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Company announcement

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Chairmans Address – Jan 2024 EGM

Shareholders have been asked to attend today's meeting to consider the future of the Company.

The resolutions put before shareholders offer two choices: Resolutions 1 and 2 provide for selling the Company's assets, paying all creditors in full, distributing the balance of cash to shareholders, and winding up the various corporate entities. This option carries the unanimous recommendation of your Board of Directors.

Alternatively, Resolutions 3, 4 and 5 have been proposed by some shareholders to continue trading and to do this under a new Board of Directors, new management and new strategy.

Let me review for a moment how the Company arrived at this situation.

The Directors, like many Shareholders, continue to believe in the potential of Phoslock's offering. However, despite best efforts, the Company has unfortunately not been able to convert this potential into profitable operating performance.

Shareholders know that Phoslock is an Australian product invented by CSIRO, that has successfully been applied in over 320 projects around the world to trap phosphates and improve the water quality of nutrient polluted lakes and other water bodies.

Sustainable fresh water is one of the planet's biggest challenges and PET has a proven and effective solution to deal with one of its major pollutants. Nutrient enriched water bodies are often the cause of significant algal growth. Algae polluted water bodies also produce methane gas which is a major contributor to climate change. Phoslock, by removing the food source phosphorus for those algae, can play a significant role in managing this issue.

PET has demonstrated that it is internationally competitive on several major projects. Its successes have included cleaning up the Serpentine Lake in Hyde Park, London, for the Olympics, and restoring to health the largest freshwater lake in Rotterdam, in the Netherlands.

In 2017, under a previous Board and management team, the Company ventured into China. It appointed a Chinese Deputy Chairman, a Chinese non-executive director and local staff. This generated significant optimism. Reports from China about rising sales and future opportunities were released to the market. The share price rose to an all time high of $1.45 in the winter of 2019. At the same time KPMG, the Company's auditors at the time, presented through its Australian and Chinese offices, unqualified audit opinions to the year ended Dec 2019.

The China venture ended disastrously. In their new roles as CEO and CFO, Lachlan McKinnon and Matthew Parker, who joined the Company in the 1st half of 2020, quickly discovered what appeared to be instances of widespread fraud, falsified accounting, bribery and corruption, bogus sales, breaches of Chinese and Australian laws, irregular tax compliance, and extensive conflicts of interest and self-dealing.

Further, after a deep dive into the Company's so-called China 'sales', it was discovered that a significant majority of sales were not of the Phoslock product at all. In some instances, non Phoslock products such as bacteria's, zeolites, water blankets and aeration machines were sourced by companies separately controlled by the appointed Chinese directors who then sold them to PET at a significant mark up. PET then on sold or applied these products to companies such as BHZQ which the same Chinese directors sat on the Board of, or had effective control over.

This lead to the Company's shares being suspended from trading on the ASX, resignation of its auditors, KPMG, who had been the Company's auditors in both China and Australia for three years, the termination of staff, a restatement of the Company's accounts, the self-reporting to the Australian Federal Police which has resulted in a long and extensive investigation by both AFP and ASIC - both of which remain ongoing.

After its ill-fated China venture and the resulting issues were exposed, the three new Directors agreed to join the Board because they believed this Australian company deserved to succeed and were committed to addressing the issues and placing appropriate process and governance standards in place.

The new Board, along with the new CEO and CFO, understood the enormous task ahead but we set about tackling the long list of challenges with determination and persistence.

The legacy issues the Company was burdened with left management with an ongoing drain on its financial resources. Nearly $10 million has been spent to date dealing with these matters, some of which are ongoing. Dealing with these legacy issues also presented a challenge for a small management team which was at the same time developing and implementing a new global sales strategy in a post Covid environment.

Both Lachie and Matt joined the Company unaware that serious issues existed. When these issues surfaced, they both stayed the course and worked with the refreshed Board to address these issues in what proved to be a stressful and demanding few years.

The Board is deeply grateful for their dedication, enthusiasm and persistence on behalf of shareholders in the face of daunting challenges.

The team oversaw the replacement of KPMG as Company auditors, and replaced KPMG with Shine Wing. This resulted in a major project to restore the integrity of the Company's accounts, lead by the CFO Matthew Parker. This took approximately 23 months to complete with a significant cost of legal and forensic accounting, further exacerbating the drain on the Company's financial resources.

We are grateful to Shine Wing for their professional help and thoroughness without which restoration of the Company's accounts to the satisfaction of the ASX would not have been possible.

With the integrity of its accounts restored, PET was then positioned to work with the ASX to allow its shares to trade again. This occurred in September 2022.

Given the serious matters of concern that it had identified under prior management in China and the disclosures it was obliged to make under Australian law, under the previous board the Company determined to self- report to the Australian Federal Police and enter into an investigation cooperation agreement. This resulted in an extensive and ongoing investigation of past dealings that required the Company to expend very significant management time and legal fees.

With regard to these legacy issues, the Company has no control over the length of the investigations and what, if any, course of action the AFP or ASIC may ultimately decide to pursue. Subject to any agreed position as to discounts under the investigation cooperation agreement, any fines imposed could be significant and remain unknown and unquantifiable contingent liabilities. The potential fines relating to each offence are themselves significant, and there is the potential for regulators to commence proceedings for multiple offences, and to seek orders under applicable proceeds of crime legislation. In addition, the likely costs relating to responding to any such proceedings would also be significant. This serious legacy issue poses a significant obstacle to raising more capital to support the business.

There are also potential liabilities in China for breaches of local laws, which may be progressed at some stage in the future.

The international sales strategy was redesigned by the CEO, refocused on high value opportunities, and diversified for a broader range of applications in mining, septic tank treatments and privately owned water bodies.

Recognising that the Company only offered a single product for standing water with Phoslock, he addressed the urgent strategic need for a complementary product to deal with flowing water. He secured Phosflow in the US to add to the Company's product offering and marketed this along with its standing water product. There is much interest in Phosflow and trials are underway with customers around the world. But despite positive feedback, this has not yet resulted in any significant sales revenues.

Shareholders are aware that remediating public water bodies has always involved a long sales cycle for the Company. Despite hundreds of successful applications, and many supportive scientific studies and papers around the world, it is a time-consuming process to make customers comfortable that the product is the appropriate option for addressing remediation issues in the water bodies they manage and the time-lines involved in trialling the product, negotiating application contracts and then relying on our customers – often government authorities – to approve funding for, and commence, the projects.

Unfortunately, COVID caused an extended delay in sales efforts as many municipalities and governmental bodies were forced to reprioritise their stretched budgets to deal with the challenges of COVID and its aftermath. COVID also prevented the CEO from travelling overseas to pursue customers and develop projects~~.~~ , and local sales staff were also severely restricted in their travel as well.

As part of the legacy issues in China, Management inherited some $10 million of bad and doubtful legacy debts in China. After lengthy negotiations failed to yield results, the Company initiated legal proceedings in Chinese courts, all of which were successful. Management then set about trying to collect on those judgments and, through their its persistence over a 3 year period, has have successfully collected around 80% of the debts owing.

Management have worked hard to develop a pipeline of potentially significant projects around the world. The nature of these projects presents a difficult challenge in predicting those which will materialize, and when this will occur. To succeed, the Company needs a sustainable flow of projects sufficient to produce a profitable trajectory of revenues capable of funding its working capital needs and increased manufacturing capacity that will be required when the production capacity of the China factory is eventually exceeded.

Management also took steps to reduce costs. Significant annual cost savings were approved and implemented in 2023. Most of the Chinese sales team was terminated and a renewed focus was directed at Europe and North America. More flexible pricing was developed with potential customers to test to what extent this might be impeding sales.

The Board has supported those sales efforts, projections and cost saving measures, but has eventually come to the difficult conclusion that it could not form a reasonable level of confidence in the Company achieving a sustainable level of annual sales in the short to medium term that would be likely to produce profitable growth and financial viability without further capital injections.

The various alternatives for funding working capital and capital works in the future will require evidence of a substantial number of recurring and committed sales. Despite all best efforts to achieve this with a new sales team, including flexible pricing offers to customers, the Company has not managed to secure this.

Shareholders will recall that in the 9 years prior to the China venture in around 2017, the Company's annual revenues averaged around $1.3 million. Under new management, the Company achieved $6.3 million in revenues in 2021 and $3 million revenues in 2022 and, subject to audit verification, $3.1 million in 2023. However, these much improved sales numbers are insufficient to achieve the level of sustainable recurring sales that will be required to achieve profitability for shareholders.

As noted previously, the revenues reported during the China years were primarily related to sales of items other than Phoslock and were products and services sourced by, and sold to, related parties. In addition, of the Phoslock sales that were recorded, the vast majority included suspected bribes to win contracts, with Xingyun Lake being a good example.

Without a level of reasonable confidence that the Company can achieve a sustainable level of significant annual sales, the Board does not believe that it can offer shareholders a reasonable value proposition to invest more capital by way of a capital raise. That option has been tested in direct communications with some of our largest shareholders who were not supportive of another call on additional capital.

Many of the potential projects being pursued in the pipeline by our sales team are exciting, and some are substantial in size. However, there is insufficient evidence that enough of these can be converted into sales on an annual basis, and will commence in the short term, leaving no reasonable basis on which future revenues can be predicted with any level of confidence.

The Company's financial resources, significantly depleted by dealing with its legacy issues, will not be sufficient to fund the overheads of the business during the time it will take to see if enough of these opportunities come to fruition.

It is important to note that the Company's sales forecasts and cost projections – based on a range of assumptions – were independently reviewed by our auditors prior to our announcement in September last year that the 2023 first half accounts had been prepared on a non-going concern basis.

In summer of 2023 the Board engaged Resolute Advisory to explore all available options for raising capital or otherwise strengthening the Company's balance sheet. It became clear the Company's serious unquantifiable legacy issues presented a serious obstacle to any fundraising options.

The Board had to make the hard decision as to whether shareholders' funds were better spent trading on in the hope that prospective opportunities would materialize in time and volume sufficient to achieve a viable company. Or, whether the interests of shareholders were better served by having those funds returned to shareholders. This decision was not taken lightly. Your Board came to its decision after much careful analysis and discussion, and after considering independent external advice, and after testing the market.

After exploring various options for a sale of assets, mergers or joint ventures the best realistic option was to agree a sale to SePRO Corporation in the USA on the terms agreed in a sale agreement. That Sales Agreement is subject to shareholder approval which is before you today in Resolutions 1 and 2 and carry the unanimous recommendation of your Board.

If shareholders approve that sale, the Company expects that upon completion that consolidated cash reserves will be between $16.6 million and $16.8 million. The Company expects that its wind down costs, including the payment in full of all current liabilities and creditors will be between $4.3 million and $5.8 million, leaving a net cash amount of between $10.8 million and $12.5 million, or approximately 1.7 – 2.0 cents per share. I note that all estimates are approximate figures based on the best information currently available and are dependent on a range of factors including whether any contingent liabilities crystallise.

As the Notice of Meeting for today's meeting sets out, shareholders have been presented with an alternative option being proposed by certain requisitioning shareholders. That option proposes the Company trades on under a new Board of Directors and management and pursues a different strategy. To date, details of that alternative business plan have not been provided to the current Board or to shareholders.

This option is not supported by your Board.

Those shareholders have stated their case to shareholders in the notice of meeting and you will decide which course you wish to pursue. This is your company and as shareholders it is ultimately for you to decide what you believe is in your best interests. Your votes cast today will determine the future of the Company.

This announcement has been approved by the Managing Director and Chairman

Mr David Krasnostein AM
Chairman

Mr Lachlan McKinnon
Managing Director & CEO

Matthew Parker
Company Secretary

– end –

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About PET

Phoslock Environmental Technologies Limited (ASX: PET) specialises in water treatment products to remediate nutrient polluted fresh waterbodies including, lakes, rivers, canals, municipal and private ponds, recreational and drinking water reservoirs.

Headquartered in Melbourne, PET also has offices in Shanghai and the UK, sales resources in China,

ANZ, Europe and the US. PET also has registered entities in Canada, USA and Belgium, and manufacturing operations based in Changxing, China. PET is represented by licensees, distributors and agents in numerous other countries including HydroScience in Brazil.

Phoslock® is a proprietary and unique water treatment product that permanently binds excess phosphorus in the water column and sediments.

Phosflow is a proprietary and unique water remediation product that removes excess phosphorus in flowing water applications.

Phoslock is certified for use in drinking water in North America, Europe, Brazil, Australia, and China. Along with Phoslock, PET also supplies zeolites and specialised solutions that address water pollution issues.

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