2007 Annual Report

Universal Biosensors

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Chairman's Letter

Dear Shareholder,

On behalf of the board of directors, I am pleased to present the annual report of Universal Biosensors, Inc. ('Company') for the year ended December 31, 2006.

I thank you for your help and support during a very eventful year for the Company, with the highlight being the listing of the Company's securities on the Australian Securities Exchange in December 2006.

Since its inception, the Company has continued to develop the skills of its employees and to advance the technology on which the Company was founded, all with a view to produce market leading diagnostic products. These diagnostic products are designed to be used close to patients to enable improved treatment of chronic diseases.

The funds the Company raised during 2006 have allowed the Company to accelerate product development and to begin the building of a regulatory and quality approved manufacturing capability to supply targeted markets. As I write this, we have received the first of our commercial scale production machines and the renovation of our new facility has begun.

To create a valuable intellectual property portfolio, to develop and then apply this to new products and to build a production capability targeted at producing world leading advantage is truly a significant series of goals. We are progressing well towards achieving them.

On your behalf and on behalf of the Board, I would like to thank all of the employees and service providers for their efforts and achievements during the last year. Great progress was made with even more anticipated in the coming year.

Yours faithfully

Andrew Denver
Chairman

CEO Report

It is a great pleasure to be able to present the 2006 annual report of the Company, our first annual report since the admission of the Company to the Australian Securities Exchange. As a specialist medical diagnostics company, the Company's focus is in developing, manufacturing and commercializing simple, robust point-of-care diagnostic test devices that enable patients and doctors to more actively and effectively manage disease and illness.

Each of the devices being developed by the Company requires only a fingerprick sample of blood which is automatically tested when drawn into the device. Data is produced almost immediately and can be reviewed on the spot (at the 'point-of-care') allowing new or existing treatment to be reviewed and adjusted straight away. It is not hard to imagine how this efficiency can lead to better outcomes for patients as well as efficiencies and cost reductions for the overall health care system.

The Company's particular focus is the development of products for chronic illnesses where current practice is suboptimal or unnecessarily expensive. Our ambition is to develop and then market tests which can improve the lives of patients with chronic illness. We have focused on the development of products for diseases which do not rely on the development of new medicines or treatments, but where existing therapies or practice can be enhanced significantly by simple and accurate diagnostic tools.

For example, immunoassay testing of C-reactive protein is routinely used in pathology laboratories for indication of inflammatory conditions. The Company has developed its own diagnostic test for C-reactive protein which is capable of use at the point-of-care setting rather than requiring samples to be sent away for testing at pathology laboratories. Likewise, prothrombin time tests are used to measure and monitor the effectiveness of the anticoagulant, warfarin.

The Company has developed a prothrombin time test with a view to enabling patients to more regularly test and monitor their dosage of anticoagulants. In the field of diabetes, Universal Biosensors continues its development of a blood glucose test for LifeScan, Inc. The advent of accurate point-of-care blood glucose monitors has enabled significant improvements in the quality of life of diabetics.

In addition to researching and developing products, the Company also aims to manufacture products for supply to the market. Commercial manufacturing and supply requires us to possess a licenced manufacturing facility, and the ability to register our products. During the course of 2006, we began to build both the capability and capacity to be a commercial supplier. Our achievements in 2006 as we started to position ourselves within the global diagnostic industry, were significant. Some of these included:

- the design of the blood glucose test strip was completed and long term stability trials of the strip and control solution were started.
- the equipment required to produce these and other test strips we develop, was designed. These manufacturing designs are customized to our proprietary manufacturing process. Construction of manufacturing equipment has started and the first pieces tested and delivered.
- a facility suitable for manufacturing our products was identified, and a lease executed. A contract for the fit out works was awarded and the fit out works have commenced.
- a prototype immunosensor blood test strip and meter system met initial testing goals set against clinical samples and competitor products, and a next iteration of prototyping was commenced.

- the Company completed a successful initial public offering in Australia and a concurrent US private placement. The capital raised has allowed us to begin accelerating product development and building on the milestones we passed earlier in the year.
- We continue to file patent applications, and build the Company's know how, to add to our already significant licensed and owned intellectual property portfolio.
- We continue to broaden our expertise and have added more skill in research, engineering, project management and regulatory affairs. At the close of the year we welcomed Mr Salesh Balak as our Chief Financial Officer.

The year ahead will be full of significant tasks:-

- During 2007 we intend to complete fit out of our new premises. These premises will have our new manufacturing equipment installed, and we will be required to validate the building and equipment to the satisfaction of regulators. The latter task in particular is rigorous and time-consuming.
- Across the same time period, we will seek to finish building our quality system and have it certified.
- We will also continue to build the registration documentation required to enable the sale of the blood glucose product.
- Both our C-reactive protein and prothrombin time tests should enter the next stage of research and development.
- We will continue to build our intellectual property portfolio.
- We intend to continue building our corporate governance and management procedures, including those we need to comply with the requirements of Sarbanes Oxley.
- Skill building within our team will continue and you can expect to see further additions of talent to your Company throughout 2007.

These are challenging, exciting times. We look forward with relish and anticipation to an important year for your Company.

Mark Morrisson

Mark Morrisson

Chief Executive Officer

Corporate Governance Statement

Universal Biosensors, Inc. ('Company') was admitted to Australian Securities Exchange on December 13, 2006. Since that time, the Company has worked to progressively develop appropriate corporate governance policies having regard to the best practice principles and recommendations issued by the ASX Corporate Governance Council and other best practice guidance. The Company is targeting adopting such policies prior to the end of the 2007 financial year. The Company expects that, once formally adopted, these policies will require amendment over time to take into account any requirements of the Sarbanes-Oxley Act which may in the future apply to the Company.

The following section is structured following the primary headings used in the ASX Corporate Governance Council's best practice principles and recommendations.

Lay solid foundations for management and oversight

The Board is responsible for the overall governance of the Company and its wholly owned subsidiary, Universal Biosensors Pty Ltd (collectively referred to as the 'Group'). The Board's responsibilities include:

- overall responsibility for corporate governance, including control and accountability systems;
- reviewing and determining strategic direction and policy in conjunction with senior management;
- monitoring senior management's performance and implementation of strategy and plans;
- appointing, removing and monitoring the performance of the Chief Executive Officer, Chief Financial Officer and Company Secretary; and
- ensuring Board committees are appropriately constituted and performing their functions.

The Chief Executive Officer and senior management responsibilities include:

- developing corporate strategy, performance objectives, business plans and budgets for review by the Board;
- developing and implementing appropriate policies and procedures for the management of the Group;
- the day to day management of the Group's affairs and the implementation of corporate strategies and policy initiatives.

The responsibilities of the Board will vary as the Group develops. The Board will regularly review the respective roles and the allocation of responsibilities between the Board and management, and will update or affirm the allocation of roles and responsibilities described above.

Structure the Board to add value

The Board currently consists of one independent director and six non independent directors.

The Company considers Dr Wilson to be an independent director. The Company considers that each of Mr Denver, Dr Adam, Mr Hanley, Mr Jane and Mr Kiefel are not independent because they are substantial shareholders or are affiliated with substantial shareholders (as the case may be). Details of the holdings of these directors is set out in the Directors Report. Mr Morrisson is not regarded as an independent director because he is an executive of the Group.

Name	Status	Experience	Appointment Date
Mr Andrew Denver	Non independent chairman	Extensive experience in the commercialisation of new technology	3 December 2002
Mr Mark Morrisson	Chief Executive Officer	Extensive experience in the in vitro diagnostic and life science industries	9 August 2005
Dr Colin Adam	Non independent director	Extensive management experience gained in the technology sector	6 December 2006
Mr Denis Hanley	Non independent director	Extensive experience in building Australian corporations to become successful global entities	14 September 2001
Mr Charles Kiefel	Non independent director	Extensive experience in investment banking and finance	6 December 2006
Mr Andrew Jane	Non independent director	Extensive experience in the technology sector gained through management positions and as a venture capitalist	15 August 2006
Dr Jane Wilson	Independent non executive director	A professional company director with a background in medicine, banking and finance and extensive experience in the commercialisation of research	6 December 2006

The skills, experience and expertise relevant to the position of director held by each director in office at the date of the annual report and details in relation to their terms of officer are included in the Directors' Report. The structure of the Board does not comply with the ASX Corporate Governance Council's recommendation that there be a majority of independent directors and that the chairman be an independent director. The Company considers that its Board membership and having a non independent chairman is appropriate given the Company's current stage of development. The Board will continuously review its performance and mix of skills to ensure that they are appropriate to allow the Board to maximise its effectiveness and its contribution to the Company. Directors of the Company 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. The determination of materiality by the Company includes both quantitative and qualitative assessments.

The Board has procedures in place whereby the directors may seek independent professional advice at the Company's expense.

Remuneration and Nomination Committee

The Board established a Remuneration and Nomination Committee immediately prior to the Company's initial public offering in Australia. The Company is in the process of finalising a Remuneration and Nomination Committee charter which will govern the operation of the Remuneration and Nomination Committee and the procedures for selecting and appointing new directors to the Board. Once adopted, the charter will be made available on the Company's website. The Remuneration and Nomination Committee comprises of Mr Jane (chairman), Dr Adam and Dr Wilson. The Remuneration and Nomination Committee did not meet between the time of the Company's initial public offering and December 31, 2006.

The composition of the Remuneration and Nomination Committee does not comply with the ASX Corporate Governance Council's recommendation that there be a majority of independent directors. The Company considers that its Remuneration and Nomination Committee membership is appropriate given the Company's current stage of development. The Board will continuously review its performance and mix of skills to ensure that they are appropriate to allow the Remuneration and Nomination Committee to maximise its effectiveness and its contribution to the Company.

Promote ethical and responsible decision making

The Company will progressively adopt a detailed code of conduct applicable to directors, senior managers and other employees as to the practices necessary to maintain confidence in the Company's integrity and the responsibility and accountability of individuals for reporting and investigating reports of unethical practices. Once adopted, the code of conduct will be available on the Company's website. The Company has adopted a securities trading policy which is available on the Company's website.

Safeguard integrity in financial reporting

The Board established an Audit and Compliance Committee immediately prior to the Company's initial public offering in Australia. The Company is in the process of finalising an Audit Committee Charter which will govern the operation of the Audit and Compliance Committee. Once adopted, the charter will be made available on the Company's website. The primary objective of the Audit and Compliance Committee is to assist the Board to fulfil its responsibilities relating to accounting and reporting practices of the Company, including, the Company's annual and half-year financial statements and all other financial information released by the Company.

The Audit and Compliance Committee comprises of Dr Wilson (chairperson), Mr Denver, Mr Hanley and Mr Kiefel. The Audit and Compliance Committee did not meet between the date of the initial public offering and December 31, 2006.

The Audit and Compliance Committee does not comply with the ASX Corporate Governance Council's recommendation that there be a majority of independent directors. The Company considers that its Audit and Compliance Committee membership is appropriate given the Company's current stage of development. The Audit and Compliance Committee requires that the Chief Executive Officer and the Chief Financial Officer 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.

The Audit and Compliance Committee is responsible for recommending the appointment and reviewing the performance of the external auditors of the Company. Subject to requirements of Delaware law and Sarbanes-Oxley Act, the lead audit partner will be required to rotate off the audit duties for the Company after their involvement for a maximum of five years.

Make timely and balanced disclosure

The Company is in the process of finalising a Continuous Disclosure and Shareholder Communication Policy which describes the processes implemented by the Company to assist the Company in complying with its continuous disclosure obligations under the Corporations Act 2001 and Listing Rules of Australian Securities Exchange. Once adopted, the Continuous Disclosure and Shareholder Communication Policy will be made available on the Company's website. The Board has established a disclosure committee to assist the Company in complying with its disclosure obligations. The disclosure committee comprises of the Chairman of the Board, the Chief Executive Officer, the Chief Financial Officer and the Company Secretary.

Respect the Rights of Shareholders

As noted above, once adopted, the Company's Continuous Disclosure and Shareholder Communication Policy will be made available on the Company's website. The Company provides shareholders with quarterly reports and utilises its website to disclose relevant information about the Company. At the date of this report, the Company has not yet held an annual general meeting as a publicly listed company. However, the Company will require that the auditors attend the annual general meetings of the Company to respond to questions that shareholders may have.

Recognise and manage risk

The Audit and Compliance Committee is responsible for reviewing the Company's internal controls and management of risk. The Board is also responsible for the oversight of risk management and reviews the effectiveness of the Company's risk managements systems on an annual basis. The Chief Executive Officer and Chief Financial Officer must provide a statement to the Board that the integrity of the Company's financial statements is founded on a sound system of risk management and internal compliance.

Encourage enhanced performance

The performance of the Board and key managers will be reviewed regularly against both measurable and qualitative performance indicators. At or around the end of each financial year, the Remuneration and Nomination Committee will conduct performance evaluations that will involve an assessment of each Board member's and key manager's performance against specific and measurable qualitative and quantitative performance criteria. The Company's previous review of management was conducted prior to Company's initial public offering in Australia. The performance criteria against which directors and management are assessed are aligned with the financial and non-financial objectives of the Company. 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.

Remunerate fairly and responsibly

The Board has established a Remuneration and Nomination Committee. The Company is in the process of finalising a Remuneration and Nomination Committee charter which will govern the operation of the Remuneration and Nomination Committee. For details of the Company's remuneration philosophy and framework, refer to the Remuneration Report in the Directors' Report. The Company does not operate any schemes for retirement benefits, other than statutory superannuation for non executive directors. Executives of the Company are remunerated by way of fixed salary, variable bonus payments and options granted under the Company's employee option plan. Non executive directors are currently paid by way of fixed fee and have neither been awarded bonus payments nor granted options.

Recognise the legitimate interests of shareholders

The Company will progressively adopt a detailed code of conduct applicable to directors, senior managers and other employees which will be made available on the Company's website.

Directors' Report

Your directors submit their report on Universal Biosensors, Inc. ('Company') for the financial year ended December 31, 2006.

DIRECTORS

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

Names, qualifications, experience and special responsibilities

Mr Andrew Denver

BSc. (Hons.), MBA, FAICD
Non-Executive Chairman
Age 58

Andrew Denver has served as a non executive director of the Company since December 2002. He has served as the non-executive Chairman of the Company since September 2005 and is a member of the Audit and Compliance Committee. Andrew's term of appointment as a director of the Company ends on the date of the 2009 annual general meeting of the Company.

Between 2002 and 2005, Andrew was President of Pall Asia, a subsidiary of Pall Corporation formed on the acquisition by Pall Corporation of US Filter's Filtration and Separations business, where he was also President.

Andrew Denver is a founder and director of The Principals Funds Management Pty Ltd, a company which helps Australian technology businesses commercialize their technologies. Andrew Denver is a non-executive director of CathRx Ltd, Anzon Australia Ltd and Cochlear Ltd and a number of other private companies.

Andrew Denver graduated from the University of Manchester with a Bachelor of Science Degree (Honors) in Chemistry and achieved a distinction in his M.B.A. at the Harvard Business School and is a Fellow of the Australian Institute of Company Directors.

Mr Mark Morrisson

BSc. (Hons.)
Managing Director / Chief Executive Officer
Age 45

Mark Morrisson has served as the Chief Executive Officer of the Company since July 2005 and has been an executive director of the Company since August 2005. Mark Morrisson's term of appointment as a director of the Company ends on the date of the 2008 annual general meeting of the Company.

After training as a biochemist with the University of Queensland in Australia, in 1986 Mark then joined AGEN Biomedical Ltd, a company focused on the advanced medical diagnosis of human diseases and a thrombosis and blood clot specialist. Mark became a member of AGEN Biomedical Ltd's global management executive team as Vice President of Marketing in 1992 and left AGEN Biomedical Ltd in 1995. More recently in 2005, Mark worked as an advisor and consultant for Thallo Biosciences, a San Francisco based corporate and strategic advisor serving the biotechnology and life sciences industries. Between 2001 and 2005, Mark served as an investment manager for CM Capital Investments Pty Limited, a Brisbane based venture capital investment company where he led that firm's investment rounds into CathRx Ltd and Pharmaxis Ltd. Mark Morrisson holds a Bachelor of Science Degree in Biochemistry (Hons).

Dr Colin Adam

B.E. (Met.), Ph.D.
Non-Executive Director
Age 63

Dr Colin Adam has been a non-executive director of the Company since December 2006. Prior to his appointment as a director of the Company, Colin was a director of Universal Biosensors Pty Ltd between July 10, 2002 and December 12, 2006. Colin Adam's term of appointment as a director of the Company ends on the date of the 2007 annual general meeting of the Company which is expected to be held in May 2007. He is a member of the Remuneration and Nomination Committee.

In 2000, Colin was the Acting Chief Executive of the CSIRO. Prior to that between 1996 to 1999, Colin was Deputy Chief Executive directly responsible for all the CSIRO's commercial activity. Prior to working with the CSIRO, Colin's career has included executive positions within the US aerospace industry for Pratt & Whitney Aircraft in Florida and Allied Corporation in New Jersey. Colin has served as a member of the Australian Government's Industry Research and Development Board, the Australian Prime Minister's Science Engineering and Innovation Council and the Victorian Premier's Science, Engineering and Technology Taskforce. Colin is a founder and director of The Principals Funds Management Pty Ltd, a company which helps Australian technology companies commercialize their technologies. Colin Adam serves on the board of Ausmelt Limited. Dr Colin Adam has a Bachelor of Metallurgical Engineering Degree and a Ph.D. in Metallurgy from the University of Queensland.

Mr Denis Michael Hanley

AM, MBA, FCPA, FAICD
Non-Executive Director
Age 59

Denis Hanley has served as a non-executive director of the Company since 14 September 2001 and is a member of the Audit and Compliance Committee. His term of appointment as a director of the Company ends on the date of the 2008 annual general meeting of the Company.

Denis is a qualified accountant and company director with more than 35 years experience in the management of technology-based growth businesses. Denis has significant experience in developing and commercializing new technology based Australian corporations to become successful global entities. His experience includes 14 years as chief executive officer of Memtec Limited, growing the start-up company to become an international force in filtration and separations technology, listed on the New York Stock Exchange. Prior to this, Denis spent more than a decade at global medical company Baxter Healthcare, both in the U.S. and also as Australian Managing Director. Denis has served on the Australian Industry Research and Development Board and various technology councils and roundtables. Denis is a founder and director of The Principals Funds Management Pty Ltd, a company which helps Australian technology businesses commercialize their technologies. Denis Hanley is currently non-executive Chairman of Pharmaxis Ltd, CathRx Ltd and Lochard Ltd and has a number of other private and public company directorships. Denis Hanley holds an M.B.A. with High Distinction from Harvard Graduate School of Business, where he was named a Baker Scholar.

Mr Andrew Jane

BSc. (Hons.), MSc
Non-Executive Director
Age 45

Andrew Jane has served as a non-executive director of the Company since August 2006 and is Chairperson of the Remuneration and Nomination Committee. Andrew Jane's term of appointment as a director of the Company ends on the date of the 2009 annual general meeting of the Company.

In 2003, Andrew joined CM Capital Investments Pty Ltd, a Brisbane based venture capital investment company, as an Investment Manager and was promoted to Partner in 2006. Prior to this, Andrew worked for Lake Technology, an audio technology company as Director of Business Development and Licensing, where he worked closely with Lake Technology's strategic partner, Dolby Laboratories an audio technology company in San Francisco, and was responsible for a significant number of global licensing deals during his four years there. Prior to Lake Technology, Andrew held R&D management positions of increasing responsibility at AGEN Biomedical and the CSIRO. Andrew is currently a director of Advent Pharmaceuticals Pty Limited and an observer to the board of Metastatix, Inc. Andrew Jane received his Master of Science in Instrumentation from the University of Manchester Institute of Science and Technology and holds a Bachelor of Science (Honors) in Physics from St Andrews University in Scotland.

Mr Charles Kiefel

B.Com., F.C.A., F.A.I.C.D.
Non-Executive Director
Age 51

Charles Kiefel has served as a non-executive director of the Company since December 2006. Prior to his appointment as a director of the Company, Charles was a director of Universal Biosensors Pty Ltd between September 19, 2002 and December 6, 2006. Charles Kiefel's term of appointment as a director of the Company ends on the date of the 2007 annual general meeting of the Company which is expected to be held in May 2007. Charles Kiefel is member of the Audit and Compliance Committee.

Charles has more than 20 years experience in finance, investment banking and the investment sector in London with Lazard Bros, New York with Lazard Freres, Sydney with Ord Minnett and with ANZ Investment Bank. Charles is Chairman of the Military Superannuation Board and serves on the advisory boards of two of Australia's largest private equity funds, Pacific Equity Partners Fund and CHAMP II Fund. Charles is a founder and director of The Principals Funds Management Pty Ltd, a company which helps Australian technology businesses commercialize their technologies. Mr. Kiefel is a Director of Business Development for two major US money managers, Turner Investment Partners and LSV Asset Management and is also a non-executive director of Pharmaxis Ltd.

Dr Elizabeth (Jane) Wilson

MBBS, MBA, FAICD
Non-Executive Independent Director
Age 48

Dr Jane Wilson has served as a non-executive director and independent member of the board of directors of Company since December 2006. Dr Jane Wilson is Chairperson of the Audit and Compliance Committee and a member of the Remuneration and Nomination Committee. Dr Jane Wilson's term of appointment as a director of the Company ends on the date of the 2008 annual general meeting of the Company.

Jane is a professional company director with a background in medicine, banking and finance and has extensive experience in the commercialization of research in both the agricultural and biotechnology sectors. Jane is the Finance Director of the Winston Churchill Memorial Trust and was the inaugural Chair of Horticulture Australia Ltd from 2000 to 2004. She is involved in a number of charitable and cultural organizations and has also served on the Queensland Government Biotechnology Taskforce and the boards of Energex Ltd, WorkCover Queensland, AGEN Biomedical Limited and Protagonist Ltd. Jane is a member of the Queensland Premier's Smart State Council and a member of the University of Queensland Senate. She has an M.B.A. from the Harvard Business School where she studied agribusiness and the health sector. Dr Jane Wilson is the current Chairperson of IMBcom Limited, the commercialization company of the Institute for Molecular Bioscience, and is Immediate Past President of the Australian Institute of Company Directors – Queensland Division, as well as a director of CathRx Ltd, UQ Holdings Ltd and the National Archives Advisory Council and a director of number of other public and private companies.

Retirement of Directors

Mr Roger Guidi retired as a director on November 3, 2006.

COMPANY SECRETARY

Mr Cameron David Billingsley

BA, LLB (Hons.)
Company Secretary
Age 30

Mr Cameron Billingsley has been company secretary of the Company and Universal Biosensors Pty Ltd since 26 February 2007 and has been involved as legal counsel for the Company since 2001. Mr Billingsley is a corporate and commercial lawyer and founder of PFM Legal Pty Ltd, a company established to provide company secretarial, general corporate and commercial legal, book-keeping and administrative support services to Australian technology companies.

MEETINGS OF DIRECTORS

The number of meetings of directors and of each board committee held during the year ended December 31, 2006 and the numbers of meetings attended by each director were as follows:-

Directors	Board of Directors		Remuneration and Nomination Committee		Audit and Compliance Committee	
	Held[1]	Attended	Held[1]	Attended	Held[1]	Attended
Mr Andrew Denver	13	13	–	–		
Mr Mark Morrisson	13	13	–	–	–	–
Dr Colin Adam	–	–	–	–	–	–
Mr Denis Hanley	13	12	–	–	–	–
Mr Andrew Jane	5	5	–	–	–	–
Mr Charles Kiefel	–	–	–	–	–	–
Dr Jane Wilson	–	–	–	–	–	–

Note 1: Represents the number of meetings held while that relevant director was in office.

COMMITTEE MEMBERSHIP

The Company has established an Audit and Compliance Committee and a Remuneration and Nomination Committee, the members of which are:

Audit and Compliance	Remuneration and Nomination
Dr Jane Wilson (Chairperson)	Mr Andrew Jane (Chairman)
Mr Andrew Denver	Dr Colin Adam
Mr Denis Hanley	Dr Jane Wilson
Mr Charles Kiefel	

DIRECTORS' INTERESTS IN SHARES AND OPTIONS OF THE COMPANY

As at the date of this report, the interests of the current directors in the shares and options of the Company were:

Director(1)	Number of Securities	Number of Options over Shares
Mr Andrew Denver	7,932,005	–
Mr Mark Morrisson	–	960,560(2)
Dr Colin Adam	6,626,951	–
Mr Denis Hanley	8,295,105	–
Mr Andrew Jane(3)	15,196,879	–
Mr Charles Kiefel	5,844,005	–
Dr Jane Wilson	1,015,000	–

Note 1: The interests in shares of common stock include shares and CDIs held legally or beneficially.

Note 2: On March 22, 2007, the Board approved the grant of a further 45,000 employees options to Mr Mark Morrisson subject to receipt of necessary shareholder approval for the grant of the options.

Note 3: Includes: (i) 11,688,767 shares held by CM Capital Investments Pty Ltd as trustee of the CM Capital Venture Trust No.3; and (ii) 3,508,112 shares held by CIBC Australia VC Fund LLC as general partner of the Australia Venture Capital Fund L.P., of which CM Capital Investments Pty Ltd is a special limited partner. Andrew Jane is a partner of CM Capital Investments Pty Ltd. Andrew Jane may be taken to have an indirect pecuniary interest in an indeterminate portion of these shares of common stock.

EARNINGS PER SHARE

	December 31, 2006 US$	December 31, 2005 US$
Basic earnings (loss) per share	(0.04)	(0.00)
Diluted earnings (loss) per share	(0.04)	(0.00)
Weighted average number of shares outstanding	49,408,822	45,573,580

DIVIDENDS

No dividends were paid during the financial year and the directors have not recommended the payment of any dividends.

PRINCIPAL ACTIVITIES

The principal activities of the Company during the financial year ended December 31, 2006 continued to be the development of a range of in vitro diagnostic tests for point–of-care use.

OPERATING AND FINANCIAL REVIEW

Review and results of operations

The Company achieved the following key milestones during the financial year ended December 31, 2006:-

- The Company undertook an initial public offering of its shares of common stock during November and December 2006 raising A$18 million through the issue of 36 million shares of common stock at an issue price of A$0.50 per share. Concurrently, the Company undertook a private placement in the United States raising A$4 million through the issue of 8 million shares of common stock at an issue price of A$0.50 per share.
- The Company was admitted to the official list of, and its shares of common stock trading in the form of CHESS Depositary Interests were quoted on, Australian Securities Exchange Ltd ('ASX') on December 13, 2006.
- Prior to its initial public offering, in June and August 2006 the Company closed two private capital raisings in which it raised a total of US$9.99 million.
- The Company has made a number of key appointments during the year including a new Chief Financial Officer. The Company has increased the total number of employees to 28 as at December 31, 2007.
- The design of manufacturing equipment which was customized to the Company's manufacturing process was completed and construction of the equipment commenced.
- The strip design on the glucose sensor strip was completed, and long term stability trials of the strip and control solution were started.
- A new facility which is suitable for manufacturing the diagnostic tests was identified and a lease entered into.
- A prototype immunosensor blood test strip and meter system met initial testing goals set against clinical samples and competitor products.

FINANCIAL HIGHLIGHTS

Research and development income

Payments totalling US$2,000,000 were made by LifeScan, Inc. ('LifeScan') during the financial year ending December 31, 2006 (2005: US$2,086,013) pursuant to a development and research agreement dated April 1, 2002 for development and research activities carried out for LifeScan in the area of diabetes management.

Interest income

Interest income increased by 245% to US$334,380 during the financial year ending December 31, 2006 as a result of greater level of funds invested during the year. The Company commenced the 2006 financial year with US$3.25 million in cash. The cash and bank balance at the end of the 2006 financial year was US$23.89 million. The increase in cash and bank balance during the financial year is as a result of a private placement mid year in which US$9.99 million was raised, A$4 million raised by way of a private placement to United States accredited investors in December 2006 and A$18 million raised in December 2006 by way of a initial public offering in Australia.

Research and development expenses

During the financial year ending December 31, 2006, overall expenditure on research and development increased by approximately 55% compared to 2005. In general this reflects the increased level of spending required as the Company's projects move through the research and development process towards a product.

Administration expenses

Total administration expenses for the financial year ending December 31, 2006 were US$1.69 million, an increase of 140%, over the 2005 financial year. This increase in expenses reflects growth in the size and complexity of the Group's operations, as well as the incremental costs of being listed on the ASX and costs associated with regulatory compliance in the United States.

Fair value of stock options issued to employees

As of January 1, 2006, the Company adopted Statement No. 123(R), 'Share Based Payment', or SFAS 123(R). The impact of the change in accounting policy is an increase in non cash expenses of US$304,180.

Income tax expense

Income tax expense relates to the reversal of research and development credits.

Risk Management

The Company takes a proactive approach to risk management. The Board is responsible for ensuring that risks, and also opportunities, are identified on a timely basis and that the Company's objectives and activities are aligned with the risks and opportunities identified by the Board. The Board has delegated certain financial risk management responsibilities to the Audit and Compliance Committee.

SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

The Company undertook an initial public offering of its shares of common stock during November and December 2006 raising A$18 million and a concurrent private placement in the United States raising A$4 million. The Company was admitted to the official list of, and its shares of common stock trading in the form of CHESS Depositary Interests were quoted on, ASX on December 13, 2006.

Capital Expenditure

Expenditure on plant and equipment during the financial year increased significantly in connection with the purchase of new manufacturing equipment. The Company ended the financial year ending December 31, 2006 with US$23.89 million in cash and deposits. During the financial year ending December 31, 2006, the net cash flows used in operating activities was US$1.53 million compared with net cash flows provided by operating activities of US$0.21 million for the year ended December 31, 2005.

SIGNIFICANT EVENTS AFTER THE BALANCE DATE

On March 28, 2007 the Company announced that, subsequent to a review of employee performance for the year ended December 31, 2006, the directors granted 845,000 employee options under the Company's Employee Option Plan. Included within this grant are 45,000 employee options granted to the Managing Director which require shareholder approval.

Other than as disclosed above, in the interval between the end of the financial year and March 30, 2007, there has not arisen any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Company, the results of those operations, or the state of affairs of the Company in future financial years.

LIKELY DEVELOPMENTS AND EXPECTED RESULTS

Over the coming financial year ending December 31, 2007, the Company will focus on:

- continuing research and development activities with respect to the Company's C-reactive protein test and prothrombin time test;
- continuing development activities in relation to the blood glucose test pursuant to the development and research agreement with LifeScan with a view to being capable of commercially manufacturing the blood glucose test at volumes suited to the market;
- seek certification of the Company's quality management system by regulatory authorities under ISO 13485:2003;
- performing a clinical trial of the glucose sensor system;
- completing the establishment of the Company's new premises at Corporate Avenue in Melbourne Victoria and moving into those premises in the second half of 2007;
- completing acquisition, then commissioning and validating manufacturing equipment customized to the Company's designs;
- seeking regulatory approval of the blood glucose test.

Information about other likely developments in the operations of the Company and the expected results of operations in future financial years have not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Company.

ENVIRONMENTAL REGULATIONS

The Company is subject to a range of environmental regulations in respect of its activities, including in relation to the disposal of chemical waste. There have been no known breaches of any material environmental regulations that apply to the Company.

INDEMNIFICATION AND INSURANCE OF OFFICERS

The certificate of incorporation of the Company provides that no director or former director shall be personally liable to the Company or any of its shareholders for monetary damages for breach of fiduciary duty as a director, except to the extent such exemption from liability or limitation is not permitted under the Delaware General Corporation Law and in such case, that the Company shall indemnify its directors and officers to the fullest extent authorized or permitted by law.

In addition to the indemnities provided in the certificate of incorporation and amended and restated by-laws, the Company has entered into indemnification agreements with certain of its officers and each of its directors. Subject to the relevant limitations imposed by applicable law, the indemnification agreements, among other things:

- indemnify the relevant officers and directors for certain expenses, judgments, fines and settlement amounts incurred by them in connection with their services as an officer or director of the Company or its subsidiaries; and
- require the Company to make a good faith determination whether or not it is practicable to maintain liability insurance for officers and directors or to ensure the Company's performance of its indemnification obligations under the agreements.

During the financial year, the Company paid insurance premiums in respect of a contract, insuring all the directors, the company secretary and chief financial officer against liability whilst acting in their capacity as a director or officer (as applicable) of the Company. In accordance with the terms of the insurance policy and commercial practice, the amount of the premium has not been disclosed.

No liability has arisen under these indemnities at the date of this report. The liabilities insured are legal costs that may be incurred in defending civil or criminal proceedings that may be brought against the officers of the Company other than where such liabilities arise out of conduct involving a willful breach of duty by the officers or the improper use by the officers of their position or of information to gain advantage for themselves or someone else or to cause detriment to the Company.

KEY MANAGEMENT PERSONNEL DISCLOSURES (UNAUDITED)

(a) Directors

The following persons were directors of the Company during the financial year ending December 31, 2006:

(i) Non-executive Chairman

Andrew Denver

(ii) Executive director

Mark Morrisson, Chief Executive Officer and Managing Director

(iii) Non-executive directors

Dr Colin Adam (appointed December 6, 2006)*

Denis Hanley

Andrew Jane (appointed August 15, 2006)

Charles Kiefel (appointed December 6, 2006)*

Dr Elizabeth (Jane) Wilson (appointed December 6, 2006)

Roger Guidi (resigned November 3, 2006)

* Prior to his appointment as a director of the Company, Dr Colin Adam was a director of Universal Biosensors Pty Ltd between July 10, 2002 and December 12, 2006. Prior to his appointment as a director of the Company, Mr Charles Kiefel was a director of Universal Biosensors Pty Ltd between September 19, 2002 and December 6, 2006.

(b) Other key management personnel

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

Name	Position
Dr Alastair Hodges	Chief Scientist
Garry Chambers	Vice President of Operations
Ronald Chatelier	Chief Research Scientist
Salesh Balak (commenced November 27, 2006)	Chief Financial Officer
Ian Bennett (resigned October 1, 2006)	Chief Financial Officer

All of the above persons were key management persons for the entire period unless otherwise stated. All executives were employed by Universal Biosensors Pty Ltd.

(c) Key management personnel compensation

	Consolidated	
	2006 $	2005 $
Short-term employee benefits	**1,056,626**	886,488
Post-employment benefits (superannuation)	**94,733**	76,633
Share-based payments	**242,828**	45,080
	1,394,187	1,008,201

(d) Equity instrument disclosures relating to key management personnel

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

Details of options provided as remuneration and shares issued on the exercise of such options, together with terms and conditions of the options, can be found in section D of the Remuneration Report.

(ii) Option holdings

The numbers of options over common stock in the Company held during the financial year by each director of the Company and other key management personnel of the Group, including their personally related parties, are set out below. No options have been granted to non executive directors.

2006* Name	Balance at the start of the year	Granted during the year as compensation	Exercised during the year	Forfeited during the year	Balance at the end of the year	Vested and exercisable at the end of the year
Directors of the Company						
M Morrisson	–	960,560	–	–	960,560	320,186
Other key management personnel of the Group						
A Hodges	768,448	36,248	–	–	804,696	768,448
G Chambers	576,336	36,248	–	–	612,584	576,336
R Chatelier	115,993	36,248	–	–	152,241	115,993
S Balak	–	–	–	–	–	–
I Bennett (resigned October 1, 2006)	115,993	36,248	–	(72,496)	79,745	79,745

320,186 options granted in 2006 vested by the end of the year.

2005* Name	Balance at the start of the year	Granted during the year as compensation	Exercised during the year	Forfeited during the year	Balance at the end of the year	Vested and exercisable at the end of the year
Directors of the Company						
M Morrisson	–	–	–	–	–	–
Other key management personnel of the Group						
A Hodges	768,448	–	–	–	768,448	512,299
G Chambers	576,336	–	–	–	576,336	384,224
R Chatelier	115,993	–	–	–	115,993	77,329
I Bennett	115,993	–	–	–	115,993	77,329

* The options numbers above are shown on a post subdivision basis to reflect the subdivision of our share capital by approximately 3,624.75 which occurred immediately prior to the issue and allotment of shares under the initial public offer of the Company in Australia in December 2006.

(iii) Share holdings

The numbers of shares in the Company held during the financial year ended December 31, 2006 by each director of the Company and other key management personnel of the Group, including their personally related parties, are set out below. There were no shares granted during the reporting period as compensation.

2006* Name	Balance at the start of the year	Received during the year on the exercise of options	Purchases during the year	Balance at the end of the year
Directors of the Company				
Common stock				
A Denver[(1)]	6,750,193	–	1,181,812	7,932,005
M Morrisson	–	–	-	-
Dr C Adam (appointed December, 6 2006)[(2)]	6,206,481	–	420,470	6,626,951
D Hanley[(3)]	7,475,145	–	819,960	8,295,105
A Jane (appointed August 15, 2006)[(4)]	–	–	15,196,879	15,196,879
C Kiefel (appointed December 6, 2006)[(5)]	5,844,005	–	–	5,844,005
Dr J Wilson (appointed December 6, 2006)	–	–	1,015,000	1,015,000
R Guidi (resigned November 3, 2006)[(6)]	10,210,926	–	8,020,803	18,231,729
Other key management personnel of the Group				
Common stock				
A Hodges	2,990,420	–	57,996	3,048,416
G Chambers	1,497,022	–	253,733	1,750,755
R Chatelier	1,497,022	–	–	1,497,022
S Balak	–	–	–	–
I Bennett (until 1 October 2006)[(7)]	–	–	–	–

The numbers of shares in the Company held during the financial year ended December 31, 2005 by each director of the Company and other key management personnel of the Group, including their personally related parties, are set out below. There were no shares granted during the reporting period as compensation.

2005* Name	Balance at the start of the year	Received during the year on the exercise of options	Purchases during the year	Balance at the end of the year
Directors of the Company				
Common stock				
A Denver(1)	6,750,193	–	–	6,750,193
M Morrisson	–	–	–	–
Dr C Adam (appointed December 6, 2006)(2)	6,206,481	-	-	6,206,481
D Hanley(3)	7,475,145	–	–	7,475,145
A Jane (appointed August 15, 2006)	–	–	–	–
C Kiefel (appointed December 6, 2006(5)	5,844,005	–	–	5,844,005
Dr J Wilson (appointed December 6, 2006)	––	–	–	–
R Guidi (resigned November 3, 2006)(6)	10,210,926	–	–	10,210,926
Other key management personnel of the Group				
Common stock				
A Hodges	2,990,420	–	–	2,990,420
G Chambers	1,497,022	–	–	1,497,022
R Chatelier	1,497,022	–	–	1,497,022
I Bennett	–	–	–	–

* Share numbers shown take into account the conversion of preferred shares into common stock on a one for one basis which occurred immediately prior to the closing of the initial public offer in Australia on 5 December 2006. Additionally, the share numbers are shown on a post subdivision basis to reflect the subdivision of our share capital by approximately 3,624.75 which occurred immediately prior to the issue and allotment of shares under the initial public offer.

(1) Includes 5,662,768 shares held by The Principals Cornerstone Fund Pty Limited on trust for Andrew Denver.

(2) Includes 5,662,768 shares held by The Principals Cornerstone Fund Pty Limited on trust for Colin Adam.

(3) Includes 5,662,770 shares held by The Principals Cornerstone Fund Pty Limited on trust for Denis Hanley.

(4) Closing balance includes: (i) 11,688,767 shares held by CM Capital Investments Pty Ltd as trustee of the CM Capital Venture Trust No.3; and (ii) 3,508,112 shares held by CIBC Australia VC Fund LLC as general partner of the Australia Venture Capital Fund L.P., of which CM Capital Investments Pty Ltd is a special limited partner. Andrew Jane is a partner of CM Capital Investments Pty Ltd. Andrew Jane may be taken to have an indirect pecuniary interest in an indeterminate portion of all shares of common stock held by CM Capital Investments Pty Ltd and CIBC Australia VC Fund LLC.

(5) Includes 5,662,768 shares held by The Principals Cornerstone Fund Pty Limited on trust for Charles Kiefel.

(6) All shares are held by Johnson & Johnson Development Corporation of which, Roger Guidi is an officer.

(7) On January 5, 2007, upon exercise of employee options, Ian Bennett acquired 79,745 shares in the Company.

(e) Loans to key management personnel

Loans made to directors of the Company and other key management personnel of the Group, including their personally related parties, are nil.

(f) Other transactions with key management personnel

Denis Hanley, Andrew Denver, Dr Colin Adam and Charles Kiefel are shareholders and directors of the Company and of The Principals Funds Management Pty Ltd, which was paid a total of US$325,000 in 2006 from the Company in connection with capital raising services. The Principals Funds Management Pty Ltd was paid a firm commitment fee of US$79,118 by Wilson HTM Corporate Finance Limited in connection with firm commitments to subscribe for shares given in connection with the Company's initial public offering in Australia.

Andrew Jane is a director of the Company and is a Partner of CM Capital Investments Pty Ltd which is a special limited partner of CIBC Australia VC Fund LLC who are shareholders of the Company. 135,000 shares were transferred to CM Capital Investments Pty Ltd by Wilson HTM Corporate Finance Limited as a commitment fees as a result of CM Capital Investments Pty Ltd subscribing for shares in the Company's initial public offering in Australia.

Dr Jane Wilson is a shareholder and director of the Company. The spouse of Dr Wilson is a substantial shareholder and officer of the parent company of Wilson HTM Corporate Finance Limited, the underwriter and lead managers of the Company's initial public offering in Australia. The transaction with Wilson HTM Corporate Finance Limited is not considered a related party as Dr Wilson accepted the appointment as a director of the Company subsequent to Wilson HTM Corporate Finance Limited accepting their engagement.

REMUNERATION REPORT (UNAUDITED)

The remuneration report is set out under the following main headings:

A Principles used to determine the nature and amount of remuneration

B Details of remuneration

C Service agreements

D Share-based compensation

A Principles used to determine the nature and amount of remuneration (unaudited)

The objective of the Group's executive reward framework is to ensure reward for performance is competitive and appropriate for the results delivered. The framework aligns executive reward with achievement of strategic objectives and the creation of value for shareholders, and conforms with market best practice for delivery of reward. The performance of the Company depends upon the quality of its directors and executives. In order to attract, motivate and retain highly skilled directors and executives, the Company embodies the following principles in its remuneration framework:

- provide competitive remuneration to attract, motivate and retain high calibre directors and executives with appropriate skills and experience;
- remunerate with a mix of short and long term components;
- remunerate executives according to individual performance and pre-determined benchmarks through cash bonuses; and
- link executive remuneration to shareholder value through options.

The Remuneration and Nomination Committee has processes in place to review the performance of the Board of Directors and senior executives of the Company.

Remuneration Structure

In accordance with best practice corporate governance, the structure of non-executive directors and executive remuneration is separate and distinct. The framework provides a mix of fixed and variable pay, and a blend of short and long-term incentives.

Non-executive directors

Fees and payments to non-executive directors reflect the demands which are made on, and the responsibilities of, the directors. Non-executive directors' fees and payments are reviewed annually by the Board. The Chairman's fees are determined independently to the fees of non-executive directors based on comparative roles in the external market. The Chairman is not present at any discussions relating to determination of his own remuneration. Non-executive directors' fees (including statutory superannuation) are determined within an aggregate directors' fee pool limit, which is periodically recommended for approval by shareholders. The pool of remuneration approved by shareholders at a general meeting currently stands at a maximum of A$500,000 per annum in total. Termination payments do not apply to non-executive directors. Non-executive directors are also entitled to be reimbursed for certain of their expenses. The annual remuneration payable to our non-executive directors currently comprises of:

- a base fee of A$100,000 per annum for the chairman and A$50,000 for other non-executive directors;
- an additional fee for directors serving on sub-committees, currently A$5,000 per annum and an additional A$5,000 for each chairperson of such sub-committees; and
- statutory superannuation for the independent non-executive directors, currently 9% of the base fee.

Executive pay

The executive pay and reward framework has four components:

- base pay;
- short-term performance incentives in the form of cash bonuses;
- long-term incentives through participation in the Company's Employee Option Plan; and
- other remuneration such as superannuation.

The combination of these comprises the executive's total remuneration.

Base pay

Structured as a total employment cost package which may be delivered as a combination of cash and prescribed non-financial benefits at the executives' discretion. Executives are offered a competitive base pay that comprises the fixed component of pay and rewards. Base pay for senior executives is reviewed annually to ensure the executive's pay is competitive with the market. An executive's pay is also reviewed on promotion. There are no guaranteed base pay increases included in any senior executives' contracts.

Short-term incentives

If the executive achieves pre-determined milestones as set by the Remuneration and Nomination Committee, a short-term incentive may be available to executives during the annual review. If payable, cash incentives (bonuses) are payable in the first quarter of each year. Each executive has a target short-term incentive opportunity depending on the accountabilities of the role and impact on the organisation or business unit performance.

Each year, the Remuneration and Nomination Committee considers the appropriate targets and key performance indicators to link short-term incentives and the level of payout if targets are met. This includes setting any maximum short-term incentive that may be paid to an executive, and minimum levels of performance to trigger payment of short-term incentive.

For the year ended December 31, 2006, the key performance indicators linked to short-term incentives were based on Group, departmental and personal objectives. The key performance indicators required performance in achieving specific targets in relation to economic value added (EVA), as well as other key, strategic non-financial measures linked to drivers of performance in future reporting periods. These key performance indicators are generic across the senior executive team.

The Remuneration and Nomination Committee is responsible for assessing whether the key performance indicators are met. To help make this assessment, the committee receives detailed reports on performance from management.

The short-term bonus payments may be adjusted up or down in line with under or over achievement against the target performance levels. This is at the discretion of the Remuneration and Nomination Committee.

B Details of remuneration (unaudited)

Amounts of remuneration

Details of the remuneration of the directors and the key management personnel of the Group are set out in the following tables.

The cash bonuses are dependent on the satisfaction of performance conditions as set out in the section headed Short-term incentives above.

Directors and key management personnel of the Company

		Short-term benefits			Post-employment benefits	Share-based payment	
Name	Year	Cash salary and fees A$	Cash bonus A$	Non monetary benefits A$	Super-annuation A$	Options (Note 2) A$	Total A$
Non-executive directors							
A Denver Chairman	2006	53,723	–	–	4,835	–	58,558
	2005	29,167	–	–	2,625	–	31,792
Dr C Adam	2006	27,030	–	–	2,433	–	29,463
	2005	25,000	–	–	2,250	–	27,250
D Hanley	2006	27,030	–	–	2,433	–	29,463
	2005	45,833	–	–	4,125	–	49,958
A Jane	2006	4,032	–	–	–	–	4,032
	2005	–	–	–	–	–	–
C Kiefel	2006	27,030	–	–	2,433	–	29,463
	2005	25,000	–	–	2,250	–	27,250
Dr J Wilson	2006	4,032	–	–	363	–	4,395
	2005	–	–	–	–	–	–
R Guidi (resigned	2006	–	–	–	–	–	–
3 November 2006)	2005	–	–	–	–	–	–
Sub-total non-executive	**2006**	**142,877**	**–**	**–**	**12,497**	**–**	**155,374**
director	**2005**	**125,000**	**–**	**–**	**11,250**	**–**	**136,250**
Executive director							
M Morrisson(1)	2006	261,458	–	–	23,531	206,227	491,216
	2005	125,000	–	–	11,250	–	136,250
Other key management personnel							
A Hodges	2006	219,264	–	–	19,733	15,445	254,442
	2005	208,850	15,000	–	18,796	22,604	265,250
G Chambers	2006	172,746	–	–	15,547	13,296	201,589
	2005	156,637	10,000	–	14,097	16,969	197,703
Dr R Chatelier	2006	130,311	–	–	11,728	7,860	149,899
	2005	121,133	10,000	–	10,902	3,394	145,429
S Balak (appointed	2006	11,875	-	–	1,068	–	12,943
November 27, 2006)	2005	–	-	–	–	–	–
I Bennett (resigned	2006	118,095	–	–	10,629	–	128,724
October 1, 2006)	2005	114,868	–	–	10,338	2,113	127,319
Totals	**2006**	**913,749**	**–**	**–**	**82,236**	**242,828**	**1,238,813**
	2005	**726,488**	**35,000**	**–**	**65,383**	**45,080**	**871,951**

(1) M Morrison commenced employment on July 1, 2005 and was appointed to the board of the Company on August 9, 2005.

(2) The options numbers above are shown on a post subdivision basis to reflect the subdivision of our share capital by approximately 3,624.75 which occurred immediately prior to the issue and allotment of shares under the initial public offer of the Company in Australia in December 2006.

C Executive service agreements (unaudited)

Remuneration and other terms of employment for the Chief Executive Officer and the other key management personnel are formalised in executive service agreements. The major provisions of the agreements relating to remuneration are set out below. All contracts with executives may be terminated early by either party with three months notice or immediately for cause. No additional payments apply on termination.

M Morrisson, *Managing Director*

- Term of agreement – subject to earlier termination, until June 30, 2008.
- Base salary, inclusive of superannuation, for the year ended January 31, 2007 of A$286,125, to be reviewed annually by the Remuneration and Nomination Committee.

A Hodges, *Chief Scientist*

- Term of agreement – subject to earlier termination, until March 31, 2009.
- Base salary, inclusive of superannuation, for the year ending January 31, 2007 of A$239,950, to be reviewed annually by the Remuneration and Nomination Committee.

G Chambers, *Vice President of Operations*

- Term of agreement – subject to earlier termination, until March 31, 2009.
- Base salary, inclusive of superannuation, for the year ending January 31, 2007 of A$207,100, to be reviewed annually by the Remuneration and Nomination Committee.

R Chatelier, *Chief Research Scientist*

- Term of agreement – subject to earlier termination, until March 31, 2009.
- Base salary, inclusive of superannuation, for the year ending January 31, 2007 of A$174,400, to be reviewed annually by the Remuneration and Nomination Committee.

S Balak, *Chief Financial Officer (from November 27, 2006)*

- Term of agreement – subject to earlier termination, until November 26, 2009.
- Base salary, inclusive of superannuation, for the year ended January 31, 2007 of A$163,500, to be reviewed annually by the Remuneration and Nomination Committee.

D Sharebased compensation (unaudited)

Options

Our Employee Option Plan was adopted by the Company in 2004 and approved by our stockholders in October 2006. The Plan permits our Board to grant stock options to our employees, directors and consultants. The total number of shares that may be issued under the Plan is such maximum amount permitted by law and the Listing Rules of ASX. When exercisable, each option is convertible into one share of common stock at an exercise price determined on the date of grant. The contractual life of each option granted is ten years. No option holder has any right under the option to participate in any other issues of shares of common stock of the Company or any other entity without first having exercised the options. The exercise price and any exercise conditions are determined by the board at the time of grant of the options. Any exercise conditions must be satisfied before the options vest and become capable of exercise. The options lapse on such date determined by the board at the time of grant or earlier in accordance with the Plan. Options granted to date have had a ten year term and generally vest in equal tranches over three years. Options may be subject to adjustment in the event of a stock split, stock dividend, consolidation or other change in the structure of our capitalization. Options carry no dividend or voting rights.

Details of options over shares in the Company provided as remuneration to each director of the Company and each of the key management personnel of the Group are set out below. Further information on the options is set out in note 6 to the financial statements.

Name	Number of options granted during the year 2006	2005	Number of options vested during the year 2006	2005
Directors				
M Morrisson	960,560	–	320,186	–
Other key management personnel of the Group				
A Hodges	36,248	–	256,149	256,150
G Chambers	36,248	–	192,112	192,112
R Chatelier	36,248	–	38,664	38,665

The assessed fair value at grant date of options granted to the individuals is allocated equally over the period from grant date to vesting date, and the amount is included in the remuneration tables above. Fair values at grant date are independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option. The model inputs for options granted during the year ended December 31, 2006 included:

	Grant Date 2006	2004
Exercise Price	US$0.33	US$0.29
Share Price at Grant Date	US$0.33	US$0.29
Volatility	55%	40% – 45%
Expected Life	10 years	10 years
Risk Free Interest Rate	4.4%	4.65%
Fair value of Option	US$0.23	US$0.08

Shares provided on exercise of remuneration options

No shares have been provided by the Company in this regard to the directors of the Company. The only shares to be issued to key management personnel of the Group are 79,745 shares issued to Ian Bennett on exercise of existing vested options on January 5, 2007.

NON-AUDIT SERVICES (UNAUDITED)

Non-Audit Services

The following non-audit services were provided by the Company's auditor, PricewaterhouseCoopers. The directors are satisfied that the provision of non-audit services during the year by PricewaterhouseCoopers is compatible with the general standard of independence for auditors. The nature and scope of each type of non-audit service provided means that auditor independence was not compromised.

PricewaterhouseCoopers received or are due to receive the following amounts for the provision of non audit services:

	2006 A$	2005 A$
Tax services	115,574	–
Grant audit	5,500	–
Initial public offering	155,000	–
Total	**276,074**	**–**

Consolidated Financial Statements and Schedules

UNIVERSAL BIOSENSORS, INC. (A Development Stage Enterprise)

Contents

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers
ABN 52 780 433 757

Freshwater Place
2 Southbank Boulevard
SOUTHBANK VIC 3006
GPO Box 1331L
MELBOURNE VIC 3001
DX 77
Website:www.pwc.com/au

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of Universal Biosensors Inc:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, changes in stockholder's equity and comprehensive income and cash flows present fairly, in all material respects, the financial position of Universal Biosensors Inc. and its subsidiaries (a development stage enterprise) at December 31, 2006 and 2005, and the results of their operations and their cash flows for the years ended December 31, 2004, December 31, 2005 and December 31, 2006 and, cumulatively, for the period from September 14, 2001 (date of inception) to December 31, 2006 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers

PricewaterhouseCoopers
March 30, 2007

Balance Sheets

(U.S. dollars)

	As of December 31,	
	2006	2005
	$	$
ASSETS		
Current assets:		
Cash	23,885,198	3,253,426
Accrued income	76,968	–
Other current assets	421,394	49,158
Total current assets	24,383,560	3,302,584
Property, plant, and equipment – net (note 9)	5,667,535	1,248,761
Total assets	30,051,095	4,551,345
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	1,226,779	85,971
Income taxes payable	128,982	–
Accrued expenses (note 10)	613,492	114,734
Deferred income	–	76,510
Employee entitlements provision	111,691	80,628
Total current liabilities	2,080,944	357,843
Non-current liabilities:		
Employee entitlements provision	55,426	26,423
Total non-current liabilities	55,426	26,423
Total liabilities	2,136,370	384,266
Commitments and contingencies (note 4)		
Stockholders' equity:		
Convertible preferred stock, $0.01 par value. Authorized 1,000,000 shares; issued and outstanding nil in 2006 (2005: 2,817 – pre-stock split)	–	3,000,000
Common stock, $0.0001 par value. Authorized 300,000,000 shares; issued and outstanding 127,999,976 shares in 2006 (2005: 43,613,014)	12,800	4,361
Additional paid-in capital	30,144,048	1,315,148
Deficit accumulated during the development stage	(2,387,877)	(168,838)
Accumulated other comprehensive income	145,754	16,408
Total stockholders' equity	27,914,725	4,167,079
Total liabilities and stockholders' equity	30,051,095	4,551,345

See accompanying notes to the financial statements.

Statement of Operations

(U.S. dollars)

	Period from inception (September 14, 2001 to December 31, 2006	Years ended December 31, 2006	2005	2004
	$	$	$	$
Revenue	–	–	–	–
Cost of goods sold	–	–	–	–
Gross profit	–	–	–	–
Operating expenses:				
Research and development	7,152,420	2,469,971	1,591,829	1,567,933
General and administrative	3,194,643	1,689,925	703,036	395,246
Fair value of stock options issued to employees related to:				
Research and development	106,463	106,463	–	–
General and administrative	197,717	197,717	–	–
Total operating expenses	10,651,243	4,464,076	2,294,865	1,963,179
Research and development income	7,652,826	2,000,000	2,086,013	1,816,813
Loss from operations	(2,998,417)	(2,464,076)	(208,852)	(146,366)
Interest and other income	726,384	367,858	171,886	89,944
Net loss before tax	(2,272,033)	(2,096,218)	(36,966)	(56,422)
Income tax expense	(115,844)	(122,821)	–	–
Net loss	(2,387,877)	(2,219,039)	(36,966)	(56,422)
Basic and diluted net loss per share	(0.06)	(0.04)	0.00	0.00

See accompanying notes to the financial statements.

Statement of Changes in Stockholders' Equity and Comprehensive Income

(U.S. dollars)

	Preference Shares		Ordinary shares				Foreign currency	Total
	Shares	Amount $	Shares	Amount $	Additional paid-in capital $	Accumulated deficit $	translation reserve $	stockholders' equity $
Balance at inception (September 14, 2001)	–	–	–	–	–	–	–	–
Issuance of ordinary shares at $0.0001 per share for cash on incorporation of the Company in September 2001 #	–	–	29,179,253	2,918	(2,798)	–	–	120
Issuance of ordinary shares at $0.03 per share for cash #	–	–	10,729,264	1,073	294,897	–	–	295,970
Issuance of ordinary shares at $0.28 per share for cash #	–	–	3,624,752	362	999,628	–	–	999,990
Issuance of preference shares at $0.29 per share for cash #	10,210,926	3,000,000	–	–	–	–	–	3,000,000
Comprehensive Income								
Net loss for period from inception to December 31, 2003	–	–	–	–	–	(75,450)	–	(75,450)
Foreign currency translation reserve	–	–	–	–	–		185,891	185,891
Total Comprehensive Income	–	–	–	–	–	–	–	110,441
Balances at December 31, 2003	10,210,926	3,000,000	43,533,269	4,353	1,291,727	(75,450)	185,891	4,406,521
Comprehensive Income								
Net loss	–	–	–	–	–	(56,422)	–	(56,422)
Foreign currency translation reserve	–	–	–	–	–	–	(22,491)	(22,491)
Total Comprehensive Income	–	–	–	–	–	–	–	(78,913)
Balances at December 31, 2004	10,210,926	3,000,000	43,533,269	4,353	1,291,727	(131,872)	163,400	4,327,608
Comprehensive Income								
Net loss	–	–	–	–	–	(36,966)	–	(36,966)
Foreign currency translation reserve	–	–	–	–	–	–	(146,992)	(146,992)
Total Comprehensive Income								(183,958)
Exercise of stock options issued to employees	–	–	79,745	8	23,421	–	–	23,429
Balances at December 31, 2005	10,210,926	3,000,000	43,613,014	4,361	1,315,148	(168,838)	16,408	4,167,079
Issuance of preference shares at $0.33 per share for cash #	30,176,036	9,990,000	–	–	–	–	–	9,990,000
Conversion of preference shares to ordinary shares	(40,386,962)	(12,990,000)	40,386,962	4,039	12,985,961	–	–	–
Issuance of ordinary shares at $0.40 per share in private placement to American institutional and sophisticated investors in December 2006, net of issuance costs #	–	–	8,000,000	800	2,825,229	–	–	2,826,029
Issuance of ordinary shares at $0.40 per share in a public offering to Australian institutional and sophisticated investors in December 2006, net of issuance costs #	–	–	36,000,000	3,600	12,713,530	–	–	12,717,130
Comprehensive Income								
Net loss	–	–	–	–	–	(2,219,039)	–	(2,219,039)
Foreign currency translation reserve	–	–	–	–	–	–	129,346	129,346
Total Comprehensive Income								(2,089,693)
Stock option expense	–	–	–	–	304,180	–	–	304,180
Balances at December 31, 2006	–	–	127,999,976	12,800	30,144,048	(2,387,877)	145,754	27,914,725

Note
Common stock has a par value of $0.0001.
All share and per share amounts from inception to December 31, 2006 presented have been retroactively adjusted to give effect to the stock split detailed in Note 11 of the financial statements. The par value of common stock was altered after the share split.

Statement of Cash Flows

(U.S. dollars)

		Years ended December 31,		
	Period from inception to December 31, 2006	2006	2005	2004
	$	$	$	$
Cash flows from operating activities provided by/(used in):				
Net loss	(2,387,877)	(2,219,039)	(36,966)	(56,422)
Adjustments to reconcile net loss to net cash used in operating activities:				
Depreciation of plant & equipment	890,451	231,613	228,103	200,944
Share based payments expense	304,180	304,180	–	–
Translation (gain)/loss	(341,552)	(148,268)	(81,270)	(72,860)
Change in assets and liabilities:				
Prepaid expenses and other current assets	(353,563)	(305,106)	(29,627)	(12,500)
Grants receivable	(76,968)	(153,477)	76,510	–
Income tax payable	128,982	128,982	–	–
Payroll liabilities	287,371	180,320	59,202	18,574
Accounts payable and accrued expenses	642,330	442,324	(8,382)	141,190
Net cash provided by/(used in) operating activities	(906,646)	(1,538,471)	207,570	218,926
Cash flows from investing activities:				
Purchases of property, plant and equipment	(3,986,323)	(3,377,721)	(214,682)	(190,023)
Net cash used in investing activities	(3,986,323)	(3,377,721)	(214,682)	(190,023)
Cash flows from financing activities:				
Net proceeds from preferred and common share issuance	28,829,239	25,533,159	–	–
Proceeds from stock options exercised	23,429	–	23,429	–
Net cash provided by financing activities	28,852,668	25,533,159	23,429	–
Net increase in cash and cash equivalents	23,959,699	20,616,967	16,317	28,903
Cash and cash equivalent at beginning of period	–	3,253,426	3,225,446	3,197,621
Effect of exchange rate fluctuations on the balances of cash held in foreign currencies	(74,501)	14,805	11,663	(1,078)
Cash and cash equivalents at end of period	23,885,198	23,885,198	3,253,426	3,225,446

See accompanying notes to the financial statements.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

(1) Organization of the Company

Universal Biosensors, Inc. (the 'Company') was incorporated on September 14, 2001 in the United States, and it's wholly owned subsidiary and operating vehicle, Universal Biosensors Pty Ltd, was incorporated in Australia on September 21, 2001. Collectively, the Company and its wholly owned subsidiary Universal Biosensors Pty Ltd are referred to as 'Universal Biosensors' or the 'Group'. The Company was listed on the Australian Securities Exchange ('ASX') on December 13, 2006 following the initial public offering in Australia of the Company's shares.

The Company is a specialist medical diagnostics company focused on the development, manufacture and commercialization of a range of in vitro diagnostic tests for point-of-care use. In vitro diagnostic testing involves the testing of a body fluid or tissue sample outside the body

The diagnostic tests comprise a novel disposable test strip and a reusable meter. The diagnostic tests are small, portable and easy-to-use.

Universal Biosensors has rights to an extensive patent suites comprising 18 patent applications owned by Universal Biosensors Pty Limited and 183 patents and 227 patent applications licensed to the Company by LifeScan, Inc. ('LifeScan'), an affiliate of Johnson & Johnson Development Corporation.

The Group has a range of point-of-care blood tests in development including a C-reactive protein test which may be used to assist in the diagnosis and management of inflammatory conditions and a prothrombin time test which may be used for monitoring the therapeutic range of the anticoagulant, warfarin. The Group has already developed a working prototype of a C-reactive protein test and a prothrombin time test.

Universal Biosensors intends to develop additional immunoassay tests by taking proven disease biomarkers currently used in the central laboratory environment and adapting those diagnostic tests to the point-of-care setting, using the Group's platform of electrochemical cell technologies.

The Group also provides research and development services to LifeScan in the development of a blood glucose test. The rights to commercialization of the blood glucose test have been retained by LifeScan.

All the business operations and research and development activities are undertaken in Melbourne, Australia by the Company's wholly owned subsidiary, Universal Biosensors Pty Ltd, under a research and development sub-contract and sub-license agreement with the Company.

The Group is considered a development stage enterprise as its planned commercial manufacturing operations have not yet commenced.

(2) Basis of Presentation

These financial statements are presented in accordance with accounting principles generally accepted in the United States of America ('U.S. GAAP'). All amounts are expressed in United States dollars unless otherwise stated.

The Company's financial statements have been prepared assuming the Company will continue as a going concern. The Company has sustained operating losses since inception and expects such losses to continue as it furthers its research and development programs.

(3) Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the financial statements of the Company and its wholly owned subsidiary Universal Biosensors Pty Ltd. All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of the consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the period. Significant items subject to such estimates and assumptions include the carrying amount of property, plant and equipment, deferred income taxes and obligations related to employee benefits. Actual results could differ from those estimates.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Cash & Cash Equivalents

The Company considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents. For cash and cash equivalents, the carrying amount approximates fair value due to the short maturity of those instruments.

Concentration of Credit Risk and Other Risks and Uncertainties

Cash and cash equivalents consists of financial instruments that potentially subject the Company to concentration of credit risk to the extent of the amount recorded on the balance sheet. The Company's cash and cash equivalents are invested with one of Australia's four largest banks. The Company is exposed to credit risk in the event of default by the banks holding the cash or cash equivalents to the extent of the amount recorded on the balance sheets. The Company has not experienced any losses on its deposits of cash and cash equivalents.

Product candidates developed by the Company may require approvals or clearances from the U.S. Food and Drug Administration or other international regulatory agencies prior to commercialized sales. There can be no assurance that the Company's product candidates will receive any of the required approvals or clearances. If the Company was denied approval or clearance of such approval was delayed, it may have a material adverse impact on the Company.

Property, Plant, and Equipment

Property, plant, and equipment are recorded at acquisition cost, less accumulated depreciation.

Depreciation on plant and equipment is calculated using the straight-line method over the estimated useful lives of the assets. The estimated useful life of machinery and equipment is 4 to 10 years. Leasehold improvements are amortized on the straight-line method over the shorter of the remaining lease term or estimated useful life of the asset. Maintenance and repairs are charged to operations as incurred and include minor corrections and normal services and does not include items of capital nature.

Research and Development

Research and development expenses consists of costs incurred to further the Group's research and development activities and include salaries and related employee benefits, costs associated with clinical trial and preclinical development, regulatory activities, research-related overhead expenses, costs associated with the manufacture of clinical trial material, costs associated with developing a commercial manufacturing process, costs for consultants and related contract research, facility costs and depreciation. Research and development costs are expensed as incurred.

The Group receives Australian government grants as compensation for expenses incurred in respect of certain research activities into dry chemistry immunosensors. Such grants reduce the related research and development expenses as and when the relevant research expenses are incurred. Grants received in advance of incurring the relevant expenditure are treated as deferred research grants and included in current liabilities on the balance sheet as the Group has not earned these amounts until the relevant expenditure has been incurred. Grants due to the Group under research agreements are included in current assets on the balance sheet.

Income Taxes

The Company applies Statement of Financial Accounting Standards No. 109 – Accounting for Income Taxes (SFAS 109) which establishes financial accounting and reporting standards for the effects of income taxes that result from a company's activities during the current and preceding years. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Where it is more likely than not that some portion or all of the deferred tax assets will not be realized the deferred tax assets are reduced by a valuation allowance. The valuation allowance is sufficient to reduce the deferred tax assets to the amount that is more likely than not to be realized. A reconciliation of the valuation and qualifying accounts is attached as Schedule ii.

Fair Value of Financial Instruments

The carrying value of all current assets and current liabilities approximates fair value because of their short-term nature. The estimated fair value of all other amounts has been determined by using available market information and appropriate valuation methodologies.

Impairment of Long-Lived Assets

The Company reviews its capital assets, including patents and licenses, for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable. In performing the review, the Company estimates undiscounted cash flows from products under development that are covered by these patents and licenses. An impairment loss would be recognized when estimated undiscounted future cash flows expected to result from the use of the asset and its eventual disposition is less than the carrying amount of the asset. Impairment, if any, is measured as the amount by which the carrying amount of the assets exceeds its fair value. Impairment, if any, is assessed using discounted cash flows.

Goods and Services Tax (GST)

Revenues, expenses and assets are recognized net of the amount of associated GST, unless the GST incurred is not recoverable from the taxation authority. In this case it is recognized as part of the cost of acquisition of the asset or as part of the expense. Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables or payables in the balance sheet. Cash flows are presented on a gross basis.

Revenue Recognition

Research and development revenue

The Company receives research and development revenue under an agreement with LifeScan (see note 7). This agreement provides details of the amount to be charged to LifeScan each year for the provision of research and development services. Revenue is recognized when services have been performed, the amount of the payment can be reliably measured and collectibility is reasonably assured.

Interest revenue

Interest revenue is recognized as it accrues, taking into account the effective yield on the financial asset

Foreign Currency

Functional and reporting currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency').

The consolidated financial statements are presented using a reporting currency of U.S. dollars.

The functional currency of the Company for financial years up to December 31, 2005 was determined by management to be U.S. dollars. This was based on the facts that the denomination of a significant proportion of transactions and the major source of finance were in U.S. dollars.

In 2006, the Company expanded significantly its Australian based research activities. All of the Company's directors became resident in Australia. All of the Company's expenditure on research and development is Australian dollar denominated. It also began planning for and successfully accomplished a capital raising in Australian dollars and listed on the Australian Stock Exchange. The majority of cash and other monetary assets now held by the Company are denominated in Australian dollars.

Due to these changes in circumstance, management are of the view that the functional currency of the Company has changed in 2006 to Australian dollars. This change has been effected from December 1, 2006. The functional currency of Universal Biosensors Pty Ltd (the Company's subsidiary) is Australian dollars for all years presented.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the Statement of Operations.

The Company has recorded foreign currency transaction gains of $67,171, $74,672, $33,478, and $262,431 for each of the years ended December 31, 2004, 2005 and 2006 and the period from inception to December 31, 2006, respectively. These are included with 'Interest and Other Income.'

Group companies

The results and financial position of all the Group entities that have a functional currency different from the reporting currency are translated into the reporting currency as follows:

- assets and liabilities for each balance sheet item reported are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this is not a reasonable approximation of the effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognized as a separate component of equity.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities are taken to the Foreign Currency Translation Reserve ('FCTR').

Commitments and Contingencies

Liabilities for loss contingencies, arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment can be reasonably estimated.

Patent and License Costs

Legal fees incurred for patent application costs have been charged to expense and reported in research and development expense.

Clinical Trial Expenses

Clinical trial costs are a component of research and development expenses. These expenses include fees paid to participating hospitals and other service providers, which conduct certain product development activities on behalf of the Company. Depending on the timing of payments to the service providers and the level of service provided, the Company records prepaid or accrued expenses relating to these costs.

These prepaid or accrued expenses are based on estimates of the work performed under service agreements.

Leased Assets

All of the Group's leases for the years ended December 31, 2004, 2005 and 2006 are considered operating leases. The costs of operating leases are charged to the statement of operations on a straight-line basis over the lease term.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Stock-based Compensation

Prior to January 1, 2006, the Company applied Accounting Principles Board (APB) Opinion No. 25, 'Accounting for Stock Issued to Employees' and related interpretations, in accounting for its fixed-plan stock options. For periods prior to January 1, 2006, the Company complied with the disclosure only provisions of FASB Statement No.123, 'Accounting for Stock-Based Compensation', or SFAS 123. No stock-based employee compensation cost was reflected in net income, as all options granted under those plans had an exercise price equal to or greater than the market value of the underlying common stock on the date of grant (or within permitted discounted prices as it pertains to the ESPP). Results for periods before January 1, 2006 have not been restated to reflect, and do not include the impact of, FASB Statement No. 123(R), 'Share Based Payment', or SFAS 123(R). The following table illustrates the effect on net income if the fair-value-based method had been applied to all outstanding and unvested awards in each period.

	2005 $	2004 $
Net loss, as reported	(36,966)	(56,422)
Add stock-based employee compensation expense included in reported net income, net of tax	–	–
Deduct total stock-based employee compensation expense determined under fair-value-based method for all awards	(36,792)	(100,740)
Pro forma net loss	(73,758)	(157,162)

As of January 1, 2006, the Company adopted SFAS No. 123(R), using the modified prospective method, which requires measurement of compensation expense of all stock-based awards at fair value on the date of grant and amortization of the fair value over the vesting period of the award. The Company has elected to use the straight-line method of amortization. Under the modified prospective method, the provisions of SFAS 123(R) apply to all awards granted or modified after the date of adoption. In addition, the unrecognized expense of awards not yet vested at the date of adoption, determined under the original provisions of SFAS No. 123 shall be recognized in net income in the periods after adoption. The fair value of stock options is determined using the Black-Scholes valuation model, which is consistent with valuation techniques previously utilized for options in footnote disclosures required under SFAS No. 123, as amended by SFAS No. 148 'Accounting for Stock-Based Compensation Transition and Disclosure'.

Such value is recognized as expense over the service period, net of estimated forfeitures, using the straight-line method under SFAS 123(R). There were no transitional adjustments on adoption of SFAS 123 (R).

The application of SFAS 123(R) had the following effect on reported amounts for the year ended December 31, 2006 relative to amounts that would have been reported under previous accounting:

	Under Previous Accounting	2006 SFAS 123(R) Adjustments	As reported
Net loss	(1,914,859)	(304,180)	(2,219,039)

Pension Costs

As required by Australian law, Universal Biosensors Pty Ltd contributes to standard defined contribution superannuation funds on behalf of all employees at an amount up to nine percent of each such employee's salary. Superannuation is a compulsory savings program whereby employers are required to pay a portion of an employee's remuneration to an approved superannuation fund that the employee is typically not able to access until they are retired. The Company permits employees to choose an approved and registered superannuation fund into which the contributions are paid. Contributions are charged to the statement of operations as they become payable.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Net Loss per Share and Anti-dilutive Securities

Basic and diluted net loss per share is presented in conformity with Statement of Financial Accounting Standards No. 128 – Earnings Per Share (SFAS 128). Basic and diluted net loss per share has been computed using the weighted-average number of common shares outstanding during the period. All periods present in these financial statements have been retroactively adjusted to give effect to the stock split in December 2006 (note 11). The potentially dilutive options issued under the Universal Biosensors Employee Option Plan and the convertible preference shares (see note 12) were not considered in the computation of diluted net loss per share because they would be anti-dilutive given the Group's loss making position in this and previous years.

Total Comprehensive Income

The Company follows Statement of Financial Accounting Standard ('SFAS') No. 130, Reporting Comprehensive Income (Loss). Comprehensive income is defined as the total change in shareholders' equity during the period other than from transactions with shareholders, and for the Company, includes net income and cumulative translation adjustments.

Recent Accounting Pronouncements

In May 2005, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 154 – Accounting Changes and Error Corrections (SFAS 154), a replacement of Accounting Principles Board Opinion No. 20 (APB 20) and Statement No. 3 (SFAS 3), which previously addressed accounting changes. SFAS 154 establishes, unless impracticable, retrospective application as the required method for reporting a change in accounting principle in the absence of explicit transition requirements specific to the newly adopted accounting principle. SFAS 154 also provides guidance for determining whether retrospective application of a change in accounting principle is impracticable and for reporting a change when retrospective application is impracticable. SFAS 154 carries forward without change the guidance in APB 20 for reporting the correction of an error in previously issued financial statements. SFAS 154 will be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of this standard has not had a material impact on the Company's consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), 'Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109, Accounting for Income Taxes,' which clarifies the accounting for uncertainty in income taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation requires that the Company recognize in the financial statements, the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The provisions of FIN 48 are effective beginning January 1, 2007 with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company is currently evaluating the possible impact of FIN 48 on the Company's consolidated financial statements.

In September 2006, the Securities and Exchange Commission (SEC) released Staff Accounting Bulletin No. 108, 'Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements' (SAB 108). SAB 108 is applicable for the current year and provides guidance on how the effects of the carryover or reversal of prior year financial statement misstatements should be considered in quantifying a current year misstatement. Prior practice allowed the evaluation of materiality on the basis of (1) the error quantified as the amount by which the current year income statement was misstated (rollover method) or (2) the cumulative error quantified as the cumulative amount by which the current year balance sheet was misstated (iron curtain method). Reliance on either method in prior years could have resulted in misstatement of the financial statements. The guidance provided in SAB 108 requires both methods to be used in evaluating materiality. Immaterial prior year errors may be corrected with the first filing of prior year financial statements after adoption.

The cumulative effect of the correction would be reflected in the opening balance sheet with appropriate disclosure of the nature and amount of each individual error corrected in the cumulative adjustment, as well as a disclosure of the cause of the error and that the error had been deemed to be immaterial in the past. The adoption of SAB 108 did not have a material impact on the Company's consolidated financial statements.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, 'Fair Value Measurements' (SFAS No. 157). This Statement defines fair value as used in numerous accounting pronouncements, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands disclosure related to the use of fair value measures in financial statements. SFAS No. 157 does not expand the use of fair value measures in financial statements, but standardizes its definition and guidance in GAAP. The Standard emphasizes that fair value is a market-based measurement and not an entity-specific measurement based on an exchange transaction in which the entity sells an asset or transfers a liability (exit price). SFAS No. 157 establishes a fair value hierarchy from observable market data as the highest level to fair value based on an entity's own fair value assumptions as the lowest level. The Statement is to be effective for our financial statements issued in 2008; however, earlier application is encouraged. We believe that SFAS No. 157 will not have a material impact on the Company's consolidated financial statements.

In September 2006 the FASB also issued SFAS No. 158, 'Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R)'. SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. SFAS 158 also requires an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006. Because the Group does not have a defined benefit pension plan or other qualifying post retirement plan our adoption of SFAS No. 158 did not have a material effect on the Company's consolidated financial position or results of operations.

(4) Commitments and Contingent Liabilities

Operating Leases

In 2005, Universal Biosensors Pty Ltd entered a non-cancelable operating lease with respect to premises at Mount Waverly Victoria for warehouse and office premises for a term of two years and nine months with no renewal option. This lease expires in September 2007. Universal Biosensors Pty Ltd has recently entered into a lease with respect to premises at 1 Corporate Avenue, Rowville Victoria which commences on 1 April 2007 for an initial period of seven years and five months, with two options to renew the lease for successive five-year periods. The period during which there will be two leases held concurrently by Universal Biosensors Pty Ltd is viewed by management as necessary to ensure a smooth, undisrupted transition. Management therefore has not made provision for surplus lease space. The Group's bankers have issued a bank guarantee of $197,825 in relation to a rental bond to secure the payments under the lease. This bank guarantee is secured by a security deposit held at the bank.

Future minimum lease payments under non-cancelable operating leases (with initial or remaining lease terms in excess of one year) as of December 31, 2006 are:

	$
2007	350,251
2008	360,834
2009	373,463
2010	386,534
2011 and thereafter	1,352,932
Total minimum lease payments	2,824,014

Rent expense was $126,506, $140,348, $159,756 and $592,518 for the fiscal years ended December 31, 2004, 2005 and 2006 and for the period from inception to December 31, 2006, respectively.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Government research grants

Universal Biosensors Pty Ltd has received an Australian Government research grant under the R&D START Program up to a maximum grant amount of $1,782,829 payable over the period from 1 January 2005 to 30 September 2007. The grant formally terminates on 30 September 2007, however Universal Biosensors Pty Ltd has submitted an application for the extension of the grant. The Government may or may not grant an extension. The Commonwealth of Australia may terminate the grant agreement for breach of the agreement by Universal Biosensors Pty Ltd, for failure to undertake the required research, if there is a change in control of Universal Biosensors Pty Ltd, or on the grounds of insolvency. In certain limited circumstances where Universal Biosensors Pty Ltd fails to use its best endeavors to commercialize the project within a reasonable time of completion or upon termination of the grant due to breach or insolvency, the Commonwealth of Australia may require Universal Biosensors Pty Ltd to repay some or all of the grant. The Company continues the development of the project funded by the START Program.

The Company believes that the likelihood of being required to repay grant funding is remote because the Company continues to act in good faith with respect to the grant. Research and development start grant advances of $283,470 (2005: $540,477) were received during 2006 and income of $436,015 (2005: $468,576, 2004: $0, and period from inception to December 31, 2006: $904,591) was recognized with $76,968 recorded as accrued income at December 31, 2006 ($76,510 recorded as deferred income at December 31, 2005).

On October 28, 2006, Universal Biosensors Pty Ltd was awarded a grant by the State of Victoria to support the establishment of a medical diagnostic manufacturing facility in Victoria, Australia for the manufacture of new technologies for disease monitoring and to increase support of local and export markets. These payments are subject to the achievement of milestones which include capital expenditure by Universal Biosensors Pty Ltd of predetermined minimum amounts. The State of Victoria may require Universal Biosensors Pty Ltd to refund any amounts paid under the grant together with interest should Universal Biosensors Pty Ltd commit a breach of its obligations under the grant agreement. The State of Victoria may also withhold, suspend, cancel or terminate any payment or payments upon a failure to comply with obligations or if Universal Biosensors Pty Ltd chooses not to proceed with these initiatives or it becomes insolvent. The total amount received under the Victorian State Government Grant at December 31, 2006 was $0 and no income has been recognized in relation to this agreement.

Government compliance costs

The Company has raised provisions totaling $330,787 in regards to certain government compliance costs. The Company is currently liaising with the relevant government authorities to finalize this matter.

This is management's best estimate of the likely outcome of these negotiations, however the final outcome may materially differ from the provision raised.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

(5) Income Taxes

The Company is subject to income tax in Australia and is required to pay taxes on its Australian profits. As provided under the Australian income tax laws, the Company and its wholly owned resident subsidiary have formed a tax-consolidated group.

A reconciliation of the (benefit) provision for income taxes with the amount computed by applying the Australian statutory company tax rate of 30% to the loss before income taxes is as follows:

	Period from inception to December 31, 2006		Years ended December 31, 2006		2005		2004	
	$	%	$	%	$	%	$	%
Loss before income taxes	(2,272,033)		(2,096,218)		(36,966)		(56,422)	
Computed by applying income tax rate of home jurisdiction	(681,610)	30	(628,865)	30	(11,090)	30	(16,927)	30
Research & development incentive	(206,019)	9	(206,019)	10	–	–	–	–
Disallowed expenses/(income)								
Share based payment	91,254	(4)	91,254	(4)	–	–	–	–
Other	(67,228)	3	13,393	(1)	3,631	(10)	(36,587)	65
Impact of translation from functional to reporting currencies	(28,249)	1	(36,633)	2	(5,354)	14	5,590	(10)
Change in valuation allowance	1,073,905	(47)	766,870	(37)	58,554	(158)	160,733	(285)
Adjustment in respect of current income tax of prior years	(66,209)	3	122,821	(6)	(45,741)	124	(112,809)	200
Income tax expense	115,844	(5)	122,821	(6)	–	–	–	–

Significant components of the Company's deferred tax assets are shown below:

	As of December 31, 2006	2005
	$	$
Deferred tax assets		
Operating loss carry forwards	1,001,394	252,485
Unamortized IPO cost	447,425	–
Depreciation and amortization	11,352	26,416
Employee entitlements	66,307	29,917
Other accruals	130,403	21,911
Total deferred tax assets	1,656,881	330,729
Valuation allowance for deferred tax assets	(1,656,881)	(330,729)
Net deferred tax asset	–	–

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting and tax purposes. A valuation allowance has been established, as realization of such assets is not more likely than not.

At December 31, 2006 the Company has $3,337,980 ($841,617 at December 31, 2005) of accumulated tax losses available for carry forward against future earnings, which under Australian tax laws do not expire but may not be available under certain circumstances.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

(6) Stock Option Plan

All share and option amounts from inception to December 31, 2006 have been retroactively adjusted to give effect to the share split described in note 11. In 2004, the Company adopted an employee option plan ('Plan'). Options may be granted pursuant to the Plan to any person considered by the board to be employed by the Group on a permanent basis (whether full time, part time or on a long term casual basis) and includes all directors. Each option gives the holder the right to subscribe for one share of common stock. The total number of options that may be issued under the Plan is such maximum amount permitted by law and the Listing Rules of ASX. The exercise price and any exercise conditions are determined by the board at the time of grant of the options. Any exercise conditions must be satisfied before the options vest and become capable of exercise. The options lapse on such date determined by the board at the time of grant or earlier in accordance with the Plan. Options granted to date have had a ten year term and generally vest in equal tranches over three years.

An optionholder is not permitted to participate in a bonus issue or new issue of securities in respect of an option held prior to the issue of shares to the optionholder pursuant to the exercise of an option. If Universal Biosensors changes the number of issued shares through or as a result of any consolidation, subdivision, or similar reconstruction of the issued capital of the Company, the total number of options and the exercise price of the options (as applicable) will likewise be adjusted. There were no stock options granted in 2005. There were 2,066,108 options granted in 2006.

In accordance with SFAS 123(R), the fair value of the option grants were estimated on the date of each grant using the Black-Scholes option pricing model. The assumptions for these grants were:

	Grant Date	
	2006	2004
Exercise Price	$0.33	$0.29
Share Price at Grant Date	$0.33	$0.29
Volatility	55%	40% – 45%
Expected Life	10 years	10 years
Risk Free Interest Rate	4.4%	4.65%
Fair value of Option	$0.23	$0.08

Stock option activity during the period indicated is as follows:

	Number of Shares	Weighted average exercise price $
Balance at January 1, 2004	–	–
Granted	2,076,982	0.29
Balance at December 31, 2004	2,076,982	0.29
Granted	–	–
Exercised	(79,745)	0.29
Forfeited	(152,240)	0.29
Expired	–	–
Balance at December 31, 2005	1,844,997	0.29
Granted	2,066,108	0.33
Exercised	–	
Forfeited	(90,618)	0.31
Expired	–	
Balance at December 31, 2006	3,820,487	0.31

At December 31, 2006, the number of options exercisable was 2,305,341 (2005: 1,207,042 and 2004: 663,329).

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

The following table represents information relating to stock options outstanding under the plans as of December 31, 2006 and 2005:

	Options Outstanding		Options exercisable
Exercise price	Shares	Weighted Average Remaining Life in Years	Shares
2006			
$0.33	2,011,736	9.1	532,838
$0.29	1,808,751	7.0	1,772,503
2005			
$0.29	1,844,997	8.0	1,207,042

(7) Economic Dependency

The Company has entered the following agreements with LifeScan.

LifeScan License and Research and Development Agreement

Since April 2002 the Company has undertaken contracted research and development activities for LifeScan pursuant to a Development and Research Agreement. The Development and Research Agreement has historically been an important source of revenue for the Company. If the Development and Research Agreement was terminated there would be a loss of revenue but at the same time costs expended under the contract would also reduce. Management believe that loss of the agreement per se would no longer have a material adverse effect on the Company. The Company also currently holds a license from LifeScan to a range of patents, patent applications and know-how, pursuant to a License Agreement. If the Company were to breach the License Agreement, which the Group does not intend to do, LifeScan might validly terminate the License Agreement. This would seriously restrict or eliminate the Company's development and commercialization activities.

In consideration for the rights, licenses and options granted under the Development and Research agreement, LifeScan made payments totaling $2,000,000 in 2006, $2,086,013 in 2005, $1,816,813 in 2004 and $7,652,826 for the period from inception to December 31, 2006.

(8) Related Party Transactions

Details of related party transactions material to the operations of the Group other than compensation arrangements, expense allowances, and other similar items in the ordinary course of business, are set out below:

Johnson & Johnson Development Corporation, a wholly owned subsidiary of Johnson and Johnson, owns approximately 14% of the Company's shares.

LifeScan, a wholly owned subsidiary of Johnson & Johnson, makes payments to the Company through a research and development agreement. The terms of the agreement are mentioned in note 7.

Denis Hanley, Andrew Denver, Colin Adam and Charles Kiefel are shareholders and directors of the Company and of The Principals Funds Management Pty Ltd, which was paid a total of $325,000 in 2006 from the Company in connection with capital raising services. The Principals Funds Management Pty Ltd was paid a firm commitment fee of $79,118 by the underwriter of the Company's initial public offering in connection with firm commitments to subscribe for shares.

Andrew Jane is a director of the Company and is a Partner of CM Capital Investments Pty Ltd and is taken to be associated with CM Capital Investments Pty Ltd, CM Capital Venture Trust No. 3, CIBC Australia VC Fund LLC and Australia Venture Capital Fund LP who are shareholders of the Company. 135,000 shares were transferred to CM Capital Investments Pty Ltd by the underwriter of the Company's initial public offering as a commitment fees as a result of CM Capital Investments Pty Ltd subscribing for shares in connection with the initial public offering in Australia.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

Dr Jane Wilson is a shareholder and director of Universal Biosensors, Inc. The spouse of Dr Wilson is a substantial shareholder and officer of the parent company of Wilson HTM Corporate Finance Limited, the underwriters and lead managers of the Company's Australian initial public offering. The transaction with Wilson HTM Corporate Finance Limited is not considered a related party as Dr Wilson accepted the appointment as a director of the Company subsequent to Wilson HTM Corporate Finance Limited accepting their engagement.

(9) Property, Plant and Equipment

	As of December 31,	
	2006	2005
	$	$
Plant and equipment	2,170,549	1,783,901
Leasehold improvements	192,724	158,226
Capital work in process	4,339,007	–
	6,702,280	1,942,127
Accumulated depreciation	(1,034,745)	(693,366)
Property, plant & equipment, net	5,667,535	1,248,761

Depreciation expense was $200,944, $228,103, $231,613 and $890,451 for the fiscal years ended December 31, 2004, 2005 and 2006 and for the period from inception to December 31, 2006, respectively.

(10) Accrued Expenses

Accrued expenses consist of the following:

	As of December 31,	
	2006	2005
	$	$
Legal, tax and accounting fees	265,086	26,692
Goods & services tax	218,399	–
Salary related on-costs	120,252	88,042
Other	9,755	–
	613,492	114,734

(11) Stockholders' Equity - Common Stock

In fiscal year 2006, in connection with an initial public offering in Australia in the form of an offer of new shares of common stock in the capital of the Company ('Public Offer') and a concurrent separate offer of shares of common stock in the US to certain US Persons (as that term is defined in Regulation S promulgated under the US Securities Act of 1933) ('US Private Placement'), shareholders approved a) the conversion of all Series A preferred stock into common stock; b) the adoption of a new certificate of incorporation which was filed with the State of Delaware on December 5, 2006; c) a subdivision of existing common stock by 3,624.7518771; and d) an issue and allotment of common stock to subscribers under the Public Offer and US Private Placement.

As noted in note 12, during fiscal year 2006 the Company also issued 30,176,036 Series A convertible preferred stock in 2 separate private placements to institutional and sophisticated investors in both the US and Australia. This preference stock was subsequently converted into common stock on December 6, 2006. Before the stock split by 3,624.7518771, the Company had on issue 12,032 shares of common stock and 11,142 Series A convertible preferred stock. After the conversion of all Series A preferred stock into shares of common stock, there were 23,174 shares of common stock on issue. Immediately following the subdivision on December 6, 2006, there were 83,999,976 shares on issue. All share and per share amounts from the period from inception to December 31, 2006 presented in the accompanying financial statements have been retroactively adjusted to give effect to the stock split.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

The Company completed its Public Offer of 36,000,000 shares of common stock and concurrent US Private Placement of 8,000,000 shares in the US to institutional and accredited investors, raising A$22 million in aggregate before costs. The Company listed on ASX on December 13, 2006.

Holders of common stock are generally entitled to one vote per share held on all matters submitted to a vote of the holders of common stock. At any meeting of the shareholders, the presence, in person or by proxy, of the majority of the outstanding stock entitled to vote shall constitute a quorum. Except where a greater percentage is required by the Company's Amended and Restated Certificate of Incorporation or By-laws, the affirmative vote of the holders of a majority of the shares of common stock then represented at the meeting and entitled to vote at the meeting shall be sufficient to pass a resolution. Holders of common stock are not entitled to cumulative voting rights with respect to the election of directors, and the common stock does not have pre-emptive rights.

Trading in our shares of common stock on ASX is undertaken using CHESS Depositary Interests ('CDIs'). Each CDI represents beneficial ownership in one underlying share. Legal title to the shares underlying CDIs is held by CHESS Depositary Nominees Pty Ltd ('CDN'), a wholly owned subsidiary of ASX.

Holders of CDIs have the same economic benefits of holding the shares, such as dividends (if any), bonus issues or rights issues as though they were holders of the legal title. Holders of CDIs are not permitted to vote but are entitled to direct CDN how to vote. Subject to Delaware General Corporation Law, dividends may be declared by the Board and holders of common stock may be entitled to participate in such dividends from time to time.

(12) Convertible preference shares

Up until the time of the Company's Australian initial public offering, the Company had on issue 40,386,962 Series A convertible preference shares. The Company issued 30,176,036 Series A convertible preferred stock on June 15, 2006 and August 30, 2006, raising a total of US$ 9,990,000 before costs associated with the issues. Immediately prior to the issue of shares in connection with the Public Offer and the U.S. Private Placement, all the Company's convertible preference shares were converted into common stock (refer note 11).

The rights and obligations attaching to the Series A preferred stock were derived by a combination of an Investor Rights Agreement (which was terminated in connection with the close of the Public Offer), the By-laws and Amended and Restated Certificate of Incorporation of the Company. Without limitation, the terms of issue of the Series A Preferred Stock were as follows:

- the right to receive notices of general meetings and to attend and vote at general meetings of the Company;
- each preferred share entitled the stockholder to such number of votes at a general meeting equal to the number of shares of common stock that the preferred stock would have converted into (whether or not it had been converted);
- rights of conversion into common stock;
- may participate in dividends declared in respect of that class of share at the discretion of the Board, the rights to which may not be similar to the rights of the holders of common stock;
- anti-dilution protection in certain circumstances; and
- a liquidation preference over common stockholders in the event of liquidation or a capital reduction of the Company.

The Series A convertible preference shares were convertible by the holders into shares of common stock at any time or could be compulsorily converted at the time of an initial public offering, subject to certain conditions. The conversion ratio was one share of common stock per convertible preference share, subject to variation for capital reconstructions and share dilutions.

In the event of a return of assets on liquidation or capital reduction or otherwise, the assets of the Company remaining after payment of its liabilities were applied first in paying the preferred stockholders an amount equal to the issue price of such preferred stock adjusted as necessary for capital reconstructions and secondly, to the common stockholders an amount equal to the relevant issue price. Thirdly an amount per preferred share equal to the amount of interest that would have accrued on the amount subscribed for by the preference stockholder if interest had accrued daily at a rate of 10% per annum from the date of issue. Finally, the balance of assets remaining (if any) was to have been distributed among the holders of preferred and common stock pari passu as if they constituted one class of shares.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

(13) Retirement Benefits

As required by Australian law, Universal Biosensors Pty Ltd contributes to standard defined contributions superannuation funds on behalf of all employees at an amount up to nine percent of employee salary. The Company permits employees to choose the superannuation fund into which the contributions are paid, provided the fund is appropriately registered.

Universal Biosensors Pty Ltd contributed $83,485, $127,487 and $222,500, and $498,476 for the fiscal years ended December 31, 2004, 2005 and 2006, and the period from inception to December 31, 2006, respectively.

(14) Net Loss per Share

Basic net loss per ordinary share was computed by dividing the net loss applicable to common stock by the weighted-average number of common stock outstanding during the period. All periods presented in the financial statements have been retroactively adjusted to give effect to the share split described in note 11. Options granted to employees under the Universal Biosensors Employee Option Plan and the convertible preference shares on issue during the current and prior periods are considered to be potential ordinary shares for the purpose of calculating diluted net loss per share. However, all these were not included in the calculation of diluted net loss per share as the effect of including them is anti-dilutive.

	Period from inception to	Years ended December 31,		
	December 31, 2006	2006	2005	2004
Weighted average number of ordinary shares used as denominator in calculating basic and diluted net loss per share	43,050,568	49,408,822	45,573,580	43,533,269

(15) Guarantees and Indemnifications

The certificate of incorporation and amended and restated by-laws of the Company provide that the Company will indemnify officers and directors and former officers and directors in certain circumstances, including for expenses, judgments, fines and settlement amounts incurred by them in connection with their services as an officer or director of the Company or its subsidiaries, provided that such person acted in good faith and in a manner such person reasonably believed to be in the best interests of the Company.

In addition to the indemnities provided in the certificate of incorporation and amended and restated by-laws, the Company has entered into indemnification agreements with certain of its officers and each of its directors. Subject to the relevant limitations imposed by applicable law, the indemnification agreements, among other things:

- indemnify the relevant officers and directors for certain expenses, judgments, fines and settlement amounts incurred by them in connection with their services as an officer or director of the Company or its subsidiaries; and
- require the Company to make a good faith determination whether or not it is practicable to maintain liability insurance for officers and directors or to ensure the Company's performance of its indemnification obligations under the agreements.

No liability has arisen under these indemnities as at December 31, 2006.

Notes to Financial Statements

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

(16) Segments

The Company operates in one segment. The principal activities of the Company are the research, development, manufacture and commercialization of a range of in vitro diagnostic tests for point-of-care use.

The Company operates predominantly in one geographical area, being Australia.

(17) Subsequent Events

On March 28, 2007 the Company announced that, subsequent to a review of employee and director performance for the year ended December 31, 2006, the directors granted 845,000 employee options under the Universal Biosensors Employee Option Plan. Included within this grant are 45,000 employee options granted to the Managing Director of the Company which requires shareholder approval prior to formal grant of those options.

The Company has recently entered into a lease with respect to premises at 1 Corporate Avenue, Rowville Victoria which commences on 1 April 2007 for an initial period of seven years and five months, with two options to renew the lease for successive five-year periods. The Company is aware of the proposed sale of 1 Corporate Avenue property to an interested third party. Management has entered into discussions with the third party to undertake the fit out of 1 Corporate Avenue premises at the third party's own cost which would have otherwise been borne by Universal Biosensors and estimated to be $3.7 million. It is likely the term of the lease will be extended to 10 years. Management has entered into these discussions aware that whilst it will result in increased rental payment, it will free up the cash flow which will then be utilized to fund the Company's core activities which management believes will provide greater returns. Upon the successful negotiation of these discussions and the subsequent signing of a lease agreement, the future minimum lease payments under non-cancellable operating leases (with initial or remaining lease terms in excess of one year) as of December 31, 2006 will be:

	$
2007	877,174
2008	887,757
2009	900,386
2010	913,457
2011 and thereafter	6,596,992
Total minimum lease payments	10,175,766

Other than as disclosed above, there has not arisen in the interval between the end of the financial year and March 30, 2007 any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Company, the results of those operations, or the state of affairs of the Company in future financial years.

Schedule ii – Valuation and Qualifying Accounts

(for the years ended December 31, 2004, 2005 and 2006 and for the period from inception (September 14, 2001) to December 31, 2006)

		Additions			
	Balance at Beginning of Period	Charged to Costs and Expenses	Charged to Other Accounts	Deductions	Balance at end of Period
	$	$	$	$	$
Description at Period from inception to December 31, 2003					
Deferred income tax valuation allowance	–	111,442	–	–	111,442
Year ended December 31, 2004					
Deferred income tax valuation allowance	111,442	160,733	–	–	272,175
Year ended December 31, 2005					
Deferred income tax valuation allowance	272,175	58,554	–	–	330,729
Year ended December 31, 2006					
Deferred income tax valuation allowance	330,729	766,871	559,281	–	1,656,881
Period from inception to December 31, 2006					
Deferred income tax valuation allowance	–	1,097,600	559,281	–	1,656,881

Additional Financial Information

The financial information provided in the following pages, consisting of the Balance Sheets and Statements of Operations are presented in the Australian currency using a convenience translation of 0.7913 (spot rate for the 2006 financial year).

A breakdown of total expenses is also attached as Schedule 1.

Balance Sheets	As of December 31, 2006 A$*	As of December 31, 2006 US$
ASSETS		
Current assets:		
Cash	30,184,756	23,885,198
Accrued income	97,267	76,968
Other current assets	532,534	421,394
Total current assets	30,814,557	24,383,560
Property, plant, and equipment - net	7,162,309	5,667,535
Total assets	37,976,866	30,051,095
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	1,550,333	1,226,779
Income taxes payable	163,000	128,982
Accrued expenses	775,296	613,492
Deferred income	–	–
Employee entitlements provision	141,149	111,691
Total current liabilities	2,629,778	2,080,944
Non-current liabilities:		
Employee entitlements provision	70,045	55,426
Total non-current liabilities	70,045	55,426
Total liabilities	2,699,823	2,136,370
Commitments and contingencies		
Stockholders' equity:		
Preferred stock	–	–
Common stock	16,176	12,800
Additional paid-in capital	38,094,336	30,144,048
Deficit accumulated during the development stage	(3,017,664)	(2,387,877)
Accumulated other comprehensive income	184,195	145,754
Total stockholders' equity	35,277,043	27,914,725
Total liabilities and stockholders' equity	37,976,866	30,051,095

* Refer note above for basis of calculation.

Additional Financial Information

Statements of Operations

	Year ended As of December 31, 2006 A$*	Year ended As of December 31, 2006 US$
Revenue	–	–
Cost of goods sold	–	–
Gross profit	–	–
Operating expenses:		
Research and development	3,121,409	2,469,971
General and administrative	2,135,631	1,689,925
Fair value of stock options issued to employees related to:		
Research and development	134,542	106,463
General and administrative	249,864	197,717
Total operating expenses	5,641,446	4,464,076
Research and development income	2,527,486	2,000,000
Loss from operations	(3,113,960)	(2,464,076)
Interest and other income	464,878	367,858
Net loss before tax	(2,649,082)	(2,096,218)
Income tax expense	(155,214)	(122,821)
Net loss	(2,804,296)	(2,219,039)

* Refer page 46 for basis of calculation

Additional Financial Information — Schedule 1

Consolidated Research and Development and Administrative Expenses (U.S. dollars)

	Period from inception (September 14, 2001 to December 31, 2006)	Years ended December 31, 2006	2005	2004
	$	$	$	$
Research and development and administrative expenses:				
Employee expenses	6,053,338	2,458,015	1,548,740	1,165,668
Government grants	(904,591)	(436,015)	(468,576)	–
Material and design costs	1,160,042	510,003	251,777	131,491
Depreciation and amortization	890,451	231,613	228,103	200,944
Rent	592,518	159,756	140,348	126,506
Legal fees	366,789	152,981	106,745	49,050
Travel and related expenses	398,596	192,861	102,925	42,401
Consulting and professional fees	753,839	467,297	120,552	107,625
Other	634,215	408,563	91,102	57,027
Auditors' remuneration	204,707	121,493	32,171	12,531
Freight	125,574	46,675	47,751	20,178
Gas and electricity	82,190	26,070	21,150	13,664
Telephone and facsimile	73,446	29,240	20,278	11,534
Stationery and supplies	78,849	38,500	19,775	8,400
Insurance	80,142	23,290	15,669	14,484
Repairs and maintenance	52,071	28,179	14,721	910
Bank charges	9,067	5,555	1,634	766
	10,651,243	4,464,076	2,294,865	1,963,179

ASX Additional Information

Additional information required by Australian Securities Exchange Ltd and not shown elsewhere in this report is as follows. The information is current as at March 26, 2007.

(a) Distribution of equity securities

As at 26 March 2007 there were:

- 128,086,971 fully paid shares of common stock held by 828 individual shareholders. All issued shares of common carry one vote per share and carry the rights to dividends.
- 4,533,508 options over shares of common stock held by 22 individual option holders. The Board has also approved the grant of a further 45,000 employee options over shares of common stock to the Managing Director of the Company, subject to receipt of necessary shareholder approval.

The Company's shares of common stock are traded on Australian Securities Exchange in the form of CHESS Depositary Interests, or CDIs. CHESS Depositary Nominees Pty Ltd, a wholly owned subsidiary of Australian Securities Exchange Ltd, holds legal title in the Company's shares of common stock on behalf of holders of CDIs. The following table sets out the beneficial interests in the underlying shares of common stock rather than legal title.

Holding ranges	Beneficial interests in shares of common stock	Options over shares of common stock
1 – 1,000	49	0
1,001 – 5,000	101	0
5,001 – 10,000	156	0
10,001 – 100,000	425	17
100,001 – and over	97	11
	828	28

There are 4 holders of CDIs with a less than marketable parcel.

(b) Substantial shareholders

	Notified interests in shares of common stock	
Name	Number	Percentage
The Principals Cornerstone Fund Pty Limited*	28,698,066	22.42
Johnson & Johnson Development Corporation	18,231,729	14.234
CM Capital Investments Pty Ltd**	15,196,879	11.86
Kaasim Pty Ltd	7,840,338	6.121

* Includes relevant interests of Messrs Denver, Hanley, Kiefel and Dr Adam. For details of their shareholdings, refer to the Directors' Report.

** Includes relevant interest of CIBC Australia VC Fund LLC. For details of their shareholdings, refer to the Directors' Report.

ASX Additional Information

(c) Twenty largest holders of quoted equity securities

Name	Beneficial interests in shares of common stock Number	Percentage
1. The Principals Cornerstone Fund Pty Limited	22,651,074	17.684
2. Johnson & Johnson Development Corporation	18,231,729	14.234
3. CM Capital Investments Pty Ltd	11,553,767	9.020
4. Kaasim Pty Ltd	7,840,338	6.121
5. CIBC Australia VC Fund LLC	3,508,112	2.739
6. Litster & Associates Pty Ltd	3,255,469	2.542
7. Mr Alastair Hodges	3,048,416	2.380
8. Equity Trustees Limited	2,708,000	2.114
9. National Nominees	2,503,000	1.954
10. Mr Denis Hanley	2,113,230	1.650
11. Megreg Holdings Pty Ltd	1,781,305	1.391
12. Mr Garry Chambers	1,750,755	1.367
13. Mr Ronald Chatelier	1,497,022	1.169
14. Mrs Lynne Carol Beck	1,449,900	1.132
15. Mr Andrew Leslie Denver	1,087,425	0.849
16. Mr Thomas William Beck & Mrs Lynne Carol Beck	1,025,804	0.801
17. Dr Elizabeth (Jane) Wilson	1,000,000	0.781
18. Mr Christopher J La Croix & Mrs Kathleen M La Croix	954,587	0.745
19. Mr Andrew L Denver & Mrs Linda Denver	909,812	0.710
20. Sayers Investments (ACT) Pty Limited	776,928	0.607
	89,646,673	82.335
	128,086,971	

(d) Restricted Securities

	Shares	Options
Securities subject to mandatory escrow ending on:		
– June 14, 2007	418,804	–
– August 29, 2007	2,893,408	–
– December 12, 2008	27,189,052	960,560

In addition, 37,262,581 share of common stock are subject to voluntary escrow until December 6, 2007.

(e) Use of funds

For the period from admission on the Australian Securities Exchange until the date of this report, the Company has used the cash and cash equivalents it had at the time of admission in a manner that is consistent with its business objectives.

Corporate Directory

Board of Directors

Mr Andrew Denver
Mr Mark Morrisson
Dr Colin Adam
Mr Denis Hanley
Mr Andrew Jane
Mr Charles Kiefel
Dr Elizabeth (Jane) Wilson

Registered Office in Australia

103 Ricketts Road
Mount Waverley VIC 3149
Australia
Telephone: + 61 3 8542 9000
Fax: + 61 3 9543 6490
Email: info@universalbiosensors.com
Web: www.universalbiosensors.com

Registered Agent in the US

Corporation Service Company
2711 Centerville Road, Suite 400,
Wilmington, County of New Castle
Delaware, Unites States of America

Share Registry

Registries Limited
Level 2
28 Margaret Street
Sydney NSW 2000
Australia
Telephone: + 61 2 9290 9600
Fax: +61 2 9279 0664
Email: registries@registries.com.au
Web: www.registries.com.au

Independent Accountant and Auditor

PricewaterhouseCoopers LLP
Freshwater Place
2 Southbank Boulevard
Southbank VIC 3006
Australia

Australian Legal Adviser

PFM Legal Pty Ltd
Level 12
117 York Street
Sydney NSW 2000
Australia

US Legal Adviser

Venable LLP
575 7th Street, NW
Washington DC 20004
United States of America

Australian Patent Attorneys

Griffith Hack
Level 3
509 St Kilda Road
Melbourne VIC 3004
Australia

ASX Code

UBI

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