TISSUE THERAPIES

ASX ANNOUNCEMENT

03 August 2006

Tissue Therapies' On Track for Commercial Development

Biomedical company, **Tissue Therapies Limited (ASX: TIS)** made substantial progress during 2005/06 in the race to develop its groundbreaking VitroGro® wound healing technology for commercial use.

Tissue Therapies' Chief Executive Officer, Dr Steven Mercer, said "The considerable achievements we have accomplished in the past 12 months provide an excellent foundation for the significant milestones we are confident of achieving by December 2007, in particular:

- Completion of a clinical trial of VitroGro® for scarless burn healing and regulatory approval for VitroGro®
- Start of clinical trials of VitroGro® to treat venous and diabetic ulcers in 2007
- Conclusion of negotiations for an international supply agreement to provide VitroGro® for scientific research. This has been enhanced by the ability of VitroGro® to replace animal and human serum for the culture of embryonic stem cells; a world first. The culture of stem cells is one of the fastest growing areas of biological science and the unique ability of VitroGro® to replace all human and animal growth promoters provides Tissue Therapies with a considerable commercial advantage."

"Our research developments are also showing encouraging data for potential new formulations of VitroGro® as well as new manufacturing techniques that we hope to announce in the coming months. I am very confident that during the next 12 months we will announce a number of exciting and significant developments and achievements", Dr Mercer said.

Tissue Therapies finished the year in a strong cash position with net assets up by $1.4 million, following two successful capital raisings totalling $5.2 million and cash resources of $3.9 million at 30 June 2006.

The Company recorded an after-tax loss of $1.86 million, in line with budget expectations.

The Company placed 2.3 million shares at $0.70 to raise $1.6 million in November, followed by the issue of 2.4 million shares under its Share Purchase Plan, raising $1.7 million in December 2005.

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Tissue Therapies Limited ABN 45 101 955 088 www.tissuetherapies.com
Level 25 Waterfront Place, 1 Eagle Street, GPO Box 1596 Brisbane Qld 4001
telephone 07 3221 0140 facsimile 07 3220 1482

Dr Mercer, said the Company had achieved a number of major milestones during the year, including:

- Breakthrough research results in May 2006 demonstrating that Tissue Therapies' VitroGro® technology could be used to replace animal and human serum in the culture of human embryonic stem cells - a major milestone in the race to use human embryonic stem cells for medical treatments and removed one of the most significant obstacles to approved use of stem cell therapies.

- Confirmation that Tissue Therapies' VitroGro® could be developed as a treatment to accelerate healing of diabetic ulcers, with the potential to dramatically reduce the number of amputations due to complications associated with the poor healing of ulcers. A clinical trial of VitroGro® to treat diabetic and venous ulcers is planned for 2007.

- Negotiations progressed significantly with major international biological supply companies to secure long term product pipeline and supply arrangements for VitroGro® products in key research and industrial cell culture markets.

- Development of an advanced manufacturing method to produce VitroGro® in a powdered form using freeze-drying, to enable cheaper, faster and more flexible distribution to global markets.

- Creation of a human live skin model for simulating skin injuries and healing, and for testing cosmetics and cosmeceuticals. This has the potential to replace animal testing and basic human testing for a range of applications, including skin wound healing treatments, cosmetics and cosmeceuticals. The skin model is also a practical demonstration of the power and versatility of VitroGro® and provides an immensely valuable research tool for the further development of VitroGro®.

- The second of the family of the VitroGro® world-wide patents was granted by New Zealand in March 2006.

- Tissue Therapies' Chief Scientific Officer, Prof. Zee Upton was awarded a three year, $100,000 per annum Smart State Senior Fellowship for her research into wound repair and skin regeneration. The Fellowship will allow Prof. Upton to focus on an accelerated commercial development program for VitroGro®.

- Completion of a second animal trial at the Royal Children's Hospital in Brisbane to gather VitroGro® dosage data for human trials. Due to anomalies in the trial results caused by an inactive ingredient, the Company will complete the repeat study late in 2006 to determine optimal doses for the VitroGro® human trial planned for early 2007.

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Tissue Therapies' Annual General Meeting has been scheduled for 10.30am, 9 November 2006, in the Seminar Room;

4th floor, Q Block
Institute of Health & Biomedical Innovation (IHBI)
Queensland University of Technology,
Cnr Musk Ave and Blamey St
Kelvin Grove QLD 4059

ENDS

Further information or for an interview:

Dr Steven Mercer
CEO, Tissue Therapies Limited
Telephone: (07) 3221 0140
Email: s.mercer@tissuetherapies.com

About Tissue Therapies Limited

Tissue Therapies Limited is an Australian company developing biomedical technologies for wound healing, tissue and various cell culture applications.

The Company has worldwide exclusive rights to commercialise VitroGro®, a platform technology developed by tissue engineering experts at Queensland University of Technology for enhancing cell growth and migration. VitroGro® has particular commercial applications in wound healing, tissue regeneration and cell culture, including adult and embryonic stem cells.

Based on its VitroGro® platform technology, Tissue Therapies is developing more effective medical treatments for wounds and burns, integration of orthopaedic and medical implants, and other applications such as cosmeceuticals.

Tissue Therapies also provides cell culture reagents to enhance the growth of mammalian cells for emerging cell-based therapies including the development of human stem cell treatments, along with research and industrial cell culture markets internationally.

More information: www.tissuetherapies.com

Appendix 4E

Preliminary Final Report to the Australian Stock Exchange

Name of Entity	**Tissue Therapies Limited**
ABN	45 101 955 088
Financial Year Ended	30 June 2006
Previous Corresponding Reporting Period	30 June 2005

Results for Announcement to the Market

	$	**$ Movement over previous corresponding period**	**Percentage increase /(decrease) over previous corresponding period**
Revenue from ordinary activities	239,315	(147,662)	(38.15%)
Profit / (loss) from ordinary activities after tax attributable to members	(1,861,242)	(934,395)	100.81%
Net profit / (loss) for the period attributable to members	(1,861,242)	(934,395)	100.81%

Dividends (distributions)	-	Franked amount per security
Final Dividend	-	-
Interim Dividend	-	-
Record date for determining entitlements to the dividends (if any)	-	

Brief explanation of any of the figures reported above necessary to enable the figures to be understood:

Refer to the accompanying director's report, financial statements and notes.

Ratios

	Current period	Previous corresponding period
Profit/(loss) before tax / revenue Profit (loss) from ordinary activities before tax as a percentage of revenue	(909.7)%	(302.4)%
Profit after tax / equity interests Net profit (loss) from ordinary activities after tax attributable to members as a percentage of equity (similarly attributable) at the end of the period	(35.61)%	(24.20)%

NTA Backing

	Current Period	Previous corresponding period
Net tangible asset backing per ordinary security	24.18 cents	22.56 cents

Commentary on the Results for the Period

Refer to the accompanying director's report, financial statements and notes.

Audit/Review Status

This report is based on accounts to which one of the following applies: (Tick one)			
The accounts have been have been audited and the audit report contains no qualifications	X	The accounts have been subject to review	
The accounts are in the process of being audited or subject to review		The accounts have not yet been audited or reviewed	

Financial Statements

Refer to the accompanying director's report, financial statements and notes.

By Order of the Board
Gregory Baynton
Director
3rd August 2006

DIRECTORS' REPORT

Your Directors present their report on Tissue Therapies Limited (the Company) for the year ended 30 June 2006.

DIRECTORS

The names of Directors at any time during or since the end of the year, and their qualifications are detailed below:

Roger Clarke – Chairman *(appointed 6 November 2003)*

Qualifications	—	*Bachelor of Commerce* *Chartered Accountant*
Experience	—	*Chairman of Board of Advice, ABN AMRO Morgans Limited* *Chairman of White Sands Petroleum Ltd* *Director of MTQ Insurance Ltd , PIPE Networks Limited and Trojan Equities Limited*
Special Responsibilities	—	*Member of the Audit Committee*
Interest in Shares and Options	—	*200,000 Ordinary Shares and options to acquire a further 150,000 ordinary shares*

Professor David Gardiner - Director *(appointed 12 November, 2003)*

Qualifications	—	*Barrister at Law*
Experience	—	*Deputy-Vice Chancellor of QUT* *Professor of Law, QUT* *Director of several R & D and commercialisation companies, including biotechnology company, Farmacule BioIndustries Pty Ltd*
Interest in Shares and Options	—	*2,255,000 Ordinary Shares and options to acquire a further 100,000 ordinary shares are held by QUT, which is a related entity of Professor David Gardiner*

Gregory Baynton – Executive Director *(appointed 6 September 2002)*

Qualifications	—	*Master of Economic Studies* *Post Graduate Diploma in Applied Finance and Investment* *Bachelor of Business* *Fellow of the Australian Institute of Company Directors* *Associate of the Financial Services Institute of Australia*
Experience	—	*Director of Lodestone Exploration Limited and PIPE Networks Limited* *Director of three Australian biotechnology companies*
Special Responsibilities	—	*Member of the Audit Committee*
Interest in Shares and Options	—	*520,000 Ordinary Shares and options to acquire a further 600,000 ordinary shares are held by Orbit Capital, which is a related entity of Gregory Baynton*

Neil Reinhardt – Director *(appointed 8 May 2003)*

Qualifications	—	*Registered Pharmacist*
Experience	—	*Director of a number of private companies in the areas of manufacturing, health care, and investments*
Special Responsibilities	—	*Chairman of the Audit Committee*
Interest in Shares and Options	—	*260,000 Ordinary Shares and options to acquire a further 100,000 ordinary shares*

Steven Mercer – Chief Executive Officer and Executive Director (appointed 10 May 2006)

Qualifications	—	*Bachelor of Medical Science, Bachelor of Medicine, Bachelor of Surgery, Fellow of the Australian Institute of Management, Fellow of the Australian Institute of Company Directors, Registered Medical Practitioner (Australia and USA).*
Experience	—	*Significant medical and commercial experience, most recently as Managing Director of Mercy Tissue Engineering, a successful tissue engineering company. Significant international expertise to Tissue Therapies following a successful career with multinational companies, including six years with Smith & Nephew as General Manager, Smith & Nephew Surgical and seven years with IBM Health Industry Centre in Australia and New York.*
Special Responsibilities	—	*Chief Executive Officer, and appointed Executive Director on 10 May 2006.*
Interest in Shares and Options	—	*69,379 Ordinary Shares and options to acquire a further 500,000 ordinary shares*

Information on Company Secretary:

Drummond McKenzie – Company Secretary

Qualifications	—	*Bachelor of Science (Economics) Honours* *Chartered Accountant* *Fellow of the Institute of Chartered Secretaries*
Experience	—	*Over 10 years experience in the financial management and administration of public companies*

Principal activities

During the year the principal activities of the Company consisted of the research, development and commercialisation of the Company's exclusive international intellectual property in wound healing and tissue regeneration.

Operating results

The loss of the Company after tax amounted to $1,861,242 (2005: loss $926,847).

Dividends

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

Review of operations

During the 2005-06 financial year:

- Tissue Therapies recorded an after-tax loss of $1,861,242, in line with budget expectations.
- Net assets increased by $1,397,532 to $5,227,194 and at 30 June 2006 the Company had cash resources of $3,940,880.
- The Company conducted a successful placement of 2.3 million shares at $0.70 to raise $1,621,000 in November 2005, and completed a successful Share Purchase Plan issuing 2.4 million shares to raise $1,703,000 in December 2005. The Company's contributed equity following the share issues and after transaction costs arising from the issue of shares, was $8,177,366.
- Tissue Therapies' VitroGro® wound healing technology moved a step closer to providing a cure for chronic diabetic ulcers in July 2005 when a study conducted at QUT demonstrated that VitroGro® stimulated human skin cell growth in samples taken from around non- healing ulcers of diabetic patients. The results indicated that VitroGro® could be developed as a treatment to accelerate healing of diabetic ulcers, and could result in a substantial reduction in amputations due to complications associated with the poor healing of ulcers. A clinical trial of VitroGro® to treat diabetic ulcers is planned for 2007.
- As part of the product development program, Tissue Therapies announced in early October that it had perfected an advanced manufacturing method to produce VitroGro® in a powdered form, using a freeze-drying process

(lyophilisation). The technique will enable cheaper, faster and more flexible distribution to global markets, and facilitate the use of VitroGro® in laboratory live cell work and human healthcare products such as advanced wound dressings.

- The Company secured multiple sources of synthetic (recombinant) vitronectin, a key human protein component of the VitroGro® wound care and cell culture technology. The biologically active synthetic sources manufacturing cost is a fraction of the world price of human-derived vitronectin, ensuring Tissue Therapies' ability to produce a totally synthetic VitroGro® product in sufficient quantities for commercial development.
- In November 2005, the Company confirmed it had successfully created a human live skin model for simulating skin injuries and healing, and for testing cosmetics and cosmeceuticals under its R&D contract with QUT. The skin model can be 'wounded' in the same way as human skin, providing a model for inexpensive, flexible testing of potential wound treatments. Preliminary results indicate that Tissue Therapies' VitroGro® can accelerate the growth and healing of the skin model, consistent with the results from earlier pre-clinical trials using VitroGro®. This development has the potential to replace animal testing and basic human testing for a range of applications, including skin wound healing treatments, cosmetics and cosmeceuticals, and is a practical demonstration of a commercial application for VitroGro®. The live human skin model has proved to be an invaluable research and development tool for the VitroGro® scientific development team.
- Tissue Therapies' second animal trial was completed at the Royal Children's Hospital in Brisbane in late 2005 to gather VitroGro® dosage data for human trials. An independent review of the trial results in early 2006 revealed anomalies caused by an excipient, or inactive, ingredient used to assist in delivery of the VitroGro® complex. The Company will repeat the study later in 2006 to determine optimal doses for the VitroGro® human trial planned for early 2007. The use of the new synthetic VitroGro® components in the second dose study will facilitate quicker, simpler and cheaper regulatory approval in 2007.
- Work on large scale commercial production of synthetic components of VitroGro® continued on schedule and on budget, ensuring that Tissue Therapies has the materials needed for preclinical and clinical trials in 2006 and 2007. It will also deliver substantial savings on the production of VitroGro® and the Good Manufacturing Practice (GMP) materials needed for clinical trials and regulatory approval for human use.
- Negotiations with major international sales and distribution companies progressed during the year, to secure long term product pipeline and supply arrangements for VitroGro® products in key research and industrial cell culture markets. Discussions are focused on long- term product development and integration of VitroGro® into strategic product ranges for international sale, rather than the standard distribution / catalogue sales agreement for basic VitroGro® kits that was previously targeted.
- The IP position of Tissue Therapies continued to gain momentum. The second of the family of the VitroGro® world wide patents was granted by New Zealand in March 2006.
- Queensland Deputy Premier Anna Bligh announced that Tissue Therapies' Chief Scientific Officer, Prof. Zee Upton had been awarded a Smart State Senior Fellowship for her research into wound repair and skin regeneration at the international BIO2006 conference in Chicago in April. The three year, $100,000 per annum Fellowship will allow Prof. Upton to focus on an accelerated development program for the practical application of VitroGro® platform to wound healing. Prof. Upton had previously been awarded the 2004 Smart Women, Smart State award.
- In May 2006, Tissue Therapies announced a breakthrough finding that VitroGro® technology can be used to replace animal and human serum in the culture of human embryonic stem cells. This world-first result was a major milestone in the race to use human embryonic stem cells for medical treatments, and removed one of the most significant obstacles to approved use of stem cell therapies.

Significant Changes in State of Affairs

- In November 2005 the Company conducted a successful share placement offering 2 .3 million shares at $0.70 to raise $1,621,000 and in December 2005 the Company completed a successful Share Purchase Plan issuing 2.4 million shares to raise $1,703,000. This increased cash balances during the year.
- The Company's contributed equity following the share issues and after transaction costs arising from the issue of shares was $8,177,367.

Adoption of Australian Equivalents to IFRS

As a result of the introduction of Australian equivalents to International Financial Reporting Standards (AIFRS), the Company's financial report has been prepared in accordance with those Standards. A reconciliation of adjustments arising on the transition to AIFRS is included in Note 2 to this report.

Matters Subsequent to the End of the Financial Year

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

Likely Developments and Expected Results of Operations

The likely developments in the operations of the Company and expected results of those operations in future financial years are as follows:

Key Achievement / Indicative Milestone	Target	Status
Complete expanded preclinical dose study of new synthetic VitroGro® components as burns treatment, in preparation for clinical trial.	Nov. 2006	Protocol design complete, Ethics Committee approved.
Negotiate VitroGro® technology integration agreement with international biological supply company.	Dec. 2006	Term sheet negotiations underway.
Start Phase 1 clinical trial of VitroGro® to treat venous and diabetic ulcers.	1st half 2007	On schedule
Complete clinical trial of VitroGro® as treatment for burns patients.	June 2007	Detailed planning underway.
Complete regulatory approval of VitroGro® for human burns treatment.	Dec. 2007	Detailed planning underway.
Continued granting of three core VitroGro® patents in worldwide territories	Ongoing	Granted Aust & NZ; pending USA, Canada, EU, Asia.

Options

At the date of this report, options over the unissued share of the Company are as follows:

Grant date	Date of Expiry	Exercise price	Number under option
29/01/2004	30/11/2008	$0.50	1,075,000
14/04/2005	14/04/2007	$0.80	40,000
10/03/2006	27/09/2008	$0.95	100,000
10/03/2006	27/09/2009	$0.95	100,000
10/03/2006	2 years from first milestone achieved *	$0.80 (at least)	300,000 *
21/04/2006	21/04/2008	$0.80	150,000
			1,765,000

- * Options issued to the CEO under the Company's Equity Option Plan in lieu of cash bonus. Options issued will vest on the achievement of certain Key Events, which are outlined in Tissue Therapies Limited's ASX announcement on 10 March 2006.
- No ordinary shares were issued on the exercise of options during the year ended 30 June 2006, or up until the date of this report.

Remuneration Report

This report outlines the remuneration arrangements in place for the directors and executives of Tissue Therapies Limited.

The Company's Board of Directors is responsible for determining and reviewing compensation arrangements for the directors, the chief executive officer (CEO) and others involved in the operation of the Company.

The Board assesses the appropriateness of the nature and amount of remuneration of directors and senior managers on a periodic basis by reference to relevant market conditions with the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality board and executive team.

Non-executive Director Remuneration

- *Objective*: The Board seeks to set aggregate remuneration at a level which provides the company with the ability to attract and retain directors of the highest calibre at a cost that is acceptable to shareholders.
- *Structure*: The Constitution and the ASX Listing Rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. An amount not exceeding the amount determined is then divided between the directors as agreed. The latest determination was at a General Meeting of members held on 29 January 2004 when shareholders approved an aggregate remuneration of $250,000 per year, with remuneration for the first year after listing being $55,000.

The amount of aggregate remuneration sought to be approved by shareholders and the manner in which it is apportioned among directors is reviewed annually. Each director receives an annual fee for being a director of the company. No incentive payments are included.

Executive Director Remuneration

- *Objective*: The Company aims to reward the Executive Director with remuneration commensurate with his position and responsibilities.
- *Structure*: The Executive Director receives a fixed annual amount in remuneration. No incentive payments are included.

Executive Remuneration

Chief Executive Officer

- *Objective*: The Company aims to reward the CEO with remuneration commensurate with his position and responsibilities.
- *Structure*: The CEO, Dr Steven Mercer is employed under contract. The current contract commenced on 27 September 2004. Dr Mercer's employment contract with Tissue Therapies encompasses a total remuneration package of $182, 000 per annum plus a share option package of 200,000 options to acquire shares in the Company at a 20 per cent premium to the Company's share price on 27 September 2004. The initial tranche of 100,000 options will vest one year from the commencement of his employment, and the second 100,000 options will vest two years from the commencement date. Each tranche of options will expire three years from their vesting date and no further options will vest if the Executive resigns or is terminated for any reason. Any vested options must be exercised within 30 days from the date of termination of the employment agreement. Under the employment agreement, the employment arrangements may be terminated by either party at any time by with not less than two months' written notice. In addition, Dr Mercer in March 2006 was awarded 300,000 options in lieu of a cash bonus. These options vest on the achievement of a series of specific performance milestones and are exercisable within two years of each tranche of options vesting.

Company Secretary

- *Objective*: The Company aims to reward the Company Secretary with remuneration commensurate with his position and responsibilities.
- *Structure*: The Company Secretary receives remuneration based on an hourly rate for his services. No incentive payments are included.

Details of Remuneration

Details of the nature and amount of each element of the emoluments of each Director and of the Company Secretary of Tissue Therapies Limited for the year ended 30 June 2006 are set out as follows:

		Primary		Post Employment	Share-based payment		
Key Management Personnel		Cash Salary and fees $	Bonus / Non-monetary benefits $	Super-annuation $	Equity $	Options (a) $	Total $
Non-Executive Directors							
R. Clarke (Chairman)	**2006**	**30,000**	**-**	**2,700**	**-**	**-**	**32,700**
	2005	25,000	-	2,250	-	-	27,250
G. Baynton	**2006**	**10,000**	**-**	**-**	**-**	**-**	**10,000**
	2005	10,000	-	-	-	-	10,000
Prof. D. Gardiner [1]	**2006**	**15,000**	**-**	**-**	**-**	**-**	**15,000**
	2005	10,000	-	-	-	-	10,000
N. Reinhardt	**2006**	**15,000**	**-**	**1,350**	**-**	**-**	**16,350**
	2005	10,000	-	1,154	-	-	11,154
Executive Directors							
G. Baynton	**2006**	**66,000**	**-**	**-**	**-**	**-**	**66,000**
	2005	66,000	-	-	-	-	66,000
Dr S. Mercer (CEO) [2]	**2006**	**166,000**	**-**	**16,284**	**-**	**13,750**	**196,034**
	2005	115,507	-	10,396	-	-	125,903
Other Key Management Personnel							
D. McKenzie	**2006**	**40,268**	**-**	**-**	**-**	**-**	**40,268**
	2005	37,926	-	-	-	-	37,926
Total	**2006**	**342,268**	**-**	**20,334**	**-**	**13,750**	**376,352**
Total	2005	274,433	-	13,800	-	-	288,233

[1] Professor D Gardiner has instructed that all fees payable to him are to be paid into The QUT Endowment Equity Fund.

[2] Dr Steven Mercer was appointed as an executive director on 10 May 2006.

Options issued to Directors & Specified Executives as part of remuneration for the year ended 30 June 2006

Options were issued as part of remuneration during the year to Steven Mercer (Director / CEO) only. Total options granted during the financial year were 500,000 with a total value for the financial year of $13,750, representing 7% of his total remuneration for the year. No options were exercised during the financial year, and no options lapsed.

Directors' and Officers' Indemnification

The Company has indemnified directors and officers to the maximum extent permitted by law, against any liability incurred by them as, or by virtue of their holding office as and acting in the capacity of, an officer of the Company.

Insurance premiums have been paid during the year in respect of a contract insuring directors and officers against legal costs incurred in defending proceedings against them. Details of the nature of liabilities covered or the amount of premiums paid are not disclosed as such disclosure is prohibited in terms of the contract.

Directors' Meetings

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

	Directors Meetings		Audit Committee	
	Eligible to Attend	**Attended**	**Eligible to Attend**	**Attended**
R. Clarke	10	9	3	3
G. Baynton	10	9	3	3
Prof. D. Gardiner	10	8	-	-
N. Reinhardt	10	9	3	3
S. Mercer [1]	1	1	-	-

[1] Dr Steven Mercer was appointed a director on 10 May 2006.

Environmental Regulation

The Company's operations are not regulated by any significant environmental regulation under a law of the Commonwealth or of a State or Territory.

Non-audit Services

The Board of Directors is satisfied that the provision of the 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:

- The accounting and taxation services provided by Hacketts Chartered Accountants are provided on an arms length basis and the fees earned by the firm for these services reflect the nature of the services provided.

	30 June 2006 $	**30 June 2005 $**
Remuneration of Hacketts Chartered Accountants for:		
▪ Audit and review of financial reports and other audit work under the Corporations Act 2001	14,000	12,000
▪ Accounting and taxation services	5,000	5,000
	19,000	17,000

Auditor's Declaration

A copy of the auditor's independence declaration as required under section 307C of the Corporations Act 2001 is attached to this Directors' Report.

Proceedings on Behalf of the Company

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

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

Greg Baynton
Director
Dated at Brisbane, this 03rd **Day of August 2006**

AUDITOR'S INDEPENDENCE DECLARATION

Hacketts
CHARTERED ACCOUNTANTS

LEVEL 3
549 QUEEN STREET
BRISBANE QLD 4000

TELEPHONE « +617 3839 9733
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PARTNERS «
THOMAS G. HACKETT
MICHAEL W. HACKETT
LIAM J. MURPHY

CONSULTANT «
JOHN L. HACKETT

3 August 2006

The Chairman
The Board of Directors
Tissue Therapies Limited
GPO Box 1596
Brisbane QLD 4001

Auditor's Independence Declaration

In accordance with section 307C of the Corporations Act 2001, I am pleased to provide the following declaration of independence to the directors of Tissue Therapies Limited.

As lead audit partner for the audit of the financial report of Tissue Therapies Limited for the year ended 30 June 2006, I declare that to the best of my knowledge and belief, there have been:

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

Yours faithfully

Hacketts

Hacketts

Liam J Murphy
Audit Partner

FINANCIAL STATEMENTS

TISSUE THERAPIES LIMITED
INCOME STATEMENT FOR THE YEAR ENDED 30 JUNE 2006

	Note	30 June 2006 $	30 June 2005 $
Revenues	3	239,315	386,977
Research and development expenses		(859,529)	(865,355)
Occupancy expenses		(39,437)	(28,006)
Administration expenses		(759,964)	(485,562)
Marketing, business development and patent protection		(239,849)	(167,471)
Laboratory expenses		(324,221)	-
Other expenses		(193,287)	(10,684)
Loss before income tax expense	4	(2,176,972)	(1,170,101)
Income tax benefit	5(b)	315,730	243,254
Loss from continuing operations after income tax benefit		(1,861,242)	(926,847)
Loss attributable to members of the entity		(1,861,242)	(926,847)
		Cents	**Cents**
Overall Operations			
Basic earnings per share	24	(10.19)	(6.06)
Diluted earnings per share	24	(10.06)	(5.90)

The accompanying notes form part of these statements.

TISSUE THERAPIES LIMITED
BALANCE SHEET AS AT 30 JUNE 2006

	Note	30 June 2006 $	30 June 2005 $
CURRENT ASSETS			
Cash and cash equivalents	6	3,940,880	3,161,021
Trade and other receivables	7(a)	48,779	55,511
Inventories	8	197,593	89,953
Current tax assets	5(d)	320,165	311,160
Other current assets	7(b)	483,571	9,545
TOTAL CURRENT ASSETS		4,990,988	3,627,190
NON-CURRENT ASSETS			
Property, plant and equipment	9	105,776	55,231
Intangible assets	10	342,250	342,250
TOTAL NON-CURRENT ASSETS		448,026	397,481
TOTAL ASSETS		5,439,014	4,024,671
CURRENT LIABILITIES			
Trade and other payables	11	211,820	195,009
TOTAL LIABILITIES		211,820	195,009
NET ASSETS		5,227,194	3,829,662
EQUITY			
Issued Capital	12	8,177,366	4,939,519
Reserves		22,354	1,427
Retained losses		(2,972,526)	(1,111,284)
TOTAL EQUITY		5,227,194	3,829,662

The accompanying notes form part of these statements.

TISSUE THERAPIES LIMITED
STATEMENT OF CHANGES IN EQUITY AS AT 30 JUNE 2006

	30 June 2006 $	30 June 2005 $
Contributed equity		
Ordinary shares at beginning of period	4,939,519	3,508,719
Shares issued during period	3,324,014	1,460,000
Transaction costs	(86,167)	(29,200)
Balance of ordinary shares at end of period	8,177,366	4,939,519
Options reserve		
Options reserve at beginning of period	1,427	-
Share options expensed during the period	20,927	1,427
Balance of options reserve at end of period	22,354	1,427
Retained earnings		
Retained earnings at beginning of period	(1,111,284)	(183,010)
Loss attributable to members of the entity	(1,861,242)	(928,274)
Retained earnings at end of period	(2,972,526)	(1,111,284)
Total equity at the end of the period	**5,227,194**	**3,829,662**

The accompanying notes form part of these statements.

TISSUE THERAPIES LIMITED
CASH FLOW STATEMENT FOR THE YEAR ENDED 30 JUNE 2006

	Note	30 June 2006 $	30 June 2005 $
CASH FLOW FROM OPERATING ACTIVITIES			
Receipts from customers (inclusive of goods and services tax)		9,611	5,873
Payments to research facility (inclusive of goods and services tax)		(1,094,932)	(831,182)
Payments to suppliers (inclusive of goods and services tax)		(1,830,790)	(733,240)
Interest received		215,299	177,792
Finance costs		(687)	(720)
Income Tax rebate received		306,725	-
Net cash provided by (used in) operating activities	23(b)	(2,394,774)	(1,381,477)
CASH FLOW FROM INVESTING ACTIVITIES			
Payments for property, plant and equipment		(88,217)	(18,499)
Net cash provided by (used in) investing activities		(88,217)	(18,499)
CASH FLOW FROM FINANCING ACTIVITIES			
Proceeds from share issues		3,323,950	1,460,000
Costs of share issue		(75,505)	(29,201)
Grant income received		14,405	177,970
Net cash provided by (used in) financing activities		3,262,850	1,608,769
Net increase (decrease) in cash held		779,859	208,793
Cash at beginning of year		3,161,021	2,952,228
Cash at end of year	23(a)	3,940,880	3,161,021

The accompanying notes form part of these statements.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 1: STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

The financial report is a general purpose financial report that has been prepared in accordance with Australian Accounting Standards, Urgent Issues Group Interpretations, other authoritative pronouncements of the Australian Accounting Standards Board and the Corporations Act 2001.

The financial report covers Tissue Therapies Limited, which is a listed public company, incorporated and domiciled in Australia.

The following is a summary of the material accounting policies adopted by the Company in the preparation of the financial report. The accounting policies have been consistently applied, unless otherwise stated.

Basis of preparation

First-time Adoption of Australian Equivalents to International Financial Reporting Standards

Tissue Therapies Limited has prepared financial statements in accordance with the Australian equivalents to International Financial Reporting Standards (AIFRS) from 1 July 2005.

In accordance with the requirements of AASB 1: First-time Adoption of Australian Equivalents to International Financial Reporting Standards, adjustments to accounts resulting from the introduction of AIFRS have been applied retrospectively to 2005 comparative figures excluding cases where optional exemptions available under AASB 1 have been applied. These accounts are the first financial statements of Tissue Therapies Limited to be prepared in accordance with Australian equivalents to IFRS.

The accounting policies set out below have been consistently applied to all years presented.

Reconciliations of the transition from previous Australian GAAP to AIFRS have been included in Note 2 to this report.

Reporting Basis and Conventions

The financial report has been prepared on an accruals basis and is based on historical costs modified by the revaluation of selected non-current assets, financial assets and financial liabilities for which the fair value basis of accounting has been applied.

Accounting Policies

a. **Income Tax**

The charge for current income tax expense is based on the profit for the year adjusted for any non-assessable or disallowed items. It is calculated using the tax rates that have been enacted or are substantially enacted by the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. No deferred income tax will be recognised from the initial recognition of an asset or liability, excluding a business combination, where there is no effect on accounting or taxable profit or loss.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or liability is settled. Deferred tax is credited in the income statement except where it relates to items that may be credited directly to equity, in which case the deferred tax is adjusted directly against equity.

Deferred income tax assets are recognised to the extent that it is probable that future tax profits will be available against which deductible temporary differences can be utilised.

The amount of benefits brought to account or which may be realised in the future is based on the assumption that no adverse change will occur in income taxation legislation and the anticipation that the economic entity will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

b. **Research and Development Expenditure**

Expenditure during the research phase of a project is recognised as an expense when incurred. Development costs are capitalised only when technical feasibility studies identify that the project will deliver future economic benefits and these benefits can be measured reliably.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 1: STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

c. Intangibles

Licenses, Patents and Trademarks

Licenses, patents and trademarks are recognised at cost of acquisition. Licenses, patents and trademarks have a finite life and are carried at cost less any accumulated amortisation and any impairment losses. Licenses, patents and trademarks are amortised over their useful life which has been assessed as ten years from the date the intangible asset is in its intended use.

d. Employee Benefits

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

Equity –settled Compensation

The Company operates an option based compensation plan. The bonus element over the exercise price of the employee services rendered in exchange for the grant of options is recognised as an expense in the income statement. The total amount to be expensed over the vesting period is determined by reference to the fair value of the shares of the options granted.

e. Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within short-term borrowings in current liabilities on the balance sheet.

f. Revenue recognition

Revenues are recognised at fair value of the consideration received net of any applicable taxes.

Interest revenue is recognised as it accrues taking into account the interest rates applicable to the financial assets.

Government research and development grant income is recognised as and when the relevant research expenditure is incurred. Grants relating to expense items are recognised as income over the periods necessary to match the grant to the costs they are compensating. Grants relating to assets are credited to deferred income at fair value and are credited to income over the expected useful life of the asset on a straight-line basis.

All revenue is stated net of the amount of goods and services tax (GST).

g. Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the statement of financial position are shown inclusive of GST.

Cash flows are presented in the cash flow statement on a gross basis, except for the GST component of investing and financing activities, which are disclosed as operating cash flows.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 1: STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

h. Property, plant and equipment

Each class of property, plant and equipment is carried at cost or fair value less, where applicable, any accumulated depreciation and impairment losses.

Plant and equipment

Plant and equipment are measured on the cost basis.

The carrying amount of plant and equipment is reviewed annually by directors to ensure it is not in excess of the recoverable amount from these assets. The recoverable amount is assessed on the basis of the expected net cash flows that will be received from the asset's employment and subsequent disposal. The expected net cash flows have been discounted to their present values in determining recoverable amounts.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation

The depreciable amount of all fixed assets including building and capitalised lease assets, but excluding freehold land, is depreciated on a straight-line basis over their useful lives to the Company commencing from the time the asset is held ready for use. The expected useful life for plant and equipment is 3 to 5 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These gains and losses are included in the income statement. When revalued assets are sold, amounts included in the revaluation reserve relating to that asset are transferred to retained earnings.

i. Inventory

Inventories are measured at the lower of cost and net realisable value. The cost of manufactured products includes direct materials, direct labour and an appropriate portion of variable and fixed overheads.

j. Trade and other creditors

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

k. Leases

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

l. Impairment of assets

At each reporting date, the Company reviews the carrying values of its tangible and intangible assets to determine whether there is any indication that those assets have been impaired. If such an indication exists, the recoverable amount of the asset, being the higher of the asset's fair value less costs to sell and value in use, is compared to the asset's carrying value. Any excess of the asset's carrying value over its recoverable amount is expensed to the income statement.

Impairment testing is performed annually for intangible assets.

Where it is not possible to estimate the recoverable amount of an individual asset, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 1: STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

m. Comparative figures

When required by Accounting Standards, comparative figures have been adjusted to conform to changes in presentation for the current financial year.

Critical Accounting Estimates and Judgments

The directors evaluate estimates and judgments incorporated into the financial report based on historical knowledge and best available current information. Estimates assume a reasonable expectation of future events and are based on current trends and economic data, obtained both externally and within the Company.

Key Estimates — Impairment

The Company assesses impairment at each reporting date by evaluating conditions specific to the group that may lead to impairment of assets. Where an impairment trigger exists, the recoverable amount of the asset is determined.

No impairment has been recognised in respect of licenses and trademarks for the year ended 30 June 2006.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 2 : FIRST-TIME ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

		As at 30 June 2005	As at 1 July 2004
		$	$
a.	**Reconciliation of Equity:**		
	Total contributed equity as reported (per previous GAAP and under AIFRS)	4,939,519	3,508,719
	Option Reserves as reported (per previous GAAP)	-	-
	- Increase in reserves resulting from recognition of share options issued, on a pro rata basis over the vesting period per AASB 2	1,427	-
	Option Reserves (under AIFRS)	1,427	-
	Retained losses as reported (as per previous GAAP)	(1,109,857)	(183,010)
	- Increase in retained losses resulting from recognition of share options expense, on a pro-rata basis over the vesting period per AASB 2	(1,427)	-
	Retained losses (under AIFRS)	(1,111,284)	(183,010)
	Total equity under AIFRS	**3,829,662**	**3,325,709**

		Year ended 30 June 2005
		$
b.	**Reconciliation of net loss for 2005**	
	Net loss reported (as per previous GAAP)	(1,109,857)
	- Increase in 'other expenses' resulting from recognition of share options expense, on a pro-rata basis over the vesting period per AASB 2.	(1,427)
	Net loss (under A-IFRS)	(1,111,284)

c. **Notes to the reconciliation**

Under AASB 2 *Share based Payments*, from 1 July 2004 the Company is required to recognise an expense for those options that were issued to employees under the Equity Option Plan after 7 November 2002 that had not vested by 1 January 2005. The shares were issued on 14 April 2005 and the company was required to recognise an expense of $1,427 in accordance with AASB 2 for the year ended 30 June 2005, and a corresponding creation of an 'Options Reserve' in equity as at the same date.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

	30 June 2006 $	30 June 2005 $
NOTE 3: REVENUE		
Operating activities:		
Product sales	9,611	5,873
Interest	215,299	177,792
Research grants	14,405	203,312
Total revenue from ordinary activities	239,315	386,977

NOTE 4: LOSS FOR THE YEAR

	30 June 2006 $	30 June 2005 $
Expenses		
Cost of sales	9,038	-
Finance costs - external	687	720
Rental expense on operating leases – minimum lease payments	34,646	28,006
Research and development costs	859,529	865,355
Depreciation expense	2,276	1,114

NOTE 5: INCOME TAX

a. The components of income tax benefit comprises

	30 June 2006 $	30 June 2005 $
Current tax	320,163	257,249
Overprovision in respect of prior years	(4,433)	(13,995)
Total tax benefit	315,730	243,254

b. The prima facie tax benefit on loss from ordinary activities before income tax is reconciled to the income tax benefit as follows:

	30 June 2006 $	30 June 2005 $
Tax benefit on loss from ordinary activities at 30% (2005 – 30%)	653,092	351,030
Tax effect of:		
Business related capital expenditure	(35,352)	13,338
Increase in accruals	(4,412)	-
Non-deductible entertainment	(587)	(590)
Share options expensed during the year	(6,278)	-
Tax Losses available	606,463	363,778
Tax losses utilised by:		
▪ Income tax benefit attributable to R&D tax offset receivable	320,163	257,249
▪ Income tax benefit attributable to R&D tax offset overstated in prior year	(4,433)	(13,995)
Income tax benefit relating to ordinary activities	315,730	243,254

TISSUE THERAPIES LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

	30 June 2006 $	30 June 2005 $
NOTE 5: INCOME TAX (continued)		
c. Deferred tax asset		
Deferred tax assets not brought to account, the benefits of which will only be realised if the conditions for deductibility set out in Note 1a occur:		
Temporary differences	151,083	111,319
Tax losses – operating losses	526,103	177,499
	677,186	288,818
d. Current Tax Asset		
Opening balance of R&D tax offset concession claimed	311,160	67,907
Less - R&D tax offset overstated in prior year	(4,434)	(13,996)
Less- Income tax benefit attributable to R&D tax offset received	(306,726)	-
Add - Income tax benefit attributable to R&D tax offset receivable	320,165	257,249
Closing balance of Research and Development tax offset concession claimed	320,165	311,160

NOTE 6: CURRENT ASSETS - CASH AND CASH EQUIVALENTS

Cash at bank	138,774	55,507
Short term bank deposits - at call *	3,802,106	3,105,514
	3,940,880	3,161,021

* The deposits are in interest bearing floating rate accounts. Interest rates vary between 5.45% and 5.75%.

NOTE 7: TRADE AND OTHER RECEIVABLES & OTHER CURRENT ASSETS

(a)

Trade debtors	6,612	4,734
GST receivable	42,167	50,777
	48,779	55,511

(b) Other Current Assets

Prepayments	483,571	9,545
	483,571	9,545

NOTE 8: INVENTORIES

Stock of raw materials – at cost	197,593	89,953
	197,593	89,953

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

	30 June 2006 $	30 June 2005 $
NOTE 9: NON-CURRENT ASSETS - PROPERTY, PLANT & EQUIPMENT		
Plant and equipment – at cost	15,192	6,721
Less: Accumulated depreciation	(4,009)	(1,357)
	11,183	5,364
Capital Works in progress	94,593	49,867
Total property, plant and equipment	105,776	55,231

Reconciliations of the carrying amounts of each class of property, plant and equipment at the beginning and end of the current financial year are set out below.	Plant & Equipment $	Capital Works in progress $	Total
Carrying amount at 1July 2005	5,364	49,867	55,231
Additions	8,095	44,726	52,821
Depreciation expense	(2,276)	-	(2,276)
Carrying amount at 30 June 2006	11,183	94,593	105,776

Based on the methodology applied in Note 1 to the financial statements, there were no impairment gains or losses booked during the current financial year.

	30 June 2006 $	30 June 2005 $
NOTE 10: NON-CURRENT ASSETS - INTANGIBLE ASSETS		
Licenses and Patents - at cost	342,250	342,250
Less: Accumulated amortisation	-	-
	342,250	342,250

Licences and patents are assessed to have finite useful lives. Amortisation shall begin when the asset is available for use, that is, when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. There are no amortisation charges for licenses and patents for the current or prior financial periods.

NOTE 11: CURRENT LIABILITIES – TRADE AND OTHER PAYABLES		
Trade creditors	130,081	132,421
Other creditors and accruals	81,739	62,588
	211,820	195,009

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

	30 June 2006	30 June 2005
	$	$
NOTE 12: ISSUED CAPITAL		
a. **Share capital**		
20,203,592 (30 June 2005: 15,455,000) fully paid ordinary shares	8,177,366	4,939,519

b. **Fully paid ordinary shares**

Ordinary shares participate in dividends and the proceeds on winding up of the Company in proportion to the number of shares held

At shareholders meetings each ordinary share is entitled to one vote when a poll is called, otherwise each shareholder has one vote on a show of hands

c. Movements in ordinary share capital:

Date	Details	No. Shares	Issue price	$
01/07/04	Balance at beginning of year	15,455,000		4,939,519
30/06/05	Balance at end of year	15,455,000		4,939,519
23/11/05	2,315,000 ordinary shares issued by placement	2,315,500	$0.70	1,620,850
22/12/05	2,433,092 ordinary shares under Share Purchase Plan	2,433,092	$0.70	1,703,164
	Transaction costs arising from the issue of shares by placement and under Share Purchase Plan			(86,167)
30/06/06	Balance at end of year	20,203,592		8,177,366

d. **Options**

i) For information relating to options issued, exercised and lapsed during the financial year and the options outstanding at year-end, refer to Note 17: Share-based Payments.

ii) For information relating to share options issued to key management personnel during the financial year, refer to Note 17: Share-based Payments.

NOTE 13: RESERVES

Option Reserve

The option reserve records items recognised as expenses on valuation of employee share options.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 14: REMUNERATION OF AUDITORS

	30 June 2006 $	30 June 2005 $
Remuneration of Hacketts Chartered Accountants for:		
▪ Audit and review of financial reports and other audit work under the Corporations Act 2001.	14,000	12,000
▪ Accounting and taxation services	5,000	5,000
	19,000	17,000

NOTE 15: FINANCIAL INSTRUMENTS

a. Credit risk exposures

The credit risk on financial assets of the company which have been recognised on the balance sheet is generally the carrying amount, net of any provisions for doubtful debts.

b. Interest rate risk exposures

The company's exposure to interest rate risk and the effective weighted average interest rate is set out in the relevant note.

c. Liquidity risk

The Company manages liquidity risk by monitoring forecast cash flows and ensuring that adequate facilities or financing options are maintained.

d. Net fair value of financial assets and liabilities

The net fair value of cash and cash equivalents and non-interest bearing monetary financial assets and the financial liabilities of the company approximates their carrying amounts.

The net fair value of other monetary financial assets and financial liabilities is based upon market prices where a market exists or by discounting the expected future cash flows by the current interest rates for assets and liabilities with similar risk profiles.

NOTE 16: KEY MANAGEMENT PERSONNEL COMPENSATION

a. Names and positions held of the Company's key management personnel in office at any time during the financial year are:

Key Management Person	Position
Mr Roger Clarke	Chairman – Non-executive
Professor David Gardiner	Director – Non-executive
Mr Greg Baynton	Executive Director
Mr Neil Reinhardt	Director – Non-executive
Dr Steven Mercer	Chief Executive Officer and Executive Director
Mr D McKenzie	Company Secretary

TISSUE THERAPIES LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 16: KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

b. Compensation Practices

Principles used to determine the nature and amount of remuneration

Remuneration of Directors and executives is currently decided at the board level.

Directors are remunerated by a fixed sum and not a commission on, or a percentage of, profits or operating revenue. The level of remuneration may not be increased except at a general meeting in which particulars of the proposed increase have been provided in the notice convening the meeting to shareholders. There is provision for directors who devote special attention to the business of the company or who perform services regarded as outside the scope of their duties as directors, or who at the request of the Board engage on any journey on company business, to be paid extra remuneration determined by the Board. Directors are also entitled to their reasonable travel, accommodation and other expenses incurred in attending company or board meetings, or meetings of any committee engaged in the Company's business.

Any director may be paid a retirement benefit as determined by the Board, consistent with the Corporations Act and ASX Listing Rules.

A director is disallowed from voting on any contract or arrangement in which he or she has directly or indirectly any material interest, if it will be contrary to the Corporations Act.

c. Key Management Personnel Compensation

		Primary		Post Employment	Share-based payment		
Key Management Personnel		**Cash Salary and fees $**	**Bonus / Non-monetary benefits $**	**Super-annuation $**	**Equity $**	**Options (a) $**	**Total $**
Non-Executive Directors							
R. Clarke (Chairman)	**2006**	**30,000**	**-**	**2,700**	**-**	**-**	**32,700**
	2005	25,000	-	2,250	-	-	27,250
G. Baynton	**2006**	**10,000**	**-**	**-**	**-**	**-**	**10,000**
	2005	10,000	-	-	-	-	10,000
Prof. D. Gardiner [1]	**2006**	**15,000**	**-**	**-**	**-**	**-**	**15,000**
	2005	10,000	-	-	-	-	10,000
N. Reinhardt	**2006**	**15,000**	**-**	**1,350**	**-**	**-**	**16,350**
	2005	10,000	-	1,154	-	-	11,154
Executive Directors							
G. Baynton	**2006**	**66,000**	**-**	**-**	**-**	**-**	**66,000**
	2005	66,000	-	-	-	-	66,000
Dr S. Mercer (CEO) [2]	**2006**	**166,000**	**-**	**16,284**	**-**	**13,750**	**196,034**
	2005	115,507	-	10,396	-	-	125,903
Other Key Management Personnel							
D. McKenzie	**2006**	**40,268**	**-**	**-**	**-**	**-**	**40,268**
	2005	37,926	-	-	-	-	37,926
Total	**2006**	**342,268**	**-**	**20,334**	**-**	**13,750**	**376,352**
Total	2005	274,433	-	13,800	-	-	288,233

[1] Professor D Gardiner has instructed that all fees payable to him are to be paid into The QUT Endowment Equity Fund.

[2] Dr Steven Mercer was appointed an executive director on 10 May 2006.

TISSUE THERAPIES LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 16: KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

d. Compensation Options

Options granted as compensation:

Key Management Personnel	Vested No.	Granted No.	Grant Date	Value per option at grant date $	Exercise price $	First exercise date	Last exercise date
Dr S. Mercer	100,000	100,000	10/03/ 2006	$0.07	$0.95	10/03/2006	27/09/2008
Dr S. Mercer	100,000	100,000	10/03/2006	$0.07	$0.95	10/03/2007	27/09/2009
Dr S. Mercer	300,000	300,000	10/03/2006	$0.10	At least $0.80	On achievement of milestones *	2 years from issue date *
Total	**500,000**	**500,000**					

- * Options issued to the CEO under the Company's Equity Option Plan in lieu of cash bonus. Options issued will vest on the achievement of certain Key Events, which are outlined in Tissue Therapies Limited's ASX announcement on 10 March 2006.

The service and performance criteria set to determine compensation are included per Note 16 (b) and Note 17.

All options were granted for nil consideration.

e. Shares Issued on Exercise of Compensation Options

There were no options exercised during the year that were granted as compensation in prior periods.

f. Option Holdings

Number of options held by Key Management Personnel:

Key Management Personnel	Balance 1.7.2005	Granted as Remuneration	Options Exercised	Balance 30.06.2006	Total Vested 30.06.06	Total Exercisable 30.06.06	Total Unexercisable 30.06.06
R. Clarke	150,000	-	-	150,000	-	150,000	-
G. Baynton [2]	600,000	-	-	600,000	-	600,000	-
Prof. D. Gardiner [1]	100,000	-	-	100,000	-	100,000	-
N. Reinhardt	100,000	-	-	100,000	-	100,000	-
Dr S. Mercer	-	500,000	-	500,000	-	100,000	400,000
D. McKenzie	25,000	-	-	25,000	-	25,000	-
Total	**975,000**	**500,000**		**1,475,000**		**1,075,000**	**400,000**

[1] A total of 2,255,000 shares and 100,000 options are held by QUT, which is a related entity of Professor David Gardiner.

[2] Orbit Capital, a related entity of Gregory Baynton holds 520,000 shares and 600,000 options.

TISSUE THERAPIES LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 16: KEY MANAGEMENT PERSONNEL COMPENSATION (continued)

g. Share Holdings

Number of Shares held by Key Management Personnel:

Key Management Personnel	Balance 1.7.2005	Received as Compensation	Options Exercised	Balance 30.06.2006
R. Clarke	200,000	-	-	200,000
G. Baynton [2]	520,000	-	-	520,000
Prof. D. Gardiner [1]	2,255,000	-	-	2,255,000
N. Reinhardt	260,000	-	-	260,000
Dr S. Mercer	69,379	-	-	69,379
D. McKenzie	-	-	-	-
Total	**3,304,379**	-	-	**3,304,379**

[1] A total of 2,255,000 shares and 100,000 options are held by QUT, which is a related entity of Professor David Gardiner.

[2] Orbit Capital, a related entity of Gregory Baynton holds 520,000 shares and 600,000 options.

NOTE 17: SHARE-BASED PAYMENTS

The following share-based payment arrangements existed at 30 June 2006:

- On 10 March 2006 100,000 share options were granted to the CEO to take up ordinary shares at an exercise price of $0.95 each. The options are exercisable on or before 27 September 2008.
- On 10 March 2006 100,000 share options were granted to the CEO to take up ordinary shares at an exercise price of $0.95 each. The options are exercisable after 27 September 2006 and on or before 27 September 2009.
- On 10 March 2006 300,000 share options were granted to the CEO to take up ordinary shares at an exercise price of at least $0.80 each. The options are exercisable after on the achievement of specified milestones and within 2 years of the achievement of each milestone.
- On 21 April 2006, 150,000 share options were granted to key research staff employed by the Queensland University of Technology to take up ordinary shares at an exercise price of $0.80 each. The options are exercisable on or before 21 April 2008.

The options hold no voting or dividend rights and are not transferable. At balance date no options had been exercised.

	2006		2005	
	Number of options	**Weighted average exercise price $**	**Number of options**	**Weighted average exercise price $**
Outstanding at the beginning of the year	1,115,000	0.51	1,075,000	0.50
Granted	650,000	0.85	40,000	0.80
Forfeited	-		-	
Exercised	-		-	
Expired	-		-	
Outstanding at year-end	1,765,000	0.63	1,115,000	0.51
Exercisable at year-end	1,365,000	0.55	1,115,000	0.51

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 17: SHARE-BASED PAYMENTS (Continued)

There were no options exercised during the year ended 30 June 2006.

The options outstanding at 30 June 2006 had a weighted average exercise price of $0.63 and a weighted average remaining contractual life of 2.51 years. Exercise prices range from $0.50 to $0.95 in respect of options outstanding at 30 June 2006.

The weighted average fair value of the options granted during the year was $0.08.

This price was calculated by using a Black Scholes option pricing model applying the following inputs:

Weighted average exercise price	$0.85
Weighted average life of the option	3.04 years
Underlying share price	$0.59
Expected share price volatility	40%
Risk free interest rate	6.13%

Historical volatility has been the basis for determining expected share price volatility as it is assumed that this is indicative of future tender, which may not eventuate.

Included under administration expense in the income statement is $20,927 (2005: $1,427), and relates, in full, to equity-settled share-based payment transactions.

NOTE 18: COMMITMENTS FOR EXPENDITURES	30 June 2006 $	30 June 2005 $
a. Commitments for consultancy services contracted for at the reporting date but not recognised as liabilities, payable		
Within one year	2,211,559	742,753
Later than one year but not later than 5 years	537,652	11,255
Later than 5 years	-	-
	2,749,211	754,008

NOTE 19: CONTINGENT LIABILITIES AND CONTINGENT ASSETS

- The Company has entered into a Deed of Assignment of Intellectual Property Rights with QUT, under which QUT will assign the Intellectual Property to the Company on the payment of $100,000 by the Company and the satisfaction of certain preconditions regarding, among other things, its level of cash reserves, the Company's share price and a minimum level of expenditure under the R&D Agreement.
- Directors are not aware of any other contingent liabilities that are likely to have a material effect on the results of the Company as disclosed in these financial statements.

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 20: RELATED PARTY TRANSACTIONS

Transactions between related parties are on normal commercial terms and conditions no more favourable than those available to other parties unless otherwise stated.

Key Management Personnel

- The Company entered into a R&D Agreement with QUT to undertake R&D Projects as requested by the Company during the term of the above Intellectual Property Licence Agreement and on normal terms and conditions. During the year $748,248 was paid to QUT in accordance with the R&D Agreement. QUT is a related entity of a Director, Professor David Gardiner.
- The Company has entered into a Corporate and Commercial Services Advisory Agreement with Orbit Capital for a period of two years from the date of listing of the Company on ASX. Orbit Capital is a related entity of a Director, Gregory Baynton. Under the terms of this Agreement, Orbit Capital receives remuneration of $5,500 per month (plus GST).
- The Company paid a fee of $31,487 to ABN AMRO Morgans Corporate Limited for its part in the successful placement of 2,315,000 ordinary shares. Roger Clarke is a director of ABN AMRO Morgans Corporate Limited.
- The Company paid fees of $14,823 for public relations services to Synchronous Communication. Synchronous Communication was a related entity of a Director, Gregory Baynton, up until 31 December 2005.

NOTE 21: SEGMENT INFORMATION

Tissue Therapies Limited operates predominantly in one business segment being biotechnology. Tissue Therapies customers and clients are located predominantly in Australia.

NOTE 22: EVENTS SUBSEQUENT TO REPORTING DATE

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

TISSUE THERAPIES LIMITED
NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 23: CASH FLOW INFORMATION	30 June 2006 $	30 June 2005 $
a. Reconciliation of Cash		
Cash at end of the financial year as shown in the statements of cash flows is reconciled to the related items in the balance sheet as follows:		
Cash and cash equivalents	3,940,880	3,161,021
	3,940,880	3,161,021
b. Reconciliation of Cash Flow from Operations with Loss after Income Tax		
Loss after income tax	(1,861,242)	(926,847)
Non-cash flows in profit from ordinary activities		
Depreciation	2,276	1,114
Amortisation of share based payments	20,927	
Changes in assets and liabilities		
(Increase)/ decrease in receivables and prepayments	(442,496)	(46,517)
Increase in payables	16,811	101,948
(Increase) in tax recoverable	(9,005)	(243,252)
(Increase) in inventory	(107,640)	(89,953)
Other- research grants included in cash flows from financing activities	(14,405)	(177,970)
Cash outflows from operations	(2,394,774)	(1,381,477)

NOTE 24: EARNINGS PER SHARE

Weighted average number of shares used as the denominator	No.	No.
Weighted average number of ordinary shares outstanding during the year used in calculation of Basic EPS	18,265,021	14,914,746
Weighed average number of options outstanding which are considered potentially dilutive	239,075	405,498
Weighted average number of potential ordinary shares outstanding during the year used in calculation of Dilutive EPS	18,504,096	15,320,244

The diluted EPS calculation includes that portion of these options considered to be potentially dilutive, weighted with reference to the date of conversion. The weighted average number included is 239,075.

TISSUE THERAPIES LIMITED

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2006

NOTE 25: CHANGE IN ACCOUNTING POLICY

The Company has assessed all AASB Amendments to Australian Accounting Standards applicable to the Company but not yet effective. They have not been adopted in the preparation of the financial statements at reporting date as there is no change or impact as a consequence of adoption.

NOTE 26: COMPANY DETAILS

The registered office and principal place of business of the Company is:

Tissue Therapies Limited
Level 25 Waterfront Place
1 Eagle Street
Brisbane Qld 4000
Australia

DIRECTORS DECLARATION

The directors of the Company declare that:

1. the financial statements and notes, as set out on pages 9 to 29, are in accordance with the Corporations Act 2001; and
   a. comply with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
   b. give a true and fair view of the Company's financial position as at 30 June 2006 and of its performance, as represented by the results of its operations and cash flows, for the year ended on that date.
2. in the directors' opinion there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.
3. The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A of the Corporations Act 2001 for the financial year ended 30 June 2006.

This declaration is made in accordance with a resolution of the Board of Directors.

Greg Baynton
Director
Dated at Brisbane, this 03rd **Day of August 2006**

Hacketts

INDEPENDENT AUDIT REPORT TO THE MEMBERS OF TISSUE THERAPIES LIMITED

Scope

The financial report and directors' responsibility:

The financial report comprises the balance sheet, income statement, statement of changes in equity, cash flow statement, accompanying notes to the financial statements, and the directors' declaration for Tissue Therapies Limited for the year ended 30 June 2006.

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

Audit Approach

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

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

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

— examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and

— assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

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

Our audit did not involve an analysis of the prudence of business decisions made by directors or management.

Independence

In conducting our audit, we followed applicable independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001. We have given the Directors of the Company a written Auditor's Independence Declaration, a copy of which is attached to the Directors' Report.

Audit Opinion

In our opinion, the financial report of Tissue Therapies Limited is in accordance with:

a. the Corporations Act 2001, including:

   i. giving a true and fair view of the company's financial position as at 30 June 2006 and of it's performance for the year ended on that date; and

   ii. complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

b. other mandatory professional reporting requirements in Australia.

Hacketts

HACKETTS CHARTERED ACCOUNTANTS

Liam Murphy
Partner

Dated at Brisbane this 3 **day of August 2006**