



PHOSLOCK WATER SOLUTIONS LIMITED

and CONTROLLED ENTITIES

ABN 88 099 555 290

INTERIM FINANCIAL STATEMENTS

FOR THE HALF YEAR ENDED 31 DECEMBER 2010

**Phoslock Water Solutions Limited
and Controlled Entities
ABN 88 099 555 290
Interim Financial Report**

DIRECTORS' REPORT

Your directors submit the financial report of the consolidated group for the half-year ended 31 December 2010.

Directors

The names of directors who held office during or since the end of the half-year:

Dr David Garman - Non-Executive Chairman
Hon. Pam Allan – Non-Executive Director
Laurence Freeman, AM – Non-Executive Director
(appointed 26 October, 2010)
Robert Schuitema – Managing Director

Review of Operations

The financial performance of the company for the first half of FY10/11 was lower than the corresponding period. Sales for the period were affected by several projects being delayed in Europe and North America by 6 and up to 12 months. Total Revenue was \$689,164 was 35% lower than the corresponding half year. The Loss before Interest Tax and Depreciation & Amortisation (EBITDA) was (\$943,452) versus (\$611,375) for the corresponding period.

Total operating expenses (including employee costs) for the first half were \$1,447,519 which is 6% higher than the corresponding period last year. Higher employee costs (10%) were as a result of additional executives in Europe and China. General operating expenses were 4% lower.

The Company issued 23.5 million new shares at 5 cents per share in September, 2010 raising approx \$1.2m. A further 2.9 million new shares were issued to PWS Directors & Executives at the Company's AGM in November, 2010 on the same terms and conditions as the September, 2010 placement.

As at 31 December, 2010 the Company had Net Assets of \$4.8 million including cash of \$634,306. The Company is debt free (other than normal trade creditors). Current Assets less Current Liabilities were \$2.6 million as at the half year end.

Over the last six months the Company has signed four Sales & Distribution Agreements with North American companies covering the whole of United States and Quebec and Atlantic Canadian provinces. All four agreements are important in developing Phoslock in the North American market. The SePRO Agreement which was announced in early February 2011 will see Phoslock integrated as part of its product range which it supplies over 160 authorised applicator companies throughout the United States.

The result for the second half of FY10/11 is dependent on several medium/large orders being secured. Customers have recently committed to orders for approx \$200,000 of product which has been supplied to customers. The Company is currently in discussions on six projects with a total sales value in excess of \$10 million in Europe, North America and Asia. The company expects to secure a number of these projects, which is likely to have a material effect on the Company's result for the full year. The sales pipeline beyond June 2011 is very strong with work well advanced on a number of very large projects in Europe, North America, Australia and Asia.

At the date this report the consolidated entity had cash reserves of \$812,000 from which to fund future operations.

Phoslock Water Solutions Limited
and Controlled Entities
ABN 88 099 555 290
Interim Financial Report

DIRECTORS' REPORT

Auditor's Declaration

The lead auditor's independence declaration under s 307C of the *Corporations Act 2001* is set out on page 4 for the half-year ended 31 December 2010.

This report is signed in accordance with a resolution of the Board of Directors.



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Robert Schuitema

Director

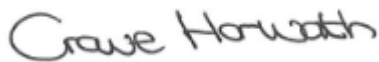
Dated this 27st day of February, 2011.

The accompanying notes form part of these financial statements.

**Auditor's Independence Declaration
Under Section 307C of the Corporations Act 2001
To the Directors of Phoslock Water Solutions Limited**

I declare that, to the best of my knowledge and belief, during the half-year ended 31 December 2010, there have been:

- (1) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the review; and
- (2) no contraventions of any applicable code of professional conduct in relation to the review.



CROWE HORWATH



VANESSA DE WAAL

Principal

Signed in Brisbane on 27 February 2011

**Phoslock Water Solutions Limited
and Controlled Entities
ABN 88 099 555 290
Interim Financial Report
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010**

	Note	Consolidated Group	
		31.12.2010	31.12.2009
		\$	\$
Revenue	2	361,969	916,062
Cost of sales		(170,669)	(301,573)
Gross profit		<u>191,300</u>	<u>614,489</u>
Other income	2	327,195	146,856
Distribution expenses		(101,353)	(57,415)
Marketing expenses		(161,525)	(232,616)
Occupancy expenses		(84,914)	(65,374)
Administrative expenses		(305,055)	(293,333)
Employee benefits expense		(743,801)	(676,924)
Depreciation and amortisation		(220,243)	(245,016)
Finance costs		(20,579)	(44,232)
Other expenses		(50,871)	(39,654)
Share of net profits of associates		-	-
Loss before income tax benefit		<u>(1,169,846)</u>	<u>(893,219)</u>
Income tax benefit		-	-
Loss for the period		<u><u>(1,169,846)</u></u>	<u><u>(893,219)</u></u>
 Other comprehensive income			
Exchange differences arising on translation of foreign controlled subsidiary		14,613	29,822
Total comprehensive income / (loss) for the period		<u><u>(1,155,233)</u></u>	<u><u>(863,397)</u></u>
 Loss attributable to:			
Members of the parent entity		(1,116,055)	(847,324)
Non-controlling interest		(53,791)	(45,895)
		<u><u>(1,169,846)</u></u>	<u><u>(893,219)</u></u>
 Total comprehensive income / (loss) attributable to:			
Members of the parent entity		(1,098,415)	(831,697)
Non-controlling interest		(56,818)	(31,700)
		<u><u>(1,155,233)</u></u>	<u><u>(863,397)</u></u>
 Earnings per share			
Basic earnings per share (cents)		(0.55)	(0.47)
Diluted earnings per share (cents)		(0.55)	(0.45)

The accompanying notes form part of these financial statements.

**Phoslock Water Solutions Limited
and Controlled Entities
ABN 88 099 555 290
Interim Financial Report
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2010**

	Note	Consolidated Group	
		31.12.2010	30.06.2010
		\$	\$
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents		634,306	462,883
Trade and other receivables		1,372,340	972,718
Inventories		1,058,775	1,138,302
Other current assets		21,577	68,425
TOTAL CURRENT ASSETS		3,086,998	2,642,328
NON-CURRENT ASSETS			
Property, plant and equipment		223,560	322,085
Intangible assets		2,261,465	2,443,042
TOTAL NON-CURRENT ASSETS		2,485,025	2,765,127
TOTAL ASSETS		5,572,023	5,407,455
CURRENT LIABILITIES			
Trade and other payables		316,944	364,664
Financial liabilities		16,642	17,593
Short-term provisions		136,352	118,255
TOTAL CURRENT LIABILITIES		469,938	500,512
NON-CURRENT LIABILITIES			
Financial liabilities		164,063	130,977
Other long-term provisions		83,376	72,458
TOTAL NON-CURRENT LIABILITIES		247,439	203,435
TOTAL LIABILITIES		717,377	703,947
NET ASSETS		4,854,646	4,703,508
EQUITY			
Issued capital	4	30,589,301	29,282,930
Reserves		1,221,663	1,204,023
Accumulated losses		(26,828,917)	(25,712,862)
Owners interest		4,982,047	4,774,091
Non-controlling interest		(127,401)	(70,583)
TOTAL EQUITY		4,854,646	4,703,508

The accompanying notes form part of these financial statements.

**Phoslock Water Solutions Limited
and Controlled Entities
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Interim Financial Report
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE HALF-YEAR ENDED 31 DECEMBER 2010**

Note	Issued Capital Ordinary	Option reserves	Foreign currency translation reserves	Non- controlling Interests	Accumulated losses	Total	
	\$	\$	\$	\$	\$	\$	
Balance at 1.7.2009	26,854,353	1,006,753	214,186	28,912	(23,935,377)	4,168,827	
Total comprehensive income							
Net loss for the period	-	-	-	(45,895)	(847,324)	(893,219)	
Other comprehensive income - Exchange differences arising on translation of foreign controlled subsidiaries	-	-	15,627	14,195	-	29,822	
Total comprehensive income	-	-	15,627	(31,700)	(847,324)	(863,397)	
Transactions with owners in their capacity as owners							
Shares issued during the period	2,466,131	-	-	-	-	2,466,131	
Transaction costs	(37,554)	-	-	-	-	(37,554)	
Options expense	-	-	-	-	-	-	
Total transactions with owners in their capacity as owners	2,428,577	-	-	-	-	2,428,577	
Balance at 31.12.2009	29,282,930	1,006,753	229,813	(2,788)	(24,782,701)	5,734,007	
Balance at 1.7.2010	29,282,930	1,006,753	197,270	(70,583)	(25,712,862)	4,703,508	
Total comprehensive income							
Net loss for the period	-	-	-	(53,791)	(1,116,055)	(1,169,846)	
Other comprehensive income - Exchange differences arising on translation of foreign controlled subsidiaries	-	-	17,640	(3,027)	-	14,613	
Total comprehensive income	-	-	17,640	(56,818)	(1,116,055)	(1,155,233)	
Transactions with owners in their capacity as owners							
Shares issued during the period	1,320,000	-	-	-	-	1,320,000	
Transaction costs	(13,629)	-	-	-	-	(13,629)	
Total transactions with owners in their capacity as owners	1,306,371	-	-	-	-	1,306,371	
Balance at 31.12.2010	4	30,589,301	1,006,753	214,910	(127,401)	(26,828,917)	4,854,646

The accompanying notes form part of these financial statements.

**Phoslock Water Solutions Limited
and Controlled Entities
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Interim Financial Report
CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE
HALF-YEAR ENDED 31 DECEMBER 2010**

	Consolidated Group	
	31.12.2010	31.12.2009
	\$	\$
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	446,351	750,721
Payments to suppliers and employees	(1,468,741)	(1,601,770)
Interest received	17,138	7,404
Finance costs	(20,579)	(22,402)
Net cash (used in)/provided by operating activities	<u>(1,025,831)</u>	<u>(866,047)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of property, plant & equipment	24,997	3,591
Purchase of other non-current assets	-	(13,459)
Purchase of property, plant & equipment	(3,237)	(7,515)
Net cash used in investing activities	<u>21,760</u>	<u>(17,383)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issue of shares (net of transactions costs)	1,175,000	1,330,575
Proceeds from borrowings (net)	32,135	27,456
Transaction costs	(13,629)	(37,554)
Net cash used in/(provided by) financing activities	<u>1,193,506</u>	<u>1,320,477</u>
Net increase/(decrease) in cash and cash equivalents held	189,435	437,047
Cash and cash equivalents at beginning of period	462,883	527,148
Effects of exchange rates on cash holdings in foreign currencies	(18,012)	(6,529)
Cash and cash equivalents at end of period	<u><u>634,306</u></u>	<u><u>957,666</u></u>

The accompanying notes form part of these financial statements.

**Phoslock Water Solutions Limited
and Controlled Entities
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Interim Financial Report**

NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

NOTE 1: BASIS OF PREPARATION

These general purpose financial statements for the interim half-year reporting period ended 31 December 2010 have been prepared in accordance with requirements of the *Corporations Act 2001* and Australian Accounting Standards including AASB 134: Interim Financial Reporting. Compliance with Australian Accounting Standards ensures that the financial statements and notes also comply with International Financial Reporting Standards.

This interim financial report is intended to provide users with an update on the latest annual financial statements of Phoslock Water Solutions Ltd and its controlled entities (the Group). As such, it does not contain information that represents relatively insignificant changes occurring during the half-year within the Group. It is therefore recommended that this financial report be read in conjunction with the annual financial statements of the Group for the year ended 30 June 2010, together with any public announcements made during the half-year.

The same accounting policies and methods of computation have been followed in this interim financial report as were applied in the most recent annual financial statements except for the adoption of the following new and revised Accounting Standards.

The half year financial statements were authorised for issue by the board of directors on 27 February 2011.

**Phoslock Water Solutions Limited
and Controlled Entities
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NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

	Consolidated Group	
	31.12.2010	31.12.2009
	\$	\$
NOTE 2: REVENUE		
Sales revenue	361,969	916,062
Other income		
Interest received	14,428	7,404
Net gain on disposal of fixed assets	13,817	-
Export development and R&D grants	298,950	139,452
Total other income	327,195	146,856
Total revenue	689,164	1,062,918

NOTE 3: OPERATING SEGMENTS

Segment Information

Identification of reportable segments

The group has identified its operating segments based on the internal reports that are reviewed and used by the board of directors (chief operating decision makers) in assessing performance and determining the allocation of resources.

The group is managed primarily on the basis of geographical areas – Australia/NZ, Europe/UK, North America and Asia. The Group's operations inherently have similar profiles and performance assessment criteria.

Types of products and services by segment

The sale of Phoslock granules and application services and lake restoration consulting services is the main business of the Group. These products and services are provided on a geographical basis with offices and representation in each of the company's four key geographical areas - Australia/NZ, Europe/UK, North America and Asia.

Basis of accounting for purposes of reporting by operating segments

Accounting policies adopted

Unless stated otherwise, all amounts reported to the Board of Directors as the chief decision maker with respect to operating segments are determined in accordance with accounting policies that are consistent to those adopted in the annual financial statements of the Group.

Inter-segment transactions

An internally determined transfer price is set for all inter-entity sales. This price is based on what would be realised in the event the sale was made to an external party at arm's-length. All such transactions are eliminated on consolidation for the Groups financial statements.

Corporate charges are allocated to reporting segments based on the segments' overall proportion of revenue generation within the Group. The Board of Directors believes this is representative of likely consumption of head office expenditure that should be used in assessing segment performance and cost recoveries.

Inter-segment loans payable and receivable are initially recognised at the consideration received net of transaction costs and then revalued to the exchange rate used at the end of the current accounting period.

**Phoslock Water Solutions Limited
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Interim Financial Report**

NOTE 3: OPERATING SEGMENTS

Segment assets

Where an asset is used across multiple segments, the asset is allocated to the segment that receives the majority of economic value from the asset. In the majority of instances, segment assets are clearly identifiable on the basis of their nature and physical location.

Unless indicated otherwise in the segment assets note, investments in financial assets, deferred tax assets and intangible assets have not been allocated to operating segments.

Segment liabilities

Liabilities are allocated to segments where there is direct nexus between the incurrence of the liability and the operations of the segment. Borrowings and tax liabilities are generally considered to relate to the Group as a whole and are not allocated. Segment liabilities include trade and other payables and certain direct borrowings.

Unallocated items

The following items of revenue, expense, assets and liabilities are not allocated to operating segments as they are not considered part of the core operations of any segment:

- net gains on disposal of available-for-sale investments;
- income tax expense;
- deferred tax assets and liabilities;
- intangible assets;

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NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

NOTE 3: OPERATING SEGMENTS (CONT'D)

	(i) Segment performance						
	Australia/NZ	Europe/UK	North America	Asia	Total	Eliminations	Total
	\$	\$	\$	\$	\$	\$	\$
Six months ended 31.12.2010							
Revenue							
External sales	160,974	128,515	35,200	37,280	361,969	-	361,969
Inter-segment sales	1,642	-	-	64,208	65,850	(65,850)	-
Other revenue	312,767	-	-	-	312,767		312,767
Total segment revenue	475,383	128,515	35,200	101,488	740,586	(65,850)	674,736
<i>Reconciliation of segment revenue to group revenue</i>							
Unallocated interest income							14,428
Total group revenue							689,164
Segment loss before income tax	(349,557)	(190,528)	(40,000)	(100,817)	(680,902)	-	(680,902)
<i>Reconciliation of segment result to group net profit/(loss) before tax</i>							
Amounts not included in segment result but reviewed by the Board:							
• Depreciation and amortisation	(187,836)	(680)	-	(31,727)	(220,243)	-	(220,243)
Unallocated items:							
• Corporate charges							(248,122)
• Finance costs							(20,579)
Loss before income tax from continuing operations							(1,169,846)

**Phoslock Water Solutions Limited
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Interim Financial Report**

NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

NOTE 3: OPERATING SEGMENTS (CONT'D)

	(i) Segment performance						
	Australia/NZ	Europe/UK	North America	Asia	Total	Eliminations	Total
	\$	\$	\$	\$	\$	\$	\$
Six months ended 31.12.2009							
Revenue							
External sales	89,921	496,577	309,814	19,750	916,062	-	916,062
Inter-segment sales	35,848	-	-	224,887	260,735	(260,735)	-
Other revenue	139,452	31	-	-	31	-	139,483
Total segment revenue	265,221	496,608	309,814	244,637	1,316,280	(260,735)	1,055,545
<i>45 Reconciliation of segment revenue to group revenue</i>							
Unallocated interest income							7,373
Total group revenue							1,062,918
Segment loss before tax	(342,074)	(121,687)	61,500	(5,448)	(407,709)	-	(407,709)
<i>Reconciliation of segment result to group net profit/(loss) before tax</i>							
Amounts not included in segment result but reviewed by the Board:							
• Depreciation and amortisation	(200,944)	(947)	-	(43,125)	(245,016)	-	(245,016)
Unallocated items:							
• Corporate charges							(196,262)
• Finance costs							(44,232)
Loss before income tax from continuing operations							(893,219)

**Phoslock Water Solutions Limited
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(ii) Segment assets

	Australia/NZ	Europe/UK	North America	Asia	Total	Elimination	Total
	\$	\$	\$	\$	\$	\$	\$
31.12.2010							
Segment assets	3,091,922	68,280	-	474,442	3,634,644	(324,086)	3,310,558
Unallocated assets:							
• Intangibles					2,261,465	-	2,261,465
Total group assets from continuing operations					5,896,109	(324,086)	5,572,023
30.6.2010							
Segment assets	3,124,108	80,247	-	527,212	3,731,567	(767,154)	2,964,413
Unallocated assets:							
• Intangibles					2,443,042	-	2,443,042
Total group assets from continuing operations					6,174,609	-	5,407,455

(iii)

Major customers

The Group has a number of customers to which it provides both products and services. The Group's largest external customer accounts 36% of external sales revenue (2009; 41%). The next most significant client accounts for 29% (2009; 27%) of external sales revenue.

**Phoslock Water Solutions Limited
and Controlled Entities
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Interim Financial Report**

NOTES TO THE FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 31 DECEMBER 2010

NOTE 4: SHARE CAPITAL

	Consolidated Group			
	31.12.2010		30.6.2010	
	Number	\$	Number	\$
At the beginning of the period	186,530,580	29,282,930	167,805,462	26,854,353
Shares issued during the period:				
10 August 2009	-	-	5,593,884	615,326
10 August 2009	-	-	357,041	53,555
18 August 2009	-	-	5,555,556	1,000,000
25 August 2009	-	-	4,988,637	548,750
22 October 2009	-	-	2,000,000	220,000
30 November 2009	-	-	230,000	28,500
6 September 2010	22,000,000	1,100,000	-	-
24 September 2010	1,500,000	75,000	-	-
30 November 2010	2,900,000	145,000	-	-
Transaction costs		(13,629)	-	(37,554)
Balance at end of reporting period	<u>212,930,580</u>	<u>30,589,301</u>	<u>186,530,580</u>	<u>29,282,930</u>

NOTE 5: CONTINGENT LIABILITIES

There has been no change in contingent liabilities since the last annual reporting date.

NOTE 6: EVENTS SUBSEQUENT TO REPORTING DATE

At the date of this report the company has entered into factoring arrangements (sale of debtor invoices to third parties) totalling \$557,842. The debtor invoices are for customers of the Phoslock Group. The company is liable to the lender for any amounts which become due and payable as a result of a default on behalf of the debtor. The company is unable to estimate any amounts which may become payable under these arrangements

There have been no material events subsequent to the reporting date which have had a material effect on the financial position of the company.

NOTE 7: DIVIDENDS PAID OR PAYABLE

No dividends have been paid or declared during the period (2009 \$nil).

**Phoslock Water Solutions Limited
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NOTE 8: GOING CONCERN

The consolidated entity recorded an operating loss after eliminating non-controlling interests of \$1,116,055 for the six months ended 31 December 2010 (2009:\$847,324) and at that date had accumulated losses of \$26,828,917 (2010: \$25,712,862). The consolidated entity had Net Assets totalling \$4,854,646 at 31 December 2010, including intangibles of \$2,261,465 (2010: \$4,703,508, and \$2,443,042).

At the date this report was authorised for issue the consolidated entity had cash reserves of \$812,000 from which to fund future operations.

The directors are satisfied that it is appropriate to report that the company as a going concern based on the following reasons:

- (i) the company's ability to increase sales from current levels in key markets (Australia, Europe and UK, North America, China and other parts of Asia);
- (ii) the ability of management to control costs;
- (iii) the company's ability to raise additional funds from the issue of new shares if required.

In support of ongoing liquidity of the group, management has prepared forecasts for the 12 month period ended 28 February 2012. These forecasts assume that the company will be successful in the following during this period:

- Sales of a minimum of \$5.3 mil;
- Purchase approx \$1.4 million of new inventory from Chinese Joint Venture;
- Operating costs being maintained at a consistent level of \$200,000 per month;
- Approval and receipt of approx \$0.48m of Export Development and Research & Development Grants relating to FY2008/09 and FY2009/10. Three of the four grant applications have been lodged and are currently being processed;
- Settlement of the balance of the Volclay receivable in relation to the sale of the Miles bentonite mine of \$323,000
- Receipt of amounts owing from executives in respect of the share placements in November 2010 of \$142,500.

If the above is achieved the company will have a consolidated cash balance of approx \$2.3 million as at 28 February 2012.

The ongoing financial viability of the Company and its ability to continue as a going concern and realise its assets, including intangibles, in the ordinary course of business is heavily dependent on the Company's ability to convert projects in the current pipeline into sales as detailed above, and its ability to achieve the underlying assumptions in the forecasts as outlined above.

Phoslock Water Solutions Limited
and Controlled Entities
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DIRECTORS' DECLARATION

The directors of the company declare that:

1. The financial statements and notes, as set out on pages 5 to 16 are in accordance with the *Corporations Act 2001*, including:
 - a. complying with Accounting Standard AASB 134: Interim Financial Reporting; and
 - b. giving a true and fair view of the consolidated entity's financial position as at 31 December 2010 and of its performance for the half-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.

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



Director

Robert Schuitema

Dated this 27th day of February, 2011

Independent Auditor's Review Report

To the members of Phoslock Water Solutions Limited

Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Phoslock Water Solutions Limited and Controlled Entities (the Consolidated Entity), which comprises the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the half-year ended on that date, notes comprising a summary of significant accounting policies and other selected explanatory information and the directors' declaration.

Directors' Responsibility for the Half-Year Financial Report

The directors of the company are responsible for the preparation of the half-year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such control as the directors determine is necessary to enable the preparation of the half-year financial report that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at 31 December 2010 and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Phoslock Water Solutions Limited, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

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

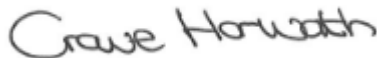
Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Phoslock Water Solutions Limited is not in accordance with the *Corporations Act 2001* including:

- (a) giving a true and fair view of the consolidated entity's financial position as at 31 December 2010 and of its performance for the half-year ended on that date; and
- (b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and *Corporations Regulations 2001*.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 8 in the financial statements which indicates that the company incurred a net loss of \$1,155,233 for the period ended 31 December 2010, and as of that date, the company had accumulated losses of \$26,828,917. Note 9 also indicates that at the date of this report the company had cash reserves of \$812,000. These conditions, along with the other matters as set forth in Note 9, indicate the existence of a material uncertainty which may cast significant doubt about the company's ability to continue as a going concern and therefore, the company may be unable to realise its assets and discharge its liabilities in the normal course of business.

**CROWE HORWATH****VANESSA DE WAAL****Principal****Signed at Brisbane, 27 February 2011**