

***Nexus Bonds Limited***

(formerly known as Select Access Investments No. 3 Limited)

ABN 23 101 744 389

**Interim financial report for the half-year ended  
31 December 2005**

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## ***Nexus Bonds Limited*** **Directors' report**

The directors present their report together with the financial report of Nexus Bonds Limited ("the Company") for the half-year ended 31 December 2005 and the auditor's report thereon.

### **Directors**

The directors of the Company at any time during or since the end of the financial year are:

| <b>Name and Qualifications</b> | <b>Experience and special responsibilities</b>   |
|--------------------------------|--|
| Mr Richard J Nettleton<br>LLB  | A solicitor with over 40 years legal experience. A director of a number of companies including JPMorgan Trust Australia Limited and Marathon Asset Management (Australia) Limited. Director since 19 August 2002.  |
| Mr Douglas W O'Neill           | A corporate finance specialist with 35 years industry experience and has been involved in over 150 stock market takeovers. Director since 19 August 2002.  |
| Mr Stephen J Treanor           | A financial consultant who has advised numerous corporations on debt financing alternatives and risk management. He has extensive expertise in the securitisation of financial assets and is a director of several associated special funding corporations. In addition to a lengthy career in commercial banking in the United States he worked for Moody's Investors Service until 1993 where he held various roles including managing director of its Australasian operations. Director since 19 August 2002. |

### **Principal activities**

The principal activities of the Company from its establishment on 19 August 2002 has been the issuance of portfolio linked notes (ie. notes linked to the creditworthiness of a number of Australian and International Companies), the placement of note proceeds on deposit, and the entering into portfolio agreements.

There have been no significant changes in the nature of the activities of the Company since establishment. There have been no note issuances or changes in investments during the half-year.

### **Review and result of operations**

The profit from ordinary activities after income tax amounted to \$1,970 (Half-year 2004: \$2,573).

There has been no significant impact on the financial position or performance of the company as a result of the change in the accounting policy for financial instruments, upon implementation of Australian equivalents to International Financial Reporting Standards ('AFIRS'). The accounting policy for financial instruments was changed from 1 July 2005 upon adoption of AASB 139 Financial Instruments: Recognition and Measurement. The implementation of the new accounting policy resulted in no net adjustment in retained earnings at 1 July 2005.

However, the application of AIFRS has resulted in significant changes to the presentation of the financial results of the company, which are explained below.

## ***Nexus Bonds Limited*** **Directors' report**

### **Review and result of operations (continued)**

#### Derivatives

Derivatives that were previously measured on an accrual basis, have been measured at fair value. Derivatives consist solely of portfolio agreements, which may also be referred to interchangeably as portfolio credit default swaps. The fair value of derivative assets was \$8,049,000 at 1 July 2005 and \$7,281,000 at 31 December 2005.

Credit derivatives are classified as trading instruments and must now be recognised at fair value with subsequent changes in fair value recognised directly in profit or loss.

#### Embedded derivatives

The revised accounting policy requires that financial instruments that contain features that can modify the cash flows of those contracts in a similar way to a derivative contract, such as the notes issued by the Company which contain a feature that is similar to a financial guarantee or credit derivative, are required to be split into two parts reflecting the embedded derivative feature and a host debt instrument. The counterparty to the embedded derivative are the note holders.

The embedded derivatives are subsequently measured at fair value and the notes are subsequently recognized at amortised cost, less amounts allocated to the fair value of the embedded derivative.

The fair value of derivative liabilities that were recognized separately from the notes as a result of this change in accounting policy was \$(8,049,000) at 1 July 2005 and \$(7,281,000) at 31 December 2005. As the company is economically hedged, the adjustments to separately recognise the derivative and embedded derivative positions at their fair value are fully offset against each other at the date of transition to AIFRS and at the end of the reporting period.

#### Derivative revenue

Previously the premium receivable from portfolio agreement counterparties was presented in the Income statement as Derivative revenue. Derivative premium is now treated as a realized gain on derivatives and is presented within a new Income statement line item: Net trading income. Derivative premium of \$4,542,000 was included in Net trading income in the half-year period. Correspondingly, there was no Derivative revenue recognised for the current reporting period.

The separate recognition of the derivatives embedded in the notes requires that derivative premium be imputed and included in Net trading income. Imputed derivative premium of \$(4,542,000) was included in Net trading income in the half-year period.

#### Financial instruments at fair value

The credit linked deposit and related Nexus 4 Topaz Notes (NXHBD) have been designated as financial instruments at fair value through profit and loss, which is the alternative accounting treatment to separating out embedded derivative and a host debt instrument. These instruments are recognised at fair value with subsequent changes in fair value recognised directly in profit and loss as Net trading income.

## ***Nexus Bonds Limited*** **Directors' report**

### **Review and result of operations (continued)**

#### Net trading income

No Net trading income has been recognized for financial instruments at fair value through profit and loss during the period as the reduction in the fair value of the credit linked deposit of \$(1,229,000) was fully offset by a reduction in the fair value of the Nexus 4 Topaz Notes of \$1,229,000.

The change in fair value of derivatives, including derivative premium, during the period of \$3,774,000 is recognised immediately in the Income statement as Net trading income. No Net trading income has been recognized for derivatives in the half-year as the change in fair value of the portfolio agreements, including derivative premium, is fully offset by the change in fair value of the embedded derivatives that have been recognized separately of \$(3,774,000).

#### Interest income

Interest income was significantly higher than the comparative period due to placement of funds raised through the issuances of two series of notes either during or subsequent to the comparative period.

#### Interest expense

Interest expense was \$4,542,000 lower than the amount that would have been recognised if interest expense was recognised on the same basis as the prior period, due to the exclusion of imputed derivative premium that is recognised in Net trading income.

#### Accrued interest balances

Accrued interest balances have been reclassified to form part of the carrying value of the related financial instrument from 1 July 2005. Previously accrued interest was recognised as either a receivable or payable. Correspondingly, the carrying values of the Company's Long term receivables and Interest-bearing liabilities have increased relative to the comparative period.

#### Deferred tax

Deferred tax assets and liabilities have been recognised in relation to the unrealised gain or loss recognised on derivatives and embedded derivatives. These balances have been netted to \$nil in accordance with the Company's accounting policies.

#### **Events subsequent to balance date**

On 3<sup>rd</sup> March 2006, a Portfolio Company in the Nexus 4 Topaz Notes Portfolio (NXHBD) filed for bankruptcy. This credit event has triggered a reduction in the future interest payments on those Notes, however, it has no impact on the repayment of the full principal amount of the Notes at their maturity date.

#### **Rounding of Amounts**

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial report and director's report have been rounded off to the nearest thousand dollars, unless otherwise stated.

*Nexus Bonds Limited*  
**Directors' report**

**Auditor's independence declaration**

A copy of the auditors' independence declaration is set out on page 6 and forms part of the Directors' report for the half-year ended 31 December 2005.

Dated at Sydney this 14<sup>th</sup> day of March 2006.

Signed in accordance with a resolution of the directors:



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R J Nettleton  
*Chairman*



*Lead Auditor's Independence Declaration under Section 307C of the Corporation Act 2001*

To: the directors of Nexus Bonds Limited

I declare that, to the best of my knowledge and belief, in relation to the review for the half-year ended 31 December 2005, there have been:

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

A handwritten signature in black ink, appearing to read 'M.Ashcroft', written in a cursive style.

Malcolm Ashcroft  
*Partner*

Sydney

14<sup>th</sup> March 2006

*Nexus Bonds Limited*

**Income Statement**

For the half-year ended 31 December 2005

|   | Note | Half-year<br>2005<br>\$'000 | 2004<br>\$'000  |
|---|------|-----------------------------|-----------------|
| Interest income   | 2    | 7,415                       | 3,380           |
| Derivative revenue  | 2    | -                           | 4,033           |
| Net trading income  | 2    | -                           | -               |
| <b>Total Revenue</b>  |      | <u>7,415</u>                | <u>7,413</u>    |
| Interest expense  | 2    | (6,260)                     | (6,257)         |
| Administrative and other expenses   |      | <u>(1,152)</u>              | <u>(1,152)</u>  |
| <b>Profit before income tax</b>   |      | <u>3</u>                    | <u>4</u>        |
| Income tax expense  |      | <u>(1)</u>                  | <u>(1)</u>      |
| <b>Profit for the half-year attributable to members of<br/><i>Nexus Bonds Limited</i></b> |      | <u><u>2</u></u>             | <u><u>3</u></u> |

The above income statement should be read in conjunction with the accompanying notes set out on pages 11 to 23.

***Nexus Bonds Limited***  
**Balance Sheet**  
As at 31 December 2005

|   | Note | 31 December<br>2005<br>\$'000 | 30 June<br>2005<br>\$'000 |
|---|------|-------------------------------|---------------------------|
| <b>ASSETS</b>   |      |                               |                           |
| Cash and cash equivalents                                   | 3    | 236                           | 14                        |
| Trade receivables   | 4    | 268                           | 1,294                     |
| Derivative financial instruments                            | 5    | 7,281                         | -                         |
| Long term trade receivables                                 | 4    | 165,429                       | 244,000                   |
| Financial assets at fair value through profit and loss      | 6    | <u>78,605</u>                 | <u>-</u>                  |
| <b>Total assets</b>   |      | <u><b>251,819</b></u>         | <u>245,308</u>            |
| <b>LIABILITIES</b>  |      |                               |                           |
| Trade and other payables                                    | 7    | 561                           | 1,237                     |
| Derivative financial instruments                            | 5    | 7,281                         | -                         |
| Current tax payable   |      | 1                             | 4                         |
| Interest-bearing liabilities                                | 8    | 165,302                       | 244,000                   |
| Financial liabilities at fair value through profit and loss | 9    | 78,605                        | -                         |
| Deferred tax liabilities                                    |      | <u>-</u>                      | <u>-</u>                  |
| <b>Total liabilities</b>                                    |      | <u><b>251,750</b></u>         | <u>245,241</u>            |
| <b>Net assets</b>   |      | <u><b>69</b></u>              | <u>67</u>                 |
| <b>EQUITY</b>   |      |                               |                           |
| Share capital   | 10   | -                             | -                         |
| Retained earnings   |      | <u>69</u>                     | <u>67</u>                 |
| <b>Total equity</b>   |      | <u><b>69</b></u>              | <u>67</u>                 |

The above balance sheet should be read in conjunction with the accompanying notes set out on pages 11 to 23.



***Nexus Bonds Limited***  
**Statement of changes in equity**  
For the half-year ended 31 December 2005

|  | Note  | Half-year      |                |
|--|-------|----------------|----------------|
|  |       | 2005<br>\$'000 | 2004<br>\$'000 |
| <b>Total equity at the beginning of the half-year</b>        |       | <u>67</u>      | <u>57</u>      |
| Adjustment on adoption of AASB 132 and AASB 139, net of tax: |       |                |                |
| Retained earnings  | 16(d) | <u>-</u>       | <u>-</u>       |
| <b>Net income recognized directly in equity</b>              |       | <u>-</u>       | <u>-</u>       |
| <b>Profit for the half-year</b>                              |       | <u>2</u>       | <u>3</u>       |
| <b>Total recognized income and expense for the year</b>      |       | <u>2</u>       | <u>3</u>       |
| <br>   |       |                |                |
| <b>Total equity at the end of the half-year</b>              |       | <u>69</u>      | <u>60</u>      |

The above statement of changes in equity should be read in conjunction with the accompanying notes set out on pages 11 to 23.

***Nexus Bonds Limited***

**Cash flow statement**

For the half-year ended 31 December 2005

|  |        | <b>Half-year</b> |                 |
|--|--------|------------------|-----------------|
|  | Note   | <b>2005</b>      | 2004            |
|  |        | <b>\$'000</b>    | <b>\$'000</b>   |
| <b>Cash flows from operating activities</b>                  |        |                  |                 |
| Cash payments in the course of operations                    |        | (933)            | (1,087)         |
| Interest received  |        | 6,987            | 3,271           |
| Derivative premium received                                  |        | 4,542            | 4,023           |
| Interest paid  |        | (10,374)         | (6,102)         |
| <b>Net cash inflow from operating activities</b>             | 12(ii) | <b>222</b>       | 105             |
| <b>Cash flows from financing activities</b>                  |        |                  |                 |
| Proceeds from note issuance                                  |        | -                | 35,000          |
| <b>Net cash inflow from financing activities</b>             |        | <b>-</b>         | <b>35,000</b>   |
| <b>Cash flows from investing activities</b>                  |        |                  |                 |
| Placement of funds on deposit                                |        | -                | (35,000)        |
| <b>Net cash (outflow) from investing activities</b>          |        | <b>-</b>         | <b>(35,000)</b> |
| <b>Net increase in cash and cash equivalents</b>             |        | <b>222</b>       | 105             |
| Cash and cash equivalents at the beginning of the half-year  |        | 14               | 350             |
| <b>Cash and cash equivalents at the end of the half-year</b> | 12(i)  | <b>236</b>       | 455             |

The above cash flow statement should be read in conjunction with the accompanying notes set out on pages 11 to 23.

***Nexus Bonds Limited***  
**Notes to the financial statements**  
31 December 2005

**1. Summary of significant accounting policies**

Nexus Bonds Limited (“the Company”) is a company domiciled in Australia. The interim financial report was authorised for issue by the Directors on 14th March 2006.

**(a) Statement of compliance**

This general purpose financial report for the interim half-year reporting period ended 31 December 2005 has been prepared in accordance with Accounting Standard AASB 134 Interim Financial Reporting and the Corporations Act 2001.

This interim financial report does not include all the notes of the type normally included in an annual financial report. Accordingly, this report is to be read in conjunction with the annual report for the year ended 30 June 2005 and any public announcements made by the Company during the half-year.

**(b) Basis of preparation of the half-year financial report**

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the periods presented unless otherwise stated. The financial report is presented in Australian dollars, which is the Company’s functional and presentation currency.

*Application of AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards (“AIFRS”):* This interim financial report is the first *Nexus Bonds Limited* interim financial report to be prepared in accordance with AIFRS’s. AASB 1 has been applied in preparing these financial statements. Early adoption: The Company has elected to apply the following accounting standards to the reporting period commencing 1 July 2005: AASB 2005-4 and AASB 2005-9.

Financial statements of the Company until 30 June 2005 had been prepared in accordance with previous Australian Generally Accepted Accounting Principles (“AGAAP”), which differs in certain respects from AIFRS. When preparing the Company’s interim financial report for the half-year ended 31 December 2005, management has amended certain accounting and valuation methods applied in the previous AGAAP financial statements to comply with AIFRS. With the exception of financial instruments, the comparative figures were restated to reflect these adjustments. The company has taken the exemption available under AASB 1 to only apply AASB 132 *Financial Instruments: Disclosure and Presentation* (“AASB132”) and AASB 139 *Financial Instruments: Recognition and Measurement* (“AASB139”) from 1 July 2005. An explanation of how the transition to AIFRS has affected the reported financial position, financial performance and cash flows of the consolidated entity and the company is provided in note 16.

*Nexus Bonds Limited*  
**Notes to the financial statements**  
31 December 2005

**1. Summary of significant accounting policies (continued)**

**(b) Basis of preparation of the half-year financial report (continued)**

The financial report has been prepared on the basis of historical costs except that derivative financial instruments and financial instruments designated at fair value through profit and loss are stated at their fair value.

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial report and Director's Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

The preparation of this financial report in conformity with AIFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. The areas involving a higher degree of judgement or complexity, or areas where assumption and estimates are significant to the financial report are the valuation of derivatives measured at fair value (refer to note 5).

**(c) Comparatives**

Certain comparative balances presented in the financial statements and notes, set out on pages 7 to 23, have been reclassified to conform to the current year presentation format.

**(d) Revenue recognition**

Revenues are recognised at fair value of the consideration received net of the amount of goods and services tax (GST).

Interest from interest-bearing assets and liabilities, including financial instruments designated at fair value through profit and loss, is recognised on an accrual basis over the life of the asset or liability based on the constant effective yield reflected in the terms of the contract.

*From 1 July 2004 to 30 June 2005*

Derivatives: Derivative revenue includes premiums received on portfolio agreements and is recognised as it accrues, taking into account the effective yield on the financial asset.

*From 1 July 2005*

Financial instruments at fair value through profit and loss: Net trading income comprises realised and unrealised gains and losses from derivatives and other financial instrument at fair value through profit and loss. Derivative premium is treated as realised gains and losses on derivatives.

*Nexus Bonds Limited*  
**Notes to the financial statements**  
31 December 2005

**1. Summary of significant accounting policies (continued)**

**(e) Income Tax**

Income tax on the income statement for the periods presented comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

**(f) Cash and cash equivalents**

Cash includes cash on hand and at bank and short-term deposits at call.

**(g) Receivables**

Loans and receivables are initially recognised at fair value and subsequently measured at amortised cost less impairment losses.

**(h) Payables**

Payables include amounts to be paid in the future for goods or services received and are initially recognised and subsequently measured at cost.

**(i) Interest-bearing liabilities**

Interest-bearing liabilities are classified as other financial liabilities and are recognised initially at fair value, net of the fair value of embedded derivatives. Subsequent to initial recognition, they are stated at amortised cost with interest recognised as Interest expense, using the effective interest method.

*Nexus Bonds Limited*  
**Notes to the financial statements**  
31 December 2005

**1. Summary of significant accounting policies (continued)**

**(j) Financial instruments at fair value through profit and loss**

This category has two sub-categories: financial assets and liabilities held for trading and those designated at fair value through profit and loss at inception. Derivatives are categorised as held for trading unless they are designated as hedges.

*From 1 July 2004 to 30 June 2005*

The company has taken the exemption available under AASB 1 to apply AASB 132 and AASB 139 from 1 July 2005. The company has applied previous AGAAP in the comparative information on financial instruments within the scope of AASB 132 and AASB 139. Derivatives are accounted for on an accruals basis and with derivative premium receivable recognised as a receivable. Credit linked deposits and Nexus 4 Topaz Notes were recognised at amortised cost.

*Adjustments on transition date: 1 July 2005*

The nature of the main adjustments to make this information comply with AASB 132 and AASB 139 are that financial instruments at fair value through profit and loss, which include derivatives, are measured on a fair value basis. At the date of transition changes to the carrying amounts of instruments at fair value are taken to retained earnings.

*From 1 July 2005*

**(i) Financial assets at fair value through profit and loss**

The credit linked deposit designated at fair value through profit and loss is initially recognised at fair value. Subsequent to initial recognition, it is stated at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the Income Statement as Net trading income. Fair value is determined by reference to the market price of the related Nexus4 Topaz Notes, or the value determined by use of a pricing model if a quoted market price is not available, on the basis that it is an offsetting risk position.

**(ii) Financial liabilities at fair value through profit and loss**

The Nexus 4 Topaz Notes are designated at fair value through profit and loss and are recognised initially at fair value. Subsequent to initial recognition, they are stated at fair value with the gain or loss on re-measurement to fair value recognised immediately in the Income Statement as Net trading income. Fair value is calculated based on the mid price quoted on the ASX if an active market exists for the Note. If an active market does not exist, management establishes fair value by use of a valuation technique, such as a pricing model that incorporates market data and discounted cash flow techniques.

*Nexus Bonds Limited*  
**Notes to the financial statements**  
31 December 2005

**1. Summary of significant accounting policies (continued)**

**(j) Financial instruments at fair value through profit and loss (continued)**

**(iii) Derivatives**

The Company is exposed to credit risk from its activities of issuing portfolio agreements. The Company has not adopted hedge accounting under AIFRS. Therefore, all derivatives held for hedging purposes under previous AGAAP are accounted for as trading instruments.

Derivatives are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the Income Statement as Net trading income. Fair value is the estimated amount that the entity could receive or pay to terminate the swap at the Balance sheet date, using pricing models incorporating market data and discounted cash flow techniques.

The interest-bearing liabilities issued by the Company are determined to contain embedded derivatives that must be bifurcated and recognised at fair value if the instrument is not designated as a financial instrument at fair value through profit and loss. These derivatives may have a fair value of zero at the date of initiating the transaction. The change in fair value of bifurcated derivatives will substantially or fully offset the change in fair value of other derivatives transacted by the Company. The portion of any coupon payments made on interest-bearing liabilities that relate to an embedded derivative that has been recognised separately are included in the determination of the fair value of the derivative and therefore not recognised within interest expense.

**(k) Impairment**

The carrying amounts of the Company's assets are reviewed at each reporting date to determine whether there is any indication of impairment. Significant receivables are individually assessed for impairment. Impairment of receivables is not recognised until objective evidence is available that a loss event has occurred.

**(l) Accounting Period**

This half-year report has been prepared for the period from 1 July 2005 until 31 December 2005.

**(m) Administrative and other expenses**

Services fees arise under a Services Deed whereby a servicer has been appointed to administer the Company. The Services Deed includes the provision of general administrative support and assistance as well as the payment of various fees and expenses, including audit fees on behalf of the Company. These transactions are on normal commercial terms.



**Nexus Bonds Limited**  
**Notes to the financial statements**  
31 December 2005

**2. Profit from ordinary activities before income tax expense**

Profit from ordinary activities before income tax expense has been arrived at after crediting/(expensing) the following items:

|  |       | <b>Half-year<br/>2005<br/>\$'000</b> | <b>Half-year<br/>2004<br/>\$'000</b> |
|--|-------|--------------------------------------|--------------------------------------|
| Interest income                                  |       |                                      |                                      |
| - Cash   |       | 4                                    | 5                                    |
| - Loans – related party                          | (i)   | 7,411                                | 3,375                                |
|  |       | <u>7,415</u>                         | <u>3,380</u>                         |
| Derivative premium – related party               | (ii)  | -                                    | 4,033                                |
| Net trading income / (expense)                   |       |                                      |                                      |
| - Derivatives – related party                    | (ii)  | 3,774                                | -                                    |
| - Embedded derivatives                           | (iii) | (3,774)                              | -                                    |
| - Financial assets at fair value – related party | (iv)  | (1,229)                              | -                                    |
| - Financial liabilities at fair value            | (iv)  | 1,229                                | -                                    |
|  |       | <u>-</u>                             | <u>-</u>                             |
| Interest expense                                 |       |                                      |                                      |
| - Interest-bearing liabilities                   | (v)   | (6,260)                              | (6,257)                              |

Explanation of significant components of profit from ordinary activities before income tax expense:

- (i) Loans: Interest income consists of interest earned on deposits or loans to related parties. Interest income was significantly higher than the comparative period due to placement of funds raised through the issuance of two series of notes either during or subsequent to the comparative period.
- (ii) Derivatives: Derivative premium paid of \$4,542,000 and unrealised losses of (\$768,000) on portfolio agreements were recognised during the period as Net trading income. In the comparative period, derivative premium of \$4,033,000 was recognised as Derivative revenue.
- (iii) Embedded derivatives: Imputed derivative premium paid of (\$4,542,000) and unrealised gains of \$768,000 were recognised during the period. The loss recognised on embedded derivatives fully offsets the gain recognised on derivatives.
- (iv) The carrying value of credit linked deposits and related Nexus 4 Topaz Notes (NXHBD) that have been designated at fair value through profit and loss are both decreased by offsetting unrealised movements in fair value of \$1,229,000 consisting of the unrealised movement in fair value attributable to market price movements net of the increase in accrued interest of \$439,000 that is recognised in interest income or expense, respectively, in accordance with the Company's accounting policy.
- (v) Interest expense recognised on Interest-bearing liabilities is net of the portion of the coupon payable to note holders of (\$4,555,000) that relates to imputed derivative premium accrued on embedded derivative financial instruments that have been bifurcated and recognised separately. The total amount due to noteholders in relation to the current period, which includes interest expense of \$(6,260,000) and imputed derivative premium, is \$(10,815,000). This amount is significantly higher than the interest expense recognised in the comparative period of \$(6,257,000) due to the issuance of two series of notes during or subsequent to the comparative period.



***Nexus Bonds Limited***  
**Notes to the financial statements**  
31 December 2005

**3. Cash and cash equivalents**

|                 | <b>31 December<br/>2005<br/>\$'000</b> | 30 June<br>2005<br>\$'000 |
|-----------------|--|---------------------------|
| Current account | <b>236</b>                             | 14                        |

All cash assets are held with large banks which have an acceptable credit rating. The carrying value of cash assets approximates its fair value.

**4. Receivables**

**Trade receivables**

|  |            |       |
|--|------------|-------|
| Accrued interest – related party           | -          | 584   |
| Accrued derivative premium – related party | -          | 499   |
| Other debtors                              | <b>268</b> | 211   |
|  | <b>268</b> | 1,294 |

**Long term trade receivables**

|                       |                |         |
|-----------------------|----------------|---------|
| Loans – related party | <b>165,429</b> | 244,000 |
|-----------------------|----------------|---------|

The ultimate credit risk on the loans is Deutsche Bank AG. Credit linked deposit with principal value of \$79,000,000 has been reclassified as a financial asset at fair value through profit and loss from 1 July 2005 (refer Note 6)

**5. Derivative financial instruments**

|  |              |   |
|--|--------------|---|
| Portfolio credit default swaps – related party   | <b>7,281</b> | - |
| Portfolio credit default swaps – embedded derivatives separated from notes issued (refer note 8) – related party | <b>7,281</b> | - |

The Company has entered into a number of portfolio agreements, also referred to as portfolio credit default swaps, with Deutsche Bank AG which has exposed the Company to the creditworthiness of well known Australian and International companies ('reference entities') with investment grade credit ratings. The Company becomes obligated to make payments to the Counterparty in the event of one of the reference entities defaulting. The fair value of the portfolio agreements is determined by using pricing models incorporating market data and discounted cash flow techniques.

***Nexus Bonds Limited***  
**Notes to the financial statements**  
31 December 2005

**6. Financial assets at fair value through profit and loss**

|                                       | <b>31 December<br/>2005<br/>\$'000</b> | 30 June<br>2005<br>\$'000 |
|---------------------------------------|--|---------------------------|
| Credit linked deposit – related party | <b>78,605</b>                          | -                         |

The Company has entered into a credit linked deposit with Deutsche Bank AG which has exposed the Company to the creditworthiness of well known Australian and International companies ('reference entities') with investment grade credit ratings. Interest is receivable based on a floating interest rate which reflects changes in the credit market's view of the reference entities and changes in market interest rates.

**7. Trade and other payables**

|   |            |       |
|---|------------|-------|
| Accrued interest – related party        | -          | 959   |
| Accrued management fees – related party | <b>561</b> | 278   |
|   | <b>561</b> | 1,237 |

**8. Interest-bearing liabilities**

|              |                |         |
|--------------|----------------|---------|
| Notes issued | <b>165,302</b> | 244,000 |
|--------------|----------------|---------|

**Notes issued**

The Company has issued 4 series of notes:

- (1) Nexus Yield Bonds: Notes issued amounting to \$60,000,000 that are 5 year, interest-bearing securities paying interest at a fixed rate of 10.25% per annum semi-annually over their term and maturing on 4 December 2007;
- (2) Portfolio linked floating rate notes: Notes issued amounting to \$70,000,000 that are 6 year, interest-bearing securities paying interest at a floating rate of 3.25% over the 90 day Bank Bill Rate quarterly over their term and maturing on 16 December 2009;
- (3) Nexus 3 notes: Notes issued amounting to \$35,000,000 that are 6 year, interest-bearing securities paying interest at a floating rate of 2.75% over the 90 day Bank Bill Rate quarterly over their term and maturing on 14 December 2010

Nexus Topaz 4 Notes with principal value of \$79,000,000 have been reclassified as a financial liability at fair value through profit and loss from 1 July 2005 (refer Note 9)

The Company's ability to pay these enhanced returns are a result of Note-holders being exposed to the creditworthiness of a portfolio of Australian and international companies. Interest amounts and principal outstanding may be reduced if one or more of the above companies experiences a severe weakening in its financial position to the extent that its senior unsecured debt may not be repaid in full when due.

***Nexus Bonds Limited***  
**Notes to the financial statements**  
31 December 2005

**8. Interest-bearing liabilities (continued)**

For accounting purposes, the notes issued are deemed to contain an embedded derivative which is split out and accounted for separately, if the note is not designated at fair value through profit and loss (refer Notes 5 and 9). An embedded derivative is a feature that can modify the cash flows of that contract in a similar way to a derivative contract. The nature of the derivative that is split from the note issued is a credit derivative or financial guarantee with the same terms as the corresponding portfolio agreement.

Interest payments will generally be sourced from interest received from Deutsche Bank by the Company under Deposit Agreements and derivative premium receipts from Portfolio Agreements.

Each series of notes is legally segregated. Note-holders of one series have no claim to any assets of the Company in respect of any other series, including in the event of liquidation.

**9. Financial liabilities at fair value through profit and loss**

|   | <b>31 December<br/>2005<br/>\$'000</b> | 30 June<br>2005<br>\$'000 |
|---|--|---------------------------|
| Credit linked note – Nexus4 Topaz Notes | <b>78,605</b>                          | -                         |

Nexus Topaz 4 Notes: Notes issued amounting to \$79,000,000 that are 10 year, interest-bearing securities paying interest at a floating rate of 2.60% for the first period over the 180 day Bank Bill Rate. Thereafter interest is payable based on a floating interest rate which reflects changes in the credit market's view of companies in the portfolio as well as changes in the market interest rates. Maturing on 23 June 2015. These notes have been designated as financial liabilities at fair value through profit and loss. The notes and related credit linked deposit are managed and their performance monitored on a fair value basis (refer Note 6).

**10. Share capital**

|   | \$       | \$       |
|---|----------|----------|
| <b>Issued and paid-up share capital</b>                           |          |          |
| 1 ordinary share, fully paid                                      | <b>1</b> | <b>1</b> |
| There have been no movements in share capital since incorporation |          |          |

**11. Segment Information**

*Geographical segment*

The Company's operations are conducted solely in Australia.

*Business segment*

The Company operates solely in the financial services sector.

***Nexus Bonds Limited***  
**Notes to the financial statements**  
31 December 2005

**12. Notes to the Cash flow statement**

**(i) Reconciliation of cash**

For the purposes of the Cash flow statement, cash includes cash on hand and at bank and short-term deposits at call, net of outstanding bank overdrafts repayable on demand. Cash as at the end of the financial year as shown in the Cash flow statement is reconciled to the related items in the statement of financial position as follows:

|             | Half-year      |                |
|-------------|----------------|----------------|
|             | 2005<br>\$'000 | 2004<br>\$'000 |
| Cash assets | 236            | 455            |

**(ii) Reconciliation of profit from ordinary activities after income tax to net cash provided by operating activities**

|  |       |       |
|--|-------|-------|
| Profit from ordinary activities after tax  | 2     | 3     |
| <i>Changes in assets and liabilities:</i>  |       |       |
| Increase in interest receivable            | (164) | (109) |
| Increase in derivative premium receivable  | (12)  | (10)  |
| (Increase) / decrease in other receivables | (57)  | 40    |
| Increase in interest payable               | 174   | 155   |
| Increase in other payables                 | 282   | 43    |
| Decrease in current tax liabilities        | (3)   | (17)  |
| Net cash provided by operating activities  | 222   | 105   |

**13. Dividends**

No dividends were paid during the half-year.

**14. Taxation**

Income tax expense for the half-year presented is the expected tax payable on the taxable income for the half-year, calculated as the estimated average annual effective income tax rate applied to the profit before income tax for the half-year. Current tax for the current and prior periods is classified as a current liability to the extent that it is unpaid.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amounts of assets and liabilities, using the estimated average annual effective income tax rate for the half-year. The primary component of the entity's recognised deferred tax assets and liabilities include temporary differences related to the remeasurement of derivatives at fair value, which include the recognition of a deferred tax asset of \$nil at 1 July 2005 (refer note 16) and a reduction in deferred tax asset of \$nil during the half-year.

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***Nexus Bonds Limited***

**Notes to and forming part of the financial statements**

31 December 2005

**15. Related parties**

**Directors**

The names of each person holding the position of director of the Company during the financial year are Messrs RJ Nettleton, DW O'Neill and SJ Treanor. No director has entered into a material contract with the Company during the financial year.

**Transactions**

The Company has significant transactions and a management agreement with Deutsche Bank AG (Sydney). Balances with related parties are detailed in notes 4, 5, 6 and 7.

For the half-year ended 31 December 2005 the Company received from Deutsche Bank AG (Sydney) interest of \$7,411,000 and premiums under the portfolio agreements of \$4,555,000.

For the year ended 31 December 2005 the Company incurred expenses of \$1,152,000 in relation to a management fee for services provided to it by Deutsche Bank AG (Sydney). Of this amount, \$561,000 remains unpaid at period end.

**16. Explanation of transition to Australian equivalents to IFRSs**

As stated in significant accounting policies note 1(b), these are the first interim financial statement prepared in accordance with AIFRSs.

The policies set out in the Significant accounting policies section of this report have been applied in preparing the financial report for the half-year ended 31 December 2005 and the comparative information presented in these financial statements and in the preparation of an opening AIFRS balance sheet at 1 July 2004 (the Company's date of transition).

In preparing its opening AIFRS balance sheet, the Company has adjusted amounts reported previously in financial report prepared in accordance with its old basis of accounting (previous AGAAP). An explanation of how the transition from previous AGAAP to AIFRSs has affected the Company's financial position, financial performance and cash flows is set out as follows:

**(a) Reconciliation of equity reported under previous AGAAP to equity under AIFRSs**

The adoption of AIFRS has not resulted in any material adjustments to equity:

- At the end of the last reporting period under previous AGAAP: 30 June 2005
- At the end of the last half-year reporting period under previous AGAAP: 31 December 2004
- At the date of transition to AIFRS: 1 July 2004

*Nexus Bonds Limited*

**Notes to and forming part of the financial statements**

31 December 2005

**16. Explanation of transition to Australian equivalents to IFRSs (continued)**

**(b) Reconciliation of profit under previous AGAAP to profit under AIFRSs**

The adoption of AIFRS has not resulted in any material adjustments to profit:

- For the half-year ended 31 December 2004
- For the year ended 30 June 2005

**(c) Reconciliation of cash flow statements under previous AGAAP to cash flow statements under AIFRSs**

The adoption of AIFRS has not resulted in any material adjustments to the cash flow statements for any period.

**(d) Application of AASB 132 and AASB 139 prospectively from 1 July 2005**

The company has taken the exemption available under AASB 1 to apply AASB 132 and AASB 139 from 1 July 2005. The adjustments to reflect the first time application of these standards are reflected in the Statement of Changes in Equity and are reconciled below.

**Adjustment on adoption of AASB 132 and AASB 139 to retained earnings in the Statement of Changes in Equity:**

| Instrument   | 1 July 2005       |                   | Adjustment<br>before tax<br>(\$'000) | Transition<br>adjustment<br>to deferred<br>tax<br>(\$'000) | Transition<br>adjustment<br>to retained<br>earnings<br>(\$'000) |
|--|-------------------|-------------------|--------------------------------------|--|---|
|  | AGAAP<br>(\$'000) | AIFRS<br>(\$'000) |                                      |  |   |
| Trade receivables  | (i) 165,000       | 165,939           | 939                                  | (282)  | 657   |
| Derivative financial instruments                               | (ii) -            | 8,049             | 8,049                                | (2,415)  | 5,634   |
| Interest-bearing liabilities                                   | (i) (165,000)     | (165,814)         | (814)                                | 244  | (570)   |
| Financial assets at fair value<br>through profit and loss      | (iii) 79,000      | 79,395            | 395                                  | (119)  | 276   |
| Derivative financial instruments<br>- liabilities (bifurcated) | (iv) -            | (8,049)           | (8,049)                              | 2,415  | (5,634)   |
| Financial liabilities at fair value<br>through profit and loss | (iii) (79,000)    | (79,395)          | (395)                                | 119  | (276)   |
| Accrued interest receivable                                    | (i) 1,083         | -                 | (1,083)                              | 325  | (758)   |
| Accrued interest payable                                       | (i) (958)         | -                 | 958                                  | (287)  | 671   |
|  |                   |                   |                                      | -  | -   |

- (i) Accrued interest balances are reclassified to form part of the carrying value of the related financial instrument.
- (ii) Derivative financial instruments (portfolio credit default swaps) are recognised at their fair value.
- (iii) Credit linked deposits and the related Nexus4 Topaz Note of principal value \$79,000,000 are restated from amortised cost to their fair value.
- (iv) Embedded derivatives that are separated from financial liabilities (notes issued) and are recognised at their fair value.

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*Nexus Bonds Limited*

**Notes to and forming part of the financial statements**

31 December 2005

**17. Additional Information**

- Nexus Bonds Limited, is incorporated and domiciled in Australia.
- The registered office:  
Level 16  
Deutsche Bank Place  
126 Phillip Street  
Sydney NSW 2000
- The number of employees at year end was Nil.

**18. Events subsequent to balance date**

On 3<sup>rd</sup> March 2006, a Portfolio Company in the Nexus 4 Topaz Notes Portfolio filed for bankruptcy. This credit event has triggered a reduction in the future interest payments on those Notes, however, it has no impact on the repayment of the full principal amount of the Notes at their maturity date.

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***Nexus Bonds Limited***  
**Directors' declaration**

In the opinion of the directors of Nexus Bonds Limited ("the Company"):

- (a) the financial statements and notes, set out on pages 7 to 23 are in accordance with the Corporations Act 2001, including:
  - (i) giving a true and fair view of the financial position of the Company as at 31 December 2005 and of its performance, as represented by the results of its operations and its cash flows for the period ended on that date; and
  - (ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Dated at Sydney this 14<sup>th</sup> day of March 2006

Signed in accordance with a resolution of the directors:



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R J Nettleton  
*Chairman*





## **Independent review report to the members of Nexus Bonds Limited**

### ***Scope***

We have reviewed the financial report of Nexus Bonds Limited ("the Company") for the half-year ended 31 December 2005, consisting of the interim income statement, balance sheet, statement of changes equity, cash flow statement, accompanying notes and the directors' declaration set out on pages 7 to 24. The Company's directors are responsible for the financial report including the relevant reconciling information regarding adjustments required under the Australian Accounting Standard AASB 1 *First-Time Adoption of Australian equivalents to International Financial Reporting Standards*.

We have performed an independent review of the financial report in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that the financial report is not presented fairly in accordance with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and other mandatory financial reporting requirements in Australia and statutory requirements, so as to present a view which is consistent with our understanding of the Company's financial position, and performance as represented by the results of its operations and its cash flows and in order for the Company to lodge the financial report with the Australian Securities and Investments Commission.

Our review has been conducted in accordance with Australian Auditing Standards applicable to review engagements. A review is limited primarily to inquiries of company personnel and analytical procedures applied to the financial data. These procedures do not provide all the evidence that would be required in an audit, thus the level of assurance is less than given in an audit. We have not performed an audit and, accordingly, we do not express an audit opinion.

### ***Statement***

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Nexus Bonds Limited is not in accordance with:

- (a) the Corporations Act 2001, including:
  - i. giving a true and fair view of the Company's financial position as at 31 December 2005 and of its performance for the half-year ended on that date; and
  - ii. complying with Australian Accounting Standard AASB 134 *Interim Financial Reporting* and the Corporations Regulations 2001; and
- (b) other mandatory financial reporting requirements in Australia.

KPMG

KPMG

Malcolm Ashcroft  
*Partner*

Sydney, 14<sup>th</sup> March 2006