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DRONESHIELD

@DroneShield
www.droneshield.com
ABN 26 608 915 859

Appendix 4E
For the year ended 31 December 2018

DroneShield Limited
ABN 26 608 915 859

1. Reporting period

The financial information contained in the attached consolidated financial report is for the year ended 31 December 2018. The previous corresponding period was the year ended 31 December 2017.

Results for announcement to the market				
	Up/ Down	% Movement		2018 $
Revenue from continuing activities	Up	215%	to	1,207,203
Loss from continuing activities after tax attributable to members	Up	16%	to	(6,336,100)
Net loss attributable to members	Up	16%	to	(6,336,100)
Dividends: No dividends are being proposed or have been paid	Nil	Nil		Nil

Additional information:

2. Commentary related to the above results

Refer to Directors Report in the attached Annual Report.

3. Net Tangible Assets/(Liabilities) per share:

31 December 2018: $0.01; 31 December 2017: $0.02

4. There was no change of control during the year

5. There were no payments of dividends during the year

6. There is no dividend reinvestment plan in operation

7. There are no associates or joint venture entities

8. This report is based on the consolidated financial report which has been audited by HLB Mann Judd Assurance (NSW) Pty Ltd.

Further information regarding the company and its business activities can be obtained by visiting the company's website at www.droneshield.com

DRONESHIELD

Annual Report

For the Year Ended
31 December 2018

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Image: DroneShield's DroneSentry™ installation

DroneShield Limited (ASX:DRO)
ASX Release
ABN 26 608 915 859

Table of Contents

Corporate Information 2
Chairman's Review 3
About DroneShield 5
Board of Directors and Executives 11
Corporate Governance Statement 13
Directors' Report 22
Directors' Report- Remuneration Report (audited) 29
Auditor's Independence Declaration 37
Consolidated Statement of Profit or Loss and Other Comprehensive Income 38
Consolidated Statement of Financial Position 39
Consolidated Statement of Changes in Equity 40
Consolidated Statement of Cash Flows 41
1. Summary of Significant Accounting Policies 42
2. Critical accounting judgements, estimates and assumptions 48
3. Options issued 49
4. Revenue 51
5. Other revenue and income 51
6. Corporate and support expense 51
7. Corporate governance expense 52
8. Income taxes relating to continuing operations 52
9. Cash and cash equivalents 53
10. Trade and other receivables 53
11. Inventories 53
12. Plant, equipment and intangible assets 54
13. Borrowings 54
14. Provisions 54
15. Other liabilities 55
16. Contributed equity 55
17. Shares and options 56
18. Commitments 57
19. Key Management Personnel disclosures and related party transactions 57
20. Parent entity financial information 58
21. Financial risk management 58
22. Earnings (loss) per share 60
23. Contingent liabilities 61
24. Remuneration of auditor 61
25. Segment information 61
26. Reconciliation from loss after income tax to net cash outflow from operating activities 63
27. Events after the reporting date 63
Directors' Declaration 64
Independent Auditor's Report 65
Shareholder Information 70

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Corporate Information

Directors & Management

Peter James Independent Non-Executive Chairman
Oleg Vornik CEO and Managing Director
Robert Clisdell Non-Executive Director
Bradley Buswell Independent Non-Executive Director

Registered Office

Level 5, 126 Phillip St
Sydney, NSW 2000
Australia

Telephone: +61 2 9995 7280

Email: info@droneshield.com
Website: www.droneshield.com

Auditors

HLB Mann Judd Assurance (NSW) Pty Ltd
Level 19, 207 Kent Street
Sydney, NSW 2000
Australia

Bankers

Commonwealth Bank of Australia
Level 21, 201 Sussex Street
Sydney, NSW 2000
Australia

PNC Bank
1405 P Street, NW
Washington DC 20005
United States of America

Solicitors

Baker & McKenzie LLP
452 Fifth Avenue
New York NY 10018
United States of America

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16 Milligan Street
Perth, WA 6000
Australia

K&L Gates
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Washington DC 20006
United States of America

WilmerHale
60 State Street
Boston MA 02109
United States of America

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267 St Georges Terrace
Perth WA 6000
Australia

Enquiries (within Australia): 1300 288 664
Enquiries (outside Australia): +61 8 9324 2099

Stock Exchange Listing

DroneShield Limited (ASX code DRO) shares are quoted on the Australian Securities Exchange.

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Chairman's Review



Peter James, Independent Non-Executive Chairman

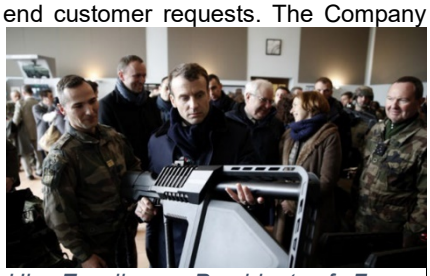
Dear Fellow Shareholders,

We believe that, due to the well-publicised events at the Gatwick Airport in the UK (see page 6 below for more detail), 2018 was a watershed year for both the counter-drone industry and DroneShield Ltd ("DroneShield" or the "Company") as a leader and early mover in that industry. The global recognition of the need for drone detection and mitigation started well before the Gatwick events; however, it was after these events that the rate of adoption of anti-drone technologies accelerated substantially. This groundswell of adoption has now started to be reflected in DroneShield's financial performance.

Among other things:

- DroneShield generated total customer cash receipts of $1,252,123 for the calendar 2018 – the Company's highest annual cash receipts to date;
- of that amount, close to half ($489,209) was received during the most recent (31 December 2018) quarter, with DroneShield producing its highest quarterly cash inflows for DroneShield to date in that most recent quarter;
- DroneShield's revenue from sales for the 2018 calendar / financial year were $953,857 (as opposed to the slightly higher cash receipts referenced above). That is a 207% increase in the year on year revenue; and
- importantly, DroneShield's cash receipts for January 2019 were $738,591. In other words, following the Gatwick events, in the first three weeks of the 2019 calendar year, DroneShield received approximately 50% more in cash from its customers than it did during the entire previous quarter.

During the year, the Company released several new products in response to end customer requests. The Company released DroneGun Tactical™ (a portable, rifle-style drone disruptor), DroneNode™ (a covert style drone disruptor), a new generation software system for its DroneSentinel™ and DroneSentry™ detection and detect-and-defeat systems, and DroneCannon RW™ (a drone disruptor for Remote Weapon Stations). The Company also partnered with Intelligent Security Integration Aust. Pty Ltd. in releasing RapidScout® (a vehicle-mounted counterdrone solution). In June 2018, DroneShield received a $3.2 million order for 70 DroneGuns™ from a Middle Eastern Ministry of Defence, the largest known order of its kind in the industry globally to date. It also made several initial sales across its product suite globally, including Central American, Asian and Western government security, defence and law enforcement agencies.

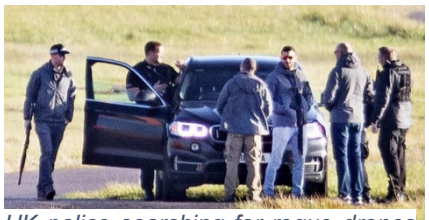


His Excellency President of France Emmanuel Macron, French Minister of the Armed Forces Florence Parly and the Chief of Staff of the Army Jean-Pierre Bosser review DroneGun Tactical™

DroneShield made significant progress with key strategic partnerships globally, including teaming agreements with the major global defence prime Thales and the Middle Eastern publicly listed telecommunications conglomerate Zain. The Company added key distributors to its global network, including two Tailored Logistics Support ("TLS") Program partners in the U.S., to assist sales to the U.S. Government. DroneShield's products were accepted into the General Service Administration ("GSA") schedule in the U.S. Further in that market, the Company participated in several high-profile U.S. military trials including U5G event at Camp Pendleton with the U.S. Navy / Marine Corps, and Asymmetric Warfare Group trials at Fort AP Hill.

The Company continued to benefit from the Australian Government's Defence Export Strategy, continuing to be selected to be a part of Team Defence Australia at key defence events globally, as well as having access to a network of Australian embassy defence attaches around the world. It received its first R&D Tax Incentive Grant from the Australian Government, and in the process of applying for a second grant for 2018's activities.

DroneShield's developments come against the rapidly increasing backdrop of terrorist organisations increasing the sophistication and frequency of use of consumer and commercial grade drones for nefarious purposes. The prolonged shutdown of the UK's Gatwick Airport at Christmas has substantially accelerated the awareness of the drone threat, and the associated procurement processes. Both the civil aviation and the defence markets are expected to be key segments for the Company going forward, and the Company is well positioned for the defence markets as it is participating in a number of tenders, and its products are undergoing a number of evaluations at present.



UK police searching for rogue drones during the Gatwick Airport shutdown in December 2018

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DroneShield continues to attract a significant amount of media interest globally, including coverage by Australian Financial Review, Sydney Morning Herald, Channel 7 and Commsec TV, ABC, Bloomberg, 3AW radio, ABC radio and 2GB radio in Australia; NewstalkZB radio in New Zealand; and key publications in the US and the UK, such as The Wall Street Journal, Forbes and The Daily Mail.

On behalf of the Board I would like to thank our Executive team for their significant contributions this year.

I would also like to thank our fellow shareholders for your support and look forward to continued growth of the Company.



Peter James
Independent Non-Executive Chairman

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About DroneShield

Based in Sydney (Australia), Virginia (USA) and Washington DC (USA), DroneShield is a leader in drone security technology. The company has developed drone security solutions that protect people, organisations and critical infrastructure from the intrusion of drones. Its team includes professionals with world-class expertise in engineering and physics, combined with substantial experience in government, defence and intelligence.

History of DroneShield

Founded on 10 January 2014, the DroneShield business began as DroneShield LLC in the United States. On 4 November 2015, DroneShield Limited was incorporated in Australia for the primary purpose of listing on the ASX and engaging in the business of offering products manufactured by DroneShield globally, as well as managing and operating DroneShield's business.

DroneShield Limited listed on the ASX on 22 June 2016, raising $7m through the issue of 35 million shares at $0.20 per share in an oversubscribed initial public offer ('IPO'). It subsequently raised $1.25m through a placement and Share Placement Plan ('SPP') in June 2017 and a further $2.32m in a placement in October 2017. Further funding was raised in early 2017 through exercise of some of the listed DROO options, which were issued as part of the IPO.

In 2018, DroneShield raised $2.55m through a placement in March and raised $1.7m through a placement and Share Placement Plan ('SPP') in November. It has subsequently raised $1.3m in a placement in February 2019.

DroneShield has grown from a small start-up to a global leader in drone detection and mitigation.

Business Model and Products

Affordable consumer-grade drones have become popular around the world, but they present unique and frequent threats to privacy, physical security and public safety in a wide variety of environments. DroneShield offers products that detect and defeat such drones to civil infrastructure operators, militaries, and other government and commercial users globally. DroneShield's distribution channels focus on third party distributors, as well as direct relationships with various key customers, such as military, security and law enforcement agencies of various governments around the world and commercial civil infrastructure operators globally. With offices in Australia and the United States, DroneShield has an experienced salesforce with approximately 60 distribution partners across 50 countries. The ultimate end-users and potential end-users of DroneShield's products come from a diverse array of global sectors, including the following:

- Defence agencies.
- Airports and other civil defence users.
- Utilities such as power plants, electricity grids and gas pipelines.
- Ports and other critical infrastructure asset owners.
- Intelligence and national security agencies.
- Prisons.
- Stadiums and other public event venues and organisers.
- Media production sites.
- Real estate owners including hotels, commercial offices and manufacturing plants.
- Executive protection including ultra-high net worth individuals and government officials.

DroneShield offers a comprehensive solution to drone threats with a suite of detection and countermeasure products. DroneShield's products are readily available and it offers one of the few commercially available and affordable solutions to the worldwide threat caused by consumer grade drones.

Please see the below for additional detail on the Company's current product range.



DroneGun Tactical™

- Portable rifle shape drone disruptor, causing the drone (or swarm) to safely land, or fly back to the starting point (potentially identifying the pilot)
- 70 units ordered by a Middle Eastern Ministry of Defence in 2018
- Additional units sold to Asian, Central and South American, and Western Governments in Q4 2018 and early 2019
- Deployed by Queensland Police at 2018 Commonwealth Games, and the Australian Defence Force at the 2018 ASEAN Summit

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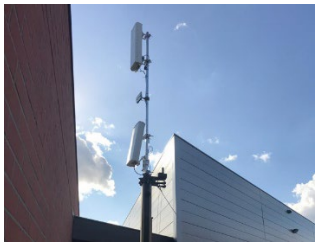


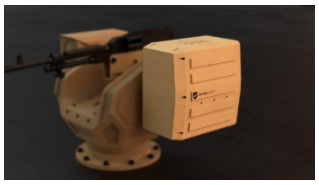
- Integrated detect-and-defeat system
- Includes radiofrequency direction finders, radars and cameras in a modular manner, with an integrated DroneCannon™ drone disruptor
- Utilises DroneShield's proprietary DroneShieldComplete™ counterdrone software engine
- Successfully deployed with the US military at U5G and AWG trials in 2018, with international sales in Central America and Europe

DroneSentry™



- Multi-sensor drone detection system
- Includes radiofrequency direction finders, radars and cameras in a modular manner
- Utilises DroneShield's proprietary DroneShieldComplete™ counterdrone software engine
- Successfully deployed with the US military at U5G and AWG trials in 2018, with initial international sales in Central America and Europe having taken place
- Deployed at the 2018 Olympic Winter Games

DroneSentinel™



- Drone disruptor module for a remote weapon station
- Allows for a layered response to a drone threat, starting with soft defeat / drone target freeze via DroneCannon, followed by utilisation of the primary kinetic weapon if required
- Released to market Q4 2018

DroneCannon RW™



- Covert portable drone disruptor
- Suitable for counterdrone protection at public gatherings and other similar situations
- Released to market Q4 2018

DroneNode™

Environment

The overall global demand for drone detection and mitigation products continued to rapidly increase through 2018 and into 2019, against the backdrop of a nearly daily barrage of news about drone threats.

Dozens of high-profile incidents and concerns took place during the year and subsequent to its end. One can read about some of these at https://www.droneshield.com/press-coverage and https://twitter.com/DroneShield.

In December 2019, multiple drone sightings forced the shutdown of Gatwick Airport for 48 hours (and then closing again due to further sightings), just days before Christmas. During the incident, labelled as economic terrorism, nearly 150,000 passengers were left stranded at the airport. The British Army was called in to manage the situation, however they were unable to use traditional kinetic weapons to stop the drones due to low visibility and the potential collateral damage to travellers. Police have been unable to track who carried out the attack. The Gatwick events, causing tens if not hundreds of millions of dollars in economic damage, have resulted in renewed calls for governments and civil infrastructure operators to invest in effective non-kinetic counter-drone measures. Experts believe that terrorist and criminal organizations will carry out similar attacks soon, as a clear vulnerability has been identified.

Dozens of other incidents involving drones and airplanes or helicopters, including a number of close calls have been recorded globally, with recent examples including:

- Drone sightings near Auckland Airport in New Zealand forced five planes into an extended holding pattern and led to the diversion of an international flight.
- A passenger jet with 126 people on board came within 50 feet of colliding with a drone over built-up London airspace.
- A firefighting helicopter in Australia was grounded by a consumer drone.
- A drone came within 20 meters of a plane carrying over 100 passengers taking off from Zurich Airport, which officials classified as a serious incident.
- A man was prosecuted under new UK drone laws for flying his drone underneath a police helicopter trying to find a missing person.
- Drones interrupted firefighting operations during the destructive Woolsey wildfires.

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- A UK RAF Tornado Jet traveling at 823 km/h came within 22m of hitting a farm drone.
- A drone flying over the Las Vegas strip put the pilots and passengers of helicopter tours at risk, prompting an FAA investigation.
- A rescue helicopter in New Zealand flying at an altitude of 400 metres came within 10 metres of a drone, forcing the pilot to take immediate evasive action.
- The number of drone incidents near airports in New Zealand increased to a record 420 in 2018, more than doubling since 2016.



Gatwick Airport shuts down for 48 hours due to drone sightings

Drones continued to be actively used by terrorists in the Middle East and elsewhere, resulting in continued priority being afforded by military forces worldwide to the counterdrone space.



Video: U.S. Defense Secretary James N. Mattis addresses the drone threat in the U.S. Congress

Venezuelan President Nicolas Maduro was reported to have been attacked on 4 August 2018 during a public address by two drones carrying C4 explosives. This was the first reported terrorist drone attack on a head of state.



Video: Drones carrying explosives attack Venezuelan President Nicolas Maduro on 4 August 2018

Drones continue to threaten militaries and public infrastructure. Governments around the world have begun acknowledging that cheap consumer drones provide terrorist and criminal groups with a powerful and inexpensive avenue to mount explosives or conduct surveillance. Relevant recent events include the following:

- ISIS-affiliated media group circulated a poster depicting a drone armed with explosives attacking the Eiffel Tower in Paris.
- Two people were arrested in Copenhagen for supplying drones to ISIS for use in combat.
- The US Military Academy issued a global alert about ISIS' drone weaponisation activities, which they believe have reached an advanced stage.
- President Trump signed the FAA Reauthorization Act, which allows US authorities to shoot down private drones which threaten security without a warrant.
- The Secretary of the Indian Department of Defence declared that drone threats will be a major challenge for their military in the future.
- A new law was introduced in the US which imposes a fine for drone pilots who use the drones to spy on or endanger the wellbeing of others.
- Councils in the UK have introduced policies banning the flying of drones in recreational areas.

Stories relating to the use of drones to smuggle drugs, weapons and cell phones into prisons and across state lines were frequently in the media:

- 15 people were sentenced for being part of a gang which used drones to smuggle half a million pounds worth of drugs into UK prisons across 55 drops.
- Police in Israel thwarted an attempt to use drones to smuggle cell phones into a high security prison.
- Two Australian men who used drones to smuggle contraband into a Queensland prison were sentenced to 18 months prison.
- A Canadian prison called for the government to implement drone detection systems, after illegal drugs, believed to be delivered by drones, were confiscated from inmates.
- Fifty-foot-high nets are being erected at prisons in Tennessee in an attempt to stem the flow of cell phones being delivered by drone.
- A woman and her daughter used an inexpensive consumer drone to smuggle contraband into a prison in Florida.
- A notorious hacker was charged with orchestrating a drone-smuggling ring from jail.

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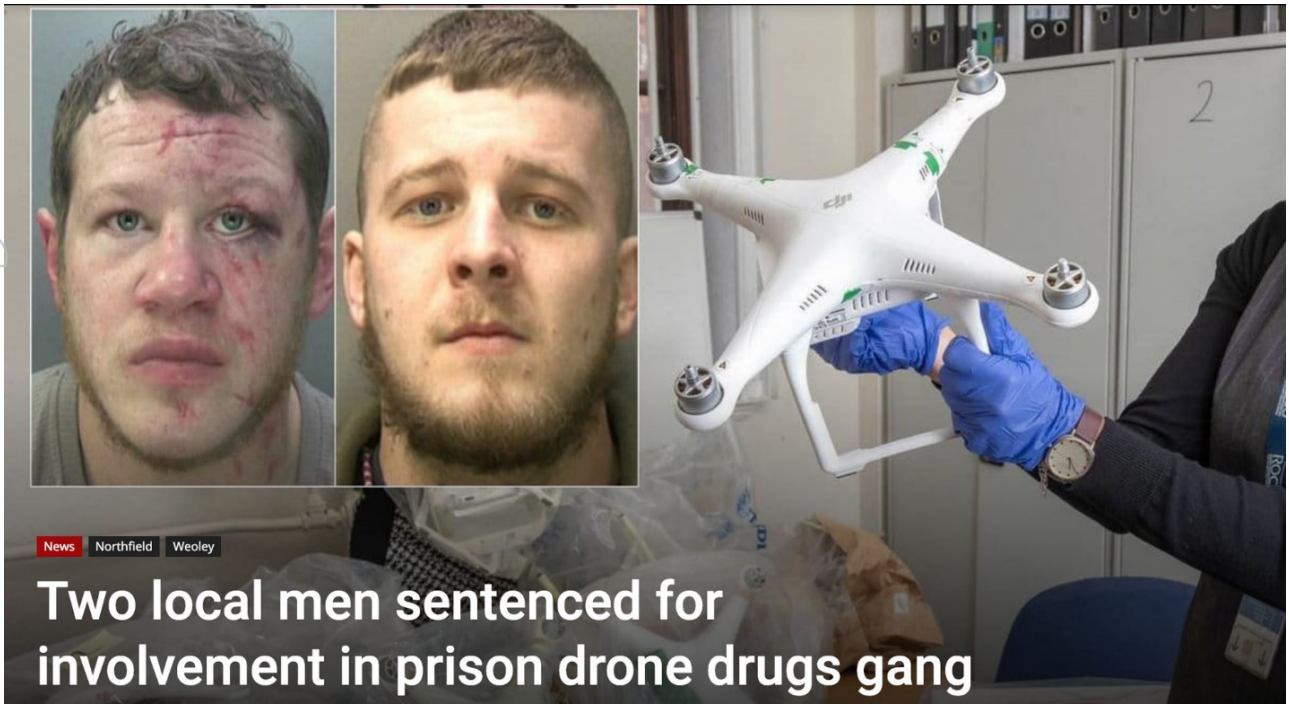

Two men sentenced for involvement in UK prison drone gang

Market Position

Through 2018, DroneShield has continued to demonstrate its track record of progression from product development to sales:

Product	Launch	Product Release	First Demo	First Sale	First Large Sale	Multiple Sales	Substantial Market Share
DroneGun™	Nov 2016	Dec 2016	Jan 2017	Nov 2017	$3.2m Jun 2018	Dec 2018	Being Secured. US$1.6bn market by 2023**
DroneSentinel™	Jul 2017	Sep 2017	Nov 2017	Mar 2018	Multiple Sales Being Advanced*		
DroneSentry™	Jul 2017	Oct 2017	Nov 2017	Sep 2018	Multiple Sales Being Advanced*	Dec 2018	

DroneShield believes that it is a leader in the drone security market for the following reasons.

- Most of the purported anti-drone products remain “vapourware” – products that have not progressed beyond an idea or a prototype. DroneShield is shipping products and has made early sales.
- DroneShield has a substantial marketing and distribution network in the industry.
- The Company is addressing what is believed to be a multibillion addressable market, with hundreds of thousands of potential user installations.

*Necessarily, not all (and there can be no assurance that any) of the Company’s sales opportunities will result in sales.

**https://www.marketsandmarkets.com/PressReleases/anti-drone.asp

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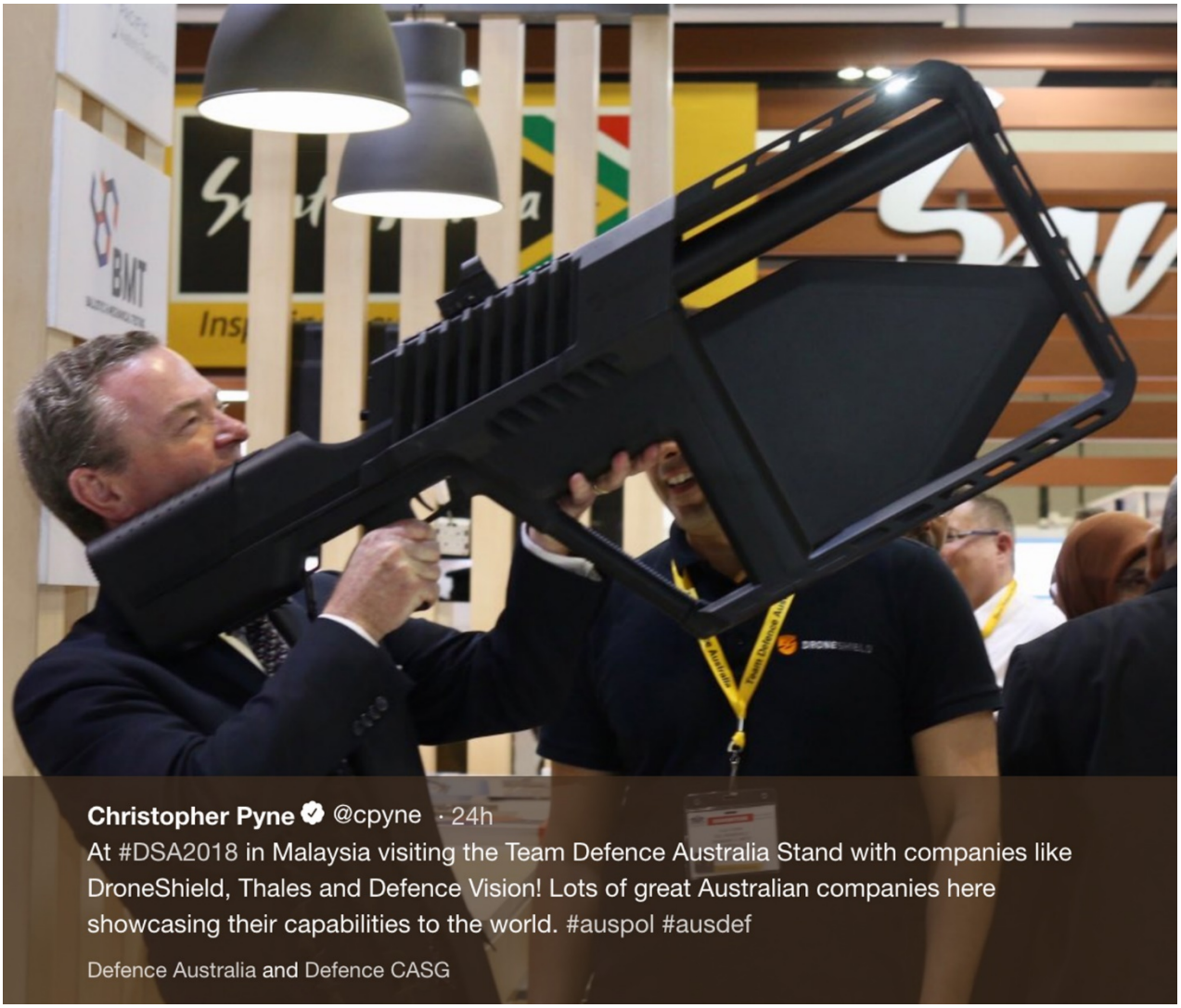
- DroneShield has made substantial sales, including a $3.2m Middle Eastern Ministry of Defence order for 70 DroneGun Tacticals™.

- DroneShield is one of the very few providers of both detection and countermeasures. DroneShield is believed to be the only provider of both detection and rifle-shaped "soft kill" countermeasures, which appeal to the military and the law enforcement markets. Most competing or purportedly competing products, prototypes and ideas provide detection or countermeasures but not both. The effectiveness of detection is limited without countermeasures, and countermeasures cannot be deployed in most circumstances without drones having first been detected.

- DroneShield's customers and potential customers favour the effectiveness of DroneShield's products. Its products are not time of day or season-dependent, do not rely on line of sight or visibility, are passive to the surrounding environment, and cover most major commercial drone models (including frequency hoppers).

- As DroneShield is an Australian company with meaningful U.S. operations, its origin is a positive factor in the decision-making process by allied country users, especially government users.

- DroneShield is prominently positioned as an Australian defence contractor, having been part of Team Defence Australia key global defence events, and having engaged in active dialogue with Australe and Centre for Defence Industry Capability (CDIC).



Hon. Christopher Pyne (Australian Minister for Defence) holding DroneGun Tactical at DSA 2018 exhibition

- DroneShield's products are materially cheaper than most competing detection products that are being marketed (particularly, systems being marketed by larger defence contractors) and are in fact capable of being delivered.

- Safety certifications further underpin the Company's position in government tenders.

Board of Directors and Executives



Peter James; Independent Non-Executive Chairman

Mr. James has over 30 years' experience in the Technology, Telecommunications and Media Industries, and has extensive experience as Chair, Non-Executive Director and Chief Executive Officer across a range of publicly listed and private companies. He is currently Chair of ASX-listed companies Macquarie Telecom, Aquabotix, Nearmap Limited, Dreamscape Networks Limited and Keytone Dairy Corporation Ltd.

Mr. James completed 12 years as a Non-Executive Director for ASX-listed iiNet; Australia's second largest DSL Internet Services Provider, chairing iiNet's Strategy and Innovation Committee. iiNet was acquired by TPG Telecom for $1,560,000,000.

Mr. James joined the Board of DroneShield on 1 April 2016, serving as Executive Chairman from 2 December 2016 to 24 January 2017. Mr. James is an experienced business leader with significant strategic and operational expertise. He is a Fellow of the Australian Institute of Company Directors, a Fellow of the Australian Computer Society and holds a BA degree with Majors in Computer Science and Business.



Oleg Vornik; CEO and Managing Director

Mr. Vornik is an experienced senior executive with investment banking and treasury experience at the Royal Bank of Canada, Leighton Contractors, Brookfield, Deutsche Bank and ABN AMRO.

Prior to becoming the CEO of DroneShield, Mr. Vornik was its Chief Financial Officer. His previous experience includes energy and industrials investment banking with the Sydney office of the Royal Bank of Canada as well as investment banking roles with Brookfield Asset Management, Deutsche Bank and ABN AMRO in Australia and New Zealand and the position of a Treasurer at Leighton Contractors. Mr. Vornik holds a BSc (Mathematics) and BCom (Hons) from University of Canterbury, New Zealand and has completed a business program with Columbia University in New York.

After co-leading the Company in the role of the Chief Financial Officer for over a year, Mr. Vornik was appointed as the CEO and Managing Director of DroneShield on 24 January 2017. Mr. Vornik does not hold any other public company directorships.



Bradley Buswell; Independent Non-Executive Director

Mr. Buswell has extensive experience leading businesses and U.S. government agencies in the defence and homeland security domains. He was president of the North American division of Rapiscan Systems, Inc., and Chief Executive Officer of Morpho Detection, Inc., both world leaders in state of the art security screening products, services and solutions.

Mr. Buswell also served at the U.S. Department of Homeland Security as the first Deputy Under Secretary for Science and Technology where he led the development of technologies in support of DHS operating components. He was the acting Undersecretary during the first year of the Obama administration. He also served over 20 years as a nuclear submarine officer in the U.S. Navy in a variety of assignments at sea and ashore.

Mr. Buswell graduated from the U.S. Naval Academy with a Bachelor of Science in Systems Engineering, and the George Washington University with a Master of Business Administration. Mr. Buswell does not hold any other public company directorships.



Robert Clisdell; Non-Executive Director

Mr. Clisdell is based in Sydney and is a Director at Brentridge Capital Ltd, an affiliate of the Company's largest shareholder. Previously, Mr. Clisdell worked in the middle market corporate advisory practice for Credit Suisse's Private Bank in Melbourne. Prior to Credit Suisse, Mr. Clisdell was an M&A banker with Caliburn Partnership (now Greenhill & Co.) in Sydney, and worked in Equity Capital Markets at Ord Minnett Corporate Finance.

Mr. Clisdell began his career with Arthur Anderson and qualified as a Chartered Accountant in 2005. He holds a Bachelor of Commerce from the University of Sydney and a Graduate Diploma in Applied Finance from FINSIA. Mr. Clisdell joined the Board of DroneShield on 24 January 2017. Mr. Clisdell is also a non-executive director of UUV Aquabotix Ltd (ASX:UUV) and Keytone Dairy Corporation Ltd (ASX:KTD).

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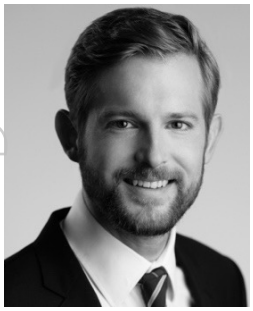


John Franklin; Chief Scientist (DroneShield LLC)

Mr. Franklin is one of DroneShield's co-founders. Mr. Franklin holds an MSc in Applied and Computational Math from John Hopkins University.

Previously, Mr. Franklin was a member of the research staff at the Air and Missile Defense Sector at Johns Hopkins University Applied Physics Laboratory, and Adjunct Research Associate (Science and Technology Division) at the Institute for Defense Analyses.



James Gatley; Chief Operating Officer

James joined DroneShield after a highly successful career with the Australian Army. This experience saw James complete 17 years service, with 12 years of this time spent serving within Special Operations. He completed 11 operational deployments and took part in active service globally. At the conclusion of his career in the Australian Defence Force, James managed a sales portfolio for a company that included Defence, Law Enforcement and Government clients within Australia. He has conducted high level Security and Risk training for various Government clients.

James holds Diplomas in Business, Project Management and Security and Risk Management. He also holds a GradCert in Terrorism and Security Studies.

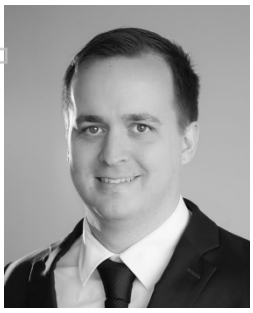


Dan Stamm; Chief Commercial Officer (DroneShield LLC)

Mr. Stamm is approaching two decades in the military defense industry. Starting his career as a mechanical engineer, he has excelled in defense technology development as he progressed through the roles of senior systems engineer, project manager, and program director at some of the United States' most renowned defense contractors.

Mr. Stamm is a leading expert in C-UAS systems, technologies, and products. He has been working in the field for more than five years and helped to define the commercial UAS countermeasure market. He has been engaged in all aspects of C-UAS technology ranging from concept creation to program management through business development.

Mr. Stamm has had the honor of working closely with some of the U.S.'s most elite Soldiers, Sailors, Airmen, and Marines through his work in the defense industry. He has four patents and multiple trade secrets for sophisticated defense technology, the details of which are often classified. He holds a Bachelor of Science degree from the Ohio State University and an MBA from Ohio University.



Dean Jagger; Company Secretary

Mr. Jagger works in the company secretarial division of Automic Group, a professional services company providing company secretarial, legal, registry and accounting services to Australian entities.

Mr. Jagger provides company secretarial and corporate compliance services to several listed public and private companies.

Mr. Jagger has 10 years' experience in the financial services sector.

Corporate Governance Statement

The board of the Company ("**Board**") recognises the importance of establishing a comprehensive system of control and accountability as the basis for the administration of corporate governance.

To the extent relevant and practical, the Company has adopted a corporate governance framework that is consistent with *The Corporate Governance Principles and Recommendations (3rd Edition)* as published by ASX Corporate Governance Council ("**Recommendations**").

The Board has adopted the following suite of corporate governance policies and procedures which are contained with the Company's **Corporate Governance Plan**, a copy of which is available on the Company's website at https://www.droneshield.com/investors .

- Board Charter
- Corporate Code of Conduct
- Public Sector Code of Conduct
- Audit and Risk Committee Charter
- Remuneration Committee Charter
- Nomination Committee Charter
- Continuous Disclosure Policy
- Risk Management Policy
- Remuneration Policy
- Trading Policy
- Diversity Policy
- Shareholder Communications Strategy
- Performance Evaluation Procedures
- Skills Matrix

The Board is committed to administering the policies and procedures with openness and integrity, pursuing the true spirit of corporate governance commensurate with the Company's needs.

The Company is pleased to report that its practices are largely consistent with the Recommendations of the ASX Corporate Governance Council and sets out below its compliance and departures from the Recommendations for the year ended 31 December 2018.

In the context of the Company's nature, scale and operations, the Board considers that the current corporate governance regime is an efficient, practical and cost-effective method of directing and managing the Company. As the Company's activities develop in size, nature and scope, the implementation of additional corporate governance policies and structures will be reviewed and considered.

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Principle 1: Lay solid foundations for management and oversight		
Recommendation 1.1 A listed entity should disclose: a) the respective roles and responsibilities of its board and management; and b) those matters expressly reserved to the board and those delegated to management.	YES	The Board is responsible for the corporate governance of the Company. The Company has adopted a Board Charter which sets out, amongst other things, the specific responsibilities of the Board, the roles and responsibilities of the Chairman, Board and management, as well as the matters expressly reserved for the decision of the Board and those delegated to management. A copy of the Company's Board Charter is contained in its Corporate Governance Plan which is available on the Company's website: https://www.droneshield.com/investors The Company is committed to the circulation of relevant materials to Directors in a timely manner to facilitate Directors' participation in Board discussions on a fully informed basis. The Company intends to regularly review the balance of responsibilities between the Board and management to ensure that the division of functions remains appropriate to the needs of the Company.

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PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Recommendation 1.2 A listed entity should: (a) undertake appropriate checks before appointing a person, or putting forward to security holders a candidate for election, as a Director; and (b) provide security holders with all material information relevant to a decision on whether or not to elect or re-elect a Director.	YES	(a) The Company's Corporate Governance Plan requires the Board to undertake appropriate checks as to the character, experience, education, criminal record and bankruptcy history of the candidate before appointing a person or putting forward to security holders a candidate for election, as a Director. (b) All material information relevant to a decision on whether to elect or re-elect a Director will be provided to security holders in any notice of meeting pursuant to which the resolution to elect or re-elect such Director will be voted on.
Recommendation 1.3 A listed entity should have a written agreement with each Director and senior executive setting out the terms of their appointment.	YES	Each Director and senior executive of the Company is party to a written agreement with the Company which sets out the terms and conditions of that Director's or senior executive's appointment.
Recommendation 1.4 The company secretary of a listed entity should be accountable directly to the board, through the chair, on all matters to do with the proper functioning of the board.	YES	The Board Charter outlines the role, responsibility and accountability of the Company Secretary. The Company Secretary is accountable directly to the Board, through the Chair, on all matters relating to the proper functioning of the Board. The Chairman and the Company Secretary co-ordinate the Board agenda.
Recommendation 1.5 A listed entity should: (a) have a diversity policy which includes requirements for the board or a relevant committee of the board: (i) to set measurable objectives for achieving gender diversity; and (ii) to assess annually both the objectives and the entity's progress in achieving them; (b) disclose that policy or a summary or it; and (c) disclose as at the end of each reporting period: (i) the measurable objectives for achieving gender diversity set by the board or a relevant committee of the board in accordance with the entity's diversity policy and its progress towards achieving them; and (ii) either: (A) the respective proportions of men and women on the board, in senior executive positions and across the whole organisation (including how the entity has defined "senior executive" for these purposes); or (B) if the entity is a "relevant employer" under the Workplace Gender Equality Act, the entity's most recent "Gender Equality Indicators", as defined in the Workplace Gender Equality Act 2012.	YES YES NO	(a) The Company has adopted a Diversity Policy which identifies gender diversity as a key area of focus for the Company. However, given the current size of the Company, the Board has determined that the benefits of the initiatives recommended by the ASX Corporate Governance Council in this regard are disproportionate to the costs involved in the implementation of such strategies. Accordingly, the Board has elected to adopt a tiered approach to the implementation of its Diversity Policy which is relative to the size of the Company and its workforce, such that: - Where the Company employs 20 or more employees, the Board will adopt practices in line with the Recommendations. - While the Company's workforce remains below this threshold, the Board will continue to drive the Company's diversity strategies on an informal basis and will apply the initiatives contained in the Diversity Policy to the extent that the Board considers relevant and necessary. (b) A copy of the Company's Diversity Policy is contained in its Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors (c) (i) As the Company did not employ 20 or more employees during the 2018 Financial Year, the Company did not formally define a set of measurable gender diversity objectives; (ii) During the reporting period (i.e. the year ended 31 December 2018), the respective proportions of men and women in the following roles were as follows:

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<table>
<tr><th>PRINCIPLES AND RECOMMENDATIONS</th><th>COMPLY (YES/NO)</th><th>EXPLANATION</th></tr>
<tr><td></td><td></td><td><table>
<tr><td></td><td>Men</td><td>Women</td></tr>
<tr><td>Board</td><td>100%</td><td>0%</td></tr>
<tr><td>Senior executives</td><td>85%</td><td>15%</td></tr>
<tr><td>Across the whole organisation</td><td>87%</td><td>13%</td></tr>
</table></td></tr>
<tr><td>Recommendation 1.6
A listed entity should:
(a) have and disclose a process for periodically evaluating the performance of the board, its committees and individual Directors; and
(b) disclose in relation to each reporting period, whether a performance evaluation was undertaken in the reporting period in accordance with that process.</td><td>YES

YES</td><td>(a) The performance of the Board as a group and of individual Directors will be assessed each year for all future years. The Remuneration Committee (the function of which is currently performed by the full Board) is responsible for evaluating the performance of the Board and individual Directors on an annual basis. The process for this is set out in the Company's Performance Evaluation Procedures policy which is contained in its Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.
(b) The Board undertook an evaluation of Board performance in 2018.</td></tr>
<tr><td>Recommendation 1.7
A listed entity should:
(a) have and disclose a process for periodically evaluating the performance of its senior executives; and
(b) disclose in relation to each reporting period, whether a performance evaluation was undertaken in the reporting period in accordance with that process.</td><td>YES

YES</td><td>(a) The Managing Director of the Company is responsible for evaluating the performance of senior executives on an annual basis. The process for this is set out in the Company's Performance Evaluation Procedures policy which is contained in its Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.
(b) A formal performance evaluation of senior executives was undertaken during the 2018 financial year.</td></tr>
<tr><td colspan="3">Principle 2: Structure the board to add value</td></tr>
<tr><td>Recommendation 2.1
The board of a listed entity should:
have a nomination committee which:
(i) has at least three members, a majority of whom are independent Directors; and
(ii) is chaired by an independent Director,
and disclose:
(iii) the charter of the committee;
(iv) the members of the committee; and
(v) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or
if it does not have a nomination committee, disclose that fact and the processes it employs to address board succession issues and to ensure that the board has the appropriate balance of</td><td>NO

NO

NO
NO

N/A

YES</td><td>Due to its size, the Board has determined that the function of the Nomination Committee is most efficiently carried out with full Board participation and accordingly, the Board has elected not to establish a separate Nomination Committee at this stage.
As a result, the duties that would ordinarily be assigned to the Nomination Committee under the Nomination Committee Charter are carried out by the full Board.
A copy of the Nomination Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.
The Board devotes time at Board meetings on at least an annual basis to discuss Board succession issues. Where appropriate, all members of the Board are involved in the Company's nomination process, to the maximum extent permitted under the Corporations Act and ASX Listing Rules.
The Board also conducts an annual review of the Company's Board Skills Matrix (in accordance with Recommendation 2.2) to ensure the Board maintains</td></tr>
</table>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
skills, experience, independence and knowledge of the entity to enable it to discharge its duties and responsibilities effectively.		an appropriate balance of skills, experience, independence and knowledge to discharge its duties and responsibilities effectively.
Recommendation 2.2 A listed entity should have and disclose a board skill matrix setting out the mix of skills and diversity that the board currently has or is looking to achieve in its membership.	YES	The Board of the Company is comprised of Directors with a broad range of technical, commercial, financial and other skills, experience and knowledge relevant to overseeing the business of a drone security company. The Company had developed a Board Skills Matrix which is used as a tool to assess the appropriate and ideal balance of skills, experience, independence and diversity necessary for the Board to discharge its duties and responsibilities effectively. A summary of the collective skills, experience, independence and diversity of the Board is set in Annexure C of the Company's Corporate Governance Plan which is available on the Company's website: https://www.droneshield.com/investors.
Recommendation 2.3 A listed entity should disclose: (a) the names of the Directors considered by the board to be independent Directors; (b) if a Director has an interest, position, association or relationship of the type described in Box 2.3 of the ASX Corporate Governance Principles and Recommendation (3rd Edition), but the board is of the opinion that it does not compromise the independence of the Director, the nature of the interest, position, association or relationship in question and an explanation of why the board is of that opinion; and (c) the length of service of each Director	YES	(a) During the 2018 financial year, the Independent Directors of the Company were: - Mr. Peter James (Non-Executive Chairman); and - Mr. Bradley Buswell (Non-Executive Director). Mr. Oleg Vornik, the Managing Director, was not considered to be independent during his tenure due to his executive role as Managing Director of the Company. (b) The Board has determined the independence of each of the Company's Directors in line with the guidance set out by the ASX's Corporate Governance Council and have not formed an opinion contrary to those guidelines. (c) The Directors who held office during and after the 2018 financial year have served continuously since their respective dates of appointment unless otherwise noted below: - Mr. Peter James: appointed 1 April 2016; - Mr. Oleg Vornik: appointed 24 January 2017; - Mr. Robert Clisdell: appointed 24 January 2017; and - Mr. Bradley Buswell; appointed 29 December 2017.
Recommendation 2.4 A majority of the board of a listed entity should be Independent Directors.	NO	The Board Charter requires that where practical the majority of the Board will be independent. During the 2018 financial year, the following two of the Company's four Directors were considered to be Independent Directors: - Mr. Peter James (Non-Executive Chairman); and - Mr. Bradley Buswell (Non-Executive Director).
Recommendation 2.5 The chair of the board of a listed entity should be an Independent Director and, in particular, should not be the same person as the CEO of the entity.	YES	The Chairman, Mr. Peter James is an Independent Non-Executive Director and is not the same person as the Managing Director of the Company.

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PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Recommendation 2.6 A listed entity should have a program for inducting new Directors and providing appropriate professional development opportunities for continuing Directors to develop and maintain the skills and knowledge needed to perform their role as a Director effectively.	YES	The Company's program for the induction of new Directors is tailored for each new Director (depending on their personal requirements, background skills, qualifications and experience) and includes the provision of a formal letter of appointment and an induction package containing sufficient information to allow the new Director to gain an understanding of the business of the Company, and the roles, duties and responsibilities of Directors and the Executive team. All Directors are encouraged to undergo continual professional development and, subject to prior approval by the Chairman, all Directors may have access to various resources and professional development training to address any skills gaps.
Principle 3: Act ethically and responsibly		
Recommendation 3.1 A listed entity should: (a) have a code of conduct for its Directors, senior executives and employees; and disclose that code or a summary of it.	YES	(a) The Company has adopted a Corporate Code of Conduct which applies to Directors, employees and contractors of the Company. The Corporate Code of Conduct is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.
Principle 4: Safeguard integrity in corporate reporting		
Recommendation 4.1 The board of a listed entity should: have an audit committee which: (i) has at least three members, all of whom are Non-Executive Directors and a majority of whom are Independent Directors; and (ii) is chaired by an Independent Director, who is not the chair of the board, and disclose: (iii) the charter of the committee; (iv) the relevant qualifications and experience of the members of the committee; and (v) in relation to each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or if it does not have an audit committee, disclose that fact and the processes it employs that independently verify and safeguard the integrity of its financial reporting, including the processes for the appointment and removal of the external auditor and the rotation of the audit engagement partner.	NO NO NO YES N/A N/A YES	Due to the current size of the Company, the Board has determined that the function of the Audit and Risk Committee is most efficiently carried out with full Board participation and accordingly, the Company has elected not to establish a separate Audit and Risk Committee at this stage. As a result, the duties that would ordinarily be assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter are carried out by the full board. The Audit and Risk Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors. The Board devotes time on at least an annual basis to consider the robustness of the various internal control systems it has in place to safeguard the integrity of the Company's financial reporting. In addition, following the completion of each half year review and annual audit review, the Company's external auditors confer with the Board on any matters identified during the course of the audit that have the potential to increase the Company's exposure to risks of material misstatements in its financial reports. The full Board also assumes responsibility for recommendations to security holders on the appointment and removal of the external auditor. Audit partner rotations will be enforced in accordance with the relevant guidelines.
Recommendation 4.2 The board of a listed entity should, before it approves the entity's financial statements for a financial period, receive from its CEO and CFO a declaration that the financial records of the entity have been properly maintained and that the	YES	Prior to the execution of the financial statements of the Company, the Company's Managing Director and Finance Manager provide the Board with written assurances that the financial records of the Company have been properly maintained and that the financial statements comply with the appropriate accounting

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.		standards and give a true and fair view of the financial position and performance of the Company and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively in all material aspects.
Recommendation 4.3 A listed entity that has an AGM should ensure that its external auditor attends its AGM and is available to answer questions from security holders relevant to the audit.	YES	An external auditor will be present at the Company's Annual General Meeting ("AGM") and be available to answer questions from security holders relevant to the audit.
Principle 5: Make timely and balanced disclosure		
Recommendation 5.1 A listed entity should: - have a written policy for complying with its continuous disclosure obligations under the Listing Rules; and - disclose that policy or a summary of it.	YES	- The Company has adopted a Continuous Disclosure Policy which details the processes and procedures which have been adopted by the Company to ensure that it complies with its continuous disclosure obligations as required under the ASX Listing Rules and other relevant legislation. - The Company's Continuous Disclosure Policy is contained within the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.
Principle 6: *Respect the rights of security holders*		
Recommendation 6.1 A listed entity should provide information about itself and its governance to investors via its website.	YES	Shareholders can access information about the Company and its governance (including its constitution and adopted corporate governance policies) from the Company's website https://www.droneshield.com/investors. The Company will regularly update the website and contents therein as deemed necessary.
Recommendation 6.2 A listed entity should design and implement an investor relations program to facilitate effective two-way communication with investors.	YES	The Company has adopted a Shareholder Communications Strategy which aims to promote and facilitate effective two-way communication with investors. The Strategy outlines a range of ways in which information is communicated to Shareholders, including via its website, through announcements released to the ASX, its annual report and general meetings. Shareholders are also welcome to contact the Company or its registrar, Automic Registry Services, via email or telephone. The Company's Shareholder Communications Strategy is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.
Recommendation 6.3 A listed entity should disclose the policies and processes it has in place to facilitate and encourage participation at meetings of security holders.	YES	As noted above, the Company's Shareholder Communications Strategy is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors. Shareholders will be encouraged to participate at all general meetings of the Company by written statement contained in every Notice of Meeting sent to shareholders prior to each meeting.

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PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
		The Company intends to accommodate shareholders who are unable to attend general meetings in person by accepting votes by proxy. Further, any material presented to shareholders at the meeting will be released to the ASX immediately prior to the commencement of the meeting for the benefit of those shareholders who are unable to attend in person. The Company will also announce to the ASX the outcome of each meeting immediately following its conclusion. At each general meeting, shareholders will be given an opportunity to ask questions in relation to the resolutions put to shareholders at that meeting, and in respect of the Company's business and operations generally. At each AGM, shareholders will also be invited by the Chairman to ask questions of the Company's external auditor and the Board in relation to the annual financial report of the Company and the conduct of the audit.
Recommendation 6.4 A listed entity should give security holders the option to receive communications from, and send communications to, the entity and its security registry electronically.	YES	Shareholders have the option of electing to receive all shareholder communications by e-mail and can update their communication preferences with the Company's registrar, Automic Registry Services, at any time. Security holders can also register with the Company at info@droneshield.com to receive email notifications following the release of a material announcement to the ASX.
Principle 7: Recognise and manage risk		
Recommendation 7.1 The board of a listed entity should: have a committee or committees to oversee risk, each of which: (i) has at least three members, a majority of whom are Independent Directors; and (ii) is chaired by an Independent Director, and disclose: (iii) the charter of the committee; (iv) the members of the committee; and (v) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or if it does not have a risk committee or committees that satisfy (a) above, disclose that fact and the process it employs for overseeing the entity's risk management framework.	NO NO NO YES N/A N/A YES	Due to its size, the Board has determined that the function of the Audit and Risk Committee is most efficiently carried out with full Board participation and accordingly, the Company has elected not to establish a separate Audit and Risk Committee at this stage. As a result, the duties that would ordinarily be assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter are carried out by the full Board. The Audit and Risk Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors. The Board devotes time on at least an annual basis to fulfil the roles and responsibilities associated with overseeing risk and maintaining the Company's risk management framework and associated internal compliance and control procedures.
Recommendation 7.2 The board or a committee of the board should: review the entity's risk management framework with management at least annually to satisfy itself that it continues to be sound, to determine whether there have been any changes in the material business risks the entity faces and to ensure that they remain within the risk appetite set by the board; and	YES	During the 2018 financial year, the Board, in carrying out the duties typically assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter, undertook a formal review the Company's risk management framework in line with its Risk Management Policy.

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
disclose in relation to each reporting period, whether such a review has taken place.		
Recommendation 7.3 A listed entity should disclose: if it has an internal audit function, how the function is structured and what role it performs; or if it does not have an internal audit function, that fact and the processes it employs for evaluating and continually improving the effectiveness of its risk management and internal control processes.	NO YES	Due to the current size of the Company and the manageable scale of its operations, the Board, in carrying out the duties typically assigned to the Audit & Risk Committee under the Audit & Risk Committee Charter, have determined that the Company's existing risk management processes and internal controls are sufficiently robust and as such, no internal audit committee is required at this stage.
Recommendation 7.4 A listed entity should disclose whether, and if so how, it has regard to economic, environmental and social sustainability risks and, if it does, how it manages or intends to manage those risks.	YES	The Company's Risk Management Policy details the Company's risk management systems which assist in identifying and managing potential or apparent business, economic, environmental and social sustainability risks (where appropriate). During the 2018 financial year, the Company undertook a formal review of the Company's risk management framework, which included an assessment of the Company's exposure to economic, environmental and social sustainability risks. The Board was satisfied with the effectiveness of the Company's risk management framework and associated internal compliance and control procedures that are in place to eliminate, mitigate or otherwise manage the Company's exposure to such risks. All material risks are announced to the market, in accordance with the requirements of the ASX listing rules and otherwise.
Principle 8: Remunerate fairly and responsibly		
Recommendation 8.1 The board of a listed entity should: have a remuneration committee which: (i) has at least three members, a majority of whom are Independent Directors; and (ii) is chaired by an Independent Director, and disclose: (iii) the charter of the committee; (iv) the members of the committee; and (v) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or if it does not have a remuneration committee, disclose that fact and the processes it employs for setting the level and composition of remuneration for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive.	NO NO YES N/A N/A YES	Due to the size of the Board and the scale of the Company's operations, the Board have determined that the function of the Remuneration Committee is most efficiently carried out with full Board participation (to the extent permitted under the Corporations Act and ASX Listing Rules), and accordingly has elected not to establish a separate Remuneration Committee at this stage. As a result, the duties that would ordinarily be assigned to the Remuneration Committee under the Remuneration Committee Charter are carried out by the full Board. The Remuneration Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors. The Board devotes time on at least an annual basis to fulfil the roles and responsibilities associated with setting the level and composition of remuneration for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive.
Recommendation 8.2 A listed entity should separately disclose its policies and practices regarding the remuneration of Non-Executive Directors and the remuneration of Executive Directors and other Senior Executives and ensure that the different	YES	The Company's general policies and practices regarding the remuneration of Non-Executive and Executive Directors and other senior employees are set out in the Remuneration Policy which is contained in the Company's Corporate Governance

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PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
roles and responsibilities of Non-Executive Directors compared to Executive Directors and other Senior Executives are reflected in the level and composition of their remuneration.		Plan which is available on the Company's website https://www.droneshield.com/investors. Further information regarding the remuneration practices of the Company is contained in the Remuneration Report section of the Company's 2018 Annual Report.
Recommendation 8.3 A listed entity which has an equity-based remuneration scheme should: (i) have a policy on whether participants are permitted to enter into transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme; and (ii) disclose that policy or a summary of it.	YES	The Company's Remuneration Committee (the function of which is currently performed by the full Board) is responsible for the review and approval of any equity-based remuneration schemes offered to Directors and Employees of the Company. Further, in accordance with the Remuneration Committee Charter, the Remuneration Committee (the function of which is currently performed by the full Board) is also responsible for granting permission, on a case by case basis, for scheme participants to enter transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme. During the 2018 financial year, the Board of the Company authorised the issue of securities to Directors and employees under its shareholder approved Incentive Option Plan. To date, no participant to the Incentive Option Plan has sought (or been granted) approval to enter in to transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme. The Company's policy in this regard is set out the Company's Remuneration Committee Charter, a copy of which is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors. The Company also has a Securities Trading Policy that prohibits Directors, Officers and employees from entering into transactions or arrangements which limits the economic risk of participating in unvested entitlements under any equity-based remuneration scheme. A copy of the Securities Trading Policy is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.

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Directors' Report

Your Directors present their report for DroneShield Limited (the "Company") and its controlled entities ("the Group") for the year ended 31 December 2018.

Directors

The names of the Company's Directors in office during the year and until the date of this report are set out below. Directors were in office for this entire period unless otherwise stated. Details of the current members of the Board, including their experience, qualifications, special responsibilities and term of office are included on page 11 of the Annual Report.

Name	Position	Effective date
Directors		
Peter James	Independent Non-Executive Chairman	Executive Chairman until 24 January 2017 Returned to Independent Non-Executive Chairman 24 January 2017
Oleg Vornik	Executive Director, CEO and Managing Director	Appointed as CEO and Managing Director 24 January 2017
Robert Clisdell	Non-Executive Director	Appointed 24 January 2017
Bradley Buswell	Independent Non-Executive Director	Appointed 29 December 2017

Meetings of Directors

Name	Meetings eligible to attend	Meetings attended
Directors		
Peter James	12	12
Robert Clisdell	12	11
Bradley Buswell	12	12
Oleg Vornik	12	12

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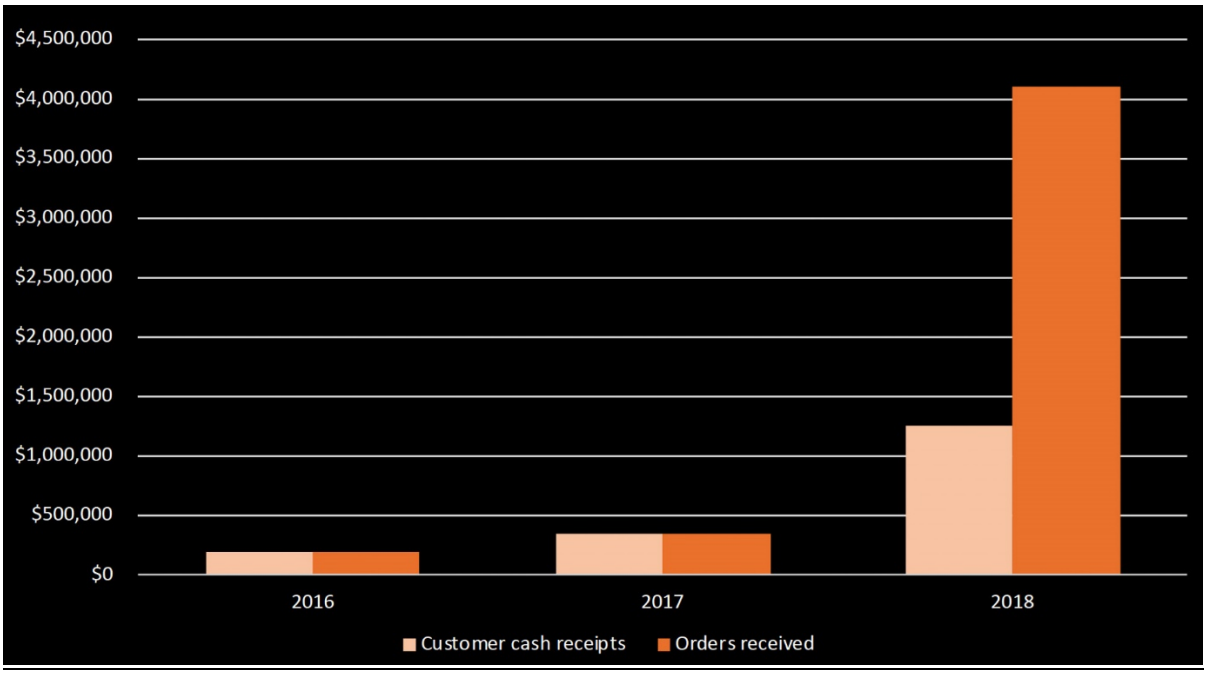
- ***DroneShield's total customer cash receipts for the calendar 2018 were $1,252,123, the Company's highest annual cash receipts to date.***

  - ***Of that amount, close to half ($489,209) was received during the most recent (31 December 2018) quarter, with DroneShield producing its highest quarterly cash inflows to date in that most recent quarter.***

- ***DroneShield's revenue from sales for the 2018 calendar / financial year were $953,857 (as opposed to the slightly higher cash receipts referenced above). That is a 207% increase in the year on year revenue (the 2017 revenue was $310,724).***



DroneShield's growing customer cash receipts and revenues

The net loss after tax for the year was $6,336,100, an increase of 16% relative to the 2017 loss of $5,476,613. That is, in 2018, DroneShield was able to substantially scale up its research and development (R&D) and sales and marketing activities, secure initial sizable orders for its products, and generate its first meaningful revenues, which were over three times higher than those in the previous year, with only a marginal increase in its net loss for the year. Importantly, $1,124,193 of the loss related to non-cash share-based payments.

During 2018, the Company undertook a $2.55m Placement in March and a $1.7m Placement and SPP in November. The Company also established a $1.855m non-convertible credit facility in October 2018 (undrawn to date). In February 2019, the Company has raised a $1.3m Placement.

No Board changes took place through 2018. Alistair McKeough of Automic Group was replaced as company secretary by Dean Jagger, also of Automic Group, in April 2018.

Following the release of DroneGun MKII™ in mid 2017, in response to end-user requirements, in January 2018, the Company launched DroneGun Tactical™. Both DroneGun MKII™ and DroneGun Tactical™ are innovative portable rifle-shaped drone disruptors, covering a broad range of tactical environments and uses. DroneGun Tactical™ represents a break-through in the product segment for tactical forward deployments, as it contains no backpack.

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Review of Operations and Financial Results *continued*

DroneShield achieved a number of important testing, compliance and certification milestones through the year, including:

- DroneGun MKII™ was assigned a NATO Stock Number ("NSN") in February 2018, with DroneGun Tactical™ having received an NSN in February 2019. An NSN is a 13-digit numeric code, identifying all the "standardised material items of supply" as they have been recognised by all NATO countries including the United States Department of Defense, and allows for any each of the 29 NATO militaries to purchase DroneGun MKII™ on a "military catalogue" basis, significantly simplifying the procurement process. The NSN was assigned following a request for such assignment from the United States Department of Defense.
- The United States Defense Logistics Agency, the logistics combat support agency of the United States Department of Defense, certified DroneShield's subsidiary DroneShield LLC under the United States / Canada Joint Certification Program DD2345 (militarily critical technical data agreement). With this certification, DroneShield LLC has established eligibility to access unclassified export-controlled technical data of the U.S. Department of Defense (DOD) and Canada's Department of National Defence (DND). DroneShield LLC's certification under this program is part of its participation in the U.S. DOD and Canadian DND procurement processes.
- The Company's products were placed on the United States' General Services Administration ("GSA") Schedule, allowing for an easier procurement by a number of US Government Agencies.
- Certification of DroneGun Tactical™ as compliant for human exposure - OneTech, a specialist SAR (Specific Absorption Rate) laboratory for global certifications, certified the product as compliant with the ARPANSA EN 50566 and EN 50663 (Australian and New Zealand Communications and Media Authority requirements for human exposure to radio frequencies) within the specific frequency bands of operation which cross references to the international ICNIRP standard. The certification was obtained in response to the DroneGun Tactical™ product advancing through procurement processes with a number of major defence and other government agencies internationally, for which this was a requirement requested by several agencies.
- The DroneSentry™ product was awarded an airport compliance certification in May 2018. The airport compliance independent certification was performed by 360°RF, a US based specialised radiofrequency testing laboratory, as compatible (that is not interfering) with the most commonly utilised communications and navigation systems employed in the United States aviation/airport environment. RfOne™ and RadarZero™, core modules within DroneShield's DroneSentinel™ detection system, have been assessed as creating no increase in background EMI when operational, measured across a wide range of aviation frequency bands used by airports and aircraft. DroneCannon™, the drone mitigation element of DroneShield's DroneSentry™ system, has been determined to operate strictly within the advertised bands. In the non-GPS mode, these ranges are outside of aviation frequency bands.

The Company also continued to improve its DroneSentinel™ and DroneSentry™ systems throughout 2018. DroneSentinel™ is a unique modular drone detection system incorporating radar, radiofrequency, and thermal and optical camera sensors. All of the detection components of DroneSentinel™ are also available as standalone products. DroneSentry™ is a detect-and-defeat product, which incorporates all of these detection capabilities and pairs them up with a jamming capability. These products are effective against both individual drones, and swarms. The developments during the year included releasing the next generation of the DroneShieldComplete™ software engine for the two systems, and the addition of revolutionary RadarZero™ compact radar. DroneShield also released DroneCannon RW™ (a drone disruptor for remote weapon stations) and DroneNode™ (a portable covert drone disruptor).



DroneShield's DroneNode™

DroneShield also made significant sale and marketing progress during the year. It closed the largest known industry order globally of portable drone mitigation equipment, a 70 DroneGun Tactical™ sale for use by a Middle Eastern Ministry of Defence, in mid-2018, in addition to other sales and deployments across its product range, including:

- a DroneSentinel™ deployment at the 2018 Olympic Winter Games,
- a DroneGun™ deployment at the 2018 Commonwealth Games in Gold Coast by the Queensland Police, following a substantial evaluation by the Australian military,
- a DroneGun™ deployment by the Australian Defence Force at the 2018 ASEAN Summit in Sydney,
- a DroneSentry™ purchase for use by a Central American government agency,
- a purchase of DroneGuns™ for use by a major Asian government agency,
- a purchase of DroneGuns™ for use by a major Western government agency, and
- a purchase of DroneGuns™ for use by a Paraguay government agency.

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Review of Operations and Financial Results *continued*



DroneGun Tactical™

DroneShield has a significant sales pipeline. It is participating in a number of trials and procurement processes across military, law enforcement and critical infrastructure customers in the United States, Australia, NATO countries and elsewhere. Its pipeline includes active engagement with dozens of potential end-users, with the size of each potential order ranging between hundreds of thousands of dollars and tens of millions of dollars[2].

Key trials in 2018 included:

- In March 2018, the Company participated in the 2018 Urban 5th Generation Marine Exploration and Experimentation Exercise (U5G) at Marine Corps Base Camp Pendleton, San Diego, California. U5G is organised by the United States Marine Corps Deputy Commandant for Combat Development & Integration ("CD&I") and the Deputy Assistant Secretary of the Navy for Research, Development, Test and Evaluation ("NR&DE"). The event focused on evaluating new technologies by the United States Marines, for subsequent acquisition and deployment considerations.
- In November 2018, DroneShield announced its participation in The British Army's Army Warfighting Experiment (Autonomous Warrior) 2018. In the four-week exercise, British soldiers tested and evaluated the effectiveness of robotic and autonomous systems (RAS) on the battlefield. The exercise was the result of a large-scale collaboration between the British Army, the Royal Navy, the Royal Air Force, the United States Army, the UK Ministry of Defence, the UK Defence Science and Technology Laboratory and the industry participants who were invited to participate. DroneShield was invited to participate in the exercise and is providing its DroneSentinel™ system to the British Army as a rapidly deployable, counterdrone system to enable troops to detect and defend against hostile drones.
- In December 2018, DroneShield announced that the U.S. Department of Defense Asymmetric Warfare Group at Fort A.P. Hill, Virginia evaluated DroneShield's products DroneSentry™ and DroneGun Tactical™ at an event facilitated by the Army Night Vision Electronic Sensors Directorate (NVESD) Unique Mission Cell (UMC). DroneShield's successful deployment at that event included:
    - participation in seven experimental scenarios,
    - detection and tracking of multiple UAVs (unmanned aerial vehicles) via combined radiofrequency (RF) and radar detection of DroneShield's DroneSentry™ platform;
    - provision of real-time battlefield intelligence of mock-threat drones to fielded experimental participants through TAK/ATAK integration (ATAK, or Android Tactical Assault Kit, is a major software platform used by the U.S. military); and
    - enabling the "Blue Force" (friendly forces) command to negate mock-threat drones through the use of our DroneGun Tactical™ and DroneCannon™ systems.

In addition to sales and other deployments, DroneShield achieved two key partnerships during the year:

- In December 2018, DroneShield entered into a teaming agreement with Zain Group (KWSE:ZAIN) ("Zain") in relation to deploying DroneShield products in the Middle East. Zain is a leading Middle Eastern mobile and data services operator headquartered in Kuwait, with substantial operations across a number of Middle Eastern countries, a workforce of over 6,000, over 47 million active individual, business and governmental customers, and a market capitalisation of approximately US$7 billion. Zain has acquired DroneShield's equipment at the time of starting the partnership.

- Also, in December 2018, DroneShield entered into a teaming agreement with Thales Programas De Electronica Y Comunicaciones S.A.U. ("Thales") (a Spanish subsidiary of Thales S.A. (ENXTPA:HO)), whereby Thales will utilise and promote DroneShield's products in its defence and security contract bids in Spain involving counterdrone aspects. Thales S.A. is one of the largest defence companies globally, with 65,000 employees, operations in 56 countries and a market capitalisation of approximately €15.8 billion. Thales in Spain combines its technology with the experience of 1,200 professionals distributed in 11 work centres in Spain, one in Turkey and one in Egypt.

- The Company continued its active engagement with the Australian and the United States governments, and recently applied for several high-value R&D grants in both countries. It received its first R&D Tax Incentive Grant from the Australian Government in mid 2018 for the 2017 activities, and expects to receive its second Grant shortly, covering the 2018 year.

[2] Not all (and there can be no assurance that any) of these sales opportunities will result in sales.

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Review of Operations and Financial Results *continued*

DroneShield was also selected to be a part of Team Defence Australia (TDA) for the high profile Eurosatori (Paris), AUSA (Washington DC) and DSA (Kuala Lumpur) military exhibitions. TDA is a joint effort with the Australian Department of Defence and Austrade.



DroneShield's exhibit at the Team Defence Australia stand at Eurosatory exhibition in Paris

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Review of Operations and Financial Results *continued*

The Company continues to work with its third-party partners across its sales partner network in approximately 50 countries, as well as its R&D and manufacturing partners to complement its in-house team, optimising its capital expenditure.

DroneShield continues to attract a significant amount of media interest globally, including coverage by Channel 7 and Commsec TV, ABC and 2GB radio and Australian Financial Review in Australia; and The Wall Street Journal, Forbes and other major publications in the US and the UK.



Video: DroneShield chairman Peter James discussing drone threat on ABC News

Principal Activities

The principal activity of the Company is the development, commercialisation and sales of hardware and software technology for drone detection and security.

Significant Changes in the State of Affairs

Other than discussed in the Review of Operations above, there have been no significant changes in the state of affairs of the Company during the year ended 31 December 2018.

Significant Events after the Balance Date

Subsequent to 31 December 2018, the following occurred;

- In January 2019, the Company issued 11,301,700 shares in a Share Placement. The issue price was $0.115, and the total cash received from the placement of shares was $1,299,696. Under the terms of the Placement, brokers participating in the Placement will receive a commission on the funds raised, as well as an aggregate of 2,825,425 unlisted Class O options which expire on 21 February 2021 with an exercise price of $0.22.
- The Company entered into an agreement to sublease an office in Sydney for $148,144 per annum, commencing 18 February 2019 and ending 31 March 2020.

No other matter or circumstance has arisen since 31 December 2018 which has significantly affected or may significantly affect:

- The Group's operations in future financial years; or
- The results of those operations in future financial years; or
- The Group's state of affairs in future financial years.

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Review of Operations and Financial Results *continued*

Likely developments and expected results of operations

Refer to the Chairman's Review to shareholders, on pages 3 to 4, for further information on likely developments and expected results of the Group.

Environmental regulation

The Group's operations are not subject to any significant environmental regulation under either Commonwealth or State legislation. The Board considers that adequate systems are in place to manage the Group's obligations and is not aware of any breach of environmental requirements as they relate to the Group.

Dividends

No dividends were declared or paid to shareholders during the financial year (2017: $nil)

Insurance of officers

During or since the end of the financial year the Company has paid, or agreed to pay, premiums to insure persons who are, or have been, an officer of the Company, or any past, present or future Director or officer of the Company. The contracts prohibit disclosure of the amount of the premium paid. The liabilities insured include costs and expenses that may be incurred in defending civil or criminal proceedings that may be brought against the officers in their capacity as officers of entities in the Group.

Proceedings on behalf of the Company

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Group, or to intervene in any proceedings to which the Group is party, for the purpose of taking responsibility on behalf of the Group for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Group with leave of the Court under section 237 of the *Corporations Act 2001*.

Non-audit services

The Company may decide to employ the auditor on assignments additional to their statutory audit duties where the auditor's expertise and experience with the Company and/or the Group are important.

Details of the amounts paid or payable to the auditor (HLB Mann Judd Assurance (NSW) Pty Ltd) for audit and non-audit services provided during the year are outlined in Note 24 to the financial statements.

The Board of Directors has considered the position and is satisfied that the provision of non-audit services is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The Directors are satisfied that the provision of non-audit services provided by the auditor did not compromise the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services have been reviewed by the Board to ensure they do not impact the objectives and impartiality of the auditor;
- none of the services undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*, including review or auditing the auditor's own work, acting in a management or decision-making capacity for the Group, acting as advocate for the Group or jointly sharing economic risks and rewards.

Auditor's Independence Declaration

A copy of the auditor's independence declaration as required under the Section 307C of the *Corporations Act 2001* is set out on page 37.

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Directors' Report- Remuneration Report (audited)

Executive remuneration governance

The Board reviews and approves the remuneration policy to enable the Company to attract and retain executives and Directors who will create value for shareholders having consideration to the amount deemed to be commensurate for a company of its size and level of activity as well as the relevant Directors' time, commitment and responsibility. The Board is also responsible for reviewing any employee incentive and equity-based plans including the appropriateness of performance hurdles and total payments proposed.

Remuneration committee

Due to the size and nature of the existing Board and the magnitude of the Company's operations, the Company does not currently have a Remuneration Committee. In accordance with the Company's Corporate Governance Plan, which is available on the Company's website https://www.droneshield.com/investors, the full Board currently carries out the duties that would ordinarily be assigned to the Remuneration Committee under the written terms of reference for that committee.

The Board will devote time on an annual basis to fulfil the roles and responsibilities associated with setting the level and composition of remuneration for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive. The Managing Director of the Company is responsible for evaluating the performance of senior executives on an annual basis. The Board of Directors is responsible for overseeing the Managing Director's performance evaluations. This evaluation is based on specific criteria, including the business performance of the Company, whether strategic objectives are being achieved and the development of management and personnel.

Directors' remuneration

The remuneration of an Executive Director is decided by the Board, without the affected Executive Director participating in that decision-making process.

In accordance with the Constitution, the total maximum remuneration of Non-Executive Directors is initially set by the Board and subsequent variation is by ordinary resolution of shareholders in general meeting in accordance with the Constitution, the *Corporations Act 2001* and the ASX Listing Rules, as applicable.

The determination of Non-Executive Directors' remuneration within that maximum will be made by the Board having regard to the inputs and value to the Company of the respective contributions by each Non-Executive Director. The current amount has been set at an amount not to exceed $500,000 per annum.

In addition, a Director may be paid fees or other amounts (i.e. subject to any necessary shareholder approval, non-cash performance incentives such as options) as the Directors determine where a Director performs special duties or otherwise performs services outside the scope of the ordinary duties of a Director.

Directors are also entitled to be paid reasonable travelling, hotel and other expenses incurred by them respectively in or about the performance of their duties as Directors.

The Group's remuneration policy for Executive Directors (including the Managing Director) and senior management is designed to promote superior performance and long-term commitment to the Group. Executives receive a base remuneration which is market related and may also be entitled to performance-based remuneration at the ultimate discretion of the Board.

Overall remuneration policies are subject to the discretion of the Board and can be changed to reflect competitive market and business conditions where it is in the interests of the Group and the Company's shareholders to do so.

Executive remuneration framework

The Group's reward policy reflects the benefits of aligning executive remuneration with shareholders' interests and to retain appropriately qualified executive talent for the benefit of the Group. The main principles of the policy are:

(a) remuneration is reasonable and fair, taking into account the Group's obligations at law, the competitive market in which the Group operates and the relative size and scale of the Group's business;
(b) individual reward should be linked to clearly specified performance targets which should be aligned to the Group's short term and long-term performance objectives; and
(c) executives should be rewarded for both financial and non-financial performance.

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Directors' Report- Remuneration Report *continued*

Executive remuneration framework *continued*

The total remuneration of Executive Directors (including the Managing Director) and other senior managers consist of the following:

(a) Salary - Executive Directors and senior managers may receive a fixed sum payable monthly in cash;
(b) Short term incentive - Executive Directors and nominated senior managers are eligible to participate in a profit participation plan if deemed appropriate. The Board may at its discretion award bonuses for exceptional performance in relation to each person's pre-agreed Key Performance Indicators;
(c) Post-employment benefits – this refers to superannuation schemes; and
(d) Long term incentives - Executive Directors may participate in share option schemes with the prior approval of shareholders. Executives may also participate in employee share option schemes, with any option issues generally being made in accordance with thresholds set in plans approved by shareholders. The Board, however, considers it appropriate to retain the flexibility to issue options to executives outside of approved Employee Option Plans in exceptional circumstances.

KMP remuneration disclosures in detail

The Directors and other Key Management Personnel ("KMP") of the Company during or since the end of the financial year were:

Name	Position	Effective date
Non-Executive Directors		
Peter James	Independent Non-Executive Chairman	Executive Chairman until 24 January 2017 Returned to Non-Executive Chairman 24 January 2017
Robert Clisdell	Non-Executive Director	Appointed 24 January 2017
Bradley Buswell	Independent Non-Executive Director	Appointed 29 December 2017
Executive Director		
Oleg Vornik	Executive Director, Managing Director and CEO	Appointed as Managing Director and CEO 24 January 2017

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Directors' Report- Remuneration Report *continued*

Shareholdings of KMP

The number of shares in the Company and subsidiary held during the financial year by each Director of DroneShield and other KMP (of which there are none), including their personally related entities, are set out in the following table:

31 December 2018	Opening balance (Number)	Received during the year on exercise of options (Number)	Other changes during the year (Number)	Balance at 31 December 2018 (Number)
Non-Executive Directors				
Peter James	313,292	250,000	107,143	670,435
Robert Clisdell	100,792	37,500	107,143	245,435
Bradley Buswell	-	-	-	-
Executive Director				
Oleg Vornik	113,292	50,000	107,143	270,435
Total	**527,376**	**337,500**	**321,429**	**1,186,305**

31 December 2017	Opening balance (Number)	Received during the year on exercise of options (Number)	Other changes during the year (Number)	Balance at 31 December 2017 (Number)
Non-Executive Directors				
Peter James	250,000	-	63,292	313,292
Winton Willesee	10,000	-	-	-[3]
Dr. Samantha Ravich	1,350,000	-	10,549	-[4]
Robert Clisdell	-	-	100,792	100,792
Bradley Buswell	-	-	-	-
Executive Director				
Oleg Vornik	50,000	-	63,292	113,292
Total	**1,660,000**	**-**	**237,925**	**527,376**

[3] Winton Willesee ceased to be a KMP on 24 January 2017.
[4] Dr. Samantha Ravich ceased to be a KMP on 29 December 2017.

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Directors' Report- Remuneration Report *continued*

Performance shares held by KMP

Holdings by KMP are listed below.

31 December 2018	Plan	Opening balance (Number)	Granted as compensation (Number)	Performance shares converted (Number)	Performance shares lapsed (Number)	Balance at 31 December 2018 (Number)
Non-Executive Directors						
Peter James		-	-	-	-	-
Robert Clisdell		-	-	-	-	-
Bradley Buswell		-	-	-	-	-
Executive Director						
Oleg Vornik		-	-	-	-	-
Total		**-**	**-**	**-**	**-**	**-**

31 December 2017	Plan	Opening balance (Number)	Granted as compensation (Number)	Performance shares converted (Number)	Performance shares lapsed (Number)	Balance at 31 December 2017 (Number)
Non-Executive Directors						
Peter James		-	-	-	-	-
Winton Willesee		-	-	-	-	-[5]
Dr Samantha Ravich	A	202,500	-	-	-	-[6]
	B	202,500	-	-	-	-[6]
	C	202,500	-	-	-	-[6]
Robert Clisdell		-	-	-	-	-
Bradley Buswell		-	-	-	-	-
Executive Director						
Oleg Vornik		-	-	-	-	-
Total		**607,500**	**-**	**-**	**-**	**-**

[5] Winton Willesee ceased to be a KMP on 24 January 2017.
[6] Dr. Samantha Ravich ceased to be a KMP on 29 December 2017.

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Directors' Report- Remuneration Report *continued*

Share options held by KMP

31 December 2018	Opening balance Number	Granted as compensation Number	Other option acquisitions Number	Options exercised Number	Balance at 31 December 2018 Number
Non-Executive Directors					
Peter James	4,750,000	6,600,000	-	(250,000)	11,100,000
Robert Clisdell	537,500	1,600,000	-	(37,500)	2,100,000
Bradley Buswell	-	1,800,000	-	-	1,800,000
Executive Director					
Oleg Vornik	4,550,000	12,400,000	-	(50,000)	16,900,000
Total	**9,837,500**	**22,400,000**	**-**	**(337,500)**	**31,900,000**

31 December 2017	Opening balance Number	Granted as compensation Number	Other option acquisitions Number	Options exercised Number	Balance at 31 December 2017 Number
Non-Executive Directors					
Peter James	4,750,000	-	-	-	4,750,000
Winton Willesee	1,010,000	-	-	-	-[7]
Dr. Samantha Ravich	1,000,000	-	-	-	-[8]
Robert Clisdell	-	500,000	37,500	-	537,500
Bradley Buswell	-	-	-	-	-
Executive Director					
Oleg Vornik	3,250,000	1,300,000	-	-	4,550,000
Total	**10,010,000**	**1,800,000**	**37,500**	**-**	**9,837,500**

[7] Winton Willesee ceased to be a KMP on 24 January 2017.
[8] Dr. Samantha Ravich ceased to be a KMP on 29 December 2017.

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Directors' Report- Remuneration Report *continued*

Remuneration details of KMP

31 December 2018	Salary and fees $	Cash bonus $	Post-employment benefits $	Termination payment $	Share based payments (options) $	Total $
Non-Executive Directors						
Peter James	100,000	-	-	-	205,615	305,615
Robert Clisdell	30,000	-	-	-	56,518	86,518
Bradley Buswell	39,325	-	-	-	125,425	164,750
Executive Director						
Oleg Vornik	225,921	-	-	-	411,022	636,943
Total	**395,246**	**-**	**-**	**-**	**798,580**	**1,193,826**

Zero Price ("Zepo") options are subject to the following vesting conditions being satisfied: DroneShield achieving $10m revenue in any 12-month period within 36 months of the date of issue of the Options; or automatic vesting in the event that DroneShield is subject to a takeover or other change of control transaction. As there is no exercise price and no near-term expectations of dividends for DroneShield, the value of the option (excluding the impact of vesting conditions) determined using Black Scholes is equivalent to the price of a DroneShield share. The value of the Options is based on the spot price of a DroneShield share on the date at which the options were issued. Based on the sales pipeline and existing orders, management estimate that the options will vest within the expiry period. At this stage, the vesting period is assumed to be three years, which will be reviewed against updated pipeline and forecasts each six months.

31 December 2017	Salary and fees $	Cash bonus $	Post-employment benefits $	Termination payment $	Share based payments (options) $	Total $
Non-Executive Directors						
Peter James	100,000	-	-	-	-	100,000
Winton Willesee	5,000	-	-	-	-	5,000[9]
Dr Samantha Ravich	30,000	-	-		-	30,000[10]
Robert Clisdell	28,387	-	-	-	85,041	113,428
Bradley Buswell	-	-	-	-	-	-
Executive Director						
Oleg Vornik	221,535	-	1,980	-	221,106	444,621
Total	**384,922**	**-**	**1,980**	**-**	**306,147**	**693,049**

[9] Winton Willesee ceased to be a KMP on 24 January 2017. Azalea Consulting Pty Ltd, an entity associated with Mr. Winton Willesee, received payments totalling $44,000 in 2017 in relation to Director services, administration and Company Secretarial services provided to the Group. No payments were received in 2018.

[10] Dr. Samantha Ravich ceased to be a KMP on 29 December 2017.

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Directors' Report- Remuneration Report *continued*

Remuneration details of KMP continued

The relative proportions of remuneration that are linked to performance and those that are fixed are as follows:

	Fixed		Performance	
	2017	**2018**	**2017**	**2018**
Non-Executive Directors				
Peter James	100%	33%	0%	67%
Winton Willesee	100%	n/a	0%	n/a
Dr Samantha Ravich	100%	n/a	0%	n/a
Robert Clisdell	25%	35%	75%	65%
Bradley Buswell	n/a	24%	n/a	76%
Executive Director				
Oleg Vornik	50%	35%	50%	65%

The performance component of remuneration received by Directors relates to share options. The issue of share options to Directors is subject to shareholder approval. Remuneration in the form of DroneShield share options is used as a tool to align KMP remuneration with shareholder interests.

The employment agreement of the Executive Director during the year included the following key terms:

Name	**Positions held during the year**	**Key terms of employment agreement**
Oleg Vornik	CEO and Managing Director	- Base remuneration of US$147,200 p.a. from 1 January 2018 to 31 July 2018 (translated to $196,837 p.a. at the average exchange rate) - Base remuneration of US$197,200 p.a. from 31 July 2018 to 31 December 2018 (translated to $263,697 p.a. at the average exchange rate) - Eligible to participate in short term incentive program - Eligible to participate in long term incentive program - A notice period of 3 months, except in defined circumstances - No fixed term

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Directors' Report- Remuneration Report *continued*

Advisory Board remuneration

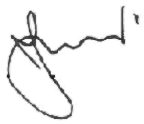
During the year, the Advisory Board has included two individuals who were remunerated as follows:

31 December 2018 $	Salary and Fees	Share based payments (options)	Total
Hon. Jay M Cohen	-	-	-
Dr Samantha Ravich	-	-	-[11]
Total	**-**	**-**	**-**

31 December 2017 $	Salary and Fees	Share based payments (options)	Total
Carol Haave	6,531	-	6,531
Hon. Jay M Cohen	12,734	-	12,734
Lieutenant General Robin Brims CB CBE DSO	6,485	-	6,485
Robert Hill	6,522	-	6,522
Joanna Riley	6,522	-	6,522
Total	**38,794**	**-**	**38,794**

End of Remuneration Report.

This Directors' Report is made in accordance with a resolution of Directors.



Peter James
Independent Non-Executive Chairman

Sydney, NSW
19 February 2019

[11] Following her resignation from the Board on 29 December 2017, Dr. Samantha Ravich transitioned to the DroneShield Advisory Board. Dr. Ravich stepped down from DroneShield's Advisory Board on 23 August 2018.

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Auditor's Independence Declaration

As lead auditor for the audit of the consolidated financial report of DroneShield Limited for the year ended 31 December 2018, I declare that, to the best of my knowledge and belief, there have been no contraventions of:

(a) the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
(b) any applicable code of professional conduct in relation to the audit.

This declaration is in relation to DroneShield Limited and the entities it controlled during the year.



Sydney, NSW
19 February 2019

A G Smith
Director

hlb.com.au

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HLB Mann Judd is a member of HLB International, the global advisory and accounting network.

Consolidated Statement of Profit or Loss and Other Comprehensive Income

	Note	31 December 2018 $	31 December 2017 $
Revenue	**4**	**1,207,203**	**383,585**
Other gains (losses)	**5**	(21,257)	(3,278)
Cost of sales		(511,454)	(230,198)
Product development expense		(2,190,863)	(1,926,420)
Sales and customer service expense		(954,663)	(1,046,604)
Corporate and support expense	**6**	(2,664,705)	(1,764,602)
Corporate governance expense	**7**	(473,718)	(475,973)
Share based payment expense	**3**	(1,124,193)	(647,743)
Loss before income tax		**(6,733,650)**	**(5,711,233)**
Income tax benefit	**8**	397,550	234,620
Loss after income tax		**(6,336,100)**	**(5,476,613)**
Other comprehensive income:			
Items that may be reclassified to profit or loss			
Adjustments on translation of foreign controlled entity		(16,366)	(25,404)
Total comprehensive loss for the period		**(6,352,466)**	**(5,502,017)**
Basic loss per share	**22**	(0.04)	(0.04)
Diluted loss per share	**22**	(0.04)	(0.04)

The above Consolidated Statement of Profit or Loss and Other Comprehensive Income should be read in conjunction with the accompanying notes.

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Consolidated Statement of Financial Position

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	Note	31 December 2018 $	31 December 2017 $
ASSETS			
Current assets			
Cash and cash equivalents	**9**	1,229,499	2,362,894
Trade and other receivables	**10**	1,289,690	207,851
Inventories	**11**	642,502	499,194
Total current assets		**3,161,691**	**3,069,939**
Non-current assets			
Plant, equipment and intangible assets	**12**	806,251	387,770
Total non-current assets		**806,251**	**387,770**
Total assets		**3,967,942**	**3,457,709**
LIABILITIES			
Current liabilities			
Trade payables		184,317	164,672
Provisions	**14**	127,926	120,214
Other liabilities	**15**	1,593,358	254,170
Total current liabilities		**1,905,601**	**539,056**
Total liabilities		**1,905,601**	**539,056**
Net assets (deficiency)		**2,062,341**	**2,918,653**
EQUITY			
Share capital	**16**	11,628,172	7,533,586
Reserves		7,342,857	5,957,655
Accumulated losses		(16,908,688)	(10,572,588)
Total equity (deficiency)		**2,062,341**	**2,918,653**

The above Consolidated Statement of Financial Position should be read in conjunction with the accompanying notes.

Consolidated Statement of Changes in Equity

	Contributed equity $	Options reserve $	Foreign currency translation reserve $	Accumulated losses $	Total equity $
Balance at 1 January 2017	**3,400,993**	**5,436,686**	**41,480**	**(5,489,408)**	**3,389,751**
Transfer from option reserve to accumulated losses	-	(393,433)	-	393,433	-
Transactions with owners in their capacity as owners:					
Options exercised	966,020	-	-	-	966,020
Options issued	-	898,326	-	-	898,326
Contributions of equity, net of transaction costs	3,166,573	-	-	-	3,166,573
	4,132,593	898,326	-	-	5,030,919
Exchange difference on translation of foreign operations	-	-	(25,404)	-	(25,404)
Loss for the period	-	-	-	(5,476,613)	(5,476,613)
Total comprehensive loss for the period	-	-	(25,404)	(5,476,613)	(5,502,017)
Balance at 31 December 2017	**7,533,586**	**5,941,579**	**16,076**	**(10,572,588)**	**2,918,653**
Balance at 1 January 2018	**7,533,586**	**5,941,579**	**16,076**	**(10,572,588)**	**2,918,653**
Transfer from option reserve to accumulated losses	-	-	-	-	-
Transactions with owners in their capacity as owners:					
Options exercised	306,711	-	-	-	306,711
Options issued	-	1,124,193	-	-	1,124,193
Contributions of equity, net of transaction costs	3,787,875	277,375	-	-	4,065,250
	4,094,586	1,401,568	-	-	5,496,154
Exchange difference on translation of foreign operations	-	-	(16,366)	-	(16,366)
Loss for the period	-	-	-	(6,336,100)	(6,336,100)
Total comprehensive loss for the period	**-**	**-**	**(16,366)**	**(6,336,100)**	**(6,352,466)**
Balance at 31 December 2018	**11,628,172**	**7,343,147**	**(290)**	**(16,908,688)**	**2,062,341**

The above Consolidated Statement of Changes in Equity should be read in conjunction with the accompanying notes.

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Consolidated Statement of Cash Flows

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	Note	31 December 2018 $	31 December 2017 $
Cash flows from operating activities			
Receipts from customers		1,252,123	340,367
Other receipts		52,690	-
Payments to suppliers and employees		(6,261,571)	(5,706,781)
Research and Development Tax and other incentives received		505,867	234,620
Net cash flows from (used in) operating activities	**26**	**(4,450,891)**	**(5,131,794)**
Cash flows from investing activities			
Purchase of plant and equipment		(1,059,704)	(428,384)
Net cash flows from (used in) investing activities		**(1,059,704)**	**(428,384)**
Cash flows from financing activities			
Interest income on cash deposits		30,603	46,252
Proceeds from option exercise		306,711	966,020
Proceeds from share and option issues		4,251,801	3,600,590
Share issue transaction costs		(163,376)	(181,958)
Net cash flows from (used in) financing activities		**4,425,739**	**4,430,904**
Cash and cash equivalents at beginning of period		**2,362,894**	**3,497,077**
Net increase (decrease) in cash and cash equivalents		(1,084,856)	(1,129,274)
Exchange rate adjustments to balances held in foreign currencies		(48,539)	(4,909)
Cash and cash equivalents at the end of the year	**9**	**1,229,499**	**2,362,894**

The above Consolidated Statement of Cash Flows should be read in conjunction with the accompanying notes.

Notes to the Financial Statements

Corporate Information

The consolidated financial report of DroneShield Limited ("the Company") and its controlled entities ("DroneShield" or "the Group") for the year ended 31 December 2018 was authorised for issue in accordance with a resolution of the Directors on 19 February 2019.

DroneShield Limited is a company incorporated in Australia, limited by shares which are publicly traded on the ASX.

The principal activity of the Company is the development, commercialisation and sales of hardware and software technology for drone detection and security.

Statement of compliance

These consolidated financial statements are general purpose financial statements which have been prepared in accordance with the *Corporations Act 2001*, Accounting Standards and Interpretations, and comply with other requirements of the law.

Accounting Standards are Australian Accounting Standards ("AAS"). Compliance with AAS ensures that the financial statements and notes of the Group comply with International Financial Reporting Standards ("IFRS").

The financial statements comprise the consolidated financial statements of the Group. For the purposes of preparing the consolidated financial statements, the Group is a for-profit entity.

1. Summary of Significant Accounting Policies

(a) Basis of preparation

The consolidated financial statements have been prepared on the basis of historical cost as explained in the accounting policies below.

The consolidated financial statements are presented in Australian dollars ("AUD"), unless otherwise noted, which is also the functional currency of the Company. The principal accounting policies are set out below.

Going Concern

During the year ended 31 December 2018, the Group incurred losses of $6,336,100 and net cash outflows from operating activities of $4,450,891, with cash on hand at 31 December 2018 of $1,229,499.

This consolidated financial report has been prepared on the basis that the Group will continue to meet its commitments and can therefore continue normal business activities and realise assets and settle liabilities in the ordinary course of business.

The Group's ability to continue as a going concern beyond this period is dependent on generating additional revenues from operations, raising further capital and / or reducing costs, thus resulting in a material uncertainty that may cast doubt on the Group's ability to continue as a going concern and, therefore, it may be unable to realise its assets and discharge its liabilities in the normal course of business.

The Directors believe that there are reasonable grounds to believe that the Group will continue as a going concern post the 12-month period to February 2020, after consideration of the following factors:

- the Group expects to generate increased revenues from the sale of its products within the next 12 months and beyond;
- the Company has the ability to issue additional shares to raise further working capital and has been successful in doing this previously, as evidenced by the successful capital raising completed during financial year ended 31 December 2016, in June and October 2017, and more recently March and November 2018;
- R&D and product development constitute a substantial part of the Company's costs. The Company has applied for, and may apply for further, non-dilutive governmental grants. If such grants are awarded, the Company's R&D and product development costs may be funded, in whole or in part, using such non-dilutive grants. The Company has already received approximately $400,000 in 2018 for the 2017 R&D activities and will be submitting a claim for the 2018 R&D activities;
- As previously disclosed, the Company has undertaken a review of its strategic options. This type of review may result in a range of transactions, including, without limitation, a partnership with a larger industry participant with more substantial financial resources, a fund-raising, and/or a M&A transaction;
- The Company has approximately 37m options excluding Zero Price Options. If in-the-money, exercise of these options is expected to bring additional proceeds to the Company.

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Notes to the Financial Statements *continued*

- the Group also has the ability to scale down its operations in order to curtail expenditure in the event insufficient cash is available to meet projected expenditure.

(b) Principles of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (i.e. subsidiaries). Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity.

Intercompany transactions, balances and unrealised gains on transactions between Group companies (if any) are eliminated. Accounting policies of all companies in the Group are consistent.

(c) Foreign currency translation

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the re-measurement of monetary items at year end exchange rates are recognised in profit or loss.

On consolidation, assets and liabilities have been translated into AUD at the closing rate at the reporting date. Income and expenses have been translated into AUD at the average rate over the reporting period. Exchange differences on consolidation are charged or credited to other comprehensive income and recognised in the foreign currency translation reserve in equity.

(d) Revenue recognition

The Group recognises revenue from the following major sources:
- Sale of hardware
- Subscription services

Revenue is measured based on the consideration specified in a contract with a customer. The Group recognises revenue when it transfers control of a product or service to a customer.

Sale of hardware

The Group sells hardware to distributors and directly to customers. Sales-related warranties associated with hardware cannot be purchased separately and they serve as an assurance that the products sold comply with agreed-upon specifications. Accordingly, the Group accounts for warranties in accordance with AASB 137 Provisions, Contingent Liabilities and Contingent Assets consistent with its previous accounting treatment.

For sales of hardware to distributors, revenue is recognised when control of the hardware has transferred, being when the hardware has been shipped to the distributor's specified location (delivery) and collected from Customs by the distributor. Following delivery, the distributor has full discretion over the manner of distribution and price to sell the hardware, has the primary responsibility when on-selling the goods and where there is a risk of obsolescence and loss in relation to the goods. A receivable is recognised by the Group when the hardware is delivered to the distributor as this represents the point in time at which the right to consideration becomes unconditional, as only the passage of time is required before payment is due.

Contracts with customers have a variable sales element, dependent on volume sold. Currently, revenue from sales is fixed with no variable consideration. Contracts do not include financing components.

For sales directly to customers, revenue is recognised when control of the hardware has transferred to the customer, being at the point the hardware is delivered to the customer. Delivery occurs when the goods have been shipped to the customer's specified location. A receivable is recognised by the Group when the hardware is delivered to the customer as this represents the point in time at which the right to consideration becomes unconditional, as only the passage of time is required before payment is due.

As shipping income is directly related to the sale of hardware, it is not seen as a separate performance obligation and is recognised as and when the related hardware sale is recognised.

Outside of warranties, customers do not have the right to return hardware sold therefore no "right to returned goods asset" is recognised.

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Notes to the Financial Statements *continued*

Subscription services

The Group provides a subscription service for software updates. Such services are recognised as a performance obligation satisfied over time.

The transaction price allocated to these services is recognised as deferred revenue at the time of the initial sales transaction and is released on a straight-line basis over the period of service

Interest income

Interest income and expenses are reported on an accrual basis using the effective interest method.

(e) Income tax

The income tax expense/ (income) for the year comprises current income tax expense/ (income) and deferred tax expense/ (income).

Current tax and deferred tax are recognised as an expense/ (income) except to the extent that they relate to a business combination or are recognised directly in equity or other comprehensive income. Current tax liabilities/ (assets) are therefore measured at the amounts expected to be paid to/ (received from) the relevant taxation authority.

Deferred income tax expense reflects movements in deferred tax assets and deferred tax liability balances during the year as well as unused tax losses.

Current and deferred income tax expense/ (income) is recognised in equity instead of profit or loss when the tax relates to items that are credited or charged directly to equity.

Except for business combinations, no deferred income tax is recognised from the initial recognition of an asset or liability where there is no effect on accounting or taxable profit or loss.

Deferred tax liabilities/ (assets) are calculated at the tax rates that are expected to apply to the period when the liability is settled (asset is realised), and their measurement also reflects the manner in which management expects to settle the carrying amount of the related liability/ (recover the assets).

Deferred tax assets relating to temporary differences and unused tax losses are recognised only to the extent that it is probable that future taxable profit will be available against which the benefits of the deferred tax asset can be utilised.

Deferred tax assets and liabilities are offset only when the Group has a right and intention to set off current tax assets and liabilities from the same taxation authority.

(f) Goods and services and other value-added taxes ("GST")

Revenue, expenses and assets are recognised net of the amount of associated GST, except where the amount of GST incurred is not recoverable from the taxation authority, in which case it is recognised as part of the acquisition cost of an asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included as part of other receivables or payables in the statement of financial position.

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.

(g) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits with terms of less than three months, together with other short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

(h) Trade and other receivables

Trade and other receivables are stated at their cost less an allowance for impairment of receivables. These receivables are unsecured and generally due for settlement prior to the shipment of goods.

Payment for hardware sales and subscription services are due from the customer on the date the invoice is issued. Contracts do not include financing components.

Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default.

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Notes to the Financial Statements *continued*

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(i) Trade and other payables

Trade and other payables are liabilities for goods and services provided to the Group prior to the end of the financial period which are unpaid. These amounts are unsecured and generally payable within 30 days of recognition.

(j) Inventories

Inventories are stated at the lower of cost and net realisable value. Costs of ordinarily interchangeable items are assigned using the average cost method. Net realisable value is the estimated selling price in the ordinary course of business less any applicable selling expenses.

(k) Leases

Leases where the lessor retains substantially all of the risks and rewards of ownership of the asset are classified as operating leases. Payments made under operating leases are recognised as an expense on a straight-line basis over the period of the lease. Associated costs, such as maintenance and insurance, are expensed as incurred.

(l) Employee benefits

Wages, salaries and annual leave

Liabilities for wages and salaries, including non-monetary benefits expected to be settled within 12 months, are recognised in other payables. Annual leave is recognised in provisions and is measured using the remuneration rate expected to apply at the time of settlement.

Long service leave

The liability for long service leave is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using interest rates on national government bonds with terms to maturity that match, as closely as possible, the estimated future cash outflows.

Post-employment benefits

The Group makes fixed percentage contributions for all Australian resident employees to complying third party superannuation funds and recognises the expense as they become payable.

(m) Provisions, contingent liabilities and contingent assets

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated.

No liability is recognised if an outflow of economic resources as a result of present obligations is not probable. Such situations are disclosed as contingent liabilities, unless the outflow of resources is remote, in which case no liability is recognised.

(n) Contributed equity

Costs directly attributable to the issue of new shares are shown as a deduction from the equity proceeds net of any income tax benefit.

(o) Plant and equipment

Plant and equipment (including fittings and furniture) are initially recognised at acquisition cost.

Depreciation is recognised on a straight-line basis to write down the cost less estimated residual value of plant and equipment. The following useful lives are applied:

Office equipment	2 - 5 years
Plant & Equipment	2 - 5 years
Demonstration equipment	2 years

Depreciation will commence for self-constructed assets once the asset is available for use.

Notes to the Financial Statements *continued*

(o) Plant and equipment *continued*

Material residual value estimates and estimates of useful life are updated as required, but at least annually.

Gains or losses arising on the disposal of property, plant and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognised in profit or loss within other income or other expenses.

(p) Intangible assets

Intangible assets relate to purchased computer software. Amortisation is recognised on a straight-line basis over an estimated useful economic life of 3 to 7 years. The estimated useful economic life is reviewed at the end of each reporting period with the effect of any changes in estimate being accounted for on a prospective basis.

(q) Earnings per share

Basic earnings per share is computed by dividing net earnings by the weighted average number of ordinary shares outstanding during each period.

Dilutive earnings per share is computed by dividing net earnings by the dilutive weighted average number of ordinary shares assuming the conversion of all dilutive potential ordinary shares.

(r) Research and development

Research is the original and planned investigation undertaken with the prospect of gaining new knowledge and understanding. Development is the application of research findings to a plan or design for the production of new or substantially improved processes or products prior to the commencement of commercial production. Research costs are expensed as they are incurred.

(s) Share-based payments

Share based compensation benefits are provided to employees via an Employee Option Plan. Information in relation to this plan is set out in Note 3.

The fair value of options granted is recognised as an employee benefits expense with a corresponding increase in equity. The total amount to be expensed is determined by reference to the fair value of the options granted, which includes any market performance conditions and the impact of any non-vesting conditions but excludes the impact of any service and non-market performance vesting conditions.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each period, the entity revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision or original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

(t) Impairment of assets

Assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely dependent of the cash inflows from other assets or other groups of assets (cash generating units).

(u) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, is the CEO.

(v) Comparative disclosures

Where appropriate, comparative disclosures have been reclassified/amended to be consistent with the current year's presentation.

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Notes to the Financial Statements *continued*

(w) New accounting standards and interpretations

DroneShield has adopted all of the new, revised or amended Accounting Standards and interpretations issued by the Australian Accounting Standards Board (AASB) that are mandatory for the current reporting period.

In the current year, the Group has applied AASB 15 *Revenue from Contracts with Customers* (AASB 15). AASB 15 introduces a 5-step approach to revenue recognition. Far more prescriptive guidance has been added in AASB 15 to deal with specific scenarios. Details of these new requirements as well as their impact on the Group's consolidated financial statements are described below.

AASB 15 uses the terms 'contract asset' and 'contract liability' to describe what might more commonly be known as 'accrued revenue' and 'deferred revenue', however the Standard does not prohibit an entity from using alternative descriptions in the statement of financial position. The Group has adopted 'contract asset' and 'deferred revenue' as 'contract liability' to describe such balances.

The Group's accounting policies for its revenue streams are disclosed in detail in 1(d) above. Apart from providing more extensive disclosures on the Group's revenue transactions, the application of AASB 15 has not had a significant impact on the financial position and/or financial performance of the Group.

The impact of AASB 15 on prior periods is not material therefore no further disclosures are made.

AASB 9 *Financial Instruments* introduced new requirements for:

1) The classification and measurement of financial assets and financial liabilities,
2) Impairment of financial assets, and
3) General hedge accounting

The adoption of AASB 9 *Financial Instruments* has not had any material impact on the disclosures or on the amounts reported in these financial statements.

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2018 reporting periods and have not been early adopted by the Group. The Group's assessment of the impact of these new standards and interpretations is set out below.

Title of standard	Nature of change	Impact to group	Application date of standard	Application date for group
AASB 16 Leases	AASB 16 is a new standard that replaces AASB 117. The new standard removes the distinction between operating and finance leases, recognising all lease assets and liabilities on the balance sheet, with limited exceptions for short term leases and leases of low value assets.	The new standard changes how the Group accounts for its current operating leases, which primarily relate to its premises. All such leases will be brought onto the Statement of Financial Position by the recognition of a 'right to use' asset, together with a liability for the present value of lease payments for the life of the lease. The future recognition of lease expenses will change, with more expenses recognised in the early periods of a lease, and less in later periods, as there will be a change from the straight-line expense currently recognised to front-ended finance charges. There will also be a change in lease expense classification from recognising operating expenses to recognising financing costs and amortisation. The Group has not yet calculated the financial impact of these changes.	1 January 2019	1 January 2019

No other standards or interpretations are expected to have a material impact on the Group.

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Notes to the Financial Statements *continued*

2. Critical accounting judgements, estimates and assumptions

In the application of the Group's accounting policies, which are described in Note 1, the Directors are required to make judgements, estimates and assumptions in the preparation of the financial statements about matters that are not readily available from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis.

The judgements, estimates and assumptions that have a significant risk of causing a material adjustment to items (refer to the respective notes) within the next financial year are discussed below.

Licence and patent expenses

There is a degree of judgement required in respect of the capitalisation of patent costs and the future commercial application thereof. The Directors have adopted a prudent approach and all patent costs incurred have been expensed.

Share based payments

The Group measures the cost of equity settled transactions by reference to the fair value of the equity instruments at the date they are granted. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liability within the next annual reporting period but may impact profit or loss and equity. Details of the key assumptions used are set out in Note 3.

Inventories

Management estimates the net realisable values of inventories, taking into account the most reliable evidence available at each reporting date. The future realisation of these inventories may be affected by future technology or other market-driven changes that may reduce future selling prices.

Demonstration Units

Management reviews its estimate of the useful lives of demonstration assets at each reporting date, based on the expected utility of these assets. Uncertainties in these estimates relate to technical obsolescence that may change the utility of certain items.

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Notes to the Financial Statements *continued*

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3. Options issued

During the year ended 31 December 2018, a number of options were issued to Directors, management and other employees of the Group as well as to the Group's corporate advisors and investors who subscribed for shares under the Share Placements that occurred in March and November 2018. Using the Black Scholes Model, the fair value of each option is as set out below and based on the following criteria/assumptions. The options below were issued at various dates between January and November 2018.

Options Issued 31 December 2018	Class A Options[1]	Class E Options	Class F Options	Class G Options[2]	Class H Options	Class L Options	Class M Options	Class N Options	Zero Price Options[3]	Other Options[4]	Total option expense for the year
No of new options	3,068,334	250,000	1,150,000	1,150,000	1,000,000	333,333	333,333	333,333	23,459,384		
Expiry (years)	1.24	3	3	4	4	3	4	5	3		
Exercise price ($)	0.22	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0		
Vesting period (years)	0	0.02	0.21	0.87	0.39	0	0.68	1.68	2.93		
Underlying volatility	87.70%	87.70%	87.70%	87.70%	87.70%	87.70%	87.70%	87.70%	n/a		
Average risk-free interest rate	1.50%	2.10%	2.15%	2.28%	2.26%	2.06%	2.30%	2.30%	n/a		
Average calculated fair value of each option ($)	0.0904	0.1433	0.0917	0.1157	0.0917	0.0854	0.0993	0.1102	0.1854		
Total expense recorded for the period ended 31 December 2018 ($)	-	35,823	88,448	96,734	64,117	28,451	10,108	4,538	732,352	63,622	1,124,193

[1] Class A options were issued to brokers as part of the capital raises and included as part of share transaction costs and treated as a deduction from equity (of $274,559 see Note 17).
[2] Class G options carry the escrow restrictions of continuous employment to 29 March 2019 and 22 June 2019 respectively.
[3] Zero Price ("Zepo") options are subject to the following vesting conditions being satisfied: DroneShield achieving $10m revenue in any 12-month period within 36 months of the date of issue of the Options; or automatic vesting in the event that DroneShield is subject to a takeover or other change of control transaction. As there is no exercise price and no near-term expectations of dividends for DroneShield, the value of the option (excluding the impact of vesting conditions) determined using Black Scholes is equivalent to the price of a DroneShield share. The value of the Options is based on the spot price of a DroneShield share on the date at which the options were issued. Based on the sales pipeline and existing orders, management estimate that the options will vest within the expiry period. At this stage, the vesting period is assumed to be three years, which will be reviewed against updated pipeline and forecasts each six months.
[4] $63,622 relates to the vesting expense from options issued in prior periods, comprising option expense for Classes F and H (issued in 2016), and J and K (issued in 2017), offset by a credit to profit or loss from the lapse of some unvested Class J and K options during the period. Refer to 2017 Annual Report for details of options issued in prior periods.

Notes to the Financial Statements *continued*

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3. Options issued *continued*

During the year ended 31 December 2017, a number of options were issued to Directors, management and other employees of the Group as well as to the Group's corporate advisors and investors who subscribed for shares under the Share Placement that occurred in October 2017. Using the Black Scholes Model, the fair value of each option is as set out below and based on the following criteria/assumptions. The options below were issued at various dates between 19 May and 1 November 2017.

Options Issued 31 December 2017	Class A Options[1]	Class D Options	Class J Options	Class K Options	Listed Options[2]	Other Options[3]	Total option expense for the year
No of new options	2,000,000	1,800,000	625,000	625,000	3,869,987		
Expiry (years)[4]	1.6	3	4	5	0.5		
Exercise price ($)	0.22	0.30	0.50	0.50	0.22		
Vesting period (days)	Immediately	Immediately	263 to 407	628 to 772	Immediately		
Underlying volatility	87.7%	87.7%	87.7%	87.7%	-		
Risk free interest rate	1.73%	1.92%	1.85% to 2.28%	1.85% to 2.28%	-		
Calculated fair value of each option ($)	0.0866	0.1701	0.0895	0.1062	0.02		
Total expense recorded for the period ended 31 December 2017 ($)	-	306,147	49,219	33,744	-	258,633	647,743

[1] Class A options were issued to brokers as part of the capital raises and included as part of share transaction costs and treated as a deduction from equity (of $173,190 Note 17).
[2] Listed DROO Options were issued to shareholders who subscribed for shares under the October 2017 share placement for $nil consideration. Accordingly, the value of these options ($77,400) has been assigned to the option reserve, instead of contributed equity.
[3] An expense of $258,633 was incurred relating to the vesting of options within classes D, F and H issued in 2016.
[4] Class J and K options carry the escrow restrictions of continuous employment to 22 June 2018 and 22 June 2019 respectively.

Notes to the Financial Statements *continued*

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	31 December 2018 $	31 December 2017 $
4. Revenue		
Subscription services	38,256	135,777
Hardware sales	894,095	154,378
Shipping income	21,506	20,569
Total revenue from sales	**953,857**	**310,724**
The Group derives its revenue from the transfer of goods and services over time and at a point in time. This is consistent with the revenue information that is disclosed for each reportable segment. (see Note 25)		
Timing of revenue recognition		
At a point in time		
Hardware sales including shipping income		
- *direct sales*	52,803	-
- *distributors*	862,798	174,947
Over time		
Subscription services		
- *distributors*	38,256	135,777
Total revenue from sales	**953,857**	**310,724**
Other revenue		
Awards and incentives revenue	94,956	-
Interest revenue	32,261	46,809
Other revenue	38,766	-
Sublease revenue	87,363	26,052
Total other revenue	**253,346**	**72,861**
Total revenue	**1,207,203**	**383,585**
5. Other gains (losses)		
Net foreign exchange gains (losses)	(21,257)	(3,278)
Total other gains (losses)	**(21,257)**	**(3,278)**
6. Corporate and support expense		
Office costs and communication	326,896	323,398
Payroll	815,445	526,475
Legal	655,307	571,886
Travel and entertainment	136,689	76,766
Marketing and advertising	98,330	78,392
Professional expenses	524,486	176,316
Other	107,552	11,369
Total corporate and support expense	**2,664,705**	**1,764,602**

Notes to the Financial Statements *continued*

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	31 December 2018 $	31 December 2017 $
7. Corporate governance expense		
Audit	63,663	56,812
Board and Advisory Board expenses	182,302	196,219
Professional expenses	50,467	109,772
Insurance	72,382	47,930
ASX fees	82,670	41,139
Other	22,234	24,101
Total corporate governance expense	**473,718**	**475,973**
8. Income taxes relating to continuing operations		
The components of tax recognised in profit or loss include:		
Current tax	-	-
Deferred tax	-	-
Research and Development Tax Incentive[20]	(397,550)	(234,620)
Total tax expense/(credit)	**(397,550)**	**(234,620)**
The income tax for the year can be reconciled to the accounting profit as follows:		
Income tax expense/ (credit) calculated at 27.5%	(1,851,754)	(1,570,589)
Tax effect of amounts which are not deductible (taxable)	313,986	191,540
Research and Development Tax Incentive	(397,550)	(234,620)
Effect of unused tax losses not recognised as deferred tax assets	1,537,768	1,379,049
Income tax expense/ (credit) recognised in profit or loss (relating to continuing operations)	**(397,550)**	**(234,620)**

The tax rate used for the 2018 and 2017 reconciliations above is the corporate tax rate of 27.5% payable by DroneShield Limited on taxable profits under Australian tax law.

The Company has unused tax losses of $5,753,949 (2017: $3,047,147). The benefit of these losses will only be recognised where it is probable that future taxable profit will be available against which the benefit of the deferred tax asset can be utilised.

[20] A tax credit of $397,550 was received in the current year in relation to expenses incurred in the 31 December 2017 financial year.

Notes to the Financial Statements *continued*

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	31 December 2018 $	31 December 2017 $
9. Cash and cash equivalents		
Cash at bank and in hand	1,046,464	312,894
Short-term deposits	183,035	2,050,000
Total cash and cash equivalents	**1,229,499**	**2,362,894**
10. Trade and other receivables		
Trade receivables	422,991	-
Deferred sales proceeds (see Note 15)	741,513	44,211
Other	9,858	69,917
Prepayments	115,328	93,723
Total trade and other receivables	**1,289,690**	**207,851**

Trade receivables disclosed above include amounts (see below for aged analysis) that are past due at the end of the reporting period for which the Group has not recognised an allowance for doubtful debts because there has not been a significant change in credit quality and the amounts are still considered recoverable.

Age of receivables that are past due but not impaired.		
60 – 90 days	370,997	-
Average age (days)	162	-

Payment for hardware sales and subscription services are due from the customer as per the terms specified in the contract.

11. Inventories		
Work in Progress	17,735	
Finished goods inventory at cost	624,767	499,194
Total Inventory	**642,502**	**499,194**

Notes to the Financial Statements *continued*

12. Plant, equipment and intangible assets

	Development equipment $	Demonstration equipment $	Office equipment $	Plant & Equipment $	Intangible Assets (software) $	Total $
Balance at 1 January 2017	**10,085**	**11,994**	**27,997**	**-**	**9,079**	**59,155**
Additions	21,298	310,226	49,026	-	3,000	383,550
Disposals	(1,708)	-	(2,376)	-	-	(4,084)
Depreciation/Amortisation	-	(31,088)	(11,347)	-	(2,517)	(44,952)
Exchange differences	(319)	(4,207)	(1,373)	-	-	(5,899)
Balance at 31 December 2017	**29,356**	**286,925**	**61,927**	**-**	**9,562**	**387,770**
Additions	163,242	765,686	27,055	137,081	11,441	1,104,505
Disposals	-	(28,393)	(1,272)	-	-	(29,665)
Transfers from (to) other fixed asset categories	(61,955)	58,047	3,908	-	-	-
Transfer from (to) inventory	(4,673)	(226,103)	-	-	-	(230,776)
Depreciation	(14,736)	(353,653)	(55,374)	(9,484)	(4,831)	(438,078)
Exchange differences	(1,295)	10,134	3,656	-	-	12,495
Balance at 31 December 2018	**109,939**	**512,643**	**39,900**	**127,597**	**16,172**	**806,251**

13. Borrowings

Convertible notes, warrants and borrowings

DroneShield Limited held no debt during the year ended 31 December 2018.

	31 December 2018 $	31 December 2017 $

14. Provisions

Onerous contract	17,575	48,765
Employee entitlements	92,603	71,449
Other	17,748	-
Total provisions	**127,926**	**120,214**

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Notes to the Financial Statements *continued*

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	31 December 2018 $	31 December 2017 $
15. Other liabilities		
Accrued expenses	149,115	112,975
Deferred Revenue		
- *Hardware sales (i)*	1,432,581	91,135
- *Subscription services (ii)*	4,248	42,072
- *Other revenue*	7,414	7,988
Total other liabilities	**1,593,358**	**254,170**

(i) For hardware sales, revenue is recognised when control of the goods has transferred to the customer, being at the point the goods are delivered to the customer (distributor or direct customer). When the customer initially places the order, the customer is invoiced and the transaction price of the invoice at that point is recognised by the Group as deferred revenue, until the goods have been delivered to the customer. As shipping income is directly related to hardware sales, shipping income is recognised at the same point in time that the hardware sale is recognised.

(ii) Revenue relating to subscription services is recognised over time with the customer paying up-front in full for these services. Deferred revenue is recognised for subscription services at the time of the initial sales transaction and is released over the service period.

	No. of shares (Note a)	$
16. Contributed equity		
Balance at beginning of period (1 January 2018)	**156,395,893**	**7,533,586**
Shares issued following option exercise during period (Note b)	1,394,140	306,711
Shares issued from Share Placement (Note c, Note d)	24,287,043	4,251,800
Transaction costs in relation to Shares issued from Share Placement (Note e)	-	(463,925)
Balance at end of period (31 December 2018)	**182,077,076**	**11,628,172**

Note (a): The number of shares disclosed is the number of shares in DroneShield Limited.

Note (b): During 2018, 1,394,140 listed options were exercised, resulting in the issue of one new share in DroneShield Limited for each option. With an exercise price of $0.22 per option, the total cash received from the exercise of options during the period was $306,711.

Note (c): In March 2018, the Company issued 12,166,193 shares in a Share Placement. The issue price was $0.21, and the total cash received from the placement of shares was $2,554,900.

Note (d): In November 2018, the Company issued 12,120,850 shares in a Share Purchase Plan ('SPP') and top-up placement. The issue price was $0.14, and the total cash received from the placement of shares was $1,696,900.

Note (e): Included within transaction costs are the value of options issued to brokers of $274,559. The assumptions used in valuing these options has been set out in Note 2.

Notes to the Financial Statements *continued*

17. Shares and options

	Number of Shares	Number of Unlisted Options	Number of Listed DROO options	Number of Performance Shares
Opening balances at 1 January 2018	156,395,893	30,200,000	34,478,988	45,000,000
March Placement shares and options issued	12,166,193	3,041,548	-	-
November Placement shares and options issued	12,120,850	26,786	-	-
Performance shares lapsed during the period	-	-	-	(15,000,000)
Options exercised during the period	1,394,140	-	(1,394,140)	-
Options lapsed during the period	-	(1,400,000)	(33,084,848)	-
Options issued to Directors and Management	-	28,259,383	-	-
Closing balance at 31 December 2018	**182,077,076**	**60,127,717**	**-**	**30,000,000**

Unlisted Options:

28,259,383 Unlisted Options were issued to Directors and Management during the year to 31 December 2018. These Options are subject to various escrow and vesting conditions relating to length of employment with the Company. 450,000 of these options lapsed due to staff leaving the Company. See Note 3 for further details.

3,041,548 Class A Options were issued to Patersons Securities Limited as part of their compensation for acting as Lead Manager for the Share Placement that occurred in March 2018. These options have an exercise price of $0.22 and expire on 14 June 2019.

26,786 Class A Options were issued to brokers as part of their compensation for the Share Placement that occurred in November 2018. These options have an exercise price of $0.22 and expire on 14 June 2019.

Listed DROO Options:

During the year ended 31 December 2018, 1,394,140 listed options were exercised, generating $306,711 in cash. The remaining 33,084,848 options lapsed on 22 June 2018.

Performance shares:

As part of the acquisition of DroneShield LLC by DroneShield Limited, 45,000,000 Performance Shares were issued to DroneShield LLC's existing shareholders. The performance shares carry the following vesting conditions, relating to the achievement of various performance milestones (with Revenue and EBIT targets in relation to the acoustic drone detection system).

Class A Performance Shares lapsed on 22 June 2018.

Class of Securities	Performance Milestones	Number on issue at 31 December 2018	Number on issue at 31 December 2017
Class A Performance Shares	30-day Volume weighted average price ("VWAP") >$0.30 + 20 paid system installations within 24 months of listing date	-	15,000,000
Class B Performance Shares	Revenue: $2,500,000 in any 12-month period or $7,000,000 cumulative within 36 months of listing date	15,000,000	15,000,000
Class C Performance Shares	EBIT: $1,000,000 annual (financial year) or $3,000,000 cumulative within 36 months of listing date	15,000,000	15,000,000

2,227,500 Class B Performance Shares and 2,227,500 Class C Performance Shares are voluntarily escrowed until 22 June 2019.

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Notes to the Financial Statements *continued*

18. Commitments

(a) Lease commitments

The cash flows in the table below relate to the minimum payments for non-cancellable operating leases. In addition to the cash flows below, at 31 December 2018 a bank guarantee for $133,035 exists in relation to the office leasing agreement.

	Minimum lease payments due		
	Within 1 year $	1-5 years $	After 5 years $
31 December 2017	125,232	87,087	-
31 December 2018	136,931	-	-

(b) Sublease arrangement

The Company entered into a sublease arrangement for the Sydney office effective 13 November 2017. The cash flows in the table below relate to the minimum receipts for non-cancellable operating lease income.

	Minimum lease receivables due		
	Within 1 year $	1-5 years $	After 5 years $
31 December 2017	86,906	59,071	-
31 December 2018	59,071	-	-

Subsequent to 31 December 2018, the Company entered into an agreement to sublease an office in Sydney. Refer to Note 27 for further details.

(c) Other commitments

At 31 December 2018, contractual agreements existed to pay suppliers $27,390 for the completion of an order (2017: $51,760).

19. Key Management Personnel disclosures and related party transactions

(a) KMP Compensation

	31 December 2018 $	31 December 2017 $
Short-term employee benefits	395,246	384,922
Post-employment benefits	-	1,980
Share-based payments	798,580	306,147
Total KMP compensation	**1,193,826**	**693,049**

Detailed remuneration disclosures are provided in the Remuneration Report on pages 29- 36.

(b) Other transactions with related parties

During the financial year, the Group engaged the services of the following related-parties on normal commercial terms and conditions no more favourable than those available to other parties:

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Notes to the Financial Statements *continued*

- Mounthaven Consulting LLC, an affiliate of substantial shareholder Long Hill Capital LLC, received payments totalling $200,000 in relation to consulting services provided to the Group. No balance was outstanding at year end.
- During the financial year, the Group entered into a $1,855,000 non-convertible unsecured credit facility agreement with Bergen Global Yield Fund, LP, an affiliate of its shareholder Long Hill Capital, LLC. The Group have not drawn down on the facility.
  If the Group elects to drawdown on the facility, interest will be payable on the amount outstanding at the rate of 12% p.a., the Group will prepay half of the interest on the balance available from the proceeds of the first draw down (and the ongoing interest payments will be reduced, effectively, to 6% per annum). In the event that the Group activates the facility, the Group will also pay an $113,000 fee, from the proceeds of the first drawdown. The principal amount outstanding in relation to each drawdown will be equal to 110% of the amount drawn down.

20. Parent entity financial information

The individual financial statements for the accounting parent entity, DroneShield LLC, show the following aggregate amounts:

	31 December 2018 $	31 December 2017 $
Statement of financial Position		
Current assets	96,266	126,643
Total assets	346,407	442,132
Current liabilities	3,685,804	1,593,407
Total liabilities	3,685,804	1,593,407
Net assets	(3,339,397)	(1,151,275)
Share Capital	1,322,547	1,322,547
Reserves	(291)	16,076
Accumulated losses	(4,661,653)	(2,489,898)
Total Equity	(3,339,397)	(1,151,275)
Loss for the year	**(2,171,757)**	**(1,270,385)**
Other comprehensive loss	**(16,367)**	**(25,404)**
Total comprehensive loss	**(2,188,124)**	**(1,295,789)**

DroneShield LLC and DroneShield Corporation Pty Ltd are both legal subsidiaries of DroneShield Limited and are 100% owned by DroneShield Limited.

21. Financial risk management

The Group's financial instruments consist mainly of deposits with banks, accounts receivable and payable and inter-entity loans.

The Directors' overall risk management strategy seeks to assist the Group in meeting its financial targets whilst minimising potential adverse effects on financial performance.

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Notes to the Financial Statements *continued*

21. Financial risk management *continued*

Credit risk

With respect to credit risk arising from other financial assets, which comprise cash and cash equivalents and prepayments, the Company's exposure to credit risk arises in the form of default of the counter party, with a maximum exposure equal to the carrying amount of these instruments. Management has considered impairment, with none noted at 31 December 2018.

Since the Company trades only with recognised parties, there is no requirement for collateral security.

The maximum exposure to credit risk at the balance date is as follows:

	31 December 2018 $	31 December 2017 $
Cash and cash equivalents	1,229,499	2,362,894
Trade and other receivables	1,289,690	207,851

Liquidity risk

The Company's policy is to maintain a comfortable level of liquidity through the continual monitoring of actual and forecast cash flows and the maturity profile of term deposits, and the raising of additional capital as required.

Foreign exchange risk

The Company operates from Australia and the U.S., and accordingly transactions currently occur in a mix of USD and AUD. As such, cash and cash equivalents used to fund working capital are held in USD and AUD bank accounts.

Transactional currency exposures arise from sales or purchases in currencies other than the Company's functional currency. For example, the Company is exposed to transactional exposure in respect of non-functional currencies on foreign currency denominated sales contract entered into by DroneShield Limited in Australia.

Additionally, the Company is exposed to foreign currency exchange risk when capital is raised in AUD and transferred to the U.S. entity. The Company closely monitors foreign currency movements at such times but does not use hedging instruments to manage such risk.

Foreign currency denominated financial assets and liabilities which expose the Company to currency risk are disclosed below. The amounts shown are translated into AUD at the closing rate.

	31 December 2018 $	31 December 2017 $
Cash	391,127	24,398
Trade and other receivables	1,064,599	93,082
Total Financial assets	**1,455,726**	**117,480**
Trade and other payables	(133,343)	(134,710)
Provisions	(53,051)	(47,363)
Total Financial liabilities	**(186,394)**	**(182,073)**

Foreign exchange risk

The following table, expressed in AUD, indicates DroneShield's sensitivity to movements in exchange rates on the profit or loss, based on the AUD strengthening/ weakening against the USD by 10%:

	31 December 2018 $	31 December 2017 $
+ 10%	80,132	(130,216)
- 10%	368,728	101,427

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Notes to the Financial Statements *continued*

21. Financial risk management *continued*

Exposure to foreign currency varies during the year depending on the volume of transactions. Nonetheless, the analysis above is considered to be representative of the Group's exposure to currency risk.

Financial instrument composition and maturity analysis

The table below reflects the undiscounted contractual settlement terms for financial liabilities.

Contractual maturities of financial liabilities	Less than 6 months $	6-12 Months $	Between 1 and 2 years $	Between 2 and 5 years $	Over 5 years $	Total contractual cash flows $	Carrying amount (assets)/ liabilities $
As at 31 December 2017							
Trade and other payables	164,672	-	-	-	-	164,672	164,672
Other financial liabilities	112,975	-	-	-	-	112,975	112,975
Total	**277,647**	**-**	**-**	**-**	**-**	**277,647**	**277,647**
As at 31 December 2018							
Trade and other payables	184,317	-	-	-	-	184,317	184,317
Other financial liabilities	149,115	-	-	-	-	149,115	149,115
Total	**333,432**	**-**	**-**	**-**	**-**	**333,432**	**333,432**

	31 December 2018 $	31 December 2017 $
22. Earnings (loss) per share		
(a) Basic earnings (loss) per share		
Total basic earnings (loss) per share attributable to the ordinary equity holders of the company	(0.04)	(0.04)
(b) Dilutive earnings per share		
Dilutive earnings (loss) per share attributable to the ordinary equity holders of the company	(0.04)	(0.04)
(c) Weighted average number of shares used as the denominator		
Weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share	168,492,973	143,593,584

Options and Performance Shares

Options on issue (Class A to Class N, and Zero Price Options as set out in Note 3) and Performance Shares set out in Note 17 are not included in the calculation of diluted earnings per share because they are considered to be antidilutive for the period ended 31 December 2018. These options and shares could potentially dilute basic earnings per share in future periods.

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Notes to the Financial Statements *continued*

23. Contingent liabilities

As at 31 December 2018 there were no contingent liabilities.

24. Remuneration of auditor

During the year, the following fees were paid or payable for services provided by the auditor, HLB Mann Judd Assurance (NSW) Pty Limited and its related practices:

	31 December 2018 $	31 December 2017 $
Audit and assurance services	63,663	57,000
Taxation services	7,772	10,979
Total Auditor's remuneration	**71,435**	**67,979**

25. Segment information

The Group operates in one operating segment, being the development and commercialisation of hardware and software technology for drone detection and security.

This operating segment is monitored by the Group's chief operating decision maker and strategic decisions are made on the basis of adjusted segment operating results. The chief operating decision maker of the Group is the CEO.

The following tables present certain information regarding geographical segments for the years ended 31 December 2018 and 31 December 2017.

Segment performance 31 December 2018	**USA $**	**Australia $**	**Elimination $**	**Total $**
Hardware sales including shipping income				
- *direct sales*	-	*52,803*	-	***52,803***
- *distributors*	-	*862,798*	-	***862,798***
Subscription services				
- *distributors*	*1,559*	*36,697*	-	***38,256***
Total revenue from sales	1,559	952,298	-	**953,857**
Other revenue	725,920	241,218	(713,792)	**253,346**
Total revenue	727,479	1,193,516	(713,792)	**1,207,203**
Depreciation	303,562	134,516	-	**438,078**
Loss after income tax expense	(2,171,757)	(4,164,343)	-	**(6,336,100)**
Assets and liabilities				
Segment assets	346,407	7,196,385	(3,574,850)	**3,967,942**
Segment liabilities	(3,685,804)	(1,794,647)	3,574,850	**(1,905,601)**

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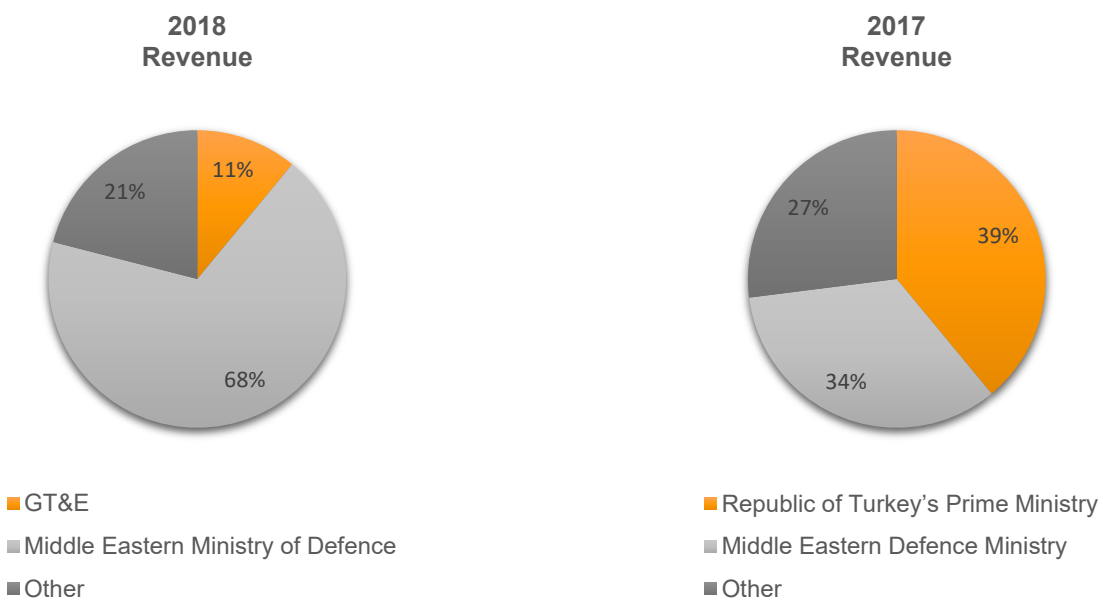
Notes to the Financial Statements *continued*

25. Segment information continued

Segment performance 31 December 2017	USA $	Australia $	Elimination $	Total $
Hardware sales including shipping income				
- *direct sales*	-	-	-	**-**
- *distributors*	*5,276*	*169,671*	-	***174,947***
Subscription services				
- *distributors*	*5,832*	*129,945*	-	***135,777***
Total revenue from sales	11,108	299,616	-	**310,724**
Other revenue	-	72,861	-	**72,861**
Total revenue	11,108	372,477	-	**383,585**
Depreciation	(33,075)	(11,877)	-	**(44,952)**
Finance costs	-	-	-	**-**
Income tax credit/ (expense)	-	234,620	-	**234,620**
Loss after income tax expense	(1,270,385)	(4,206,228)	-	**(5,476,613)**
Assets and liabilities				
Segment assets	442,131	4,491,307	(1,475,729)	**3,457,709**
Segment liabilities	(1,593,407)	(421,378)	1,475,729	**(539,056)**

Information about major customers

The following chart presents certain information regarding customers/distributors who contributed 10 per cent or more to the Group's revenue for the years ended 31 December 2018 and 31 December 2017.



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Notes to the Financial Statements *continued*

26. Reconciliation from loss after income tax to net cash outflow from operating activities

	31 December 2018 $	31 December 2017 $
Operating loss for the year after tax	**(6,336,100)**	**(5,476,613)**
Bad debts	13,118	
Depreciation	438,078	44,952
Effects of foreign currency translation	(139,370)	(17,489)
Inventory impairment expense	273,439	
Loss on disposal of fixed asset	34,353	4,083
Provisions	7,712	72,135
Share option expense	1,124,193	647,743
Change in operating assets and liabilities		
Decrease/(Increase) in trade and other receivables	(1,081,839)	58,776
(Increase) in inventory	(143,308)	(260,921)
(Decrease)/increase in trade and other payables	1,358,833	(204,460)
Net cash flows from (used in) operating activities	**(4,450,891)**	**(5,131,794)**

27. Events after the reporting date

Subsequent to 31 December 2018, the following occurred;

- In January 2019, the Company issued 11,301,700 shares in a Share Placement. The issue price was $0.115, and the total cash received from the placement of shares was $1,299,696. Under the terms of the Placement, brokers participating in the Placement will receive a commission on the funds raised, as well as an aggregate of 2,825,425 unlisted Class O options which expire on 21 February 2021 with an exercise price of $0.22.
- The Company entered into an agreement to sublease an office in Sydney for $148,144 per annum, commencing 18 February 2019 and ending 31 March 2020.

No other matter or circumstance has arisen since 31 December 2018 which has significantly affected or may significantly affect:

- The Group's operations in future financial years; or
- The results of those operations in future financial years; or
- The Group's state of affairs in future financial years.

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Directors' Declaration

1. In the opinion of the Directors:

   (a) the consolidated financial statements and notes set out on pages 38 to 63 are in accordance with the *Corporations Act 2001*, including:

      (i) giving a true and fair view of the Group's financial position as at 31 December 2018 and of its performance for the financial year ended on that date; and

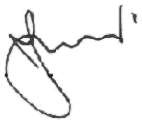
      (ii) complying with Australian Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; and

   (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.

2. The notes to the consolidated financial statements include a statement of compliance with International Financial Reporting Standards.

3. The Directors have been given the declarations by the Chief Executive Officer and the Finance Manager for the year ended 31 December 2018 required by section 295A of the *Corporations Act 2011*.

This declaration is made in accordance with a resolution of the Directors.



Peter James
Independent Non-Executive Chairman

Sydney, NSW
19 February 2019

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Independent Auditor's Report to the Members of DroneShield Limited:

REPORT ON THE AUDIT OF THE FINANCIAL REPORT

Opinion

We have audited the financial report of DroneShield Limited ("the Company") and its controlled entities ("the Group"), which comprises the consolidated statement of financial position as at 31 December 2018, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of DroneShield Limited is in accordance with the *Corporations Act 2001*, including:

(a) giving a true and fair view of the Group's financial position as at 31 December 2018 and of its financial performance for the year then ended; and

(b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* ("the Code") that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Company, would be in the same terms if given to the directors as at the time of this auditor's report.

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

Material Uncertainty Related to Going Concern

We draw attention to Note 1(a) in the financial report, which indicates that, the Group incurred a net loss of $6,336,100 and incurred cash outflows from operating activities of $4,450,891 for the year ended 31 December 2018. As stated in Note 1(a), these events or conditions, along with other matters as set forth in Note 1(a), indicate that a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

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Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In addition to the matter described in the *Material Uncertainty Related to Going Concern* section, we have determined the matters described below to be the key audit matters to be communicated in our report**.**

Key Audit Matter	How our audit addressed the key audit matter
Revenue recognition	
The Group has applied Accounting Standard AASB 15 *Revenue* for the first time in preparing its financial statements for the year ended 31 December 2018. We focussed on this area as a key audit matter due to the judgements involved in applying AASB 15, and as this is the first time the Group has applied this Standard.	We reviewed management's revenue recognition accounting policy to assess whether it complied with AASB 15. We reviewed a sample of contracts to assess whether revenue recognised was in accordance with the requirements of AASB 15. We also reviewed disclosures in the financial statements to assess whether these were in accordance with AASB 15.
Capitalised Demonstration Equipment (Note 9)	
At 31 December 2018, the Group held demonstration equipment with a carrying value of $512,643. We focussed on this area as a key audit matter as the carrying value of capitalised demonstration equipment at 31 December 2018 is a significant asset, and due to the judgement used by management in preparing its assessment of impairment.	We reviewed the cost of these items by agreeing a sample to purchase invoices. We assessed whether the policy to capitalise the demonstration equipment was in accordance with accounting standards. We discussed with management its plans to generate sales, and obtained sales forecasts prepared to identify if any impairment indicators existed. We reviewed sales made during the year to assess if any impairment indicators existed. We reviewed the useful life of these assets. We enquired of management whether there was any indication that the technological advances would indicate that the items capitalised were obsolete.

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Valuation of Share Options (Note 3)	
The Company issued a number of share options to directors, management, investors and advisors. The fair value of the options at grant date was determined by management, and used to account for the options. The key assumptions used in determining the fair value of the options are set out in Note 3 to the financial statements. We focused on this area as a key audit matter due to the judgement involved in assessing the fair value of the options.	We reviewed the valuation of the options, and the methodology used. We also reviewed the key assumptions in the valuation. We assessed whether the Group's disclosures met the requirements of accounting standards.

Information Other than the Financial Report and Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the information included in the Group's annual report for the year ended 31 December 2018, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

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As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the financial report of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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REPORT ON THE REMUNERATION REPORT

Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 29 to 36 of the directors' report for the year ended 31 December 2018.

In our opinion, the Remuneration Report of DroneShield Limited for the year ended 31 December 2018 complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

HLB Mann Judd Assurance (NSW) Pty Ltd
Chartered Accountants

A G Smith
Director

Sydney, NSW
20 February 2019

Shareholder Information

Holdings distribution at 19 February 2019

Holding Ranges	Holders	Total Shares	% Issued Share Capital
1 - 1,000	55	9,558	0.01%
1,001 - 5,000	619	2,011,345	1.10%
5,001 - 10,000	399	3,316,397	1.82%
10,001 - 100,000	739	23,954,860	13.16%
100,001 - over	127	152,784,916	83.91%
Total	**1,939**	**182,077,076**	**100.00%**

The shareholders are entitled to one vote for each share held.

Twenty largest shareholders at 19 February 2019

Position	Holder Name	Shares Held	% Issued Share Capital
1	LONG HILL CAPITAL LLC	55,000,001	30.21%
2	BNP PARIBAS NOMINEES PTY LTD <IB AU NOMS RETAILCLIENT DRP>	15,841,229	8.70%
3	JOHN FRANKLIN	14,438,334	7.93%
4	EAGLE'S VIEW MULTI-STRATEGY LLC	6,538,548	3.59%
5	BNP PARIBAS NOMS PTY LTD <DRP>	6,159,655	3.38%
6	EAGLE'S VIEW CAPITAL PARTNERS L P	5,294,496	2.91%
7	ROBERT DINKEL & KATHLEEN DINKEL	4,500,000	2.47%
7	LAURENCE ROSENFELD	4,500,000	2.47%
8	EAGLE'S VIEW DIVERSIFIED OPP FUND L P	4,134,622	2.27%
9	EAGLE'S VIEW PARTNERS LTD	3,492,128	1.92%
10	AZOTH LLC	2,250,000	1.24%
11	EAGLE'S VIEW OFFSHORE FUND LTD CLASS B	1,708,583	0.94%
12	J P MORGAN NOMINEES AUSTRALIA PTY LIMITED	1,697,985	0.93%
13	MERRILL LYNCH (AUSTRALIA) NOMINEES PTY LIMITED	1,553,818	0.85%
14	CITICORP NOMINEES PTY LIMITED	1,215,135	0.67%
15	EAGLE'S VIEW OFFSHORE FUND LTD CLASS E	1,025,954	0.56%
16	MR DAVID JOHN IRON <IFRA A/C>	750,000	0.41%
17	BOND STREET CUSTODIANS LIMITED <ANDANG - I20149 A/C>	670,435	0.37%
18	JNW SFUND PTY LTD <JNW SUPER FUND A/C>	627,236	0.34%
19	MR MURAT DANACI	600,000	0.33%
20	BERGEN GLOBAL OPPORTUNITY FUND LP	582,101	0.32%
Total		**132,580,260**	**72.82%**
Balance of register		49,496,816	27.18%
Total issued capital		**182,077,076**	**100.00%**

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