

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED
ACN 092 708 364

FINANCIAL REPORT FOR THE FINANCIAL YEAR ENDED
31 DECEMBER 2011

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

CORPORATE DIRECTORY

Directors

Mr Fred Bart (Chairman)
Dr Ben Greene (Chief Executive Officer)
Mr Ian Dennis
Mr Mark Ureda
Lt Gen Peter Leahy AC
Mr Kevin Scully

Company Secretary

Mr Ian Dennis

Registered Office

Suite 2, Level 12
75 Elizabeth Street
Sydney NSW 2000
Australia

Telephone:- 612 9233 3915
Facsimile:- 612 9232 3411

Web site www.eos-aus.com

Share Registry

Computershare Investor Services Pty Limited
Level 3
60 Carrington Street
Sydney NSW 2000
Australia

GPO Box 7045
Sydney NSW 1115

Telephone:- 1300 855 080 or 613 9611 5711 outside Australia
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Auditors

Deloitte Touche Tohmatsu
Chartered Accountants
The Barrington
Level 10
10 Smith Street
Parramatta NSW 2150
Australia

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

REVIEW OF OPERATIONS

1. RESULTS FOR FULL-YEAR ENDING 31 DECEMBER 2011

The consolidated entity earned a net profit during the year of \$180,188 (2010: \$3,175,142) on revenues of \$32,775,391 (2010: \$33,828,658).

Net cash used by operating activities was \$3,778,311 (2010 - \$3,113,613 provided). As at 31 December 2011, the consolidated entity had cash of \$4,885,761 (2010 - \$8,088,355) of which \$496,296 (2010 - \$496,692) is restricted as it secures bank guarantees on existing contracts with local and overseas customers. The cash will become unrestricted when the contract is concluded or renegotiated.

2. REMOTE WEAPON SYSTEMS BUSINESS

Orders

Existing EOS customers for remote weapon systems continue to place new orders at levels consistent with recent years. At the issue date of this review the company is holding firm, funded and unfulfilled weapon system orders for over \$36 million.

Most of the current order backlog is for our most advanced R-600 model of remote weapon system which has now sold over 300 units. This product has been in production for more than 12 months and recent orders will see its production continue with regular monthly shipments to late in 2014.

In June 2011 EOS executed and announced agreements to supply remote weapon systems to a military customer which had not previously purchased remote weapon systems from any source. The program requirement is for 400 weapon systems over approximately 5 years from 2013, subject to annual budget appropriations and performance reviews.

Initial deliveries of four units under this contract have been made and accepted, and these delivered units are being used for training and full testing for compliance with technical and performance specifications. Those reviews will be completed in mid-2012 and subject to satisfactory product performance the program funding will be released in annual blocks from late 2012.

Business Model Adjustments

During 2011 EOS adjusted its business model in this sector to allocate more production to offshore partners. This adjustment allows EOS to allocate more production into the customer countries, as increasingly required by statutes in these countries. It will also provide an improved hedge against the expected long-term rise in the exchange value of the Australian dollar.

EOS' arrangements for closer production relationship with Northrop Grumman in the USA have already been announced, and licensed production of significant parts of EOS remote weapon systems is being negotiated in other customer countries.

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REVIEW OF OPERATIONS (cont)

The announced relocation of US production facilities to Huntsville (AL) is under way and will be completed in mid-2012. The company expects to achieve cost savings on all remote weapon system programs through this initiative.

New Technology and Products

Since 2008 EOS has been developing a significant new weapon system at its own expense, towards a 2013 production target for new customer requirements. In 2011 the likelihood of success of the technical developments was increased significantly through full prototype testing and initial firing trials. At the same time customer responses confirmed funding and contract awards were still highly probable.

EOS also increased investment in sensor development for several customer-requested upgrades for current products, and for potential CROWS requirements. The new products include thermal imagers and laser rangefinders. These will reach production from late in 2013 and are expected to increase sales.

EOS thermal imagers were purchased for trial use in television broadcast of cricket, where the camera can discern which surface has been touched by the ball. Industrial security applications for EOS' ruggedized thermal cameras at sea are increasing.

CROWS Developments

EOS is teamed with Northrop Grumman Corporation ("NGC") to meet the US Army's requirements for common remotely operated weapon stations ("CROWS") with NGC to act as prime contractor and EOS as first-tier subcontractor to NGC.

In January 2012 the Army released its "invitation to tender" documents for the CROWS program, with responses due by 23 March 2012. EOS has supported the preparation of a response to this invitation to tender which was lodged by NGC on 23 March 2012.

The contract award for CROWS is expected by September 2012. This is approximately 12 months later than expected and this delay has caused additional cost to all potential bidders, including EOS.

Financial Performance

The remote weapon systems business caused a drag on the company's financial performance in 2011, arising from the following factors:

- Inventory impairment of \$1.6m during the year relating to a provision for obsolescence for EOS parts inventory .
- Increased marketing and tender costs of approximately \$450,000 relating to delays in the US Army releasing the CROWS tender documents, from mid-2011 to early in 2012. CROWS-related outlays will return to normal levels through 2012 .
- Increased product engineering and development expenses of approximately \$650,000 for sensor and remote weapon products approaching production in 2013. Provided

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REVIEW OF OPERATIONS (cont)

customer interest in these new products remains strong, this activity will not decline in 2012.

- In the second half of 2011, delays of approximately 5 weeks in completion and shipping of a \$24 million order, deliverable over 15 months from mid-2011. This resulted in a reduction in revenue of over \$2 million from expected levels. Production has resumed at normal output in 2012.

3. SPACE BUSINESS

Space Technology

The EOS collaboration with the Australian National University (ANU) for the development of adaptive optics (AO) technology is meeting or exceeding technical objectives. Next-generation telescopes will require AO technology at up to \$70 million per telescope, and there are several such projects already under way. ANU and EOS expect to compete for commercial contracts to provide AO for new telescope programs as they are required from around 2013.

EOS continues to work in collaboration with international partners to optimise for Australian conditions and requirements synthetic aperture radar (“SAR”) satellite systems and other space surveillance capabilities. EOS expects Australia to outlay substantial sums on these capabilities over the next 3-5 years, and is positioning to meet these requirements in its domestic market.

Space Information

Space operations contracts for provision of space data to the Australian Government from two separate optical tracking sites in Australia continue to operate to expectation. During this period EOS received high ratings for performance and bonus payments under these long-term contracts.

EOS continues to refine its space sensors under \$7.5m of customer-funded awards. These developments will be completed in 2013. The company is unaware of any sensor development from any other source that can better complement existing space surveillance infrastructure to improve the safety and cost-effectiveness of space exploitation.

In 2011 the company provided sensor performance data to key international partners, and is presently negotiating several memoranda or agreements towards establishing business ventures with those partners for commercial exploitation of EOS space sensors.

Financial Performance

All key metrics for space business improved in 2011 such that the net loss of this sector fell 54% to \$0.974 million at the same time as strategically important space data activities increased 48% to \$3.2 million of activity.

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REVIEW OF OPERATIONS (cont)

4. SUMMARY AND OUTLOOK

During 2012 the company's remote weapons systems business financial performance is expected to recover with additional orders. The current order book is strong and all orders are for mature products with low production risk.

EOS will continue to invest in CROWS activities and new product development where customers are already committed to the intended product.

EOS space business is expected to be stable in 2012 after changes in 2011 completing the transfer of emphasis from telescope systems to space information and telescope sub-systems (adaptive optics). The improved (reduced) drain on company finances for funding the space business towards commercial maturity is expected to be sustained in 2012. This improvement in the sector's financial performance is underwritten by stronger customer contracts for space data and sensors.

In both space and remote weapon systems, activity in Europe subsided significantly over 2011 and this is not expected to recover in 2012. EOS operations in Germany have been reduced to core technology support for specific products.

EOS continues to pursue its key strategic objectives in space and remote weapon systems while performing commercial contracts that better position EOS resources to execute those objective programs when captured.

Ben Greene
Chief Executive Officer
30 March 2012

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DIRECTORS REPORT

The directors of Electro Optic Systems Holdings Limited submit herewith the annual financial report of the company for the year ended 31 December 2011. In order to comply with the provisions of the Corporations Act 2001, the directors report as follows:

Directors

The names and particulars of the directors of the company during or since the end of the financial year are:

Name	Particulars
Fred Bart	Chairman (Age 57). A director since 8 May 2000. He has been Chairman and Director of numerous private companies since 1980, specialising in manufacturing, property and technology. He is a member of the Australian Institute of Company Directors and is a member of the Audit Committee and Remuneration Committee.
Dr Ben Greene	BE (Hons), Phd in Applied Physics (Age 60) is the Chief Executive Officer of Electro Optic Systems. Dr Greene was involved in the formation of Electro Optic Systems. He is widely published in the subject areas of laser tracking, space geodesy, quantum physics, satellite design, laser remote sensing, and the metrology of time, and is currently regarded as a world leader in these fields. Dr Greene is a member of Australia's Space Industry Innovation Council. Appointed to the Board on 11 April 2002.
Ian Dennis	BA, C.A. (Age 54) is a Chartered Accountant with experience as director and secretary in various public listed companies and unlisted technology companies in Australia and overseas. He has been involved in the investment banking industry and stockbroking industry for the past twenty five years. Prior to that, he was with KPMG, Chartered Accountants in Sydney. Appointed to the Board on 8 May 2000. He is a member of the Australian Institute of Company Directors and is a member of the Audit Committee and Remuneration Committee. He is also company secretary of Electro Optic Systems Holdings Limited.

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DIRECTORS' REPORT (cont)

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|-----------------------|---|
| Mark Ureda | Non-executive director (Age 57). Appointed to the Board on 28 April 2005. Mark was vice president, Strategy and Technology for Northrop Grumman Corporation, a global defence company until August 2010. Mark is now Vice President and General Manager of the Harman Professional Loudspeaker Group. Mark received a bachelor's degree in Engineering from the University of California at Los Angeles, a master's degree in Acoustics from the Pennsylvania State University and a master's degree in Finance from the UCLA Graduate School of Management. |
| Lt Gen Peter Leahy AC | Non-executive director (Age 59). Appointed to the Board on 4 May 2009. Peter Leahy AC retired from the Australian Army in July 2008 as a Lieutenant General in the position of Chief of Army. As well as being Chairman of the Army's Advisory Committee he was also a Member of the Defence Committee, the Chiefs of Service Committee, the Council of the Australian War Memorial and the Board of Defence Housing Australia.
Among his qualification he holds a BA (Military Studies), a Master of Military Arts and Science and is a member of the Australian Institute of Company Directors. In October 2008 he was appointed as a Professor and the foundation Director of the National Security Institute at the University of Canberra. He is a director of both Codan Limited and the Kokoda Foundation and a member of the Defence South Australia Advisory Board. |
| Kevin Scully | Non-executive director (Age 54). Appointed to the Board on 19 September 2011. Kevin Scully has more than 26 years of experience in equities research and analysis, corporate advisory and related matters, having worked for more than 12 years in various positions such as the head of research and director of Schrodgers and the Netresearch group (which he founded). Kevin is an advisor to two regulatory authorities of the Singaporean Government (Commercial Affairs Department and the Monetary Authority of Singapore) since 1999. |

Apart from Kevin Scully who was appointed on 19 September 2011, the above named directors held office during and since the end of the financial year.

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DIRECTORS' REPORT (cont)

Directorships of other listed companies

Directorships of other listed companies held by directors in the three years immediately before the end of the financial year were as follows:

Name	Company	Period of directorship
Fred Bart	Genetic Technologies Limited	26 October 1996 to 25 November 2009
	Gtech International Resources Limited	7 November 1996 to 25 November 2009
	Audio Pixels Holdings Limited	5 September 2000 to date
Ian Dennis	Audio Pixels Holdings Limited	5 September 2000 to date
Lt Gen Peter Leahy AC	Codan Limited	19 September 2008 to date
Kevin Scully	PNE Micron Holding Limited	11 April 2011 to date

Principal activities

The principal activities of the consolidated entity are in the space systems, space surveillance and defence products business.

The company is listed on the Australian Securities Exchange.

Review of operations

A detailed review of operations is included on pages 3 to 6 of this financial report.

Changes to the state of affairs

There was no significant changes in the state of affairs of the consolidated entity that occurred during the financial period.

Subsequent events

Since the end of the financial year, the Group has repaid the two secured promissory notes detailed in Note 13. The Chief Financial Officer, Mr John Palisi resigned on 3 February 2012 and has been replaced by Mr Scott Lamond as Acting Chief Financial Officer. The Common Remotely Operated Weapons Stations ("CROWS") bid for the US Army was lodged by Northrop Grumman Corporation ("NGC") on 23 March 2012 with NGC as the prime contractor and EOS as a first tier subcontractor. Apart from these items there has not been any matter or circumstance that has arisen since the end of the financial year, that has significantly affected or may significantly affect the operations of the consolidated entity, the results of those operations or the state of affairs of the consolidated entity in future financial years.

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DIRECTORS' REPORT (cont)

Future developments

The company will continue to operate in the space systems, space surveillance and defence products business.

Further disclosure of information regarding likely developments in the operations of the consolidated entity in future financial years and the expected results of those operations is likely to result in unreasonable prejudice to the consolidated entity. Accordingly, this information has not been disclosed in this report.

Environmental Regulations

In the opinion of the directors the consolidated entity is in compliance with all applicable environmental legislation and regulations.

Dividends

The directors recommend that no dividend be paid and no amount has been paid or declared by way of dividend since the end of the previous financial year and up to the date of this report.

Share Options

Share options granted to directors and executives

During and since the end of the financial year no share options were granted to any directors of the company and consolidated entity as part of their remuneration. On 10 December 2009 the Company issued 1,800,000 options to staff including the executives listed in the Remuneration Report under the terms of the Employee Share Option Plan. Since these options were issued, 262,000 have been cancelled due to staff resignations leaving a balance currently outstanding of 1,538,000 options. These options have an exercise price of \$1.30 and are exercisable on or before 8 December 2013 and are subject to the normal vesting provisions under the Employee Share Option Plan. No options have been issued to executives since the end of the financial year.

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DIRECTORS' REPORT (cont)

Share options on issue at year end or exercised during the year

Details of unissued shares or interests under option are:

Issuing entity	Number of shares under option	Class of shares	Exercise price of option	Expiry date of options
Electro Optic Systems Holdings Limited	1,538,000	Ordinary	\$1.30	8 December 2013
	<u>1,538,000</u>			

1,564,800 Options issued to directors at an exercise price of \$1.95 lapsed on 31 May 2011.

Options issued to directors and executives during 2007 were issued with an exercise price set as a 25% premium to the weighted average market price for the quarter ended 31 March 2007. This price was approved by members at the Annual General Meeting on 31 May 2007. The holders of such options do not have the right, by virtue of the option, to participate in any share issue or interest issue of any other body corporate or registered scheme.

Options issued to executives and staff during 2009 were issued at an exercise price of \$1.30 determined by the directors. The holders of such options do not have the right, by virtue of the option, to participate in any share issue or interest issue of any other body corporate or registered scheme.

There were no shares or interests issued during the financial year as a result of exercise of an option.

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DIRECTORS' REPORT (cont)

Indemnification and Insurance of Officers and Auditors

During the financial year, the company paid a premium in respect of a contract insuring the Directors and Officers of the Company and any related body corporate against a liability incurred as such a Director or Officer to the extent permitted by the Corporations Act 2001. The contract of insurance prohibits disclosure of the nature of the coverage provided and the amount of the premium. The Company has agreed to indemnify the current Directors, Company Secretary and Executive Officers against all liabilities to other persons that may arise from their position as Directors or Officers of the Company and its controlled entities, except where to do so would be prohibited by law. The agreement stipulates that the Company will meet the full amount of any such liabilities, including costs and expenses.

The Company has not, during or since the financial year indemnified or agreed to indemnify an auditor of the company or of any related body corporate against any liability incurred as such an auditor.

Directors' meetings

The following table sets out the number of directors' meetings (including meetings of committees of directors) held during the financial year and the number of meetings attended by each director (while they were a director or committee member). During the financial year, 14 Board meetings, 2 audit committee meetings and 3 Remuneration committee meetings were held.

	Board of directors		Audit committee		Remuneration committee	
Directors	Held	Attended	Held	Attended	Held	Attended
Mr Fred Bart	14	13	2	2	3	3
Dr Ben Greene	14	14	-	-	-	-
Mr Ian Dennis	14	13	2	2	3	3
Mr Mark Ureda	14	13	-	-	-	-
Lt Gen Peter Leahy AC	14	14	2	2	3	3
Mr Kevin Scully	3	3	-	-	-	-

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DIRECTORS' REPORT (cont)

Directors' shareholdings

The following table sets out each Director's relevant interest in shares and options of the company or a related body corporate as at the date of this report.

Directors	Fully paid ordinary shares	Options
Mr Fred Bart	5,309,075	-
Dr Ben Greene	3,954,185	-
Mr Ian Dennis	170,050	-
Mr Mark Ureda	-	-
Lt Gen Peter Leahy AC	15,000	-
Mr Kevin Scully	-	-

Remuneration report (Audited)

The key management personnel of Electro Optic Systems Holdings Limited during the year were:

Mr Fred Bart (Chairman, Non executive director)

Dr Ben Greene (Chief Executive Officer and director)

Mr Ian Dennis (Non-executive director)

Mr Mark Ureda (Non-executive director)

Lt Gen Peter Leahy AC (Non-executive director)

Mr Kevin Scully (Non-executive director) – Commenced 19 September 2011

Mr Mark Bornholt (Chief Executive Officer of Defence Systems) – Commenced 21 March 2011

Mr Ron Thompson (Group General Manager) – retired 30 September 2011

Dr Craig Smith (Chief Executive Officer of EOS Space Systems Pty Limited)

Mr John Palisi (Chief Financial Officer – Electro Optic Systems Pty Limited) – resigned 3 February 2012

Mr Hugo Keyner (Chief Executive Officer EOS Technologies Inc)

This report outlines the remuneration arrangements in place for Directors and Executives of the Company.

The Directors are responsible for remuneration policies and packages applicable to the Board members and executives of the company. The Company has a separate Remuneration Committee. The broad remuneration policy is to ensure the remuneration package properly reflects the persons duties and responsibilities.

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

Remuneration structure

In accordance with best practice corporate governance, the structure of Non-Executive Director and senior manager remuneration is separate and distinct.

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, whilst incurring a cost which is acceptable to shareholders.

Structure

The Company's Constitution and the Australian Securities Exchange Listing Rules specify the aggregate remuneration of Non- Executive Directors shall be determined from time to time by a General Meeting of shareholders. An amount not exceeding the amount determined is then divided between the Directors as agreed. The latest determination was at the Annual General Meeting held on 11 April 2002, when shareholders approved a maximum aggregate remuneration of \$230,000 per year excluding options. The Board considers that in light of this level of fees, and the present situation of the Company, it is appropriate for options to be made available to Directors.

The amount of aggregate remuneration sought to be approved by shareholders, the manner in which it is apportioned amongst Directors, and the policy of granting options to Directors, are reviewed annually.

Each Non-Executive Director receives a fee for serving as a Director of the Company. No additional fees are paid to any Director for serving on a committee of the Board. A company associated with Mr Ian Dennis receives a fee in recognition of services provided to the Company.

Executive Director and Senior Management remuneration

Objective

The Company aims to award Executives with a level and mix of remuneration commensurate with their position and responsibilities within the Company and so as to:

- reward Executives for Company and individual performance against targets set by reference to suitable benchmarks;
- align the interests of Executives with those of shareholders; and
- ensure that the total remuneration paid is competitive by market standards.

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

Structure

The remuneration paid to Executives is set with reference to prevailing market levels and typically comprises a fixed salary and option component. Options are granted to Executives in line with their respective levels of experience and responsibility. Details of the amounts paid and the number of options granted to Executives are disclosed elsewhere in the Directors' Report.

Employment contracts

There are no employment contracts in place with any Non-Executive Director of the Company. There are standard Contracts of Employment with Executive Directors and Senior Management which contain no unusual terms. The contracts provide for a termination period in respect of Ben Greene of 180 days and 90 days in respect of other senior executives. The current employment contract with Ben Greene expires on 30 June 2013. There are no other termination payments or golden parachutes for any directors or senior executives.

Director remuneration

The following tables disclose the remuneration of the directors of the Company:

2011	Short term		Post Employment	Equity	Other Long	Total
	Salary & Fees \$	Non- monetary \$	Super- annuation \$	Options \$	Term Benefits \$	\$
Mr Fred Bart	61,000	-	5,490	-	-	66,490
Dr Ben Greene*	300,000	39,182	27,000	-	-	366,182
Mr Ian Dennis	37,500	-	3,375	-	-	40,875
Mr Mark Ureda	40,875	-	-	-	-	40,875
Lt Gen Peter Leahy AC	37,500	-	3,375	-	-	40,875
Mr Kevin Scully	11,535	-	-	-	-	11,535
	<u>488,410</u>	<u>39,182</u>	<u>39,240</u>	<u>-</u>	<u>-</u>	<u>566,832</u>
* Executive Director during the financial year						

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

2010	Short term		Post Employment	Equity	Other Long	Total
	Salary & Fees \$	Non-monetary \$	Super-annuation \$	Options \$	Term Benefits \$	\$
Mr Fred Bart	55,500	-	2,745	10,203	-	68,448
Dr Ben Greene*	273,001	57,616	27,000	49,218	-	406,835
Mr Ian Dennis	33,750	-	1,688	10,203	-	45,641
Mr Mark Ureda	35,438	-	-	10,203	-	45,641
Lt Gen Peter Leahy AC	33,750	-	3,038	-	-	36,788
	<u>431,439</u>	<u>57,616</u>	<u>34,471</u>	<u>79,827</u>	<u>-</u>	<u>603,353</u>
* Executive Director during the financial year						

Executive remuneration

No executives are employed by the holding company. The following table discloses the remuneration of the executives of the consolidated entity:

2011	Short term		Post Employment	Equity	Other Long	Total
	Salary & Fees \$	Non-monetary \$	Super-annuation \$	Options \$	Term Benefits \$	\$
Mr Ron Thompson	172,083	-	13,288	35,597	42,760	263,728
Dr Craig Smith	197,532	-	17,750	35,597	-	250,879
Mr Mark Bornholt	128,423	-	11,340	-	-	139,763
Mr John Palisi	196,946	-	17,724	35,597	-	250,267
Mr Hugo Keyner	<u>154,889</u>	<u>854</u>	<u>-</u>	<u>35,597</u>	<u>-</u>	<u>191,340</u>
	<u>849,873</u>	<u>854</u>	<u>60,102</u>	<u>142,388</u>	<u>42,760</u>	<u>1,095,977</u>

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

2010	Short term		Post Employment	Equity	Other Long	Total
	Salary & Fees \$	Non-monetary \$	Super-annuation \$	Options \$	Term Benefits \$	\$
Mr Ron Thompson	174,321	-	16,182	58,376	-	248,879
Dr Craig Smith	190,392	-	17,103	62,109	-	269,604
Mr John Palisi	184,387	-	16,594	58,376	-	259,357
Mr Hugo Keyner	<u>140,804</u>	<u>9,914</u>	<u>-</u>	<u>58,376</u>	<u>-</u>	<u>209,094</u>
	<u>689,904</u>	<u>9,914</u>	<u>49,879</u>	<u>237,237</u>	<u>-</u>	<u>986,394</u>

Non-monetary includes the provision for motor vehicles and health benefits.

Value of options issued to directors and executives

The following table discloses the value of options granted and exercised during the 2011 year:

	Options Granted Value at grant date (i) \$	Options Exercised Value at exercise date \$	Total value of options granted and exercised \$	Value of options included in remuneration for the year (i) \$	Percentage of total remuneration for the year that consists of options %
Dr Ben Greene	-	-	-	-	-
Mr Fred Bart	-	-	-	-	-
Mr Mark Ureda	-	-	-	-	-
Lt Gen Peter Leahy AC	-	-	-	-	-
Mr Kevin Scully	-	-	-	-	-
Mr Ian Dennis	-	-	-	-	-
Dr Craig Smith	154,080	-	154,080	35,597	14.19
Mr Mark Bornholt	-	-	-	-	-
Mr Ron Thompson	154,080	-	154,080	35,597	13.50
Mr John Palisi	154,080	-	154,080	35,597	14.22
Mr Hugo Keyner	154,080	-	154,080	35,597	18.60

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

(i) The value of options granted during the period is recognised in compensation over the vesting period of the grant.

Value of options – basis of calculation

The total value of options included in remuneration for the year is calculated as follows:

- The value of the options is determined at grant date, and are included in remuneration on a proportionate basis from grant date to vesting date. Where the options immediately vest the full value of the option is recognised in remuneration in the current year.

Elements of remuneration related to performance

There are no performance conditions other than service attached to the above remuneration to directors and executives. Directors and senior executives receive options as disclosed in the above tables which are not subject to specific performance conditions other than service. The overall performance of the company as measured by the share price will determine whether the options are exercised and whether the director or executive receives any benefit from these options. The time service condition has been chosen by the Board as an appropriate condition as it helps in the retention and motivation of staff. Options issued to certain directors and executives are also subject to vesting provisions as disclosed below.

Key management personnel option holdings

2011	Balance at 1/1/11	Granted as remuneration	(Lapsed)	Balance at 31/12/11	Balance vested at 31/12/11	Options vested during year
	No.	No.	No.	No.	No.	
Mr Fred Bart	200,000	-	(200,000)	-	-	100,000
Dr Ben Greene	964,800	-	(964,800)	-	-	482,400
Mr Ian Dennis	200,000	-	(200,000)	-	-	100,000
Mr Mark Ureda	200,000	-	(200,000)	-	-	100,000
Lt Gen Peter Leahy AC	-	-	-	-	-	-
Mr Kevin Scully	-	-	-	-	-	-
Mr Ron Thompson	160,000	-	-	160,000	80,000	48,000
Mr Mark Bornholt	-	-	-	-	-	-
Dr Craig Smith	280,000	-	(120,000)	160,000	80,000	108,000
Mr John Palisi	160,000	-	-	160,000	80,000	48,000
Mr Hugo Keyner	160,000	-	-	160,000	80,000	48,000

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

On 10 December 2009, The Directors' issued 1,800,000 unlisted options to executives and staff. The options issued to executives and staff have an exercise price of \$1.30 and expire on 8 December 2013. These options vest 20% after 12 months, 30% after 2 years and the balance after 3 years.

2010	Balance at 1/1/10	Granted as remuneration	(Lapsed)	Balance at 31/12/10	Balance vested at 31/12/10	Options vested during year
	No.	No.	No.	No.	No.	
Mr Fred Bart	200,000	-	-	200,000	200,000	100,000
Dr Ben Greene	964,800	-	-	964,800	964,800	482,400
Mr Ian Dennis	200,000	-	-	200,000	200,000	100,000
Mr Mark Ureda	200,000	-	-	200,000	200,000	100,000
Lt Gen Peter Leahy AC	-	-	-	-	-	-
Mr Ron Thompson	160,000	-	-	160,000	32,000	32,000
Dr Craig Smith	280,000	-	-	280,000	152,000	92,000
Mr John Palisi	160,000	-	-	160,000	32,000	32,000
Mr Hugo Keyner	160,000	-	-	160,000	32,000	32,000

All options issued during the year ended 31 December 2007 were issued on 31 May 2007. The options issued to directors have an exercise price of \$1.95 and expired on 31 May 2011. These options vest 20% after 12 months, 30% after 2 years and the balance after 3 years.

The 120,000 options issued to Dr Craig Smith during the year ended 31 December 2007 at an exercise price of \$1.95 vest 20% after 12 months, 30% after 2 years and the balance after 3 years. These options lapsed during the year.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

Other Key Management Personnel options vest 20% after 12 months, 30% after 2 years and the balance after 3 years.

On 31 May 2007, 200,000 Options to each of Fred Bart, Ian Dennis, Mark Ureda and Robert Schuitema at an exercise price of \$1.95 expired on 31 May 2011. 964,800 Options were also issued on 31 May 2007 to Dr Ben Greene at an exercise price of \$1.95 expiring on 31 May 2011 to replace the previously approved (but not issued) 964,800 options at an exercise price of \$3.06. These 964,800 options issued to Dr Ben Greene were his entitlement for the year ended 31 December 2007.

The percentage of the options granted on 31 May 2007 which vested in the current year to Mr Fred Bart, Dr Ben Greene, Mr Ian Dennis, Mr Mark Ureda and Dr Craig Smith was 50%.

No options were forfeited by key management personnel in the current year.

In the year ended 31 December 2012 the number of options that will vest if service conditions are met are Mr Ron Thompson – 80,000, Mr John Palisi – 80,000, Mr Hugo Keyner - 80,000 and Dr Craig Smith – 80,000

The Board policy is not to allow any person to hedge their exposure to risk in relation to the options granted. This policy may be reviewed should the options become in the money.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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DIRECTORS' REPORT (cont)

Remuneration Report (cont)

The table below sets out summary information about the company's earnings and movements in shareholder wealth for the last 5 financial years.

	31 December 2011 \$	31 December 2010 \$	31 December 2009 \$	31 December 2008 \$	31 December 2007 \$
Revenue	32,775,391	33,828,658	37,005,723	38,958,206	38,716,391
Net profit / (loss) before tax	180,188	3,175,142	2,436,249	2,213,006	(20,734,269)
Net profit/(loss) after tax	180,188	3,175,142	2,436,249	2,213,006	(20,734,269)

	31 December 2011 \$	31 December 2010 \$	31 December 2009 \$	31 December 2008 \$	31 December 2007 \$
Share price at start of year	1.35	1.05	0.41	0.50	1.38
Share price at end of year	0.55	1.35	1.05	0.41	0.50
Dividends paid	-	-	-	-	-

Audit Committee

The Board appointed three non-executive directors to form the committee, with a majority of independent directors and the Chairman being an independent person. The current members of the committee are Lt Gen Peter Leahy AC (Chairman), Mr Ian Dennis and Mr Fred Bart.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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DIRECTORS' REPORT (cont)

Non-audit services

The Directors are satisfied that the provision of non-audit services, during the year, by the auditor (or by another person or firm on the auditor's behalf) is compatible with the general standard of independence for auditors imposed by the Corporations Act 2001. The Directors have formed this view based on the fact that the nature and scope of each type of non-audit service provided means that the audit independence was not compromised.

Details of amounts paid or payable to the auditor for non-audit services provided during the year by the auditor are contained in note 10 to the financial statements.

Auditor's independence declaration

The auditor's independence declaration is included on page 23 of the annual report.

Signed in accordance with a resolution of directors made pursuant to s.298(2) of the Corporations Act 2001.

On behalf of the Directors

A handwritten signature in black ink, appearing to read 'I A Dennis', with a stylized flourish at the end.

I A Dennis
Director

Dated at Sydney this 30 day of March 2012

The Board of Directors
Electro Optic Systems Holdings Limited
Suite 2, Level 12
75 Elizabeth Street
SYDNEY NSW 2000

30 March 2012

Dear Board Members

Electro Optic Systems Holdings Limited

In accordance with section 307C of the Corporations Act 2001, I am pleased to provide the following declaration of independence to the directors of Electro Optic Systems Holdings Limited.

As lead audit partner for the audit of the financial statements of Electro Optic Systems Holdings Limited for the year ended 31 December 2011, I declare that to the best of my knowledge and belief, there have been no contraventions of:

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

Yours sincerely



DELOITTE TOUCHE TOHMATSU



Glen Sanford
Partner
Chartered Accountants

Independent Auditor's Report to the members of Electro Optic Systems Holdings Limited

Report on the Financial Report

We have audited the accompanying financial report of Electro Optic Systems Holdings Limited, which comprises the statement of financial position as at 31 December 2011, the statement of comprehensive income, the statement of cash flows and the statement of changes in equity for the year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity, comprising the company and the entities it controlled at the year's end or from time to time during the financial year as set out on pages 26 to 107.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

Auditor's Responsibility

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

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

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

Auditor's Independence Declaration

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of Electro Optic Systems Holdings Limited, would be in the same terms if given to the directors as at the time of this auditor's report.

Opinion

- (a) the financial report of Electro Optic Systems Holdings Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 31 December 2011 and of their performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- (b) the financial statements also comply with International Financial Reporting Standards as disclosed in Note 1.

Report on the Remuneration Report

We have audited the Remuneration Report included on pages 13 to 21 of the directors' report for the year ended 31 December 2011. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion the Remuneration Report of Electro Optic Systems Holdings Limited for the year ended 31 December 2011, complies with section 300A of the *Corporations Act 2001*.



DELOITTE TOUCHE TOHMATSU



Glen Sanford
Partner
Chartered Accountants
Parramatta, 30 March 2012

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

DIRECTORS' DECLARATION

The directors declare that:

- (a) 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;
- (b) in the directors' opinion, the attached financial statements and notes thereto are in accordance with the Corporations Act 2001, including compliance with accounting standards and giving a true and fair view of the financial position and performance of the company and the consolidated entity;
- (c) the directors have been given the declarations required by s.295A of the Corporations Act 2001; and
- (a) the attached financial statements are in compliance with International Financial Reporting Standards, as stated in note 1 to the financial statements.

Signed in accordance with a resolution of the directors made pursuant to s.295(5) of the Corporations Act 2001.

On behalf of the Directors



I A Dennis
Director

Dated at Sydney this 30 day of March 2012.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

STATEMENT OF COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2011

	Note	Consolidated		Company	
		31	31	31	31
		December	December	December	December
		2011	2010	2011	2010
		\$	\$	\$	\$
Revenue	2	32,775,391	33,828,658	333,807	273,900
Changes in inventories of finished goods and work in progress		(164,152)	2,655,051	-	-
Raw materials and consumables used		(14,214,487)	(13,091,811)	-	-
Employee benefits expense	2(b)	(13,338,261)	(13,118,633)	(320,650)	(375,937)
Administration expenses		(3,210,571)	(4,240,571)	(436,729)	(432,707)
Amortisation of intangibles		(131,533)	(148,474)	-	-
Finance costs	2(b)	(302,881)	(107,496)	-	-
Depreciation and amortisation of property, plant and equipment	2(b)	(426,512)	(498,816)	(1,095)	(1,825)
Impairment	2(b)	333,561	(459,953)	-	-
Loss on disposal of fixed assets	2(b)	2,287	(15,167)	-	-
Foreign exchange gain/(losses)	2(b)	573,317	(121,751)	669	25,663
Occupancy costs		(1,356,956)	(1,477,375)	-	-
Reversal of /(provision for) non-recovery of loan	2(b)	-	-	(3,573,685)	5,207,141
Provision for non-recovery of investment	2(b)	-	-	(400,464)	(650,263)
Other expenses		<u>(359,015)</u>	<u>(28,520)</u>	<u>-</u>	<u>-</u>
Profit /(loss) before income tax benefit	2	180,188	3,175,142	(4,398,147)	4,045,972
Income tax benefit	4	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Profit /(loss) for the period	20	<u>180,188</u>	<u>3,175,142</u>	<u>(4,398,147)</u>	<u>4,045,972</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

	Note	Consolidated		Company	
		31	31	31	31
		December	December	December	December
		2011	2010	2011	2010
		\$	\$	\$	\$
Other comprehensive income					
Exchange differences arising on translation of foreign operations		(527,622)	(553,048)	-	-
Income tax relating to components of other comprehensive income		-	-	-	-
		<u>(527,622)</u>	<u>(553,048)</u>	<u>-</u>	<u>-</u>
Total comprehensive income/(loss) for the period		<u>(347,434)</u>	<u>2,622,094</u>	<u>(4,398,147)</u>	<u>4,045,972</u>
Earnings per share					
Basic (cents per share)	3	0.3	5.6		
Diluted (cents per share)	3	0.3	5.6		

Notes to the financial statements are included on pages 34 to 107.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2011

		Consolidated		Company	
	Note	December 2011	December 2010	December 2011	December 2010
		\$	\$	\$	\$
CURRENT ASSETS					
Cash and cash equivalents	22	4,885,761	8,088,355	1,324,726	5,356,661
Trade and other receivables	6	9,835,027	15,509,461	21,156	14,553
Inventories	7	10,704,724	11,603,252	-	-
Other	8	101,316	253,520	-	-
TOTAL CURRENT ASSETS		<u>25,526,828</u>	<u>35,454,588</u>	<u>1,345,882</u>	<u>5,371,214</u>
NON-CURRENT ASSETS					
Property, plant and equipment	11	2,431,083	2,361,836	1,642	2,737
Intangibles	9	714,830	849,852	-	-
Other financial assets	5	-	-	-	-
Other	8	-	-	-	-
TOTAL NON-CURRENT ASSETS		<u>3,145,913</u>	<u>3,211,688</u>	<u>1,642</u>	<u>2,737</u>
TOTAL ASSETS		<u>28,672,741</u>	<u>38,666,276</u>	<u>1,347,524</u>	<u>5,373,951</u>
CURRENT LIABILITIES					
Trade and other payables	12	8,890,029	14,745,292	120,961	149,705
Borrowings	13	1,991,867	5,321,708	-	-
Provisions	14	4,763,852	5,531,382	-	-
TOTAL CURRENT LIABILITIES		<u>15,645,748</u>	<u>25,598,382</u>	<u>120,961</u>	<u>149,705</u>
NON-CURRENT LIABILITIES					
Borrowings	13	117,223	231,034	-	-
Provisions	14	249,523	229,643	-	-
TOTAL NON-CURRENT LIABILITIES		<u>366,746</u>	<u>460,677</u>	<u>-</u>	<u>-</u>
TOTAL LIABILITIES		<u>16,012,494</u>	<u>26,059,059</u>	<u>120,961</u>	<u>149,705</u>
NET ASSETS		<u>12,660,247</u>	<u>12,607,217</u>	<u>1,226,563</u>	<u>5,224,246</u>
EQUITY					
Issued capital	17	75,383,567	75,383,567	75,383,567	75,383,567
Reserves	19	7,569,374	7,696,532	7,523,594	7,123,130
Accumulated losses	20	(70,292,694)	(70,472,882)	(81,680,598)	(77,282,451)
TOTAL EQUITY		<u>12,660,247</u>	<u>12,607,217</u>	<u>1,226,563</u>	<u>5,224,246</u>

Notes to the financial statements are included on pages 34 to 107.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011

Consolidated	Total	Accumulated losses	Issued capital	Foreign currency translation reserve	Employee equity settled benefits reserve
	\$	\$	\$	\$	\$
2011					
Balance at 1 January 2011	<u>12,607,217</u>	<u>(70,472,882)</u>	<u>75,383,567</u>	<u>573,402</u>	<u>7,123,130</u>
Profit for the period	<u>180,188</u>	<u>180,188</u>	—	—	—
Exchange differences arising on translation of foreign operations	<u>(527,622)</u>	—	—	<u>(527,622)</u>	—
Total comprehensive (loss)/income for the year	<u>(347,434)</u>	<u>180,188</u>	—	<u>(527,622)</u>	—
Recognition of share based payments	<u>400,464</u>	—	—	—	<u>400,464</u>
Balance at 31 December 2011	<u>12,660,247</u>	<u>(70,292,694)</u>	<u>75,383,567</u>	<u>45,780</u>	<u>7,523,594</u>
2010					
Balance at 1 January 2010	<u>9,244,831</u>	<u>(73,648,024)</u>	<u>75,383,567</u>	<u>1,126,450</u>	<u>6,382,838</u>
Profit for the period	<u>3,175,142</u>	<u>3,175,142</u>	—	—	—
Exchange differences arising on translation of foreign operations	<u>(553,048)</u>	—	—	<u>(553,048)</u>	—
Total comprehensive income for the year	<u>2,622,094</u>	<u>3,175,142</u>	—	<u>(553,048)</u>	—
Recognition of share based payments	<u>740,292</u>	—	—	—	<u>740,292</u>
Balance at 31 December 2010	<u>12,607,217</u>	<u>(70,472,882)</u>	<u>75,383,567</u>	<u>573,402</u>	<u>7,123,130</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2011

Company	Total	Accumulated losses	Issued capital	Foreign currency translation reserve	Employee equity settled benefits reserve
	\$	\$	\$	\$	\$
2011					
Balance at 1 January 2011	<u>5,224,246</u>	<u>(77,282,451)</u>	<u>75,383,567</u>	<u>-</u>	<u>7,123,130</u>
Profit/(loss) for the period	<u>(4,398,147)</u>	<u>(4,398,147)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total comprehensive income for the year	<u>(4,398,147)</u>	<u>(4,398,147)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Recognition of share based payments	<u>400,464</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>400,464</u>
Balance at 31 December 2011	<u>1,226,563</u>	<u>(81,680,598)</u>	<u>75,383,567</u>	<u>-</u>	<u>7,523,594</u>
2010					
Balance at 1 January 2010	<u>437,982</u>	<u>(81,328,423)</u>	<u>75,383,567</u>	<u>-</u>	<u>6,382,838</u>
Profit for the period	<u>4,045,972</u>	<u>4,045,972</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total comprehensive income for the year	<u>4,045,972</u>	<u>4,045,972</u>	<u>-</u>	<u>-</u>	<u>-</u>
Recognition of share based payments	<u>740,292</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>740,492</u>
Balance at 31 December 2010	<u>5,224,246</u>	<u>(77,282,451)</u>	<u>75,383,567</u>	<u>-</u>	<u>7,123,130</u>

Notes to the financial statements are included on pages 34 to 107.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	Consolidated 31 December 2011 \$	31 December 2010 \$	Company 31 December 2011 \$	31 December 2010 \$
Cash flows from operating activities					
Receipts from customers		36,594,370	33,094,566	4,361	13,427
Payments to suppliers and employees		(40,418,655)	(30,152,162)	(792,057)	(715,012)
Interest received		348,855	278,705	329,446	260,472
Interest and other costs of finance paid		(302,881)	(107,496)	-	-
Net cash (outflows)/inflows from operating activities	22(b)	<u>(3,778,311)</u>	<u>3,113,613</u>	<u>(458,250)</u>	<u>(441,113)</u>
Cash flows from investing activities					
Advances (to) from wholly-owned controlled entities		-	-	(3,573,685)	5,207,141
Proceeds from sale of property, plant and equipment		14,418	-	-	-
Payment for property, plant and equipment		(175,690)	(552,550)	-	-
Net cash (outflows)/ inflows from investing activities		<u>(161,272)</u>	<u>(552,550)</u>	<u>(3,573,685)</u>	<u>5,207,141</u>
Cash flows from financing activities					
Proceeds of borrowings		<u>739,020</u>	<u>323,638</u>	-	-
Net cash inflows from financing activities		<u>739,020</u>	<u>323,638</u>	-	-

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Note	Consolidated 31 December 2011 \$	31 December 2010 \$	Company 31 December 2011 \$	31 December 2010 \$
Net (decrease)/increase in cash and cash equivalents		(3,200,563)	2,884,701	(4,031,935)	4,766,028
Cash and cash equivalents at the beginning of the financial year		8,088,355	5,572,052	5,356,661	590,633
Effects of exchange rate fluctuations on the balances of cash held in foreign currencies		<u>(2,031)</u>	<u>(368,398)</u>	<u>-</u>	<u>-</u>
Cash and cash equivalents at the end of the financial year	22(a)	<u>4,885,761</u>	<u>8,088,355</u>	<u>1,324,726</u>	<u>5,356,661</u>

Notes to the financial statements are included on pages 34 to 107.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011

1. Summary of Accounting Policies

Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with the Corporations Act 2001 and Accounting Standards and complies with other requirements of the law. Accounting Standards include Australian equivalents to International Financial Reporting Standards ("A-IFRS"). The financial report includes the separate financial statements of the company and the consolidated financial statements of the group. Compliance with A-IFRS ensures that the financial statements and notes of the company and the consolidated entity comply with International Financial Reporting Standards ("IFRS").

The financial statements were authorised for issue by the Directors on 30 March 2012.

Basis of preparation

The financial report has been prepared on the basis of historical cost. Cost is based on the fair values of the consideration given in exchange for assets. All amounts are presented in Australian dollars, unless otherwise stated.

In the application of A-IFRS management is required to make judgments, estimates and assumptions about carrying values of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstance, the results of which form the basis of making the judgments. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgments made by management in the application of A-IFRS that have significant effects on the financial statements and estimates with a significant risk of material adjustments in the next year are disclosed, where applicable, in the relevant notes to the financial statements. The areas of judgement made by management are in the areas of asset impairment of property, plant and equipment, inventory obsolescence and percentage completion of construction contracts.

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

The following significant accounting policies have been adopted in the preparation and presentation of the financial report:

(a) Going Concern

The financial report has been prepared on the basis that the company and the consolidated entity are going concerns, which assumes continuity of normal business activities and the realisation of assets and the settlement of liabilities in the ordinary course of business.

The consolidated entity earned a net profit during the year of \$180,188 (2010: \$3,175,142). Net cash used by operating activities was \$3,778,311 (2010 - \$3,113,613 provided). As at 31 December 2011, the consolidated entity had cash of \$4,885,761 (2010 - \$8,088,355) of which \$496,296 (2010 - \$496,692) is restricted as it secures bank guarantees on existing contracts with local and overseas customers. The cash will become unrestricted if the contract is concluded or renegotiated.

In the opinion of the directors, the ability of the company and the consolidated entity to continue as going concerns and pay their debts as and when they fall due is dependent upon:

- The ability to achieve target production levels and the required technical/ quality levels for the military business. The directors believe that this is achievable based on current production plans.
- The ability to obtain further new profitable contracts

The directors are in the process of bidding for new military and space contracts. The results of these bids are not known as at the date of this financial report. The Directors are confident that new contracts will be received during the next 12 months from the current bids outstanding and from new contracts which have not been bid at the date of the directors' report.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(a) Going concern (cont)

- The successful completion of the telescope and enclosure contracts on hand

The space systems division has progressed the completion of the contracts on hand and the consolidated entity has already provided for expected losses on contracts in accordance with Australian Accounting Standard AASB111 “Construction Contracts”.

- The successful close down of the Tucson, Arizona operations and relocation to Huntsville, Alabama by June 2012.

- The willingness and ability of key military customers to make timely payments for goods supplied in accordance with agreed terms.

- The continued support of the company’s shareholders

Should the company need to raise additional capital to fund new orders it may seek capital from existing or new shareholders. The company has no current plans to raise capital.

At the date of this report and having considered the above factors, in the opinion of the directors, the company and the consolidated entity can continue as going concerns and pay their debts as and when they become due and payable.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

ACN 092 708 364

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(b) Borrowings

Borrowings are recorded initially at fair value, net of transaction costs. Subsequent to initial recognition, borrowings are measured at amortised cost with any difference between the initial recognised amount and the redemption value being recognised in profit and loss over the period of the borrowing using the effective interest rate method.

(c) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, cash in banks and investments in money market instruments, net of outstanding bank overdrafts. Cash and cash equivalents includes restricted cash to the extent it relates to operating activities.

(d) Construction contracts and work in progress

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the reporting date, as measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Deferred revenue is represented by advance billings on contracts and the basis of recognition is the percentage of completion basis.

(e) Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not measured at fair value with changes in fair value recognised in profit and loss.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(f) Employee benefits

Provision is made for benefits accruing to employees in respect of wages and salaries, annual leave, and long service leave when it is probable that settlement will be required and they are capable of being measured reliably.

Provisions made in respect of short term employee benefits are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of long term employee benefits are measured as the present value of the estimated future cash outflows to be made by the consolidated entity in respect of services provided by employees up to the reporting date.

Defined contribution plans – Contributions to defined benefit contribution superannuation plans are expensed when incurred.

(g) Financial assets

Subsequent to initial recognition, investments in subsidiaries are measured at cost less any impairment.

Other financial assets are classified into the following specified categories: held to maturity investments and loans and receivables. The classification depends on the nature and purpose of the financial assets and is determined at the time of the initial recognition.

Held to maturity investments

Bills of exchange are recorded at amortised cost using the effective interest method less impairment, with revenue recognised on an effective yield basis. The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Loans and receivables

Trade receivables, loans and other receivables are recorded at amortised cost less impairment.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(h) Financial instruments issued by the company

Debt and equity instruments

Debt and equity instruments are classified as either liabilities or as equity in accordance with the substance of the contractual arrangement.

Transaction costs on the issue of equity instruments

Transaction costs arising on the issue of equity instruments are recognised directly in equity as a reduction of the proceeds of the equity instruments to which the costs relate. Transaction costs are the costs that are incurred directly in connection with the issue of those equity instruments and which would not have been incurred had those instruments not been issued.

Interest

Interest is classified as an expense consistent with the statement of financial position classification of the related debt.

(i) Foreign currency

Foreign currency transactions

All foreign currency transactions during the financial year are brought to account using the exchange rate in effect at the date of the transaction. Foreign currency monetary items at reporting date are translated at the exchange rate existing at reporting date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined.

Exchange differences are recognised in profit and loss in the period they arise.

Foreign operations

On consolidation, the assets and liabilities of the consolidated entity's overseas operations are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are recognised in the foreign currency translation reserve, and recognised in profit and loss on disposal of the foreign operation.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(j) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (GST), except:

- i. where the amount of GST incurred is not recoverable from the taxation authority, it is recognised as part of the cost of acquisition of an asset or as part of an item of expense; or
- ii. for receivables and payables which are recognised inclusive of GST.

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

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

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(k) Government grants

Government grants are assistance by the government in the form of transfers of resources to the consolidated entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. Government grants include government assistance where there are no conditions specifically relating to the operating activities of the consolidated entity other than the requirement to operate in certain regions or industry sectors.

Government grants relating to income are recognised as income over the periods necessary to match them with the related costs. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the consolidated entity with no future related costs are recognised as income in the period in which it becomes receivable.

(l) Impairment of assets

At each reporting date, the consolidated entity reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the consolidated entity estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Goodwill, intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually and whenever there is an indication that the asset may be impaired. An impairment of goodwill is not subsequently reversed. Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(l) Impairment of assets (cont)

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in profit or loss immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in profit and loss immediately.

(m) Income tax

Current tax

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax

Deferred tax is accounted for using the comprehensive balance sheet liability method in respect of temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax base of those items.

In principle, deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary differences or unused tax losses and tax offsets can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities (other than as a result of business combination) which affects neither taxable income nor accounting profit. Furthermore, a deferred tax liability is not recognised in relation to taxable temporary differences arising from goodwill.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(m) Income tax (cont)

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries except where the consolidated entity is able to control the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets arising from deductible temporary differences associated with these investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period(s) when the assets and liabilities giving rise to them are realised or settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the consolidated entity expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the company/consolidated entity intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period

Current and deferred tax is recognised as an expense or income in the statement of comprehensive income, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity, or where it arises from the initial accounting for a business combination, in which case it is taken into account in the determination of goodwill or excess.

Tax consolidation

The company and all its wholly-owned Australian resident entities are part of a tax consolidated group under Australian taxation law. Electro Optic Systems Holdings Limited is the head entity in the tax-consolidated group. Tax expense/income, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'separate taxpayer within the group' approach.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(m) Income tax (cont)

Current tax liabilities and assets and deferred tax assets arising from unused tax losses and tax credits of the members of the tax-consolidated group are recognised by the company (as head entity in the tax-consolidated group).

There are no formal tax funding arrangements within companies within the tax-consolidated entity.

(n) Intangible assets

Research and development costs

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Where no internally-generated intangible assets can be recognised, development expenditure is recognised as an expense in the period as incurred.

Intangible assets acquired in a business combination

Intangible assets acquired in a business combination are identified and recognised separately from goodwill where they satisfy the definition of an intangible asset and their fair value can be measured reliably.

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately.

(o) Inventories

Inventories are measured at the lower of cost and net realisable value. Costs are assigned on a first-in first-out basis. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(p) Leased assets

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Consolidated entity as lessee

Assets held under finance leases are initially recognised at their fair value or, if lower, at amounts equal to the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income.

Finance leased assets are amortised on a straight line basis over the estimated useful life of the asset.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

Lease incentives

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefits of incentives are recognised as a reduction of rental expenses on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

(q) Payables

Trade payable and other accounts payable are recognised when the consolidated entity becomes obliged to make future payments resulting from the purchase of goods and services.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(r) Principles of consolidation

The consolidated financial statements are prepared by combining the financial statements of all the entities that comprise the consolidated entity, being the company (the parent entity) and its subsidiaries as defined in Accounting Standard AASB 127 Consolidated and Separate Financial Statements. Consistent accounting policies are employed in the preparation and presentation of the consolidated financial statements.

On acquisition, the assets, liabilities and contingent liabilities of a subsidiary are measured at their fair values at the date of acquisition. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. If, after reassessment, the fair values of the identifiable net assets acquired exceeds the cost of acquisition, the deficiency is credited to profit and loss in the period of acquisition.

The consolidated financial statements include the information and results of each subsidiary from the date on which the company obtains control and until such time as the company ceases to control such entity.

In preparing the consolidated financial statements, all inter-company balances and transactions and unrealised profits within the consolidated entity are eliminated in full.

(s) Property, plant and equipment

Plant and equipment, leasehold improvements and equipment under finance lease are stated at cost less accumulated depreciation and impairment. Cost includes expenditure that is directly attributable to the acquisition of an item. In the event that settlement of all or part of the purchase consideration is deferred, cost is determined by discounting the amounts payable in the future to their present value as at the date of acquisition.

Depreciation is provided on property, plant and equipment. Depreciation is calculated so as to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter, using the straight line method. The estimated useful lives, residual values and depreciation method is reviewed at the end of each annual accounting period.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(s) Property, plant and equipment (cont)

The following estimated useful lives are used in the calculation of depreciation:

Plant and equipment	5 to 15 years
Leasehold improvements	3 to 5 years
Equipment under finance lease	3 to 5 years
Office equipment	5 to 15 years
Furniture, fixture and fittings	5 to 15 years
Motor vehicles	3 to 5 years

(t) Provisions

Provisions are recognised when the consolidated entity has a present obligation, the future sacrifice of economic benefits is probable, and the amount of the provision can be measured reliably.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is probable that recovery will be received and the amount of the receivable can be measured reliably.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

Warranties – Provisions for warranty costs are recognised as agreed in individual sales contracts, at the directors best estimate of the expenditure required to settle the consolidated entity's liability.

Surplus lease space – The company has entered into contracts for the lease of premises in Tucson, USA which are surplus to the current requirements of the company. Present obligations under the onerous lease contract are recognised as a provision.

Redundancy costs – The company has recognised costs for redundancy costs in its Tucson, USA plant which is being relocated to Huntsville, Alabama.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(t) Provisions (cont)

Onerous contracts – Present obligations arising under onerous contracts are recognised and measured as a provision. An onerous contract is considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Decommissioning cost and make good of leased premises – a provision for decommissioning cost and make good of leased premises is recognised when there is a present obligation, it is probable that an outflow of economic benefits will be required to settle the obligation, and the amount of the provision can be measured reliably. The estimated future obligations include the costs of removing the facilities and restoring the premises.

(u) Revenue recognition

Construction revenue is recognised on the basis of the terms of the contract adjusted for any variations or claims allowable under the contract.

Revenue from contracts to provide services is recognised on a monthly basis in accordance with the services contracts.

Interest income is recognised as it accrues.

Revenue from the sale of goods is recognised when the consolidated entity has transferred to the buyer the significant risks and rewards of ownership of the goods.

(v) Share based payments to employees

Equity-settled share-based payments are measured at fair value at the date of the grant. Fair value is measured by use of a modified Cox-Rubenstein binomial model. The expected life used in the model has been adjusted, based on management best estimates, for the effects of non-transferability, exercise restrictions and behavioural considerations. The fair value determined at the grant date of the equity-settled share based payments is expensed on a straight-line basis over the vesting period, based on the consolidated entity's estimate of shares that will eventually vest.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(w) AASB Accounting Standards not yet effective

The entity has not elected to early adopt the following Standards and Interpretations which have been issued or revised by the AASB but are not yet effective:

All other new and revised Standards and Interpretations effective for the period ended 31 December 2011 have been adopted with no impact on the amounts or disclosures in the financial statements.

Standards and Interpretations in issue not yet adopted

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

Standard/Interpretation	Effective for annual reporting periods beginning on or after	Expected to be initially applied in the financial year ending
AASB 9 Financial Instruments	1 January 2013	31 December 2013
AASB 10 Consolidated Financial Statements	1 January 2013	31 December 2013
AASB 11 Joint Arrangements	1 January 2013	31 December 2013
AASB 12 Disclosure of Interests in Other Entities	1 January 2013	31 December 2013
AASB 13 Fair Value Measurement	1 January 2013	31 December 2013
AASB 127 Separate Financial Statements	1 January 2013	31 December 2013
AASB 1054 Australian Additional Disclosures	1 July 2011	30 June 2012
AASB 2010-7 Amendments to Australian Accounting Standards arising from AASB 9 (December 2010) [AASB 1, 3, 4, 5, 7, 101, 102, 108, 112, 118, 120, 121, 127, 128, 131, 132, 136, 137, 139, 1023 & 1038 and Interpretations 2, 5, 10, 12, 19 & 127]	1 January 2013	31 December 2013
AASB 2010-8 Amendments to Australian Accounting Standards – Deferred Tax: Recovery of Underlying Assets [AASB 112]	1 January 2012	31 December 2012
AASB 2011-4 Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements [AASB 124]	1 July 2013	30 June 2014

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

1. Summary of Accounting Policies (cont)

(w) AASB Accounting Standards not yet effective (cont)

Standard/Interpretation	Effective for annual reporting periods beginning on or after	Expected to be initially applied in the financial year ending
AASB 2011-6 Amendments to Australian Accounting Standards – Extending Relief from Consolidation, the Equity Method and Proportionate Consolidation – Reduced Disclosure Requirements [AASB 127, AASB 128 & AASB 131]	1 July 2013	30 June 2014
AASB 2011-7 Amendments to Australian Accounting Standards arising from the Consolidation and Joint Arrangements Standards [AASB 1, 2, 3, 5, 7, 9, 2009-11, 101, 107, 112, 118, 121, 124, 132, 133, 136, 138, 139, 1023 & 1038 and Interpretations 5, 9, 16 & 17]	1 January 2013	31 December 2013
AASB 2011-8 Amendments to Australian Accounting Standards arising from AASB 13 [AASB 1, 2, 3, 4, 5, 7, 9, 2009-11, 2010-7, 101, 102, 108, 110, 116, 117, 118, 119, 120, 121, 128, 131, 132, 133, 134, 136, 138, 139, 140, 141, 1004, 1023 & 1038 and Interpretations 2, 4, 12, 13, 14, 17, 19, 131 & 132]	1 January 2013	31 December 2013
AASB 2011-9 Amendments to Australian Accounting Standards – Presentation of Items of Other Comprehensive Income [AASB 1, 5, 7, 101, 112, 120, 121, 132, 133, 134, 1039 & 1049]	1 July 2012	30 June 2013
AASB 2011-10 Amendments to Australian Accounting Standards arising from AASB 119 (September 2011) [AASB 1, AASB 8, AASB 101, AASB 124, AASB 134, AASB 1049 & AASB 2011-8 and Interpretation 14]	1 January 2013	31 December 2013

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material financial impact on the financial statements of the company but may change disclosures made.

(x) Comparative amounts

Where the Group changes the presentation or classification of items in its financial statements, it reclassifies the comparative amounts for consistency and comparability between financial years.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
2. Profit/(loss) from operations				
(a) Revenue				
Revenue from operations consisted of the following items:				
Revenue from the sale of goods	24,363,281	26,632,887	-	-
Revenue from the rendering of services	5,787,406	3,373,427	-	-
Construction contract revenue	<u>2,227,355</u>	<u>3,220,211</u>	<u>-</u>	<u>-</u>
	<u>32,378,042</u>	<u>33,226,525</u>	<u>-</u>	<u>-</u>
Interest revenue:				
Bank deposits	<u>348,855</u>	<u>278,705</u>	<u>329,446</u>	<u>260,472</u>
Other				
Other	<u>48,494</u>	<u>323,428</u>	<u>4,361</u>	<u>13,428</u>
	<u>32,775,391</u>	<u>33,828,658</u>	<u>333,807</u>	<u>273,900</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
(b) Profit/(loss) from operations (cont)				
Profit/(loss) before income tax has been arrived at after charging the following expenses:				
Borrowing costs				
Finance lease finance charges	111,371	39,588	-	-
Interest paid – Other entities	<u>191,510</u>	<u>67,908</u>	-	-
	<u>302,881</u>	<u>107,496</u>	-	-
Depreciation – property, plant and equipment	426,512	498,816	1,095	1,825
Impairment /(write back) of property, plant and equipment	(333,561)	459,953	-	-
Amortisation - intangibles	131,533	148,474	-	-
(Reversal of)/ provision for non-recovery of loan – wholly-owned controlled entity	-	-	3,573,685	(5,207,141)
Provision for non-recovery of investment in subsidiary	-	-	400,464	650,263
(Reversal of)/ writedown of inventory to net realisable value	1,650,540	(1,708,629)	-	-
Loss/(profit) on sale of property, plant and equipment	(2,287)	15,167	-	-
Foreign exchange gain/(loss)	573,317	(121,751)	(669)	(25,663)
Operating lease rental expenses:				
Minimum lease payments	<u>542,209</u>	<u>688,060</u>	-	-
Employee benefit expense:				
Share based payments:				
Equity settled	400,464	740,292	-	90,029
Contributions to defined contribution superannuation plans	1,222,520	879,590	12,240	7,470
Other employee benefits	<u>11,715,277</u>	<u>11,498,751</u>	<u>308,410</u>	<u>278,438</u>
	<u>13,338,261</u>	<u>13,118,633</u>	<u>320,650</u>	<u>375,937</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

Consolidated	
31	31
December	December
2011	2010
\$	\$

3. Earnings per Share

Basic earnings per share	<u>0.3 cents</u>	<u>5.6 cents</u>
Diluted earnings per share	<u>0.3 cents</u>	<u>5.6 cents</u>

Basic Earnings per Share

Earnings (a)	<u>180,188</u>	<u>3,175,142</u>
Weighted average number of ordinary shares (b)	<u>56,845,926</u>	<u>56,845,926</u>

(a) Earnings used in the calculation of basic earnings per share are the same as the net profit in the statement of comprehensive income.

(b) Options are considered to be potential ordinary shares and are therefore excluded from the weighted average number of shares used in the calculation of basic earnings per share. Where dilutive, potential ordinary shares are included in the calculation of diluted earnings per share (see below).

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated	
	31	31
	December	December
	2011	2010
	\$	\$

3. Earnings per Share (cont)

Diluted Earnings per Share

Earnings (a)	<u>180,188</u>	<u>3,175,142</u>
Weighted average number of ordinary shares (b)	<u>56,845,926</u>	<u>56,845,926</u>

(a) Earnings used in the calculation of diluted earnings per share are the same as the net profit in the statement of comprehensive income.

(b) The weighted average number of ordinary shares and potential ordinary shares used in the calculation of diluted earnings per share are as follows:

Weighted average number of shares used in the calculation of basic earnings per share	56,845,926	56,845,926
Directors options	-	-
Staff Share plan	<u>-</u>	<u>-</u>
Weighted average number of shares used in the calculation of diluted earnings per share	<u>56,845,926</u>	<u>56,845,926</u>

(c) The following potential ordinary shares are not dilutive and therefore excluded from the weighted average number of ordinary shares and potential ordinary shares used in the calculation of diluted earnings per share:

Directors options	-	1,564,800
Staff Share plan	<u>1,538,000</u>	<u>1,829,000</u>
	<u>1,538,000</u>	<u>3,393,800</u>

(d) Weighted average number of converted, lapsed, or cancelled potential ordinary shares used in the calculation of diluted earning per share:

None used as they are not considered dilutive.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
4. Income Tax				
(a) The prima facie income tax benefit on pre-tax accounting profit/(loss) from operations reconciles to the income tax benefit in the financial statements as follows:				
Profit/(loss) from operations	<u>180,188</u>	<u>3,175,142</u>	<u>(4,398,147)</u>	<u>4,045,972</u>
Income tax expense/ (benefit) calculated at 30%	54,056	952,543	(1,319,444)	1,213,792
Non-deductible provision for non-recovery of loan	-	-	1,072,106	(1,562,142)
Non-deductible provision for non recovery of investment	-	-	120,139	195,079
Share based payments	120,139	222,088	-	27,009
Previously unrecognised and unused tax losses now recognised	-	(1,019,214)	-	-
Other non-deductible/ non assessable items	<u>(367,922)</u>	<u>(155,417)</u>	<u>5,626</u>	<u>(24,173)</u>
	(193,727)	-	(121,573)	(150,435)
Unused tax losses and tax offsets not recognised as deferred tax assets	<u>193,727</u>	<u>-</u>	<u>121,573</u>	<u>150,435</u>
Income tax attributable to operating profit/(loss)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

The tax rate used in the above reconciliation is the corporate tax rate of 30% payable by Australian corporate entities on taxable profits under Australian tax law, 25% in Germany, 17% in Singapore and the federal tax rate applicable in the USA and the State of Arizona has been assumed to approximate a combined rate 40% as their tax rates apply on a sliding scale. There has been no change in the corporate tax rate when compared with the previous reporting period.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$

4. Income Tax (Cont)

(b) Unrecognised deferred tax balances

The following deferred tax assets have not been brought to account as assets

Tax losses – revenue	18,294,131	18,100,404	6,384,925	6,263,352
Temporary differences	<u>1,504,013</u>	<u>1,728,308</u>	<u>-</u>	<u>-</u>
	<u>19,798,144</u>	<u>19,828,712</u>	<u>6,384,925</u>	<u>6,263,352</u>

Tax consolidation

Relevance of tax consolidation to the consolidated entity

The company and its wholly-owned Australian resident entities have formed a tax-consolidated group with effect from 1 January 2003 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated group is Electro Optic Systems Holdings Limited. The members of the tax-consolidated entity group are identified in Note 24.

Nature of tax funding arrangements and tax sharing agreements

There are no formal tax funding or tax sharing arrangements within the tax-consolidated group.

5. Other financial assets

Non-Current – at cost

Unlisted shares in controlled entities

at cost	-	-	3,811,923	3,411,459
provision for non recovery	<u>-</u>	<u>-</u>	<u>(3,811,923)</u>	<u>(3,411,459)</u>
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

Carrying value at start of financial year

share options provided at no cost	-	-	400,464	650,263
provision for non recovery	<u>-</u>	<u>-</u>	<u>(400,464)</u>	<u>(650,263)</u>
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

Consolidated		Company	
31	31	31	31
December	December	December	December
2011	2010	2011	2010
\$	\$	\$	\$

5. Other financial assets (Cont)

The directors have assessed the carrying value of the unlisted shares held in controlled entities and have determined that, as at 31 December 2011, based upon the net asset position of the controlled entities, the current and historic trading results and the foreseeable future results from signed contracts on hand the investments are fully impaired.

6. Trade and other receivables

Current

Trade receivables	9,126,990	12,654,228	-	-
GST receivable	108,417	59,034	21,156	7,268
Amounts due from customers under construction contracts (Note 30)	599,620	2,795,808	-	-
Other debtors	-	391	-	7,285
	<u>9,835,027</u>	<u>15,509,461</u>	<u>21,156</u>	<u>14,553</u>

The average credit period on sales of goods is 30 days. No interest is charged on late payments and no general allowance for doubtful debts has been made as most contracts are with governments and government agencies.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
6. Trade and other receivables (cont)				
Ageing of past due not impaired				
31 -60 days	772,031	6,481	-	-
61-90 days	5,148	709,957	-	-
120 days +	<u>58,015</u>	<u>635,782</u>	<u>-</u>	<u>-</u>
	<u>835,194</u>	<u>1,352,220</u>	<u>-</u>	<u>-</u>
Ageing of past due and impaired				
120 days +	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Movement in allowance for doubtful debts				
Balance at the beginning of the financial year	-	45,398	-	-
Amount released	<u>-</u>	<u>(45,398)</u>	<u>-</u>	<u>-</u>
Balance at the end of the financial year	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
7. Current Inventories				
Finished goods – at cost	2,354,511	5,214,995	-	-
Raw materials – at net realisable value	4,644,227	5,706,907	-	-
Work in progress – at cost	<u>3,705,986</u>	<u>681,350</u>	<u>-</u>	<u>-</u>
	<u>10,704,724</u>	<u>11,603,252</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
8. Other Assets				
Current				
Prepayments	<u>101,316</u>	<u>253,520</u>	<u>-</u>	<u>-</u>
Non-current				
Amounts due from wholly-owned controlled entity	-	-	68,082,984	64,509,299
Less Allowance for uncollectible amounts	<u>-</u>	<u>-</u>	<u>(68,082,984)</u>	<u>(64,509,299)</u>
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Movement in allowance for uncollectible amounts				
Balance at the beginning of the financial year	-	-	64,509,299	69,716,440
(Reversal of)/ provision recognised in profit and loss	<u>-</u>	<u>-</u>	<u>3,573,685</u>	<u>(5,207,141)</u>
Balance at the end of the financial year	<u>-</u>	<u>-</u>	<u>68,082,984</u>	<u>64,509,299</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
9. Intangibles				
License agreement	<u>714,830</u>	<u>849,852</u>	<u>-</u>	<u>-</u>
On 3 December 2009 as part of the acquisition of the assets of Recon Optical Inc of the USA, the consolidated entity acquired a licence for the Kollmorgen Licensed patents. The license expires on the expiry of the patents which expire on 16 July 2017 and relates to the manufacturing of gimbals.				
Movement in intangible assets				
Gross carrying amount				
Balance at the beginning of the financial year	849,852	1,119,695	-	-
Amortisation	(131,533)	(148,474)	-	-
Net foreign currency exchange differences	<u>(3,489)</u>	<u>(121,369)</u>	<u>-</u>	<u>-</u>
Balance at the end of the financial year	<u>714,830</u>	<u>849,852</u>	<u>-</u>	<u>-</u>
Net book value	<u>714,830</u>	<u>849,852</u>	<u>-</u>	<u>-</u>

10. Auditors Remuneration

(a) Auditor of the Parent Entity

Audit or review of the financial report	242,860	199,570	242,860	199,570
Taxation services	<u>12,000</u>	<u>11,000</u>	<u>12,000</u>	<u>11,000</u>
	<u>254,860</u>	<u>210,570</u>	<u>254,860</u>	<u>210,570</u>

The auditor of Electro Optic Systems Holdings Limited is Deloitte Touche Tohmatsu

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
11. Property, Plant and Equipment				
(a) Plant and equipment – at cost	6,013,397	6,047,822	-	-
Less accumulated depreciation and impairment	<u>(4,944,358)</u>	<u>(4,299,133)</u>	<u>-</u>	<u>-</u>
	<u>1,069,039</u>	<u>1,748,689</u>	<u>-</u>	<u>-</u>
 (b) Leased assets – at cost	342,866	414,285	-	-
Less accumulated amortisation and impairment	<u>(58,292)</u>	<u>(62,539)</u>	<u>-</u>	<u>-</u>
	<u>284,574</u>	<u>351,746</u>	<u>-</u>	<u>-</u>
 (c) Office equipment – at cost	2,752,175	2,601,098	15,048	15,048
Less accumulated depreciation and impairment	<u>(1,996,675)</u>	<u>(2,578,921)</u>	<u>(13,406)</u>	<u>(12,311)</u>
	<u>755,500</u>	<u>22,177</u>	<u>1,642</u>	<u>2,737</u>
 (d) Furniture, fixtures and fittings – at cost	300,212	299,546	-	-
Less accumulated depreciation and impairment	<u>(274,814)</u>	<u>(290,212)</u>	<u>-</u>	<u>-</u>
	<u>25,398</u>	<u>9,334</u>	<u>-</u>	<u>-</u>
 (e) Leasehold improvements – at cost	1,140,721	1,142,806	-	-
Less accumulated depreciation and impairment	<u>(844,149)</u>	<u>(912,916)</u>	<u>-</u>	<u>-</u>
	<u>296,572</u>	<u>229,890</u>	<u>-</u>	<u>-</u>
 (f) Motor vehicle –at cost	18,081	18,104	-	-
Less accumulated depreciation and impairment	<u>(18,081)</u>	<u>(18,104)</u>	<u>-</u>	<u>-</u>
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
 (g) Satellite – at cost	7,000,000	7,000,000	-	-
Less impairment	<u>(7,000,000)</u>	<u>(7,000,000)</u>	<u>-</u>	<u>-</u>
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total net book value of Property, Plant and Equipment	<u>2,431,083</u>	<u>2,361,836</u>	<u>1,642</u>	<u>2,737</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
11. Property, Plant and Equipment (cont)				
<u>Cost</u>				
Plant and equipment				
Balance at beginning of year	6,047,822	5,095,139	-	-
Additions	33,060	2,325	-	-
Asset transfers	-	1,480,310	-	-
Disposals	(62,168)	(116,853)	-	-
Net foreign currency exchange differences	<u>(5,317)</u>	<u>(413,099)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>6,013,397</u>	<u>6,047,822</u>	<u>-</u>	<u>-</u>
Leased assets				
Balance at beginning of year	414,285	122,365	-	-
Additions	-	352,524	-	-
Disposals	-	(53,417)	-	-
Transfer to office equipment	(71,431)	-	-	-
Net foreign currency exchange differences	<u>12</u>	<u>(7,187)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>342,866</u>	<u>414,285</u>	<u>-</u>	<u>-</u>
Office equipment				
Balance at beginning of year	2,601,098	2,917,760	15,048	15,048
Additions	115,149	19,480	-	-
Transfer from leased assets	71,431	-	-	-
Disposals	(30,322)	(88,258)	-	-
Net foreign currency exchange differences	<u>(5,181)</u>	<u>(247,884)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>2,752,175</u>	<u>2,601,098</u>	<u>15,048</u>	<u>15,048</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated 31 December 2011 \$	31 December 2010 \$	Company 31 December 2011 \$	31 December 2010 \$
11. Property, Plant and Equipment (cont)				
Furniture, fixtures and fittings				
Balance at beginning of year	299,546	349,501	-	-
Additions	7,586	-	-	-
Disposals	(6,590)	(6,446)	-	-
Net foreign currency exchange differences	<u>(330)</u>	<u>(43,509)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>300,212</u>	<u>299,546</u>	<u>-</u>	<u>-</u>
Leasehold improvements				
Balance at beginning of year	1,142,806	1,040,902	-	-
Additions	19,895	178,221	-	-
Disposals	(21,159)	-	-	-
Net foreign currency exchange differences	<u>(821)</u>	<u>(76,317)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>1,140,721</u>	<u>1,142,806</u>	<u>-</u>	<u>-</u>
Motor vehicle				
Balance at beginning of year	18,104	21,078	-	-
Net foreign currency exchange differences	<u>(23)</u>	<u>(2,974)</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>18,081</u>	<u>18,104</u>	<u>-</u>	<u>-</u>
Satellite				
Balance at beginning of year	7,000,000	7,000,000	-	-
Balance at end of year	<u>7,000,000</u>	<u>7,000,000</u>	<u>-</u>	<u>-</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
11. Property, Plant and Equipment (cont)				
Accumulated Depreciation/Amortisation/ Impairment				
Plant and equipment				
Balance at beginning of year	(4,299,133)	(3,896,435)	-	-
Depreciation	(318,269)	(841,881)	-	-
Impairment	(371,085)	-	-	-
Disposals	50,711	116,853	-	-
Net foreign currency exchange differences	(6,582)	322,330	-	-
Balance at end of year	<u>(4,944,358)</u>	<u>(4,299,133)</u>	<u>-</u>	<u>-</u>
Leased plant and equipment				
Balance at beginning of year	(62,539)	(122,365)	-	-
Amortisation expense	(67,089)	(860)	-	-
Impairment	(83)	-	-	-
Transfer to office equipment	71,431	-	-	-
Disposals	-	51,467	-	-
Net foreign currency exchange differences	(12)	9,219	-	-
Balance at end of year	<u>(58,292)</u>	<u>(62,539)</u>	<u>-</u>	<u>-</u>
Office equipment				
Balance at beginning of year	(2,578,921)	(2,792,204)	(10,486)	(7,444)
Depreciation	(15,458)	(97,727)	(1,825)	(3,042)
Impairment	633,698	-	-	-
Transfer from leased assets	(71,431)	-	-	-
Disposals	30,322	75,091	-	-
Net foreign currency exchange differences	5,115	235,919	-	-
Balance at end of year	<u>(1,996,675)</u>	<u>(2,578,921)</u>	<u>(12,311)</u>	<u>(10,486)</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
11. Property, Plant and Equipment (cont)				
Furniture, fixtures and fittings				
Balance at beginning of year	(290,212)	(338,947)	-	-
Depreciation	(1,220)	(1,220)	-	-
Impairment	9,697	-	-	-
Disposals	6,591	6,446	-	-
Net foreign currency exchange differences	<u>330</u>	<u>43,509</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>(278,814)</u>	<u>(290,212)</u>	<u>-</u>	<u>-</u>
Leasehold improvements				
Balance at beginning of year	(912,916)	(972,151)	-	-
Amortisation	(24,476)	(17,081)	-	-
Impairment	60,534	-	-	-
Disposals	21,159	-	-	-
Net foreign currency exchange differences	<u>11,550</u>	<u>76,316</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>(844,149)</u>	<u>(912,916)</u>	<u>-</u>	<u>-</u>
Motor vehicle				
Balance at beginning of year	(18,104)	(21,078)	-	-
Net foreign currency exchange differences	<u>23</u>	<u>2,974</u>	<u>-</u>	<u>-</u>
Balance at end of year	<u>18,081</u>	<u>(18,104)</u>	<u>-</u>	<u>-</u>
Satellite				
Balance at beginning of year	(7,000,000)	(7,000,000)	-	-
Balance at end of year	<u>(7,000,000)</u>	<u>(7,000,000)</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

11. Property, Plant and Equipment (cont)

Aggregate depreciation, impairment and amortisation allocated during the period is recognised as an expense and disclosed in Note 2 to the financial statements.

Impairment of property, plant and equipment

The consolidated entity has assessed the carrying amount of plant and equipment in the Queanbeyan and Tucson facilities and determined an impairment (reversal) charge for the year of (\$333,561) (2010: \$459,953). The basis to assess for any potential impairment was fair value less costs to sell and fair value determined by reference to an active market for second hand manufacturing equipment.

Consolidated		Company	
31	31	31	31
December	December	December	December
2011	2010	2011	2010
\$	\$	\$	\$

12. Current trade and other payables

Trade payables	3,223,921	4,370,193	6,802	51,378
Accruals	295,309	904,365	114,159	98,327
Amounts due to customers under construction contracts (Note 30)	<u>5,370,799</u>	<u>9,470,734</u>	<u>-</u>	<u>-</u>
	<u>8,890,029</u>	<u>14,745,292</u>	<u>120,961</u>	<u>149,705</u>

The average credit period on purchases of goods is 30 days and no interest is payable on goods purchased within agreed credit terms. The consolidated entity has financial risk management policies in place to ensure that all payables are paid within the credit timeframe.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
13. Borrowings				
Secured - At amortised cost				
Current				
Finance lease liabilities (Note 26)	113,524	106,712	-	-
Secured promissory note 2	1,139,323	5,214,996	-	-
Secured promissory note 3	<u>739,020</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>1,991,867</u>	<u>5,321,708</u>	<u>-</u>	<u>-</u>
Non-current				
Finance lease liabilities (Note 26)	<u>117,223</u>	<u>231,034</u>	<u>-</u>	<u>-</u>
The finance lease liabilities are secured by the leased assets. The average weighted interest rate charged on the finance leases was 9.95% (2010 – 10.12%). The secured promissory note 2 of \$1,139,323 (US\$1,159,375) is denominated in US dollars and attracts an interest rate of 5%. The secured promissory note 3 of \$739,020 (US\$752,027) is denominated in US dollars and attracts an interest rate of 5%. The promissory notes are secured by the inventory purchased and a guarantee from the parent company. The promissory note 2 is repayable by 31 January 2012 or at the rate of US\$165,625 per completed inventory item sold which was acquired as part of this purchase agreement. The promissory note 3 is repayable by 31 January 2012 or at the rate of US\$35,811 per completed inventory item sold which was acquired as part of this purchase agreement. Since the end of the financial year, both secured promissory notes have been repaid in full.				
14. Provisions				
Current				
Employee benefits (Note 16)	2,126,061	2,062,241	-	-
Surplus lease space	87,642	110,141	-	-
Contract losses	22,422	166,496	-	-
Redundancy costs	201,185	-	-	-
Decommissioning costs	250,000	250,000	-	-
Make good of leased premises	29,481	29,519	-	-
Warranty (Note 15)	<u>2,047,061</u>	<u>2,912,985</u>	<u>-</u>	<u>-</u>
	<u>4,763,852</u>	<u>5,531,382</u>	<u>-</u>	<u>-</u>
Non-current				
Employee Benefits	<u>249,523</u>	<u>229,643</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$

14. Provisions (cont)

Movement in surplus lease space provision – current

Balance at 1 January	110,141	87,901	-	-
Additional provision recognised	-	110,141	-	-
Payments made	<u>(22,499)</u>	<u>(87,901)</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>87,642</u>	<u>110,141</u>	<u>-</u>	<u>-</u>

The surplus lease space provisions relate to the leased premises at 3160 East Transcon Way, Tucson, Arizona, USA.

Movement in contract loss provision

Balance at 1 January	166,496	1,164,878	-	-
Additional provision recognised	-	-	-	-
Reductions resulting from re-measurement	<u>(144,074)</u>	<u>(998,382)</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>22,422</u>	<u>166,496</u>	<u>-</u>	<u>-</u>

The provision for contract losses is based on assessment by management of the additional costs to complete existing contracts not recoverable from the customer.

Movement in onerous contract provision

Balance at 1 January	-	172,253	-	-
Reductions resulting from re-measurement	<u>-</u>	<u>(172,253)</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2010	2009	2010	2009
	\$	\$	\$	\$
14. Provisions (cont)				
Movement on redundancy provision				
Balance at 1 January	-	-	-	-
Additional provision recognised for Tucson relocation	<u>201,185</u>	<u>-</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>201,185</u>	<u>-</u>	<u>-</u>	<u>-</u>
Movement on decommissioning costs				
Balance at 1 January	250,000	220,000	-	-
Additional provision recognised	<u>-</u>	<u>30,000</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>250,000</u>	<u>250,000</u>	<u>-</u>	<u>-</u>
The provision for decommissioning costs relate to an obligation to dismantle and refurbish a telescope at a future date.				
Movement on make good of leased premises				
Balance at 1 January	29,519	33,591	-	-
Reductions resulting from re-measurement	<u>(38)</u>	<u>(4,072)</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>29,481</u>	<u>29,519</u>	<u>-</u>	<u>-</u>
The provision for make good of leased premises costs relate to an obligation to make good the premises in at 3160 East Transcon Way, Tucson, Arizona, USA on expiry of the lease.				

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
15. Warranty Provisions				
Movement in warranty provision				
Balance at 1 January	2,912,985	2,235,633	-	-
Reductions resulting from re-measurement	(1,835,221)	-	-	-
Additional provisions recognised	<u>969,297</u>	<u>677,352</u>	<u>-</u>	<u>-</u>
Balance as at 31 December	<u>2,047,061</u>	<u>2,912,985</u>	<u>-</u>	<u>-</u>

The provision for warranty claims represents the present value of the directors' best estimate of the future sacrifice of economic benefits that will be required under the consolidated entity's 12-month warranty program for military products and telescopes. The estimate has been made on the basis of historical industry accepted warranty trends and may vary as a result of new materials, altered manufacturing processes or other events affecting product quality.

16. Employee Benefits

The aggregate employee benefits liability recognised in the financial statements is as follows:

Provision for employee entitlements

Current (Note 14)	<u>2,126,061</u>	<u>2,062,241</u>	<u>-</u>	<u>-</u>
Non-Current (Note 14)	<u>249,523</u>	<u>229,643</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$

17. Issued capital

Balance at the beginning of the financial year – Ordinary shares	75,383,567	75,383,567	75,383,567	75,383,567
Balance at the end of the financial year	<u>75,383,567</u>	<u>75,383,567</u>	<u>75,383,567</u>	<u>75,383,567</u>

Changes to the then Corporations Law abolished the authorised capital and par value concept in relation to share capital from 1 July 1998. Therefore, the company does not have a limited amount of authorised capital and issued shares do not have a par value.

Fully Paid Ordinary Shares	Number	Number	Number	Number
Balance at the beginning of financial year	56,845,926	56,845,926	56,845,926	56,845,926
Balance at end of financial year	<u>56,845,926</u>	<u>56,845,926</u>	<u>56,845,926</u>	<u>56,845,926</u>

Fully paid ordinary shares carry one vote per share and carry the right to dividends.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

18. Directors and Employee Share Option Plan

(a) Unlisted Options issued under the Employee Share Option Plan

On 28 June 2002, shareholders approved the adoption of an Employee Share Option Plan.

At the shareholders meeting held on 31 May 2007, shareholders approved the issue of options to directors at an exercise price of \$1.95 expiring on 31 May 2011 as follows:

- (a) 200,000 Options to each of Fred Bart, Ian Dennis, Mark Ureda and Robert Schuitema;
- (b) 964,800 Options to Dr Ben Greene in lieu of the previously approved 964,800 options at an exercise price of \$3.06. These 964,800 options issued to Dr Ben Greene were his entitlement for the year ended 31 December 2007.

During the financial year ended 31 December 2007, the Directors also approved the issue of 34,000 options at an exercise price of \$3.06 expiring on 30 September 2009 to Dr Craig Smith and 120,000 options at an exercise price of \$1.95 expiring on 31 May 2011.

On 10 December 2009 Directors approved the issue of 1,800,000 unlisted options to staff at an exercise price of \$1.30 exercisable on or before 8 December 2013.

The consolidated entity has an ownership-based compensation scheme for employees (including directors) of the company. In accordance with the provisions of the scheme, as approved by shareholders at a previous annual general meeting, employees with more than three months service with the company may be granted options to purchase ordinary shares at exercise prices determined by the directors based on market prices at the time the issue of options were made.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

18. Directors and Employee Share Option Plan (cont)

Each share option converts to one ordinary share in Electro Optic Systems Holdings Limited. No amounts are paid or payable by the recipient on receipt of the options. The options carry neither rights to dividends nor voting rights. Options may be exercised at any time from the date of vesting to the date of expiry.

The number of options granted is determined by the directors and takes into account the company's and individual achievements against both qualitative and quantitative criteria.

(b) Unlisted Options issued under the Employee Share Option Plan

	2011		2010	
	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$
Balance at the beginning of the financial year (i)	3,393,800	1.61	3,484,800	1.61
Granted during the year (ii)			-	-
Exercised during the year (iii)	-		-	
Lapsed during the year (iv)	(1,855,800)		(91,000)	1.61
Balance at the end of the financial year (v)	<u>1,538,000</u>	<u>1.30</u>	<u>3,393,800</u>	<u>1.61</u>
Exercisable at end of the year	<u>769,000</u>		<u>2,026,600</u>	

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

18. Directors and Employee Share Option Plan (cont)

(b) Unlisted Options issued under the Employee Share Option Plan (cont)

(i) Balance at the beginning of the year

2011	<u>Number</u>	<u>Grant date</u>	<u>Expiry date</u>	<u>Exercise Price</u>	<u>Fair value at grant date</u>
Staff options	60,000	31/5/07	31/5/11	\$1.95	\$44,100
Director options	1,564,800	31/5/07	31/5/11	\$1.95	\$1,150,128
Staff options	60,000	23/11/07	31/5/11	\$1.95	\$7,764
Staff options	<u>1,709,000</u>	10/12/09	8/12/13	\$1.30	<u>\$1,645,767</u>
	<u>3,393,800</u>				<u>\$2,847,759</u>

2010	<u>Number</u>	<u>Grant date</u>	<u>Expiry date</u>	<u>Exercise Price</u>	<u>Fair value at grant date</u>
Staff options	60,000	31/5/07	31/5/11	\$1.95	\$44,100
Director options	1,564,800	31/5/07	31/5/11	\$1.95	\$1,150,128
Staff options	60,000	23/11/07	31/5/11	\$1.95	\$7,764
Staff options	<u>1,800,000</u>	10/12/09	8/12/13	\$1.30	<u>\$1,733,400</u>
	<u>3,484,400</u>				<u>\$2,935,392</u>

Staff and Director options carry no rights to dividends and no voting rights.

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)****18. Directors and Employee Share Option Plan (cont)****(b) Unlisted Options issued under the Employee Share Option Plan (cont)****(ii) Granted during the year**

	Number	Grant Date	Expiry Date	Exercise Price	Fair Value Received \$	Fair value at grant date \$
2011	-	-	-	-	-	-
2010	-	-	-	-	-	-

There were no options issued during 2011.

All the options granted to staff during 2009 vest over a three year period with 20% vesting after 12 months, a further 30% after 2 years and the balance after 3 years. Options were priced using a modified Cox- Rubenstein binomial pricing model. Where relevant, the expected life used in the model has been adjusted based on management's best estimate for the effects of non-transferability, exercise restrictions and behavioural conditions. Expected volatility is based on the historical share price volatility over a two year period.

The following inputs were used in the model for grants during the year ended 31 December 2009:

Dividend yield	-
Expected volatility (linearly interpolated)	133.9%
Risk free interest rate	3.75%
Expected life of options	4 years
Grant date share price	\$1.20
Exercise price	\$1.30

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)****18. Directors and Employee Share Option Plan (cont)**

(b) Unlisted Options issued under the Employee Share Option Plan (cont)

(iii) Exercised during the year

	Number of Options Exercised	Grant Date	Exercise Date	Expiry Date	Exercise Price	No. of Shares Issued	Fair Value Received	Fair Value of Shares at Date of Issue
2011								
	Nil	-	-	-	-	Nil	Nil	Nil
2010								
	Nil	-	-	-	-	Nil	Nil	Nil

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

18. Directors and Employee Share Option Plan (cont)

(iv) Lapsed during the year

	Number of Options Lapsed	Grant Date	Exercise Date	Expiry Date	Exercise Price	No. of Shares Issued	Fair Value Received	Fair Value of Shares at Date of Issue
2011								
Staff	60,000	31/5/07	-	31/5/11	\$1.95	-	-	-
Staff	60,000	23/11/07	-	31/5/11	\$1.95	-	-	-
Directors	1,564,800	31/5/07	-	31/5/11	\$1.95	-	-	-
Staff	<u>171,000</u>	10/12/09	-	8/12/13	\$1.30	-	-	-
	<u>1,855,800</u>							
2010								
Staff	91,000	10/12/09	-	8/12/13	\$1.30	-	-	-

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)****18. Directors and Employee Share Option Plan (cont)**

(v) Balance at the end of the financial year

2011	<u>Number</u>	<u>Grant date</u>	<u>Expiry date</u>	<u>Exercise Price</u>	<u>Fair value at grant date</u>
Staff options	<u>1,538,000</u>	10/12/09	8/12/13	\$1.30	<u>\$1,481,094</u>
	<u>1,538,000</u>				

2010	<u>Number</u>	<u>Grant date</u>	<u>Expiry date</u>	<u>Exercise Price</u>	<u>Fair value at grant date</u>
Staff options	60,000	31/5/07	31/5/11	\$1.95	\$44,100
Director options	1,564,800	31/5/07	31/5/11	\$1.95	\$1,150,128
Staff options	60,000	23/11/07	31/5/11	\$1.95	\$7,764
Staff options	<u>1,709,000</u>	10/12/09	8/12/13	\$1.30	<u>\$1,645,767</u>
	<u>3,393,800</u>				<u>\$2,847,759</u>

Staff and Director options carry no rights to dividends and no voting rights.

All the options granted to staff during 2009 vest over a three year period with 20% vesting after 12 months, a further 30% after 2 years and the balance after 3 years.

No options were issued during 2010.

No options were issued during 2011.

The difference between the total market value of the options issued during the financial year, at the date of issue, and the total amount received from employees (nil) is recognised in the financial statements over the vesting period as disclosed in Note 18 to the financial statements.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
19. Reserves				
Foreign currency translation	45,780	573,402	-	-
Employee equity-settled benefits	<u>7,523,594</u>	<u>7,123,130</u>	<u>7,523,594</u>	<u>7,123,130</u>
	<u>7,569,374</u>	<u>7,696,532</u>	<u>7,523,594</u>	<u>7,123,130</u>
Foreign currency translation				
Balance at beginning of financial year	573,402	1,126,450	-	-
Translation of foreign operations	<u>(527,622)</u>	<u>(553,048)</u>	<u>-</u>	<u>-</u>
Balance at end of financial year	<u>45,780</u>	<u>573,402</u>	<u>-</u>	<u>-</u>
Exchange differences relating to the translation from US dollars, being the functional currency of the consolidated entity's foreign controlled entities in the USA, Euros, being the functional currency of the consolidated entity's foreign controlled entity in Germany and Singaporean dollars, being the functional currency of the consolidated entity's foreign controlled entity in Singapore, into Australian dollars are brought to account by entries made directly to the foreign currency translation reserve.				
Employee equity-settled benefits				
Balance at beginning of financial year	7,123,130	6,382,838	7,123,130	6,382,838
Share based payment	<u>400,464</u>	<u>740,292</u>	<u>400,464</u>	<u>740,492</u>
Balance at end of financial year	<u>7,523,594</u>	<u>7,123,130</u>	<u>7,523,594</u>	<u>7,123,130</u>
The employee equity-settled benefits reserve arises on the grant of share options to directors and executives under the Employee Share Option plan. Further information about share-based payments to employees is made in note 18 to the financial statements.				

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
20. Accumulated Losses				
Balance at beginning of financial year	(70,472,882)	(73,648,024)	(77,282,451)	(81,328,423)
Net Profit/(loss) attributable to members of the parent entity	<u>180,188</u>	<u>3,175,142</u>	<u>(4,398,147)</u>	<u>4,045,972</u>
Balance at end of financial year	<u>(70,292,694)</u>	<u>(70,472,882)</u>	<u>(81,680,598)</u>	<u>(77,282,451)</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

21. Key management personnel compensation

The key management personnel of Electro Optic Systems Holdings Limited during the year were:

Mr Fred Bart (Chairman, Non executive)

Dr Ben Greene (Chief Executive Officer)

Mr Ian Dennis (Non-executive)

Mr Mark Ureda (Non-executive)

Lt Gen Peter Leahy AC (Non-executive)

Mr Kevin Scully (Non-executive) – Commenced 19 September 2011

Mr Ron Thompson (Group General Manager) – retired 30 September 2011

Dr Craig Smith (Chief Executive Officer of EOS Space Systems Pty Limited)

Mr Mark Bornholt (Chief Executive Officer Defence Systems) Commenced 21 March 2011

Mr John Palisi (Chief Financial Officer – Electro Optic Systems Pty Limited) resigned 3 February 2012

Mr Hugo Keyner (Chief Executive Officer EOST)

Key management personnel compensation policy

The board reviews the remuneration packages of all key management personnel on an annual basis. Remuneration packages are reviewed and determined with regard to current market rates and are benchmarked against comparable industry salaries, adjusted by a performance factor to reflect changes in the performance of the company.

The aggregate compensation of the key management personnel of the consolidated entity and company is set out below:

	Consolidated		Company	
	2011	2010	2011	2010
	\$	\$	\$	\$
Short-term employee benefits	1,378,322	1,188,873	188,410	158,438
Post-employment benefits	99,342	84,350	12,240	7,470
Share-based payment	142,388	317,064	-	79,287
Other long term benefits	<u>42,760</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>1,662,812</u>	<u>1,590,287</u>	<u>200,650</u>	<u>244,735</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

21. Key management personnel compensation (Cont)

The compensation of the non executive directors is paid by the holding company and is the same for both the holding company and the consolidated entity. The compensation for Dr Ben Greene and the senior executives are paid by subsidiary companies.

2011	Short term		Post Employment	Equity settled Share based payments	Other Long	Total
	Salary & Fees \$	Non- monetary \$	Super- annuation \$	Options \$	Term Benefits \$	\$
Directors						
Mr Fred Bart	61,000	-	5,490	-	-	66,490
Dr Ben Greene*	300,000	39,182	27,000			366,182
Mr Ian Dennis	37,500	-	3,375	-	-	40,875
Mr Mark Ureda	40,875	-	-	-	-	40,875
Lt Gen Peter Leahy AC	37,500	-	3,375	-	-	40,875
Mr Kevin Scully	<u>11,535</u>	<u>-</u>	<u>-</u>	<u>-</u>		<u>11,535</u>
	<u>488,410</u>	<u>39,182</u>	<u>39,240</u>	<u>-</u>	<u>-</u>	<u>566,832</u>
Executives						
Mr Ron Thompson	172,083	-	13,288	35,597	42,760	263,728
Dr Craig Smith	197,532	-	17,750	35,597	-	250,879
Mr Mark Bornholt	128,423	-	11,340	-	-	139,763
Mr John Palisi	196,946	-	17,724	35,597	-	250,267
Mr Hugo Keyner	<u>154,889</u>	<u>854</u>	<u>-</u>	<u>35,597</u>	<u>-</u>	<u>191,340</u>
	<u>849,873</u>	<u>854</u>	<u>60,102</u>	<u>142,388</u>	<u>42,760</u>	<u>1,095,977</u>
	<u>1,338,283</u>	<u>40,036</u>	<u>99,342</u>	<u>142,388</u>	<u>42,760</u>	<u>1,662,809</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

21. Key management personnel compensation (Cont)

2010	Short term		Post Employment	Equity settled Share based payments	Other Long	Total
	Salary & Fees \$	Non- monetary \$	Super- annuation \$	Options \$	Term Benefits \$	\$
Directors						
Mr Fred Bart	55,500	-	2,745	10,203	-	68,448
Dr Ben Greene*	273,001	57,616	27,000	49,218	-	406,835
Mr Ian Dennis	33,750	-	1,688	10,203	-	45,641
Mr Mark Ureda	35,438	-	-	10,203	-	45,641
Lt Gen Peter Leahy AC	<u>33,750</u>	<u>-</u>	<u>3,038</u>	<u>-</u>	<u>-</u>	<u>36,788</u>
	<u>431,439</u>	<u>57,616</u>	<u>34,471</u>	<u>79,827</u>	<u>-</u>	<u>603,353</u>
Executives						
Mr Ron Thompson	174,321	-	16,182	58,376	-	248,879
Dr Craig Smith	190,392	-	17,103	62,109	-	269,604
Mr John Palisi	184,387	-	16,594	58,376	-	259,357
Mr Hugo Keyner	<u>140,804</u>	<u>9,914</u>	<u>-</u>	<u>58,376</u>	<u>-</u>	<u>209,094</u>
	<u>689,904</u>	<u>9,914</u>	<u>49,879</u>	<u>237,237</u>	<u>-</u>	<u>986,934</u>
	<u>1,121,343</u>	<u>67,530</u>	<u>84,350</u>	<u>317,064</u>	<u>-</u>	<u>1,590,287</u>

* Executive director

Non-monetary includes the provision for motor vehicles and health benefits.
Further details on options can be found in note 18.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

22. Notes to the Cash Flow Statement

(a) Reconciliation of Cash and cash equivalents

For the purposes of the cash flow statement, cash includes cash on hand and at call deposits with banks or financial institutions, investments in money market instruments maturing within less than two months and net of bank overdrafts. Cash at the end of the financial year as shown in the statements of cash flows is reconciled to the related items in the statement of financial position as follows:

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated 31 December 2011 \$	31 December 2010 \$	Company 31 December 2011 \$	31 December 2010 \$
22. Notes to the Cash Flow Statement (Cont)				
Cash and cash equivalents	<u>4,885,761</u>	<u>8,088,355</u>	<u>1,324,726</u>	<u>5,356,661</u>
(b) Reconciliation of Profit for the period to net cash flows from operating activities				
Profit/(loss) for the period	180,188	3,175,142	(4,398,147)	4,045,972
(Profit)/Loss on disposal of fixed assets	(2,287)	15,167	-	-
Equity settled share-based payments	400,464	740,292	-	90,029
Amortisation of intangibles	131,533	148,474	-	-
Depreciation of fixed assets	426,512	498,816	1,095	1,825
Impairment	(333,561)	459,953	-	-
Foreign exchange movements	(520,741)	37,372	-	-
Provision for non-recovery of loan	-	-	3,573,685	(5,207,141)
Provision for non-recovery of investment	-	-	400,464	650,263
(Increase)/decrease in assets				
Current receivables	5,674,434	(8,049,098)	(6,603)	(2,223)
Inventories	898,528	574,778	-	-
Other current assets	152,204	(125,202)	-	-
Increase/(decrease) in liabilities				
Provisions	(747,650)	(269,446)	-	-
Current trade and other payables	(1,146,272)	2,528,608	(28,474)	(19,838)
Other	(608,056)	207,852	-	-
Borrowings for inventory	(4,182,672)	(2,127,421)	-	-
Deferred income and amounts due to customers under construction contracts	<u>(4,100,935)</u>	<u>5,298,326</u>	<u>-</u>	<u>-</u>
Net cash inflows/(outflows) from operating activities	<u>(3,778,311)</u>	<u>3,113,613</u>	<u>(458,250)</u>	<u>(441,113)</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

22. Notes to the Cash Flow Statement (Cont)

(c) Non-Cash Operating Activities

In December 2010, a subsidiary company EOS Defense Systems, Inc acquired 32 completed inventory units for a purchase price of US\$5,300,000, payable in certain instalments in accordance with and under the terms of a promissory note executed by EOS Defense Systems, Inc. The promissory note provides for interest to be paid at 5% per annum, with all principal and interest due in full by 31 January 2012.

In September 2011, a subsidiary company EOS Defense Systems, Inc acquired 21 completed inventory units for a purchase price of US\$752,027, payable in certain instalments in accordance with and under the terms of a promissory note executed by EOS Defense Systems, Inc. The promissory note provides for interest to be paid at 5% per annum, with all principal and interest due in full by 31 January 2012.

23. Related party disclosures

(a) Equity interests in related parties

Details of the percentage of ordinary shares held in subsidiaries are disclosed in Note 24.

(b) Key management personnel compensation

Details of key management personnel compensation are disclosed in Note 21.

(c) Key management personnel equity holdings (represented by holdings of fully paid ordinary shares in Electro Optic Systems Holdings Limited)

2011	Balance at 1/1/11	Granted as remuneration	Received on exercise of options	Net other change	Balance at 31/12/11
	No.	No.	No.	No.	No.
Mr Fred Bart	5,309,075	-	-	-	5,309,075
Dr Ben Greene	3,954,185	-	-	-	3,954,185
Mr Ian Dennis	170,050	-	-	-	170,050
Mr Mark Ureda	-	-	-	-	-
Lt Gen Peter Leahy AC	15,000	-	-	-	15,000
Mr Kevin Scully	-	-	-	-	-
Mr Mark Bornholt	-	-	-	-	-
Mr Ron Thompson	347,745	-	-	-	347,745
Dr Craig Smith	89,450	-	-	-	89,450
Mr John Palisi	-	-	-	-	-
Mr Hugo Keyner	-	-	-	-	-

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

23. Related party disclosures (cont)

2010	Balance at 1/1/10	Granted as remuneration	Received on exercise of options	Net other change	Balance at 31/12/10
	No.	No.	No.	No.	No.
Mr Fred Bart	5,309,075	-	-	-	5,309,075
Dr Ben Greene	7,452,485	-	-	(3,498,300)	3,954,185
Mr Ian Dennis	170,050	-	-	-	170,050
Mr Mark Ureda	-	-	-	-	-
Lt Gen Peter Leahy AC	-	-	-	15,000	15,000
Mr Ron Thompson	347,745	-	-	-	347,745
Dr Craig Smith	89,450	-	-	-	89,450
Mr John Palisi	-	-	-	-	-
Mr Hugo Keyner	-	-	-	-	-

(d) Key management personnel option holdings

2011	Balance at 1/1/11	Granted as remuneration	Exercised (Lapsed)	Balance at 31/12/11	Balance vested and exercisable at 31/12/11	Options vested during year
	No.	No.	No.	No.	No.	
Mr Fred Bart	200,000	-	(200,000)	-	-	-
Dr Ben Greene	964,800	-	(964,800)	-	-	-
Mr Ian Dennis	200,000	-	(200,000)	-	-	-
Mr Mark Ureda	200,000	-	(200,000)	-	-	-
Lt Gen Peter Leahy AC	-	-	-	-	-	-
Mr Kevin Scully	-	-	-	-	-	-
Mr Mark Bornholt	-	-	-	-	-	-
Mr Ron Thompson	160,000	-	-	160,000	80,000	48,000
Dr Craig Smith	280,000	-	(120,000)	160,000	80,000	48,000
Mr John Palisi	160,000	-	-	160,000	80,000	48,000
Mr Hugo Keyner	160,000	-	-	160,000	80,000	48,000

The Company did not issue any options during the year ended 31 December 2010 and 2011 to directors. Refer to Note 18 for further details of options outstanding.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

23. Related party disclosures (cont)

2010	Balance at 1/1/10	Granted as remuner- ation	Exercised (Lapsed)	Balance at 31/12/10	Balance vested and exercisable at 31/12/10	Options vested during year
	No.	No.	No.	No.	No.	
Mr Fred Bart	200,000	-	-	200,000	200,000	100,000
Dr Ben Greene	964,800	-	-	964,800	964,800	482,400
Mr Ian Dennis	200,000	-	-	200,000	200,000	100,000
Mr Mark Ureda	200,000	-	-	200,000	200,000	100,000
Lt Gen Peter Leahy AC	-	-	-	-	-	-
Mr Ron Thompson	160,000	-	-	160,000	32,000	32,000
Dr Craig Smith	280,000	-	-	280,000	152,000	92,000
Mr John Palisi	160,000	-	-	160,000	32,000	32,000
Mr Hugo Keyner	160,000	-	-	160,000	32,000	32,000

Refer to Note 18 for further details of options outstanding.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

23. Related party disclosures (cont)

(e) Transactions with other related parties

Other related parties includes:

- the parent entity;
- entities with significant influence over the consolidated entity; and
- subsidiaries.

Amounts receivable from entities in the wholly-owned group are disclosed in note 8 to the financial statements.

Certain entities within the group have lent money to other entities within the wholly-owned group on an interest free basis. The amounts receivable by the ultimate parent entity in the wholly-owned group are disclosed in note 8 to the financial statements. The ultimate parent entity in the wholly-owned group has provided for this amount based upon the net asset position of the controlled entities.

(f) Other transactions with key management personnel

During the year, the Company paid a total of \$66,490 (2010: \$58,245) to 4F Investments Pty Limited, a company associated with Mr Fred Bart in respect of directors fees and superannuation for Fred Bart.

During the year, the Company received \$4,361 (2010: \$13,428) from 4F Investments Pty Limited, a company associated with Mr Fred Bart in respect of shared Sydney office facilities.

During the year, the Company paid \$40,875 (2010: \$35,438) to Dennis Corporate Services Pty Limited, a company associated with Mr Ian Dennis in respect of directors fees and superannuation for Ian Dennis.

During the year, the Company paid \$120,000 (2010: \$120,000) to Dennis Corporate Services Pty Limited, a company associated with Mr Ian Dennis in respect of consulting fees for company secretarial and accounting services.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

23. Related party disclosures (cont)

(g) Parent entity

The parent entity in the consolidated group is Electro Optic Systems Holdings Limited.

24. Controlled Entities

Name of Entity	Country of Incorporation	December 2011 %	December 2010 %
Parent Entity			
Electro Optic Systems Holdings Limited	Australia #		
Controlled Entities			
Electro Optic Systems Pty Limited	Australia #	100	100
Fire Control Systems Pty Limited	Australia #	100	100
FCS Technology Holdings Pty Limited	Australia #	100	100
EOS Space Systems Pty Limited	Australia #	100	100
EOS Optronics GmbH	Germany	100	100
EOS Defense Systems Pte Limited	Singapore	100	-
EOS USA, Inc. (Inc in Nevada)	USA	100	100
EOS Technologies, Inc. (Inc in Arizona)	USA	100	100
EOS Defense Systems, Inc (Inc in Arizona)	USA	100	100

These companies form part of the Australian consolidated tax entity.

All entities are audited by Deloitte Touche Tohmatsu.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

25. Contingent Liabilities

a) Entities within the consolidated entity are involved in contractual disputes in the normal course of contracting operations. The directors believe that the entities within the consolidated entity can settle any contractual disputes with customers and should any customers commence legal proceedings against the company, the directors believe that any actions can be successfully defended. As at the date of this report no legal proceedings have been commenced against any entity within the group.

b) On 10 June 2010 the parent company provided a guarantee in respect of an advance payment received of US\$3,531,255 and A\$2,136,443 by a subsidiary company in relation to the supply of 91 remote weapon systems to a customer. The guarantee can be satisfied by the delivery of the remote weapon systems or if the subsidiary company is in breach of its obligations it will be required to deliver shares in the parent company for the outstanding amount of the guarantee less the total value of any deliverable items actually delivered and accepted by the customer. The value of shares to be issued to satisfy the guarantee will be based on the average weighted share price over the period of 60 days prior to the guarantee being called. As at 31 December 2011, the amount still outstanding subject to the guarantee were US\$2,106,901 and A\$1,948,616.

c) In December 2010, a subsidiary company EOS Defense Systems, Inc acquired 32 completed inventory units for a purchase price of US\$5,300,000, payable in certain instalments in accordance with and under the terms of a promissory note executed by EOS Defense Systems, Inc. The promissory note provides for interest to be paid at 5% per annum, with all principal and interest due in full by 31 January 2012. The company is required to repay US\$165,625 for each unit sold on receipt of the payment from the end customer. The parent company, Electro Optic Systems Holdings Limited has guaranteed the repayment of the debt. As at 31 December 2011, there was US\$1,159,375 owing in respect of 7 units. Since the end of the financial year, the note has been repaid in full.

d) In September 2011, a subsidiary company EOS Defense Systems, Inc acquired 21 completed inventory units for a purchase price of US\$752,027, payable in certain instalments in accordance with and under the terms of a promissory note executed by EOS Defense Systems, Inc. The promissory note provides for interest to be paid at 5% per annum, with all principal and interest due in full by 31 January 2012. The company is required to repay US\$35,811 for each unit sold on receipt of the payment from the end customer. The parent company, Electro Optic Systems Holdings Limited has guaranteed the repayment of the debt. As at 31 December 2011, there was US\$752,027 owing in respect of 21 units. Since the end of the financial year, the note has been repaid in full.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		The Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
26. Capital and Leasing Commitments				
(a) Finance leasing commitments				
Payable – minimum future lease payments				
not later than one year	131,634	135,847	-	-
later than one year and not later than five years	125,701	257,335	-	-
later than five years	-	-	-	-
Minimum lease payments	257,335	393,182	-	-
Less future finance charges	(26,588)	(55,436)	-	-
Total lease liability	<u>230,747</u>	<u>337,746</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		The Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
26. Capital and Leasing Commitments (cont)				
(b) Finance leasing commitments				
Payable – Present value of minimum future lease payments				
not later than one year	118,033	106,999	-	-
later than one year and not later than five years	112,714	230,747	-	-
later than five years	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Present value of minimum lease payments	<u>230,747</u>	<u>337,746</u>	<u>-</u>	<u>-</u>
Represented by:				
Current liability (Note 13)	113,524	106,712	-	-
Non-current liability (Note 13)	<u>117,223</u>	<u>231,034</u>	<u>-</u>	<u>-</u>
	<u>230,747</u>	<u>337,746</u>	<u>-</u>	<u>-</u>
(c) Operating lease commitments				
Non-cancellable operating leases contracted for but not recognised in the financial statements:				
Payable:				
not later than one year	556,453	831,540	-	-
later than one year and not later than five years	-	1,365,639	-	-
later than five years	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>556,453</u>	<u>2,197,179</u>	<u>-</u>	<u>-</u>

Operating Leases

Leasing arrangements
Operating leases relate to:

The lease on the US premises at 925 West Grant Road, Tuscon, Arizona expired on 30 June 2011 and the company has vacated the premises.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

26. Capital and Leasing Commitments (cont)

Premises at 3160 East Transcon Way, Tuscon Arizona with a lease term which expires on 30 April 2012 following an agreed lease variation with the landlord. There is no option to renew after 30 April 2012 and future lease payments are fixed under the contract. The landlord has agreed that the company can continue to lease the premises at a reduced rate on a month to month basis until the property is vacated. There is no option to purchase the property. A liability has been recognised relating to the lease incentive received upon signing of the lease and a liability has been recognised relating to surplus lease space.

Premises in Queanbeyan, Australia for a 5 year period to 31 December 2008 with a 5 year option. The Company has the first right of refusal in respect of the purchase of the property. The Company is on a month to month basis whilst a new lease is negotiated.

Finance Leases

Leasing arrangements

Finance leases relate to motor vehicles, computer and office equipment with lease terms of between one and three years. The consolidated entity has options to purchase the computer and office equipment for a nominal amount at the conclusion of the lease arrangements. The consolidated entity has options to purchase motor vehicles for agreed residual amounts at the conclusion of the lease arrangements.

27. Subsequent Events

Since the end of the financial year, the Group has repaid the two secured promissory notes detailed in Note 13. The Chief Financial Officer, Mr John Palisi resigned on 3 February 2012 and has been replaced by Mr Scott Lamond as Acting Chief Financial Officer. The Common Remotely Operated Weapons Stations ("CROWS") bid for the US Army was lodged by Northrop Grumman Corporation ("NGC") on 23 March 2012 with NGC as the prime contractor and EOS as a first tier subcontractor. Apart from the above, the Directors are not aware of any significant subsequent events since the end of the financial period and up to the date of this report.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies

The Group's principal financial instruments comprise receivables, payables, borrowings, finance leases, cash and short term deposits.

Due to the small size of the group significant risk management decisions are taken by the board of directors. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

The Group does not use derivative financial instruments to hedge these risk exposures.

Risk Exposures and Responses

(a) Interest rate risk

The Group's exposure to market interest rates relates primarily to the Group's cash holdings.

At balance date, the Group had the following mix of financial assets and liabilities exposed to Australian variable interest rate risk that are not designated in cash flow hedges:

	Consolidated		Company	
	2011	2010	2011	2010
	\$	\$	\$	\$
Financial assets				
Cash and cash equivalents	<u>4,885,761</u>	<u>8,088,355</u>	<u>1,324,726</u>	<u>5,356,661</u>

The Group constantly analyses its interest rate exposure. Within this analysis consideration is given to potential renewals of existing positions, alternative financing and the mix of fixed and variable interest rates.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont)

At 31 December 2011, if interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

Judgements of reasonably possible movements	Post Tax Profit Higher/(Lower)		Equity Higher/(Lower)	
	2011 \$	2010 \$	2011 \$	2010 \$
Consolidated				
+1% (100 basis points)	48,858	80,884	48,858	80,884
-.5% (50 basis points)	<u>(24,429)</u>	<u>(40,442)</u>	<u>(24,429)</u>	<u>(40,442)</u>
Company				
+1% (100 basis points)	13,247	53,567	13,247	53,567
-.5% (50 basis points)	<u>(6,624)</u>	<u>(26,783)</u>	<u>(6,624)</u>	<u>(26,783)</u>

The movements in profits are due to higher interest rates on cash balances. The cash balances were lower in 2011 than in 2010 and accordingly the sensitivity is lower.

(b) Foreign currency risk

As a result of significant operations in the United States and purchases of inventory denominated in United States Dollars, the Group's statement of financial position can be affected significantly by movements in the US\$/A\$ exchange rates. Exchange rates are managed within approved policy parameters using natural hedges and no derivatives are used.

The Group also has transactional currency exposures. Such exposures arise from sales or purchases by an operating entity in currencies other than the functional currency.

The policy of the Group is to convert surplus foreign currencies to Australian dollars. The group also holds cash deposits in US dollars to secure US dollar bank guarantees to overseas customers.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont)

At 31 December 2011, the Group had the following exposure to US\$ foreign currency:

	Consolidated		Company	
	2011	2010	2011	2010
	\$	\$	\$	\$
Financial assets				
Cash and cash equivalents	241,350	1,799,530	12,806	956
Trade and other receivables	<u>4,350,913</u>	<u>4,475,387</u>	<u>-</u>	<u>-</u>
	<u>4,592,263</u>	<u>6,274,917</u>	<u>12,806</u>	<u>956</u>
Financial liabilities				
Trade and other payables	3,504,284	9,533,757	-	-
Promissory note	1,878,343	5,214,996	-	-
Finance leases	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>5,382,627</u>	<u>14,748,753</u>	<u>-</u>	<u>-</u>
Net exposure	<u>(790,364)</u>	<u>(8,473,836)</u>	<u>12,806</u>	<u>956</u>

All US\$ denominated financial instruments were translated to A\$ at 31 December 2011 at the exchange rate of 1.0176 (2010: 1.0163).

At 31 December 2011, had the Australian Dollar moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

Judgements of reasonably possible movements	Post Tax Profit Higher/(Lower)		Equity Higher/(Lower)	
	2011	2010	2011	2010
	\$	\$	\$	\$
Consolidated				
AUD/USD +10%	96,491	770,349	96,491	770,349
AUD/USD -5%	<u>(13,068)</u>	<u>(445,991)</u>	<u>(13,068)</u>	<u>(445,991)</u>
Company				
AUD/USD +10%	(1,165)	(96)	(1,165)	(96)
AUD/USD -5%	<u>583</u>	<u>48</u>	<u>583</u>	<u>48</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont)

Management believes the balance date risk exposures are representative of risk exposure inherent in financial instruments.

As noted, foreign currency transactions entered into during the financial year are managed within approved policy parameters using natural hedges. The director's do not consider that the net exposure to foreign currency transactions is material after considering the effect of natural hedges.

(c) Credit risk management

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in a financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties which are continuously monitored.

The credit risk on liquid funds is limited because the counterparties are banks with high credit-ratings assigned by international credit agencies.

(d) Liquidity risk management

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due.

Ultimate responsibility for liquidity risk management rests with the board of directors, who has built an appropriate risk management framework for the management of the Group's short, medium and long term funding and liquidity requirements. The Group manages liquidity by maintaining adequate cash reserves by continuously monitoring forecast and actual cash flows and managing maturity profiles of financial assets. Significant uncertainties relating to the ability of the company and the consolidated entity to continue as going concerns and pay their debts as and when they fall due are set out in Note 1(a).

Liquidity and interest tables

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

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont) (d) Liquidity risk management (cont)

Consolidated	Weighted average effective interest rate %	Less than 1 month \$	1-3 months \$	3 months to 1 year \$	1-5 years \$
2011					
Other non interest bearing liabilities	0.00	3,519,230	-	-	-
Finance lease liability	9.95	10,970	21,940	98,730	125,701
Promissory note	5.00	<u>1,925,302</u>	<u>-</u>	<u>-</u>	<u>-</u>
2010					
Other non interest bearing liabilities	0.00	5,274,559	-	-	-
Finance lease liability	9.92	11,321	22,642	101,889	257,335
Promissory note	5.00	<u>21,729</u>	<u>43,458</u>	<u>5,280,183</u>	<u>-</u>
		<u>5,307,609</u>	<u>65,100</u>	<u>5,382,072</u>	<u>257,335</u>
Company	Weighted average effective interest rate %	Less than 1 month \$	1-3 months \$	3 months to 1 year \$	1-5 years \$
2011					
Other non interest bearing liabilities	0.00	<u>120,961</u>	<u>-</u>	<u>-</u>	<u>-</u>
2010					
Other non interest bearing liabilities	0.00	<u>149,705</u>	<u>-</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont) (d) Liquidity risk management (cont)

The following tables detail the Company's and the Group's remaining contractual maturity for its non-derivative financial assets. The tables have been drawn up based on the undiscounted contractual maturities of the financial assets including interest that will be earned on these assets except where the Company/Group anticipates that the cash flow will occur in a different period.

Consolidated	Weighted average effective interest rate %	Less than 1 month \$	1-3 months \$	3 months to 1 year \$	1-5 years \$
2011					
Non interest bearing	-	259,045	-	-	-
Variable interest rate instruments	-	-	-	-	-
Fixed interest rate instruments	3.64	<u>4,434,199</u>	<u>40,336</u>	-	-
		<u>4,693,244</u>	<u>40,336</u>	-	-
2010					
Non interest bearing	-	1,518,862	-	-	-
Variable interest rate instruments	-	-	-	-	-
Fixed interest rate instruments	4.62	<u>6,388,450</u>	<u>40,336</u>	-	-
		<u>7,907,312</u>	<u>40,036</u>	-	-

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

28. Financial risk management objectives and policies (cont)

(d) Liquidity risk management (cont)

Company	Weighted average effective interest rate %	Less than 1 month \$	1-3 months \$	3 months to 1 year \$	1-5 years \$
2011					
Non interest bearing	-	12,806	-	-	-
Variable interest rate instruments	-	-	-	-	-
Fixed interest rate instruments	4.54	<u>1,316,783</u>	<u>-</u>	<u>-</u>	<u>-</u>
2010					
Non interest bearing	-	956	-	-	-
Variable interest rate instruments	-	-	-	-	-
Fixed interest rate instruments	5.12	<u>5,338,385</u>	<u>-</u>	<u>-</u>	<u>-</u>

(e) Price risk

The Group's exposure to commodity price risk is minimal. The Group does not make investments in equity securities.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

29. Segment Information

AASB 8 requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess performance. The identification of the Group's reportable segments has not changed from those disclosed in the previous Annual Report.

The consolidated entity operates in Australia, USA, Singapore and Germany in the development, manufacture and sale of telescopes and dome enclosures, laser satellite tracking systems and the manufacture of electro-optic fire control systems.

Product and Services within each Segment

Space Systems

EOS is a global supplier of large optical systems. During the period the consolidated entity continued the process of completing existing contracts.

Space Surveillance

EOS's laser-based space surveillance systems have been demonstrated in customer trials and EOS is now well-placed to be a major contributor to the next generation of space tracking capability. Future business is dependent on large government contracts being awarded in the space sector.

In addition, EOS has substantial space resources in its own right, and may enter the market for space data provision in the future.

Defence

EOS develops, manufactures and markets advanced fire control, surveillance, and weapon systems to approved military customers. These products either replace or reduce the role of a human operator for a wide range of existing and future weapon systems in the US, Australia and other markets.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

29. Segment Information (Cont)

Segment Revenues

	Consolidated	
	31 December 2011 \$	31 December 2010 \$
Space systems	824,200	1,431,169
Space surveillance	3,214,813	2,165,902
Defence	<u>28,387,523</u>	<u>29,952,882</u>
Total of all segments	32,426,536	33,549,953
Unallocated	<u>348,855</u>	<u>278,705</u>
Total	<u>32,775,391</u>	<u>33,828,658</u>

Segment Results

Space systems	(577,615)	(1,519,583)
Space surveillance	(395,895)	(589,698)
Defence	<u>1,978,160</u>	<u>6,445,592</u>
Total of all segments	1,004,650	4,336,311
Unallocated	<u>(824,462)</u>	<u>(1,169,169)</u>
Profit before income tax expense	180,188	3,175,142
Income tax expense	—	—
Profit for the period	<u>180,188</u>	<u>3,175,142</u>

The revenue reported above represents revenue from external customers. There were no intersegment sales during the period. There were no discontinued operations during the period. The consolidated entity has two customers who each provided in excess of 10% of consolidated revenue. These two customers are within the Defence segment with total revenue of \$24,021,715 (2010 - \$28,577,597).

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

29. Segment Information (cont)

Segment Assets and Liabilities

	Assets		Liabilities	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
Space systems	434,378	1,144,226	803,320	1,795,473
Space surveillance	1,090,208	826,728	2,966,952	1,824,477
Defence	<u>22,262,394</u>	<u>28,606,967</u>	<u>12,011,474</u>	<u>22,101,362</u>
Total all segments	23,786,980	30,577,921	15,781,746	25,721,312
Unallocated	<u>4,885,761</u>	<u>8,088,355</u>	<u>230,748</u>	<u>337,747</u>
Consolidated	<u>28,672,741</u>	<u>38,666,276</u>	<u>16,012,494</u>	<u>26,059,059</u>

Assets used jointly by reportable segments are allocated on the basis of the revenue earned by the individual reportable segments.

Other Segment Information

	Depreciation, impairment and amortization of segment assets		Acquisition of segment assets	
	31	31	31	31
	December	December	December	December
	2011	2010	2011	2010
	\$	\$	\$	\$
Space systems	1,619	11,710	7,953	34,428
Space surveillance	6,316	17,721	27,598	39,803
Defence	<u>685,388</u>	<u>894,587</u>	<u>140,140</u>	<u>1,958,629</u>
Total all segments	693,323	924,018	175,691	2,032,860
Unallocated	<u>600,372</u>	<u>34,751</u>	<u>-</u>	<u>-</u>
Consolidated	<u>92,951</u>	<u>958,769</u>	<u>175,691</u>	<u>2,032,860</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

29. Segment Information (cont)

Information on Geographical Segments

31 December 2011

Geographical Segments	Revenue from External Customers \$	Segment Assets \$	Acquisition of Segment Assets \$
Australasia	28,942,040	22,878,566	138,444
North America	3,810,273	5,692,857	31,104
Germany	<u>23,078</u>	<u>101,318</u>	<u>6,142</u>
Total	<u>32,775,391</u>	<u>28,672,741</u>	<u>175,690</u>

31 December 2010

Geographical Segments	Revenue from External Customers \$	Segment Assets \$	Acquisition of Segment Assets \$
Australasia	32,044,356	25,194,724	372,589
North America	1,646,906	13,427,190	1,658,530
Germany	<u>137,396</u>	<u>44,362</u>	<u>1,741</u>
Total	<u>33,828,658</u>	<u>38,666,276</u>	<u>2,032,860</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

	Consolidated		Company	
	31	31	31	31
	December	December	December	December
	2011	2010	2010	2010
	\$	\$	\$	\$
30. Construction Contracts				
Construction work in progress	<u>9,662,837</u>	<u>31,801,315</u>	<u>-</u>	<u>-</u>
Less				
Provision for losses	(22,422)	(166,496)	-	-
Progress billings	<u>(14,411,594)</u>	<u>(38,309,745)</u>	<u>-</u>	<u>-</u>
	<u>(4,771,179)</u>	<u>(6,674,926)</u>	<u>-</u>	<u>-</u>
Recognised and included in the financial statements as amounts due:				
From customers under construction contracts:				
Current (note 6)	<u>599,620</u>	<u>2,795,808</u>	<u>-</u>	<u>-</u>
To customers under construction contracts:				
Current (note 12)	<u>(5,370,799)</u>	<u>(9,470,734)</u>	<u>-</u>	<u>-</u>
	<u>(4,771,179)</u>	<u>(6,674,926)</u>	<u>-</u>	<u>-</u>
Retentions included in progress billings	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2011 (cont)

31. Additional Company Information

Electro Optic Systems Holdings Limited is a listed public company in Australia, incorporated in Australia. The company and its subsidiaries operate in Australia, North America, Singapore and Germany.

Registered Office

Suite 2, Level 12
75 Elizabeth Street
Sydney NSW 2000
Australia

Tel: 02 9233 3915

Fax: 02 9232 3411

Principal Place of Business

EOS House
Mt Stromlo Observatory
Cotter Road
Weston Creek ACT 2611
Australia

Tel: 02 6222 7900

Fax: 02 6299 7687

USA Operations

3160 East Transcon Way
Suite 180
Tucson, Arizona 85706
USA
Tel: +1 (520) 624 6399
Fax: +1 (520) 624 1906

German Operations

Ulrichsberger Str. 17 3 OG
94469 Deggendorf
Germany
Tel: +49 991 2910083
Fax: +49 991 2910399

Singapore Operations

Co-Ord Centre Pte Ltd
4 Shenton Way #28-01
SGX Centre II
Singapore 068807

Tel: +65 6224 0100

Fax: +65 6227 6002

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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AND CONTROLLED ENTITIES

ASX ADDITIONAL INFORMATION

Additional information required by the Australian Stock Exchange Listing Rules and not disclosed elsewhere in this report.

HOME EXCHANGE

The Company's ordinary shares are quoted on the Australian Stock Exchange Limited under the trading symbol "EOS". The Home Exchange is Sydney.

SUBSTANTIAL SHAREHOLDERS

At 8 March 2012 the following substantial shareholders were registered:

	Ordinary Shares	Percentage of total Ordinary shares
Fred Bart Group	5,309,075	9.33%
Technology Investments Pty Limited	3,954,185	6.96%
Northrop Grumman Space and Mission Systems Corp.	<u>5,000,000</u>	<u>8.80%</u>
	<u>14,263,260</u>	<u>25.09%</u>

VOTING RIGHTS

At 8 March 2012 there were 1,111 holders of fully paid ordinary shares.

Rule 74 of the Company's Constitution stipulates the voting rights of members as follows:

"Subject to any rights or restrictions for the time being attached to any class or classes of shares and to this Constitution:

- (a) on a show of hands every person present in the capacity of a Member or a proxy, attorney or representative (or in more than one of these capacities) has one vote; and

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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AND CONTROLLED ENTITIES

ASX ADDITIONAL INFORMATION (Cont)

- (b) On a poll every person present who is a Member or proxy, attorney or Representative has member present has:
- (i) For each fully paid share that the person holds or represents – one vote; and
 - (ii) For each share other than a fully paid share that the person holds or represents – that proportion of one vote that the amount paid (not credited) on the shares bears to the total amount paid and payable on the share (excluding amounts credited).”

OTHER INFORMATION

In accordance with Listing Rule 4.10.19, the Company has used the cash and assets in a form readily convertible to cash that it had at the time of admission in a way consistent with its business objectives.

The Company has a sponsored Level 1 American Depositary Receipt (ADR) program on the Over-The-Counter (OTC) market in the USA with the ADR ticker symbol of EOPSY. The ratio of ADR's to Ordinary shares is 1:5 and the CUSIP Number is 28520B1070. The local custodian is National Australia Bank Limited and the US Depositary Bank is BNY Mellon.

DISTRIBUTION OF SHAREHOLDINGS

At 8 March 2011 the distribution of share and option holdings were:

Range	Ordinary Shareholders	Number of Shares
1-1,000	184	108,667
1,001 – 5,000	392	1,185,058
5,001 – 10,000	218	1,895,614
10,001 – 100,000	247	8,345,714
100,001 and over	<u>70</u>	<u>45,310,873</u>
	<u>1,111</u>	<u>56,845,926</u>

There were 128 ordinary shareholders with less than a marketable parcel.

There is no current on-market buy-back.

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TWENTY LARGEST SHAREHOLDERS - QUOTED

TWENTY LARGEST ORDINARY SHAREHOLDERS - QUOTED

At 8 March 2012 the 20 largest ordinary shareholders held 60.20% of the total issued fully paid quoted ordinary shares of 56,845,926.

Shareholder	Fully Paid Ordinary Shares	Percentage of Total
1. Citicorp Nominees Pty Limited	5,899,900	10.38%
2. N & J Properties Pty Limited	4,090,000	7.19%
3. Mr Kevin Tay Hak Leong	2,839,970	5.00%
4. Technology Transformations Pty Limited	2,509,905	4.42%
5. Crea8ive Nominees Pty Limited	1,911,328	3.36%
6. Capitol Enterprises Limited	1,550,000	2.73%
7. Emichrome Pty Limited	1,516,488	2.67%
8. A & D Wire Limited	1,457,276	2.56%
9. Technology Investments Pty Limited	1,444,280	2.54%
10. DBS Vickers Securities (Singapore) Pte Ltd	1,342,000	2.36%
11. Landed Investments Limited	1,255,201	2.21%
12. Madam Lim Gek Kuan	1,171,493	2.06%
13. Mr Teo Kian Giap	1,099,981	1.94%
14. Landed Investments NZ Limited	1,010,000	1.78%
15. National Nominees Limited	1,009,409	1.78%
16. Rinfast Pty Limited	1,000,000	1.76%
17. Emichrome Pty Limited <Super Fund A/C>	997,500	1.75%
18. HSBC Custody Nominees (Australia) Pty Limited	895,120	1.56%
19. Kam Superannuation Fund Pty Limited	693,000	1.22%
20. JP Morgan Nominees Australia Limited	529,663	0.93%
	<u>34,222,464</u>	<u>60.20%</u>

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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CORPORATE GOVERNANCE STATEMENT

The Board of Directors of Electro Optic Systems Holdings Limited is responsible for the corporate governance of the consolidated entity. The Board guides and monitors the business and affairs of Electro Optic Systems Holdings Limited on behalf of the shareholders by whom they are elected and to whom they are accountable.

The Directors are committed to protecting stakeholders' interests and keeping investors fully informed about the performance of the Company, while meeting stakeholders' expectations of sound corporate governance practices. To ensure the best representation of Shareholder interests, the Board will regularly review its corporate governance practices.

The Corporate Governance Statement follows the Australian Stock Exchange Corporate Governance Council's (the "Council's") amendments to the 2nd edition of the Corporate Governance Principles and Recommendations released 30 June 2010 in relation to diversity, remuneration, trading policies and briefings.

In accordance with the Council's recommendations, the Corporate Governance Statement must now contain certain specific information and must disclose the extent to which the Company has followed the guidelines during the period. Where a recommendation has not been followed, that fact must be disclosed, together with the reasons for the departure. Electro Optic Systems Holdings Limited's Corporate Governance Statement is now structured with reference to the Corporate Governance Council's principles and recommendations, which are as follows:

Principle 1.	Lay solid foundations for management and oversight
Principle 2.	Structure the Board to add value
Principle 3.	Promote ethical and responsible decision making
Principle 4.	Safeguard integrity in financial reporting
Principle 5.	Make timely and balanced disclosure
Principle 6.	Respect the rights of shareholders
Principle 7.	Recognise and manage risk
Principle 8.	Remunerate fairly and responsibly

Electro Optic Systems Holdings Limited's corporate governance practices were in place throughout the year ended 31 December 2011 and embrace the Council's best practice recommendations which are being put in place as appropriate.

The Audit Committee was formed on 28 April 2005 and consists of three non-executive directors. The members of the Audit Committee are Lt Gen Peter Leahy AC (Chairman), Mr Ian Dennis and Mr Fred Bart. The majority of the Audit Committee are independent directors and the Chairman is an independent person.

The Remuneration Committee was formed on 23 March 2007. The members of the Remuneration Committee are Lt Gen Peter Leahy AC (Chairman), Mr Ian Dennis and Mr Fred Bart. The majority of the Remuneration Committee are independent directors and the Chairman is an independent person.

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CORPORATE GOVERNANCE STATEMENT (cont)

The Company has documented risk management policies and procedures in accordance with its ISO 9001 certification for its operating activities which are regularly reviewed. During the current year the Directors have adopted a formal risk assessment plan in order to comply with Principle 7.

Additional information regarding the Company's corporate governance policies, its Directors, Insider Trading Policy and other relevant information can be found on the Company's website: www.eos-aus.com

Structure of the Board

The skills, experience and expertise relevant to the position of director held by each Director in office at the date of this Annual Report is included in the Directors' Report on pages 9 and 10. Directors of Electro Optic Systems Holdings Limited are considered to be independent when they are independent of management and free from any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement.

In the context of director independence, "materiality" is considered from both the Company and individual director perspective. The determination of materiality requires consideration of both quantitative and qualitative elements. An item is presumed to be quantitatively immaterial if it is equal or less than 5 percent of the appropriate base amount. It is presumed to be material (unless there is qualitative evidence to the contrary) if it is equal to or greater than 10 percent of the appropriate base amount. Qualitative factors considered include whether a relationship is strategically important, the competitive landscape, the nature of the relationship and the contractual or other arrangements governing it and other factors which point to the actual ability of the director in question to shape the direction of the Company's loyalty.

In accordance with the definition of independence above, and the materiality thresholds set, the following Directors of Electro Optic Systems Holdings Limited are considered to be independent:

Name	Position
Mr. Ian Dennis	Non-Executive Director and Company Secretary
Lt Gen Peter Leahy AC	Non-Executive Director
Mr Kevin Scully	Non-executive Director

There are procedures in place, agreed by the Board, to enable directors, in furtherance of their duties, to seek independent professional advice at the Company's expense.

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CORPORATE GOVERNANCE STATEMENT (cont)

The term in office held by each Director in office at the date of this report is as follows:

Name	Position	Term in Office
Mr Fred Bart	Non-Executive Chairman	11 years 10 months
Dr Ben Greene	Executive Director	8 years 9 months
Mr. Ian Dennis	Non-Executive Director	11 years 10 months
Mr Mark Ureda	Non-Executive Director	7 years 10 months
Lt Gen Peter Leahy AC	Non-Executive Director	2 year 9 months
Mr Kevin Scully	Non-Executive Director	6 months

For additional details regarding board appointments, please refer to the Company's website.

Nomination Committee

The Board does not currently have a formal Nomination Committee. However, the Board continues to operate within the established guidelines, including when necessary, selecting candidates for the position of Director and, where appropriate, seeking the services of an independent consultant who is not a director of the Company to provide assistance in the recruitment of potential Directors.

Performance

The performance of the Board and key executives is reviewed regularly against both measurable and qualitative indicators. During the reporting period, an assessment of the performance of each Board member and key executive against specific and measurable qualitative and quantitative performance criteria was undertaken. The performance criteria against which directors and executives are assessed is aligned with the financial and non-financial objectives of Electro Optic Systems Holdings Limited. Directors whose performance is consistently unsatisfactory may be asked to retire.

Remuneration

One of the Company's key objectives is to provide maximum stakeholder benefits from the retention of a high quality Board and executive team by remunerating Directors and key executives fairly and appropriately with reference to relevant employment market conditions. A Remuneration Committee was formed on 23 March 2007. The nature and amount of Executive Directors' and Officers' emoluments are linked to the Company's financial and operational performance. The expected outcomes of the remuneration structure are:

- Retention and motivation of key executives;
- Attraction of quality management to the Company; and
- Performance incentives which allow executives to share the rewards of the success of Electro Optic Systems Holdings Limited.

For details regarding the amount of remuneration and all monetary and non-monetary components for Directors and executives, refer to Note 21 of the Notes to the Financial

ELECTRO OPTIC SYSTEMS HOLDINGS LIMITED

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CORPORATE GOVERNANCE STATEMENT (cont)

Statements. In relation to the payment of bonuses, options and other incentive payments, discretion is exercised by the Board, having regard to the overall performance of Electro Optic Systems Holdings Limited and the performance of the individual during the period.

There is no scheme to provide retirement benefits, other than statutory superannuation, to non-executive directors.

The Board is responsible for determining and reviewing compensation arrangements for the Directors themselves, the Chief Executive Officer and the executive team.

Diversity Policy

The Company values diversity and recognises the benefits it can bring to the organisation's ability to achieve its goals. Accordingly, the Company is in the process of developing a diversity policy which will outline its diversity objectives in relation to gender, age, cultural background and ethnicity. It will include requirements for the Board to establish measurable objectives for achieving diversity, and for the Board to assess annually both the objectives, and the Company's progress made in achieving them.

Safeguard integrity in financial reporting

The chief executive officer and the chief financial officer are required to state in writing to the board that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards.

Policy on Trading in Securities

Directors and employees of EOSH should not buy or sell securities in EOSH, when EOSH is in possession of price sensitive information that is not generally available to the market.

The Securities Trading Policy of the Company is available on the Company's website at www.eos-aus.com and has been lodged with ASX Limited