



ADVANCED ENGINE COMPONENTS LIMITED

ABN 67 009 081 770

**ANNUAL REPORT
2009**

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Corporate Information

This annual report covers both Advanced Engine Components Limited (“AEC” or “the Company”) as an individual entity and the consolidated entity comprising Advanced Engine Components Limited and its subsidiaries. The group’s functional and presentation currency is AUD (\$).

A description of the Group’s operations and principal activities is included in the review of operations and activities in the directors’ report on pages 3 to 16.

Directors

Mr. G Keys (Chairman)

Mr. A. Middleton (Managing Director)

Mr. A Pun (Non-Executive Director)

Mr. A Chan (Non-Executive Director)

Company Secretary

Ms. S Hunter

Registered and Principal Office

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Malaga WA 6090

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Email: shares@advancedengine.com

Share Registrar

Computershare Investor Services Pty Limited

Level 2, 45 St Georges Terrace

Perth WA 6000

Tel: 1300 85 05 051

Bankers

St George Bank

152-158 St Georges Terrace

Perth WA 6000

Auditors

BDO Kendalls Audit and Assurance (WA) Pty Ltd

128 Hay Street

Subiaco WA 6008

Website

www.advancedengine.com

ASX Code

ACE

Directors' Report

The Directors submit their report on the consolidated entity constituting Advanced Engine Components Limited and the entities it controlled at the end of or during the year ended 30 June 2009.

DIRECTORS

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

Mr. Graham Keys
BEc (Monash) ACA FFin
MAICD(Dip)
(Non-executive Chairman)

Mr. Keys is a former corporate finance partner of Ernst & Young. He has experience as Executive Director, and subsequently Managing Director, of a publicly listed company, as non-executive Chairman of publicly listed companies and as the executive officer of two large private companies. He formed Norvest Corporate Pty Ltd, a specialist corporate advisory firm, in April 2000 and is the current Executive Chairman of that company. He was appointed a Non-executive Director of AEC on 9 May 2003 and Chairman on 19 October 2004. During the past three years, Mr. Keys has also served as a director of Brand New Vintage Ltd and Cape Range Wireless Ltd.

Mr. Antony Middleton
BE MBA FIE (Aust) FCILT
(Managing Director)

Mr. Middleton holds a Bachelor of Engineering and Master of Business Administration from the University of Western Australia, and a Company Directors' Diploma from the University of New England. Mr. Middleton has held senior management positions with government agencies including Chairman and Chief Executive Officer of Transperth and also on various international engineering projects. He is past National Chairman and a Fellow of the Chartered Institute of Logistics and Transport in Australia, and a Fellow of the Institution of Engineers (Australia). Mr. Middleton was appointed a Director of AEC in March 1997 and Chairman in December 2002. He retired as Chairman and was appointed Managing Director in August 2003. During the past three years Mr. Middleton has not served as a director for any other Australian listed companies.

Mr. Kin Wa Pun (Albert)
MSC BSocSc
(Non-Executive Director)

Mr. Pun has significant international investment experience. Mr. Pun is the Managing Director and founder of Cherry Capital Management Limited ("Cherry"), a Hong Kong based financial advisory company, providing strategic and financial advice to its clients. He is currently appointed as the Chief Advisor of KGI Asia Limited, a Hong Kong based regional investment bank. Prior to joining Cherry, Mr. Pun was the Chief Financial Officer and a member of the board of Directors of KG Investment Holdings Limited, a regional financial services group in Hong Kong. Both KGI Asia Limited and KG Investment Holdings Limited are part of the Koos Group which is one of the largest business groups in Taiwan. Mr. Pun also previously worked at Morgan Stanley Asia Limited as Vice President. Mr. Pun has a Master of Sciences and Bachelor of Social Sciences degree from the University of Hong Kong. Mr. Pun was appointed a Non-executive Director of AEC on 28 November 2006. During the past three years Mr. Pun has not served as a director for any other Australian listed companies.

Mr. Ming Fai (Arnold) Chan
BSocSc
(Non-Executive Director)
(Appointed 28 May 2009)

Mr. Chan has significant international investment experience. He is currently the Chief Executive Officer of Full Seas Technology Limited which is a technology provider for an intelligent management system used in electric power network in some Chinese cities. Prior to that, he was the President of Dandelion Capital Group ("Dandelion"), a company focusing on special situation investment opportunities in China. Mr. Chan has over twenty years experience in investment advisory and asset management. He established Dandelion, in 2006, and co-founded the KGI Group, a pan-Asian investment bank, in 1997. He has also worked with HSBC and Jardine Fleming, based in Hong Kong, with responsibilities throughout Asia. Mr. Chan is an independent non executive Director of China LotSynergy Holdings Limited a company listed on the Hong Kong stock exchange. Mr. Chan has a Bachelor of Social Sciences degree from the University of Hong Kong with a major in Economics. Mr. Chan was appointed a Non-executive Director of AEC on 28 May 2009. During the past three years Mr. Chan has not served as a director for any other Australian listed companies.

Mr. Thomas Liu
BS MBA
(Non-Executive Director)
(Resigned 28 May 2009)

Mr. Liu is the Director and Head of the Beijing office of Aetos Capital, a real estate private equity fund, responsible for identifying and making investments in real estate projects and assets in the greater China region. Before joining Aetos, he was the Executive Director and Head of the real estate investment group with CDIB Capital Limited, a subsidiary of China Development Industrial Bank in Taiwan. Previously, Mr. Liu was the Managing Director of 698 Capital Holdings Limited and also the Chief Operating Officer of a real estate development company, He Qiao, in Beijing, China. Before moving to Beijing in 2004, Mr. Liu held various senior management positions in investment banking and management consulting firms in Hong Kong. Mr. Liu was appointed a Non-executive Director of AEC on 7 August 2003 and resigned on 28 May 2009. During the past three years Mr. Liu has not served as a director for any other Australian listed companies.

Company Secretary

Ms. Susan Hunter BCom, ACA, FFSIA(Dip), MAICD(Dip), ACIS(Dip)

Ms. Susan Hunter has over 15 years experience in the corporate finance industry. Ms. Hunter holds a Bachelor of Commerce degree from the University of Western Australia majoring in accounting and finance, is a Member of the Australian Institute of Chartered Accountants, a Fellow of the Financial Services Institute of Australasia, a Member of the Australian Institute of Company Directors and a Member of the Institute of Chartered Secretaries in Australia. She is currently the Company Secretary of several Australian Stock Exchange listed companies.

DIRECTORS' INTERESTS

As at the date of this report, the interests of the Directors in the shares and options of Advanced Engine Components Limited were:

Director	Number of Ordinary Shares	Number of Options over Ordinary Shares
Mr. G Keys (ii)	3,700,000	419,298
Mr. A Middleton (ii)(iii)	3,562,947	540,649
Mr. A Pun (i)	250,000	-
Mr. A Chan	-	-

- (i) Mr. Pun, through his directorship of 698 Capital International Ltd, has an interest in 64,423,731 AEC shares and 9,258,153 options held by that company.
- (ii) 144,298 options held by Mr. Keys, 140,649 options held by Mr. Middleton and 4,258,153 options held by 698 Capital International Ltd were issued pursuant to the November 2007 rights issue. These options are exercisable at \$0.128 per share on or before 30 November 2009.



- (iii) Mr. Keys was issued with 275,000 options in November 2008 pursuant to a shareholders resolution at the 2008 Annual General Meeting. These options are exercisable at \$0.20 per share on or before 31 December 2010.
- (iii) Mr. Middleton was issued with 400,000 options pursuant to the company's Employee Share Option Plan in November 2007. These options are exercisable at \$0.18 per share on or before 31 December 2009.
- (iv) 698 Capital International Ltd was issued with 5,000,000 options, pursuant to a shareholders resolution at the 2008 Annual General Meeting, as a term of its related party 698 Capital Asia Pacific Ltd providing AEC with a \$2,000,000 working capital facility. These options are exercisable at \$0.20 per share on or before 31 December 2010.

PRINCIPAL ACTIVITIES

The Company's principal activities in the course of the financial year were the sale of AEC patented Natural Gas Vehicle Systems ("NGVS"), natural gas engines incorporating AEC's NGVS and associated components and spare parts.

OPERATING RESULTS

The consolidated loss after tax for the year attributable to the members of Advanced Engine Components Limited was \$2,840,527 (2008: \$2,072,610).

DIVIDENDS

No dividends have been declared or paid to shareholders at the date of this report.

REVIEW OF OPERATIONS

Overview

The 2009 financial year has been a very challenging year for AEC, although the company was able to register its fifth consecutive year of year-on-year sales growth.

The previous financial year (2008) recorded a 52% increase in sales revenue over the preceding year (2007) and, with no reason to anticipate the global financial crisis (GFC) building on the horizon, we confidently expected that sales trend to continue and improve in the 2009 financial year just ended.

That expectation appeared well-founded when first quarter sales registered a 226% increase on the corresponding period of the previous year, together with strong forward orders and customer interest. On the back of this sales growth and interest, AEC completed an \$873,000 capital raising, at 20 cents per share, and put in place a \$2.0 million sales financing facility. These debt and equity raisings were expected to provide your company with sufficient working capital to take it through to a positive cash flow position.

Unfortunately, by the second quarter, the impact of the GFC began to affect AEC's markets. The price of oil, a critical decision-making factor in purchasing natural gas vehicles ("NGVs"), fell from an average of US\$136.44 per barrel in June/July 2008 to an average of US\$48.24 in November/ December 2008. Demand slowed, deliveries were deferred and customer payments delayed.

Key highlights

Despite the impact of the GFC on the final nine months of the financial year, overall sales increased for the fifth year in a row. In addition, your company advanced further in its mission to be the leading supplier of alternative fuel engine systems and components to the Asia Pacific Region through innovation and quality. Particularly notable advances included:

- Signing an engine development and ten year purchase agreement with Tata Motors Limited, India's largest automobile company. Tata Motors is the world's second largest medium and heavy bus manufacturer and the fourth largest manufacturer of medium and heavy trucks.
- Signing a strategic alliance agreement with Norinco Equipment Co of China for the marketing and sale of NGVs and products in the Chinese domestic and export markets.
- Doubling the number of NGVs using the AEC system in the Asia Pacific Region.
- Achieving a 65% increase in recurring sales of spares and consumables around the world.
- Commencing commercial production of the more cost competitive and efficient fifth generation AEC electronic control unit ("ECU").

- Strengthening of the AEC China management team.

Review of key markets

China

China continues to be your company's major market.

For the 2009 financial year, China domestic sales represented 63% of AEC's total sales compared to 40% for 2008. By 30 June 2009, there were over 370 vehicles, in more than 27 Chinese cities, using the AEC natural gas vehicle system ("NGVS").

On the downside, in the last nine months of the 2009 financial year AEC faced major negotiating difficulties with what had previously been our major customer in China. These difficulties have seen ongoing delays in payment to AEC of amounts outstanding, and a current ceasing of all orders from that customer.

However, the period has also seen renewed interest in the sale of NGV engines throughout China by Deutz (Dalian) Engine Co Ltd ("DDE"). DDE is a subsidiary of China First Auto Works Group Corporation, one of the largest vehicle manufacturers in China. In past years, AEC and DDE have collaborated in a number of engine developments and DDE has purchased, and for some years held, a large stock of AEC NGVS. This stockholding is now close to fully utilised, paving the way for a new flow of orders.

In the second half of FY2009, as part of DDE's renewed interest, DDE and AEC collaborated on the development of a hybrid natural gas/electric bus using the AEC NGVS. Buses using the hybrid system have been successfully trialed in route service and DDE's commercial sales of the buses have now commenced.

The run-down of DDE's NGVS stock, through increasing sales of DDE LNG and CNG engines, the availability of AEC's ECU5 and the development of the hybrid system, will result in increasing AEC NGVS sales to DDE throughout the 2010 financial year and beyond.

In March 2009, AEC entered into a strategic alliance agreement with Chinese company Norinco Equipment, a subsidiary of the state owned enterprise China North Industries Group Corporation. Norinco is involved in the development and export of CNG vehicles, engines and related natural gas products from China. AEC, in conjunction with Norinco, has already commenced discussions with parties in the key markets of Egypt, Iran, Myanmar and Thailand. The Board of AEC believes the links with Norinco Equipment will be very important to the company's future development in China and many other countries around the world.

Sales of DDE, Aussen and Xilian engines, incorporating AEC's NGVS, together with the Norinco Equipment alliance, will ensure China remains a major sales market for AEC NGVS and components in 2010.

India

No other country can match the potential of India as a market for natural gas vehicles.

India is already the fifth largest NGV market in the world, with 28 city projects in process, involving 450,000 vehicles and 373 natural gas refuelling stations. Over 220 Indian cities are planned for CNG development, involving more than 12,000 km of networked pipeline. This pipeline network is in addition to the massive Iran-Pakistan-India and Turkmenistan-Afghanistan-Pakistan-India pipelines. By the end of calendar year 2009, gas availability in India will have doubled; by 2012 India's CNG pipeline will connect 15 states and reach a population of 160 million people.

Legislation in India requires all buses and trucks servicing the major cities to comply with Euro 4 emission standards by April 1, 2010, and this requirement will increase to Euro 5 by 1 April 2014. These increasingly stringent standards give your company a major competitive edge, since AEC's technology already has the capability to meet Euro 5 emission standards.

AEC is strategically placed to benefit from the rapid development of India's interest in natural gas vehicles via its agreement with Tata Motors. The development of naturally aspirated and turbo charged natural gas versions of Tata's four and six cylinder engines is well advanced, with two reference engines under development at the

company's Malaga workshop. Development is expected to be completed, and commercial production commenced, in the first half of calendar 2010.

Thailand and Indonesia

Purchases of natural gas engines from AEC, as a percentage of total AEC sales, were considerably lower in 2009 (5%) than 2008 (37%).

The Thai NGV market was impacted by the low oil price and political instability, while the slow-down in the Indonesian market was more related to lack of natural gas infrastructure in that country. Interest and activity increased in both countries in the latter part of the 2009 financial year. Sales orders recommenced subsequent to year end and will continue throughout the 2010 financial year.

France

France continues to be a stable market for AEC with ongoing sales of spares and consumables. Sales for 2009 were up 63% to \$1.4 million. Sales to France represented 30% of total sales compared to 19% for 2008. The substantial increase in sales of spares and consumables to a fleet that has not increased in numbers in recent years demonstrates that component sales in relation to any specific vehicle will increase on a year-on-year basis as the vehicle ages. Clearly, after-markets sales will produce very considerable revenues for your company in the years ahead.

Australia

Domestic sales remained relatively low at 2% in 2009 compared to 4% in 2008. These sales relate to services, spares and consumables, mainly to Perth Public Transport Authority, for existing bus engines converted to AEC's NGVS. In addition, AEC has two vehicles with Isuzu engines (190hp and 220hp) converted to CNG and a vehicle with an Isuzu 255hp engine converted to LNG, operating commercially in Australia. A further vehicle, with an Isuzu 295hp engine, is in the final stages of development.

Although Australia is unlikely to become a major market, our work with Isuzu has the potential to help us develop a valuable niche market. Apart from their wide commercial use, Isuzu trucks in these engine sizes are extensively used as the base for service vehicles used by local authorities, all of whom are under pressure to demonstrate their commitment to sustainability and environmental responsibility, and thus potential buyers of natural gas vehicles

Financial review

Income Statement

Although low, at 3%, the 2009 financial year was AEC's fifth year in a row of year on year growth in sales. The 2008 sales were 52% higher than 2007; 2007 was 20% higher than 2006; and 2006 was 45% higher than 2005.

The \$2.8 million loss for the financial year was 37% higher than the \$2.1 million loss for 2008.

Despite the increased loss, the 2009 financial year showed the resilience of the AEC business model to a downturn in economic cycles. Sales of NGVS kits increased to 39% (2008: 29%) of total sales, mainly in the first quarter; sales of engines decreased to 7% (2008: 37%); but most importantly, sales of spares and consumables increased from \$1.5 million (33%) in 2008 to \$2.6 million (53%) in 2009. Sales of spares and consumables will increase exponentially each year, regardless of economic conditions, with every new vehicle utilising the AEC NGVS that becomes operational.

The gross margin was down for 2009 (32%) compared to 2008 (40%). Margins on NGVS were consistent in both periods; margins on engines were well down, due to different markets, but with little impact on the overall margin due to the small dollar value; and margins on spares and consumables were up.

The main reason for the drop in the margin related to warranty claims in the China and Thailand markets. The high level of these claims reflects the many different geographical and climatic conditions in which the AEC NGVS operates throughout China; the customer's lack of knowledge for the different operating characteristics of NGVs; and the need in some cases, particularly LNG vehicles, for AEC to alter the operating capabilities of the NGVS. AEC is

confident, although issues will always arise in new markets, that 2010 will see warranty claims return to normal acceptable levels.

Earnings before interest, tax, depreciation and amortisation ("EBITDA") was a loss of \$1.46 million in 2009 compared to a loss of \$1.2 million in 2008. The variation in the EBITDA loss is materially the same as the variation in the warranty claim figure.

The 2009 EBITDA also benefited from foreign exchange gains of \$590,000, included as Other Income, and a saving in Australian employment and other overhead costs. However, these gains and savings were more than offset by additional China overheads, principally marketing related, for employee costs; travel and external testing. These additional costs will benefit AEC throughout 2010 and beyond.

Borrowing costs were \$353,000 higher in 2009 than 2008. This reflects the difficulty in obtaining finance in the current economic climate. However, half of this increase relates to the book value of share options issued as part of the refinancing. This willingness of financiers, both external and related, to accept equity as part of their financing consideration reflects their long term belief in AEC's future.

Balance Sheet

As at 30 June 2009 AEC's working capital, excluding short term interest bearing loans and provision for long service leave, is \$1.6 million higher than as at 30 June 2008. This improvement is principally the result of a \$2.0 million increase in trade receivables. Unfortunately, this increase is the result of delayed payments rather than increased sales. AEC continues to negotiate to reduce the amounts owing by the major customer. The reduction is occurring slowly and will continue through the 2010 financial year.

Delays in trade receivables have principally been funded by short term interest bearing loans from related parties. In addition, a short term borrowing of \$750,000 from a third party has been refinanced and assigned to related parties. The other major increase in short term borrowings relates to the reclassification of the convertible note, held by a related party, being reclassified from a long term borrowing to a short term borrowing pursuant to the terms of that note.

As at 30 June 2009, other than low value leasing and premium funding loans, all interest bearing secured borrowings are from parties related to the Directors of AEC.

Summary

The 2009 financial year, although starting well, has been a very challenging year for AEC. The main focus, because of international economic conditions, has been on cash flow and funding of delayed orders, deliveries and receipts from customers.

However, added to Government stimulus packages beneficial to AEC, the key business drivers for AEC remain positive:

- the current price of oil above US\$70 per barrel;
- security of energy concerns; and
- environmental concerns.

As a result, the usage of compressed natural gas (CNG), liquefied natural gas (LNG), bio methane, hydrogen blended with CNG (HCNG) and natural gas – electric hybrid systems, all of which require the AEC NGVS or equivalent, are increasingly being accepted as the preferred alternative fuel of choice for Governments and heavy duty vehicle users around the world.

Together with the key business drivers, AEC's newly established relationships with TML and Norinco Equipment are expected to provide positive results for AEC in the 2010 financial year.

While the key focus in the short term must remain on cash flow and funding, AEC is seeing renewed interest and demand particularly in China, Thailand, Indonesia and India.

SIGNIFICANT CHANGES IN STATE OF AFFAIRS

AEC raised \$0.87 million through KGI Asia Limited underwriting the shortfall in the exercise of 4.36 million 20 cent options that expired on 30 June 2008.

During the year 5.0 million options were issued to CIM Special Situations Fund Limited ("CIM"). The options were issued as part of CIM's agreement to extend the repayment term of their \$750,000 loan to AEC from 31 October 2008 to 30 November 2009. The options were issued, in tranches of 1.25 million options, at the end of each month commencing 31 December 2008 and ending 31 March 2009. The options are exercisable, on or before 30 November 2011, at the volume weighted average share price for the calendar month preceding the date of issue. Effective 1 April 2009, the \$750,000 loan was refinanced by a syndicate lead by Norvest Corporate Pty Ltd a related entity of an AEC Director. The refinancing provided AEC with a lower interest rate, less options to be issued and an extended repayment period.

During the year, 5.86 million options exercisable at 12.8 cents per share and 440,000 options exercisable at 19 cents per share lapsed.

During the year 698 Capital Asia Pacific Ltd, a party related to an AEC Director, agreed to provide a \$3.0 million sales finance facility to AEC. As at 30 June 2009 \$2.67 million had been drawn down.

A \$3.0 million convertible note, held by 698 Capital Asia Pacific Ltd a company related to an AEC Director, issued in 2005 and maturing on 31 December 2009 has been reclassified from a non current to current liability.

AFTER BALANCE DATE EVENTS

On 3 July 2009 shareholders approved the issue of up to 9.75 million options in tranches of 0.75 million per month commencing as of 30 April 2009. The options, part of refinancing of the existing \$750,000 loan facility, are exercisable on or before 30 November 2011. The exercise price of each option will be determined each month based on the previous calendar month's volume weighted average price of ACE shares. 60,000 of these options were issued prior to 30 June 2009 and a further 3.75 million have been issued to the date of this report.

Subsequent to year end the Company has received, less taxation consultant fees, \$325,000 for the 2008 R&D tax concession offset rebate. The Company will receive a similar amount for the 2009 R&D tax rebate prior to 31 December 2009.

Subsequent to year end the Company has drawn down the remaining \$330,000 balance of the 698 Capital Asia Pacific Ltd \$3.0 million sales finance facility.

FUTURE DEVELOPMENTS, PROSPECTS AND BUSINESS STRATEGIES

Refer to the Review of Operations included in this report of the Directors.

ENVIRONMENTAL ISSUES

The consolidated entity's operations are not subject to the public reporting requirements of the Energy Efficient Opportunities Act 2006 and the National Greenhouse and Energy Reporting Act 2007 and the National Environmental Protection (National Pollutant Inventory) Measure. However, the Board believes that the consolidated entity has adequate systems in place for the management of its environmental requirements and is not aware of any breach of these environmental requirements as they apply to the consolidated entity.

MEETINGS OF DIRECTORS

The number of Directors' meetings and number of meetings attended by each of the Directors of the Company during the financial year are detailed below:

Directors	Board of Directors	
	Held	Attended
Mr. G Keys (Chairman)	10	10
Mr. A Middleton	10	10
Mr. A Pun	10	10
Mr. A Chan	1	1
Mr. T Liu (resigned 28 May 2009)	9	7

MEETINGS OF AUDIT COMMITTEE

The Company's Audit Committee comprised of 2 non-executive Directors, Mr. G Keys and Mr. A Pun. During the financial year, 2 Audit Committee meetings were held, which were attended by BDO Kendalls Audit & Assurance (WA) Pty Ltd, the Company's auditors.

Members	Audit Committee	
	Held	Attended
Mr. G Keys (Chairman)	2	2
Mr. A Pun	2	2

SHARES UNDER OPTION

The following were unissued ordinary shares under option as at the date of this report:

- 7,119,972 options - exercisable at 12.8 cents per share on or before 30 November 2009.
- 1,180,000 options - exercisable at 18.0 cents per share on or before 31 December 2010.
- 5,505,000 options - exercisable at 20.0 cents per share on or before 31 December 2010.
- 2,500,000 options - exercisable at 6.0 cents per share on or before 30 November 2011.
- 1,250,000 options - exercisable at 5.5 cents per share on or before 30 November 2011.
- 1,250,000 options - exercisable at 5.0 cents per share on or before 30 November 2011.
- 30,000 options - exercisable at 4.7 cents per share on or before 30 November 2011.
- 30,000 options - exercisable at 4.4 cents per share on or before 30 November 2011.

The holders of these options do not have any rights under the options to participate in any share issue of the company or of any other entity.

REMUNERATION REPORT (AUDITED)

This report details the nature and amount of remuneration for each Director of AEC and for the key management personnel receiving the highest remuneration.

(a) Remuneration Policy

The objective of the Company's key management personnel reward framework is to ensure reward for performance is competitive and appropriate for the results delivered. The Board reviewed the key management remuneration at a meeting held on 30 May 2008 and agreed the approach to be taken over the following 12 months. The Non executive Directors held a further meeting, on 6 June 2008, to agree the approach in relation to the Managing Directors remuneration. Subsequent to these meetings the approach has been regularly reviewed having regard to the impact of the financial global crisis on the financial position of the Group.

AEC's remuneration policy has been designed to align Director and key management personnel objectives with shareholder and business objectives by providing a fixed remuneration component and offering specific short and long-term incentives. For the Managing Director's remuneration, profit and sales targets were set that must be achieved prior to salary increases and a bonus in the 2009 financial year. There is no direct relationship between performance and Non Executive Directors and key management personnel remuneration. When assessing individual remuneration levels consideration is given to the employee's service to reward the achievement of corporate goals and strategic objectives. The Board of AEC believes, and having regard to the global financial crisis, the remuneration policy to be appropriate and effective in its ability to attract and retain the best key management personnel and Directors to run and manage the Company to create goal congruence between Directors, key management personnel and shareholders, and to remunerate these key management personnel and Directors on normal commercial terms, having regard to the Company's financial position, commensurate with their experience and responsibilities.

During the year ended 30 June 2009 AEC did not have a separately established remuneration committee. The duties and responsibilities typically delegated to such committee is included in the responsibilities of the full Board.

The Board's policy for determining the nature and amount of remuneration for Board members and senior executives is as follows:

The remuneration policy, setting the terms and conditions for the Executive Director and key management personnel, was approved by the non- executive Directors on the Board. All key management personnel receive a base salary (based on factors such as length of service and experience), superannuation, fringe benefits, options and performance incentives. The Board reviews key management personnel packages annually by reference to the economic entity's performance, key management personnel performance and comparable information from industry sectors and other listed companies in similar industries.



The Managing Director and key management receive a superannuation guarantee contribution required by the government, which is currently 9%, and do not receive any other retirement benefits. Some individuals, however, have chosen to sacrifice part of their salary to increase payments towards superannuation.

All remuneration paid to Directors and key management personnel is valued at the cost to the company and expensed. Options are valued at the time of issue using the Black-Scholes methodology.

The Board policy is to remunerate Non-Executive Directors at market rates for comparable companies for time, commitment and responsibilities but which also takes into consideration the financial state of the company. The Board determines payments to the Non-Executive Directors and reviews their remuneration annually. The maximum aggregate amount of fees that can be paid to Non-Executive Directors is subject to approval by shareholders at the Annual General Meeting.

Other than as stated above, to 30 June 2009 there was no direct relationship between performance and Director and key management personnel remuneration. The tables below set out summary information about AEC consolidated earnings and share price movements for the five years to 30 June 2009.

	30 June 2009	30 June 2008	30 June 2007	30 June 2006	30 June 2005
	\$	\$	\$	\$	\$
Revenue	4,826,837	4,672,220	3,076,717	2,570,712	1,766,338
Net (loss) before tax	(2,840,527)	(2,072,610)	(3,131,445)	(1,390,985)	(1,506,187)
Net (loss) after tax	(2,840,527)	(2,072,610)	(3,131,445)	(1,386,454)	(1,510,712)
Basic loss per share	(0.0192)	(0.015)	(0.028)	(0.015)	(0.018)
Share price	0.04	0.18	0.20	0.09	0.13
Dividends	-	-	-	-	-

(b) Options Issued as Part of Remuneration for the Year Ended 30 June 2009

During the year the Company did not grant any options over ordinary shares to the Managing Director and key management personnel as part of their remuneration.

(c) Directors' and Other Key Management Personnel Remuneration

Names and positions held of parent entity Directors and other key management personnel in office at any time during the financial year are:

Parent Entity Directors

Mr. G Keys	Chairman – Non-Executive
Mr. A Middleton	Managing Director – Executive
Mr. A Pun	Director - Non-Executive
Mr. A Chan	Director - Non-Executive (appointed 28 May 2009)
Mr. T Liu	Director - Non-Executive (resigned 28 May 2009)

Other Key Management Personnel

Mr. B Neumann	Engine Development Manager
Mr. N McLaren	Electronics Division Manager
Mr. M McKay	Senior Mechanical Engineer
Mr. D Wang	General Manager - AEC China

Compensation of key management personnel (Group) for the year ended 30 June 2009

30 June 2009	Short Term	Post Employment	Long Term	Share-based Payment	Total	% of Value of Remuneration that Consists of Options
	Salary & Fees	Superannuation	Long Service Leave Provision	Options		
	\$	\$	\$	\$	\$	
<i>Directors</i>						
Mr. G Keys	25,000	-	-	8,718	33,718	25.9%
Mr. A Middleton	68,763	99,663	6,321	-	174,747	-
Mr. A Pun	-	-	-	-	-	-
Mr. A Chan (i)	-	-	-	-	-	-
Mr. T Liu (ii)	-	-	-	-	-	-
<i>Other Key Management</i>						
Mr. B Neumann	93,356	39,882	16,096	-	149,334	-
Mr. N McLaren	122,231	11,001	12,016	-	145,248	-
Mr. M McKay	122,231	11,001	-	-	133,232	-
Mr. D Wang	179,857	-	-	-	179,857	-
Total	611,438	161,547	34,433	8,718	816,136	

No proportion of the above remuneration is performance based

(i) Mr. Chan was appointed on 28 May 2009

(ii) Mr. Liu resigned on 28 May 2009

Compensation of key management personnel (Group) for the year ended 30 June 2008

30 June 2008	Short Term	Post Employment	Long Term	Share-based Payment	Total	% of Value of Remuneration that Consists of Options
	Salary & Fees	Superannuation	Long Service Leave Provision	Options		
	\$	\$	\$	\$	\$	
<i>Directors</i>						
Mr. G Keys	25,000	-	-	-	25,000	-
Mr. A Middleton	61,433	108,134	15,649	29,720	214,936	13.8%
Mr. A Pun	-	-	-	-	-	-
Mr. T Liu	-	-	-	-	-	-
Mr. W Lee (i)	-	-	-	-	-	-
<i>Other Key Management</i>						
Mr. B Neumann	78,916	41,086	6,803	7,430	134,235	5.0%
Mr. N McLaren	115,115	9,865	13,122	7,430	145,532	5.1%
Mr. M McKay	109,615	9,865	-	7,430	126,910	5.7%
Mr. D Wang	123,813	-	-	-	123,813	-
Total	513,892	168,950	35,574	52,010	770,426	

No proportion of the above remuneration is performance based

(i) Mr. Lee resigned 10 September 2007

The only cash bonuses, special incentive or share based payment bonuses paid to Directors or key management in either the 2008 or 2009 financial years were the Share based option payments as shown in the above tables.

(d) Share-based compensation

The Employee Share Option Plan is used to reward Directors and employees for their performance and to align their remuneration with the creation of shareholder wealth. There are no performance requirements to be met before exercise can take place. The Plan is designed to provide long-term incentives to deliver long-term shareholder returns. Participation in the Plan is at the discretion of the Board and no individual has a contractual right to participate in the plan or to receive any guaranteed benefits.

The issue of options is not linked to performance conditions because by setting the option price at a level above the current share price at the time the options are granted, provides incentive for management to improve the Company's performance.

The terms and conditions of each grant of the Employee Share Option Plan options affecting remuneration in the previous, this or future reporting periods are as follows:

Grant date	Date vested and exercisable	Expiry date	Exercise price	Value per option at grant date
25 November 2005	25 November 2005	31 December 2008	\$0.19	\$0.069
23 November 2007	23 November 2007	31 December 2010	\$0.18	\$0.074

Options granted under the Plan carry no dividend or voting rights. The grant date equals the vesting date for all options.

Details of options over ordinary shares in the Company provided as remuneration to the Directors and key management personnel of AEC is set out below. When exercisable, each option is convertible into one ordinary share of AEC.

Name	No. of options granted / vested during the year	
	2009	2008
Directors		
Mr. G Keys	275,000	-
Mr. A Middleton	-	400,000
Mr. A Pun	-	-
Mr. A Chan (appointed 28 May 2009)	-	-
Mr. T Liu (resigned 28 May 2009)	-	-
Mr. W Lee (resigned 10 Sept 2007)	-	-
Other key management		
Mr. B Neumann	-	100,000
Mr. N McLaren	-	100,000
Mr. M McKay	-	100,000
Mr. D Wang	-	-

(e) Equity instruments issued on exercise of remuneration options

No shares were issued during the period to Directors or key management as a result of options exercised that had previously been granted as compensation.

(f) Value of options to Directors and key management

Details of the value of options granted, exercised and lapsed during the year to Directors and key management as part of their remuneration are summarised below:

Directors	Value of options at grant date	Value of options exercised	Value of options lapsed
Mr. G Keys	\$8,718	-	-
Mr. A Middleton	-	-	-
Mr. A Pun	-	-	-
Mr. A Chan (i)	-	-	-
Mr. T Liu (ii)	-	-	-
Other Key Management			
Mr. B Neumann	-	-	-
Mr. N McLaren	-	-	-
Mr. M McKay	-	-	-
Mr. D Wang	-	-	\$6,900
Total	\$8,718	-	\$6,900

(i) Mr. A Chan was appointed on 28 May 2009

(ii) Mr. T Liu resigned on 28 May 2009

(g) Service contracts

Executive Service Contracts

Mr. Antony Middleton, Managing Director

Mr. Middleton joined AEC as an Executive Director in March 1997, became the Executive Chairman in December 2002 and was appointed Managing Director in August 2003. Mr. Middleton's remuneration package is reviewed annually as part of the annual appraisal scheme. For the 2009 financial year Mr. Middleton's salary was set at \$160,568 per annum effective 1 July 2009. His salary was to increase, on a quarterly basis, by a further \$15,000 per annum, effective for the 2009 financial year if rolling quarterly sales targets were achieved. A \$10,000 bonus was payable at 30 June 2009 if the company achieved \$18.4 million in sales for the 2009 financial year and a breakeven net profit before tax. Due to the impact of the global financial crisis all Australian based employees hours were reduced from February 2009. It is intended that Mr. Middleton will return to normal hours and his salary and milestones reviewed when the financial position and future requirements of the Company become clear. The Company or the employee may terminate the contract by providing one months notice of intention to terminate or by payment or forfeiture of salary in lieu. Where the employee is aged over 45 years and has completed at least two years continuous service an additional one weeks notice or payment in lieu will be given.

Mr. Barry Neumann, Engine Development Manager

Mr. Neumann joined AEC as Engine Development Manager in 1987. For the 2009 financial year, Mr. Neumann's remuneration package was set at \$130,000 per annum effective 1 July 2008. The remuneration package is reviewed annually as part of the annual appraisal scheme. Due to the impact of the global financial crisis all Australian based employees hours were reduced from February 2009. It is intended that Mr. Neumann will return to normal hours and that his salary will be reviewed as the financial position and future requirements of the Company become clear. The Company or the employee may terminate the contract by providing one months notice of intention to terminate or by payment or forfeiture of salary in lieu. Where the employee is aged over 45 years and has completed at least two years continuous service an additional one weeks notice or payment in lieu will be given.

Mr. Nathon McLaren, Electronics Division Manager

Mr. McLaren joined AEC in 1999. He was appointed Electronics Division Manager in 2003. For the 2009 financial year, Mr. McLaren's remuneration package was set at \$130,000 per annum effective 1 July 2008. The remuneration package is reviewed annually as part of the annual appraisal scheme. Due to the impact of the global financial crisis all Australian based employees hours were reduced from February 2009. It is intended that Mr. McLaren will return to normal hours and that his salary will be reviewed as the financial position and future requirements of the Company become clear. The Company or the employee may terminate the contract by providing one months notice of intention to terminate or by payment or forfeiture of salary in lieu. Where the employee is aged over 45 years and has completed at least two years continuous service an additional one weeks notice or payment in lieu will be given.

Mr. Mike McKay, Senior Mechanical Engineer

Mr. McKay joined AEC as Senior Mechanical Engineer in 2006. For the 2009 financial year, Mr. McKay's remuneration package was set at \$130,000 per annum effective 1 July 2008. The remuneration package is reviewed annually as part of the annual appraisal scheme. Due to the impact of the global financial crisis all Australian based employees hours were reduced from February 2009. It is intended that Mr. McKay will return to normal hours and that his salary will be reviewed as the financial position and future requirements of the Company become clear. The Company or the employee may terminate the contract by providing one months notice of intention to terminate or by payment or forfeiture of salary in lieu. Where the employee is aged over 45 years and has completed at least two years continuous service an additional one weeks notice or payment in lieu will be given.

Mr. David Wang, General Manager China

Mr. Wang joined AEC in June 2005 as General Manager China. Mr. Wang does not have a formal employment contract with the Company. For the 2009 financial year, Mr. Wang's remuneration package was set at RMB 930,000 (approximately A\$170,000) per annum. The remuneration package is reviewed annually as part of the annual appraisal scheme. Mr. Wang's salary will next be reviewed at 31 December 2009. In March 2009, due to the impact of the global financial crisis, all Chinese based executive employees had their salaries reduced by 20% until the financial position and future requirements of the Company become clear.

End of Remuneration Report (audited)

INDEMNIFYING OFFICERS

Every officer of the consolidated entity is indemnified by the consolidated entity against any liability incurred by him in his capacity as officer in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted or in connection with any application in relation to any such proceedings in which relief is under the Law granted to him by the Court.

The Directors have not included details of the nature of the liabilities covered or the amount of the premium paid in respect of the Company's insurance contracts, as such disclosure is prohibited under the terms of the contract.

NON-AUDIT SERVICES

The Board of Directors, in accordance with advice from the audit committee, is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the Corporations Act 2001. The Directors are satisfied that the services disclosed below did not compromise the external auditor's independence for the following reasons:

- All non-audit services are reviewed and approved by the audit committee prior to commencement to ensure they do not adversely affect the integrity and objectivity of the auditor; and
- The nature of the services provided do not compromise the general principles relating to auditor independence as set out in the Institute of Chartered Accountants in Australia and CPA Australia's APES 110 Code of Ethics for Professional Accountants.

Details of the amounts paid or payable to the auditor for non audit services provided during the year are set out below:

	Consolidated	
	2009 \$	2008 \$
Taxation Services (related parties of BDO Kendalls Audit & Assurance (WA) Pty Ltd)		
<i>Tax compliance including review of Company income tax returns</i>	-	7,300
<i>Grant Applications</i>	-	7,304

PROCEEDINGS ON BEHALF OF THE COMPANY

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Company with leave of the Court under section 237 of the *Corporations Act 2001*.

AUDITOR'S INDEPENDENCE DECLARATION

The auditor's independence declaration for the year ended 30 June 2009 has been received and can be found on page 25.

Signed in accordance with a resolution of the Board of Directors.

A MIDDLETON
Managing Director
 PERTH, WESTERN AUSTRALIA

Dated 30th September 2009

CORPORATE GOVERNANCE STATEMENT

Corporate governance is the set of processes, customs, policies, laws and institutions affecting the way a corporation is directed, administered or controlled. Corporate governance also includes the relationships among the many stakeholders involved and the goals for which the corporation is governed.

The Board of Directors of Advanced Engine Components Limited ("AEC" or "the Company") is responsible for its corporate governance and the Board has adopted a manual of corporate governance policies and procedures based on control systems and accountability. A summary of the Company's corporate governance policies and procedures is included in this Statement.

The Company's corporate governance policies and procedures are in line with the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations 2nd Edition ("the ASX Principles & Recommendations"). The Company has followed the Principles & Recommendations where the Board has considered the recommendation to be an appropriate benchmark for its corporate governance practices. Where, after due consideration by the Board, the Company's corporate governance practices depart from the Principles & Recommendations, the Board has fully disclosed the departure and the reason for the adoption of its own practice, in compliance with the "if not, why not" exception reporting regime.

Further information about the Company's corporate governance practices including the information on the Company's charters, code of conduct and other policies and procedures is set out on the Company's website at www.advancedengine.com.au.

Role of the Board and Management

The Board is responsible for promoting the success of the Company in a way which ensures that the interests of shareholders and stakeholders are promoted and protected. The Board may delegate some powers and functions to the Managing Director for the day-to-day management of the Company. Powers and functions not delegated remain with the Board.

Specific responsibilities of the Board include:

- to develop, review and monitor the Group's long-term business strategies and provide strategic direction to management;
- to ensure policies and procedures are in place to safeguard the Group's assets and business and to enable the Group to act ethically and prudently;
- to develop and promote a system of corporate governance which ensures the Group is properly managed and controlled;
- to identify the Group's principal risks and ensure that it has in place appropriate systems of risk management, internal control, reporting and compliance;
- to monitor management's performance and the Group's financial results on a regular basis;
- to ensure the Group has in place appropriate systems to comply with relevant legal and regulatory requirements that impact on its operations;
- to determine the appropriate capital management for the Group;
- to manage the fair and responsible remuneration of the Company's executives based on their own performances; and
- to provide relevant support and advice to the Managing Director and executive management as required.

The Board carries out its responsibilities according to the following principles:

- The Board should possess a broad range of skills, qualifications and experience.
- All available information in connection with items to be discussed at a meeting of the Board shall be provided to each Director prior to that meeting.

- If a vacancy exists, through whatever reason, or where it is considered that the Board would benefit from the services of a new Director with particular skills, a candidate with appropriate expertise and experience is chosen.
- A Director (other than the Managing Director) may not retain office for more than three years without submitting for re-election.

The Board has delegated responsibilities and authorities to management to enable management to conduct the Company's day to day activities and progress the strategic direction provided by the Board in accordance with the delegated authorities for expenditure levels and materiality thresholds in place. Matters which are not covered by these delegations require Board approval. The separation of responsibilities between the Board and management is clearly understood and respected within the business.

The Managing Director is responsible for overseeing the daily operations, management and development of the Group by providing leadership and identifying strategic opportunities.

The Finance Manager is responsible for managing the financial and administration controls across the Company, including the overall management and statutory reporting for the Group.

At this stage of the development of the Company, AEC has only informal procedures in place for performance evaluation of the Board, its committees and individual Directors. It is noted the Company will undertake a formal evaluation of the performance of the Board, its Directors and its committees during the 2010 financial year. Senior executives undertake annual performance and remuneration reviews conducted by the Managing Director. Senior executives are reviewed against a number of qualitative and quantitative factors relevant to their role and position.

A summary of the Board Charter, a statement of matters reserved for the Board and senior management is available on the Company's website.

Composition of the Board

The Company has adopted a Policy on Assessing the Independence of Directors which is consistent with the guidelines detailed in the ASX Principles & Recommendations.

The Company's Board Charter includes guidelines for assessing the materiality of matters which are summarised below:

- Balance sheet items are material if they have a value of more than 5% of pro-forma net asset.
- Profit and loss items are material if they will have an impact on the current year operating result of 5% or more.
- Items are also material if (i) they impact on the reputation of the Company, (ii) they involve a breach of legislation or may potentially breach legislation, (iii) they are outside the ordinary course of business, (iv) they could affect the Company's rights to its assets, (v) if accumulated they would trigger the quantitative tests above, (vi) they involve a contingent liability that would have a probable effect of 5% or more on balance sheet or profit and loss items or (vii) they will have an effect on operations which is likely to result in an increase or decrease in net income or dividend distribution of more than 5%.
- Contracts will be considered material if (i) they are outside the ordinary course of business, (ii) they contain exceptionally onerous provisions, (iii) they impact on income or distribution in excess of the quantitative tests above, (iv) any default, should it occur may trigger any of the quantitative or qualitative tests above, (v) they are essential to the activities of the Company and cannot be replaced, or cannot be replaced without an increase in cost of such a quantum, triggering any of the quantitative tests above, (vi) they contain or trigger change of control provisions, (vii) they are between or for the benefit of related parties or (viii) they otherwise trigger the quantitative tests above.

The current Board consists of a non-executive Chairman (Mr. Graham Keys), two non-executive Directors (Mr. Arnold Chan and Mr. Albert Pun) and one executive Director (Mr. Antony Middleton), who also performs the role of Managing Director. A profile of each Director containing their date of appointment, skills, experience and expertise is set out in the Directors' Report.

The Board considers that Mr. Graham Keys and Mr. Arnold Chan are considered independent based on the criteria for independence included in the Company's Policy on Assessing the Independence of Directors and the ASX Principles & Recommendations. When applying the Company's Policy on Assessing the Independence of Directors and the ASX Principles & Recommendations Mr. Albert Pun is not considered an independent Director due to his direct association with the major shareholder of the Company.

As only two of the four Directors are independent, there is not a majority of independent Directors on the Board. The Board believes that given the size and scale of the Company, it is not practical to have a majority of independent Directors. The Board will continue to reassess its composition on a regular basis to ensure it has the necessary skill set and decision making capabilities to best serve all shareholders.

A minimum of three Directors is required under the Company's Constitution. Any changes to the composition of the Board will be determined by the Board, subject to any applicable laws and the resolutions of Shareholders. The Board seeks to nominate persons for appointment to the Board who have the qualifications, experience and skills to augment the capabilities of the Board. All Directors (except the Managing Director) are required by the Constitution of the Company to submit themselves for re-election at regular intervals and at least every three years.

New Directors are provided with a letter of appointment which sets out the key terms and conditions of their appointment and undergo an induction program.

A summary of the Company's policy for re-election of Directors and selection and appointment of new Directors is available on the Company's website.

Conflicts of Interest

In accordance with the Corporations Act, 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 does not receive the relevant Board papers and is not present at the meeting whilst the item is considered.

Statement Concerning Availability of Independent Professional Advice

The Board considers that to assist Directors with independent judgement a Director may consider it necessary to obtain independent professional advice to properly discharge the responsibility of their office as a Director. Provided the Director first obtains approval for incurring such expense from the Chairman, the Company will pay the reasonable expenses associated with obtaining such advice.

Nomination Committee

Given the present size of the Company, the whole Board acts as the Nomination Committee, if required. The Board believes no efficiencies or other benefits could be gained by establishing a separate Nomination Committee. To assist the Board to fulfil its function as the Nomination Committee, the Board has adopted a Nomination Committee Charter. A summary of the Nomination Committee Charter is available on the Company's website.

Remuneration Committee

Given the present size of the Company, the whole Board acts as the Remuneration Committee, if required. The Board believes no efficiencies or other benefits could be gained by establishing a separate Remuneration Committee. To assist the Board to fulfil its function as the Remuneration Committee, the Board has adopted a Remuneration Committee Charter. All matters of remuneration are determined by the Board pursuant to the Corporations Act and the ASX Listing Rule requirements, especially in respect of related party transactions. That is, no Directors participated in any deliberation regarding his own remuneration or related issues.

The Company has a Remuneration Policy adopted by the Board. Remuneration of Directors and senior management is determined with regard to payments made by other companies of similar size and industry and in accordance with the skills and experience of the particular person. Details of remuneration of Directors and Key Management Personnel are disclosed in the Remuneration Report.

There are no termination or retirement benefits for non-executive Directors (other than for superannuation).

Pursuant to the Remuneration Policy, executives are prohibited from entering into transactions or arrangements which limit the economic risk of participating in unvested entitlements.

A summary of the Remuneration Committee Charter and the Remuneration Policy are available on the Company's website.

Audit Committee

To assist in the execution of its responsibilities, the Board has established an Audit Committee.

The primary role of the Audit Committee is to monitor and review, on behalf of the Board, the effectiveness of the control environment of the Group in the areas of operational and balance sheet risk, legal/regulatory compliance and financial reporting. The overriding objective of the Committee is to provide an independent and objective review of financial and other information prepared by management, in particular that to be provided to members and/or filed with regulators. The Committee meets and receives regular reports from its external auditors concerning matters that arise in connection with their audit. The Committee is also responsible for review of performance of the external auditors.

The Committee is comprised of Mr. Graham Keys (Chairman) and Mr. Albert Pun both of whom are non-executive Directors. Mr. Graham Keys is considered independent. Details of the Directors' attendance at the Audit Committee meetings are set out in the Directors' Report.

The Audit Committee provides recommendations to the Board in relation to the initial appointment of the external auditor and the appointment of a new external auditor should a vacancy arise. Any appointment of a new external auditor made by the Board must be ratified by shareholders at the next annual general meeting.

Proposed external auditors must be able to demonstrate complete independence from the Group and an ability to maintain independence through the engagement period. In addition, the successful candidate for external auditor must have arrangements in place for the rotation of the audit engagement partner on a regular basis. Other than these mandatory criteria, the Board may select an external auditor based on other criteria relevant to the Company such as references, cost and any other matters deemed relevant by the Board.

A formal Audit Committee Charter has been adopted, a copy of which is available on the Company's website.

The Company Secretary provides secretarial services for the audit committee, whilst the Managing Director and Finance Manager are invited to audit committee meetings in attendance only.

Integrity of Financial Reporting

The Company's Managing Director and Finance Manager have provided a declaration to the Board in writing pursuant to section 295A of the Corporations Act and the ASX Listing Rules that:

- the consolidated financial statements of the Company and its controlled entities for each half and full year present a true and fair view, in all material aspects, of the Company's financial condition and operational results and are in accordance with accounting standards;
- the above statement is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board; and
- the Company's risk management and internal compliance and control framework is operating efficiently and effectively in all material respects.

Risk Management

The operation of internal controls and the measurement of risk are important in the creation and preservation of shareholder value and is a high priority for the Board and management. A summary of the Company's Risk Management Policy is available on the Company's website. Responsibility for control and risk management is delegated to the appropriate level of management with the Managing Director having ultimate responsibility to the Board for the risk management and control framework. The Audit Committee assists the Board in monitoring this role.

The Company is committed to the identification, monitoring and management of risks associated with its business activities and has established various financial and operational reporting procedures and other internal control and compliance systems in this regard. These include the following:

- the Managing Director is required to report on the management of risk as a standing agenda item at each Board meeting. This involves that tabling of a Risk Register which is actively monitored and updated by management;
- delegated authority limits exist in respect of financial expenditure and other business activities;
- a comprehensive insurance programme is undertaken;
- internal controls exist to safeguard the Company's assets and ensure the integrity of business processes and reporting systems;
- annual budgeting and monthly reporting systems for business operations is undertaken which enable the monitoring of progress against performance targets and the evaluation of trends;
- appropriate due diligence procedures are undertaken for acquisitions and divestments; and
- disaster recovery procedures and crisis management systems exist.

The Company's Managing Director and the Finance Manager have provided a declaration 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. Additionally, the Managing Director and Finance Manager have stated that this declaration is based on a sound system for risk management and internal compliance and control which implements the policies adopted by the Board and the Company's risk management and internal compliance and control framework is operating efficiently and effectively in all material respects.

The Board also requires management to report to it confirming that those risks are being managed effectively. The Board has received assurance from the Managing Director that the Company's management of its material business risks are effective.

Continuous Disclosure

The Company is a "disclosing entity" for the purposes of Part 1.2A of the Corporations Act. As such, the Company has an Information Policy. The purpose of this Information Policy is to set out the procedure for:

- protecting confidential information from unauthorised disclosure;
- identifying material price sensitive information and reporting it to the Managing Director and Company Secretary for review;
- ensuring the Company achieves best practice in complying with its continuous disclosure obligations under the Corporations Act and ASX Listing Rules; and
- ensuring the Company and individual officers do not contravene the Corporations Act or ASX Listing Rules.

The Company has obligations under the Corporations Act and ASX Listing Rules to keep the market fully informed of information which may have a material effect on the price or value of the Company's securities and to correct any material mistake or misinformation in the market. The Company discharges these obligations by releasing information to the ASX in the form of an ASX release or disclosure in other relevant documents, for example, the Annual Report.

The Company recognises that the maintenance of confidentiality is also of paramount importance to the Company both to protect its trade secrets and to prevent any false market for the Company's shares from developing.

All relevant information provided to ASX in compliance with the continuous disclosure requirements of the Corporations Act and ASX Listing Rules is promptly posted on the Company's web site.

A summary of the Information Policy is available on the Company's website.

Communication to Shareholders

The Company has a Shareholder Communications Policy that promotes effective communication with shareholders and encourages presentation of information to shareholders in a clear, concise and effective manner. The Board aims to ensure that Shareholders are informed of all major developments affecting the Company's state of affairs. Information will be communicated to Shareholders through its annual report, annual general meeting, half-yearly results and quarterly activities and cash flow announcements, ASX announcements and the Company's website.

The Company considers general meetings to be an effective means to communicate with shareholders and encourages shareholders to attend the meeting. Information included in the notice of meeting sent to shareholders is presented in a clear, concise and effective manner.

A summary of the Shareholder Communications Policy is available on the Company's website.

Code of Conduct

The Company has adopted a Code of Conduct that outlines how the Company expects its Directors and employees to behave and conduct business in the workplace on a range of issues. The Company is committed to the highest level of integrity and ethical standards in all business practices. The objective of the Code is to:

- provide a benchmark for professional behaviour;
- support the Company's business reputation and corporate image; and
- make Directors and employees aware of the consequences if they breach the code.

The Code records the Company's commitment and responsibilities with respect to various stakeholders, in particular, employees, clients, shareholders, governments and surrounding communities.

It sets out the Company's expectations of its Directors and employees with respect to a range of issues including compliance with the law, fair dealing, discrimination, financial inducements, occupational health and safety, confidentiality of information, conflicts of interest, use of Company assets and outside employment.

A breach of the code is subject to disciplinary action which may include termination of employment.

A summary of the Code of Conduct is available on the Company's website.

Ethical Standards

The Board considers that the success of the Company will be enhanced by a strong ethical culture within the Group. Accordingly, the Board is committed to the highest level of integrity and ethical standards in all business practices. Employees must conduct themselves in a manner consistent with current community and corporate standards and in compliance with all legislation.

Guidelines for Dealing in Securities

The Guidelines for Dealing in Securities Policy adopted by the Board prohibits trading in shares by a Director, officer or employee during certain blackout periods (in particular, prior to release of interim or annual results) except in exceptional circumstances and subject to procedures set out in the Guidelines.

Outside of these blackout periods, a Director, officer or employee must first obtain clearance in accordance with the Guidelines before trading in shares. For example:

- a Director must receive clearance from the Chairman before he may buy or sell shares;
- if the Chairman wishes to buy or sell shares he must first obtain clearance from the Managing Director; and
- other officers and employees must receive clearance from the Managing Director before they may buy or sell shares.

Directors must advise the Company Secretary of any transactions conducted by them in securities of the Company as soon as reasonably possible after the date of the change and in any event no later than three business days after the date of the change.

Directors, officers and employees must observe their obligations under the Corporations Act not to buy or sell shares if in possession of price sensitive non-public information and that they do not communicate price sensitive non-public information to any person who is likely to buy or sell shares or communicate such information to another party.

A summary of the Guidelines for Dealing in Securities Policy is available on the Company's website.

ASX Listing Rule Disclosure – Exception Reporting

As required by ASX Listing Rules, the following table discloses the extent to which the Company has not followed the best practice recommendations set by the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations (2nd Edition).

Principle No	Best Practice Recommendation	Compliance	Reasons for Non-compliance
2.1	A majority of the Board should be independent Directors.	Currently, the Company has two independent Directors and two Directors that are not considered to be independent.	The Board considers that its structure has been, and continues to be, appropriate in the context of the Company's recent history and the scope and scale of the Company's operations. Persons have been selected as Directors to bring specific skills and industry experience relevant to the Company. The Board will continue to reassess its composition on a regular basis to ensure it has the necessary skill set and decision making capabilities to best serve all shareholders.
2.4	The Board should establish a nomination committee.	The Board has not established a separate nomination committee, however, the responsibilities of a nomination committee are carried out by the full Board.	Given the present size of the Company, the whole Board acts as a nomination committee, if required. The Board believes no efficiencies or other benefits could be gained by establishing a separate Nomination Committee. However, it is noted the Board has adopted a Nomination Committee Charter. The Board will re-consider establishing a separate Nomination Committee as the Company's operations grow.
2.5	Companies should disclose the process for evaluating the performance of the Board, its committees and individual Directors.	The Company has in place informal procedures for evaluating the performance of the Board, its committees and individual Directors.	At this stage of the development of the Company, only informal procedures are in place for performance evaluation of the Board, its committees and individual Directors against qualitative indicators. It is noted the Company will undertake a formal evaluation of the performance of the Board, its Committees and individual Directors during the 2010 financial year.
4.2	The Audit Committee should consist of a majority of independent Directors, be chaired by an independent Director who is not Chair of the Board and have at least 3 members.	Currently, the Audit Committee has one independent Director and one Director who is not considered to be independent. There are only two members of the Audit Committee and the Committee is chaired by the Chairman of the Board.	The Board considers that the structure of the Audit Committee has been, and continues to be, appropriate in the context of the Company's recent history and the scope and scale of the Company's operations and given the size of the Board. The members of the Committee have specific skills and experience relevant to the efficient operation of the Committee. The Board will continue to reassess its composition of the Audit Committee on a regular basis to ensure it has the necessary skill set and experience to best

			serve the Board and all shareholders. It is noted the Chairman of the Committee, whilst Chair of the Board, is an independent Director that possesses skills and experience suitable for leading the Audit Committee.
8.1	The Board should establish a remuneration committee.	The Board has not established a separate remuneration committee, however, the responsibilities of a remuneration committee are carried out by the full Board.	Given the present size of the Company, the whole Board acts as a remuneration committee, if required. The Board believes no efficiencies or other benefits could be gained by establishing a separate remuneration committee. All matters of remuneration are determined by the Board in accordance with Corporations Act requirements, particularly in respect of related party transactions. No director participates in any discussion or decision regarding his own remuneration or related issues. The Board has adopted a Remuneration Committee Charter and Remuneration Policy.



BDO Kendalls

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ABN 79 112 284 787

30 September 2009

The Directors
Advanced Engine Components Limited
11 Energy Street
MALAGA WA 6090

Dear Sirs

**DECLARATION OF INDEPENDENCE BY PETER TOLL TO THE DIRECTORS OF
ADVANCED ENGINE COMPONENTS LIMITED**

As lead auditor of Advanced Engine Components Limited for the year ended 30 June 2009, I declare that, to the best of my knowledge and belief, there have been no contraventions of:

- the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Advanced Engine Components Limited and the entities it controlled during the period.

Peter Toll
Director

BDO Kendalls Audit & Assurance (WA) Pty Ltd
Perth, Western Australia.

Income Statements

For the Financial Year Ended 30 June 2009

	Notes	AEC Group		AEC Entity	
		2009 \$	2008 \$	2009 \$	2008 \$
Sales revenue	8	4,826,837	4,672,220	3,499,629	2,544,341
Cost of goods sold		(3,283,492)	(2,827,442)	(2,009,845)	(1,575,851)
Gross profit		1,543,345	1,844,778	1,489,784	968,490
Other revenue from continuing operations	8	810,953	227,871	412,443	270,815
Distribution expenses		(118,123)	(84,262)	(116,747)	(84,262)
Marketing expenses		(269,011)	(209,160)	(246,350)	(188,005)
Occupancy expenses		(300,580)	(270,933)	(227,306)	(190,448)
Corporate costs		(571,646)	(452,664)	(537,247)	(310,948)
Administration expenses		(1,692,723)	(1,370,371)	(1,651,258)	(919,682)
Development expenses		(1,440,584)	(1,198,524)	(1,220,385)	(1,127,468)
Finance costs	8	(802,158)	(448,680)	(798,649)	(448,680)
Share of loss of joint venture		-	(29,386)	-	-
Foreign exchange net loss	8	-	(81,279)	(168,408)	(81,279)
Loss before income tax expense		(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
Income tax expense	9	-	-	-	-
Net Loss attributable to members of the parent entity	25	(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
 Basic loss per share	10	(\$0.0192)	(\$0.0150)	(\$0.0207)	(\$0.0153)
Diluted loss per share	10	(\$0.0192)	(\$0.0150)	(\$0.0207)	(\$0.0153)

The above income statements should be read in conjunction with the accompanying notes.

Balance Sheets

As at 30 June 2009

	Notes	AEC Group		AEC Entity	
		2009 \$	2008 \$	2009 \$	2008 \$
Current Assets					
Cash and cash equivalents	12	279,955	169,476	265,750	93,769
Trade and other receivables	13	4,199,320	2,062,056	4,324,043	2,689,082
Inventories	14	1,604,622	1,499,257	914,609	721,422
Total Current Assets		6,083,897	3,730,789	5,504,402	3,504,273
Non-Current Assets					
Other financial assets	15	-	-	-	-
Investment accounted for using the equity method	16	40,317	40,317	69,703	69,703
Plant and equipment	17	418,926	599,424	400,711	580,859
Intangible assets	18	4,232,970	3,586,873	4,232,970	3,586,873
Total Non-Current Assets		4,692,213	4,226,614	4,703,384	4,237,435
Total Assets		10,776,110	7,957,403	10,207,786	7,741,708
Current Liabilities					
Trade and other payables	19	2,734,467	1,964,298	2,446,269	1,812,621
Borrowings	20	8,821,580	2,066,958	8,821,580	2,066,958
Provisions	21	324,254	257,002	324,254	257,002
Total Current Liabilities		11,880,301	4,288,258	11,592,103	4,136,581
Non-Current Liabilities					
Borrowings	22	-	2,974,912	-	2,974,912
Total Non-Current Liabilities		-	2,974,912	-	2,974,912
Total Liabilities		11,880,301	7,263,170	11,592,103	7,111,493
Net (Liabilities) / Assets		(1,104,191)	694,233	(1,384,317)	630,215
Equity					
Contributed equity	23	18,366,020	17,482,203	18,366,020	17,482,203
Reserves	24	1,307,413	1,149,127	1,244,940	1,079,166
Accumulated losses	25	(20,777,624)	(17,937,097)	(20,995,277)	(17,931,154)
Total Equity		(1,104,191)	694,233	(1,384,317)	630,215

The above balance sheets should be read in conjunction with the accompanying notes.

Statements of Changes in Equity

For the year ended 30 June 2009

AEC Group

2008-09

	Issued Capital \$	Convertible Notes \$	Asset Revaluation Reserve \$	Share Based Payments Reserve \$	Foreign Exchange Translation Reserve \$	Accumulated Losses \$	Total Equity \$
Opening balance as at 1 July 2008	17,324,203	158,000	750,000	329,166	69,961	(17,937,097)	694,233
Loss for the year	-	-	-	-	-	(2,840,527)	(2,840,527)
<i>Total recognised income and expenses for the year</i>	-	-	-	-	-	(2,840,527)	(2,840,527)
<i>Total movements for the year recognised in equity:</i>							
Issue of share capital	944,906	-	-	-	-	-	944,906
Exercise of options	826	-	-	-	-	-	826
Share issue costs	(61,915)	-	-	-	-	-	(61,915)
Costs of share based payment	-	-	-	165,774	-	-	165,774
Foreign exchange on translation	-	-	-	-	(7,488)	-	(7,488)
Closing balance as at 30 June 2009	18,208,020	158,000	750,000	494,940	62,473	(20,777,624)	(1,104,191)

2007-08

	Issued Capital \$	Convertible Notes \$	Asset Revaluation Reserve \$	Share Based Payments Reserve \$	Foreign Exchange Translation Reserve \$	Accumulated Losses \$	Total Equity \$
Opening balance as at 1 July 2007	15,099,939	158,000	750,000	241,492	48,097	(15,864,487)	433,041
Loss for the year	-	-	-	-	-	(2,072,610)	(2,072,610)
<i>Total recognised income and expenses for the year</i>	-	-	-	-	-	(2,072,610)	(2,072,610)
<i>Total movements for the year recognised in equity:</i>							
Issue of share capital	2,294,343	-	-	-	-	-	2,294,343
Exercise of options	5,652	-	-	-	-	-	5,652
Share issue costs	(75,731)	-	-	-	-	-	(75,731)
Costs of share based payment	-	-	-	87,674	-	-	87,674
Foreign exchange on translation	-	-	-	-	21,864	-	21,864
Closing balance as at 30 June 2008	17,324,203	158,000	750,000	329,166	69,961	(17,937,097)	694,233

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

Statements of Changes in Equity

For the year ended 30 June 2009

AEC Entity

2008-09	Issued Capital \$	Convertible Notes \$	Asset Revaluation Reserve \$	Share Based Payments Reserve \$	Accumulated Losses \$	Total Equity \$
Opening balance As at 1 July 2008	17,324,203	158,000	750,000	329,166	(17,931,154)	630,215
Loss for the year	-	-	-	-	(3,064,123)	(3,064,123)
<i>Total recognised income and expenses for the year</i>	-	-	-	-	(3,064,123)	(3,064,123)
<i>Total movements for the year recognised in equity:</i>						
Issue of share capital	944,906	-	-	-	-	944,906
Exercise of options	826	-	-	-	-	826
Share issue costs	(61,915)	-	-	-	-	(61,915)
Cost of share based payment	-	-	-	165,774	-	165,774
Closing balance as at 30 June 2009	18,208,020	158,000	750,000	494,940	(20,995,277)	(1,384,317)

2007-08	Issued Capital \$	Convertible Notes \$	Asset Revaluation Reserve \$	Share Based Payments Reserve \$	Accumulated Losses \$	Total Equity \$
Opening balance As at 1 July 2007	15,099,939	158,000	750,000	241,492	(15,819,687)	429,744
Loss for the year	-	-	-	-	(2,111,467)	(2,111,467)
<i>Total recognised income and expenses for the year</i>	-	-	-	-	(2,111,467)	(2,111,467)
<i>Total movements for the year recognised in equity:</i>						
Issue of share capital	2,294,343	-	-	-	-	2,294,343
Exercise of options	5,652	-	-	-	-	5,652
Share issue costs	(75,731)	-	-	-	-	(75,731)
Cost of share based payment	-	-	-	87,674	-	87,674
Closing balance as at 30 June 2008	17,324,203	158,000	750,000	329,166	(17,931,154)	630,215

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

Cash Flow Statements

For the Year Ended 30 June 2009

	Note	AEC Group		AEC Entity	
		2009 \$	2008 \$	2009 \$	2008 \$
Cash Flows From Operating Activities					
Receipts from customers		4,661,250	3,533,479	2,875,061	1,400,196
Payments to suppliers and employees		(6,446,069)	(5,139,980)	(4,453,450)	(2,919,179)
Interest received		3,732	19,323	3,732	18,470
Interest and other costs of finance paid		(651,833)	(90,704)	(798,649)	(90,704)
Net cash (used in) operating activities	12	(2,432,920)	(1,677,882)	(2,373,306)	(1,591,217)
Cash Flows From Investing Activities					
Payments for plant and equipment		(6,957)	(21,397)	(5,069)	(14,514)
Payment for capitalised development costs		(1,102,778)	(1,080,957)	(1,102,778)	(1,080,957)
Payment for investments		-	(69,703)	-	(69,703)
Net cash (used in) investing activities		(1,109,735)	(1,172,057)	(1,107,847)	(1,165,174)
Cash Flows From Financing Activities					
Proceeds from issue of shares		945,732	2,299,995	945,732	2,299,995
Transaction costs associated with issue of shares		(61,915)	(75,731)	(61,915)	(75,731)
Proceeds from borrowings		4,272,940	1,666,463	4,272,940	1,666,463
Repayments of borrowings		(1,503,623)	(1,482,451)	(1,503,623)	(1,482,451)
Net cash from financing activities		3,653,134	2,408,276	3,653,134	2,408,276
Net increase / (decrease) in cash and cash equivalents		110,479	(441,663)	171,981	(348,115)
Cash and cash equivalents at beginning of year		169,476	611,139	93,769	441,884
Cash and cash equivalents at end of year	12	279,955	169,476	265,750	93,769

The above cash flow statements should be read in conjunction with the accompanying notes.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

1. Reporting Entity

Advanced Engine Components Limited (the "Company") is a company limited by shares incorporated in Australia whose shares are publicly traded on the Australian Stock Exchange. The Company's registered office is 14 Energy St Malaga WA 6090.

The consolidated financial statements of the Company as at and for the year ended 30 June 2009 comprise the Company and its subsidiaries (together referred to as the "Group"). The nature of the operations and principal activities of the Group are described in the Directors' Report.

2. Basis of Preparation

(a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AASBs) (including Australian Interpretations) adopted by the Australian Accounting Standards Board (AASB) and the Corporations Act 2001. The consolidated financial report of the Group also complies with International Financial Reporting Standards (IFRSs) and interpretations adopted by the International Accounting Standards Board. The financial statements were approved by the Board of Directors on 30 September 2009.

(b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except where stated, does not take into account changing money values or fair valuations of non-current assets.

(c) Functional and presentation currency

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

3. Critical Accounting Judgements and Key Sources of Estimation Uncertainty

In the application of the Group's accounting policies, management is required to make judgments, estimates and assumptions about carrying values of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Refer to note 18 for a discussion of critical judgements in applying the entity's accounting policies, and key sources of estimation uncertainty.

4. Adoption of New and Revised Accounting Standards

In the current year, the Group has adopted all of the new and revised Standards and Interpretations issued by the Australian Accounting Standards Board (the "AASB") that are relevant to its operations and effective for the current annual reporting period. Details of the impact of the adoption of these new accounting standards are set out in the individual accounting policy notes set out below.

5. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities.

(a) Basis of consolidation

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

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(a) Basis of consolidation (continued)

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. Adjustments are made to bring into line any dissimilar accounting policies that may exist.

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

There is no minority interest in any subsidiary of the Group.

Investments in subsidiaries are accounted for at cost in the financial statements.

(b) Investment in joint venture

Joint ventures are those entities over whose activities the consolidated entity has joint control. Joint ventures are accounted for using equity method (equity accounted investees). The consolidated financial statements include the consolidated entity's share of the income and expenses of equity accounted investees, after adjustments to align the accounting policies with those of the consolidated entity, from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. When the consolidated entity's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the consolidated entity has an obligation or has made payment on behalf of the investee.

(c) Segment reporting

A business segment is identified for a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other business segments. A geographical segment is identified when products or services are provided within a particular economic environment subject to risks and returns that are different from those of segments operating in other economic environments.

(d) Foreign currency transaction and balances

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date.

All exchange differences in the consolidated financial report are taken to the income statement.

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

The functional currency of the overseas subsidiaries AEC China Holdings Limited is Hong Kong Dollar and AEC China Limited is the Chinese Yuan.

As at the reporting date the assets and liabilities of these overseas subsidiaries are translated into the presentation currency of Advanced Engine Components Limited at the rate of exchange ruling at the balance sheet date and the income statements are transferred at the weighted average rates for the year.

The exchange differences arising on the retranslation are taken directly to a separate component of equity.

(e) Revenue recognition

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

Sale of goods

Revenue is recognised when the significant risks and rewards of the goods have passed to the buyer and can be measured reliably. Risks and rewards are considered passed to the buyer at the time of delivery of the goods to the customer.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(e) Revenue recognition (continued)

Interest

Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument) to the net carrying amount of the financial asset.

(f) Income tax

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 reporting purposes.

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

- except where the deferred income tax liability 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; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences 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.

Deferred tax assets and deferred tax liabilities shall be offset only if:

- (a) there is a legally enforceable right to set-off current tax assets against current tax liabilities; and
- (b) the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either:
 - (i) the same taxable entity; or
 - (ii) different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or 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 substantially enacted at the balance sheet date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the income statement.

The Group has not implemented the tax consolidation legislation.

(g) Other taxes

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

- (a) 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
- (b) Receivables and payables are stated with amounts 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 financial activities, which are recoverable from, or payable to, the taxation authority, are classified as operating cash flows.

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

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(g) Other taxes (continued)

In case of AEC China Limited, revenue is recognised net of value added tax of the People Republic of China and expenses and assets are recognised inclusive of value added tax where the right to claim the credit of tax paid is yet to be established.

(h) Leases

Leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership.

Operating Leases

The minimum lease payments made under operating leases are charged against profits in equal instalments over the accounting periods covered by the lease term where the lessor effectively retains substantially all of the risks and benefits of ownership of the leased item.

The cost of improvements to or on leasehold property is capitalised, disclosed as leasehold improvements and amortised.

Finance leases

Leases which effectively transfer substantially all of the risks and rewards incidental to ownership of the leased item to the Group are capitalised at the present value of the minimum lease payments and disclosed as property, plant and equipment under lease. A lease liability of equal value is also recognised.

Capitalised lease assets are depreciated over the shorter of the estimated useful life of the assets and the lease term. Minimum lease payments are allocated between interest expense and reduction of the lease liability with the interest expense calculated using the interest rate implicit in the lease and recognised directly in net profit.

(i) Impairment of assets with indefinite useful life

At each reporting date, management assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, management 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 cost 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 groups 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.

(j) Cash and cash equivalents

Cash and short-term deposits in the Balance Sheet comprise cash at bank and in hand and short-term deposits with an original maturity 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.

(k) Investments and other financial assets

All investments are initially recognised at cost, being the fair value of the consideration given including acquisition charges associated with the investment.

Loans and non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has a positive intention and ability to hold to maturity. Investments intended to be held for an undefined period are not included in this classification.

Amortised cost is calculated by taking into account any discount or premium on acquisition, over the period to maturity.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(k) Investments and other financial assets (continued)

Investments are recognised and derecognised on trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs except for those financial assets classified as at fair value through profit or loss which are initially measured at fair value.

Subsequent to initial recognition, investments in subsidiaries are measured at cost in the company financial statements.

Other financial assets are classified into 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments.

Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method less impairment.

Interest income is recognised by applying the effective interest rate.

Impairment of financial assets

Financial assets are assessed from indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that as a result of one or more events that occurred after the initial recognition of the financial asset the estimated future cash flows of the investment have been impacted.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of financial assets including uncollectible trade receivables is reduced by the impairment loss through the use of an allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or it transfers the financial asset and subsequently all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

(l) Inventories

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

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

Raw Materials – purchase cost on a first in, first out basis.

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

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(l) Inventories (continued)

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

(m) Derivative financial instruments and hedging

The Group has adopted the policy of keeping the exposure open and accordingly no foreign exchange risk exposure of the Group has been hedged.

(n) Plant and equipment

Plant and equipment and leasehold improvements are carried at cost, less accumulated depreciation and any impairment in value.

(i) Depreciation & Amortisation

Depreciation is calculated on a straight –line basis over the estimated useful life of the asset as follows:

- Plant and equipment – over 3 to 13 years
- Leasehold improvements – 10 years

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

(ii) 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 value exceeds the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount. The impairment losses are recognised in the income statement.

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.

An item of 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 on de-recognition 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 year the item is derecognised.

(iii) Revaluations

Following initial recognition at cost, plant and equipment are carried at a revalued amount, which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and any subsequent impairment losses. An independent expert valuer determined the fair value by reference to the market-based evidence, which is the amount, which the asset could be exchanged between knowledgeable parties at an arm's length transactions.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(o) Intangible assets

Research and development costs

Current expenditure on research activities, undertaken with the prospect of obtaining new scientific or technical understanding is recognised in the income statement as an expense when it is incurred.

Expenditure on development activities, being the application of research findings or other knowledge to a plan or design for the production of new or substantially improved products before the start of commercial production or use is capitalised if the products are technically and commercially feasible and adequate resources are available to complete development.

Expenditure on equipment used in research and development activities is capitalised in plant and equipment and depreciated over its estimated useful life.

Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use on a straight line basis over its usual life which is currently 5 years.

(p) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

(q) Interest-bearing loans and borrowings

Convertible notes are brought to account on issue at the value of the net proceeds received. The Convertible Notes are compound financial instruments where interest is paid annually in arrears. The present value of the interest and principle payable on conversion are discounted at the market rate of interest at issue date and are brought to account as borrowings. The difference between the net proceeds received and the borrowing component is brought to account as equity.

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method.

Gains and losses are recognised in profit or loss when the liabilities are derecognised.

Compound instruments

The component parts of compound instruments are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for a similar non-convertible instrument. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or upon the instruments reaching maturity. The equity component initially brought to account is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This is recognised and included in equity, net of income tax effects and is not subsequently remeasured.

Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

(r) Borrowing costs

Borrowing costs are recognised as an expense when incurred, except where they are directly attributable to the acquisition or construction of qualifying assets, in which case they are capitalised as part of the cost of that asset.

(s) Provisions

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

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(s) Provisions (continued)

Where the Group 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 the income statement net of any reimbursement.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(t) Employee leave benefits

(i) Wages and salaries, annual leave and sick leave

Liabilities for wages and salaries, including non-monetary benefits, annual leave and accumulating sick leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled.

(ii) Long service leave

The liability for long service leave is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using market value at the reporting date on national government bonds with terms to maturity and currency that match, as closely as possible, the estimated future cash outflows.

(u) Pension and employment benefits

The Group contributes to various superannuation plans in accordance with and at rates set down by law. Some employees contribute to these plans at differing percentages of their salaries.

The Group contribution plan and costs are charged as an expense as incurred.

(v) Governments grants

Government grants are assistance by the government in the form of transfers of resources to the Group in relation to the current development programme.

Government grants are not recognised until there is reasonable assurance that the grants will be received.

Government grants are presented in the balance sheet by deducting the grant in arriving at the carrying amount of the assets.

(w) Share-based payment transactions

The Group operates an Employee Share Option Plan (ESOP), which provides benefits to employees (including Directors) of the Group in the form of share-based payment transactions, whereby employees render services in exchange for shares or rights over shares ("equity-settled transactions").

The cost of these equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. An external valuer using an option-pricing model determines the fair value.

From 1 July 2004, options granted as part of employee remuneration have been valued using an option pricing model which takes into account the factors including the option exercise price, the current level and volatility of the underlying share price, the risk-free interest rate, expected dividends on the underlying share, current market price of the underlying share, the expected life of the option, and any barriers associated with vesting.

The fair value of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the option ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects:

- (i) The extent to which the vesting period has expired, and
- (ii) The number of options that, in the opinion of the Directors of the Group, will ultimately vest. This opinion is formed based on the best available information at balance date. No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(w) Share-based payment transactions (continued)

No expense is recognised for options that do not ultimately vest, except for options where vesting is conditional upon a market condition.

Where the terms of an equity-settled option are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled option is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the option is recognised immediately. However, if a new option is substituted for the cancelled option, and designated as a replacement option on the date that it is granted, the cancelled and new option are treated as if they were a modification of the original option, as described in the previous paragraph.

The dilutive effect, if any, of outstanding options is reflected as additional share dilution in the computation of earnings per share.

The Group has applied the requirements of AASB 1 "First-time Adoption of Australian Equivalents to International Financial Reporting Standards" in respect of equity-settled options and has applied AASB 2 "Share-Based Payments" only to equity instruments granted before 7 November 2002 that had not vested on or before 1 January 2005.

(x) Contributed equity

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

(y) Earnings per share

(i) Basic earnings per share

Basic earnings per share is determined by dividing net profit after income tax attributable to members of the Company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

(ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

(z) New standards and interpretation not yet adopted

At the date of authorisation of the financial report, the Standards and Interpretations listed below were in issue but not yet effective.

Initial application of the following Standard will not affect any of the amounts recognised in the financial report, but will change the disclosure presently made in relation to the Group and the Company's financial report:

- **AASB 3 'Business Combinations' (reissued March 2008)**

Effective for business combinations where the acquisition date is on or after the beginning of the first reporting period that commences 1 July 2009 or later

- **AASB 127 'Consolidated and Separate Financial Statements' (reissued March 2008)**

Effective for annual reporting periods beginning on or after 1 July 2009

- **AASB 2008-3 (issued March 2008) 'Amendments to Australian Accounting Standards arising from AASB 3 and AASB 127 [AASB 1, AASB2, AASB4, AASB 5, AASB 7, AASB 101, AASB 107, AASB 112, AASB 114, AASB 116, AASB 121, AASB 128, AASB 131, AASB 133, AASB 134, AASB 136, AASB 137, AASB 138, AASB 139, Interpretation 9 and Interpretation 107]**

Effective for annual reporting periods beginning on or after 1 July 2009

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(z) New standards and interpretation not yet adopted (continued)

- **AASB 2008-1 (issued February 2008) 'Amendments to AASB – Share-based Payments – Vesting Conditions and Cancellations'**

Effective for annual reporting periods beginning on or after 1 January 2009

- **AAB 2008-5 (issued July 2008) 'Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB5, 7, 101, 102, 107, 108, 110, 116, 118, 119, 120, 123, 127, 128, 129, 131, 132, 134, 136, 138, 139, 140, 141, 1023 & 1038]'**

Effective for annual reporting periods beginning on or after 1 January 2009

- **AASB 2008-6 (issued July 2008) 'Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 1 & AASB 5]'**

Effective for annual reporting periods beginning on or after 1 July 2009

- **AASB 2008-7 (issued July 2008) 'Amendments to Australian Accounting Standards – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate [AASB1, AASB 118, AASB 121, AASB 127 and AASB 136]'**

Effective for annual reporting periods beginning on or after 1 January 2009

- **AASB 2009-5 (issued May 2009) 'Further Amendments to Australian Accounting Standards arising from the Annual Improvement Process'**

Effective for annual reporting periods beginning on or after 1 January 2010

- **AASB 8 (issued Feb 2007) 'Operating Segments'**

Effective for annual reporting periods beginning on or after 1 January 2009

- **AASB 101 (Revised Sep 2007) 'Presentation of Financial Statements'**

Effective for annual reporting periods beginning on or after 1 January 2009

- **AASB 2009-2 (issued April 2009) 'Amendments to Australian Accounting Standards – Improving Disclosures about Financial Instruments'**

Effective for annual reporting periods beginning on or after 1 January 2009

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

6. Going Concern

The consolidated entity incurred a loss for the year ended 30 June 2009 of \$2,840,527 (2008: \$2,072,610). For the year ended 30 June 2009, the consolidated entity had a net cash outflow from operating activities of \$2,432,920 (2008: \$1,677,882).

At 30 June 2009 the consolidated entity had cash assets of \$279,955 (2008: \$169,476), negative working capital of \$5,796,404 (2008: negative \$557,469) and net liabilities of \$1,104,191 (2008: net assets of \$694,233).

The Company has continued to incur losses and have net cash outflows from operating activities. These losses and cash outflows were exacerbated by the impact of the global financial crisis. As a result, the Company has increasingly relied on related party financial support. The willingness to provide this financial support demonstrates the Directors and major shareholders belief in the future of the Company.

At 30 June 2009, the consolidated entity had interest bearing liabilities, including accrued interest of \$7,960,047 owing to 698 Capital Asia Pacific Limited, a related party of the Company's major shareholder 698 Capital International Limited. All of these monies are at call or will be at call within the next 12 months. 698 Capital International Limited has resolved to provide financial support, in circumstances that will enable the Company to be able to meet its debts as and when they fall due, at least until one year from the signature of the Directors' Declaration. The financial support, of 698 Asia Pacific Capital Limited and 698 Capital International Limited, is subject to 698 Capital International Limited remaining the major shareholder of the Company holding not less than 40% of the ordinary issued shares in the Company.

The only other major, interest bearing, secured debt is \$750,000 owed to a Syndicate of investors principally made up of parties related to the Company's directors.

Based on 698 Capital International Limited's support, close to completed engine developments with major original equipment manufacturers in China and India, strategic international alliances and the expectation of improved sales revenue over the next twelve months, the Directors consider it appropriate that the financial report be prepared on a going concern basis.

7. Segment Information

The Group's primary segment reporting format is geographic segment as the Group's risks and rates of return are affected predominantly by relative performance of product in the geographic segment. Secondary segment information reported is business segment being performance of its product.

The operating businesses are organised and managed separately according to the relative performance of each geographic area with each segment representing a strategic business that offers varying opportunities and faces different economic conditions.

The French segment is predominantly the sale of spares and consumables. The China segment was predominantly the sale of NGVS kits to original equipment natural gas engine manufacturers in 2008 but includes both kits and spares in 2009. The Australian market is developing and offering both kits and spares but was predominantly spares through 2009. The South East Asia market is predominantly sales of Chinese manufactured natural gas engines incorporating the AEC NGVS.

Transfer prices between the Australian parent company and Chinese subsidiary company are set at an arms length basis in a manner similar to transactions with third parties. Segment revenue, segment expenses and segment results include transfers between business segments. Those transfers are eliminated on consolidation.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

7. Segment Information continued

Geographic segments

The Group's geographic segments are determined based on the relative performance of the segment. The following table presents revenue, expenditure and certain asset information regarding geographic segments for the years ended 30 June 2009 and 30 June 2008.

Primary reporting geographic segments	France	Australia	South East Asia	China	Consolidated
30 June 2009	\$	\$	\$	\$	\$
Segment Revenue:					
Sales to external customers	1,443,689	109,402	220,381	3,053,365	4,826,837
Inter-segment sales	-	1,866,695	-	65,595	1,932,290
Total sales revenue	1,443,689	1,976,097	220,381	3,118,960	6,759,127
Other revenue	-	145,460	39,555	625,938	810,953
Total segment revenue	1,443,689	2,121,557	259,936	3,744,898	7,570,080
Inter-segment sales elimination					(1,932,290)
Unallocated revenue					-
Consolidated revenue					5,637,790
Segment Result:					
Segment result	772,353	(3,426,354)	202,937	(389,463)	(2,840,527)
Unallocated revenue less unallocated expenses					-
Income tax expenses					-
Net profit/(loss) for the year					(2,840,527)
Segment Assets and Liabilities:					
Segment assets	-	9,956,693	40,173	3,544,712	13,541,578
Intersegment elimination					(2,765,468)
Total assets					10,776,110
Segment liabilities	-	10,436,242	-	4,209,527	14,645,769
Intersegment elimination					(2,765,468)
Total liabilities					11,880,301
Primary reporting geographic segments					
30 June 2009					
Other Segment Information:					
Capital expenditure	-	5,069	-	1,888	6,957
Depreciation	-	(185,217)	-	(6,501)	(191,718)
Amortisation	-	(340,541)	-	-	(340,541)
Government grant received for capitalised development costs	-	(116,140)	-	-	(116,140)
Unrealised exchange gain	-	11,751	-	-	11,751
Amount set aside for provisions	-	(270,268)	-	-	(270,268)
Provision for doubtful debt written back	-	12,000	-	-	12,000
Cash Flow Information:					
Net cash (outflow) from operating activities	-	(1,620,821)	-	(812,099)	(2,432,920)
Net cash (outflow) from investing activities	-	(1,129,017)	-	19,282	(1,109,735)
Net cash inflow from financing activities	-	3,653,134	-	-	3,653,134

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

Primary reporting geographic segments	France	Australia	South East Asia	China	Consolidated
30 June 2008	\$	\$	\$	\$	\$
Segment Revenue:					
Sales to external customers	884,763	181,129	1,747,278	1,859,050	4,672,220
Inter-segment sales	-	1,479,570	-	80,348	1,559,918
Total sales revenue	884,763	1,660,699	1,747,278	1,939,398	6,232,138
Other revenue	141,700	85,318	-	853	227,871
Total segment revenue	1,026,463	1,746,017	1,747,278	1,940,251	6,460,009
Inter-segment sales elimination					(1,559,918)
Unallocated revenue					-
Consolidated revenue					4,900,091
Segment Result:					
Segment result	681,405	(4,071,977)	1,036,453	281,509	(2,072,610)
Unallocated revenue less unallocated expenses					-
Income tax expenses					-
Net profit/(loss) for the year					(2,072,610)
Segment Assets and Liabilities:					
Segment assets	-	7,748,913	40,317	2,698,016	10,487,246
Intersegment elimination					(2,529,843)
Total assets					7,957,403
Segment liabilities	-	6,792,574	-	3,000,439	9,793,013
Intersegment elimination					(2,529,843)
Total liabilities					7,263,170

Primary reporting geographic segments	France	Australia	South East Asia	China	Consolidated
30 June 2008	\$	\$	\$	\$	\$
Other Segment Information:					
Investment in joint venture	-	-	40,317	-	40,317
Share of loss of joint venture	-	-	(29,386)	-	(29,386)
Capital expenditure	-	14,514	-	6,883	21,397
Depreciation	-	(195,216)	-	(9,440)	(204,656)
Amortisation	-	(219,433)	-	-	(219,433)
Government grant received for capitalised development costs	-	(108,495)	-	-	(108,495)
Unrealised exchange loss	-	(21,864)	-	-	(21,864)
Amount set aside for provisions	-	(122,394)	-	-	(122,394)
Provision for doubtful debt written back	-	129,571	-	-	129,571

Cash Flow Information:					
Net cash (outflow) from operating activities	-	(865,783)	-	(812,099)	(1,677,882)
Net cash (outflow) from investing activities	-	(1,191,339)	-	19,282	(1,172,057)
Net cash inflow from financing activities	-	2,408,276	-	-	2,408,276

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

7. Segment Information (continued)

Secondary reporting format – business segments

The Group currently operates within one business segment that being the commercialisation and sale of the AEC patented NGVS, associated components and products.

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
8. Revenue and Expenses				
(a) Revenue from continuing operations				
Sales revenue:				
Sales of goods	4,826,837	4,672,220	3,499,629	2,544,341
Total sales revenue	4,826,837	4,672,220	3,499,629	2,544,341
(b) Other income				
Interest revenue	3,732	19,323	3,372	18,470
Foreign exchange gain	589,556	14,722	191,406	14,722
Government grant	215,811	52,126	215,811	52,126
Other income	1,854	141,700	1,854	185,497
Total other revenue	810,953	227,871	412,443	270,815
Total revenue and other income	5,637,790	4,900,091	3,912,072	2,815,156
(c) Cost of inventories				
Included in cost of sales:				
Cost of inventories	2,563,079	2,841,150	1,771,063	1,365,964
(d) Employee benefits expense				
Wages and salaries	2,335,511	2,133,192	1,827,141	1,822,781
Superannuation expenses	143,936	142,512	143,936	142,512
Annual leave	124,811	84,093	124,811	84,093
Long service leave	59,926	61,800	59,926	61,800
Share based payments expenses	1,976	87,674	1,976	87,674
Total	2,666,160	2,509,271	2,157,790	2,198,860

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
8. Revenue and Expenses (continued)				
(e) Finance costs				
Interest:				
Director related entities-				
698 Capital Asia Pacific Limited	334,065	357,976	334,065	357,976
Norvest Corporate Pty Ltd	8,436	-	8,436	-
Other financial loans	459,657	90,704	456,148	90,704
	<u>802,158</u>	<u>448,680</u>	<u>798,649</u>	<u>448,680</u>
(f) Lease payments				
Operating lease rental expenses				
Minimum lease payments	<u>222,789</u>	<u>172,767</u>	<u>155,683</u>	<u>119,689</u>
(g) Development costs				
Development costs charged directly to the income statement	<u>1,035,045</u>	<u>820,641</u>	<u>815,526</u>	<u>732,092</u>
(h) Other disclosure items in respect of the loss from continuing operations				
Depreciation of plant and equipment	172,500	185,385	165,999	175,945
Amortisation of leasehold Improvements	19,218	19,271	19,218	19,271
Amortisation of intangible assets	340,541	219,433	340,541	219,433
Foreign exchange net loss	-	81,279	168,408	81,279
<i>Net transfer to / (from) provisions:</i>				
Provision for warranties	28,853	3,000	28,853	3,000
Employee entitlements	<u>262,942</u>	<u>119,394</u>	<u>262,942</u>	<u>119,394</u>
Provision for doubtful debts written back	(12,000)	(129,571)	(12,000)	(173,367)
Share of loss of joint venture	-	29,386	-	-
Impairment expenses	<u>50,800</u>	<u>-</u>	<u>760,239</u>	<u>-</u>

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
9. Taxation				
The reconciliation between tax expense and the product of accounting loss before tax multiplied by Group's applicable income tax rate is as follows				
Loss before income tax	(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
Income tax /(benefit) @ 30%	(852,158)	(621,783)	(919,237)	(633,440)
Tax effect of amounts which are not deductible in calculating taxable income:				
Share based payments	67,012	26,307	67,012	26,307
Sundry items not deductible	19,349	1,206	19,349	1,206
Temporary differences not recognised	(28,378)	(157,420)	393,000	(159,236)
Deferred tax assets relating to tax losses not recognised	782,491	743,063	439,876	765,163
Adjustment due to the difference of tax rates between China and Australia	11,684	8,627	-	-
Total income tax benefit	-	-	-	-
The franking account balance at year end was \$nil (2008: \$nil)				
Deferred tax assets and liabilities not recognised relate to the following:				
Deferred tax assets:				
Tax losses	10,236,476	8,398,979	9,551,764	8,364,707
Other temporary differences	679,032	623,234	1,100,411	621,418
	10,915,508	9,022,213	10,652,175	8,986,125
Deferred tax liabilities	1,294,489	698,143	1,294,489	698,143
Net deferred tax assets	9,621,019	8,324,070	9,357,686	8,287,982

Net deferred tax assets have not been brought to account as it is not probable within the immediate future that tax profits will be available against which deductible temporary differences and tax losses can be utilised.

Tax Consolidation Legislation

For the purposes of income taxation, Advanced Engine Components Limited has not elected to form a tax-consolidated group. It is not expected the Group will elect to form a consolidated tax group, as there does not appear to be any benefit in doing so. There will be no consequences to the deferred tax assets, deferred tax liability, un-utilised tax losses by not joining the consolidated tax regime.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
10. Loss Per Share				
Net loss attributable to ordinary equity holders of the parent	(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
Weighted average number of ordinary shares for basic and diluted loss per share	148,139,591	137,734,574	148,139,591	137,734,574
Loss per share				
- Basic loss per share	(\$0.0192)	(\$0.0150)	(\$0.0207)	(\$0.0153)
- Diluted loss per share	(\$0.0192)	(\$0.0150)	(\$0.0207)	(\$0.0153)

Diluted loss per share has not been calculated as the result is currently anti-dilutive in nature. The issued options and convertible notes however, could be potentially dilutive in the future.

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
11. Remuneration of Auditors				
<i>Auditors of the Company - BDO Kendalls Audit & Assurance (WA) Pty Ltd: audit and review of the financial report</i>				
- Current year	67,950	62,743	60,142	56,665
<i>Non assurance services – taxation related parties of BDO Kendalls Audit & Assurance (WA) Pty Ltd</i>				
- Tax compliance	-	7,300	-	7,300
- Other	-	7,304	-	7,304
	67,950	77,347	60,142	71,269

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
12. Cash and Cash Equivalents				
For the purposes of the Cash Flow Statement, cash and cash equivalents comprise the following at 30 June				
Cash at bank and in hand	279,955	169,476	265,750	93,769
(a) Reconciliation to cash at the end of the year				
Balance as above	279,955	169,476	265,750	93,769
Bank overdraft	-	-	-	-
Balance per statement of cash flows	279,955	169,476	265,750	93,769
(b) Reconciliation of loss from continuing operations after income tax to net cash flows used in operations				
Loss from continuing operations after income tax	(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
Government grant received and offset against capitalised development costs	116,140	108,495	116,140	108,495
<i>Add non-cash items:</i>				
Depreciation and amortisation of non-current assets	532,259	424,089	525,758	414,649
Provision for doubtful debt written back	(12,000)	(129,571)	(12,000)	(173,367)
Share of loss of joint venture	-	29,386	-	-
Costs of share based payment	165,774	87,674	165,774	87,674
Unrealised foreign exchange loss	(11,751)	21,864	-	-
Net cash (used in) operating activities before changes in net assets and liabilities	(2,038,105)	(1,530,673)	(2,256,451)	(1,674,016)
Changes in net assets and liabilities:				
<i>(Increase)/decrease in assets:</i>				
Current trade and other receivables	(1,126,871)	(1,009,167)	(612,568)	(970,777)
Current inventories	(105,365)	(34,027)	(193,187)	321,350
<i>Increase/(decrease) in liabilities:</i>				
Current trade and other payables	770,169	833,334	633,648	669,575
Current and non-current provisions	67,252	62,651	67,252	62,651
Net cash (used in) operating activities	(2,432,920)	(1,677,882)	(2,373,306)	(1,591,217)

Non-cash financing and investing activities

During the year ended 30 June 2009 there were the following non-cash financing and investing transactions:

- (i) Insurance premiums with a fair value of \$134,922 (2008: \$214,174) were financed.
- (ii) A loan of \$750,000 from CIM Special Situations Fund Limited was assigned to a syndicate led by Norvest Corporate Pty Ltd, a company related to a Director of the Company (note 20).
- (iii) The Company facilitated a US\$700,000 (AUD1,010,393) loan from an unrelated company, CCM Global Limited, to the Thailand joint venture company, Monika AEC Limited. The loan was delivered directly to Monika AEC Limited and did not involve cash flow through the Company. The Company has recorded an asset and a liability of US\$700,000 (AUD1,010,393) in the consolidated accounts. For facilitating the loan the Company is entitled to a margin on interest payable (notes 13 and 20).

Refer to note 29 for more information on the risk exposure.

AEC Group

AEC Entity

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
13. Trade and Other Receivables				
Trade receivables (i)	3,218,630	1,940,620	585,638	332,442
Provision for doubtful debts	(172,728)	(184,728)	(172,728)	(184,728)
	3,045,902	1,755,892	412,910	147,714
Loan to Monika AEC Limited (ii)	1,010,393	-	1,010,393	-
Other receivables:				
Prepayments	143,025	306,164	135,271	211,263
Inter company loan	-	-	695,155	794,808
Less: provision for diminution of loan	-	-	(695,155)	(794,808)
Inter company trade receivable	-	-	2,765,469	2,330,105
	<u>4,199,320</u>	<u>2,062,056</u>	<u>4,324,043</u>	<u>2,689,082</u>
Non hedging foreign currency receivable above (iii)	504,527	253,801	504,527	253,803

- (i) Trade receivables are non-interest bearing and are generally on 30 to 90 day terms. An allowance for doubtful debts is made when there is objective evidence that a trade receivable is impaired.
- (ii) The Company facilitated a US\$700,000 (AUD1,010,393) loan from an unrelated company, CCM Global Limited, to the Thailand joint venture company, Monika AEC Limited. The loan was delivered directly to Monika AEC Limited and did not involve cash flow through the Company. The Company has recorded an asset and a liability of US\$700,000 (AUD1,010,393) in the consolidated accounts. For facilitating the loan the Company is entitled to a margin on interest payable. The loan is unsecured.
- (iii) Non hedging foreign currency receivable represents the net receivable from a foreign customer expressed in EURO182,009 (2008: EURO 154,590).
- (iv) The average credit period on sales of goods is 90 days with no credit period applied to sales of spare parts. No interest is charged on the trade receivables. The normal credit term applied to established customers is 60 days and new customers are required to pay 30% deposit in advance before the delivery of goods and 70% remaining upon delivery of goods. The Group has not provided for all receivables over 120 days because historical experience is such that receivables that are past due beyond 120 days are still recoverable. Trade receivables are provided for based on estimated irrecoverable amounts from the sale of goods, determined by reference to past default experience.

Of the trade receivables balance at the end of the year, \$2,867,658 (2008: \$1,646,164) is due from Weifang Weichai Peterson Gas Engine Co. Ltd (44%), Deutz (Dailian) Engine Co. Ltd (5%), Norinco Equipment Co. Ltd (23%), Iveco France SA (10%) and Aussen engine (Dalian) Co., Ltd (7%), the Group's largest customers. There are no other customers who represent more than 5% of the total balance of trade receivables.

Receivables owing by Weifang Weichai Peterson Gas Engine Co. Ltd have been outstanding in excess of 240 days. The Company has been negotiating recovery for in excess of 180 days with part recoveries being received in that period. Subsequent to year end agreement has been reached for payment of kits associated with engine sales facilitated by the Company. Further reductions will result from return and resale of unused kits. The balance, of less than 50%, remains the subject of further negotiation.

(a) Ageing of trade receivables past due but not impaired

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
60 – 90 days	4,092	253,177	59,303	104,811
90 – 120 days	15,826	28,455	112,492	37,506
3 months – 6 months	1,249	177,587	135,916	488,983
6 months +	2,078,232	82,077	3,369,448	1,362,468
Total	<u>2,099,399</u>	<u>541,296</u>	<u>3,677,159</u>	<u>1,993,768</u>

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(b) Movement in the allowance for doubtful debts

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
Balance at the beginning of the year	(184,728)	(314,299)	(184,728)	(314,299)
Amounts recovered during the year	12,000	129,571	12,000	129,571
Balance at the end of the year	(172,728)	(184,728)	(172,728)	(184,728)

In determining the recoverability of a trade receivable, the Group considers any change in the credit quality of the trade receivable from the date credit was initially granted up to the reporting date. The concentration of credit risk is limited due to the customer base being large and unrelated. Accordingly, the Directors believe that there is no further credit provision required in excess of the allowance for doubtful debts.

(c) Ageing of impaired trade receivables

As at 30 June 2009, \$172,728 (2008: \$184,728) of trade receivables for the Group and the Parent were impaired. The amount of the provision was \$172,728 (2008: \$184,728).

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
60 – 90 days	-	-	-	-
90 – 120 days	-	-	-	-
120 days +	172,728	184,728	172,728	184,728
Total	172,728	184,728	172,728	184,728

(d) Fair value and credit risk

Due to the short-term nature of these receivables, their carrying amount is assumed to approximate their fair value.

The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivables mentioned above. Refer to note 29 for more information on the risk management policy of the Group and the credit quality of the Group's trade receivables.

(e) Foreign currency of trade receivables

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
RMB	2,632,992	1,608,104	-	-
EUR	504,527	253,801	504,527	253,801
AUD	81,111	78,715	2,846,580	2,408,746
Total	3,218,630	1,940,620	3,351,107	2,662,547

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
14. Inventories				
Raw materials – at cost	453,066	419,882	453,066	419,883
Work in progress – at cost	202,590	151,897	202,590	151,897
Finished goods – at cost	948,966	927,478	258,953	149,642
Total Inventories at the lower of cost and net realisable value	1,604,622	1,499,257	914,609	721,422

Inventories recognised as an expense during the year ended 30 June 2009 amounted to \$2,563,079 (2008: \$2,841,150).

15. Other Financial Assets (Non-current)

Investment in controlled entities (note 28)	-	-	156,013	156,013
Less: Provision for diminution	-	-	(156,013)	(156,013)
	-	-	-	-

These financial assets are carried at amortised cost.

16. Investments Accounted for Using the Equity Method (Non-Current)

The Company has entered into a joint venture arrangement in Thailand to build new natural gas (“NG”) powered vehicles and re-power existing diesel vehicles with NG engines. The Company is partners in joint venture with Monika Motors Limited (51%), a Thai based strategic investment company (19%) and a Thai based individual with wide experience in Thailand’s public transport and government (9%). During the year, as a result of the dilution of the 19% shareholder in Monika AEC Limited, the Company’s shareholding has increased from 21% to 26%.

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
Investment in jointly controlled entity	40,317	40,317	69,703	69,703

Reconciliation of movement in investments accounted for using the equity method:

	AEC Group	AEC Group
	2009	2008
	\$	\$
Balance as at 1 July	40,317	-
Addition	-	69,703
Share of loss	-	(29,386)
Balance at 30 June	40,317	40,317

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

16. Investments Accounted for Using the Equity Method (Non-Current) (continued)

The interest in the joint venture is accounted for in the consolidated financial statement using the equity method of accounting and is carried at cost by the parent entity. The Group has not recognised profit relating to Monika AEC Limited for the year ended 30 June 2009 based on an evaluation of risks and rewards. Information relating to the joint venture for the year ended 30 June 2009 not adjusted for the percentage ownership holding by the Group is set out below.

	2009	2008
	\$	\$
Share of joint venture's assets and liabilities		
Current assets	607,168	139,454
Non-current assets	28,421	9,046
Total assets	635,589	148,500
 Current liabilities	472,526	108,183
Total liabilities	472,526	108,183
 Net assets	163,063	40,317
 Share of revenue, expenses and results		
Revenue	1,387,137	-
Expenses	(1,348,000)	(16,390)
Profit/(loss) before income tax	39,137	(16,390)

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

17. Plant and Equipment

	AEC Group				
	Plant and Equipment \$	Leased Plant & Equipment \$	Leasehold Equipment \$	Capital WIP \$	Total \$
At 1 July 2007					
Cost or deemed cost	2,420,270	737,541	233,503	176,647	3,567,961
Accumulated depreciation	(1,972,537)	(737,541)	(75,200)	-	(2,785,278)
Net book amount	447,733	-	158,303	176,647	782,683
Year ended 30 June 2008					
Opening net book amount	447,733	-	158,303	176,647	782,683
Additions	20,491	-	-	906	21,397
Depreciation charge	(185,385)	-	(19,271)	-	(204,656)
Closing net book amount	282,839	-	139,032	177,553	599,424
At 30 June 2008					
Cost or deemed cost	2,440,761	737,541	233,503	177,553	3,589,358
Accumulated depreciation	(2,157,922)	(737,541)	(94,471)	-	(2,989,934)
Net book amount	282,839	-	139,032	177,553	599,424
Year ended 30 June 2009					
Opening net book amount	282,839	-	139,032	177,553	599,424
Additions	4,638	-	-	2,319	6,957
Depreciation charge	(172,500)	-	(19,218)	-	(191,718)
Exchange difference	4,263	-	-	-	4,263
Closing net book amount	119,240	-	119,814	179,872	418,926
At 30 June 2009					
Cost or deemed cost	2,445,399	737,541	233,503	179,872	3,596,315
Accumulated depreciation	(2,330,422)	(737,541)	(113,689)	-	(3,181,652)
Exchange difference	4,263	-	-	-	4,263
Net book amount	119,240	-	119,814	179,872	418,926

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

17. Plant and Equipment (continued)

	AEC Entity				
	Plant and Equipment \$	Leased Plant & Equipment \$	Leasehold Equipment \$	Capital WIP \$	Total \$
At 1 July 2007					
Cost or deemed cost	2,383,258	737,541	233,503	176,647	3,530,949
Accumulated depreciation	(1,956,647)	(737,541)	(75,200)	-	(2,769,388)
Net book amount	426,611	-	158,303	176,647	761,561
Year ended 30 June 2008					
Opening net book amount	426,611	-	158,303	176,647	761,561
Additions	13,608	-	-	906	14,514
Depreciation charge	(175,945)	-	(19,271)	-	(195,216)
Closing net book amount	264,274	-	139,032	177,553	580,859
At 30 June 2008					
Cost or deemed cost	2,396,866	737,541	233,503	177,553	3,545,463
Accumulated depreciation	(2,132,592)	(737,541)	(94,471)	-	(2,964,604)
Net book amount	264,274	-	139,032	177,553	580,859
Year ended 30 June 2009					
Opening net book amount	264,274	-	139,032	177,553	580,859
Additions	2,750	-	-	2,319	5,069
Depreciation charge	(165,999)	-	(19,218)	-	(185,217)
Closing net book amount	101,025	-	119,814	179,872	400,711
At 30 June 2009					
Cost or deemed cost	2,399,616	737,541	233,503	179,872	3,550,532
Accumulated depreciation	(2,298,591)	(737,541)	(113,689)	-	(3,149,821)
Net book amount	101,025	-	119,814	179,872	400,711

(i) Revaluation of plant and equipment

An independent valuation of plant and equipment was undertaken by Garside and Webb (Specialist Auctioneers and Valuers) on 13 April 2005. The valuation was based upon a going concern basis. Upon revaluation, the Directors consider the fair value is deemed costs for plant and equipment.

(ii) Leased assets are pledged as security for the related finance lease.

(iii) Plant and equipment are subject to a first charge to secured loan from 698 Capital Asia Pacific Limited.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

18. Intangible Assets

	AEC Group and AEC Entity
	Development Costs
	\$
At 1 July 2007	2,833,844
Additions – internal development (i)	1,080,957
Government grant received	(108,495)
Amortisation charge	(219,433)
Net of accumulated amortisation at 30 June 2008	3,586,873
Additions – internal development (i)	1,102,778
Government grant received	(116,140)
Amortisation charge	(340,541)
Net of accumulated amortisation at 30 June 2009	4,232,970

Development costs have been capitalised at cost. This intangible asset has been assessed as having a finite life of five years and amortised using a straight-line method over the period from commencement of commercial sales.

- (i) During the year total development costs incurred were \$2,137,823 (2008: \$1,901,598). Of this \$1,035,045 (2008: \$820,641) was expensed, whilst \$1,102,778 (2008: \$1,080,957) was capitalised. .

Key assumptions

As at the reporting date the Group has performed an impairment assessment. Apart from \$50,800 impairment made for 3 terminated projects, no other impairment was noted for the years ended 30 June 2008 and 2009. The key assumptions used in the value in use calculations for developments costs of the Group are as follows:

Budgeted growth

Average growth in the period immediately before the budget period, plus growth percentage based on the orders received. Management expected these were 100% plus 100% from actual then 30% average 30% growth (2008: 50%) for the next five years.

Budgeted selling price and costs

Average selling price and costs immediately before the budget period, plus orders received. Management expected falling selling prices with similar percentage falling in costs in the next couple of years (2008: selling prices with similar percentage falling in costs).

Budgeted gross margin

Average gross margins of 25% (2008: 40%) achieved in the period immediately before the budget period, increased for expected efficiency improvements. This reflects past experience. Management expects gross margin will remain consistent for the next couple of years.

Discount rate

12.45% (2008: 10%) discount rate was used as current higher interest rates of 9% plus 10% withholding tax was considered to be reasonable discount rate.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
19. Trade and Other Payables				
Trade payables (i)	673,574	485,909	677,736	480,608
Other payables (ii)	1,731,794	1,205,831	1,530,646	1,199,776
GST payables	91,212	140,321	-	-
Non-hedging foreign currency payable (iii)	237,887	132,237	237,887	132,237
	<u>2,734,467</u>	<u>1,964,298</u>	<u>2,446,269</u>	<u>1,812,621</u>

- (i) Trade payables are non-interest bearing and are predominantly settled on 60-day terms.
- (ii) Other payables includes \$962,531 (2008: \$735,431) of accrued interest owing on the convertible note held by 698 Capital Asia Pacific Limited (refer note 22) a related party.
- (iii) Information regarding effective interest rate and credit risk of current payable is set out in note 29.

(a) Foreign currency of trade payables

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
RMB	38,033	75,264	-	-
USD	206,008	79,195	206,008	79,195
EURO	31,006	53,045	31,006	53,045
THB	873	-	873	-
AUD	635,541	410,642	677,736	480,605
Total	<u>911,461</u>	<u>618,146</u>	<u>915,623</u>	<u>612,845</u>

(b) Amount not expected to be settled within the next 12 months

Other payables include accruals for annual leave. The entire obligation is presented as current, since the Group does not have an unconditional right to defer settlement. However, based on past experience, the Group does not expect all employees to take the full amount of accrued leave within the next 12 months. The following amounts reflect leave that is not expected to be taken within the next 12 months.

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
Annual leave obligation expected to be settled after 12 months	131,246	154,146	131,246	154,146

Refer to note 29 for the risk exposure.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
20. Borrowings (current liabilities)				
<i>Unsecured:</i>				
Insurance premiums finance (i)	134,922	214,174	134,922	214,174
Loan from 698 Capital Asia Pacific Ltd (ii)	869,589	1,045,479	869,589	1,045,479
Loan from Syndicate / CIM SSF (iii)	-	778,767	-	778,767
Loan from Norvest Corporate Pty Ltd (iv)	46,361	-	46,361	-
Loan from CCM Global Limited (v)	1,010,393	-	1,010,393	-
<i>Secured:</i>				
Loan from 698 Capital Asia Pacific Ltd (vi)	2,994,476	-	2,994,476	-
Loan from Syndicate / CIM SSF (iii)	759,247	-	759,247	-
Convertible Note held by 698 Capital Asia Pacific Ltd (vii)	2,975,451	-	2,975,451	-
Commercial loan from Westpac (viii)	31,141	28,538	31,141	28,538
	<u>8,821,580</u>	<u>2,066,958</u>	<u>8,821,580</u>	<u>2,066,958</u>

- (i) Terms are 3.51% (2008: 3.38%) interest per annum on borrowed amount repayable over 10 months to February 2010.
- (ii) Terms are 9% (2008: 9%) interest per annum payable quarterly in arrears and the principal is repayable on demand.
- (iii) Terms are 15% (2008: 9%) interest per annum and the principal is repayable on 30 April 2010. Secured by a fixed charge over the Irisbus Contract with the Company by Deed of Charge dated 9 March 2009. A Syndicate was formed to takeover the loan and security from CIM Special Situations Fund Limited in March 2009.
- (iv) Terms are 15% interest per annum and the principal is repayable on demand.
- (v) The Company facilitated a US\$700,000 (AUD1,010,393) loan from an unrelated company, CCM Global Limited, to the Thailand joint venture company, Monika AEC Limited. The loan was delivered directly to Monika AEC Limited and did not involve cash flow through the Company. The Company has recorded an asset and a liability of US\$700,000 (AUD1,010,393) in the consolidated accounts. For facilitating the loan the Company is entitled to a margin on interest payable.
- (vi) Terms are 11.68% interest per annum payable quarterly in arrears and the principal is repayable on 31 December 2009. Secured by a fixed charge over the accounts receivable and inventory of the Company excluding those associated with the Irisbus Contract.
- (vii) Secured by a fixed and floating charge over the assets of the Company. The net carrying amount as at 30 June 2009 is \$101,025 (2008: \$264,274). The maturity date is by 31 December 2009. The lender has agreed to allow the Syndicate/CIM SSF prior charge over the Irisbus Contract and Westpac Bank prior charge over certain plant & equipment.
- (viii) Terms are 8.5% interest per annum repayable along with principal over 48 months to June 2010. Secured by a fixed charge over certain plant & equipment.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

20. Borrowings (current liabilities) (continued)

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
(ix) Total facilities				
- Insurance premium finance loan	168,753	258,269	168,753	258,269
Facilities used at reporting date				
- Insurance premium finance loan	168,753	258,269	168,753	258,269
Assets pledged as security				
<i>The carrying amounts of assets pledged as security are:</i>				
Fixed & floating charge over assets				
- Current assets	5,803,942	3,561,313	5,238,652	3,410,504
- Plant and equipment	101,025	264,274	101,025	264,274
- Intangible assets	4,232,970	3,586,873	4,232,970	3,586,873

(x) Fair value disclosures

Details of the fair values of borrowings and interest rate exposure for the Group are set out in note 29.

21. Provisions

AEC Group and AEC Entity	2009			2008		
	Warranties	Long Service Leave	Total	Warranties	Long Service Leave	Total
	\$	\$	\$	\$	\$	\$
Opening balance	82,840	174,162	257,002	81,989	112,362	194,351
Arising during the year	28,853	59,926	88,779	3,000	61,800	64,800
Utilised	(21,527)	-	(21,527)	(2,149)	-	(2,149)
Closing balance	90,166	234,088	324,254	82,840	174,162	257,002
Current	90,166	234,088	324,254	82,840	174,162	257,002
Non current	-	-	-	-	-	-

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

21. Provisions (continued)

(a) Warranties

A provision is recognised for expected warranty claims on products sold during the year based on past experience of the level of repairs and returns. Assumptions used to calculate the provision for warranties were based on current sales levels and current information available about returns based on the warranty period for all products sold.

(b) Amounts not expecting to be settled within 12 months

The current provision for long service leave includes all entitlements where employees have completed the 7 years services. The non-current provision for long service leave includes all entitlements where employees have not completed 7 years services. However, based on past experience, the Group does not expect all employees to take the full amount of accrued long service leave or require payment within the next 12 months. The following amounts reflect leave that is not expected to be taken or paid within the next 12 months.

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
Long service leave obligation expected to be settled after 12 months	-	174,162	-	174,162

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
22. Borrowings (Non-current Liabilities)				
Secured:				
Convertible Note held by 698 Capital Asia Pacific Ltd (i)	-	2,943,771	-	2,943,771
Commercial loan from Westpac (ii)	-	31,141	-	31,141
	-	2,974,912	-	2,974,912

(i) Secured by a fixed and floating charge over the assets of the Company. The net carrying amount as at 30 June 2009 is \$101,025 (2008: \$264,274). The maturity date is by 31 December 2009. The lender has agreed to allow the Syndicate/CIM SSF prior charge over the Irisbus Contract and Westpac Bank prior charge over certain plant & equipment.

(ii) Terms are 8.5% interest per annum repayable along with principal over 48 months to June 2010. Secured by a fixed charge over certain plant & equipment.

Details of the fair values of borrowings and interest rate exposure for the Group are set out in note 29.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
23. Contributed Equity				
(a) Share capital				
Ordinary shares	18,208,020	17,324,203	18,208,020	17,324,203
Movement in Ordinary shares on issue	Number	\$	Number	\$
At 1 July 2007	129,052,214	15,099,939	129,052,214	15,099,939
Shares Issued -				
• Rights Issue on 22 November 2007	14,339,644	2,294,343	14,339,644	2,294,343
• Options exercised	44,161	5,652	44,161	5,652
• Share issue costs		(75,731)		(75,731)
Balance as at 30 June 2008	143,436,019	17,324,203	143,436,019	17,324,203
Shares Issued -				
• Options exercised	6,450	826	6,450	826
• Pursuant to Underwriting Agreement with KGI	4,361,529	872,306	4,361,529	872,306
• Part settlement of creditor accounts	1,254,118	72,600	1,254,118	72,600
• Share issue costs		(61,915)		(61,915)
Balance as a 30 June 2009	149,058,116	18,208,020	149,058,116	18,208,020
<i>Terms and conditions</i>				
Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders meetings.				
In the event of winding up of the Company, ordinary shareholders rank after all other shareholders and creditors, and are fully entitled to any surplus proceeds of liquidation.				
	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
(b) Convertible notes				
Balance as at 1 July and 30 June	158,000	158,000	158,000	158,000
Total contributed equity	18,366,020	17,482,203	18,366,020	17,482,203

On 6 April 2005, Advanced Engine Components Limited issued 3,000,000 Convertible Notes at \$1.00 each to 698 Capital Asia Pacific Ltd. The Convertible Notes can be converted into fully paid ordinary shares at 40 cents per share at any time on or before 31 December 2009. The Convertible Notes are secured by a first fixed and floating charge over all present and future assets and undertakings of the Company and its subsidiaries. Interest is paid annually in arrears at a rate of 7.57%. The equity component of the Convertible Notes was revalued on adoption of AIFRS and an adjustment of \$1,165,000 was transferred to Borrowings (non-current liabilities) during the year ended 30 June 2006.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

23. Contributed Equity and Reserves (continued)

(c) Options

As at 30 June 2009, the following were options over unissued ordinary shares:

- 7,119,272 (2008: 7,125,722) options exercisable at 12.8 cents per share on or before 30 November 2009.
- 1,180,000 (2008: 1,180,000) options exercisable at 18 cents per share on or before 31 December 2010.
- 5,505,000 (2008: Nil) options exercisable at 20 cents per share on or before 31 December 2010.
- 2,500,000 (2008: Nil) options exercisable at 6.0 cents per share on or before 30 November 2011.
- 1,250,000 (2008: Nil) options exercisable at 5.5 cents per share on or before 30 November 2011.
- 1,250,000 (2008: Nil) options exercisable at 5.0 cents per share on or before 30 November 2011.
- 30,000 (2008: Nil) options exercisable at 4.7 cents per share on or before 30 November 2011.
- 30,000 (2008: Nil) options exercisable at 4.4 cents per share on or before 30 November 2011.
- Nil (2008: 5,859,375) options exercisable at 12.8 cents per share on or before 31 October 2008.
- Nil (2008: 440,000) options exercisable at 19 cents per share on or before 31 December 2008.

Refer to note 29 for the risk exposure.

24. Reserves

	AEC Group				AEC Entity		
	Asset Revaluation Reserve	Share Based Payments Reserve	Foreign Currency Translation Reserve	Total	Asset Revaluation Reserve	Share Based Payments Reserve	Total
	\$	\$	\$	\$	\$	\$	\$
At 1 July 2007	750,000	241,492	48,097	1,039,589	750,000	241,492	991,492
Value of share based payment	-	87,674	-	87,674	-	87,674	87,674
Currency translation	-	-	21,864	21,864	-	-	-
Balance as at 30 June 2008	750,000	329,166	69,961	1,149,127	750,000	329,166	1,079,166
Value of share based payment	-	165,774	-	165,774	-	165,774	165,774
Currency translation	-	-	(7,488)	(7,488)	-	-	-
Balance as at 30 June 2009	750,000	494,940	62,473	1,307,413	750,000	494,940	1,244,940

Nature and purpose of reserves

Asset revaluation reserve

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

Share based payments reserve

This reserve is used to record the value of equity benefits to employees, Directors and consultants, as part of their remuneration, and to financiers as part of their financing package. When the options are exercised the amount recorded in the Share Based Payments Reserve relevant to those options is transferred to share capital.

Foreign currency translation reserve

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

Options

Refer note 27 for details of Employee Share Option Plan.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

25. Accumulated Losses

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
Accumulated losses at the beginning of the year	(17,937,097)	(15,864,487)	(17,931,154)	(15,819,687)
Net loss after income tax	(2,840,527)	(2,072,610)	(3,064,123)	(2,111,467)
Accumulated losses at the end of the year	(20,777,624)	(17,937,097)	(20,995,277)	(17,931,154)

26. Commitments for Expenditure

Operating leases

Leasing arrangements

The Group leases property and equipment under non-cancellable and cancellable operating leases expiring from 1 to 4 years. Leases generally provide the Group with a right of renewal at which time all terms are re-negotiated.

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
Not later than 1 year	144,356	129,916	127,378	127,378
Later than 1 year and not later than 5 years	356,106	467,052	339,674	467,052
	500,462	596,968	467,052	594,430

27. Share Based Payments

(a) Employee Share Option Plan

There were no share options granted to eligible staff during the year ended 30 June 2009 (2008: 1,180,000). The exercise price of the Employee Share Option Plan options is equal to 110% of the weighted average sale price of shares trading on ASX calculated over a 5 business day period ending on the day prior to the date of grant. The options issued in 2008 are exercisable on or before 31 December 2010. The expense recognised in the income statement in relation to share based payment plans for 2008 is disclosed in note 24.

The following table details number, weighted average exercise prices (WAEP) and movements in share options issued under the Employee Share Option Plan during the year.

	2009 Nos.	2009 WAEP	2008 Nos.	2008 WAEP
Outstanding at the beginning of the year	1,620,000	18.3 cents	450,000	19.0 cents
Cancelled during the year	(440,000)	19.0 cents	(10,000)	19.0 cents
Exercised during the year	-	-	-	-
Granted during the year	-	-	1,180,000	18.0 cents
Outstanding at the end of the year	1,180,000	18 cents	1,620,000	18.3 cents
Exercisable at the end of year	1,180,000	18 cents	1,620,000	18.3 cents

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

- (i) The outstanding balance as at 30 June 2009 is represented by 1,180,000 (2008: 1,620,000) options, granted on 23 November 2007, over ordinary shares with an exercise price of \$0.18 each, exercisable on or before 31 December 2010.
- (ii) The weighted average remaining contractual life for the share options outstanding as at 30 June 2009 is 18 months.
- (iii) The exercise price for 1,180,000 options outstanding at the end of the year was \$0.18.
- (iv) There were no options granted under the Employee Share Option Plan during the 2009 year.
- (v) The fair value of the equity settled options granted under the options is estimated using Black-Scholes options pricing model taking into account the terms and conditions upon which the instruments were granted.
- (vi) There is no alternative to equity settlement option.

The following table lists the inputs to the model used for the years ended 30 June 2009 (refer note 27(b)(i)) and 2008:

	2009	2008
Dividend Yield (%)	0%	0%
Expected volatility (%)	126.8%	75.1%
Risk-free interest rate (%)	3.18%	6.47%
Expected life of option (years)	2.0 years	2.5 years
Option exercise price (\$)	\$0.20	\$0.18
Spot share price at grant date (\$)	\$0.07	\$0.15

(b) Options issued for Services Rendered

During the year the following options, as approved by shareholders at the 2008 Annual General Meeting or ratified by shareholders at the 3 July 2009 General Meeting:

Options issued #	Services rendered	Value \$
275,000 (i)	Chairman of the Company	8,718
230,000(i)	Third party consulting services	6,731
5,000,000(ii)	In lieu of interest	12,500
5,000,000(iii)	Part consideration for finance	137,750
60,000(iii)	Part consideration for finance	75

- (i) 275,000 options were issued in consideration of services provided by Mr. G Keys as Chairman of the Company and 230,000 options were issued for third party consulting services. The options are exercisable on or before 31 December 2010 at an exercise price of 20 cents per share. The fair value of the services is estimated using the Black-Scholes options pricing model taking into account the terms and conditions upon which the instruments were granted (refer note 27(a)).
- (ii) 5,000,000 options were issued to 698 Capital Asia Pacific Limited as consideration for a 0.75% reduction in the base interest rate of the \$2,000,000 financing facility. The options are exercisable on or before 31 December 2010 at an exercise price of 20 cents per share. The value was calculated based on the value of the interest forgone by the lender.
- (iii) 5,060,000 options were issued to third parties as part consideration for extending existing finance facilities. The options are exercisable on or before 30 November 2011 at an exercise price calculated on the volume weighted share price in the month preceding the date of issue. The fair value of the cost of finance is estimated using the Black-Scholes options pricing model taking into account the terms and conditions upon which the instruments were granted.

(c) Shares issued for services rendered

During the year 1,254,118 shares were issued, as ratified by shareholders at the 3 July 2009 General Meeting, for consulting services rendered. The issue price of the shares was calculated as the volume weighted average share price in the month preceding the date of issue. 960,000 shares were issued, at an issue price of 6 cents per share in February 2009, to satisfy an outstanding creditor payment of \$57,600 and 294,118 shares were issued, at an issue price of 5.1 cents per share in May 2009, to satisfy an outstanding creditor payment of \$15,000

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

28. Controlled Entities

		Ownership Interest	
Name of Entity	Country of Incorporation	2009 %	2008 %
Parent Entity			
Advanced Engine Components Limited	Australia		
Controlled Entities			
Transcom NGVS Research Pty Ltd.	Australia	100	100
AEC Vehicle Technology Pty Ltd.	Australia	100	100
AEC China Holdings Ltd.	British Virgin Island	100	100
AEC China Ltd.	China	100	100

29. Financial Risk Management

The Group's activities expose it to a variety of financial risks: market risk (including currency risk and interest risk), credit risk and liquidity risk. The Group uses different methods to measure different types of risk to which it is exposed. These methods include sensitivity analysis in the case of interest rate and foreign exchange, aging analysis for credit risk. Please refer to methods below for each risk.

Risk management is carried out by the Financial Department under policies approved by the Board of Directors. Financial Department identifies and evaluates financial risks in close co-operation with the Group's operating units. The Board provides direction on overall risk management, as well as policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of non-derivative financial instruments, and investment of excess liquidity.

The Group's Financial Department function provides services to the business, co-ordination access to domestic and international financial markets, monitors and manages the financial risks relating to the operations of the Group through internal risk reports which analyse exposures by degree and magnitude of risks. These risks include market risk (including currency risk, fair value and interest rate risk), credit risk and liquidity risk.

The Group does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

(a) Capital risk management

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. The Group's overall strategy remains unchanged from year 2008.

The capital structure of the Group consists of debt, which includes the borrowings disclosed in notes 20 and 22, cash and cash equivalents disclosed in note 12, equity attributable to equity holders of the parent, comprising issued capital, reserves and accumulated losses as disclosed in notes 23, 24 and 25 respectively. The Group operates in Australia, France, China and South East Asia, primarily through subsidiary companies and a jointly controlled entity established in the markets in which the Group trades. None of the Group's entities are subject to externally imposed capital requirements.

Operating cash flows are used to maintain and expand the Group's manufacturing and distribution assets, as well as to make the routine outflows of repayment of maturing debt and interest. The Group's policy is to borrow centrally, using a variety of borrowing facilities, to meet anticipated funding requirements.

Gearing ratio

The Directors review the capital structure on an ongoing basis. As a part of this review the Directors consider the cost of capital and the risks associated with each class of capital. A gearing ratio is expected as the Group is in its development stage and more debts are required to fund the operation and development activities.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
<u>Financial assets</u>				
Debt (i)	8,821,580	5,041,870	8,821,580	5,041,870
Cash and cash equivalents	(279,955)	(169,476)	(265,750)	(93,769)
Net debt	8,541,625	4,872,394	8,555,830	4,948,101
Equity (ii)	(1,104,191)	694,233	(1,384,317)	630,215
Net debt to equity ratio	707%	726%	564%	800%

(i) Debt is defined as long term and short term borrowings, as detailed in notes 20 and 22.

(ii) Equity includes all capital and reserves.

(b) Categories of financial instruments

	AEC Group		AEC Entity	
	2009	2008	2009	2008
	\$	\$	\$	\$
<u>Financial assets</u>				
Loans and receivables	4,199,320	2,062,056	4,324,043	2,689,082
Cash and cash equivalents	279,955	164,476	265,750	93,769
<u>Financial liabilities</u>				
Borrowings	8,821,580	5,041,870	8,821,580	5,041,870

The carrying amount reflected above represents the Company's and the Group's maximum exposure to credit risk for such loans and receivables.

(c) Market risk

(i) Foreign currency

The Group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates as set below and interest rates (refer note (d)(ii)). At a company level, market risks are managed through sensitivity analysis.

There has been no change to the Group's exposure to market risks or the manner in which it manages and measures the risk from the previous period.

The Group undertakes certain transactions denominated in foreign currencies, hence exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters.

The Group's core operations are located in China where both revenues and expenses are recorded. Foreign exchange risks arise from commercial transactions and recognised assets and liabilities denominated in a currency that is not the entity's functional currency. Foreign currency exposure is mitigated by translating in an entity's functional currency.

The Group is mainly exposed to USD and EURO. RMB exposure arises from translation of China operation in AUD.

No Group foreign currency sensitivity analysis is disclosed as foreign currency risk is not considered to have a material impact on profit / loss or equity for both years 2008 and 2009.

(ii) Interest rate risk management

The Company and the Group are not exposed to interest rate risk as entities in the Group borrow funds at fixed interest rate only. The risk is managed by the Group by maintaining borrowings with fixed interest rate by ensuring the interest rates are below or close to the market interest rate. In addition, the Group maintains its fixed interest rate borrowings with interest rates consistent with the market interest risk in order to minimise the interest rate risk for the Group.

The Company and the Group's exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section (e).

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(iii) Cash flow interest rate risk

The Group's main interest rate risk arises from short-term and long-term borrowings. The Company and the Group are however exposed to interest rate risk due to variable interest earned on its bank accounts. Group policy is to maintain 100% of its borrowings at fixed rate. Accordingly the Company and the Group are not exposed to interest rate risk.

Interest rate sensitivity analysis

The sensitivity analyses have been determined based on the exposure to interest rates for non-derivative instruments at the reporting date and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period. A 50 basis point increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the possible change in interest rates.

No Group interest rate sensitivity analysis is disclosed as interest rate risk is not considered to have a material impact on profit / loss or equity for both years 2008 and 2009.

(d) Credit risk management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral where appropriate, as a means of mitigating the risk of financial loss from defaults. The Group only transacts with entities with established relationships and known repayment history. The Group's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties.

Trade receivables consist of a number of customers spread across diverse geographical areas. Ongoing credit evaluation is performed on the financial condition of accounts receivable.

The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The credit risk on liquid funds is limited because the counterparties are all with established relationships and 30% deposit is required for new customers.

The carrying amount of financial assets recorded in the financial statements, net of any allowance for losses, represents the Group's maximum exposure to credit risk without taking account of the value of any collateral obtained.

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates:

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
Trade receivables				
Counterparties without external credit ratings*				
Group 1	6,757	34,807	5,457	20,107
Group 2	1,620,743	1,717,554	393,930	124,149
Group 3	1,591,130	188,259	2,951,720	2,518,291
Total trade receivables	3,218,630	1,940,620	3,351,107	2,662,547
Cash at bank and short term deposits				
A-	4,045	61,119	-	-
AA	263,750	91,769	263,750	91,769
Deposits with suppliers (rating not available)	7,668	12,607	-	-
Total cash at bank	275,463	165,495	263,750	91,769

* Group 1 – new customers (less than 6 months)

Group 2 – existing customers (more than 6 months) with no defaults in the past

Group 3 – existing customers (more than 6 months) with some defaults in the past. All defaults were fully recovered.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(e) Liquidity risk management

Ultimate responsibility for liquidity risk management rests with the Board of Directors, who have built an appropriate liquidity risk management framework for the management of the Group's short, medium and long-term funding and liquidity management requirements. The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

Liquidity and interest risk tables

The following tables detail the Company's and the Group's remaining contractual maturity for its non-derivative financial liabilities. The tables have been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

	Weighted Average Interest Rate %	<6 months \$	>6 - 12 months \$	1 - 2 years \$	2 - 5 years \$	5+ years \$
AEC Group 2009						
Financial assets						
Non-interest bearing	-	2,150,792	2,078,232	-	-	-
Cash	1.79	279,955	-	-	-	-
Financial liabilities						
Non-interest bearing	-	1,392,618	529,236	-	-	-
Insurance finance	3.51	3,427	131,495	-	-	-
Loan – 698 Capital	12.43	4,083,014	-	-	-	-
Loan – Syndicate / CIM SSF	15.00	56,712	786,986	-	-	-
Convertible note	7.57	3,114,483	-	-	-	-
Loan from Norvest Corporate Pty Ltd	15.00	46,417	-	-	-	-
Commercial loan	8.50	1,066	31,536	-	-	-
		11,128,484	3,557,485	-	-	-

	Weighted Average Interest Rate %	<6 months \$	>6 - 12 months \$	1 - 2 years \$	2 - 5 years \$	5+ years \$
AEC Group 2008						
Financial assets						
Non-interest bearing	-	1,680,956	259,664	-	-	-
Cash	3.10	169,476	-	-	-	-
Financial liabilities						
Non-interest bearing	-	355,500	262,646	-	-	-
Insurance finance	3.40	5,154	254,817	-	-	-
Loan – 698 Capital	9.00	300,308	799,897	-	-	-
Loan – CIM SSF	9.00	778,767	-	-	-	-
Convertible note	7.57	114,483	113,239	3,114,483	-	-
Commercial loan	8.50	2,311	1,672	111,411	-	-
		3,406,955	1,691,935	3,225,894	-	-

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

AEC Entity 2009	Weighted Average Interest Rate %	<6 months \$	>6 - 12 months \$	1 - 2 years \$	2 - 5 years \$	5+ years \$
Financial assets						
Non-interest bearing	-	990,961	1,554,960	1,815,578	695,155	-
Cash	1.79	265,750	-	-	-	-
Financial liabilities						
Non-interest bearing	-	1,456,407	446,041	21,638	1,915	-
Insurance finance	3.51	3,427	131,495	-	-	-
Loan – 698 Capital	12.43	4,083,014	-	-	-	-
Loan – Syndicate / CIM SSF	15.00	56,712	786,986	-	-	-
Convertible note	7.57	3,114,483	-	-	-	-
Loan from Norvest Corporate Pty Ltd	15.00	46,417	-	-	-	-
Commercial loan	8.50	1,066	31,536	-	-	-
		10,018,237	2,951,018	1,837,216	697,070	-

AEC Entity 2008	Weighted Average Interest Rate %	<6 months \$	>6 - 12 months \$	1 - 2 years \$	2 - 5 years \$	5+ years \$
Financial assets						
Non-interest bearing	-	811,096	1,851,451	794,808	-	-
Cash	3.10	93,769	-	-	-	-
Financial liabilities						
Non-interest bearing	-	330,467	282,378	-	-	-
Insurance finance	3.40	5,154	254,817	-	-	-
Loan – 698 Capital	9.00	300,308	799,897	-	-	-
Loan – CIM SSF	9.00	778,767	-	-	-	-
Convertible note	7.57	114,483	113,239	3,114,483	-	-
Commercial loan	8.50	2,311	1,672	111,411	-	-
		2,436,355	3,303,454	4,020,702		-

The Company's and the Group's financial assets and liabilities that are recorded on the balance sheet are carried at amounts that approximate net fair values.

Valuation approach

Net fair values of financial assets and liabilities are determined by the Group on the following basis:

Cash, cash equivalents: The carrying amount approximates fair value because of their short-term to maturity.

Receivables and payables: The carrying amount approximates fair value.

Short term borrowings: The carrying amount approximates fair value because of their short- term to maturity.

Long-term borrowings: The fair value of long-term loans receivable approximates the carrying amount as they are in fixed interest rates.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

30. Related Party Disclosure

Transactions and balances with Key Management Personnel

Directors

Mr. Graham Keys

Mr. Keys is a Director and the major Shareholder of Norvest Corporate Pty Limited, which provides various corporate, capital raising, accounting, management and company secretarial services to the Company at normal commercial rates. During the year Norvest Corporate Pty Limited supplied these services to the Company to the value of \$286,088 (2008: \$193,388). As at 30 June 2008, the Company owed Norvest Corporate Pty Ltd \$234,733 (2008: \$183,363), this amount is reflected in payables and is non interest bearing.

During the year, Norvest Corporate Pty Limited made various unsecured loans to the Company with a maximum outstanding at any point in time of \$300,000 (2008: \$110,000). At 30 June 2009 the amount outstanding was \$46,361 (2008: nil). Interest of 15%pa was payable on the daily outstanding balance.

In April 2009, Norvest Corporate Pty Ltd facilitated refinancing of the CIM SSF \$750,000 loan through a syndicate of investors. Mr. Keys, through his private company Seibu Pty Ltd ATF G L Keys FT, provided \$315,000 of the funding. Pursuant to the terms of the refinancing, and shareholder approval granted on 3 July 2009, Seibu Pty Ltd is entitled to receive interest of 15%pa, calculated on the outstanding daily loan balance, and up to 4,117,000 options. 1,000 options are to be issued each month for every \$1,000 outstanding, with an exercise price calculated on the preceding months VWAP and an expiry date of 30 November 2011.

During the current year, the Company accrued directors fees of \$25,000 (2008: \$25,000) payable to Mr. Keys. At 30 June 2009 an amount of \$25,000 (2008: \$25,000) remained payable.

Mr. Antony Middleton

Mr. Middleton, through his private company Jildane Pty Ltd ATF Middleton Super Fund, provided \$30,000 of the syndicate funding to refinance the CIM SSF \$750,000 loan. Pursuant to the terms of the refinancing, and shareholder approval granted on 3 July 2009, Jildane Pty Ltd is entitled to receive interest of 15%pa, calculated on the outstanding daily loan balance, and up to 368,000 options. 1,000 options are to be issued each month for every \$1,000 outstanding, with an exercise price calculated on the preceding months volume weighted average share price and an expiry date of 30 November 2011.

Mr. Pun

Mr. Pun is a Director of AEC's major Shareholder 698 Capital International Ltd and its related entities ("698 Capital"). In August 2008, 698 Capital agreed to provide AEC with a \$2 million sales financing facility. Interest is charged at the National Australia Bank Indicator rate at the time of execution of the agreement together with a \$17,500 facility fee. As AEC shareholders agreed to the issue of 5 million options, exercisable at 20 cents on or before 31 December 2010, the interest rate was reduced by 0.75%.

698 Capital subsequently agreed to increase the sales financing facility to \$3 million. As part consideration for the increase AEC has agreed, subject to shareholder approval at the 2009 Annual General Meeting, to issue 698 Capital with a further 6 million options. The new options will be allocated in monthly instalments of 1 million options up to a maximum of 6 million. In the event the Company makes a prepayment of the facility, the number of options to be issued will be reduced accordingly. The exercise price of the options is calculated on the preceding months volume weighted average share price with an expiry date of 30 November 2011.

698 Capital provided \$375,000 of the syndicate funding to refinance the CIM SSF \$750,000 loan. Pursuant to the terms of the refinancing, and shareholder approval granted on 3 July 2009, 698 Capital is entitled to receive interest of 15%pa, calculated on the outstanding daily loan balance, and up to 4,875,000 options. 1,000 options are to be issued each month for every \$1,000 outstanding, with an exercise price calculated on the preceding months volume weighted average share price and an expiry date of 30 November 2011.

Subsidiaries

The following table provides the total amount of transactions that were entered into with subsidiaries for the relevant financial years:

Year ended 30 June 2009

AEC Entity	Sales to subsidiaries	Loan to subsidiaries (i)	Purchases from subsidiaries	Amounts owed by subsidiaries
AEC China Limited	\$1,866,695	\$495,417	\$65,596	\$3,474,907
AEC China Holdings Limited	-	\$199,738	-	-

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

Year ended 30 June 2008

AEC Entity	Sales to subsidiaries	Loan to subsidiaries (i)	Purchases from subsidiaries	Amounts owed by subsidiaries
AEC China Limited	\$1,504,090	\$595,070	\$80,348	\$2,330,105
AEC China Holdings Limited	-	\$199,738	-	-

(i) The possibility of non collection of AEC loans to subsidiaries was fully provided for in the 30 June 2009 and 2008 financial statements.

Other balances with related parties

During the year 698 Capital Asia Pacific Limited, a related entity, advanced the Company an additional \$2,667,000 (2008: \$1,250,000) and was repaid \$250,000 (2008: \$1,000,000). A further \$333,000 has been drawn down subsequent to 30 June 2009. At year-end the 698 Capital Asia Pacific Limited outstanding loans to AEC, including accrued interest, stood at \$3,864,065 (2008: \$1,045,479), refer to note 20. The loan is at call.

Terms of the \$3,000,000 (2008: \$3,000,000) convertible note held by 698 Capital Asia Pacific Limited are set out in notes 20 and 23(b). At the 30 June 2009, the outstanding balance of the convertible note, including accrued interest, was \$4,095,982 (2008: \$3,837,202).

All loan, sales and purchase transactions with related parties are made in arm's length transactions on normal commercial terms. Other than as set out in note 20 all related party loan balances are unsecured, interest free and settlement occurs in cash.

698 Capital International Limited have resolved to provide financial support, in circumstances that will enable the Company to be able to meet its debts as and when they fall due, at least until one year from signature of the Directors' Declaration. This support is subject to 698 Capital International Limited remaining the majority shareholder of the Company.

During the year the Company facilitated a US\$700,000 loan from an unrelated company, CCM Global Limited, to the Thailand joint venture company, Monika AEC Limited. The monies were paid directly to Monika AEC Limited and did not involve cash flow through AEC. The Company has recorded an asset (note 13) and liability (note 20) of US\$700,000 (A\$1,010,393). The loan facilitated Monika AEC Limited's acquisition of natural gas engines for the Thailand market. The loan is unsecured, other than a covenant that priority will be given for all monies received on sale of the engines to first be directed to repayment of the US\$700,000 loan. The Company's repayment of the CCM Global Limited loan is limited recourse to funds the Company receives from repayment of the AEC loan to Monika AEC Limited. The Company received a fee for facilitating the loan and receives a margin on the interest due and payable. .

31. Key Management Personnel Disclosures

(a) Directors

The following persons were Directors of the Company during the financial year:

(i) Chairman – Non-executive

Mr. G Keys

(ii) Executive Directors

Mr. A Middleton

(iii) Non-Executive Directors

Mr. A Pun

Mr. A Chan (appointed 28 May 2009)

Mr. T Liu (resigned 28 May 2009)

(b) Other Key Management Personnel

The following persons also had authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, during the financial year:

<u>Name</u>	<u>Position</u>	<u>Employer</u>
Mr. B Neumann	Engine Development Manager	Advanced Engine Components Limited
Mr. N McLaren	Electronics Division Manager	Advanced Engine Components Limited
Mr. M McKay	Senior Mechanical Engineer	Advanced Engine Components Limited
Mr. D Wang	General Manager	AEC China Ltd

All of the above persons were also key management persons during the year ended 30 June 2008.

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

(c) Key Management Personnel Compensation

	AEC Group		AEC Entity	
	2009 \$	2008 \$	2009 \$	2008 \$
Short-term employee benefits	663,928	568,386	484,071	444,573
Post-employment benefits	161,547	168,950	161,547	168,950
Share-based payments	8,718	52,010	8,718	52,010
	<u>834,193</u>	<u>789,356</u>	<u>654,336</u>	<u>665,533</u>

Detailed remuneration disclosures are provided in sections (b), to (g) of the remuneration report on pages 11 to 14.

Other than as disclosed in Related Party Disclosure (note 30) no director or executive of the Company has entered into a material contract with the Company or Group since the end of the previous financial year and no material contracts exist at year end.

(d) Equity Instruments Disclosures Relating to Key Management Personnel

(i) Options provided as remuneration and shares issued on exercise of such options

Details of options provided as remuneration and shares issued on the exercise of such options, together with terms and conditions of the options, can be found below and section(d), (e) and (f) of the remuneration report.

(ii) Option holdings

Details of options held directly, indirectly or beneficially by Directors and key management personnel including their related parties are as follows:

Parent Entity		Opening Balance	Granted as remuneration	Options Exercised	Net Change Other	Closing Balance	Total Vested and Exercisable as at Year End	Unvested as at Year End
Directors								
Mr. G Keys	2009	144,298	275,000	-	-	419,298	419,298	-
	2008	1,450,000	-	-	(1,305,702)	144,298	144,298	-
Mr. A Middleton	2009	540,649	-	-	-	540,649	540,649	-
	2008	-	400,000	-	140,649	540,649	540,649	-
Mr. A Pun*	2009	4,258,153	-	-	5,000,000	9,258,153	9,258,153	-
	2008	-	-	-	4,258,153	4,258,153	4,258,153	-
Mr. A Chan**	2009	-	-	-	-	-	-	-
	2008	-	-	-	-	-	-	-
Mr. T Liu ***	2009	-	-	-	-	-	-	-
	2008	-	-	-	-	-	-	-
Mr. W Lee ****	2009	-	-	-	-	-	-	-
	2008	-	-	-	-	-	-	-
Total	2009	4,943,100	275,000	-	5,000,000	11,118,100	11,118,800	-
	2008	1,450,000	400,000	-	3,093,100	4,943,100	4,943,100	-

* Options held by 698 Capital International Limited and related entities

** Appointed 28 May 2009

*** Resigned 28 May 2009

**** Resigned 10 September 2007

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

Parent Entity Key Management Personnel		Opening Balance	Granted as remuneration	Options Exercised	Net Change Other	Closing Balance	Total Vested and Exercisable as at Year End	Unvested as at Year End
Mr. B Neumann #	2009	117,639	-	-	-	117,639	117,639	-
	2008	155,00	100,000	-	(137,361)	117,639	117,639	-
Mr. McLaren	2009	106,389	-	-	-	106,389	106,389	-
	2008	-	100,000	-	6,389	106,389	106,389	-
Mr. D Wang	2009	100,000	-	-	(100,000)	-	-	-
	2008	100,000	-	-	-	100,000	100,000	-
Mr. M McKay	2009	100,000	-	-	-	100,000	100,000	-
	2008	-	100,000	-	-	100,000	100,000	-
Total	2009	424,028	-	-	(100,000)	324,028	324,028	-
	2008	255,000	300,000	-	130,972	424,028	424,028	-

In 2008, Mr. B Neumann held 155,000 options at 20 cents which lapsed on 30 June 2008 and acquired 17,639 under the right issue

(iii) Share holdings

The number of shares in the Company held by Directors and other key management personnel of the Group, including their related parties, during the financial year were as follows:

		Opening Balance #	Received During Year on Exercise of Options #	Net Change Other #	Closing Balance #
Parent Entity Directors and Related Parties					
Mr. G Keys (i)	2009	3,401,017	-	298,983	3,700,000
	2008	2,597,334	-	803,683	3,401,017
Mr. A Middleton (i)	2009	3,562,947	-	-	3,562,947
	2008	3,181,651	-	381,296	3,562,947
Mr. A Pun (ii)	2009	250,000	-	-	250,000
	2008	-	-	250,000	250,000
Mr. A Chan (iii)	2009	-	-	-	-
	2008	-	-	-	-
Mr. T Liu (iv)	2009	-	-	-	-
	2008	-	-	-	-
Mr. W Lee (v)	2009	-	-	-	-
	2008	-	-	-	-
Other Key Management Personnel					
Mr. B Neumann	2009	644,778	-	-	644,778
	2008	459,500	-	185,278	644,778
Mr. N McLaren	2009	127,778	-	-	127,778
	2008	60,000	-	67,778	127,778
Mr. M McKay	2009	110,000	-	-	110,000
	2008	-	-	110,000	110,000
Mr. D Wang	2009	-	-	-	-
	2008	-	-	-	-

Notes to the Financial Statements for the Financial Year Ended 30 June 2009

- (i) These shares are held nominally.
- (ii) Mr. A Pun was appointed a director of 698 Capital International Limited which owns 64,423,731 shares in the company (2008: 64,423,731), on 20 August 2007.
- (iii) Mr. A Chan was appointed a director of AEC on 28 May 2009.
- (iv) Mr. Liu resigned as a director of AEC on 28 May 2009. Mr. Liu was a director of 698 Capital International Limited until his resignation as a director of that company on 20 August 2007.
- (v) Mr. Lee resigned as a director of AEC on 10 September 2007. Mr. Lee was a director of 698 Capital International Limited until his resignation as a director of that company on 20 August 2007.

(e) Loans to Key Management Personnel

There were no loans made to the Directors of the Company or other key management personnel of the Group, including their related parties during the financial year (2008: nil).

(f) Other Transactions with Key Management Personnel

All other transactions with key management personnel are set out in note 31.

32. Contingencies

There were no contingent liabilities at 30 June 2009 (2008: Nil).

33. After Balance Sheet Date Events

On 3 July 2009 shareholders approved the issue of up to 9.75 million options in tranches of 0.75 million per month commencing as of 30 April 2009. The options, part of refinancing of the CIM SSF \$750,000 loan facility, are exercisable on or before 30 November 2011. The exercise price of each option will be determined each month based on the previous calendar month's volume weighted average price of ACE shares. 60,000 of these options were issued prior to 30 June 2009 and a further 3.75 million have been issued to the date of this report.

Subsequent to year end the Company has received, less taxation consultant fees, \$325,000 for the 2008 R&D tax concession offset rebate. The Company will receive a similar amount for the 2009 R&D tax rebate prior to 31 December 2009.

Subsequent to year end the Company has drawn down the remaining \$330,000 balance of the 698 Capital Asia Pacific Ltd \$3,000,000 sales finance facility.

Apart from the above, there are no other matters or circumstances that have arisen since 30 June 2009 that have or may significantly affect the operations, results, or state of affairs of the Group in the future financial years.

Directors' Declaration

In accordance with a resolution of directors of Advanced Engine Components Limited, I state that

In the opinion of the Directors:

- (a) the financial report and notes of the Company and of the consolidated entity are in accordance with the Corporations Act 2001, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2009 and of their performance for the year ended on that date; and
 - (ii) complying with Accounting Standards and the Corporations Regulations 2001;
- (b) the remuneration disclosures set out in the directors report (as part of the Audited Remuneration Report), for the year ended 30 June 2009, comply with Section 300A of the Corporations Act 2001.; and
- (c) 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 ended 30 June 2009.

On behalf of the Board



A Middleton
Managing Director

Perth, 30 September 2009



INDEPENDENT AUDITOR'S REPORT

To the members of Advanced Engine Components Limited

Report on the Financial Report

We have audited the accompanying financial report of Advanced Engine Components Limited, which comprises the balance sheet as at 30 June 2009, and the income statement, statement of changes in equity and cash flow statement for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration of the consolidated entity comprising the and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 2, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

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

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001* would be in the same terms if it had been given to the directors at the time that this auditor's report was made.



Auditor's Opinion

In our opinion:

- (a) the financial report of Advanced Engine Components Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2009 and of their performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*; and
- (b) the financial report also complies with International Financial Reporting Standards as disclosed in Note 2.

Material Uncertainty Regarding Continuation as a Going Concern

We draw attention to Note 6 in the financial report which indicates as at 30 June 2009 the consolidated entity had a net asset deficiency of \$1,104,191. This condition, along with other matters as set forth in Note 6, indicate the existence of a material uncertainty which may cast significant doubt about the entity's ability to continue as a going concern and therefore whether it will realise its assets and settle its liabilities in the normal course of business and at the amounts stated in the financial report.

Material Uncertainty Regarding Recoverability of Trade Receivables

Without qualification to the opinion expressed above, attention is drawn to the recoverability of the consolidated entity's trade receivables as disclosed in Note 13 (iv) owing from Weichai Peterson Gas Engine Co. Ltd. The recoverability of the trade receivables is dependent upon the directors being able to successfully negotiate the repayment of the debt. Should the company not be successful, uncertainty exists which may cast doubt about the recoverability of this receivable at the value recorded in the balance sheet.

Report on the Remuneration Report

We have audited the Remuneration Report included in the directors' report for the year ended 30 June 2009. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion, the Remuneration Report of Advanced Engine Components Limited for the year ended 30 June 2009, complies with section 300A of the *Corporations Act 2001*.

BDO Kendalls Audit & Assurance (WA) Pty Ltd

BDO Kendalls

Peter Toll
Director

Signed in Perth, Western Australia
Dated this 30th day of September 2009

Additional Stock Exchange Information

as at 15 September 2009

Number of Holders of Equity Securities

Ordinary Share Capital

149,058,116 shares are held by 944 individual holders.

Options

For details of options on issue refer note 23(c).

Distribution of Holders of Equity Securities

			Fully Paid Ordinary Shares		
			Holders	Total Units	%
1	-	1,000	60	19,199	0.01
1,001	-	5,000	146	487,742	0.33
5,001	-	10,000	133	1,064,701	0.71
10,001	-	100,000	485	16,923,205	11.36
100,001 and over			113	130,563,269	87.59
Totals			937	149,058,116	100.00

Substantial Shareholders

<i>Ordinary Shareholders</i>	<i>Fully Paid</i>	
	Number	Percentage
698 Capital International Ltd	64,423,731	43.59
HSBC Custody Nominees (Australia) Limited	20,768,529	13.93
LIM Asia Multi Strategy Fund Inc	14,745,000	9.98

Twenty Largest Holders of Quoted Equity Securities

		<i>Fully Paid</i>	
<i>Ordinary Shareholders</i>		Number	Percentage
1	698 Capital International Ltd	64,423,731	43.59
2	HSBC Custody Nominees (Australia) Limited	20,768,529	13.93
3	Seibu Pty Ltd GL Keys Super Fund Account	3,700,000	2.48
4	Mr. Mark John Conway	2,026,575	1.38
5	ANZ Nominees Limited <Cash Income A/C>	2,026,575	1.36
6	Jildane Pty Ltd <Middleton Super Fund A/C>	1,568,502	1.05
7	Jildane Pty Ltd <Middleton Super Fund A/C>	1,338,889	0.90
8	H L Fry Holdings Pty Ltd	1,200,000	0.81
9	Jingie Investments Pty Ltd	1,200,000	0.81
10	Mr. Vivekanathan	1,125,000	0.75
11	Mr. Paul Massarotto	1,105,455	0.74
12	Rodney Ralph Gregory and Philip Geoffrey Gregory	1,017,000	0.68
13	Mr. Paul Robert Baster <Baster Family A/C>	1,000,000	0.67
14	M Squared Nominees Pty Ltd	960,000	0.64
15	Mr. Boyd Stewart Milligan	948,418	0.64
16	Mr. Robert Bruce Thompson and Mr.s Lorraine Florence Thompson	830,000	0.56
17	Jowene Pty Ltd <Citer Family A/C>	794,736	0.53
18	Mr. Michael John Steer	773,668	0.52
19	Mr. Allan Graham Jenzen & Mr.s Elizabeth Jenzen <A&E Jenzen P/L No.2 S/F A/C>	750,000	0.50
20	Jildane Pty Ltd <Middleton Super Fund A/C>	655,556	0.44
		108,238,595	72.61

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