



HIGHLANDS PACIFIC LIMITED ARBN 078 118 653
Incorporated in Papua New Guinea

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28 March 2007

Annual Financial Statements

The Board of Highlands Pacific Limited today releases the annual financial statements for the Group for the year ended 31 December 2006.

The financial statements detail a loss from operations of USD27.5 million. Added to this the Group has also been required, under the hedge accounting standards, to bring forward a loss of USD36.2 million for its ineffective gold forward sales contracts, resulting in a reported loss of USD63.8 million. Delays in the ramp-up to full production at the Kainantu gold mine resulted in the deferral of a number of forward sales contracts during the 2006 year and the likely deferral of a number of 2007 contracts.

It is important to note that reported losses attached to these forward sales contracts are not cash flow transactions, rather accounting transactions, i.e. the Group has not incurred a cash outflow in respect of these contracts.

Hedge accounting allows for cumulative losses of highly probable forecast transactions to be recognised directly in the Hedging Reserve for the period when the hedges were effective. When forecast transactions no longer meet the definition of 'highly probable' or the contract is rescheduled, the cumulative losses arising from the difference between the forward sales contract price and the current spot price is required to be recognised in the income statement. This is the current position.

As detailed in the annual financial statements, a total of 147,000 ounces of the 250,000 ounces of hedge contracts owned by the Company at 31 December 2006 were deemed to not meet the definition of 'highly probable'. The subsequent restructuring of the Company's full forward sales program in February 2007 does not allow these ounces to be re-determined as probable.

As a consequence of reporting the USD36.2 million accounting loss in the 2006 Accounts, when the contracted forward sales which were deemed to be ineffective under the International Financial Reporting Standards are settled, they will be accounted for at the then spot price, even though the net actual cash flow received from the settled contracts is at the disclosed forward sales contract price. The outcome will be that the accounting result and the cash flow result may differ going forward. However, the Group is required to report under the International Financial Reporting Standards.

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HIGHLANDS PACIFIC LIMITED AND SUBSIDIARY COMPANIES

INDEPENDENT AUDIT REPORT TO THE MEMBERS

For the Year Ended 31 December 2006

Audit opinion

In our opinion,

- a) the financial statements of Highlands Pacific Limited and subsidiaries set out on pages 3 to 45:
 - Gives a true and fair view, as required by the Companies Act 1997 in Papua New Guinea, of the financial position of Highlands Pacific Limited and Highlands Pacific Limited Group at 31 December 2006, and of their performance for the year ended on that date, and
 - Is presented in accordance with the Companies Act 1997, International Financial Reporting Standards and other generally accepted accounting practice in Papua New Guinea.
- b) proper accounting records have been kept by the Company as far as appears from our examination of those records; and
- c) we have obtained all the information and explanations we have required.

This opinion must be read in conjunction with the rest of our audit report.

Material uncertainty regarding continuation as a Going Concern

Without qualification to the opinion expressed above, attention is drawn to the following matter. As a result of the matters disclosed in note 1 there is material uncertainty whether the Group will be able to continue as a going concern and whether it will realise its assets and extinguish its liabilities in the normal course of business and at the amounts stated in the financial report.

Scope

The financial report and directors' responsibility

The financial report comprises the balance sheet, income statement, statement of movements in equity, statement of cash flows, and the accompanying notes to the financial statements for both Highlands Pacific Limited (the Company) and Highlands Pacific Limited and subsidiaries (the Group), for the year ended 31 December 2006. The Group comprises both the Company and the entities it controlled during that year.

The directors of the Company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Companies Act 1997. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit approach

We conducted an independent audit in order to express an opinion to the members of the Company. Our audit was conducted in accordance with International Standards on Auditing, in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Companies Act 1997, International Financial Reporting Standards and other generally accepted accounting practice in Papua New Guinea, a view which is consistent with our understanding of the Company's and the Group's financial position, and of their performance as represented by the results of their operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report, and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant accounting estimates made by the directors.

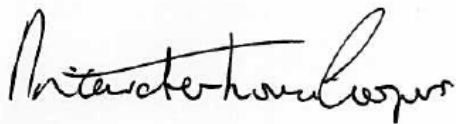
We read the other information in the Annual Report to determine whether it contained any material inconsistencies with the financial report.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

Our audit did not involve an analysis of the prudence of business decisions made by directors or management.

Independence

In conducting our audit, we followed applicable independence requirements of the CPA Papua New Guinea and the Companies Act 1997.



PricewaterhouseCoopers
By: **Stephen Beach**
Registered under the Accountants Act 1996
Lae
Date 27 March 2007

Robert Hubbard

Brisbane

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

INCOME STATEMENT

For the Year Ended 31 December 2006

	Notes	Consolidated		Holding Company	
		2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Gold concentrate sales		10,724	-	-	-
Realisation of hedging instruments		(4,796)	-	-	-
Finance Income	2	1,267	645	-	-
Other revenue	2	41	23	-	-
Total Operating Income		7,236	668	-	-
Mining costs		7,050	-	-	-
Processing costs		3,155	-	-	-
Maintenance costs		4,859	-	-	-
General and administrative costs		12,082	4,068	108,568	1,939
Exploration costs		33	990	-	-
Changes in inventories of work in progress / finished goods		(1,198)	-	-	-
Depreciation and amortisation		5,247	32	-	-
Interest expense		2,400	-	-	-
Net foreign exchange (gains) / losses		1,136	977	(28)	(2)
Total Operating Costs	3	34,764	6,067	108,540	1,937
Profit (Loss) from operations		(27,528)	(5,399)	(108,540)	(1,937)
Gains / (losses) on cash flow hedges	31 (d)	(36,224)	-	-	-
Profit (Loss) before income tax		(63,752)	(5,399)	(108,540)	(1,937)
Income tax (expense) benefit	5	(30)	(17)	-	-
Net profit (loss)		(63,782)	(5,416)	(108,540)	(1,937)
Earnings per share					
Basic & Diluted	6	US\$(0.12)	US\$(0.01)		

These profit and loss statements are to be read in conjunction with the accompanying notes.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

STATEMENT OF CHANGES IN EQUITY

For the Year Ended 31 December 2006

	Notes	Share Capital US\$000	Reserves US\$000	Retained Earnings US\$000	Total US\$000
CONSOLIDATED					
Year Ended 31 December 2006					
Balance as at 1 January 2006		212,864	(49,154)	(119,084)	44,626
Net profit (loss)		-	-	(63,782)	(63,782)
Issue of Share Based Payments	32	-	72	-	72
Net movement on cash flow hedges	21	-	14,196	-	14,196
Issue of share capital	20	42,323	-	-	42,323
Costs associated with Issue	20	(292)	-	-	(292)
Balance as at 31 December 2006		254,895	(34,886)	(182,866)	37,143
Year Ended 31 December 2005					
Balance as at 1 January 2005		193,745	(31,359)	(113,588)	48,798
Net profit (loss)		-	-	(5,416)	(5,416)
Issue of Share Based Payments	32	-	582	-	582
Adjustment to prior year retained earnings for expensing of Share Based Payments	32	-	-	(80)	(80)
Deferred gains (losses) on cash flow hedges	21	-	(18,377)	-	(18,377)
Issue of share capital	20	19,676	-	-	19,676
Costs associated with Issue	20	(557)	-	-	(557)
Balance as at 31 December 2005		212,864	(49,154)	(119,084)	44,626
HOLDING COMPANY					
Year Ended 31 December 2006					
Balance as at 1 January 2006		212,864	(5,686)	(140,717)	66,461
Net profit (loss)		-	-	(108,540)	(108,540)
Issue of Share Based Payments	32	-	72	-	72
Issue of share capital	20	42,323	-	-	42,323
Costs associated with Issue	20	(292)	-	-	(292)
Balance as at 31 December 2006		254,895	(5,614)	(249,257)	24
Year Ended 31 December 2005					
Balance as at 1 January 2005		193,745	(6,268)	(138,780)	48,697
Net profit (loss)		-	-	(1,937)	(1,937)
Issue of Share Based Payments	32	-	582	-	582
Issue of share capital	20	19,676	-	-	19,676
Costs associated with Issue	20	(557)	-	-	(557)
Balance as at 31 December 2005		212,864	(5,686)	(140,717)	66,461

These statements of changes in equity are to be read in conjunction with the accompanying notes.

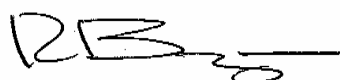
HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

BALANCE SHEET

As at 31 December 2006

	Notes	Consolidated		Holding Company	
		2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
CURRENT ASSETS					
Cash and cash equivalents	7	16,577	10,545	18	5
Inventories	8	4,309	1,665	-	-
Receivables	9	134	116	-	-
		21,020	12,326	18	5
NON-CURRENT ASSETS					
Property, plant and equipment	10	18,666	19,227	-	-
Exploration & Evaluation expenditure	11	27,595	26,926	-	-
Development expenditure	12	-	66,533	-	-
Mineral Properties	13	65,249	-	-	-
Investment in subsidiaries	15	-	-	9	64,009
Advance to subsidiaries	16	-	-	-	2,450
		111,510	112,686	9	66,459
TOTAL ASSETS		132,530	125,012	27	66,464
CURRENT LIABILITIES					
Trade and other payables	17	7,636	9,790	-	-
Borrowings	18	10,000	5,000	-	-
Provisions	19	352	339	-	-
Provision for income tax		13	6	-	-
Derivative financial instruments	31 (d)	37,883	11,387	-	-
		55,884	26,522	-	-
NON-CURRENT LIABILITIES					
Borrowings	18	14,770	24,880	-	-
Provisions	19	1,115	898	-	-
Derivative financial instruments	31 (d)	23,618	28,086	-	-
Advances from subsidiaries	16	-	-	3	3
		39,503	53,864	3	3
TOTAL LIABILITIES		95,387	80,386	3	3
NET ASSETS		37,143	44,626	24	66,461
SHAREHOLDERS' EQUITY					
Contributed equity	20	254,895	212,864	254,895	212,864
Reserves	21	(34,886)	(49,154)	(5,614)	(5,686)
Retained earnings		(182,866)	(119,084)	(249,257)	(140,717)
TOTAL SHAREHOLDERS' EQUITY		37,143	44,626	24	66,461

For, and on behalf of, the board



Robert Bryan
Chairman

27 March 2007



Ian Holzberger
Managing Director

These balance sheets are to be read in conjunction with the accompanying notes.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

CASH FLOW STATEMENT

From the Year Ended 31 December 2006

	Notes	Consolidated		Holding Company	
		2006	2005	2006	2005
		US\$000	US\$000	US\$000	US\$000
CASH FLOW FROM OPERATING ACTIVITIES					
Receipt from gold sales (net of hedge payments)		5,928	23	-	-
Receipt from other operations		41			
Interest from investments		1,254	663	-	-
Income tax paid		(28)	(10)	-	-
Interest paid		(2,400)	-	-	-
Payments to suppliers and employees		(30,655)	(5,048)	-	-
Net cash used in operating activities		(25,860)	(4,372)	-	-
CASH FLOW FROM INVESTING ACTIVITIES					
Proceeds from sale of property, plant and equip't		24	1	-	-
Investment in subsidiaries		-	-	(35,000)	(30,000)
Advance from (to) subsidiaries		-	-	(6,990)	10,883
Purchase of property, plant and equipment		(1,267)	(71)	-	-
Exploration, evaluation, development and mineral properties		(2,650)	(42,562)	-	-
Net cash used in investing activities		(3,893)	(42,632)	(41,990)	(19,117)
CASH FLOW FROM FINANCING ACTIVITIES					
Proceeds from issue of ordinary shares		42,323	19,676	42,323	19,676
Costs associated with Issue		(292)	(557)	(292)	(557)
Repayment of borrowings		(5,830)	-	-	-
Proceeds from borrowings		720	22,920	-	-
Net cash from financing activities		36,921	42,039	42,031	19,119
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS					
		7,168	(4,965)	41	2
Add cash brought forward		10,545	14,310	5	5
Effect of exchange rate change on cash and cash equivalents		(1,136)	1,200	(28)	(2)
CASH AND CASH EQUIVALENTS CARRIED FORWARD		16,577	10,545	18	5
CASH COMPRISES					
Cash and cash equivalents	7	16,577	10,545	18	5

These statements of cash flows are to be read in conjunction with the accompanying notes.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

CASH FLOW STATEMENT (Continued)

From the Year Ended 31 December 2006

Reconciliation of Net Profit (Loss) after Taxation to Cash Flow from Operating Activities

	Notes	Consolidated		Holding Company	
		2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Reported Net Profit (Loss) after Taxation		(63,782)	(5,416)	(108,540)	(1,937)
<i>Add (less) non-cash items:</i>					
Loss on cash flow hedges		36,224	-	-	-
Depreciation and amortisation		5,247	32	-	-
Provision for exploration costs		33	990	-	-
Provision for doubtful debts		-	-	9,568	1,939
Provision for diminution of investments		-	-	99,000	-
Tax		30	17	-	-
Fair value of share based payments		72	90	-	-
(Profit) loss on sale of property, plant & equipment		-	(1)	-	-
Net (gain) loss on foreign currency balances		1,136	(1,200)	(28)	(2)
		42,742	(72)	108,540	1,937
<i>Add (less) movements in working capital items:</i>					
(Increase) decrease in debtors and prepayments		(18)	50	-	-
(Increase) decrease in inventories		(2,644)	(1,665)	-	-
Increase (decrease) in creditors and provisions		(2,158)	2,731	-	-
		(4,820)	1,116	-	-
Net Cash Flow from Operating Activities		(25,860)	(4,372)	-	-

These statements of cash flows are to be read in conjunction with the accompanying notes.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

1. STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES

Highlands Pacific Limited (the Company) and its subsidiaries (together the Group) carry out exploration, development and mining activities in the mining industry. All the Group's current activities are carried out in Papua New Guinea, where the Company is incorporated and domiciled. The registered office is in Port Moresby, Papua New Guinea.

The Company is listed on both the Australian Stock Exchange and the Port Moresby Stock Exchange.

The consolidated financial statements were authorised for issue by the Board of Directors on 26 March 2007. The Company has the power to amend and revise the financial report.

BASIS OF PREPARATION

These financial statements are presented in accordance with the Papua New Guinea Companies Act (1997) and comply with International Financial Reporting Standards and other generally accepted accounting practises in Papua New Guinea.

The financial statements have been prepared on the basis of historical costs, except assets and liabilities that are carried at fair value – for example financial instruments. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year.

This financial report has been prepared on a going concern basis. The Group has experienced a delayed start up to its mining operations and subsequently, production at Kainantu has been significantly below expectations.

As a result, the Group has incurred substantial losses due to operating losses and losses arising from the close out of gold forward contracts and the recognition of unrealised losses on future gold forward contracts no longer qualifying for hedge accounting. This has resulted in a loss for the year of US\$63.8 million and a working capital deficiency of US\$34.9 million

The Group has developed a new life of mine plan and restructured its forward sales contracts to align them to the expectations of future gold production and sales. Other than the restructuring of its forward sales contracts, the Group has raised equity capital of US\$20 million by a private placement announced on 12 February 2007.

It is not possible to forecast with any certainty the mine's production performance at this stage. As a result there is material uncertainty whether the Group will continue as a going concern and therefore, whether the Group will realise its assets and settle its liabilities and commitments in the normal course of business and at the amounts stated in the financial report.

However, the directors believe the future gold production will be sufficient to service its commitments and maintain the value of non current assets in excess of their current carrying values, and have accordingly prepared the financial report on a going concern basis. At this time the directors are of the opinion that no asset is likely to be realised for an amount less than the amount at which it is recorded in the financial report at 31 December 2006. Accordingly, no adjustments have been made to the financial report relating to the recoverability and classification of the asset carrying amounts or the amounts and classification of liabilities that might be necessary should the company not continue as a going concern.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

SPECIFIC ACCOUNTING POLICIES

(a) Principals of consolidation

(i) Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Highlands Pacific Limited ("Company") as at 31 December 2006 and the results of all subsidiaries for the year then ended. Highlands Pacific Limited and its subsidiaries together are referred to in this financial report as the Group or the Consolidated Entity.

Subsidiaries are all those entities (including Special Purpose Entities) over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Investments in subsidiaries are accounted for at cost in the individual financial statements of Highlands Pacific Limited. Such investments include both investments in shares issued by the subsidiaries and other parent entity interests that in substance for part of the parent entity's investment in the subsidiaries.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(ii) Joint venture - Jointly controlled assets

The proportionate interests in the assets, liabilities and expenses of a joint venture activity have been incorporated in the financial statements under the appropriate headings. Details of the joint venture are set out in note 24.

(b) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment and is subject to risks and returns that are different from those of segments operating in other economic environments.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(c) Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in US dollars, which is Highlands Pacific Limited's functional and presentation currency. The Board has determined that the primary economic environment in which the Group operates is determined by the US dollar, as the Group's investment process is based on US dollars and the majority of its fixed asset purchases and costs and likely future revenue streams are in US dollars or currencies related to US dollars.

(ii) Transaction and balances

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

Translation differences on non-monetary financial assets and liabilities are reported as part of the fair value gain or loss.

(iii) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates; and
- all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities are taken to shareholders' equity.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(d) Revenue recognition

Sales of gold concentrate are recognised as revenue only when there has been a passing of title and risk to the customer, and:

- (i) the product is in a form suitable for delivery and no further processing is required by, or on behalf of, the Group;
- (ii) the quantity and quality (grade) of the product can be determined with reasonable accuracy;
- (iii) the product has been dispatched to the customer and is no longer under the physical control of the Group (or property in the product has earlier passed to the customer);
- (iv) the selling price can be measured reliably;
- (v) it is probable that the economic benefits associated with the transaction will flow to the Group; and
- (vi) the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Sales revenue represents the gross proceeds receivable from the customer.

(e) Interest income

Interest income is recognised on a time proportion basis using the effective interest rate method.

(f) Income tax

The income tax expense for the period is the tax payable on the current period's taxable income based on the national income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and to unused tax losses.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities are settled, based on those tax rates which are enacted for each jurisdiction. The relevant tax rates are applied to the cumulative amounts of deductible and taxable temporary differences to measure the deferred tax asset or liability. An exception is made for certain temporary differences arising from the initial recognition of an asset or a liability. No deferred tax asset or liability is recognised in relation to these temporary differences if they arose in a transaction that at the time of the transaction did not affect either accounting profit or taxable profit or loss.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

(g) Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases (refer note 29). Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(h) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents includes cash on hand, deposits held at call with banks, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value, and bank overdrafts.

(i) Inventories

Stores, production work in progress and finished goods are stated at the lower of cost and net realisable value. Costs are assigned to individual items of inventory on the basis of weighted average costs. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

(j) Derivatives

The Group is exposed to changes in commodity prices from its activities. The Group enters into forward sales contracts to hedge commodity price risk. Derivative financial instruments are not held for speculative purposes.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value at each reporting date. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates the derivatives as hedges of cash flows of highly probable forecast transactions (cash flow hedges).

On the date a derivative contract is entered into, the contract is designated as a hedge against specific future production.

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity in the hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item will affect profit or loss (for instance when the forecast production that is hedged takes place). The gain or loss relating to the effective portion of forward sales contracts is recognised in the income statement within 'sales'.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

In assessing the fair value of non-traded derivatives, the Group obtains a valuation from an independent external party.

(k) Non-current assets

(i) *Property, Plant and Equipment*

The cost of purchased property, plant and equipment is the value of the consideration given to acquire the assets and the value of other directly attributable costs which have been incurred in bringing the assets to the location and condition necessary for their intended service.

An assets carrying amount is written down immediately to its recoverable amount if the assets carrying amount is greater than its estimated recoverable amount (para (iii) below).

Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in operating profit. Where revalued assets are sold, the amounts included in fair value and other reserves are transferred to retained earnings.

Repairs and maintenance are charged to the income statement during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the asset when it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Group. Major renovations are depreciated over the remaining useful life of the related asset.

The depreciation calculation is dependent on whether the property, plant and equipment relates to the Kainantu gold project or general corporate operations.

Of the property, plant and equipment relating to the Kainantu gold project, approximately 90% will be depreciated based on the units-of-production method, using total tonnage of ore crushed as a determinant. The remaining useful life of mine assets is approximately 4 to 5 years. Those assets depreciated on a straight line basis are done so predominantly as follows:

Buildings	3 – 5 years
Plant and Equipment	2 – 5 years
Motor Vehicles	3 – 5 years

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

The depreciation on property, plant and equipment relating to general operations is calculated on a straight line basis to write off the cost or revalued amount of each asset to their residual value over their estimated useful lives as follows:

Buildings	20 – 50 years
Plant and Equipment	5 – 10 years
Motor Vehicles	3 – 5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

(ii) *Exploration, evaluation and development expenditure*

Cumulative exploration, evaluation and development expenditure incurred by or on behalf of the Group is carried forward as an asset when it is incurred in relation to separate areas of interest for which rights of tenure are current. Cost includes the cost of acquisition, exploration, evaluation and development, and an allocation of overhead costs associated with these functions.

Cumulative exploration and evaluation expenditure for each area of interest is provided against unless:

- the expenditure is expected to be recouped through successful development and exploration, or alternatively, sale of the area; or
- exploration expenditures in the areas of interest which have not reached a stage which permits a reasonable assessment of economically recoverable mineral reserves are fully provided for.

When an area of interest is abandoned, any expenditure carried forward in respect to that area is written off, firstly against any existing provision for that expenditure with any remaining balance being charged to earnings.

Upon commencement of development, accumulated expenditure is transferred from exploration and evaluation expenditure and is carried forward with development expenditure until the commencement of mining operations, at which time the expenditure is transferred to mining properties and property, plant and equipment.

Development costs relating to an area of interest are carried forward to the extent that they are expected to be recouped either through sale or successful exploitation.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(iii) Impairment of long life assets

Property, plant and equipment and other non-current assets, including mineral properties are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the assets exceeds its recoverable amount. The recoverable amount is the higher of an asset's net selling price and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash flows.

(l) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 45 days of recognition.

(m) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance date.

(n) Borrowing costs

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use or sale. Other borrowing costs are expensed.

(o) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow or resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance date. The discount rate used to determine the present value reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognised as interest expense.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(i) *Long service leave*

The liability for long service leave is recognised in the provision for employee benefits and 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.

(ii) *Restoration, rehabilitation and environmental expenditure*

A provision is raised for anticipated expenditure to be made on restoration and rehabilitation to be undertaken after mine closure. These costs include the costs of dismantling and demolition of the process plant infrastructure, the closure of all mine openings and the remediation of disturbed areas and removal of any residual material.

The provision is only raised in respect of damage incurred up to balance date. The amount of any provision recognised is the full amount that has been estimated based on current costs to be required to settle present obligations, discounted using a pre-tax discount rate of 8%.

The amortisation or 'unwinding' of the discount applied in establishing the net present value of provisions is charged to the income statement in each accounting period. The amortisation of the discount is shown as a financing cost, rather than as an operating cost. Other movements in the provision, including those resulting from new disturbances, updated cost estimates, changes to the lives of operations and revisions to discount rates are capitalised within capital expenditure. These costs are then depreciated over the lives of the assets to which they relate.

(p) **Employee benefits**

Wages and salaries, annual leave and sick leave

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' service up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled. Accumulated sick leave is not accrued and not payable on cessation of employment.

Retirement benefit obligations

The Group contributes to a number of defined contribution plans for its employees. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior periods. For defined contribution plans, the Group pays contributions to a privately administered pension plan on a mandatory basis. Once the contributions have been paid, the Group has no further payment obligations. The regular contributions constitute net periodic costs for the year in which they are due and as such are included in staff costs.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

Share-based payments

Share-based compensation benefits are provided to employees via the Executive Option Scheme. Information relating to this scheme is set out in note 33.

The fair value of the options granted is recognised as an employee benefit expense with a corresponding increase in equity. The fair value is measured at a grant date and recognised over the period during which the employees become unconditionally entitled to the options.

The fair value at grant date is independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the vesting and performance criteria, the impact of dilution, the non-tradable nature of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

The fair value of the options granted excludes the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimate of the number of options that are expected to become exercisable. The employee benefit expense recognised each period takes into account the most recent estimate.

Upon the exercise of options, the balance of the share-based payments reserve relating to those options is transferred to share capital and the proceeds received, net of any directly attributable transactions costs, are credited to share capital.

(q) Contributed equity

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown as equity as a deduction, net of tax, from the proceeds.

(r) Earnings per share

(i) Basic earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity holders of the Group, excluding and costs of servicing equity holders other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

(ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(s) Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the Group and that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below

(i) Carrying value of Mineral Properties

The Group tests annually whether the carrying value long life assets; such as exploration and evaluation expenditure, mineral properties, and property, plant and equipment; have suffered any impairment. The recoverable amounts of cash-generating units, such as the Kainantu gold mine, have been determined on a value-in-use calculation. The recoverable amounts of non operating projects, such as Ramu and Frieda River, have been determined using a discounted net present value of forecasted cash flow streams. These calculations require the use of assumptions.

(ii) Derivative financial instruments

The Group continually calculates the fair value of derivative financial instruments at each reporting date. This fair value calculation is performed independently to the Group by the counter parties to the derivative financial instruments. In the designation process (refer note 1 (j)) the Group is required to makes assumptions on the status of highly probable forecasted transactions. Refer note 31 (d) for details of these assumptions and the potential impact of changes to the assumptions.

(iii) Provision for restoration, rehabilitation and environmental expenditure

The Group reviews the provision for restoration, rehabilitation and environmental expenditure in relation to the Kainantu gold mine at each reporting date. As set out in note 1 (o) (ii) certain assumptions are required to be made in determining the amount the Group is expected to incur to settle its obligations in relation to this expenditure. Key assumptions include the amount and timing of future cash flow estimates. A 10% increase to cost assumptions will result in a USD110,000 increase in the liability and in the carrying value of the asset. An increase in the discount rate to 10% will result in a USD150,000 decrease in the liability and in the carrying value of the asset.

(t) Rounding

The financial statements have been rounded to the nearest thousand dollars.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(u) Release of new International Financial Reporting Standards (IFRS)

The International Accounting Standards Board has issued the following standards, amendments and interpretations that are applicable to the Group for accounting periods beginning on or after 1 March 2006 or later and which the Group has not adopted early:

- (i) IFRS 7: Financial Instruments: Disclosure
- (ii) IFRS 8: Operating Segments
- (iii) IAS 1 (Amendment): Presentation of Financial Statements – Capital Disclosures
- (iv) IFRIC 7: Applying the restatement approach under IAS 29
- (v) IFRIC 8: Scope of IFRS 2
- (vi) IFRIC 9: Reassessment of Embedded Derivatives
- (vii) IFRIC 10: Interim Financial Reporting and Impairment

The Group has conducted investigations and does not consider that there are any measurement or recognition issues arising from the release of these new pronouncements that will have a significant impact on the reported financial position or financial performance of the Group. However the Group continues to investigate the disclosure requirements of these standards for the purpose of future financial statements.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

2. REVENUE

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Operating Income				
Rental income	41	23	-	-
Finance Income				
Interest income	1,267	645	-	-

3. EXPENSES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Total operating costs	34,764	6,067	108,540	1,937
Operating costs are stated after charging:				
Auditors' remuneration				
- audit	79	45	-	-
- other services	40	44	-	-
Depreciation				
- land and buildings	165	10	-	-
- plant and equipment	1,641	22	-	-
Amortisation				
- mineral properties	2,650	-	-	-
- exploration and evaluation	72	-	-	-
- borrowing costs	719	-	-	-
Profit on disposal of fixed assets	-	(1)	-	-
Provision for doubtful debts (refer note 16)	-	-	9,568	1,939
Provision for diminution of investments (refer note 15)	-	-	99,000	-

4. STAFF COSTS

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Wages and salaries	8,124	1,400	-	-
Other benefits	962	342	-	-
	<u>9,086</u>	<u>1,742</u>	<u>-</u>	<u>-</u>

The average number of people employed by the Group during the year was 451 (2005: 356). The Holding Company does not have any direct employees. The average number of casual employees was 63 (2005: 80). A portion of staff costs were capitalized during the 2005 year.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

5. INCOME TAX

	Consolidated		Holding Company	
	2006	2005	2006	2005
	US\$000	US\$000	US\$000	US\$000
Reconciliation of income tax expense to prima facie tax expense				
Loss before income tax expense for the year	(63,752)	(5,399)	(108,540)	(1,937)
Income tax benefit on the loss for the year at an average of 30% (2005: 30%)	(19,125)	(1,620)	(32,562)	(581)
Tax effect of amounts which are not deductible (taxable) in calculating taxable income:				
Provision for doubtful debts	-	-	2,870	581
Provision for diminution of investments	-	-	29,700	-
Sundry items	96	337	-	-
	(19,029)	(1,283)	8	-
Deferred tax asset not brought to account	19,059	1,300	(8)	-
Income tax expense	30	17	-	-
Tax Losses				
Unused tax losses for which no deferred tax asset has been recognised	30,116	7,553	-	-
Potential tax benefit @ 30%	9,035	2,266	-	-
Other deferred tax assets not recognised				
<i>Amounts recognised in profit and loss</i>				
Provision for exploration costs	129,845	129,813	-	-
Amorisation and depreciation	5,215	-	-	-
Loss on cash flow hedges	61,501	39,473	-	-
Unrealised foreign exchange gains (losses)	173	202	173	202
Provision for employee entitlements	508	417	-	-
Sundry items	198	191	-	-
	197,440	170,096	173	202
Potential tax benefit @ 30%	59,232	51,029	52	61
Deferred tax liabilities not recognised				
<i>Amounts recognised in profit and loss</i>				
Unrealised foreign exchange gains (losses)	1,455	910	-	-
Sundry items	30	1	-	-
	1,485	911	-	-
Set-off deferred tax assets associated with carried forward losses and other deferred tax assets not recognised	(1,485)	(911)	-	-

The benefits for tax losses will only be obtained if:

- assessable income of a nature and of an amount sufficient to enable the benefit to be realised is derived,
- conditions of deductibility imposed by law continue to be complied with, and
- no changes in tax legislation adversely affect the ability in realising the benefit.

The tax losses are available to be carried forward for a maximum of 20 years.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

6. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares on issue during the year. The diluted earnings per share is calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

Earnings per share	2006	2005
Net profit (loss) attributable to shareholders (US\$000)	(63,782)	(5,416)
Weighted average number of ordinary shares on issue (000)	543,845	456,946
Basic earnings per share (US\$)	(0.12)	(0.01)
Diluted earnings per share		
Weighted average number of ordinary shares on issue (000)	543,845	456,946
Weighted average number of ordinary shares for diluted earnings per share on issue (000)	559,141	468,881
Diluted earnings per share (US\$)	(0.12)	(0.01)

Options granted to employees are considered to be potential ordinary shares and have been included, to the extent they are dilutive, in the determination of diluted earnings per share. The options have not been included in the determination of basic earnings per share. Details relating to options are set out in note 32.

Refer to note 31 for details on the issue of ordinary fully paid shares and options that occurred after 31 December 2006.

7. CASH AND CASH EQUIVALENTS

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Cash at bank and in hand	1,811	2,182	18	5
Short-term bank deposits	14,766	8,363	-	-
	16,577	10,545	18	5

8. INVENTORIES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Stores	3,112	1,665	-	-
Production work in progress	395	-	-	-
Finished goods	802	-	-	-
	4,309	1,665	-	-

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

9. RECEIVABLES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Non-Current				
Other receivables*	1,000	1,000	-	-
Less: Provision for doubtful debts**	(1,000)	(1,000)	-	-
Current				
Other receivables	134	116	-	-
Less: Provision for doubtful debts	-	-	-	-
	134	116	-	-

* Non-current receivables include the following:

Amounts owing by Nord Australex Nominees (PNG) Limited ("Nord") totaling US\$1.00 million (2005: US\$1.00 million)

This balance is receivable as follows:

- US\$500,000 – When debt and equity funding is available for the development of the Ramu project.
- US\$500,000 – When the Ramu project commences production.

** A provision for US\$1 million was raised in 1999 against these two tranches:

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

10. PROPERTY, PLANT AND EQUIPMENT

	Land & Buildings US\$000	Plant & Equip't US\$000	Total US\$000
CONSOLIDATED - 2006			
Cost			
Cost brought forward	4,122	16,434	20,556
Additions	-	1,267	1,267
Disposals	(10)	(473)	(483)
Cost carried forward	4,112	17,228	21,340
Depreciation			
Brought forward	114	1,215	1,329
Charge for the year	165	1,641	1,806
Disposals	(9)	(452)	(461)
Depreciation carried forward	270	2,404	2,674
Net book value at 31 December 2006	3,842	14,824	18,666
CONSOLIDATED - 2005			
Cost			
Cost brought forward	168	1,310	1,478
Additions	-	71	71
Transfer from Investment Property	315	-	315
Transfer from Development	3,639	15,064	18,703
Disposals	-	(11)	(11)
Cost carried forward	4,122	16,434	20,556
Depreciation			
Brought forward	104	1,204	1,308
Charge for the year	10	22	32
Disposals	-	(11)	(11)
Depreciation carried forward	114	1,215	1,329
Net book value at 31 December 2005	4,008	15,219	19,227

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

11. EXPLORATION & EVALUATION EXPENDITURE

	Ramu US\$000	Kainantu US\$000	Frieda US\$000	Other US\$000	Total US\$000
Balance 1 January 2006	16,000	926	10,000	-	26,926
Capitalised during the year	13	741	-	45	799
Less amortisation of exploration costs	-	(72)	-	-	(72)
Less provisions for exploration costs	(13)	-	-	(45)	(58)
Balance 31 December 2006	16,000	1,595	10,000	-	27,595
Balance 1 January 2005	16,000	-	10,000	-	26,000
Capitalised during the year	889	926	34	67	1,916
Less provision for exploration costs	(889)	-	(34)	(67)	(990)
Balance 31 December 2005	16,000	926	10,000	-	26,926

The realisation of the carrying value of the Group's interest in the Ramu and Frieda projects is dependent upon either the successful development or sale of these assets. The future development of the projects are dependent upon Highlands Pacific and / or its joint venture partners securing sufficient funding from equity, debt or other sources of funding. The Directors remain confident that these assets will ultimately be developed – it is projected that Ramu project will commence development in the 2007 year, however with the Frieda project development cannot be predicted with any certainty. Consequently, in assessing the carrying value of the Ramu and Frieda projects, the Directors have considered their value by reference to the present value of the future cash flows, at a risk adjusted discount rate, to be generated by these assets assuming their ultimate successful development and their potential current realisable value by reference to comparable transactions and farm-in arrangements.

12. DEVELOPMENT EXPENDITURE

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Kainantu				
Balance brought forward	62,693	41,472	-	-
Capitalised during the year	-	39,924	-	-
Transfer to Mineral Properties	(62,693)	-	-	-
Transferred to property, plant & equipment	-	(18,703)	-	-
Balance carried forward	-	62,693	-	-
Deferred finance costs				
Balance brought forward	3,840	2,250	-	-
Capitalised during the year	-	1,590	-	-
Transfer to Mineral Properties	(3,840)	-	-	-
Balance carried forward	-	3,840	-	-
Total	-	66,533	-	-

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

13. MINERAL PROPERTIES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Kainantu				
Balance brought forward	-	-	-	-
Transferred from development	62,693	-	-	-
Capitalised during the year	1,746	-	-	-
Amortisation	(2,650)	-	-	-
Balance carried forward	61,789	-	-	-
Deferred finance costs				
Balance brought forward	-	-	-	-
Transferred from development	3,840	-	-	-
Capitalised during the year	339	-	-	-
Amortisation	(719)	-	-	-
Balance carried forward	3,460	-	-	-
Total	65,249	-	-	-

The Kainantu gold project commenced production in early 2006.

The deferred financing costs relate to the establishment and ongoing managing of the US\$31 million limited recourse project finance facility.

14. INVESTMENT PROPERTY

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Balance brought forward	-	315	-	-
Transferred to Property, Plant and Equipment	-	(315)	-	-
Balance carried forward	-	-	-	-

The property classified as an Investment Property has been transferred to Property, Plant and Equipment as the property is now occupied internally by the Group.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

15. INVESTMENTS IN SUBSIDIARIES

	% Shareholding	Country of Incorp
Ramu Nickel Limited	100	PNG
Highlands Frieda Limited	100	PNG
Highlands Pacific Resources Limited	100	PNG
Highlands Pacific Indonesia Limited ¹	100	PNG
PT Haigol Sumber Daya Servis	100	Indonesia
PT Miwah Tambang Emas	90	Indonesia
PT Tripa Tambang Nusa	90	Indonesia
Highlands Pacific Australia Pty Limited	100	Australia
Highlands Pacific Services Limited	100	PNG
Astrolabe Limited	100	PNG
Highlands Kainantu Limited (Note 1 below)	100	PNG

1. The Company has entered into an agreement whereby it will sell a 5% interest in Highlands Kainantu Limited to the Kainantu mine area Landowners. At balance date, Highlands Pacific Limited continued to own 100% of the interest.

INVESTMENTS AT COST

	Holding Company	
	2006 US\$000	2005 US\$000
Investments in subsidiaries - at cost	130,186	95,186
Less provision for diminution	(130,177)	(31,177)
	9	64,009

During the year Highlands Pacific Limited purchased 35,000 Redeemable Preference Shares in Highlands Kainantu Limited at US\$1,000 per share for a total of US\$35 million. Highlands Kainantu Limited used these funds to repay an intercompany loan to Highlands Pacific Limited.

A provision has been raised against the investment in Highlands Kainantu Limited by the Holding Company due to insufficient asset backing.

16. SUBSIDIARY ADVANCES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Advances to subsidiaries				
Advances	-	-	157,323	115,203
Less provision for write-off	-	-	(157,323)	(112,753)
			-	2,450
Advances from subsidiaries				
Advances	-	-	3	3

The advances within in the Group are interest free with no set repayment terms.

Highlands Kainantu Limited is restricted in paying dividends and repaying loans in cash to the Holding Company due to the bank borrowings Highland Kainantu Limited has in place.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

17. TRADE AND OTHER CREDITORS

	Consolidated		Holding Company	
	2006	2005	2006	2005
	US\$000	US\$000	US\$000	US\$000
Trade creditors	1,395	820	-	-
Other creditors (note 1 below)	3,580	2,561	-	-
Accruals	2,661	6,409	-	-
	7,636	9,790	-	-

1. Includes an amount of US\$2 million payable to Nippon Mining & Metals Co. Ltd when the Kainantu gold project commences commercial production.

18. BORROWINGS

	Consolidated		Holding Company	
	2006	2005	2006	2005
	US\$000	US\$000	US\$000	US\$000
Non-Current				
Bank borrowings	14,770	24,880	-	-
Current				
Bank borrowings	10,000	5,000	-	-
	24,770	29,880	-	-

The bank borrowings are limited recourse with a fixed and floating charge over the assets of Highlands Kainantu Limited and the shares of Highlands Kainantu Limited, guaranteed by Highlands Pacific Limited until completion.

Under the facility the following ratios are to be complied with:

- Debt Service Cover Ratio at greater than 1.25:1; and
- Loan Life Cover Ratio at greater than 1.5:1.

The above borrowings are to be repaid as follows:

- Within 1 year US\$10.0 million
- Between 1 and 2 years US\$14.77 million

The effective interest rate at the balance sheet date was 9.65%, including political risk insurance.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

19. PROVISIONS

Consolidated

	Rehabilitation	Employee Entitlements	Total
	US\$000	US\$000	US\$000
Balance 1 January 2006	892	345	1,237
Charged for the year	-	80	80
Foreign exchange impact	-	2	2
Additional provisions recognised	210	-	210
Utilised / paid during year	-	(62)	(62)
Balance 31 December 2006	1,102	365	1,467

	2006 US\$000	2005 US\$000
Analysis of total provisions:		
Current	352	339
Non-Current	1,115	898
	1,467	1,237

Employee entitlements for annual leave are classified as "Other Creditors" in accordance with the requirements of International Financial Reporting Standards.

Refer to note 1(o)(ii) for details on the provision for restoration, rehabilitation and environmental.

20. SHARE CAPITAL

a) Paid Up Capital

Consolidated and Holding Company

	2006 US\$000	2005 US\$000	2006 Shares 000's	2005 Shares 000's
Balance 1 January	212,864	193,745	478,725	419,548
Issued during the year	42,323	19,676	86,045	59,177
Less costs associated with issue	(292)	(557)	-	-
Balance 31 December	254,895	212,864	564,770	478,725

The total number of shares issued as at 31 December 2006 was 564,770,123 (2005: 478,725,053). In accordance with the Papua New Guinea Companies Act 1997 the Company's shares are fully paid, have no par value and there is no authorised capital level.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

b) Movement in paid up capital

Date	Details	Notes	No. of Shares	Issue Price	
				AU\$	US\$000
1 January 2005	Opening Balance		419,547,523		193,745
26 April 2005	Share Placement	(i)	39,639,867	0.42	13,121
30 May 2005	Share Purchase Plan	(ii)	17,514,750	0.42	5,705
5 December 2005	Exercise of options	(iii)	500,000	0.54	199
30 December 2005	Issue of shares	(iv)	1,522,913	0.58	651
	Transaction costs arising on share issues				(557)
31 December 2005	Balance		478,725,053		212,864
3 February 2006	Exercise of options	(iii)	500,000	0.54	200
	Issue of shares	(v)	1,307,190	0.54	746
14 March 2006	Share Placement	(i)	62,000,000	0.67	30,601
8 May 2006	Exercise of options	(iii)	2,000,000	0.54	792
12 May 2006	Share Purchase Plan	(vi)	20,237,880	0.67	9,984
	Transaction costs arising on share issues				(292)
31 December 2006	Balance		564,770,123		254,895

(i) Share placement to domestic and international institutions and sophisticated investors. The share price was set at the 20 day volume weighted average price.

(ii) Share Purchase Plan to existing shareholders on the same terms and conditions as the Share Placement on 26 April 2005.

(iii) Exercise of options issued to banking syndication.

(iv) Fee relating to the completion of the transaction with China Metallurgical Group Corporation in relation to the Ramu nickel/cobalt project. The share price was set at the 20 day volume weighted average price.

(v) Fee relating to the Engineering, Procurement, Construction and Management contract for the process plant at the Kainantu gold mine. The share price was set at the 20 day volume weighted average price.

(vi) Share Purchase Plan to existing shareholders on the same terms and conditions as the Share Placement on 14 March 2006

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

c) Share Options

The number of unissued ordinary shares under option at 31 December 2006 is 15,375,733 (2005: 17,244,483).

Options issued to the banking syndicate financing the Kainantu gold mine

	Issued	Exercised during year
Outstanding at the end of the year		
Exercise Price	A\$0.54	A\$0.54
Number of Options	12,144,483	2,500,000
Expiry Date	31 Dec 2007	31 Dec 2007

Options issued under the Directors' and Executives' Share Option Scheme

	Issued	Exercised during year
Outstanding at the end of the year		
Exercise Price	A\$0.37	A\$0.37
Number of Options	1,093,750	Nil
Exercise Price	A\$0.43	A\$0.43
Number of Options	137,500	Nil
Exercise Price	A\$0.423	A\$0.43
Number of Options	2,000,000	Nil

The options issued to the banking syndicate were approved at the 2004 and 2005 annual general meetings. These options are exercisable any time up to 31 December 2007.

The options issued under the Directors' and Executives Share Option Scheme are exercisable after the completion of certain performance hurdles by certain dates. The exercise period for these options commence on the day that the performance hurdle is achieved ("vesting date") and will end on the third anniversary of the vesting date. Options are granted under the plan for no consideration.

All options granted carry no dividend or voting rights. Each option, when exercisable, is converted into one ordinary share.

IRFS 2 Share Based Payments has been adopted as at 1 January 2005.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

21. RESERVES

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Foreign Currency Translation Reserve				
Balance brought forward	(10,263)	(10,263)	(6,268)	(6,268)
Movement for the year	-	-	-	-
Balance carried forward	(10,263)	(10,263)	(6,268)	(6,268)
Hedging Reserve				
Balance brought forward	(39,473)	(21,096)	-	-
Transferred to income statement	14,196	-	-	-
Deferred loss on cash flow hedges	-	(18,377)	-	-
Balance carried forward	(25,277)	(39,473)	-	-
Share-based Payments Reserve				
Balance brought forward	582	-	582	-
Fair value of options expensed	72	582	72	582
Balance carried forward	654	582	654	582
	(34,886)	(49,154)	(5,614)	(5,686)

Nature and purpose of reserves

(a) Foreign Currency Translation Reserve

Exchange difference arising on translation of the Groups functional currency from the Papua New Guinean Kina to US Dollar resulted in a foreign currency translation reserve. The reserve will have no further movement.

(b) Hedging Reserve

The hedging reserve is used to record gains or losses on a hedging instrument in a cash flow hedge that are recognised directly in equity, as described in note 1(j). Amounts are recognised in the profit and loss when the associated hedged transaction occurs.

(c) Share-based Payments Reserve

The share-based payments reserve is used to recognise the fair value of options issued but not exercised.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

22. REMUNERATION OF EMPLOYEES

The number of employees (not including Directors), whose remuneration and benefits exceeded K100,000 fall within the following bands:

Kina	Group No. of Employees	
	2006	2005
100,000 - 109,999	16	15
110,000 - 119,999	-	2
140,000 - 149,999	4	2
150,000 - 159,999	1	2
160,000 - 169,999	2	-
170,000 - 179,999	-	3
180,000 - 189,999	-	1
190,000 - 199,999	7	1
200,000 - 209,999	-	1
210,000 - 219,999	2	2
220,000 - 229,999	-	1
270,000 - 279,999	-	1
280,000 - 289,999	-	1
310,000 - 319,999	2	-
320,000 - 329,999	2	-
340,000 - 349,999	-	1
360,000 - 369,999	1	-
370,000 - 379,999	1	-
420,000 - 429,999	-	1
480,000 - 489,999	2	-
520,000 - 529,999	-	1
600,000 - 609,999	1	-
620,000 - 629,999	1	-
730,000 - 739,999	-	1
740,000 - 749,999	-	2
770,000 - 779,999	1	-
780,000 - 789,999	-	1
Total	43	39

The remuneration includes costs to the Group of accommodation in PNG and other like benefits provided to employees.

The 2005 comparatives have been converted at the current year exchange rates to arrive at the equivalent US\$ bands.

PGK1.00 = US\$0.3512

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

23. REMUNERATION OF DIRECTORS

Directors' remuneration, received during the year, including the value of benefits and the fair value of options charged during the year, was as follows:

2006 Year

Name & Position	Cash Remuneration & Fees	Non-monetary Benefits	Superannuation	Share-based Payments	Total
	US\$000	US\$000	US\$000		US\$000
R Bryan, <i>Chairman</i>	100	-	9	-	109
I Holzberger, <i>Managing Director</i>	275	22	30	-	327
A Berry, <i>Non-Executive Director</i>	50	-	5	-	55
R Mitchell, <i>Non-Executive Director</i>	50	-	5	-	55
F Williame-Igara, <i>Non-Executive Director</i>	50	-	5	-	55
J Forbes, <i>Executive Director</i>	196	9	10	-	215
Total	721	31	64	-	816

2005 Year

Name & Position	Cash Remuneration & Fees	Non-monetary Benefits	Superannuation	Share-based Payments	Total
	US\$000	US\$000	US\$000		US\$000
R Bryan, <i>Chairman</i>	100	-	9	-	109
I Holzberger, <i>Managing Director</i>	280	23	31	54	388
A Berry, <i>Non-Executive Director</i>	50	-	4	-	54
R Mitchell, <i>Non-Executive Director</i>	50	-	4	-	54
F Williame-Igara, <i>Non-Executive Director</i>	38	-	3	-	41
J Forbes, <i>Executive Director</i>	220	19	24	14	277
Total	738	42	75	68	923

Ms Williame-Igara was appointed as a Director on the 24th March 2005.

US\$50,000 cash remuneration for Mr Mitchell is paid directly to the "NASFUND".

Mr J Forbes resigned as a Director on the 3rd July 2006. The remuneration paid to Mr Forbes was for his position as Chief Financial Officer and as an Executive Director and in the 2006 year includes the payment of leave entitlements on resignation.

24. JOINT VENTURES

At 31 December 2006 joint venture interests comprised:

	Percentage Interest	Activity
Ramu joint venture (Note 1 below)	8.56	Exploration & Evaluation
Frieda River joint venture (Note 2 below)	88.9	Exploration & Evaluation

- During the 2005 the Group's interest in the Ramu joint venture decreased from 68.5% to 8.56%. This reduction was the result of the agreement signed between the previous Ramu joint venture parties and China Metallurgical Construction (Group) Corporation (MCC) whereby MCC is responsible for the construction of the project with no recourse to the other joint venture parties. The Group's 8.56% interest increases to 11.30% at no cost to the Group after the debt for the financing of the project has been repaid. At this time the Group also has the option to purchase an additional 9.25% interest at market value, which if exercised would take the Group's interest to 20.55%.
- Subject to the right of the Independent State of Papua New Guinea to acquire a 30% equity interest in any major mining development in that country.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

The following amounts represent the Group's share of assets, liabilities, sales and results for the Ramu and Frieda River joint ventures that are included in the consolidated balance sheet and profit and loss statements:

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Current assets	-	-	-	-
Non-current assets	26,000	26,000	-	-
	26,000	26,000	-	-
Current liabilities	-	-	-	-
Non-current liabilities	-	-	-	-
	-	-	-	-
Net Assets	-	-	-	-
Revenues	-	-	-	-
Expenses	-	-	-	-
Net profit before tax	-	-	-	-
	-	-	-	-

25. RELATED PARTY TRANSACTIONS

(a) Parent entity

The parent entity within the Group is Highlands Pacific Limited.

(b) Subsidiaries

Interests in subsidiaries are set out in note 15.

(c) Key management personnel

Refer to note 23 for details regarding directors. Other key management personnel, those that had authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, during the year are as follows:

<i>Name</i>	<i>Position</i>
G De Ross	General Manager Technical Services
J Forbes	General Manager Finance (from 1 January to 3 July)
K Grice	General Manager Finance (from 13 June to 31 December)
R Guest	General Manager Kainantu

Messrs De Ross, Forbes and Guest were also key management persons during the 2005 year.

(d) Key management personnel compensation

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Short-term employee benefits	498	440	-	-
Share based payments	25	32	-	-
	523	472	-	-

Directors' remuneration is disclosed in note 23.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(e) Equity instrument disclosures relating to key management personnel

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

Details of share-based payments are disclosed in note 33.

Option holdings

The number of options over ordinary shares in the Company held during the financial year by each director and other key management personnel of the Group, including their personally related parties, are set out below.

2006 Year

Name	Balance at the start of the year	Granted during the year as compensation	Exercised during the year	Lapsed during the year	Balance at the end of the year	Vested and exercisable at the end of the year
Directors of Highlands Pacific Limited						
I Holzberger	750,000	-	-	(400,000)	350,000	350,000
J Forbes	475,000	-	-	(100,000)	375,000	375,000
Other key management personnel of the Group						
G De Ross	150,000	300,000	-	(50,000)	400,000	100,000
R Guest	325,000	300,000	-	(250,000)	375,000	75,000

2005 Year

Name	Balance at the start of the year	Granted during the year as compensation	Exercised during the year	Lapsed during the year	Balance at the end of the year	Vested and exercisable at the end of the year
Directors of Highlands Pacific Limited						
I Holzberger	1,200,000	-	-	(450,000)	750,000	350,000
J Forbes	700,000	-	-	(225,000)	475,000	375,000
Other key management personnel of the Group						
G De Ross	400,000	-	-	(250,000)	150,000	100,000
R Guest	600,000	-	-	(275,000)	325,000	75,000

Mr Jeffrey Forbes resigned as a Director on the 3rd July 2006, therefore his balance at the end of the year relates to this date.

Share holdings

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

2006 Year

Name	Balance at the start of the year	Received during the year on the exercise of options	Other changes during the year	Balance at the end of the year
Directors of Highlands Pacific Limited				
R Bryan	693,130	-	14,920	708,050
A Berry	152,940	-	14,920	167,860
I Holzberger	71,040	-	7,460	78,500
J Forbes	112,080	-	14,920	127,000

No other key management personnel of the Group held shares

Mr Jeffrey Forbes resigned as a Director on the 3rd July 2006, therefore his balance at the end of the year relates to this date.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

2005 Year

Name	Balance at the start of the year	Received during the year on the exercise of options	Other changes during the year	Balance at the end of the year
Directors of Highlands Pacific Limited				
R Bryan	669,330	-	23,800	693,130
A Berry	129,140	-	23,800	152,940
I Holzberger	59,140	-	11,900	71,040
J Forbes	88,280	-	23,800	112,080

No other key management personnel of the Group held shares

(f) Loans to key management personnel

There are no loans between directors or other key management personnel and any of the Group companies.

(g) Other transactions with key management personnel

Mr R Mitchell is the Chief Executive Officer of the NASFUND, which is a major shareholder in the Company and manages a retirement plan in which the Company participates. NASFUND is also leasing five executive houses to Highlands Kainantu Limited at commercial rates.

(h) Transactions with related parties

The following transactions occurred with related parties:

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
<i>Superannuation contributions</i>				
Contributions to superannuation funds on behalf of employees	238	191	-	-

(i) Advances to / from related entities

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
<i>Advances to / from subsidiaries</i>				
Beginning of the year	-	-	115,200	125,498
Movements during the year	-	-	42,120	(10,298)
End of year	-	-	157,320	115,200

Refer note 16 for provisions raised against these advances to subsidiaries.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

26. SEGMENT REPORTING

a) Primary Reporting (Business Segments)

Consolidated	Gold	Exploration	Unallocated	Group
	US\$000	US\$000	US\$000	US\$000
2006				
Segment revenue	5,928	-	41	5,969
Segment result	(63,003)	(33)	(716)	(63,752)
Income tax (expense) benefit	-	-	(30)	(30)
Net Loss	(63,003)	(33)	(746)	(63,782)
Segment assets	87,732	27,595	17,203	132,530
Segment liabilities	93,295	-	2,092	95,387
Acquisition of segment assets	3,347	799	-	4,146
Segment depreciation and amortisation	5,140	72	35	5,247
2005				
Segment revenue	-	-	23	23
Segment result	(1,598)	(990)	(2,811)	(5,399)
Income tax (expense) benefit	-	-	(17)	(17)
Net Loss	(1,598)	(990)	(2,828)	(5,416)
Segment assets	86,900	26,926	11,186	125,012
Segment liabilities	79,164	-	1,222	80,386
Acquisition of segment assets	41,514	1,916	71	43,501
Segment depreciation and amortisation	-	-	32	32

b) Secondary Reporting (Geographic Segments)

Consolidated

	Papua New Guinea		Japan		Australia		Total	
	2006	2005	2006	2005	2006	2005	2006	2005
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
Segment Sales Revenue	-	-	10,724	-	-	-	10,724	-
Segment Assets	117,187	115,470	-	-	15,343	9,542	132,530	125,012
Acquisition of Segment Assets	4,146	43,501	-	-	-	-	4,146	43,501
Segment Liabilities	(6,950)	(8,948)	(2,000)	(2,000)	(86,437)	(69,438)	(95,387)	(80,386)

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

27. COMMITMENTS FOR EXPENDITURE

	Consolidated 2006 US\$000	2005 US\$000
Capital commitments		
Commitments for the expenditure on the Kainantu gold project development not recognised as liabilities, payable:		
Within one year	-	270

28. MAJOR COMMITMENTS

Highlands Kainantu Limited, a wholly owned subsidiary of Highlands Pacific Limited (refer note 15), has entered into a number of major contracts in relation to the operation of the Kainantu gold mine. Contracts current as at balance date include a contract for the provision of technical services, a contract for generated power supply, an off-take contract and hedging contracts.

29. OPERATING LEASE OBLIGATIONS

	Consolidated		Holding Company	
	2006 US\$000	2005 US\$000	2006 US\$000	2005 US\$000
Obligations payable after balance date on non-cancellable operating leases are as follows:				
Within one year	854	100	-	-
One to two years	783	91	-	-
Two to five years	608	28	-	-
	2,245	219	-	-

30. CONTINGENT LIABILITIES

During 1999, Highlands Pacific entered into an agreement with Eastern Pacific Mines Limited ("Eastern") to purchase Eastern's 10% interest in the Ramu joint venture. The following contingent liabilities arose as a result of the acquisition:

- When debt and equity funding is available for the development of the Ramu project, the payment of the Kina equivalent of US\$73,033 plus A\$1.5 million which may be satisfied by payment in Kina (cash) on or by an issue of Highlands Pacific's shares at a price determined by the average trading price of Highlands Pacific's shares on the ASX over the preceding ten (10) days. The satisfaction of the payment by cash or by the issue of shares is at Highlands Pacific's election.
- When the Ramu project commences commercial production, the payment of the Kina equivalent of A\$0.25m plus A\$1.25m which may be satisfied in the same manner as the A\$1.5 million payment mentioned above.

There are no other material matters pending which, in the opinion of the Directors, could give rise to any liabilities which should be disclosed as contingent liabilities.

31. FINANCIAL INSTRUMENTS

(a) Activities and Management Policies

(i) Currency risk

The Group undertakes transactions denominated in a range of currencies from time to time and, resulting from these activities, exposures in those currencies arise. Though there are no specific hedging activities to mitigate any currency risk, this exposure is monitored by management on an ongoing basis.

The Company provides loans to other members of the Group. These loans are effectively denominated in US dollars consistent with the functional currency of the Group.

(ii) Credit risk

The Group has entered into an off-take agreement with a large multinational corporation for the sale of product from the Kainantu gold mine. The Board of Directors do not believe there is a credit risk from this agreement due to the credit worthiness of the corporation involved.

(iii) Liquidity risk

The Group engages in prudent liquidity risk management by maintaining sufficient cash and cash equivalents.

(iv) Interest rate risk

While the Group has interest-bearing deposits as at the balance sheet date, these funds are predominantly committed to the ongoing operations of the Kainantu gold mine and hence the Group does not rely on any interest revenue from these deposits.

The Group has interest bearing borrowings as at balance sheet date, these funds have been used for the construction of the Kainantu gold mine. The interest rate on these borrowings is based on LIBOR plus a fixed margin as per the facility agreement. The Group does not enter into any financial instruments to manage this interest rate risk.

(b) Fair Values

The carrying values of the assets and liabilities are not significantly different to their fair values.

The cash and bank balances include bank term deposits, which generally mature within 1 and 180 days and receive interest at rates between 2.00% to 6.15%. The interest rate achieved depends on the currency on deposit.

(c) Currency Control

The Papua New Guinea Central Banking (Foreign Exchange and Gold) Regulations generally require PNG companies to hold all cash reserves in Kina unless authority is given by the Bank of Papua New Guinea to hold funds off shore. Prior approval of the Bank of Papua New Guinea is required to convert funds from Kina into other currencies. The Group has permission to hold funds off shore.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

(d) Derivative financial instruments

	Consolidated 2006 US\$000	Consolidated 2005 US\$000
Current Liabilities		
Forward contracts	37,883	11,387
Non-current Liabilities		
Forward contracts	23,618	28,086
Shareholders equity - fair value and other reserves		
Deferred hedging gains (losses)	(25,277)	(18,377)
	(25,277)	(18,377)
<p>The estimates net amount of gains / (losses) contained in the fair value and other reserves, which are expected to be reclassified to earnings within the next 12 months, is as follows:</p>		
Forward contracts	(9,483)	(11,387)
	(9,483)	(11,387)

A series of agreements were entered into with financial institutions in relation to future sales of gold for the Kainantu gold project. The purpose of these transactions is to protect the level of income in future years. It is not Group policy to engage in speculative hedging activities. Refer note 31 for subsequent changes to these contracts since the end of the year.

During the year it was identified that a number of the derivative financial instruments (147,000 ounces) were not matched against highly probable transactions and therefore hedge accounting was not applicable for these instruments. As a result, accounting for the deferred loss through the Hedging Reserve was not allowed and the total unrealised loss for these instruments was charged to the income statement. The amount required to be charged to the income statement for the year was US\$36,224,000.

As at 31 December 2006 the hedge book amounted to 250,000 ounces of flat forward gold sales as shown in the following summary.

Forward Sales		
	Ounces	Average Committed Price
2007	160,000	US\$408
2008	90,000	US\$404

Forward sales are transactions against which the Group will be obliged to deliver when they fall due.

The forward gold sales were restructured on 22 February 2007, refer note 33.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

32. SHARE-BASED PAYMENTS

(a) Executive Option Scheme

The establishment of the Executive Option Scheme was ratified by shareholders at the 2005 annual general meeting. Staff eligible to participate in the plan are those of a senior management level and above. A further issue of 2,000,000 options under this Scheme took place in the 2006 year. The performance hurdle for all of these options is 12 months continuous employment with the Company to 31 July 2007.

Options are granted under the plan for no consideration and carry no dividend or voting rights. When exercisable, each option is convertible into one fully paid ordinary share.

The exercise price of options is based on the volume weighted average price of all trades of shares on the Australian Stock Exchange during the period of 20 trading days ending the day before the options are issued.

The options will only be exercisable if the performance hurdle is achieved by the required date. The exercise period will commence on the day that the performance hurdle is achieved and will end on the third anniversary of this date.

Set out below are summaries of the options granted under the plan:

Grant date	Hurdle / vesting date	Exercise Price (AUD)	Balance start of year	Granted during year	Exercised during year	Expired during year	Balance at end of year	Exercisable at end of year
6/8/04	1/10/2004	0.37	200,000	-	-	-	200,000	200,000
6/8/04	31/12/2004	0.37	50,000	-	-	-	50,000	50,000
6/8/04	30/03/2005	0.37	300,000	-	-	-	300,000	300,000
6/8/04	25/05/2005	0.37	100,000	-	-	-	100,000	100,000
6/8/04	31/10/2005	0.37	50,000	-	-	-	50,000	50,000
6/8/04 *	31/12/2005	0.37	318,750	-	-	(75,000)	393,750	393,750
6/8/04	1/01/2006	0.37	100,000	-	-	100,000	-	-
6/8/04	30/09/2006	0.37	750,000	-	-	750,000	-	-
20/5/05	31/12/2005	0.43	137,500	-	-	-	137,500	137,500
7/8/06	31/07/2007	0.423	-	2,000,000	-	-	2,000,000	-
			2,006,250	2,000,000		775,000	3,231,250	1,231,250
Weighted average exercise price (AUD)			0.37	0.42		0.37	0.41	0.38

* 75,000 options were previously disclosed as expiring incorrectly.

The weighted average remaining contractual life of options outstanding at the end of the period was 2.8 years. No options were exercised during the year.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

Fair value of options granted

The assessed fair value at grant date of options granted during the year ending 31 December 2006 was AUD0.13 cents per option. The fair value at grant date is independently determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the vesting and performance criteria, the impact of dilution, the non-tradeable nature of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term of the option.

The model inputs for the options granted during 31 December 2006 included:

Exercise Price	AUD0.423
Grant Date	7th August 2006
Share price at grant date	AUD0.34
Expected volatility of Company's shares	50%
Expected dividend yield	0%
Risk-free interest rate	5.90%

The expected price volatility is based on the historic volatility (based on the remaining life of the options), adjusted for any expected changes to future volatility due to publicly available information.

(b) Cost arising from share-based payment transactions

Total cost from share-based payment transactions recognised during the period as part of a share based payment was as follows:

	December 2006 US\$000	December 2005 US\$000
Options issued under Executive Option Scheme	72	133
Options issued to Financiers	-	360
Total	72	493

33. EVENTS OCCURRING AFTER BALANCE DATE

Frieda project

On 22 January 2007 Xstrata Copper (Xstrata) exercised its option to acquire 81.82% of the Groups' current interest in the Frieda River project. As a result of the exercise of the option the Groups' interest will be reduced to 16.22%. To maintain this interest Xstrata must by 23 January 2012, commission and arrange to have completed a feasibility study; pay the Groups' share of project expenditure until completion of the feasibility study; and should the project be developed include the Group in any debt financing it arranges or alternatively provide the Group with a completion guarantee for any debt funding that the Group arranges. Should Xstrata fail to complete the feasibility study or withdraw from the joint venture then all of Xstrata's interest will be transferred back to the Group at no cost. As at 31 December 2006 the Group shows an interest of 88.9% (refer note 24).

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

Share placement

On 12 February 2007, the Group announced that it had agreed terms for a placement of ordinary shares to raise US\$20 million. The placement consisted of three separate parts.

The first being a placement of 82.7 millions shares on 6 March 2007 raising US\$19.2 million; the second being a placement of 3.3 million shares raising US\$0.8 million; and the third being the issue of 43 million options. The 3.3 million shares and 43 million options were subject to shareholder approval and this was given on 20 March 2007 at a special meeting of shareholders.

The options were granted for no consideration and carry no dividend or voting rights. When exercisable, each option is convertible into one fully paid ordinary share. The exercise price of the options is summarised below:

10,756,477 at AU\$0.50
10,756,477 at AU\$0.55
10,756,477 at AU\$0.60
10,756,477 at AU\$0.65

As part of the above transaction the Group also agreed an Amending Deed to the Facility Agreement (refer note 18 disclosing bank borrowings). There were no material adjustments involved in the Amending Deed.

Financial instruments

On 22 February 2007 the Group restructured the forward gold sales contracts that had been in place on 31 December 2006 and are detailed in note 32(d). The revised forward gold sales contracts totalling 250,000 ounces are summarized in the table below.

	Forward Sales	
	Ounces	Average Committed Price
2007	39,539	US\$400
2008	70,156	US\$400
2009	70,156	US\$400
2010	70,149	US\$400

The restructure provides that the greater of 65% of the gold sold in any quarter or the designated delivery schedule is acquitted against the forward gold sales contracts with any gold delivered in excess of the designated quarterly delivery being applied to the outstanding deliveries in reverse order of maturity.

HIGHLANDS PACIFIC LIMITED AND SUBSIDIARIES

34. SUPPLEMENTARY INFORMATION

In accordance with Accounting Standards Board Directive 2 (ASBD 2) and the Investment Promotion Authority approval to prepare and lodge US dollar financial statements, the Company discloses the following information in PNG Kina terms:

	Consolidated		Holding Company	
	2006 K000	2005 K000	2006 K000	2005 K000
Revenue	20,604	1,988	-	-
Net Profit (Loss) after tax	(181,612)	(16,114)	(15,729)	(5,257)
Total Assets	371,232	363,936	288,636	192,291
Total Liabilities	267,190	234,020	8	9
Net Assets	104,042	129,916	288,628	192,282

Asset and liability balances are translated from US dollars at the rate prevailing at 31 December 2006 of PGK1.00 = \$0.3570 (2005 year PGK1.00 = 0.3435) while income and expense items are translated at the average rate for the year PGK1.00 = \$0.3512 (2005 year PGK1.00 = \$0.3361).

27/3/07
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Form 405

Corporations Act 2001
601CK(1), 100(1)(d),
Class Order [CO 03/823], Class Order [CO 06/68]

Statement to verify financial statements of a foreign company

If there is insufficient space in any section of the form, you may photocopy the relevant page(s) and submit as part of this lodgement

Lodgement details

Who should ASIC contact if there is a query about this form?

Name

CEAIG LENNON

ASIC registered agent number (if applicable)

Telephone number

07 3239 7800

Postal address

GPO Box 3086

BRISBANE QLD 4001

Please provide an estimate of the time taken to complete this form.

0 hrs 5 mins

1 Details of foreign company

Company name

HIGHLANDS PACIFIC LIMITED

ARBN

078 118 653

Place of incorporation

PAPUA NEW GUINEA

Financial year ended

31/12/06
[D] [D] [M] [M] [Y] [Y]

Annual general meeting held

30/05/06
[D] [D] [M] [M] [Y] [Y]

Registered office in Australia

Contact name (officer or employee)

Registered office address in Australia

Family name

LENNON

Given name

CEAIG THOMAS

At the office of / CI- (if applicable)

Office, unit, level

LEVEL 4, EMIRATES HOUSE

Street number and Street name

167 SPACE STREET

Suburb/City

BRISBANE

State/Territory

QLD

Postcode

4000

1 Continued... Details of foreign company

Does the company occupy the premises?

Yes

No

if no, name of occupier?

Occupier's consent (Select box to indicate the statement below is correct)

The occupier of the premises has consented in writing to the use of the specified address as the address of the registered office of the company and has not withdrawn that consent.

At the office of / CI- (if applicable)

HIGHLANDS PACIFIC LIMITED

Office, unit, level

9TH FLOOR PACIFIC PLACE

Street number and Street name

MUSGRAVE STREET

Suburb/City

PORT MOESBY NCD

State/Territory

Postcode

Country

PAPUA NEW GUINEA

Registered office in place of incorporation

If no registered office, provide the address of the principal place of business in place of incorporation.

2 Details of local agent

Enter family and given names or, if a company, name of the company and ACN. Address must be in Australia.

Family name

Given names

Company name

HIGHLANDS PACIFIC AUSTRALIA PTY LTD

ACN/ABN

075 075 517

Office, unit, level

LEVEL 4, SMIBATES HOUSE

Street number and Street name

167 SAGLE STREET

Suburb/City

BRISBANE

State/Territory

QLD

Postcode

4000

2 Continued... Details of additional local agent

Enter family and given names or, if a company, name of the company and ACN. Address must be in Australia.

Family name

Given names

Company name

ACN/ABN

Office, unit, level

Street number and Street name

Suburb/City

State/Territory

Postcode

3 Details of director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	HOLZBERGER		Given names	IAN RAYMOND	
Company name					
ACN/ARBN					
Office, unit, level					
Street number and Street name	435 GIOVANNI ROAD				
Suburb/City	ST LUCIA			State/Territory	QLD
Postcode	4067		Country	AUSTRALIA	

If the director is an individual, give their usual residential address.

3 Continued... Details of additional director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	BRYAN		Given names	ROBERT	
Company name					
ACN/ARBN					
Office, unit, level					
Street number and Street name	BERADLANDS FARM, 303 LAMBERT ROAD				
Suburb/City	NINDOONBAH			State/Territory	QLD
Postcode	4285		Country	AUSTRALIA	

If the director is an individual, give their usual residential address.

3 Continued... Details of additional director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	BEEBY		Given names	ANDREW JEFFERSON	
Company name					
ACN/ARBN					
Office, unit, level					
Street number and Street name	37 HOLLY ROAD				
Suburb/City	BURRAGO			State/Territory	NSW
Postcode	2576		Country	AUSTRALIA	

If the director is an individual, give their usual residential address.

3 Details of director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	Given names
<input type="text" value="MITCHELL"/>	<input type="text" value="LOO"/>
Company name	
<input type="text"/>	
ACN/ARBN	
<input type="text"/>	
Office, unit, level	
<input type="text"/>	
Street number and Street name	
<input type="text" value="APARTMENT 95 ALWAYS HOTEL, JACKSON PARADE"/>	
Suburb/City	State/Territory
<input type="text" value="SAGAGA, APT 100ESBY"/>	<input type="text"/>
Postcode	Country
<input type="text"/>	<input type="text" value="PAPUA NEW GUINEA"/>

If the director is an individual, give their usual residential address.

3 Continued... Details of additional director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	Given names
<input type="text" value="WILLIAMS-IGARA"/>	<input type="text" value="FIU FESAITU"/>
Company name	
<input type="text"/>	
ACN/ARBN	
<input type="text"/>	
Office, unit, level	
<input type="text"/>	
Street number and Street name	
<input type="text" value="SECTION 42, LOT 16, BAINVIEW CRESCENT"/>	
Suburb/City	State/Territory
<input type="text" value="BUCOKO NCD"/>	<input type="text"/>
Postcode	Country
<input type="text"/>	<input type="text" value="PAPUA NEW GUINEA"/>

If the director is an individual, give their usual residential address.

3 Continued... Details of additional director

Enter family and given names or, if a company, name of the company and ACN or ARBN

Family name	Given names
<input type="text" value="BIRVILL"/>	<input type="text" value="IAN CHARLES"/>
Company name	
<input type="text"/>	
ACN/ARBN	
<input type="text"/>	
Office, unit, level	
<input type="text"/>	
Street number and Street name	
<input type="text" value="118 CLYDE STREET"/>	
Suburb/City	State/Territory
<input type="text" value="MOSMAN PARK"/>	<input type="text" value="WA"/>
Postcode	Country
<input type="text" value="6012"/>	<input type="text" value="AUSTRALIA"/>

If the director is an individual, give their usual residential address.

4 Annexures - financial statements

Tick boxes which apply

- balance sheet made up to the end of its last financial year annexure marked (*A*) of (*45*) pages
- profit and loss statement for its last financial year annexure marked (*A*) of (*45*) pages
- cash flow statement for last financial year annexure marked (*A*) of (*45*) pages
- any other documents still required to be prepared by the law of the company's place of origin. annexure marked (.) of () pages
- Give brief description of those documents (if any)
-

If the foreign company is the holder of an Australian financial services licence:

- Are you relying on Class Order [CO 03/823]? Yes No
- Are you relying on Class Order [CO 06/68]? Yes No

Note: Class Order [CO 03/823] grants an exemption to foreign authorised deposit-taking institutions (foreign ADIs) who hold an Australian financial services licence from the financial reporting requirements of Division 6 of Part 7.8 on the condition that the foreign entity lodges the financial statements required by subsection 601CK(1) and lodges an auditor's report on those financial statements. Class Order [06/68] grants a similar exemption to foreign licensees (other than foreign ADIs).

Signature

Name

CEAIG T. LENNON

Capacity

- Director of the foreign company
- Secretary of the foreign company
- Duly appointed local agent of the foreign company
- Director or secretary of a company which has been duly appointed as local agent of the foreign company

Company name

ACN/ABN

I verify that the copies annexed to this form are true copies of the documents required to be lodged under Section 601CK(1) of the Corporations Act 2001.

Signature

[Handwritten Signature]

Date signed

/ /

[D] [D] [M] [M] [Y] [Y]

Lodgement

Send completed and signed forms to:
Australian Securities and Investments Commission,
PO Box 4000, Gippsland Mail Centre VIC 3841.

For help or more information

Telephone 03 5177 3988
Email info.enquiries@asic.gov.au
Web www.asic.gov.au