. Whilst Anthony Kiernan, the Chairman, is a non-executive director he does provide legal and consulting services to the Company from time to time and therefore on an interpretation of Recommendation 2.1 may not be considered to be truly independent, notwithstanding he takes no part in the day to day management of the Company. Directors having a conflict of interest in relation to a particular item of business being considered by the Board must offer to absent themselves from the Meeting during discussion and in any event will not participate in any vote. The Chairman can also ask a director to absent themselves from the Meeting if he considers it is correct to do so in all the circumstances.

Refer Section 1.2 of Corporate Governance Statement.

Council Recommendation 2.2:
The chairperson should be an independent director.

The Company's Chairman, Anthony Kiernan, is not considered to be independent in terms of the ASX Corporate Governance Council's definition of independent director as such because he provides legal and consulting services to the Company from time to time. This is notwithstanding that he is non-executive and not involved in the day to day operations of the Company. However the Board believes that the Chairman is able and does bring quality and independent judgment to all relevant issues falling within the scope of the role of a Chairman.

Refer Section 1.2 of Corporate Governance Statement.

Council Recommendation 2.3:
The roles of the chairperson and chief executive officer should not be exercised by the same individual.

The Company complies with this recommendation.

Council Recommendation 2.4:
The board should establish a nomination committee.

The Board considers that the Company is not currently of a size to justify the formation of a nomination committee. The Board as a whole undertakes the process of reviewing the skill base and experience of existing directors to enable identification or attributes required in new directors.

The Board acknowledges this does not comply with recommendation 2.4 of the ASX Corporate Governance Guidelines. If the Company's activities increase in size, scope and nature, the appointment of a nomination committee will be reviewed by the Board and implemented if appropriate.

Refer Section 1.3 of Corporate Governance Statement.

Corporate Governance Statement (Cont.)

Council Principle 3:
Promote ethical and responsible decision-making

Council Recommendation 3.1:
Establish a code of conduct to guide the directors, the chief executive officer (or equivalent), the chief financial officer (or equivalent) and any other key executives as to:

3.1.1 the practices necessary to maintain confidence in the company's integrity;
3.1.2 the responsibility and accountability of individuals for reporting and investigating reports of unethical practice.

The Company has in place a level of expectation of conduct which is set out in Sections 2.1 and 2.2 of Corporate Governance Statement.

Council Recommendation 3.2:
Disclose the policy concerning trading in company securities by directors, officers and employees.

The Company complies with this recommendation. Refer Section 2.3 of Corporate Governance Statement.

Council Principle 4:
Safeguard integrity in financial reporting

Council Recommendation 4.1:
Require the Chief Executive Officer (or equivalent) and the Chief Financial Officer (or equivalent) to state in writing to the board that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards.

The Company complies with this recommendation.

Council Recommendation 4.2:
The board should establish an audit committee.

The Board has established an Audit Committee which currently comprises non-executive directors Kiernan and Grant.
Refer Section 1.3 of Corporate Governance Statement.

Council Recommendation 4.3:
Structure the audit committee so that it consists of:

- *only Non-executive directors;*
- *a majority of independent directors;*
- *an independent chairperson, who is not chairperson of the board;*
- *at least three members.*

Refer Recommendation 4.2. The company does not fully comply with this recommendation due to the size of the company and the availability of Directors to act on the Audit Committee.

Council Recommendation 4.4
The audit committee should have a formal operating charter.

The Audit Committee does not have a formal operating charter as such but does act independently of management and has ready access to all accounts and the auditor at all times. The Committee reviews all financial information and reports of a financial nature prior to release to ASX.

Corporate Governance Statement (Cont.)

Council Principle 5:
Make a timely and balanced disclosure

Council Recommendation 5.1:
Establish written policies and procedures designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior management level for that compliance.

The Company complies with this recommendation. Refer Section 3.1 of Corporate Governance Statement.

Council Principle 6:
Respect the rights of shareholders

Council Recommendation 6.1:
Design and disclose a communications strategy to promote effective communication with shareholders and encourage effective participation at general meetings.

The Company complies with this recommendation. Refer Section 3.2 of Corporate Governance Statement.

Council Recommendation 6.2:
Request the external auditor to attend the annual general meeting and be available to answer shareholder questions about the conduct of the audit and the preparation and content of the auditor's report.

The Company complies with this recommendation. Refer Section 4.3 of Corporate Governance Statement.

Council Principle 7:
Recognise and manage risk

Council Recommendation 7.1:
The Board or appropriate board committee should establish policies on risk oversight and management.

The Company complies with this recommendation. Refer Section 4.1 of Corporate Governance Statement.

Council Recommendation 7.2
The chief executive officer and the chief financial officer should state in writing that:

- *7.2.1 the statement given in accordance with best practice recommendation 4.1 is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the board;*
- *7.2.2 the company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.*

The Company complies with this recommendation. Refer Section 4.1 of Corporate Governance Statement.

Council Principle 8:
Encourage enhanced performance

Council Recommendation 8.1:
Disclose the process for performance evaluation of the board, its committees and individual directors, and key executives.

Refer Section 5 of Corporate Governance Statement.

Council Principle 9:
Remunerate fairly and responsibly

Council Recommendation 9.1:
Provide disclosure in relation to the company's remuneration policies to enable investors to understand (i) the costs and benefits of those policies and (ii) the link between remuneration paid to directors and key executives and corporate performance.

Corporate Governance Statement (Cont.)

The Company complies with this recommendation insofar as is set out in Section 6 of Corporate Governance Statement.

Council Recommendation 9.2
The board should establish a remuneration committee.

The Board considers that the Company is not currently of a size, nor are its affairs of such complexity to justify the formation of a remuneration committee. The Board as a whole is responsible for the remuneration arrangements for directors and executives of the Company.

The Board acknowledges this does not comply with recommendation 9.2 of the ASX Corporate Governance Guidelines. If the Company's activities increase in size, scope and nature, the appointment of a remuneration committee will be reviewed by the Board and implemented if appropriate.

Refer Section 1.3 of Corporate Governance Statement.

Council Recommendation 9.3
Clearly distinguish the structure of Non-executive directors' remuneration from that of executives.

The Company complies with this recommendation. Refer Section 5 of Corporate Governance Statement.

Council Recommendation 9.4
Ensure that payment of equity-based executive remuneration is made in accordance with thresholds set in plans approved by shareholders.

The Company complies with this recommendation.

Council Principle 10:
Recognise the legitimate interests of stakeholders

Council Recommendation 10.1:
Establish and disclose a code of conduct to guide compliance with legal and other obligations to legitimate stakeholders.

The Company complies with this recommendation. Refer Section 2.4 of Corporate Governance Statement.

Directors' Report

Your Directors submit their report for the year ended 30 June 2006.

DIRECTORS

The names and details of the Directors of the Company in office during the financial year and until the date of this report are listed below. Directors were in office for this entire period unless otherwise stated.

Anthony Kiernan (Chairman) Non Executive

Mr Kiernan is a Solicitor with considerable experience in the administration and operation of listed public companies and practises extensively in the areas of media, resources and information technology law.

In addition to his legal practice, Mr Kiernan provides commercial and corporate advice to various entities. In the past 3 years Mr Kiernan has been and still is a director of Uranium Equities Limited listed on Australian Stock Exchange and a number of non public entities. He is also Chairman of Anglicare (WA) and a member of the Company's Audit Committee.

Dr Graeme Howie (Managing Director - Appointed 6/10/2005)

Dr Howie has worked in the Australian and global pharmaceutical industry for over 28 years including as a senior product development executive for Pharmacia and later Pfizer in the United States primarily responsible for the research and development of a number of biotechnology projects. He is a non executive director of Neuren Pharmaceuticals Limited

Michael Grant (Non Executive)

Mr Grant has a masters degree from UWA and sixteen years experience in the securities industry. Over this period he has worked in the UK, USA and Australian markets in both the mutual fund sector and private client advisory roles. He has wide experience within the broking industry at both domestic and international levels. In recent times he has been a senior advisor with Merrill Lynch Australia and is currently a senior client advisor with Bell Potter Securities.

His early background in medical sciences and long experience in the financial markets brings a valuable and balanced contribution to the board of Solbec. He is a member of the Audit Committee.

Stephen J Carter FAIM MRACI (Non Executive)

Mr Carter has qualifications in Chemistry and over twelve years experience in the Pharmaceutical Industry in drug development and registration in Australia, USA and other parts of the world. Stephen held the positions of Research and Development Manager and a General Manager for Delta West Ltd prior to its takeover by the Pharmacia Pharmaceutical group. He is also Chairman of Colltech Australia Ltd., appointed on 23 December 2005.

Professor John Papadimitriou, AM, OStJ (Non Executive)

Professor Papadimitriou has had a distinguished academic career in pathology and was awarded a personal chair for his many contributions.

He is presently Emeritus Professor in the School of Surgery and Pathology at The University of Western Australia and is also on the consultant staff of the Royal Perth Hospital and the PathCentre, the Western Australian Centre for Pathology and Medical Research. He has an international reputation in both diagnostic and experimental pathology and is the author and co-author of three books and some 460 scientific papers. He is a director of the Neurological Research Institute and the Child Heath Research Foundation of Western Australia and Deputy Director of the Australian Research Centre for Medical Engineering. He was also a Director of Meditech Research Ltd in the last 3 years and resigned on 29 May 2006.

Professor Papadimitriou was made a Member of the Order of Australia for services rendered to medical research and the community.

Dr David Hung (Non Executive - Resigned 8/07/06)

Dr Hung is a California-based physician and entrepreneur. His specialist medical expertise is in internal medicine and oncology. He is currently President and Chief Executive Officer of Medivation Inc., which develops early stage pharmaceutical projects.

Dr Hung previously served as founding President and CEO of Pro.Duct Health Inc., a company which developed, manufactured and commercialized a device used in breast cancer risk assessment. Pro.Duct Health Inc. was acquired by Cytyc Corporation. Dr Hung also held senior roles in product and clinical development with pioneering biotechnology company, Chiron Corporation.

Directors' Report (Cont.)

INTERESTS IN THE SHARES AND OPTIONS OF THE COMPANY

As at the date of this report the interests of the directors in the shares and options of the company were:-

Director	Ordinary Shares		Options	
	Direct Interest	Indirect Interest	Direct Interest	Indirect Interest
Anthony Kiernan	791,930	993,715	2,000,000	-
Michael Grant	1,101,935	890,143	2,000,000	-
Stephen J Carter	28,572	1,379,075	3,000,000	-
John Papadimitriou	-	55,000	2,000,000	-
David Hung (resigned 8/07/06)	-	-	2,000,000	-
Graeme Howie (appointed 6/10/05)	100,000	50,000	-	-

COMPANY SECRETARY

John Sendziuk is a chartered accountant. He has been in practice for 20 years providing corporate secretarial, taxation and business advice to a diverse group of business clients and public companies.

CORPORATE INFORMATION

Solbec Pharmaceuticals Ltd is a company limited by shares incorporated and domiciled in Australia. At balance date the Company had ten full time employees (2005: ten full time employees).

The Company is the ultimate parent entity of the consolidated group comprising the Company and its wholly-owned subsidiary, Solbec (No 1) Pty Ltd.

PRINCIPAL ACTIVITY

The principal activity of the Company during the year was pharmaceutical research.

RESULTS OF OPERATIONS

The loss after income tax for the financial year was $1,703,301 (2005 : $2,911,254).

DIVIDENDS

No dividend was paid during the financial year and the Directors do not recommend payment of a dividend.

REVIEW OF OPERATIONS

Detailed comments on operations are included separately in this annual report under the Chairman's Report and Review of Operations.

COMPANY PERFORMANCE

Solbec's core focus is on the clinical development of its lead compound Coramsine®. Building on the strong base of research to date, the Company reports that it has progressed Coramsine® through to Phase II clinical trials. Research and development expenditure for the year was $1,253,558 not including consultant's fees and wages and salaries, which is a decrease on last years expenditure of $1,525,913.

Other matters pertinent to Solbec's performance during last financial year are set out in the comprehensively Review of Operations above.

Directors' Report (Cont.)

OBJECTIVES AND GOALS

Objectives

Over the next twelve months the Company's primary objective is to continue advancing the Australian Phase II clinical trials. Maximising patient recruitment in these Phase II trials will be of paramount importance. Solbec expects to perform a mid-point analysis of the clinical trial results after recruiting 20 patients in each indication. The data from this mid-point analysis will then be used to determine which indication(s) are best to proceed with Phase II trials in the US and planning for these trials will then likely commence. During this time Solbec will continue to present to potential investors and licensing partners on the progress of the Company and Coramsine's® clinical development.

Throughout the year, Solbec will continue to develop its IP portfolio with several patent filings coming up for examination over the next 12-18 months. Solbec will also seize any opportunity to expand Coramsine's® patent family with further layers of patent protection.

Goals

- Maximise recruitment in Coramsine's® Phase II cancer clinical trials to be conducted in Australia
- Identify key and clinicians to engage for US clinical trials
- Progress with the planning stages of Coramsine's® proposed Phase II cancer clinical trials in the USA
- Continue progressing licensing communications with potential global partners
- Further strengthen and expand Coramsine's® IP portfolio

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

There were no significant changes in the state of affairs of the company that occurred during the financial year not otherwise disclosed in this report or the accounts.

SIGNIFICANT EVENTS AFTER THE BALANCE DATE

The consolidated entity raised $1,298,491 in August 2006 through the issue of 18,549,858 shares at 7 cents per share for working capital.

No other matters or circumstances have arisen since the end of the financial year which significantly affected or may significantly affect the operations of the company, the results of those operations, or the state of affairs of the company in future financial years.

LIKELY DEVELOPMENTS AND EXPECTED RESULTS OF OPERATIONS

These are discussed in the Operations Review and Objectives and Goals.

REMUNERATION REPORT

Remuneration Philosophy

This section details the remuneration arrangements in place for the executives and directors of Solbec Pharmaceuticals Ltd.

The broad remuneration philosophy is to ensure that remuneration properly reflects the relevant person's duties and responsibilities, and that the remuneration is competitive in attracting, retaining and motivating people of the highest quality. The Board believes that the best way to achieve this objective is to provide any executive directors and executives with a remuneration package consisting of components that reflect the person's responsibilities, duties, personal and corporate performance.

To this end Solbec follows the following principles;

- Provide competitive rewards.
- That a part of the senior executive's remuneration is "at risk" that is linked to pre-determined achievements.
- That any variable executive remuneration has appropriate and demanding performance hurdles attached.

Directors' Report (Cont.)

Remuneration Committee

Solbec does not have a remuneration committee. The remuneration of non-executive directors is determined by the Board as a whole having regard to industry standards of similar sized entities.

The aggregate amount payable to the Company's non-executive directors must not exceed the maximum annual amount approved by the Company's shareholders. An aggregate amount of $200,000 was approved by shareholders at the Annual General Meeting held in May 2006.

Senior Manager and Executive Director Remuneration

The company aims to reward executives with a level and mix of remuneration commensurate with their position and responsibilities within the company and so as to:

- reward executives for company, business unit and individual performance against targets set by reference to appropriate benchmarks;
- align the interests of executives with those of shareholders;
- link rewards with the strategic goals and performance of the company; and
- ensure total remuneration is competitive by market standards.

The Chairman, subject to Board approval, generally sets remuneration of the Managing Director and the General Manager.

Fixed Remuneration

The level of fixed remuneration for executives is set so as to provide a base level of remuneration which is both appropriate to the position and competitive in the market.

Fixed remuneration is reviewed annually.

Variable Remuneration

Short term incentives (STI) may be linked to achievement of the companies operational targets with the remuneration received if the relevant executives achieve the target.

The directors, subject to shareholder approval, and executives are eligible to participate in the Company's share option plan whereby options may be granted at an exercise price above the prevailing share price. This premium in conversion price, coupled with an appropriate vesting period, provides a long term incentive (LTI) whereby directors and executives will benefit only if there is a substantial improvement in the Company's share price. The number of options granted to each director and executive is determined by the Board based on the Company's and the eligible participant's performance.

Employment Contracts

The Managing Director, Dr Graeme Howie is employed under contract. The current employment commenced on the 15th of May 2006. The key terms of the contract are;

- Dr. Howie may resign from his position giving 6 months written notice and thus terminate his contract.
- The Company may terminate his contract by providing 6 months written notice or provide 3 months pay in lieu of notice however, the contract may be terminated at any time without notice if serious misconduct has occurred.
- Dr Howie will be paid a base salary of $160,000 per annum plus statutory superannuation and receive a vehicle allowance of $4,000 per annum.

SOLBEC PHARMACEUTICALS LTD

Directors' Report (Cont.)

The General Manager, Mr. David Sparling, is employed under contract. The current employment commended 20th March 2006. The key terms of the contract are;

- Term of contract 24 months.
- Base salary of $160,000 per annum plus superannuation.
- 1,500,000 options vesting over a period of 12 months.
- The Company may terminate his contract by providing 6 months written notice or provide 6 months pay in lieu of notice however, the contract maybe terminated without notice if serious misconduct has occurred.

Details of remuneration for year ended 30 June 2006

There are no other employment contracts.

The remuneration for each director and each of the executive officers of the consolidated entity receiving remuneration during the year was as follows.

Directors remuneration for the year ended 30 June 2006.

2006	Short Term			Post Employment	Share Based Payment		% performance based
	Consulting Fees	Salary	Directors Fees	Super	Options	Total	
Name	$	$	$	$	$	$	
G Howie (Managing Director)	24,590	37,110	-	3,340	-	65,040	-
S J Carter (Non Executive)	68,590	131,460	11,477	11,101	-	222,628	-
A Kiernan (Chairman)	10,585	-	22,500	2,025	-	35,110	-
M Grant (Non Executive)	3,100	-	18,375	1,654	-	23,129	-
J Papadimitriou (Non Executive)	-	-	18,375	1,654	-	20,029	-
D Hung (Non Executive)	-	-	18,375	-	-	18,375	-
	106,865	168,570	89,102	19,774	-	384,311	-

Remuneration of highest paid executives for the end of 30 June 2006.

2006	Short Term		Post Employment	Share based payment	Long Term Incentive Plan	
	Consulting Fees	Salary	Superannuation	Options	Shares	Total
Name	$	$	$	$	$	$
David Sparling (General Manager)	-	118,729	9,714	15,182	1,000	144,625
John Sendziuk (Company Secretary)	35,805	-	-	-	-	35,805
	35,805	118,729	9,714	15,182	1,000	180,430

The shares issued to David Sparling under the long term incentive plan were part of a bonus payment to the company's employees.

Directors' Report (Cont.)

Options Granted as part of remuneration

2006	Granted Number	Grant date	Terms and Conditions for each Grant Value per option at grant date	Exercise price per share	First exercise date	Last exercise date	% of Remuneration
Name							
D Sparling	500,000	15/05/06	.016 cents	12 cents	15/05/06	31/12/09	2.8
	750,000	15/05/06	.012 cents	15 cents	30/09/06	31/12/09	1.0
	250,000	15/05/06	.022 cents	18 cents	30/03/07	31/12/09	7.4

No options granted as part of remuneration were exercised or lapsed during the year ended 30 June 2006.

INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

Indemnification:
The Company has agreed to indemnify all the directors and the company secretary who have held office in the Company during this financial year, against all liabilities to another person (other than the Company or its related body corporate) that may arise from their position as a director or officer of the Company and its controlled entities, except where the liability arises out of conduct involving a lack of good faith. The agreement stipulates that the Company will meet the full amount of any such liabilities, including costs and expenses.

Insurance Premiums:
During the financial year the Company has paid insurance premiums of $25,556 in respect of directors and officers liability and legal expenses insurance contracts, for current and former directors and officers, including executive officers of the Company and directors, executive officers and secretaries of its controlled entity. The insurance premiums relate to:

- Costs and expenses incurred by the relevant officers in defending proceedings, whether civil or criminal and whatever their outcome;
- Other liabilities that may arise from their position, with the exception of conduct involving the wilful breach of duty or improper use of information or position to gain a personal advantage.

Directors' Report (Cont.)

SHARE OPTIONS

Unissued Shares

At the date of this report, there were options over ordinary shares on issue as follows:

- 4,000,000 director options at an issue price of 22 cents expiring 9 June 2007.
- 3,000,000 executive options at an issue price of 20 cents expiring 9 June 2007.
- 4,000,000 director options an issue price of 22 cents expiring 25 November 2007.
- 500,000 executive options exercisable at 12 cents on the 31 December 2009.
- 750,000 executive options exercisable at 15 cents on the 31 December 2009.
- 250,000 executive options exercisable at 18 cents on the 31 December 2009.
- 15,182,200 options at an issue price of 30 cents if exercised by 19 September 2006.

The option holders do not have any right, by virtue of the option to participate in any share issue of the Company or any related body corporate.

Shares Issued As A Result Of The Conversion Of Options

During the financial year, as a capital management initiative, 133,482,631 options were cancelled in consideration of one new share for every seven options cancelled. During the financial year and up to the date of this report there have been no options exercised.

Options Lapsed During The Period

No options lapsed during the year.

DIRECTORS' MEETINGS

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

	Directors' Meetings		Audit Committee	
	Number eligible to attend	Meetings Attended	Number eligible to attend	Meetings Attended
Stephen J Carter	7	7	-	-
Anthony Kiernan	7	7	7	7
Michael Grant	7	5	7	7
John Papadimitriou	7	5	-	-
David Hung (resigned 8/07/06)	7	1	-	-
Graeme Howie (appointed 6/10/05)	6	6	-	-

CORPORATE GOVERNANCE

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Solbec Pharmaceuticals Ltd support and have adhered to the principles of corporate governance. The company's corporate governance statement is contained in the additional corporate governance section of this annual report.

Director's Report (Cont.)

Non Audit Services

No non audit services were provided during the year by the Auditors.

Auditor's Independence Declaration

In accordance with section 307C of the Corporations Act 2001, the Directors have obtained a declaration of independence from Ernst and Young, Perth, the consolidated entity's auditors, as presented on page 30 of this year's financial report. The company did not receive any non-audit services from the auditors.

Signed at Perth this 29th September 2006 in accordance with a resolution of the directors.

Anthony Kiernan - Chairman

Michael Grant - Director

Auditor's Independence Declaration

ERNST & YOUNG

The Ernst & Young Building
11 Mounts Bay Road
Perth WA 6000
Australia

GPO Box M939
Perth WA 6843

Tel 61 8 9429 2222
Fax 61 8 9429 2436

Auditor's Independence Declaration to the Directors of Solbec Pharmaceuticals Ltd

In relation to our audit of the financial report of Solbec Pharmaceuticals Ltd for the year ended 30 June 2006, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the Corporations Act 2001 or any applicable code of professional conduct.

Ernst & Young

J P Dowling
Partner
Perth
29 September 2006

JPD:ND:SOLBEC:061

SOLBEC
PHARMACEUTICALS LTD

Independent Audit Report To The Members Of Solbec Pharmaceuticals Ltd

ERNST & YOUNG

The Ernst & Young Building
11 Mounts Bay Road
Perth WA 6000
Australia

GPO Box M939
Perth WA 6843

Tel 61 8 9429 2222
Fax 61 8 9429 2436

Independent audit report to members of Solbec Pharmaceuticals Ltd

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, statement of changes in equity, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for Solbec Pharmaceuticals Ltd (the company) and the consolidated entity, for the year ended 30 June 2006. The consolidated entity comprises both the company and the entities it controlled during that year.

The directors of the company are responsible for preparing a financial report that gives a true and fair view of the financial position and performance of the company and the consolidated entity, and that complies with Accounting Standards in Australia, in accordance with the *Corporations Act 2001*. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit approach

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

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001*, including compliance with Accounting Standards in Australia, and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report; and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

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

We performed procedures to assess whether the substance of business transactions was accurately reflected in the financial report and the remuneration disclosures. These and our other procedures did not include consideration or judgement of the appropriateness or reasonableness of the business plans or strategies adopted by the directors and management of the company.

Independent Audit Report To The Members Of Solbec Pharmaceuticals Ltd

ERNST & YOUNG

Independence
We are independent of the company and the consolidated entity and have met the independence requirements of Australian professional ethical pronouncements and the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the Directors' Report.

Audit opinion
In our opinion the financial report of Solbec Pharmaceuticals Ltd is in accordance with:

(a) the *Corporations Act 2001*, including:

  (i) giving a true and fair view of the financial position of Solbec Pharmaceuticals Ltd and the consolidated entity at 30 June 2006 and of their performance for the year ended on that date; and

  (ii) complying with Accounting Standards in Australia and the *Corporations Regulations 2001*; and

(b) other mandatory financial reporting requirements in Australia.

Ernst & Young

J P Dowling
Partner
Perth
29 September 2006

Directors' Declaration

The Directors of the company declare that:

1. the financial statements and notes of the company and the consolidated entity, are in accordance with the *Corporations Act 2001* including:
   a. complying with Accounting Standards and the Corporations Regulations 2001; and

   b. giving a true and fair view of the financial position as at 30 June 2006 and of the performance for the year ended on that date of the company and consolidated entity;

2. in the director's opinion there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

   This declaration has been made after receiving the declarations required to be made to the directors in accordance with sections 295A of the Corporations Act 2001 for the financial period ending 30 June 2006.

Dated this 29th September 2006.

Signed in accordance with a resolution of the directors:

Anthony Kiernan - Chairman

Michael Grant - Director

Income Statement

For The Year Ended 30 June 2006

	Note	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
Revenue	3(a)	35,814	129,023	97,089	381,780
Other Income	3(c)	656,166	158,065	656,166	158,065
Total Income		**691,980**	**287,008**	**753,255**	**539,845**
Depreciation		(37,890)	(30,982)	(37,890)	(30,982)
Allowance for doubtful debts		10,349	(122)	(7,251)	(240,022)
Impairment of plant and equipment		(30,415)	-	(30,415)	-
Research and development expenditure		(1,253,558)	(1,525,913)	(1,180,667)	(1,525,993)
Other expenses	3b	(1,601,348)	(1,641,245)	(1,663,425)	(1,641,335)
Loss before Income Tax		(2,220,882)	(2,911,254)	(2,166,393)	(2,898,487)
Income Tax Benefit	4	517,581	-	502,499	-
Loss After Income Tax		**(1,703,301)**	**(2,911,254)**	**(1,663,894)**	**(2,898,287)**
Net loss Attributable To Members Of Solbec Pharmaceuticals Ltd		**(1,703,301)**	**(2,911,254)**	**(1,663,894)**	**(2,898,287)**
Basic earnings/(loss) per share - cents per share	26	(1.0)	(1.7)		
Diluted earnings/(loss) per share - cents per share	26	(1.0)	(1.7)		

Balance Sheet

As At 30 June 2006

	Note	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
CURRENT ASSETS					
Cash and cash equivalents	23(a)	888,908	1,405,349	884,807	1,345,149
Trade and other receivables	5	3,104	118,368	-	131,957
Other assets	6	52,231	39,128	52,231	39,128
Total Current Assets		944,243	1,562,845	937,038	1,516,234
NON-CURRENT ASSETS					
Land and improvements at fair value	8	1,020,000	-	1,020,000	-
Other property, plant and equipment	8	291,212	521,212	291,212	521,212
Other Financial assets	9	-	36,176	1	36,176
Total Non-Current Assets		1,311,212	557,388	1,311,213	557,388
Total Assets		**2,255,455**	**2,120,233**	**2,248,251**	**2,073,622**
CURRENT LIABILITIES					
Trade and other payables	10	636,156	523,012	636,156	523,012
Provisions	11	20,853	58,901	20,853	58,901
Other liabilities	12	282,295	-	282,295	-
Total Current Liabilities		939,304	581,913	939,304	581,913
Total Liabilities		939,304	581,913	939,304	581,913
Net Assets		**1,316,151**	**1,538,320**	**1,308,947**	**1,491,709**
EQUITY					
Contributed equity	13	19,730,688	17,138,366	19,730,688	17,138,366
Reserves	14	1,382,509	2,493,699	1,382,509	2,493,699
Accumulated Losses	15	(19,797,046)	(18,093,745)	(19,804,250)	(18,140,356)
Total Equity		**1,316,151**	**1,538,320**	**1,308,947**	**1,491,709**

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2006

Consolidated	Issued Capital	Accumulated Losses	Asset Revaluation Reserve	Other Reserves	Total Equity
	$	$	$	$	$
As at 1 July 2004	16,053,409	(15,182,491)	-	2,493,699	3,364,617
Loss for the period	-	(2,911,254)	-	-	(2,911,254)
Exercise of options	1,084,957	-	-	-	1,084,957
As at 30 June 2005	**17,138,366**	**(18,093,745)**	**-**	**2,493,699**	**1,538,320**
Consolidated					
As at 1 July 2005	17,138,366	(18,093,745)	-	2,493,699	1,538,320
Impact of adopting AASB 132/139	-	-	-	-	-
Employee options	-	-	-	15,181	15,181
Redemption of options by issue of shares	1,659,022	-	-	(1,659,022)	-
Revaluation of land and buildings to fair value	-	-	759,645	-	759,645
Income tax on items recognised in equity	-	-	(226,994)		(226,994)
Loss for the period	-	(1,703,301)	-	-	(1,703,301)
Share Issues	933,300	-	-	-	933,300
As at 30 June 2006	**19,730,688**	**(19,797,046)**	**532,651**	**849,858**	**1,316,151**

Parent	Issued Capital	Accumulated Losses	Asset Revaluation Reserve	Other Reserves	Total Equity
	$	$	$	$	$
As at 1 July 2004	16,053,409	(15,241,869)	-	2,493,699	3,305,239
Loss for the period	-	(2,898,487)	-	-	(2,898,487)
Exercise of options	1,084,957	-	-	-	1,084,957
As at 30 June 2005	**17,138,366**	**(18,140,356)**	**-**	**2,493,699**	**1,491,709**
Parent					
As at 1 July 2005	17,138,366	(18,140,356)	-	2,493,699	1,491,709
Impact of adopting AASB 132/139	-	-	-	-	-
Employee options	-	-	-	15,181	15,181
Redemption of options by issue of shares	1,659,022	-	-	(1,659,022)	-
Revaluation of land and buildings to fair value	-	-	759,645	-	759,645
Income tax on items recognised in equity	-	-	(226,994)	-	(226,994)
Loss for the period	-	(1,663,894)	-	-	(1,663,894)
Share Issues	933,300	-	-	-	933,300
As at 30 June 2006	**19,730,688**	**(19,804,250)**	**532,651**	**849,858**	**1,308,947**

Statement Of Cash Flows

For The Year Ended 30 June 2006

	Note	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
CASH FLOWS FROM OPERATING ACTIVITIES					
Government Grants		936,363	68,975	936,363	68,975
Receipts from operations		54,383	131,764	100,053	384,521
Payments to suppliers and employees		(645,284)	(1,266,308)	(714,144)	(1,286,355)
Borrowing costs paid		-	-	-	-
Payments relating to research projects		(2,062,019)	(1,425,993)	(1,976,002)	(1,425,993)
Income Tax refunds received		290,587	-	275,505	-
Interest received		37,768	124,458	35,773	124,458
Net Cash Used In Operating Activities	23(b)	**(1,388,202)**	**(2,367,104)**	**(1,342,452)**	**(2,134,394)**
CASH FLOWS FROM INVESTING ACTIVITIES					
Payments for plant and equipment		(99,813)	(72,608)	(99,813)	(72,608)
Proceeds from sale of investments		38,273	34,983	38,273	34,983
Redemption of Security Deposit		-	39,584	-	39,584
Payment for Investments		-	(785)	-	(785)
Net Cash Provided By/(Used In) Investing Activities		**(61,540)**	**1,174**	**(61,540)**	**1,174**
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from shares issued		933,301	1,084,957	933,301	1,084,957
Repayment (Advances) of loan from controlled entity		-	-	10,349	(239,900)
Net Cash Provided By Financing Activities		**933,301**	**1,084,957**	**943,650**	**845,057**
Net increase (decrease) in cash held		(516,441)	(1,280,973)	(460,342)	(1,288,163)
Cash held at the beginning of the financial year		1,405,349	2,686,322	1,345,149	2,633,312
Cash Held At The End Of The Financial Year	23(a)	**888,908**	**1,405,349**	**884,807**	**1,345,149**

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

1. CORPORATE INFORMATION

The financial report of Solbec Pharmaceuticals Limited for the year ended 30 June 2006 was authorised for issue in accordance with a resolution of the directors on 29 September 2006. Solbec Pharmaceutical Limited is a company limited by shares incorporated in Australia whose shares are publicly traded on the Australian stock exchange. The nature of the operations and principal activities of the consolidated entity are described in note 3.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Basis of Preparation

This financial report is a genera-purpose financial report, which has been prepared in accordance with the requirements of the *Corporations Act 2001* and Australian Accounting Standards. The financial report has also been prepared on a historical cost basis, except for land and improvements, and available-for-sale investments, which have been measured at fair value. The financial report is presented in Australian dollars.

b) Statement of compliance

The financial report complies with Australian Accounting Standards, which include Australian equivalents to International Financial Reporting Standards (AIFRS). Compliance with AIFRS ensures that the financial report, comprising the financial statements and notes thereto, complies with International Financial Reporting Standards (IFRS).

This is the first financial report prepared on AIFRS and comparatives for the year ended 30 June 2005 have been restated accordingly except for the adoption of AASB 132 *Financial Instruments: Disclosure and Presentation and* AASB 139 *Financial Instruments: Recognition and Measurement.* The company has adopted the exemption under AASB 1 *First-time Adoption of Australian Equivalents to International Financial Reporting Standards* from having to apply AASB 132 and AASB 139 to the comparative period. Reconciliations of AIFRS equity and profit for 30 June 2005 to the balances reported in the 30 June 2005 financial report and at transition to AIFRS are detailed in note 28.

Australian Accounting Standards that have recently been issued or amended but are not yet effective have not been adopted for the annual reporting period ending 30 June 2006:

AASB Amendment	Affected Standard (s)	Nature of change to accounting policy	Application date of standard*	Application date for Group
2005-1	AASB 139: *Financial Instruments: Recognition and Measurement*	No change to the accounting policy required. Therefore no impact	1 January 2006	1 July 2006
2005-5	AASB 1: *First-time adoption of AIFRS,* AASB 139: *Financial Instruments: Recognition and Measurement*	No change to accounting policy required. Therefore no impact	1 January 2006	1 July 2006
2005-6	AASB 3: *Business Combinations*	No change to accounting policy required. Therefore no impact	1 January 2006	1 July 2006

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

2005-10	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 AIFRS*, AASB 4: *Insurance Contracts*, AASB 1023: *General Insurance Contracts* and AASB 1038: *Life Insurance Contracts*	No change to accounting policy required. Therefore no impact	1 January 2007	1 July 2007
New Standard	AASB 7 *Financial Instruments: Disclosures*	No change to accounting policy required. Therefore no impact	1 January 2007	1 July 2007
New UIG	UIG 4 Determining whether an Arrangement contains	No change to accounting policy required. Therefore no impact	1 January 2006	1 July 2006

* Application date is for the annual reporting beginning on or after the date shown in the above table.

The following amendments are not applicable to the Consolidated Entity and therefore have no impact.

AASB Amendment	Affected Standard(s)
2005-2	AASB 1023: *General Insurance Contracts*
2005-4	AASB 139: *Financial Instruments: Recognition and Measurement*, AASB 132: *Financial Instruments: Discloser and Presentation*, AASB 1: *Firsts-time adoption of AIFRS*, AASB 1023: *General Insurance Contracts* and AASB 1023: *Life Insurance Contracts*
2005-9	AASB 4: *Insurance Contracts*, AASB 1023: *General Insurance Contracts*, AASB 139: *Financial Instruments: Recognition and Measurement* and AASB 132: *Financial Instruments: Disclosure* *Presentation*
2005-12	AASB 1038: *Life Insurance Contracts* and AASB 1023: *General Insurance Contracts*
2005-13	AAS 25: *Financial Reporting by Superannuation Plans*
New Standard	AASB119: *Employee Benefits*
New UIG	UIG 5 *Rights to Interest in Decommissioning, Restoration and Environmental Rehabilitation Funds*
New UIG	UIG 7 Applying the Restatement Approach under AASB 129 Financial Reporting in Hyperinflati Economics
New UIG	UIG 8 *Scope of AASB 2*
New UIG	UIG 9 *Reassessment of Embedded Derivatives*

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

c) Going Concern

The financial report has been prepared on a going concern basis. In arriving at this position the directors have had regard to the fact that the company has access to a $5 million standby equity facility with a US-based investment fund, allowing the company to draw down the facility by the issue of shares. Refer to Note 22c for further details of this facility. As a result of this facility, the directors are confident that the consolidated entity will have sufficient cash and other assets to fund committed expenditure for a period of not less than 12 months from the date of this report.

d) Change in Accounting Policy

During the period ended 30 June 2006, the consolidated entity changed its accounting policy in relation to the valuation of land and improvements. The consolidated entity now recognises land and buildings at fair value, whereas previously this class of assets was recognised at cost. The directors believe that the new accounting policy improves the relevance and reliability of the financial statements and results in a more accurate reflection of the tangible assets held by the consolidated entity. The change in accounting policy has resulted in an increase in the value of land and buildings of $759,645 ($532,651 after tax) during the year ended 30 June 2006, and a corresponding increase in the asset revaluation reserve. The change in accounting policy has had no impact on the loss of the consolidated entity for the year.

e) Basis of Consolidation

The consolidated financial statements comprise the financial statements of Solbec Pharmaceuticals Ltd and its subsidiaries ("the consolidated entity").

All inter-company balances and transactions between entities in the consolidated entity, including any unrealised profit or losses, have been eliminated on consolidation.

Where controlled entities have entered or left the consolidated entity during the period, their operating results have been included from the date control was obtained or until the date control ceased.

f) Significant accounting judgements, estimates and assumptions

(i) Significant accounting judgements
In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements:

Development costs
The Group makes an assessment of whether a development project displays the required degree of technical feasibility in order to determine whether costs associated with the project should be capitalised or expensed.

(ii) Significant accounting estimates and assumptions
The carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of certain assets and liabilities within the next annual reporting period are:

Share-based payment transactions
The consolidate entities measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by using the Black-Scholes formula, using the assumptions detailed in note 20.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

The consolidated entities measures the cost of cash-settled share-based payments at fair value at the grant date using the Black-Scholes formula taking into account the terms and conditions upon which the instruments were granted, as discussed in note 20.

g) **Income Tax**

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

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

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

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

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

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

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

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

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

Income taxes relating to items recognised directly in equity are recognised in equity and not in profit or loss.

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

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

h) **Other taxes**

Revenue, expenses and assets are recognised net of the amount of GST except:

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

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

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

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

i) **Revenue**

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

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

Administration fees are on an accrual basis as the services are rendered.

j) **Government grants**

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with.

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

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

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

k) Investments

The consolidated entity has elected to apply the option available under AASB1 of adopting AASB 132 and AASB 139 from 1 July 2005. Outlined below are the relevant accounting policies for investments applicable for the years ending 30 June 2006 and 30 June 2005.

Accounting polices applicable for the year ending 30 June 2006.
Financial assets in the scope of AASB 139 *Financial Instruments: Recognition and Meaurement* are classified either as financial assets at fair value through profit or loss, loans and receivable, held-to-maturity, or available for sale investments as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not fair value through profit or loss, directly attributable transaction. The Group determines the classification of its financial assets after initial recognition and, when allowed and appropriate, rev-evaluate this designation at each financial year-end.

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sale of financial assets under contracts that require delivery of assets within the period of established generally by regulations or convention in the market place.

Available-for-sale financial assets
Available for sale financial assets include any financial assets not included in the above categories. Available-for-sale financial assets are reflected at fair value. Unrealised gains and losses arising from changes in fair value are taken directly to equity.

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

Investments in controlled entities
Investments in controlled entities are carried in the company's financial statements at cost less and impairment losses.

Accounting Policies applicable for the year ending 30 June 2005

Investments
Investments were carried at the lower of cost and recoverable amount.

l) Property, Plant and Equipment

Plant and equipment is stated at cost less accumulated depreciation and any impairment in value.

Land and improvements are measured at fair value less accumulated depreciation and any impairment losses on improvements after the date of the revaluation.

Depreciation is calculated on reducing balance over the estimated useful life of the asset as follows:

		Depreciation Rate
Buildings and improvements	-	5-20%
Plant and equipment	-	5-20%

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Impairment
The carrying values of plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

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.

If any such indication exists and where the carrying values exceed the estimated recoverable amounts, the assets or cash-generating units are written down to their recoverable amount.

The recoverable amount of plant and equipment is the greater of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Revaluations
Following initial recognition at cost, land and improvements are carried at a revalued amount which is the fair value at the date of the revaluation less any accumulated impairment losses.

Fair value is determined by reference to market-based evidence, which is the amount for which the assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transaction as at the valuation date.

Any revaluation surplus is credited to the asset revaluation reserve included in the equity section of the balance sheet unless it reverses a revaluation decrease of the same asset previously recognised in the income statement.

Any revaluation deficit is recognised in the income statement unless it directly offsets a previous surplus of the same asset in the asset revaluation reserve.

An annual transfer from the asset revaluation reserve is made to retained earnings for the depreciation relating to the revaluation surplus.

In addition, any accumulated depreciation as at revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset.

Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Independent valuations are performed with sufficient regularity to ensure that the carrying amount does not differ materially from the asset's fair value at the balance sheet date.

An item property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the period the item is derecognised.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

m) Leases

Leases of fixed assets where substantially all the risks and benefits incidental to the ownership of the asset, but not the legal ownership that are transferred to entities in the consolidated entity are classified as finance leases.

Finance leases are capitalised by recording an asset and a liability at the lower of the amounts equal to the fair value of the leased property or the present value of the minimum lease payments, including any guaranteed residual values. Lease payments are allocated between the reduction of the lease liability and the lease interest expense for the period.

Leased assets are depreciated on a straight-line basis over their estimated useful lives where it is likely that the consolidated entity will obtain ownership of the asset or over the term of the lease.

Lease payments for operating leases, where substantially all the risks and benefits remain with the lessor, are charged as expenses in the periods in which they are incurred.

Lease incentives under operating leases are recognised as a liability and amortised on a straight-line basis over the life of the lease term.

n) Employee Benefits

Provision is made for the company's liability for employee benefits arising from services rendered by employees to balance date. Employee benefits that are expected to be settled within one year have been measured at the amounts expected to be paid when the liability is settled, plus related on-costs. Employee benefits payable later than one year have been measured at the present value of the estimated future cash outflows to be made for those benefits.

o) Trade and other receivables

The Group has elected to apply the option available under AASB 1 of adopting AASB132 and AASB 139 from 1 July 2005. Outlined below are the relevant accounting policies for trade and other receivables applicable for the years ending 30 June 2005.

Accounting policies applicable for the year ending 30 June 2006
Trade receivables, which generally have 30-90 day terms, are recognised and carried at original invoice amount less an allowance for any uncollectible amounts.

An allowance for doubtful debts is made when there is objective evidence that the Group will not be able to collect the debts. Bad debts are written off when identified.

Accounting policies applicable for the year ending 30 June 2005.
Trade receivables were recognised and carried at original invoice amount less a provision for any uncollectible debts. An estimate for doubtful debts was made when collection of the full amount was no longer probable. Bad debts were written off as incurred.

p) Share-based payments

Share-based compensation benefits are provided to directors and executives.

The fair value of options granted to directors and executives is recognised as an employee benefit expense with a corresponding increase in contributed equity over the vesting period. The fair value is measured at grant date and recognised over the period during which the directors and/or executives becomes unconditionally entitled to the options.

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

The fair value at grant date is independently determined using an option pricing model that takes into account the exercise price, the term of the option, the vesting and performance criteria, the impact of dilution, the non-tradeable nature of the option, the share price at grant date and expected price volatility of the underlying share, the expected divided yield and the risk-free interest rate for the term of the option.

q) Cash and cash equivalents

Cash and cash equivalents in the balance sheet includes cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less. For the purposes of the Cash Flow Statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

r) Earnings per Share

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

Diluted EPS is calculated as net profit attributable to members, adjusted for:

- costs of servicing equity (other than dividends) and preference share dividends;
- the after tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary changes in revenues or expenses during the period that would result from the dilution of potential ordinary shares;

divided by the weighted average number of ordinary shares and dilutive potential ordinary shares, adjusted for any bonus element.

s) Trade Payables

The Group has elected to apply the option available under AASB 1 adopting AASB 132 and AASB 139 from July 1 2005. Outlines below are the relevant accounting policies for payable for the years ending 30 June 2006 and 30 June 2006

Accounting policies applicable for the year ending 30 June 2006.
Liabilities are recognised for amounts to be paid in the future, for goods and services received, whether or not billed to the consolidated entity. Trade accounts are normally settled in 60 days.

Accounting policies applicable for the year ending 30 June 2005.
Liabilities are recognised for amounts to be paid in the future, for goods and services received, whether or not billed to the consolidated entity. Trade accounts are normally settled in 60 days.

t) Research and Development Costs

Research costs are expensed as incurred.

Development expenditure incurred on an individual project is recognised as intangible assets only when the Group can demonstrate the technical feasibility of completing the project so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the development and the ability to measure reliably the expenditure attributable to the intangible asset during its development.

Notes To, And Forming Part Of, The Financial Statements For The Year Ended 30 June 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortisation and accumulated impairment losses.

Any expenditure carried forward is amortised over the period of expected future sales from the related project.

The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use, or more frequently when an indicator of impairment arises during the reporting year indicating that the carrying value may not be recoverable.

u) **Impairment of assets**

At each reporting date, the consolidated entity assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, the consolidated entity makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or group of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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.

w) **Provisions**

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

When the consolidated entity expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in income statement net of any reimbursement.

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

When discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
3. REVENUE AND EXPENSES				
3a. Revenue				
Operating activities				
Administration fees	-	-	62,270	252,757
Other income	2,664	5,105	2,664	5,105
Total Revenue	2,664	5,105	64,934	257,862
Non operating activities				
Interest received	33,150	123,918	32,155	123,918
Total Revenue	33,150	123,918	32,155	123,918
Total revenue	**35,814**	**129,023**	**97,089**	**381,780**
3b. Other Expenses				
Impairment in Value Of Investments	-	(28,951)	-	(28,951)
Loss on Disposal of Investments	-	17,284	-	17,284
Corporate Administration Costs				
ASX fees	27,354	29,215	27,354	29,215
Share based payments	15,181	-	15,181	-
Other administration expenses	451,303	692,829	513,377	692,919
Salaries and wages	776,970	663,247	776,970	663,247
Share registry expenses	54,116	26,851	54,116	26,851
Rent - Operating lease	58,569	53,575	58,569	53,575
Legal expenses	27,603	69,301	27,603	69,301
Consulting fees	190,255	117,894	190,255	117,894
Total Administration Costs	1,601,348	1,652,912	1,663,425	1,653,002
Total Other Expenses	**1,601,348**	**1,641,245**	**1,663,425**	**1,641,335**
3c. Other Income				
Other income	2,098	-	2,098	-
Government Grants	654,068	68,975	654,068	68,975
Legal fees refund	-	89,090	-	89,090
Total other income	**656,166**	**158,065**	**656,166**	**158,065**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
4. INCOME TAX				
The major components of income tax expenses are:				
Income Statement				
Current income tax				
Current income tax benefit:	-	-	-	-
Adjustments in respect of current income tax of previous years (research and development)	290,587	-	275,505	-
Deferred income tax benefit:				
Relating to origination and reversal of temporary differences	226,994	-	226,994	-
Income tax benefit reported in the income statement	517,581	-	502,499	-
Statement of Changes in Equity				
Deferred income tax related to items charged or credited directly to equity:				
Deferred income tax expenses arising from revaluation of land and improvements	226,994	-	226,994	-
Income tax expense reported in equity	226,994	-	226,994	-
A reconciliation between tax expense and the product of accounting profit before income tax multiplied by the consolidated entities applicable income tax rate is as follows:				
Accounting loss before income tax	(2,220,882)	(2,911,254)	(2,166,393)	(2,898,487)
At the company's statutory income tax rate of 30% (2005: 30%)	(666,265)	(873,376)	(649,918)	(869,546)
Non-deductible expenses	12,630	25,424	12,630	25,424
Adjustments in respect of current income tax of previous years (research and development)	(290,587)	-	(275,505)	-
Deferred tax assets not previously brought to account now recognised	(226,994)	-	(226,994)	-
Deferred tax assets not recognised	666,434	847,952	650,087	844,122
Other	(12,799)	-	(12,799)	-
Income tax benefit reported in the income statement	(517,581)	-	(502,499)	-

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

Deferred Income Tax	Balance sheet		Income statement	
	2006	2005	2006	2005
	$	$	$	$
Consolidated				
Deferred tax liabilities				
Revaluation of land and improvements*	(226,994)	-	-	-
Gross deferred income tax liabilities	(226,994)	-	-	-
*income tax expense recognised in equity				
Deferred tax assets				
Provisions	6,256	16,285	10,029	-
Tax losses available for offset against future taxable income	4,425,956	3,849,972	(575,984)	-
Deferred tax assets not recognised	(4,205,218)	(3,866,257)	338,961	-
Gross deferred income tax assets	226,994	-		
Total deferred tax (income)/expense			(226,994)	-
Parent				
Deferred tax liabilities				
Revaluation of land and improvements*	(226,994)	-	-	-
Gross deferred income tax liabilities	(226,994)	-	-	-
*income tax expense recognised in equity				
Deferred tax assets				
Provisions	6,256	16,285	10,029	-
Tax losses available for offset against future taxable income	4,425,956	3,849,972	(575,984)	-
Deferred tax assets not recognised	(4,205,218)	(3,866,257)	338,961	-
Gross deferred income tax assets	226,994	-		
Total deferred tax (income)/expense			(226,994)	-

Deferred tax assets in relation to losses will only be available if:

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

The consolidated entity has not formed a tax consolidation group as at 30 June 2006.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006	Consolidated Entity 2005	Parent 2006	Parent 2005
5. CURRENT ASSETS - RECEIVABLES				
Receivables - trade	-	15,447	-	39,552
Receivables - sundry	3,104	98,303	-	87,787
Accrued interest receivables	-	4,618	-	4,618
	3,104	**118,368**	**-**	**131,957**

Trade and sundry receivables are non interest bearing and are generally received on 30-60 day terms.

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
6. CURRENT ASSETS - OTHER ASSETS				
Prepayments	52,231	39,128	52,231	39,128
	52,231	**39,128**	**52,231**	**39,128**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006	Consolidated Entity 2005	Parent 2006	Parent 2005
7. NON CURRENT ASSETS - RECEIVABLES				
Loan to controlled entity	-	-	**417,680**	**410,429**
Allowance for doubtful debts	-	-	**(417,680)**	**(410,429)**
	-	-	-	-
7. NON-CURRENT ASSETS - PROPERTY, PLANT AND EQUIPMENT				
Plant And Equipment				
Plant and equipment at cost	330,228	300,987	330,228	300,987
Less accumulated depreciation	(117,406)	(87,754)	(117,406)	(87,754)
	212,822	**213,233**	**212,822**	**213,233**
Land and improvements at cost	-	257,991	-	257,991
Land and improvements at fair value	1,020,000	-	1,020,000	-
	1,020,000	**257,991**	**1,020,000**	**257,991**
Leased improvements at cost	95,220	58,030	95,220	58,030
Less accumulated depreciation	(16,830)	(8,042)	(16,830)	(8,042)
	78,390	**49,988**	**78,390**	**49,988**
	1,311,212	**521,212**	**1,311,212**	**521,212**
Reconciliations				
Plant and equipment				
Carrying amount at the beginning of the year	213,233	178,929	213,233	178,929
Additions	59,656	61,017	59,656	61,017
Impairment	(30,415)	-	(30,415)	-
Depreciation	(29,652)	(26,713)	(29,652)	(26,713)
Carrying Amount At End Of Year	**212,822**	**213,233**	**212,822**	**213,233**
Land and improvements				
Carrying amount at the beginning of the year	257,991	254,654	257,991	254,654
Additions	2,364	3,337	2,364	3,337
Revaluation during the year	759,645	-	759,645	-
Carrying Amount At End Of Year	**1,020,000**	**257,991**	**1,020,000**	**257,991**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006	Consolidated Entity 2005	Parent 2006	Parent 2005
	$	$	$	$
8. NON-CURRENT ASSETS - PROPERTY, PLANT AND EQUIPMENT (cont.)				
Leasehold improvements				
Carrying amount at the beginning of the year	49,988	46,003	49,988	46,003
Additions	36,640	8,254	36,640	8,254
Depreciation	(8,238)	(4,269)	(8,238)	(4,269)
Carrying Amount At End Of Year	**78,390**	**49,988**	**78,390**	**49,988**
8a. Revaluation of land and buildings				
The consolidated entity engaged Valuations WA an accredited independent valuer, to determine the fair value of its land and buildings. Fair value is determined directly by reference to market-based evidence, which is the amounts for which the assets could be exchanged between a knowledgeable willing buyer and a knowledgeable willing seller in an arm's length transaction as at the valuation date. The effective date of the revaluation was 30 June 2006.				
If land and buildings were measured using the cost model the carrying amounts would be as follows:				
Net carrying amount	**260,355**	**257,991**	**260,355**	**257,991**
9. NON CURRENT ASSETS - OTHER FINANCIAL ASSETS				
Available for sale investments (9a)				
Cost	-	36,175	-	36,175
	-	36,175	-	36,175
Shares in unlisted controlled entities (9b)	-	-	1	1
Carrying amount at end of year	**-**	**36,175**	**1**	**36,176**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

9b. SUBSIDIARY COMPANIES
Interests held by the company in controlled entities:

Company Name and Place of Incorporation	Principal Activities	Ownership Interest 2006 %	Ownership Interest 2005 %	Carrying Amount of Investment 2006 $	Carrying Amount of Investment 2005 $
Solbec (No 1) Pty Ltd (incorporated in Australia)	Pharmaceuticals Research	100	100	1	1

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
10. CURRENT LIABILITIES - PAYABLES				
Trade creditors and accruals	636,156	523,012	636,156	523,012
	636,156	**523,012**	**636,156**	**523,012**

Trade payable are non-interest bearing and are normally settled on 30 day termS.

	Consolidated Entity 2006	Consolidated Entity 2005	Parent 2006	Parent 2005
11. CURRENT LIABILITIES - PROVISIONS				
Employee benefits	20,853	58,901	20,853	58,901
	20,853	**58,901**	**20,853**	**58,901**
12. CURRENT LIABILITIES - Other				
Unearned grant income	282,295	-	282,295	-
	282,295	-	**282,295**	-

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
13. CONTRIBUTED EQUITY				
13a. Issued and Paid Up Capital				
(2006 : 198,421,556) (2005 : 168,372,334) ordinary fully paid shares	19,730,688	17,138,366	19,730,688	17,138,366
	19,730,688	**17,138,366**	19,730,688	**17,138,366**

	2006		2005	
	Number of shares	$	Number of shares	$
13b. Movement in shares				
Beginning of the financial year	168,372,334	17,138,366	159,332,025	16,053,409
Issued during the year:				
9,038,809 options exercised at 12 cents each	-	-	9,038,809	1,084,657
1,500 options exercised at 20 cents each	-	-	1,500	300
Shares issued on cancellation of options	19,069,222	1,659,022	-	-
10,980,000 shares issued at 8.5 cents per share 20 May 2006	10,980,000	933,300	-	-
End of the financial year	198,421,556	19,730,688	168,372,334	17,138,366

Effective 1 July 1998, the Corporation legislation in place abolished the concepts of authorised capital and par value shares. Accordingly, the Parent does not have authorised capital nor par value in respect of its issued shares.

During the year 19,069,222 shares were issued on cancellation of options at one share for seven options held. The value on the closing date of the issue was $ 0.0870 per share.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 Number	Consolidated Entity 2005 Number	Parent 2006 Number	Parent 2005 Number
13c. Terms And Conditions of Ordinary Shares				
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. Ordinary shares entitle their holder to one vote, either in person or by proxy, at a meeting of the company.				
13d. Movement in Options				
Balance at beginning of year	159,664,831	167,705,140	159,664,831	167,705,140
Granted to General Manager on 25 May 2006.	1,500,000	-	1,500,000	-
Granted to the Directors at the General Meeting of Shareholders on 25 November 2004.	-	4,000,000	-	4,000,000
Expired 31 December 2004	-	(3,000,000)	-	(3,000,000)
Options redeemed via issue of shares	(133,482,631)	-	(133,482,631)	-
Exercised during the year	-	(9,040,309)	-	(9,040,309)
*** Balance At End Of Year**	**27,682,200**	**159,664,831**	**27,682,200**	**159,664,831**

* Option details at 30 June 2006
500,000 exercisable at 12 cents on the 31 December 2009.
750,000 exercisable at 15 cents on the 31 December 2009.
250,000 exercisable at 18 cents on the 31 December 2009.
4,000,000 exercisable at 22 cents on the 25 November 2007.
4,000,000 exercisable at 22 cents on the 9 June 2007.
3,000,000 exercisable at 20 cents on the 9 June 2007.
15,182,200 exercisable at 30 cents 19 September 2006

* Option details at 30 June 2005
4,000,000 exercisable at 22 cents on the 25 November 2007.
4,000,000 exercisable at 22 cents on the 9 June 2007.
3,000,000 exercisable at 20 cents on the 9 June 2007.
148,664,831 exercisable at 30 cents 19 September 2006

Option holders do not have any rights, by virtue of their option holding, to vote at a meeting of the Company.

Share Options

For details of the share based payment option scheme under which options to subscribe for the company shares are granted to directors and executives. Refer to note 20.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
14. RESERVES				
Option premium reserve (14 a)	849,858	2,493,699	849,858	2,493,699
Asset revaluation reserve (14 b)	532,651	-	532,651	-
Total reserves	1,382,509	2,493,699	1,382,509	2,493,699
14a. Option Premium Reserve				
Balance at beginning of the financial year	2,493,699	2,493,699	2,493,699	2,493,699
Issue of options	15,181	-	15,181	-
Options redeemed on issue of shares	(1,659,022)	-	(1,659,022)	-
Balance At End Of The Financial Year	**849,858**	**2,493,699**	**849,858**	**2,493,699**
14b. Asset Revaluation Reserve				
Balance at beginning of the year	-	-	-	-
Revaluation of property during the year (net of tax)	532,657	-	532,657	-
Balance at end of financial year	**532,657**	**-**	**532,657**	**-**

Nature and purpose of reserves

Asset revaluation reserves

The asset revaluation reserve is used to record increases in the fair value of buildings and decreases to the extent that such decreases relate to an increase on the same asset previously recognised in equity.

Option premium reserve

The option premium reserve is used to record premiums received when options are issued to shareholders at a premium.

15. ACCUMULATED LOSSES				
Balance at beginning of the year	(18,093,745)	(15,182,491)	(18,140,356)	(15,241,869)
Net loss for the period	(1,703,301)	(2,911,294)	(1,663,894)	(2,898,487)
Balance At End Of Year	**(19,797,046)**	**(18,093,745)**	**(19,804,250)**	**(18,140,356)**

16. SEGMENT INFORMATION

The company is involved in one business and one geographical segment being pharmaceutical research and development in Australia.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
17. EXPENDITURE COMMITMENTS				
17a. Lease expenditure commitments (non cancellable)				
The company entered into an operating lease contract for the premises it occupies at Unit 1, 298 Selby Street, Osborne Park on 1st June 2005. The lease is for 24 months.				
Commitments payable				
Not later than 1 year	56,000	56,000	56,000	56,000
Later than 1 year but not later than 5 years	-	56,000	-	56,000
Aggregated lease expenditure contracted for at reporting date	**56,000**	**112,000**	**56,000**	**112,000**
17b. Capital Expenditure Commitments				
There were no capital expenditure commitments contracted for at balance date.				
17c. Remuneration commitments				
Commitments for the payment of salaries and other remuneration under long-term employment contracts in existence at the reporting date but not recognised as liabilities, payable:				
Within one year	348,800	-	348,800	-
After one year but not more than five years	319,733	-	319,733	-
Longer than five years	-	-	-	-
	668,533	**-**	**668,533**	-
Amounts disclosed as remuneration commitments include commitments arising from the service contracts of directors and executives referred to in note 19 that are not recognised as liabilities and are not included in the directors' or executives' remuneration.				
18. REMUNERATION OF AUDITOR				
Amounts received, or due and receivable by the auditor for:				
Audit or review of the financial statements	35,685	15,629	35,685	15,629
Other	-	-	-	-
	35,685	**15,629**	**35,685**	**15,629**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
19. EMPLOYEE BENEFITS AND SUPERANNUTION COMMITMENTS				
Employee benefits				
The aggregate employee benefit liability is comprised of:				
Accrued wages, salaries and on-costs	50,868	10,463	50,868	10,463
Provisions (current)	20,853	58,901	20,853	58,901
	71,721	**69,364**	**71,721**	**69,364**

20. SHARE BASED PAYMENTS

Executive and Director Share Based Payment Plan

An Executive and Director Share Based Payment Plan ("the Plan") has been established where the company, at the discretion of the Directors, may grant options over the ordinary shares of the company to executives and directors of the company. The company has adopted this plan to enable executives and directors to acquire an ownership interest in the company.

The options issued under the Plan are not quoted on the ASX.

In May 2006, the company issued options to executives. These options were issued for nil consideration, other than services rendered. The exercise prices of the options are detailed in the table below. Once exercised, the shares rank equally with the existing shares of the company.

The following table illustrates the number of and movements in share options issued during the year.

Terms and Conditions for each Grant

	2006 Numbers	2005 Numbers
Outstanding at the beginning of the year	4,000,000	-
Granted during the year	1,500,000	4,000,000
Outstanding at the end of the year	5,500,000	4,000,000

The outstanding balance as at 30 June 2006 is represented by:

- 4,000,000 options over ordinary shares with an exercise price of 22 cents, exerciseable until 25 November 2007;
- 500,000 options over ordinary shares with an exercise price of 12 cents, exerciseable until 31 December 2009;
- 750,000 options over ordinary shares with an exercise price of 15 cents, exerciseable until 31 December 2009;
- 250,000 options over ordinary shares with an exercise price of 18 cents, exerciseable until 31 December 2009;

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

During the financial year and up to the date of this financial report nil options have been exercised. The market price of ordinary shares of the company was 6.5 cents at 30 June 2006.

The amounts recognised in the financial statements of the company and consolidated entity in relation to the executive share options exercised during the financial year were nil.

(i) work at commercial rates.
These payments are not included in the compensation disclosures above.

21. DIRECTOR AND EXECUTIVE DISCLOSURES

21a. Details of Key Management Personnel

(i) Directors

Anthony Kiernan	Chairman
Stephen J Carter	Non-Executive
Michael Grant	Non Executive
Professor John Papadimitriou	Non Executive
Dr David Hung	Non Executive (resigned 8/07/06)
Dr Graeme Howie	Managing Director (appointed 6/10/05)

(ii) Executives

David Sparling	General Manager
John Sendziuk	Company Secretary

21b. Remuneration Philosophy

This section details the remuneration arrangements in place for the executives and directors of Solbec Pharmaceuticals Ltd.

The broad remuneration philosophy is to ensure that remuneration properly reflects the relevant person's duties and responsibilities, and that the remuneration is competitive in attracting, retaining and motivating people of the highest quality. The Board believes that the best way to achieve this objective is to provide any executive directors and executives with a remuneration package consisting of components that reflect the person's responsibilities, duties, personal and corporate performance.

To this end Solbec follows the following principles;

- Provide competitive rewards.
- That a part of the senior executive's remuneration is "at risk" that is linked to pre-determined achievements.
- That any variable executive remuneration has appropriate and demanding performance hurdles attached.

Remuneration Committee

Solbec does not have a remuneration committee. The remuneration of non-executive directors is determined by the Board as a whole having regard to industry standards of similar sized entities.

The aggregate amount payable to the Company's non-executive directors must not exceed the maximum annual amount approved by the Company's shareholders. An aggregate amount of $200,000 was approved by shareholders at the Annual General Meeting held in May 2006.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

Senior Manager and Executive Director Remuneration

The company aims to reward executives with a level and mix of remuneration commensurate with their position and responsibilities within the company and so as to"

- reward executives for company, business unit and individual performance against targets set by reference to appropriate benchmarks;
- align the interests of executives with those of shareholders;
- link rewards with the strategic goals and performance of the company; and
- ensure total remuneration is competitive by market standards.

The Chairman, subject to Board approval, generally sets remuneration of the Managing Director and the General Manager.

Fixed Remuneration

The level of fixed remuneration for executives is set so as to provide a base level of remuneration which is both appropriate to the position and competitive in the market.

Fixed remuneration is reviewed annually.

Variable Remuneration

Short term incentives (STI) may be linked to achievement of the companies operational targets with the remuneration received if the relevant executives achieve the target.

The directors, subject to shareholder approval, and executives are eligible to participate in the Company's share option plan whereby options may be granted at an exercise price above the prevailing share price. This premium in conversion price, coupled with an appropriate vesting period, provides a long term incentive (LTI) whereby directors and executives will benefit only if there is a substantial improvement in the Company's share price. The number of options granted to each director and executive is determined by the Board based on the Company's and the eligible participant's performance.

Employment Contracts

The Managing Director, Dr Graeme Howie is employed under contract. The current employment commenced on the 15th of May 2006. The key terms of the contract are;

- Dr. Howie may resign from his position giving 6 months written notice and thus terminate his contract.
- The Company may terminate his contract by providing 6 months written notice or provide 3 months pay in lieu of notice however, the contract may be terminated at any time without notice if serious misconduct has occurred.
- Dr Howie will be paid a base salary of $160,000 per annum plus statutory superannuation and receive a vehicle allowance of $4,000 per annum.

The General Manager, Mr. David Sparling, is employed under contract. The current employment commended 20th March 2006. The key terms of the contract are;

- Term of contract 24 months.
- Base salary of $160,000 per annum plus superannuation.
- 1,500,000 options vesting over a period of 12 months.
- The Company may terminate his contract by providing 6 months written notice or provide 6 months pay in lieu of notice however, the contract maybe terminated without notice if serious misconduct has occurred.

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Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

Details of remuneration for year ended 30 June 2006
The remuneration for each director and each of the executive officers of the consolidated entity receiving remuneration during the year was as follows.

Directors remuneration

2006	Short Term			Post Employment	Share Based Payment		
	Consulting Fees	Salary	Directors Fees	Super	Options	Total	% performance based
Name	$	$	$	$	$	$	
G Howie (Managing Director)	24,590	37,110	-	3,340	-	65,040	-
S J Carter (Non Executive)	68,590	131,460	11,477	11,101	-	222,628	-
A Kiernan (Chairman)	10,585	-	22,500	2,025	-	35,110	-
M Grant (Non Executive)	3,100	-	18,375	1,654	-	23,129	-
J Papadimitriou (Non Executive)	-	-	18,375	1,654	-	20,029	-
D Hung (Non Executive)	-	-	18,375	-	-	18,375	-
	106,865	168,570	89,102	19,774	-	384,311	-

2005	Short Term			Post Employment	Share Based Payment		
	Consulting Fees	Salary	Directors Fees	Super	Options	Total	% performance based
Name	$	$	$	$	$	$	
S J Carter (Non Executive)	-	189,356	-	16,083	-	205,439	-
A Kiernan (Chairman)	31,944	-	30,000	2,700	-	64,644	-
M Grant (Non Executive)	12,925	-	24,500	2,205	-	39,630	-
J Papadimitriou (Non Executive)	-	-	25,725	2,315	30,000	58,040	52
D Hung (Apptd 13/10/04) (Non Executive)	-	-	17,369	-	30,000	47,369	63
	44,869	189,356	97,594	23,303	60,000	415,122	14

Remuneration of other key management personnel

2006	Short Term		Post Employment	Share based payment	Long Term Incentive Plan		
	Consulting Fees	Salary	Superannuation	Options	Shares	Total	% performance Based
Name	$	$	$	$	$	$	%
David Sparling (General Manager)	-	118,729	9,714	15,182	1,000	144,625	11
John Sendziuk (Company Secretary)	35,805	-	-	-	-	35,805	-
	35,805	118,729	9,714	15,182	1,000	180,430	9

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

2005	Short Term		Post Employment	Share based payment	Long Term Incentive Plan		% performance
	Consulting Fees	Salary	Superannuation	Options	Shares	Total	Based
Name	$	$	$	$	$	$	
John Sendziuk (Company Secretary)	27,404	-	-	-		27,404	-
	27,404	-	-	-	-	27,404	-

Compensation of Key Management Personnel by category

	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
Short-term	519,071	359,223	519,071	359,223
Post-employment	29,488	23,303	29,488	23,303
Share-based payment	15,182	60,000	15,182	60,000
Long-term incentive	1,000	-	1,000	-

Options Granted as part of remuneration

Terms and Conditions for each Grant

2006 Name	Granted Number	Grant date	Value per option at grant date	Exercise price per share	First exercise date	Last exercise date	% of Remuneration
D Sparling	500,000	15/05/06	.016 cents	12 cents	15/05/06	31/12/09	2.8
	750,000	15/05/06	.012 cents	15 cents	30/09/06	31/12/09	1.0
	250,000	15/05/06	.022 cents	18 cents	30/03/07	31/12/09	7.4

2005 Name	Granted Number	Grant date	Value per option at grant date	Exercise price per share	First exercise date	Last exercise date	% of Remuneration
J Papadimitriou	2,000,000	24/11/04	.015 cents	22 cents	15/05/06	24/11/07	2.8
D Hung	2,000,000	24/11/0	.015 cents	22 cents	30/09/06	24/11/07	1.0
D Sparling	-	-	-	-	-	-	-

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

21c. Option Holdings of Directors and Their Related Parties

	Beginning of Period	Granted as Remuneration	Options Lapsed	Options Exercised	Cancelled for shares	Net other change	Balance at end of Period
2006:							
SJ Carter	4,185,414	-	-	-	(1,185,414)	-	3,000,000
A Kiernan	3,537,500	-	-	-	(1,537,500)	-	2,000,000
M Grant	4,882,169	-	-	-	(2,882,169)	-	2,000,000
J Papadimitriou	2,000,000	-	-	-	-	-	2,000,000
D Hung	2,000,000	-	-	-	-	-	2,000,000
G Howie	-	-	-	-	-	-	-
2005:							
SJ Carter	5,886,686	-	(1,500,000)	-	-	(201,272)	4,185,414
A Kiernan	3,500,000	-	-	-	-	37,500	3,537,500
M Grant	5,082,169	-	-	(200,000)	-	-	4,882,169
J Papadimitriou	-	2,000,000	-	-	-	-	2,000,000
D Hung	-	2,000,000	-	-	-	-	2,000,000

21d. Shareholdings of Directors and Their Related Parties

	Beginning of Period	Net Change during Period	Balance at end of Period
2006:			
SJ Carter	1,238,300	169,347	1,407,647
A Kiernan	1,275,000	510,645	1,785,645
M Grant	1,464,339	527,739	1,992,078
J Papadimitriou	-	55,000	55,000
D Hung	-	-	-
G Howie	-	150,000	150,000
2005:			
SJ Carter	1,102,058	136,242	1,238,300
A Kiernan	875,000	400,000	1,275,000
M Grant	1,264,339	200,000	1,464,339
J Papadimitriou	-	-	-
D Hung	-	-	-

The options which were cancelled for shares and form part of the net change during the 2006 year period were exchanged on the basis of one share for seven options. They were part of the cancellation of options for shares offer which was made to all option holders of the company. The remainder of the net change during 2006 relates to market purchases made during the year.

The net change during 2005 relates to market purchases made during the year.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

21e. Option Holdings of Executives

	Beginning of Period	Net Change during Period	Balance at end of Period
2006:			
D Sparling	-	1,500,000	1,500,000
J Sendziuk	-	-	-
2005:			
J Sendziuk	-	-	-

Options issued to D Sparling during 2006 formed part of his remuneration for that year.

21f. Share holdings of Executives

The executives do not hold/or held any shares in the company during the year.

21g. Other Transactions with Key Management Personnel

(i) A J Kiernan, a director of the company was paid $10,585 (2005 : $31,944) for legal consulting work at commercial rates.
(ii) M Grant a director of the company was paid $3,100 (2005 - 12,925) for consulting work at commercial rates.
(iii) S Carter a director of the company was paid $68,590 (2005 - nil) for consulting work at commercial rates.
(iv) G Howie a director of the company was paid $24,590 (2005 - nil) for consulting work at commercial rates.

These payments are not included in the compensation disclosures above.

22. RELATED PARTY TRANSACTIONS

Ultimate Parent

Solbec Pharmaceuticals Ltd is the ultimate parent company.

Other related party transactions

The company funded the activities of the wholly owned subsidiary Solbec (No 1) Pty Ltd. At balance date the amount loaned to the subsidiary amounted to $417,680. This loan is interest free and has no specified repayment date. The loan has been fully provided against in the parent company.

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

23. NOTES TO THE STATEMENT OF CASH FLOWS	Consolidated Entity 2006 $	Consolidated Entity 2005 $	Parent 2006 $	Parent 2005 $
23a. Reconciliation of cash and cash equivalents				
Cash as at the end of the financial year as shown in the Statement of Cash Flows is reconciled to the related items in the balance sheet as follows:				
Cash at bank	888,708	97,259	884,607	37,059
Cash on hand	200	200	200	200
Term deposits	-	1,307,890	-	1,307,890
TOTAL CASH AND CASH EQUIVALENTS	**888,908**	**1,405,349**	**884,807**	**1,345,149**
23b. Reconciliation Of Net Loss After Income Tax To Net Cash Used In Operating Activities				
Operating loss after income tax	(1,703,301)	(2,911,254)	(1,663,894)	(2,898,287)
Loss on disposal of non-current assets	30,415	-	30,415	-
(Gain)/loss on disposal of investments	(2,098)	17,284	(2,098)	17,284
Allowance for diminution in value of non current assets	-	(28,951)	-	(28,951)
Share based payments	15,181	-	15,181	-
Allowance for doubtful debts	-	-	-	239,900
Depreciation	37,890	30,982	37,890	30,982
Movement in Assets and Liabilities				
Receivables	116,417	112,799	122,760	92,642
Prepayments	(13,103)	(11,225)	(13,103)	(11,225)
Unearned income	282,295	-	282,295	-
Trade creditors and accruals	113,144	400,514	113,144	400,514
Deferred tax liability recognised in equity	(226,994)	-	(226,994)	-
Provisions	(38,048)	22,747	(38,048)	22,747
Net Cash Used In Operating Activities	**(1,388,202)**	**(2,367,104)**	**(1,342,452)**	**(2,134,394)**

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

23c. Financing facilities

At balance date, the following financing facilities had been negotiated and were available:

Total Facilities	
Bank overdraft -	$400,000
Used	Nil
Unused	$400,000
Visa facility	$10,000
Facility used to reporting date is	$5,997
Facility unused at reporting date	$4,003
Cornell Capital Partners Offshore	
Equity line of credit agreement	$5,000,000
Used	Nil
Unused	$5,000,000

Details of Financing Facilities

(A) The over draft is secured on the freehold property owned by the Consolidated Entity and is reviewed annually.

(B The visa facility is unsecured, is ongoing and is cleared monthly.

(C) The Cornell Capital Facility is an equity line of credit facility with a total capital available of $5M. Solbec has 3 years to use the facility commencing on the activation date (i.e. the date Solbec first calls on the facility). The facility contains a provision for a once off loan amount of up to $500,000 which is at the discretion of Cornell Capital. Each draw down notice can be made for up to $100,000 at a time and the equity consideration for each such draw down is calculated at 98% of the volume weighted average price for the previous ten trading days. A once off activation fee of $70,000 (which may be paid via stock) is payable at the time of the first draw down, an implementation fee of $20,000 (which may be paid via stock) is payable at the time of each draw down and the facility has an annual fee of $15,000.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

24. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The consolidated entity's principal financial instruments, comprise bank loans and overdrafts, cash and short-term deposits, and receivables and payables.

The main purpose of these financial instruments is to raise fiancé for the consolidated entity's operations. The consolidated entity has various other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations. It is, and has been throughout the period under review, the consolidated entity's policy that no trading in financial instruments shall be undertaken. The main risks arising from the consolidated entity's financial instruments are cash flow interest rate risk, liquidity risk, and credit risk. The Board reviews and agrees policies for managing each of these risks by direction to the Managing Director at Directors meetings.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 2 to the financial statements.

25. FINANCIAL INSTRUMENTS

25a. Interest Rate Risk

The Consolidated entity's exposure to interest rate risk, which is the risk that a financial instrument's value will fluctuate as a result of changes in market, interest rates and the effective weighted average interest rates on this financial assets, is as follows:

2006 Consolidated	Weighted Average Effective Interest	Floating Interest	Non-Interest Bearing	Total
	%	$	$	$
Financial Assets				
Other receivables	-	-	55,335	55,335
Cash at bank	5.1	888,908	-	888,908
Total Financial Assets	-	888,908	55,335	944,243
Financial Liabilities				
Trade payables	-	-	636,156	636,156
Pre-payments	-	-	282,295	282,295
Provisions	-	-	20,853	20,853
Total Financial Liabilities	-	-	939,304	939,304
Net Financial Assets (liabilities)	**-**	888,908	**(883,969)**	**4,939**

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

2005 Consolidated	Weighted Average Effective Interest	Floating Interest	Non-Interest Bearing	Total
	%	$	$	$
Financial Assets				
Interest bearing deposits	5.2	1,307,890	-	1,307,890
Trade receivables	-	-	15,447	15,447
Cash at bank	4.5	98,303	-	98,303
Security deposits	-	-	97,459	97,459
Investments	-	-	36,175	36,175
Total Financial Assets		1,406,193	247,384	1,555,274
Financial Liabilities	-	-		
Trade payables	-	-	523,012	523,012
Provisions	-	-	58,901	58,901
Total Financial Liabilities		-	581,913	581,913
Net Financial Assets (liabilities)		1,307,890	(334,529)	973,361

25b. Credit Risk

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date, to recognised financial assets is the carrying amount, net of any provisions for doubtful debts, as disclosed in the statement of financial position and notes to the financial statements.

The consolidated entity does not have any material risk exposure to any single debtor or group of debtors, under financial instruments entered into by it.

25c. Net fair values

Methods and assumptions used in determining net fair value.

For assets and other liabilities, the net fair value approximates their carrying value. No financial assets and financial liabilities are readily traded on organised markets in standardised form, other than listed investments. The fair value of listed investments is determined by reference to the share price at the balance date. The economic entity has no financial assets where carrying amount exceeds net fair values at balance date.

The aggregate net fair values and carrying amounts of financial assets and financial liabilities are disclosed in the balance sheet and in the notes to and forming part of the financial statements.

26. EARNINGS PER SHARE

Basic earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent (after deducting interest on the convertible redeemable preference shares) by the weighted average number of ordinary shares outstanding during the year.

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

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

SOLBEC PHARMACEUTICALS LTD

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

26. EARNINGS PER SHARE (cont.)	Consolidated Entity 2006	Consolidated Entity 2005
Basic earnings per share - loss per share	(1.0 cents)	(1.7) cents
Diluted earnings per share - loss per share	(1.0 cents)	(1.7) cents
Weighted average number of ordinary shares outstanding during the year in calculation of basic earnings per share	177,332,852	168,372,334
Weighted average number of ordinary shares outstanding during the year in calculation of diluted earnings per share	177,332,852	168,372,334
Loss used in calculating basic and diluted EPS	1,703,301	2,911,294

There are 27,682,200 options on issue that are not dilutive.

27. SUBSEQUENT EVENTS

The consolidated entity raised $1,298,491 in August 2006 through the issue of 18,549,858 shares at 7 cents per share for working capital.

No other matters or circumstances have arisen since the end of the financial year which significantly affected or may significantly affect the operations of the company, the results of those operations, or the state of affairs of the company in future financial years.

28. TRANSITION TO AIFRS

For all periods up to and including the year ended 30 June 2005, the Group prepared its financial statements in accordance with Australian generally accepted accounting practice (AGAAP). These financial statements for the year ended 30 June 2006 are the first the Group is required to prepare in accordance with Australian equivalents to International Financial Reporting Standards (AIFRS).

Accordingly, the Group has prepared financial statements that comply with AIFRS applicable for periods beginning on or after 1 January 2005 and the significant accounting policies meeting those requirements are described in note 2. In preparing these financial statements, the Group has started from an opening balance sheet as at 1 July 2004, the Group's date of transition to AIRFS, and made those changes in accounting policies and other restatements required by AASB 1 *First-time adoption of AIFRS.*

This note explains the principal adjustments made by the Group in restating its AGAAP balance sheet as at 1 July 2004 and its previously published AGAAP financial statements for the year ended 30 June 2005.

AASB 1 allows first-time adopters certain exemption from the general requirement to apply AIFRS retrospectively.
The Consolidated entity has taken the following exemptions:

- AASB 2 Share -Based Payments has not been applied to any equity instruments that were granted on or before 7 November 2002, nor has it been applied to equity instruments granted after 7 November 2002 that vested before 1 January 2005.

- AASB 132 Financial Instruments: Disclosure and Presentation and AASB 139 Financial Instruments: Recognition and Measurement have been applied from 1 January 2005.

The impact of adoption of AIFRS on the total equity and profit after tax as reported under Australian Accounting Standards applicable before 1 July 2005 ('AGAAP') are illustrated below.

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

(a) Reconciliation of total equity under AGAAP to that under AIFRS

	Note	Consolidated		Parent	
		1 July 2004 $	30 June 2005 $	1 July 2004 $	30 June 2005 $
Total equity under AGAAP		3,403,653	1,792,170	3,344,275	1,745,559
De-recognition of research costs (c)		(39,036)	(253,850)	(39,036)	(253,850)
Total equity under AIFRS		3,364,617	1,538,320	3,305,239	1,491,709

Notes To, And Forming Part Of, The Financial Statements

For The Year Ended 30 June 2006 continued

28. TRANSITION TO AIFRS (cont.)

(b) Reconciliation of profit after tax under AGAAP to that under AIFRS

	Note	Consolidated Entity Year Ended 30 June 2005 $	Parent Year Ended 30 June 2005 $
Loss after tax under AGAAP		2,696,440	2,683,673
Adjustment to research costs (c)		214,814	214,814
Loss after tax under AIFRS		2,911,254	2,898,487

(c) Description of AIFRS adjustments

Under AGAAP, Solbec capitalised certain costs in respect of research product inventory and its application for patents and licences associated with its research projects. Under AASB 138, all costs relating to research projects are required to be expensed as incurred. The costs capitalised as at the date of transition to AIFRS (1 July 2004) have been adjusted against accumulated losses, and costs incurred subsequently have been adjusted against research and development expenditure in the relevant period.

(d) Explanation of material adjustments to the cash flow statements

There are no material differences between the cash flow statements presented under AIFRS and those presented under AGAAP.

(d) Impact of adoption of AASB 132 and AASB 139

There is no material impact to the Company or the Consolidated entity upon the adoption of AASB 132 and ASB 139 on 1 July 2005

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Shareholders' Information

DIRECTORS' INTERESTS IN SECURITIES AS AT 23rd AUGUST 2006

In compliance with requirements of the Australian Stock Exchange Limited, the following statement shows the interests of the directors in the securities of the company as at the date of this report:

Director	Ordinary Shares		Options	
	Direct Interest	Indirect Interest	Direct Interest	Indirect Interest
Stephen J Carter	28,572	1,379,075	3,000,000	-
Anthony Kiernan	791,930	993,715	2,000,000	-
Michael Grant	1,101,935	890,143	2,000,000	-
John Papadimitriou	-	55,000	2,000,000	-
David Hung (resigned 8/07/06)	-	-	2,000,000	-
Graeme Howie (appointed 6/10/05)	100,000	50,000	-	-

COMPANY DETAILS

i) The name of the company secretary is John E Sendziuk.

ii) The address of the registered office in Australia is C/- RSM Bird Cameron, Unit 1-6, 18 Parry Street, Fremantle WA 6062. The telephone number is (08) 9336 1266, facsimile number is (08) 9430 6744.

The address of the principal office is Unit1, 298 Selby Street, Osborne Park WA 6018.

The telephone number is (08) 9446 7555, facsimile number is (08) 9446 8777.

VOTING RIGHTS

a) On a show of hands each member present in person or by proxy has one vote.

b) On a poll every member present in person or by proxy has one vote for each share held in the company.

STOCK EXCHANGES THAT HAVE GRANTED QUOTATION TO THE COMPANY'S SECURITIES

The company's securities are quoted on the Australian Stock Exchange Limited.

SOLBEC PHARMACEUTICALS LTD

Shareholders' Information continued

DISTRIBUTION AND NUMBER OF HOLDERS OF LISTED SHARES AS AT 23rd AUGUST 2006

Spread Of Holdings:	Holders	Units
1 - 1,000	51	22,083
1,001 - 5,000	355	1,276,906
5,001 - 10,000	511	4,321,618
10,001 - 100,000	1,549	59,410,604
100,001 - over	367	151,940,203
	2,833	**216,971,414**
Holders holding less than a marketable parcel	**576**	**2,351,131**
Percentage held by twenty largest holders is		

TOP TWENTY SHAREHOLDERS AS AT 23rd AUGUST 2006	No of Shares	% of Issued Shares
Yandal Investments Pty Ltd	10,464,286	4.82
Apple Nominees Pty Ltd	6,000,000	2.77
Mr Todd Matthew Wright Bennett	5,761,000	2.66
Mr Grant Karl Maynard Bennett	5,194,286	2.39
Ms Angela Mary Maynard Wright	4,976,134	2.29
Reeb Investments Pty Ltd	3,830,858	1.77
Mr Geoffrey Cribb	2,580,404	1.19
Mr David Jiang	2,276,733	1.05
Gisbone Grazing Company Pty Ltd	2,240,975	1.03
Aintree Holdings Pty Ltd	2,152,099	0.99
Dr Wolf Gerhard Martinick	1,800,000	0.83
Mr David Sen Jee Ms Janet Juliana Lee	1,772,000	0.82
Kelanco Pty Ltd	1,743,592	0.80
Plato Prospecting Pty Ltd	1,500,000	0.69
Oceanbay Nominees Pty Ltd	1,351,540	0.62
Wakeford Holdings Pty Ltd	1,249,715	0.58
Kelanco Pty Ltd	1,221,429	0.56
Martinick Investments Pty Ltd	1,216,858	0.56
D G Begbie Pty Ltd	1,203,000	0.55
Mr Michael Grant	1,101,935	0.51
	59,636,844	**27.48**

Shareholders' Information continued

NUMBER OF HOLDERS OF LISTED OPTIONS AS AT23rd AUGUST 2006

TOP TWENTY OPTIONHOLDERS AS AT 23rd August 2006	No of Options	% of Issued Options
Irrewarra Investments Pty Ltd	1,918,966	12.64
Classic Roofing Pty Ltd	837,960	5.52
Kelanco Pty Ltd	774,183	5.10
Clodene Pty Ltd	725,000	4.78
Mr Chee Chin	600,000	3.95
Ms Janet Elizabeth White	500,000	3.29
Aimwin Pty Ltd	400,000	2.63
Mr John Maas & Mrs Jennifer Maas	317,500	2.09
Lost Ark Nominees Pty Ltd	300,000	1.98
Mr Kevin Bertrett Pinkstone & Mrs Narelle Kay Pinkstone	300,000	1.98
Mr Simon Edward Wright	285,698	1.88
Havenranch Pty Ltd	270,000	1.78
Kemview Holdings Pty Ltd	262,500	1.73
Swanman Pty Ltd	250,000	1.65
Mr Stephen Clarke Jones	220,000	1.45
Walsec Pty Ltd	210,000	1.38
Mr Hamish Keith Kibblewhite	200,003	1.32
Bowlink Pty Ltd	200,000	1.32
Mr Lynette Jane Castrique	200,000	1.32
Mr Paul McCarthy & Mr Stephen Jessup	200,000	1.32
	8,971,810	**59.11**

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Glossary

GLOSSARY OF ONCOLOGY TERMS

adenocarcinoma (AD-in-o-kar-sin-O-ma): Cancer that begins in cells that line certain internal organs and that have glandular (secretory) properties.

adjuvant therapy (AD-joo-vant): Treatment given after the primary treatment to increase the chances of a cure. Adjuvant therapy may include chemotherapy, radiation therapy, or hormone therapy.

alkaloid : A member of a large group of chemicals that are made by plants and have nitrogen in them. Some alkaloids have been shown to work against cancer.

anecdotal report : An incomplete description of the medical and treatment history of one or more patients. Anecdotal reports may be published in places other than peer-reviewed, scientific journals.

animal model : An animal with a disease either the same as or like a disease in humans. Animal models are used to study the development and progression of diseases and to test new treatments before they are given to humans. Animals with transplanted human cancers or other tissues are called xenograft models.

antibody (AN-tih-BOD-ee): A type of protein made by certain white blood cells in response to a foreign substance (antigen). Each antibody can bind to only a specific antigen. The purpose of this binding is to help destroy the antigen. Antibodies can work in several ways, depending on the nature of the antigen. Some antibodies destroy antigens directly. Others make it easier for white blood cells to destroy the antigen.

apoptosis (ap-o-TOE-sis): A normal series of events in a cell that leads to its death.

carcinosarcoma : A malignant tumor that is a mixture of carcinoma (cancer of epithelial tissue, which is skin and tissue that lines or covers the internal organs) and sarcoma (cancer of connective tissue, such as bone, cartilage, and fat).

clinical trial : A research study that tests how well new medical treatments or other interventions work in people. The study tests new methods of screening, prevention, diagnosis, or treatment of a disease.

controlled study : An experiment or clinical trial that includes a comparison (control) group.

disease-free survival : Length of time after treatment during which no cancer is found. Can be reported for an individual patient or for a study population.

disease-specific survival : The percentage of subjects in a study who have survived a particular disease for a defined period of time. Usually reported as time since diagnosis or treatment. In calculating this percentage, only deaths from the disease being studied are counted. Subjects who died from some other cause are not included in the calculation.

ex-vivo : from a living organism.

fibrosarcoma : A type of soft tissue sarcoma that begins in fibrous tissue, which holds bones, muscles, and other organs in place.

gastric (GAS-trik): Having to do with the stomach.

glioma (glee-O-ma): A cancer of the brain that comes from glial, or supportive, cells.

interferon (in-ter-FEER-on): A biological response modifier (a substance that can improve the body's natural response to infection and disease). Interferons interfere with the division of cancer cells and can slow tumor growth. There are several types of interferons, including interferon-alpha, -beta, and -gamma. These substances are normally produced by the body. They are also made in the laboratory for use in treating cancer and other diseases.

In-vitro : In a test tube.

In-vivo : In a living organism.

Glossary (Cont.)

lectin : A protein of non-immune origin that binds with high specificity and high affinity to carbohydrate molecules. Lectins are able to bind to the outside of a cell and cause biochemical changes in it. Lectins are made by both animals and plants.

lymphoma (lim-FO-ma): Cancer that arises in cells of the lymphatic system.

metastasis (meh-TAS-ta-sis): The spread of cancer from one part of the body to another. Tumors formed from cells that have spread are called "secondary tumors" and contain cells that are like those in the original (primary) tumor. The plural is metastases (meh-TAS-ta-seez).

monoclonal antibody : A protein of immune system origin designed by scientists to recognise one particular protein found on the surface of some cancer cells. The monoclonal antibody recognises the protein and locks onto it (like a key in a lock). This may then trigger the body's immune system to attack the cancer cells and can sometimes cause the cells to destroy themselves.

partial response : A decrease in the size of a tumor, or in the extent of cancer in the body, in response to treatment.

phase I trial : Phase I trials are the first step in testing a new treatment in humans. These studies test the best way to give a new treatment (for example, by mouth, intravenous infusion, or injection) and the best dose. The dose is usually increased a little at a time in order to find the highest dose that does not cause harmful side effects. Because little is known about the possible risks and benefits of the treatments being tested, phase I trials usually include only a small number of patients who have not been helped by other treatments.

phase I/II trial : A trial to study the safety, dosage levels, and response to a new treatment.

phase II trial : Phase II cancer trials test whether a new treatment has an anti cancer effect (for example, whether it shrinks a tumor or improves blood test results) and whether it works against a certain type of cancer.

phase III trial : Phase III trials compare the results of people taking a new treatment with the results of people taking the standard treatment (for example, which group has better survival rates or fewer side effects). In most cases, studies move into phase III trials only after a treatment seems to work in phases I and II. Phase III trials may include hundreds of people.

primary tumor : The original tumor.

prospective : In medicine, a study or clinical trial in which participants are identified and then followed forward in time.

quality of life : The overall enjoyment of life. Many clinical trials measure aspects of an individual's sense of well-being and ability to perform various tasks to assess the effects of cancer and its treatment on the quality of life.

radiation therapy (ray-dee-AY-shun): The use of high-energy radiation from x-rays, gamma rays, neutrons, and other sources to kill cancer cells and shrink tumors. Radiation may come from a machine outside the body (external-beam radiation therapy), or it may come from radioactive material placed in the body in the area near cancer cells (internal radiation therapy, implant radiation, or brachytherapy). Systemic radiation therapy uses a radioactive substance, such as a radiolabeled monoclonal antibody, that circulates throughout the body. Also called radiotherapy.

squamous cell carcinoma (SKWAY-mus. . .kar-sin-O-ma): Cancer that begins in squamous cells, which are thin, flat cells resembling fish scales. Squamous cells are found in the tissue that forms the surface of the skin, the lining of the hollow organs of the body, and the passages of the respiratory and digestive tracts. Also called epidermoid carcinoma.

stage I melanoma : Cancer is found in the outer layer of the skin (epidermis), the upper part of the inner layer of skin (dermis), or both but it has not spread to nearby lymph nodes. The tumor is no thicker than 1.5 millimeters.

stage IIB melanoma : Melanoma in which the tumor is more than 4 millimetres thick. It has spread through the lower part of the inner layer of skin (dermis) and into subcutaneous (under the skin) tissue, but not to nearby lymph nodes.

stage III pancreatic cancer : Cancer of the pancreas in which the cancer has spread to the lymph nodes near the pancreas. Cancer may have spread to nearby organs.

stage IV pancreatic cancer : Cancer of the pancreas in which the cancer has spread to organs near the pancreas (stage IVA) or to organs far away from the pancreas (stage IVB)