Half-Year Report of *Electro Optic Systems Holdings Limited* for the Half-Year Ended 30 June 2005

ACN 092 708 364

This Half-Year Report is provided to the Australian Stock Exchange (ASX) under ASX Listing Rule 4.2A.3.

Current Reporting Period:	Half year ended 30 June 2005
Previous Corresponding Period:	Half year ended 30 June 2004

Results for Announcement to the Market

Revenue and Net Profit/(Loss)

		Percentage Change %	Amount
Revenue from ordinary activities	up	93.5	To $14,667,671
Profit/(loss) from ordinary activities after tax attributable to members	down	220	To ($7,998,825)
Net profit/(loss) attributable to members	down	220	To ($7,998,825)

Dividends (Distributions)

	Amount per security	Franked amount per security
Final dividend	Nil¢	Nil¢
Interim dividend	Nil¢	Nil¢
Record date for determining entitlements to the dividend:		
• final dividend		N/A
• interim dividend		N/A

Brief Explanation of Revenue, Net Profit/(Loss) and Dividends (Distributions)

Refer to Directors' Report

Directors Report

The directors of Electro Optic Systems Holdings Limited submit herewith the financial report for the half-year ended 30 June 2005. In order to comply with the provisions of the Corporations Act 2001, the directors report as follows:

The names of the directors of the company during or since the end of the half year are:

Mr Fred Bart (Chairman)
Dr Ben Greene (Chief Executive Officer)
Dr Bob Dean (Chief Executive Officer - EOST)
Mr Ian Alistair Dennis
Ms Cheryl Bart
Mr John Gordon
Mr Mark Ureda (Appointed 28 April 2005)

Review of Operations

The consolidated entity continues to operate in the space systems and defence sectors.

The Company has expended significant capital and human resources towards business expansion during the period, particularly in the military business with the commencement of CROWS production. Significant outlays have been made by the Company for production capacity, and to totally re-engineer its business processes to meet large increases in revenue in coming months. These costs include outlays to procure an ERP system from SAP, and associated costs for its implementation that will continue for another 18 months.

This effort has resulted in increased revenue from the Military business, and is positioning the Company's space businesses to undertake larger programs from 2006.

The key areas of effort and expense have been:

Military Production.

The Company has production commitments of approximately $90m for its military products to 31 December 2006 and in the half-year to 30 June 2005 expenditures of approximately $10m were made towards expanding production capacity in Australia and establishing production capacity in the US.

Capacity at 30 June 2005 was on schedule to reach $7m per month by early in 2006 with further programmed investment.

In this half-year an operating loss of $4**.7**m was incurred in this sector due to expenses for non-capital items, including plant set-up, process re-engineering and staff recruitment and training.

Space Systems.

In this established business area the Company suffered an operating loss of $0.1m due to costs associated with process re-engineering and also unexpected increases in the cost of specialized optics.

Space Surveillance.

The Company outlaid a further $0.3m in this period towards customer testing of its space surveillance data capabilities. Customers pay almost all data testing costs, but some costs are the responsibility of the Company.

Research and Development.

The Company has an announced commitment to complete its space debris de-orbit capability by 2007. This effort is co-funded by the Australian Federal Government under a R & D Start Grant. In this period there was approximately $0.7m in outlays.

These factors gave rise to an operating loss of $8m for the half-year period. Included in the operating loss for the half-year period is a charge of $2.3m in relation to share based payments in respect of options awarded to directors on 29 April 2005. This expense is a non cash operating expense and was required to be booked in accordance with A-IFRS.

The consolidated entity's cash position is such that all working capital requirements for the current round of customer contracts can be met from existing reserves.

Further information concerning the operations and financial condition of the consolidated entity can be found in the financial report and in releases made to the Australian Stock Exchange (ASX) during the half year.

Auditor's independence declaration

The auditor's independence declaration is included on page 5 of the half-year financial report.

Signed in accordance with a resolution of the directors made pursuant to s.306(3) of the Corporations Act 2001.

On behalf of the Directors

I.A Dennis
Director
Sydney, 01 September 2005

Deloitte

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The Board of Directors
Electro Optic Systems Holdings Limited
Level 12
75 Elizabeth Street
Sydney NSW 2000

01 September 2005

Dear Board Members

Electro Optic Systems Holdings Limited

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

As lead audit partner for the review of the financial statements of Electro Optic Systems Holdings Limited for the financial half-year ended 30 June 2005, I declare that to the best of my knowledge and belief, there have been no contraventions of:

(i) the auditor independence requirements of the Corporations Act 2001 in relation to the review; and

(ii) any applicable code of professional conduct in relation to the review.

Yours sincerely

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

D. Black.

David Black
Partner
Chartered Accountants

Deloitte.

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Independent review report to the members of Electro Optic Systems Holdings Limited

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, cash flow statement, statement of changes in equity, accompanying notes to the financial statements and the directors' declaration for the consolidated entity for the half-year ended 30 June 2005 as set out on pages 7 to 38. The consolidated entity comprises both Electro Optic Systems Holdings Limited (the company) and the entities it controlled at the end of the half-year or from time to time during the half-year.

The directors of the company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Corporations Act 2001. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Review Approach

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 the Corporations Act 2001, Accounting Standards AASB 134 'Interim Financial Reporting' and AASB 1 'First-time Adoption of Australian Equivalents to International Financial Reporting Standards' and other mandatory professional reporting requirements in Australia, so as to present a view which is consistent with our understanding of the consolidated entity'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 was conducted in accordance with Australian Auditing Standards applicable to review engagements. A review is limited primarily to inquiries of the entity's 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 provided 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 Electro Optic Systems Holdings Limited is not in accordance with:

(a) the Corporations Act 2001, including:

  (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2005 and of its performance for the half-year ended on that date; and

  (ii) complying with Accounting Standards AASB 134 'Interim Financial Reporting' and AASB 1 'First-time Adoption of Australian Equivalents to International Financial Reporting Standards' and the Corporations Regulations 2001; and

(b) other mandatory professional reporting requirements in Australia.

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

D. Black.

David Black
Partner
Chartered Accountants
Canberra, 01 September 2005

Member of
Deloitte Touche Tohmatsu

Directors' Declaration

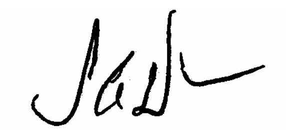
The directors declare that:

a) in the directors opinion, there are reasonable grounds to believe that the disclosing entity will be able to pay its debts as and when they become due and payable; and

b) in the directors opinion, the attached financial statements and notes thereto are in accordance with the Corporations Act 2001, including compliance with accounting standards and giving a true and fair view of the financial position and performance of the consolidated entity.

Signed in accordance with a resolution of the directors made pursuant to s.303(5) of the Corporations Act 2001.

On behalf of the Directors



I A Dennis
Director
Sydney, 01 September 2005

Consolidated income statement for the half-year ended 30 June 2005

	Note	Half-year ended 30 June 2005 $	Half-year Ended 30 June 2004 $
Revenue	2(a)	14,506,840	5,731,072
Other Income	2(b)	160,831	1,850,082
Changes in inventories of finished goods and work in progress		2,479,389	(240,931)
Raw materials and consumables used		(11,970,124)	(4,473,893)
Employee benefits expense		(9,497,008)	(3,485,040)
Administrative costs		(2,124,556)	(1,187,455)
Finance costs		(55,856)	(40,521)
Depreciation expense		(407,191)	(177,115)
Lease expenses		(16,700)	(14,155)
Occupancy costs		(867,612)	(314,304)
Other expenses		(206,838)	(147,760)
Loss before income tax expense	2	(7,998,825)	(2,500,020)
Income tax expense		-	-
Loss for the period	4	(7,998,825)	(2,500,020)
Earnings per share:			
Basic (cents per share)		(20.0)	(7.2)
Diluted (cents per share)		(20.0)	(7.2)

Notes to the financial statements are included on pages 12 to 38

Consolidated balance sheet
as at 30 June 2005

	Note	30 June 2005 $	31 December 2004 $
Current Assets			
Cash and cash equivalents		15,699,445	3,686,742
Trade and other receivables		8,049,976	4,192,238
Inventories		3,545,374	1,065,985
Other		217,731	170,979
Total Current Assets		27,512,526	9,115,944
Non-Current Assets			
Property, plant and equipment		5,395,975	1,657,120
Goodwill		5,505,764	5,505,764
Total Non-Current Assets		10,901,739	7,162,884
Total Assets		38,414,265	16,278,828
Current Liabilities			
Trade and other payables		4,930,000	2,092,819
Borrowings		484,889	354,186
Provisions		2,204,109	1,122,618
Other		2,073,751	2,748,453
Total Current Liabilities		9,692,749	6,318,076
Non-Current Liabilities			
Borrowings		1,152,944	588,689
Provisions		386,833	99,465
Total Non-Current Liabilities		1,539,777	688,154
Total Liabilities		11,232,526	7,006,230
Net Assets		27,181,739	9,272,698
Equity			
Issued capital		46,393,848	22,805,829
Reserves	3	2,585,544	265,597
Accumulated losses	4	(21,797,653)	(13,798,828)
Total Equity		27,181,739	9,272,598

Notes to the financial statements are included on pages 12 to 38

Consolidated statement of recognised income and expense for the half-year ended 30 June 2005

	Note	Half-year ended 30 June 2005 $	Half-year Ended 30 June 2004 $
Translation of foreign operations:			
Exchange differences taken to equity		(13,934)	51,974
Net income recognised directly in equity		(13,934)	51,974
Loss for the period		(7,998,825)	(2,500,020)
Total recognised income and expense for the period		(8,012,759)	(2,448,046)

Notes to the financial statements are included on pages 12 to 38

Consolidated cash flow for the half-year ended 30 June 2005

	Note	Half-year ended 30 June 2005 $	Half-year ended 30 June 2004 $
Cash Flows From Operating Activities			
Receipts from customers		9,257,253	9,456,100
Receipts from insurance claim for destruction of assets		-	1,894,979
Payments to suppliers and employees		(17,797,625)	(10,825,208)
Interest and bill discounts received		466,118	148,197
Interest and other costs of finance paid		(55,856)	(40,521)
Net cash provided by/ (used in) operating activities		(8,130,110)	633,547
Cash Flows From Investing Activities			
Amounts advanced to non related parties		-	(200,000)
Payment for property, plant and equipment		(4,146,046)	(163,702)
Net cash (used in)/ provided by investing activities		(4,146,046)	(363,702)
Cash Flows From Financing Activities			
Proceeds from the exercise of options		1,088,019	76,061
Proceeds from placement of shares		22,500,000	-
Proceeds from borrowings		694,958	-
Repayment of borrowings			(115,142)
Net cash (used in)/ provided by financing activities		24,282,977	(39,081)
Net Increase/(Decrease) In Cash Held		12,006,821	230,764
Cash and cash equivalents at the beginning of the half-year		3,686,742	5,930,878
Effects of exchange rate changes on the balance of cash held in foreign currencies		5,882	(47,672)
Cash and cash equivalents at the end of the half-year		15,699,445	6,113,970

Notes to the financial statements are included on pages 12 to 38

1. Summary of accounting policies

Basis of preparation

The half-year financial report is a general purpose financial report prepared in accordance with the Corporations Act 2001 and AASB 134 Interim Financial Reporting. Compliance with AASB 134 ensures compliance with International Financial Reporting Standard IAS34 Interim Financial Reporting. The half-year financial report does not include notes of the type normally included in an annual financial report and shall be read in conjunction with the most recent annual financial report.

The consolidated entity changed its accounting policies on 1 January 2005 to comply with A-IFRS. The transition to A-IFRS is accounted for in accordance with Accounting Standard AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards, with 1 January 2004 as the date of transition. An explanation of how the transition from superseded policies to A-IFRS has affected the consolidated entity's financial position, financial performance and cash flows is discussed in Note 12.

The accounting policies set out below have been applied in preparing the financial statements for the half-year ended 30 June 2005, the comparative information presented in these financial statements, and in the preparation of the opening A-IFRS balance sheet at 1 January 2004 (as disclosed in Note 12, the consolidated entity's date of transition, except for the accounting policies in respect of financial instruments. The consolidated entity has not restated comparative information for financial instruments, including derivatives, as permitted under the first-time adoption transitional provisions. The accounting policies for financial instruments applicable to the comparative information are consistent with those adopted and disclosed in the lodged 2004 annual financial report. The impact of changes in these accounting policies on 1 January 2005, the date of transition for financial instruments, is discussed further in note 12.

Significant accounting policies

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

(a) Borrowings

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

1. Summary of accounting policies (cont'd)

(b) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, cash in banks and investments in money market instruments, net of outstanding bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the balance sheet.

(c) Construction contracts and work in progress

Construction work in progress is valued at cost plus profit recognised to date, less any provision for anticipated future losses. Costs include both variable and fixed costs relating to specific contracts, and those costs that are attributable to the contract activity in general and can be allocated on a reasonable basis.

Construction profits are recognised on the percentage completion basis measured using the proportion of costs incurred to date as compared to expected total costs. Where losses are anticipated they are provided in full.

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

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

(d) Employee benefits

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

Provisions made in respect of employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Provisions made in respect of employee benefits which are not expected to be settled within 12 months are measured as the present value of the estimated future cash outflows to be made by the consolidated entity in respect of services provided by employees up to the reporting date.

Defined contribution plans

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

1. Summary of accounting policies (cont'd)

(e) Financial assets

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

Held to maturity investments

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

Loans and receivables

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

(f) Financial instruments issued by the company

Debts and equity instruments

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

Transaction costs on the issue of equity instruments

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

Interest

Interest is classified as an expense consistent with the balance sheet classification of the related debt.

(g) Foreign currency

Foreign currency transactions

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

1. Summary of accounting policies (cont'd)

(g) Foreign currency (cont'd)

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

Foreign operations

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

Goodwill and fair value adjustments arising on the acquisition of a foreign entity on or after the date of transition to A-IFRS are treated as assets and liabilities of the foreign entity and translated at exchange rates prevailing at the reporting date. Goodwill arising on acquisitions before the date of transition to A-IFRS is treated as an Australian dollar denominated asset.

(h) Goods and services tax

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

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

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

1. Summary of accounting policies (cont'd)

(i) Goodwill

Goodwill, representing the excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired, is recognised as an asset and not amortised, but tested for impairment annually and whenever there is an indication that the goodwill may be impaired. Any impairment is recognised immediately in the profit and loss and is not subsequently reversed. Refer also note 1(k).

(j) Government grants

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

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

(k) Impairment of assets

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

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

1. Summary of accounting policies (cont'd)

(k) Impairment of assets (cont'd)

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

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

(l) Income tax

Current tax

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

Deferred tax

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

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

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

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

1. Summary of accounting policies (cont'd)

(l) Income tax (cont'd)

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

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

Current and deferred tax for the period

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

Tax consolidation

The company and all its wholly-owned Australian resident entities are part of a tax consolidated group under Australian taxation law. Electro Optic Systems Holdings Limited is the head entity in the tax-consolidated group.

(m) Intangible assets

Intangible assets acquired in a business combination

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

(n) Inventories

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

1. Summary of accounting policies (cont'd)

(o) Investment property

Investment property, which is properly held to earn rentals and/or for capital appreciation, is measured at its fair value at the reporting date. Gains or losses arising from changes in the fair value of the investment property are included in the profit and loss in the period in which they arise.

(p) Leased assets

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

Consolidated entity as lessee

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

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

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

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

Lease incentives

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

(q) Payables

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

1. Summary of accounting policies (cont'd)

(r) Principles of consolidation

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

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

The interest of minority shareholders is stated at the minority's proportion of the fair values of the assets and liabilities recognised.

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

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

(s) Property, plant and equipment

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

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

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

Plant and equipment	5 to 15 years
Leasehold improvements	5 years
Equipment under finance lease	5 years

1. Summary of accounting policies (cont'd)

(t) Provisions

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

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

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

Warranties – Provisions for warranty costs are recognised at the date of sale of the relevant products, at the directors best estimate of the expenditure required to settle the consolidated entity's liability.

(u) Research and development costs

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

(v) Revenue recognition

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

Rental revenue comprises revenue earned from the rental of the investment property at 40 Frankston Road, Dandenong, Victoria. Rental revenue is recognised when the rent in respect of the premises is receivable.

Interest income is recognised as it accrues.

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

(w) Share based payments

Equity–settled share-based payments granted after 7 November 2002 that were unvested as of 1 January 2005, are measured at fair value at the date of the grant. Fair value is measured by use of a binomial model. The expected life used in the model has been adjusted, based on management best estimates, for the effects of non-transferability, exercise restrictions and behavioural considerations.
The fair value determined at the grant date of the equity-settled share based payments is expensed on a straight-line basis over the vesting period, based on the consolidated entity's estimate of shares that will eventually vest.

1. Summary of accounting policies (cont'd)

(x) Comparative information – financial instruments

The consolidated entity has not restated comparative information for financial instruments as permitted under the first-time adoption transitional provisions. The accounting policies for financial instruments applicable to the comparative information are consistent with those adopted and disclosed in the lodged 2004 annual financial report.

2. Loss From Ordinary Activities

Loss from ordinary activities before income tax includes the following items of revenue and expense:

	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $
(a) Revenue		
Contract receipts	14,040,722	4,418,601
Insurance proceeds received	-	1,094,979
Interest received	466,118	148,197
Rental income	-	69,295
Total revenue	14,506,840	5,731,072
(b) Income		
Grant revenue	-	1,822,891
Profit on sale of fixed assets	33,305	5,054
Foreign exchange gain	94,546	10,849
Other revenue	32,980	11,288
	160,831	1,850,082
(c) Expenses		
Depreciation of non-current assets	407,191	177,115

	30 June 2005 $	31 December 2004 $

3. Reserves

	30 June 2005 $	31 December 2004 $
Foreign currency translation reserve	(24,708)	(10,774)
Employee Equity settled benefits reserve	2,610,252	276,771
Balance at end of financial period	2,585,544	265,997

4. Accumulated Losses

	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $
Balance at beginning of financial period	(13,798,828)	(7,882,708)
Net loss for the period	(7,998,825)	(2,500,020)
Balance at end of financial period	(21,797,653)	(10,382,728)

5. Earnings Per Share

	2005 ¢ per share	2004 ¢ per share
Basic EPS	(20.0 cents)	(7.2 cents)
Diluted EPS	(20.0 cents)	(7.2 cents)

Basic Earnings per Share

The earnings and weighted average number of ordinary shares used in the calculation of basic earnings per share are as follows:

	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $
Earnings (a)	(7,998,825)	(2,500,020)

	2005 No.	2004 No.
Weighted average number of ordinary shares used in the calculation of basic earnings per share	39,907,473	34,497,048

(a) Earnings used in the calculation of basic earnings per share is the same as net loss in the profit and loss.

Diluted Earnings per Share

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

	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $
Earnings (a)	(7,998,825)	(2,500,020)

	2005 No.	2004 No.
Weighted average number of ordinary shares and potential ordinary shares (b) & (c)	39,907,473	34,497,048

(a) Earnings used in the calculation of diluted earnings per share is the same as net loss in the profit and loss.

5. Earnings Per Share (cont'd)

(b)The following are considered to be potential ordinary shares but are not dilutive and are therefore excluded from the weighted average number of ordinary shares used in the calculation of basic and diluted earnings per share.

	30 June 2005- Number	30 June 2004 Number
Vendor options at $0.20	295,967	353,708
CEO options at $0.20	-	4,563,925
Directors options at $1.64	400,000	400,000
Staff Share Plan at $1.64	659,500	811,500
Staff Share Plan at $2.85	672,500	700,000
Directors options at $2.58	300,000	-
Directors options at $2.56	200,000	-
Directors options at $3.06	688,800	-
Total unlisted options	3,216,767	6,829,133

(c) Weighted average number of ordinary shares and potential ordinary shares used in the calculation of diluted earnings per share reconciles to the weighted average number of ordinary shares used in the calculation of basic earnings per share as follows:		
Weighted average number of ordinary shares used in the calculation of basic earning per share	39,907,473	34,497,048
Shares deemed to be issued for no consideration in respect of:		
CEO Options	-	-
Vendor Options	-	-
Weighted average number of ordinary shares and potential ordinary shares used in the calculation of diluted earnings per share	39,907,473	34,497,048

6. Contingent Liabilities

Electro Optic Systems Pty Limited provided a guarantee to Fire Control Systems Pty Limited, a controlled entity, on 16 October 1996 to meet any genuine commitments of Fire Control Systems Pty Limited, either current or to be raised in the foreseeable future.

Electro Optic Systems Pty Limited has engaged in Research and Development syndications during the period from 1992 through to 1996. The taxation treatment undertaken was in accordance with specific and general taxation rulings issued by the Australian Taxation Office. However, Electro Optic Systems Pty Limited has a contingent liability under indemnities given to Research and Development Investors in the event that the Australian Taxation Office reverses its rulings.

The Australian Taxation Office has been conducting a review of Research and Development syndications and has offered a settlement to all investors in such Research and Development syndicates in order to allow them to close off the matter. In relation to the 3D Imaging Systems Research and Development project in which Electro Optic Systems Pty Limited was involved the Australian Tax Office has offered a settlement of $881,100 plus interest. The directors of Electro Optic Systems Pty Limited have rejected this settlement offer based upon legal advice received. The directors are of the view that the circumstances of this investment were significantly different from the majority of other syndications and that Electro Optic Systems Pty Limited has a defendable position and hence no outstanding tax liability in relation to this matter.

On 8 December 2003, the parent company and the subsidiary company Electro Optic Systems Pty Limited entered into a Deed of Undertaking with the Industry Research and Development Board on behalf of the Commonwealth of Australia. The undertaking from the parent company was to ensure that the subsidiary company was able to contribute matching funding under the R & D Start Program for the Project.

7. Segment Information

	External Sales		Total	
	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $	Half-year to 30 June 2005 $	Half-year to 30 June 2004 $
Space systems	11,121,003	5,138,288	11,121,003	5,138,288
Defence	2,919,719	417,731	2,919,719	417,731
Investment	-	69,295	-	69,295
Total of all segments	14,040,722	5,625,314	14,040,722	5,625,314
Eliminations	-	-	-	-
Unallocated	466,118	105,758	466,118	105,758
Consolidated	14,506,840	5,731,072	14,506,840	5,731,072

7. Segment Information (cont'd)

Segment Results

	2005 $	2004 $
Space systems	(2,261,567)	(1,434,525)
Defence	(5,812,227)	(746,928)
Investment	-	69,295
Total of all segments	(8,073,794)	(2,112,158)
Unallocated	74,969	(387,862)
Loss from ordinary activities before income tax expense	(7,998,825)	(2,500,020)
Income tax benefit relating to ordinary activities	-	-
Loss from ordinary activities after related income tax expense	(7,998,825)	(2,500,020)

7. Segment Information (cont'd)

Product and Services within each Business Segment

Space Systems

EOS is a supplier of large optical systems. During the period the order intake in this sector continued to reflect the growing demand.

Space Surveillance

In the next 2 years the Company expects several billion dollars of space surveillance infrastructure, world-wide, to be upgraded.

EOS's laser-based space surveillance systems have been demonstrated in customer trials and EOS is now well-placed to be a major contributor to the next generation of space tracking capability.

In addition, EOS has substantial space resources in its own right, and will enter the market for space data provision from early 2006.

Defence

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

In 2001 EOS participated in a team that was awarded the US Army "CROWS" program. After 2 years of testing and commended service in current conflicts, CROWS was approved for production during 2004.

EOS is producing these CROWS units for the US Army from its Queanbeyan facility and will start producing units at its Tucson production facility in September 2005.

Investment

The parent company had a commercial property in Dandenong, Victoria which was rented to independent tenants. The parent company sold the property in October 2004.

8. Subsequent Events

Since 30 June 2005, two option holders have exercised a total of 17,000 options with an exercise price of $1.64 raising $27,880.

On 22 July 2005 a new wholly owned subsidiary was formed in Germany called EOS Optronics GmbH. The new subsidiary will undertake projects in Europe and has a Joint Cooperation Agreement with the University of Applied Sciences, Deggendorf, Germany.

9. Issuance of Securities

On 31 January 2005, Electro Optic Systems Holdings Limited issued 5,000,000 ordinary shares at $4.50 each to Northrop Grumman Space and Mission Systems Corp for cash of $22,500,000. In addition to the placement of ordinary shares a total of 4,716,196 options (including 4,563,925 CEO options) were exercised at various exercise prices raising a further $1,088,019.

Electro Optic Systems Holdings Limited issued 1,188,800 share options over ordinary shares to Directors under the Employee Share Option Plan on 29 April 2005 following shareholder approval on 29 April 2005. The issue of these options resulted in a charge to profit and loss during the half year of $2,333,881 which is included under employee compensation.

On 20 May 2005, Dr Ben Greene, the CEO of the company exercised all of his 4,563,925 CEO options at an exercise price of 20 cents raising a total of $912,785.

10. Impacts of the adoption of Australian equivalents to International Financial Reporting Standards

The consolidated entity changed its accounting policies on 1 January 2005 to comply with Australian equivalents to International Financial Reporting Standards (A-IFRS). The transition to A-IFRS is accounted for in accordance with Accounting Standard AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards, with 1 January 2004 as the date of transition, except for financial instruments, including derivatives, where the date of transition is 1 January 2005.

An explanation of how the transition from superseded policies to A-IFRS has affected the consolidated entity's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables.

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effect of A-IFRS on the balance sheet as at 1 January 2004

	Note	Super-seded policies * $	Effects of transition to A-IFRS $	A-IFRS $
Current Assets				
Cash assets		5,930,878	-	5,930,878
Receivables		5,437,566	-	5,437,566
Inventories		805,656	-	805,656
Other		19,842	-	19,842
Total Current Assets		12,193,942	-	12,193,942
Non-Current Assets				
Property, plant and equipment	(a)	6,860,729	(5,600,000)	1,260,729
Investment property	(b)	1,645,251	161,736	1,806,987
Goodwill	(c)	5,505,764	-	5,505,764
Total Non-Current Assets		14,011,744	(5,438,264)	8,573,480
Total Assets		26,205,686	(5,438,264)	20,767,422
Current Liabilities				
Payables		1,923,524	-	1,923,524
Interest-bearing liabilities		163,752	-	163,752
Provisions		1,010,367	-	1,010,367
Other		2,303,871	-	2,303,871
Total Current Liabilities		5,401,514	-	5,401,514
Non-Current Liabilities				
Interest-bearing liabilities		537,833	-	537,833
Provisions		80,235	-	80,235
Total Non-Current Liabilities		618,068	-	618,068
Total Liabilities		6,019,582	-	6,019,582
Net Assets		20,186,104	(5,438,264)	14,747,840
Equity				
Issued capital		22,630,548	-	22,630,548
Reserves	(d)	(101,256)	101,256	-
Accumulated losses		(2,343,188)	(5,539,520)	(7,882,708)
Total Equity		20,186,104	(5,438,264)	14,747,840

* Reported financial position for the year ended 31 December 2003

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effect of A-IFRS on the income statement for the half-year ended 30 June 2004

	Note	Super-seded policies* $	Effect of transition to A-IFRS $	A-IFRS $
Revenue from ordinary activities	(e)	7,618,539	(37,385)	7,581,154
Changes in inventories of finished goods and work in progress		(240,931)	-	(240,931)
Raw materials and consumables used		(4,473,893)	-	(4,473,893)
Employee benefits expense		(3,445,558)	(39,482)	(3,485,040)
Amortisation expense	(c)	(333,246)	333,246	-
Administrative costs		(1,187,455)	-	(1,187,455)
Borrowing costs		(40,521)	-	(40,521)
Depreciation expense	(a)	(527,115)	350,000	(177,115)
Net Book Value of fixed assets disposed	(e)	(37,385)	37,385	-
Lease expenses		(14,155)	-	(14,155)
Occupancy costs		(314,304)	-	(314,304)
Other expenses from ordinary activities		(147,760)	-	(147,760)
Loss before income tax expense		(3,143,784)	643,764	(2,500,020)
Income tax expense		-	-	-
Loss for the period		(3,143,784)	643,764	(2,500,020)

* Reported financial results under previous Australian AGAAP

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effect of A-IFRS on the income statement for the financial year ended 31 December 2004

	Note	Super-seded policies* $	Effect of transition to A-IFRS $	A-IFRS $
Revenue from ordinary activities	(e)	15,878,583	(1,806,987)	14,071,596
Changes in inventories of finished goods and work in progress		260,329	-	260,329
Raw materials and consumables used		(7,882,369)	-	(7,882,369)
Employee benefits expense	(f)	(7,917,614)	(276,371)	(8,193,985)
Amortisation expense	(c)	(666,492)	666,492	-)
Administrative costs		(2,754,183)	-	(2,754,183)
Borrowing costs		(104,297)	-	(104,297)
Cost of property sold	(e)	(1,688,264)	1,688,264	-
Depreciation expense	(a)	(1,122,322)	700,000	(422,322)
Foreign exchange losses		(160,809)	-	(160,809)
Lease expenses		(36,682)	-	(36,682)
Occupancy costs		(626,207)	-	(626,207)
Other expenses from ordinary activities		(124,178)	(43,013)	(167,191)
Loss before income tax expense		(6,944,505)	928,385	(6,016,120)
Income tax expense		100,000	-	100,000
Loss for the period		(6,844,505)	928,385	(5,916,120)

* Reported financial results under previous Australian AGAAP

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effect of A-IFRS on the balance sheet as at 30 June 2004

	Note	Super-seded policies * $	Effects of transition to A-IFRS $	A-IFRS $
Current Assets				
Cash assets		6,113,970	-	6,113,970
Receivables		2,711,150	-	2,711,150
Inventories		564,725	-	564,725
Other		235,590	-	235,590
Total Current Assets		9,625,435	-	9,625,435
Non-Current Assets				
Property, plant and equipment	(a)	6,715,966	(5,250,000)	1,465,966
Investment property	(b)	1,645,251	161,736	1,806,987
Goodwill	(c)	5,172,518	333,246	5,505,764
Total Non-Current Assets		13,533,735	(4,755,018)	8,778,717
Total Assets		23,159,170	(4,755,018)	18,404,152
Current Liabilities				
Payables		1,375,188	-	1,375,188
Interest-bearing liabilities		191,574	-	191,574
Provisions		1,131,207	-	1,131,207
Other		2,676,973	-	2,676,973
Total Current Liabilities		5,474,942	-	5,474,942
Non-Current Liabilities				
Interest-bearing liabilities		617,821	-	617,821
Provisions		-	-	-
Total Non-Current Liabilities		617,821	-	617,821
Total Liabilities		6,092,763	-	6,092,763
Net Assets		17,066,407	(4,755,018)	12,311,389
Equity				
Issued capital		22,706,609	-	22,706,609
Reserves	(d)	(153,230)	140,738	(12,492)
Accumulated losses		(5,486,972)	(4,895,756)	(10,382,728)
Total Equity		17,066,407	(4,755,018)	12,311,389

* Reported financial position under previous AGAAP.

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effect of A-IFRS on the balance sheet as at 31 December 2004

	Note	Super-seded policies * $	Effects of transition to A-IFRS $	A-IFRS $
Current Assets				
Cash assets		3,686,742	-	3,686,742
Receivables		4,192,238	-	4,192,238
Inventories		1,065,985	-	1,065,985
Other		170,979	-	170,979
Total Current Assets		9,115,944	-	9,115,944
Non-Current Assets				
Property, plant and equipment	(a)	6,557,120	(4,900,000)	1,657,120
Goodwill	(c)	4,839,272	666,492	5,505,764
Total Non-Current Assets		11,396,392	(4,233,508)	7,162,884
Total Assets		20,512,336	(4,233,508)	16,278,828
Current Liabilities				
Payables		2,092,819	-	2,092,819
Interest-bearing liabilities		354,186	-	354,186
Provisions		1,122,618	-	1,122,618
Other		2,748,453	-	2,748,453
Total Current Liabilities		6,318,076	-	6,318,076
Non-Current Liabilities				
Interest-bearing liabilities		588,689	-	588,689
Provisions		99,465	-	99,465
Total Non-Current Liabilities		688,154	-	688,154
Total Liabilities		7,006,230	-	7,006,230
Net Assets		13,506,106	(4,233,508)	9,272,598
Equity				
Issued capital		22,805,829	-	22,805,829
Reserves	(d),(f)	(112,030)	377,627	265,597
Accumulated losses		(9,187,693)	(4,611,135)	(13,798,828)
Total Equity		13,506,106	(4,233,508)	9,272,598

* Reported financial position under previous AGAAP

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

Effects of A-IFRS on the cash flow statement for the financial year ended 31 December 2004

There are no material differences between the cash flow statement presented under A-IFRS and the cash flow statement presented under the superseded policies.

Notes to the reconciliations of income and equity

(a) Impairment of assets

The consolidated entity decided to write down the value of the Westpac satellite of $5,600,000 at the date of transition. The decision was taken on the basis that there is no active market or basis for valuation to determine the fair value of the satellite less costs to sell, the value in use based upon contracts on hand at transition date of 1 January 2004 was nil and the present value of expected future cash flows from the assets discounted back and the most significant cash flows are expected to occur after 5 years from transition date, however no reliable estimate of these can be formed at the transition date. The effect of the transitional adjustment is that an annual depreciation charge will be reduced by $700,000 per annum.

(b) Investment property

The consolidated entity decided to revalue its investment property at the date of transition by increasing the value by $161,736 to $1,806,987. The adjustment was recognised as a transitional adjustment. The property was subsequently sold in October 2004 and the consolidated entity received net proceeds from the sale of $1,806,987.

(c) Goodwill

The consolidated entity has elected not to restate business combinations that occurred prior to the date of transition to A-IFRS, and accordingly, the carrying amount of goodwill at the date of transition has not changed.
However, goodwill, which was amortised under superseded policies, is not amortised under A-IFRS from the date of transition. The effect of this change is an increase in the carrying amount of goodwill by $333,492 and a reduction in the loss of $333,492 for the half-year ended 30 June 2004, and by $666,492 for the financial year ended 31 December 2004. There is no tax effect as deferred taxes are not recognised for temporary differences arising from goodwill for which amortisation is not deductible for tax purposes.

(d) Foreign Currency Translation Reserve

The consolidated entity decided to reset the foreign currency reserve to Nil as a transitional adjustment. The effect of the adjustment was a reduction in the reserve of $101,256 and a reduction in accumulated losses.

10. Impacts of adopting the Australian equivalents to International Financial Reporting Standards (Cont'd)

(e) Revenue

Under superseded policies, the consolidated entity recognised the gain or loss on disposal of property, plant and equipment on a gross basis by recognising the proceeds of sale as revenue, and the carrying amount of the property, plant and equipment disposed as an expense. Under A-IFRS, the gain or loss on disposal is recognised on a net basis, and is classified as income, rather then revenue. Accordingly, the gross amounts have been reclassified within the income statement for A-IFRS reporting purposes.

(f) Share-based payment

For the half-year ended 30 June 2004 and the financial year ended 31 December 2004, share based payments of $39,482 and $276,371 (included in employee benefit expenses) which were not recognised under the superseded policies were recognised under A-IFRS, with a corresponding increase in the employee equity settled benefits reserve.

11. Other Significant Information

None

12. Information on Audit or Review

This half yearly report is based on accounts to which one of the following applies.

- ☐ The accounts have been audited.
- ☒ The accounts have been subject to review.
- ☐ The accounts are in the process of being audited or subject to review.
- ☐ The accounts have not yet been audited or reviewed.

Description of likely dispute or qualification if the accounts have not yet been audited or subject to review or are in the process of being audited or subjected to review.

Description of dispute or qualification if the accounts have been audited or subjected to review.