



ANNUAL REPORT

Balance Date 30 June 2005

Report Date 5th September 2005

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FINANCIAL REPORT

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DIRECTORS' REPORT

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WINDFLOW TECHNOLOGY LIMITED
CONSOLIDATED STATEMENT OF FINANCIAL PERFORMANCE
FOR THE YEAR ENDED 30TH JUNE 2005

| | Notes | This Year | | Last Year | |
|--|----------|--------------------|--------------------|--------------------|--------------------|
| | | Group | Parent | Group | Parent |
| | | \$ | \$ | \$ | \$ |
| Operating Revenue | 1 | 401,001 | 159,293 | 294,426 | 277,497 |
| Operating Expenses | 2 | | | | |
| Amortisation of Licences | | 75,038 | 75,038 | 150,076 | 150,076 |
| Cost of Sales | | 98,801 | - | 32,364 | 53,841 |
| Engineering Costs | | 183,721 | 129,576 | 85,388 | 82,271 |
| Research and Development Costs | | 793,962 | 914,064 | 597,240 | 597,138 |
| Marketing Costs | | 203,253 | 211,086 | 96,966 | 89,133 |
| General and Administration Costs | 3 | 741,441 | 581,377 | 535,067 | 441,917 |
| Depreciation | | 331,882 | 238,422 | 287,685 | 249,798 |
| | | 2,428,098 | 2,149,563 | 1,784,786 | 1,664,174 |
| Less Amortisation of Wind Rights Recovered | | - | 217,580 | - | - |
| | | 2,428,098 | 1,931,983 | 1,784,786 | 1,664,174 |
| Share of Associate Deficit | 4 | 233 | - | - | - |
| | | 2,428,331 | 1,931,983 | 1,784,786 | 1,664,174 |
| Net Deficit | | (2,027,330) | (1,772,690) | (1,490,360) | (1,386,677) |
| Net Deficit comprises: | | | | | |
| Parent Interests | | (2,037,045) | (1,772,690) | (1,490,360) | (1,386,677) |
| Minority Interests | | 9,715 | - | - | - |
| Net Deficit | | (2,027,330) | (1,772,690) | (1,490,360) | (1,386,677) |

WINDFLOW TECHNOLOGY LIMITED
CONSOLIDATED STATEMENT OF MOVEMENTS IN EQUITY
FOR THE YEAR ENDED 30TH JUNE 2005

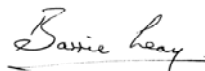
| | | This Year | | Last Year | |
|--|----------|--------------------|--------------------|--------------------|--------------------|
| | | Group | Parent | Group | Parent |
| | | \$ | \$ | \$ | \$ |
| Equity at Beginning of Year | | 5,651,996 | 5,757,063 | 2,143,434 | 2,144,818 |
| Less Prior Period Adjustment | 5 | 20,357 | - | - | - |
| | | 5,631,639 | 5,757,063 | 2,143,434 | 2,144,818 |
| Less | | | | | |
| Net Deficit comprising | | | | | |
| Parent interests | | (2,037,045) | (1,772,690) | (1,490,360) | (1,386,677) |
| Minority Interests | | 9,715 | - | - | - |
| Total Net Deficit | | (2,027,330) | (1,772,690) | (1,490,360) | (1,386,677) |
| Contributions from Owners | | | | | |
| Ordinary Shares Issued during the Year | | 3,302,266 | 3,302,266 | 4,998,922 | 4,998,922 |
| Equity at End of Year | | 6,906,575 | 7,286,639 | 5,651,996 | 5,757,063 |
| Equity at end of year comprises: | | | | | |
| Parent interests | | 6,917,216 | 7,286,639 | 5,651,996 | 5,757,063 |
| Minority Interests | | (10,641) | - | - | - |
| | | 6,906,575 | 7,286,639 | 5,651,996 | 5,757,063 |

WINDFLOW TECHNOLOGY LIMITED
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT THE 30TH JUNE 2005

| | Note: | This Year | | Last Year | |
|-------------------------------------|-------|------------------|------------------|------------------|------------------|
| | | Group | Parent | Group | Parent |
| | | \$ | \$ | \$ | \$ |
| Shareholders' Equity | | | | | |
| Contributed Capital | 8 | 12,283,029 | 12,283,029 | 8,980,763 | 8,980,763 |
| Retained Earnings Account | 9 | (5,365,813) | (4,996,390) | (3,328,767) | (3,223,700) |
| | | 6,917,216 | 7,286,639 | 5,651,996 | 5,757,063 |
| <i>Minority Interest</i> | | | | | |
| Contributed Capital | | 22,375 | | | |
| Retained Earnings Account | | (33,016) | | | |
| | | (10,641) | | | |
| Total Shareholders' Equity | | 6,906,575 | 7,286,639 | 5,651,996 | 5,757,063 |
| Current Liabilities | | | | | |
| Accounts Payable | 11 | 348,186 | 282,505 | 327,820 | 291,734 |
| Total Current Liabilities | | 348,186 | 282,505 | 327,820 | 291,734 |
| Total Equity and Liabilities | | 7,254,761 | 7,569,144 | 5,979,816 | 6,048,797 |
| Current Assets | | | | | |
| Cash on Hand and at Bank | | 3,173,317 | 3,126,721 | 270,975 | 263,495 |
| Term Deposits | 12 | 16,391 | 16,391 | 2,621,583 | 2,621,583 |
| Interest Accrued | 12 | 67 | 67 | 9,821 | 9,821 |
| Accounts Receivable | 12 | 24,684 | 10,890 | 49,168 | 5,625 |
| Prepayments | | 625,090 | 625,090 | 356,965 | 356,965 |
| GST Refund | | 116,812 | - | 105,999 | 105,999 |
| Work in Progress and Stock on Hand | 12 | 1,040,797 | 1,040,797 | 423,196 | 423,196 |
| Other Assets | | 1,690 | 1,356 | 44 | - |
| Total Current Assets | | 4,998,848 | 4,821,312 | 3,837,751 | 3,786,684 |
| Non Current Assets | | | | | |
| Fixed Assets | 13 | 1,087,553 | 1,004,786 | 1,256,318 | 1,171,037 |
| Intangible Assets | 14 | 1,147,816 | 308,687 | 765,450 | 765,450 |
| Advances to Equity Investment | 4 | 20,544 | 20,777 | - | - |
| Advance to Joint Venture | | - | 136,090 | 120,297 | 262,969 |
| Advance to Subsidiary | | - | 408,631 | - | 62,657 |
| Shares - NZ Windfarms Ltd | | - | 846,486 | - | - |
| Shares - Wind Blades Ltd | | - | 22,375 | - | - |
| Total Non Current Assets | | 2,255,913 | 2,747,832 | 2,142,065 | 2,262,113 |
| Total Assets | | 7,254,761 | 7,569,144 | 5,979,816 | 6,048,797 |

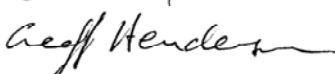
Signed for and on behalf of the Board

Director



Dated 5 September 2005

Director



WINDFLOW TECHNOLOGY LIMITED
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30TH JUNE 2005

| | This Year | | Last Year | |
|---|--------------------|--------------------|--------------------|--------------------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| Cash Flows from operating activities | 20 | | | |
| <i>Cash was provided from:</i> | | | | |
| Receipts from Outwork | 250,064 | - | - | - |
| Receipts from Consulting Fees | 37,145 | 37,145 | 16,388 | 16,388 |
| Funding Received | 11,700 | 11,700 | 59,165 | 59,165 |
| Other Income | 19,938 | 19,938 | 36,652 | 19,688 |
| Interest Received | 85,944 | 93,795 | 161,655 | 161,541 |
| Net GST Inflows | 10,356 | 155,261 | - | - |
| | 415,147 | 317,839 | 273,860 | 256,782 |
| <i>Cash was disbursed to:</i> | | | | |
| Payments to suppliers | 1,968,042 | 1,583,340 | 1,227,849 | 1,051,921 |
| Payments to employees | 562,867 | 458,752 | 427,780 | 392,786 |
| Instalment Payments for Wind Blades | - | 498,147 | 140,035 | 280,073 |
| Interest paid | 459 | 459 | - | - |
| Net GST | - | - | 72,990 | 72,990 |
| Income Tax | - | - | 44 | - |
| | 2,531,368 | 2,540,698 | 1,868,698 | 1,797,770 |
| Net Cash Flows from operating activities | (2,116,221) | (2,222,859) | (1,594,838) | (1,540,988) |
| Cash flows from investing activities | | | | |
| <i>Cash was provided from:</i> | | | | |
| Sale of Fixed Assets | 7,538 | 7,538 | 75,791 | 151,581 |
| Disbursed from Term Deposit Accounts | 2,605,192 | 2,605,192 | 525,906 | 525,906 |
| | 2,612,730 | 2,612,730 | 601,697 | 677,487 |
| <i>Cash was disbursed to:</i> | | | | |
| Development of the Wind Turbine and associated costs | - | - | 356,814 | 356,814 |
| Acquisition of Intangible Assets | 168,465 | - | - | - |
| Purchase of other Fixed Assets | 85,695 | 80,030 | 78,958 | 44,065 |
| Disbursed to Term Deposit Accounts | 356,035 | 356,035 | 3,130,570 | 3,130,570 |
| | 610,195 | 436,065 | 3,566,342 | 3,531,449 |
| Net Cash Flows from investing activities | 2,002,535 | 2,176,665 | (2,964,645) | (2,853,962) |
| Cash flows from financing activities | | | | |
| <i>Cash was provided from:</i> | | | | |
| Issue of Shares | 3,302,266 | 3,302,266 | 4,998,971 | 4,998,971 |
| Advance from Joint Venture Company | - | 104,504 | - | - |
| Advance from Subsidiary | - | 8,184 | - | - |
| | 3,302,266 | 3,414,954 | 4,998,971 | 4,998,971 |
| <i>Cash was disbursed to:</i> | | | | |
| Prospectus Costs | 265,461 | 173,753 | 134,548 | 134,548 |
| Advance to Subsidiary | - | 311,004 | - | 45,000 |
| Advance to Equity Partner | 20,777 | 20,777 | - | - |
| Advance to Joint Venture Partner | - | - | 127,013 | 254,026 |
| | 286,238 | 505,534 | 261,561 | 433,574 |
| Net Cash Flows from financing activities | 3,016,028 | 2,909,420 | 4,737,410 | 4,565,397 |
| Net Increase (Decrease) in cash held | 2,902,342 | 2,863,226 | 177,927 | 170,447 |
| Cash at beginning of year | 270,975 | 263,495 | 93,048 | 93,048 |
| Cash at end of year | 3,173,317 | 3,126,721 | 270,975 | 263,495 |

WINDFLOW TECHNOLOGY LIMITED
STATEMENT OF ACCOUNTING POLICIES
FOR THE YEAR ENDED 30TH JUNE 2005

REPORTING ENTITY

Windflow Technology Limited is a company registered under the Companies Act 1993.

Windflow Technology Limited is an issuer for the purpose of the Financial Reporting Act 1993. The financial statements of the Company and Group have been prepared in accordance with the Financial Reporting Act 1993.

MEASUREMENT BASE

The accounting principles, recognised as appropriate for the measurement and reporting of earnings and financial position on an historical cost basis, are followed by the group.

NATURE OF BUSINESS

Wind power development.

The Company operates solely within New Zealand.

SPECIFIC ACCOUNTING POLICIES

The financial statements are prepared in accordance with New Zealand generally accepted accounting practice. The accounting policies that materially affect the measurement of the financial performance, financial position and cash flows are set out below:

Basis of Consolidation

The consolidated financial statements are prepared from the financial statements of the Company and its subsidiaries.

All significant inter company transactions are eliminated on consolidation.

Subsidiaries are entities that are controlled, either directly or indirectly, by the Company. The subsidiaries are combined using the purchase method.

The associate company is reflected in the consolidated financial statements using the equity method whereby the group's share of the retained deficit of this associate is included in consolidated earnings and its share of post acquisition increases and decreases in net assets in the consolidated Statement of Financial Position.

WINDFLOW TECHNOLOGY LIMITED
STATEMENT OF ACCOUNTING POLICIES
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

Revenue Recognition

Revenues are recognised when services are performed.

Investment Revenue

Interest revenue from investments and fixed deposits is recognised on an accruals basis.

Stock on Hand

Stock of component parts has been valued at lower of cost and market value.

Work in Progress

Work in Progress has been valued at the lower of cost and net realisable value.

Goods and Services Tax

The accounts have been prepared on a GST exclusive basis; except that all receivables and payables are shown GST inclusive to the extent that GST is payable or receivable on the transaction that gave rise to the payable or receivable.

Financial Instruments

Financial instruments recognised within the Consolidated Statement of Financial Position include cash and bank deposits, receivables and payables. The valuation and recognition method adopted for each of these instruments is disclosed in the policy statement associated with each particular item.

Taxation

Taxation recognised in the Statement of Financial Performance for the period is based on the accounting result, adjusted for timing differences between accounting and income taxation rules.

Any income tax expenses charged to the statement of financial performance includes both the current year's provision and the income tax effect of timing differences calculated using the liability method.

A deferred tax benefit relating to tax losses is recognised only if there is a virtual certainty of realisation.

There is no deferred tax asset or liability as at the 30th June 2005.

WINDFLOW TECHNOLOGY LIMITED
STATEMENT OF ACCOUNTING POLICIES
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

Valuation of Assets

Receivables

Receivables are stated at their estimated realisable value.

Fixed Assets

The Company has the following classes of fixed assets:

| | |
|------------------------------------|----------------|
| Wind Turbine and Associated Assets | Motor Vehicles |
| Office Equipment | |

All fixed assets are recorded at cost.

Depreciation is provided for on a straight line basis on all tangible fixed assets at depreciation rates calculated to allocate the assets cost less estimated residual value, over their estimated useful lives.

No depreciation is charged on part constructed assets.

Major depreciation periods are:

| | | |
|--|-------------|-------|
| Wind Turbine and Associated Assets (Commenced on completion, 1 ST July 2003) | 8.0 to 10.0 | years |
| Motor Vehicles | 4.6 | years |
| Office Equipment | 2.8 to 8.3 | years |

Intangibles

1. Research and Development Costs

Research expenditure is recognised in the statement of financial performance in the period in which it is incurred.

Development costs are deferred where future benefits are expected to exceed those costs, otherwise such costs are recognised in the statement of financial performance in the period in which they are incurred.

Development expenditure, recognised as an asset, is stated at cost and amortised in the statement of financial performance over the period of expected benefits.

All other development expenditure is recognised in the statement of financial performance as incurred.

2. Licences

Fair value of the licences, being the TLG patent licence together with the option to obtain wind farm development rights ("wind rights" for short) was determined by the Directors. A summary of the terms and conditions in regard to the acquisition of this intellectual property was listed under clauses 7 and 11, note 17.4 of the Prospectus, dated 9th July 2001. Refer also to the Prospectus dated 28th July 2003 Statement of Accounting Policies, subheading "Licences" on page 21.

The TLG patent licence is valued at fair value and amortised to the statement of financial performance on a straight line basis over the estimated useful life, this has been determined to be 8 years and the write off to be one eighth, per financial period.

WINDFLOW TECHNOLOGY LIMITED
STATEMENT OF ACCOUNTING POLICIES
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

Wind rights were historically amortised over their estimated useful life of 8 years and the write off to be one eighth, per financial period. With the confirmation of the wind right option, the Directors consider that the wind rights now have a useful life of 70 years, being the life of the licence. Wind rights will now be amortised evenly over this useful life.

On the 30th June 2005, the Directors transferred the wind rights to NZ Windfarms Limited for \$ 600,305, being the original cost to Windflow Technology Limited.

Employee Entitlements

A liability for annual leave and long service leave is accrued and recognised in the statement of financial position. The liability is equal to the present value of the estimated future cash outflows as a result of employee services provided at balance date.

A share option plan to the benefit of employees of the Company is in existence. (Refer Note 10).

Foreign Currency Transactions

Transactions in foreign currencies are converted at the New Zealand rate of exchange ruling at the date of the transaction.

Changes in Accounting Policies

There have been no changes in accounting policies during the year.

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005

| | 30th June 2005 | | 30th June 2004 | |
|----------|--|---------------|----------------------------------|---------------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 1 | Operating Revenue | | | |
| | Operating Revenue include | | | |
| | 33,860 | 33,860 | 18,387 | 18,387 |
| | 269,495 | 19,938 | 36,341 | 19,526 |
| | 11,700 | 11,700 | 62,165 | 62,165 |
| | 85,946 | 93,795 | 177,533 | 177,419 |
| | ----- | ----- | ----- | ----- |
| | 401,001 | 159,293 | 294,426 | 277,497 |
| 2 | Operating Expenses | | | |
| | Operating Expenses include: | | | |
| | 75,038 | 75,038 | 150,076 | 150,076 |
| | 793,962 | 914,064 | 597,240 | 597,138 |
| | 10,675 | 10,675 | 4,000 | 4,000 |
| | 72,250 | 72,250 | 87,656 | 75,000 |
| | 20 | 13 | 50 | 50 |
| | 80,647 | 23,147 | 57,770 | 16,500 |
| 3 | Prospectus Costs | | | |
| | General and Administration Costs include: | | | |
| | 340,323 | 229,901 | 90,744 | 83,756 |
| 4 | Investments in Associates | | | |
| | At the 30 th June 2005 the Company held a 20% shareholding in Windpower Otago Limited. The principal activity of this Company is the development of wind farms, balance date is the 30 th June. | | | |
| | Results of Associate | | | |
| | <i>Statement of Financial Position</i> | | | |
| | 367 | - | - | - |
| | 10,307 | - | - | - |
| | 10,076 | - | - | - |
| | (233) | - | - | - |
| | <i>Statement of Financial Performance</i> | | | |
| | (233) | - | - | - |
| | <i>Details of Amounts recognised are:</i> | | | |
| | 20,777 | | | |
| | 233 | | | |
| | ----- | | | |
| | 20,544 | - | - | - |
| 5 | Prior Period Adjustment | | | |
| | This takes into account the change in treatment as regards the consolidation of Wind Blades Limited, which was previously treated as a joint venture. It has been determined this year that Windflow Technology Limited controls this entity and therefore a full consolidation has taken place. | | | |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

| | 30th June 2005 | | 30th June 2004 | |
|---|----------------------------------|---------------|----------------------------------|---------------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 6 | Taxation | | | |
| Operating Deficit | 2,037,045 | 1,772,690 | 1,490,360 | 1,386,677 |
| Prima facie taxation expense at 33% | - | - | - | - |
| Less taxation effect of permanent differences: | | | | |
| Amortisation of Intangibles | 75,038 | 75,038 | 150,076 | 150,076 |
| Amortisation of Wind Rights Recovered | - | (217,580) | - | - |
| Prospectus Costs | 340,323 | 229,901 | 90,744 | 83,756 |
| Non Deductible Entertainment & Legal Fees | 5,562 | 5,562 | - | - |
| | ----- | ----- | ----- | ----- |
| | 420,923 | 92,921 | 240,820 | 233,832 |
| | ----- | ----- | ----- | ----- |
| | 1,616,122 | 1,679,769 | 1,249,540 | 1,152,845 |
| Losses brought forward | 2,458,283 | 2,360,201 | 1,208,743 | 1,207,356 |
| | ----- | ----- | ----- | ----- |
| Deficit and losses carried forward for taxation purposes | 4,074,405 | 4,039,970 | 2,458,283 | 2,360,201 |
| | ----- | ----- | ----- | ----- |
| There is no income tax payable for the period. | | | | |
| RWT on Interest received to be refunded | 1,524 | 1,356 | - | - |
| 7 | Imputation Credit Account | | | |
| Balance at beginning of period | - | - | - | - |
| Income Tax refunded during the year | - | - | - | - |
| | ----- | ----- | ----- | ----- |
| | - | - | - | - |
| Income tax payments during the year: | | | | |
| Resident Withholding Tax paid | 1,524 | 1,356 | - | - |
| | ----- | ----- | ----- | ----- |
| Balance at end of period | (1,524) | (1,356) | - | - |
| | ----- | ----- | ----- | ----- |
| 8 | Share Capital | | | |
| Balance at beginning of period | 8,980,763 | 8,980,763 | 3,981,841 | 3,981,841 |
| Ordinary Shares Issued | 3,302,266 | 3,302,266 | 4,998,922 | 4,998,922 |
| | ----- | ----- | ----- | ----- |
| Total Share Capital | 12,283,029 | 12,283,029 | 8,980,763 | 8,980,763 |
| | ----- | ----- | ----- | ----- |
| Number of shares on issue | 6,675,303 | 6,675,303 | 5,238,231 | 5,283,231 |

Ordinary shares issued were a result of rights issues as per the Prospectus registered 28th April 2005 and the Prospectus registered on 28th July 2003. All ordinary shares have equal voting rights and share equally in dividends and surplus on winding up.

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

| | 30 th June 2005 | | 30 th June 2004 | |
|------------------------------------|----------------------------|-------------|----------------------------|-------------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 9 Retained Earnings Account | | | | |
| Balance at beginning of the year | (3,328,767) | (3,223,700) | (1,838,407) | (1,837,023) |
| Net Deficit | (2,037,046) | (1,772,690) | (1,490,360) | (1,386,677) |
| | ----- | ----- | ----- | ----- |
| Balance at end of year | (5,365,813) | (4,996,390) | (3,328,767) | (3,223,700) |

10 Share Option Plan

The Company entered into a share option plan with Mr G Henderson, the Chief Executive Officer and a Director on the 20th January 2002.

This put into effect the terms of the Licence Agreement as outlined in the prospectus, dated 9th July 2001, and as summarised below.

The agreement transferring the TLG Licence from Wind Torque Limited to Windflow Technology Limited provided that a royalty was payable to Mr G Henderson for each of the first 100 wind turbines sold or retained by the Company (other than any turbines retained as demonstration turbines). The amount of the royalty is \$10,000 per turbine plus 10,000 share options of \$1.00 each. The total number of options is limited to 20% of the Windflow Technology Limited shares on issue.

Each option to purchase shares will lapse if not exercised within six months of issue. The option price is \$1.00, or if a market price for Windflow Technology Limited shares has been established at a level which raises concerns for the Directors that the option price is not fair and reasonable to existing shareholders, the option price will be determined as the average market price in the last month of the quarter less one third.

As at 30th June 2005 no turbines had been sold or retained by the Company (other than the prototype / demonstration turbine at Gebbies Pass) and therefore no royalty payments have been made to Mr G Henderson nor any options issued to him.

The Company, on the 19th December 2002, entered into a share option plan for the benefit of all employees of the Company who have attained the age of twenty years and, who have been employed by the Company, for at least one year.

The selection of the participants and the number of shares comprised in options shall be determined by the Directors. Any offer of an option shall be at a price equal to the market price at the date of the resolution by the Directors to make an offer.

As at the 30th June 2005 19,759 options had been issued to employees (2004 10,707 options).

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

| | 30 th June 2005 | | 30 th June 2004 | |
|---|----------------------------|-----------|----------------------------|-----------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 11 Current Liabilities | | | | |
| Current liabilities consist of accounts payable and accruals, which are unpaid as at the period end. | | | | |
| Trade Payables | 223,046 | 169,782 | 289,470 | 237,834 |
| Trade Payables – Asset Purchases | 19,816 | 9,698 | 3,456 | 21,742 |
| Employee entitlements | 46,071 | 43,772 | 34,894 | 32,158 |
| GST Payable | 59,253 | 59,253 | - | - |
| | ----- | ----- | ----- | ----- |
| | 348,186 | 282,505 | 327,820 | 291,734 |
| 12 Current Assets | | | | |
| <u>Term Deposits</u> | | | | |
| Term Deposits maturing within six months | 16,391 | 16,391 | 2,621,583 | 2,621,583 |
| Term Deposits maturing within one year | - | - | - | - |
| | ----- | ----- | ----- | ----- |
| | 16,391 | 16,391 | 2,621,583 | 2,621,583 |
| The carrying amounts of cash, deposits and receivables are at fair value and are the maximum exposure to credit risk. The group is not exposed to any concentration of credit risk. | | | | |
| <u>Accounts Receivable</u> | | | | |
| Trade Receivables | 24,684 | 10,890 | 49,168 | 5,625 |
| Interest Accrued | 67 | 67 | 9,821 | 9,821 |
| | ----- | ----- | ----- | ----- |
| | 24,751 | 10,957 | 58,989 | 15,446 |
| <u>Stock on Hand and Work in Progress</u> | | | | |
| Wind turbine component parts | 375,608 | 375,608 | 128,121 | 128,121 |
| Completed wind blades | 660,000 | 660,000 | 258,427 | 258,427 |
| Materials for wind blades | 5,189 | 5,189 | 36,648 | 36,648 |
| | ----- | ----- | ----- | ----- |
| | 1,040,797 | 1,040,797 | 423,196 | 423,196 |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

| | 30 th June 2005 | | 30 th June 2004 | |
|--|----------------------------|-----------|----------------------------|-----------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 13 Fixed Assets | | | | |
| Wind Turbine and Associated Assets | | | | |
| Site Costs | 33,520 | 33,520 | 33,520 | 33,520 |
| Turbine | 972,584 | 972,584 | 972,584 | 972,584 |
| Tooling, Equipment, Moulds | 647,607 | 395,607 | 446,879 | 325,408 |
| | ----- | ----- | ----- | ----- |
| Total Wind Turbine and Associated Assets | 1,653,711 | 1,401,711 | 1,452,983 | 1,331,512 |
| Less Accumulated Depreciation | 593,743 | 424,510 | 247,330 | 209,888 |
| | ----- | ----- | ----- | ----- |
| | 1,059,968 | 977,201 | 1,205,653 | 1,121,624 |
| | | | | |
| Motor Vehicles | 11,556 | 11,556 | 17,342 | 17,342 |
| Less Accumulated Depreciation | 3,523 | 3,523 | 8,147 | 8,147 |
| | ----- | ----- | ----- | ----- |
| | 8,033 | 8,033 | 9,195 | 9,195 |
| | | | | |
| Office Equipment | 136,581 | 136,581 | 133,718 | 132,022 |
| Less Accumulated Depreciation | 117,029 | 117,029 | 92,248 | 91,804 |
| | ----- | ----- | ----- | ----- |
| | 19,552 | 19,552 | 41,470 | 40,218 |
| | | | | |
| Total Fixed Assets | 1,087,553 | 1,004,786 | 1,256,318 | 1,171,037 |
| | ----- | ----- | ----- | ----- |
| | | | | |
| 14 Intangible Assets | | | | |
| Fair value of TLG licence | 600,305 | 600,305 | 600,305 | 600,305 |
| Less Accumulated Amortisation | 291,618 | 291,618 | 217,580 | 217,580 |
| | ----- | ----- | ----- | ----- |
| | 308,687 | 308,687 | 382,725 | 382,725 |
| | | | | |
| Fair value of Wind Rights | 600,304 | - | 600,304 | 600,304 |
| Less Accumulated Amortisation | 217,580 | - | 217,579 | 217,579 |
| | ----- | ----- | ----- | ----- |
| | 382,724 | - | 382,725 | 382,725 |
| | | | | |
| Resource consent charges | 246,983 | - | - | - |
| Wind farm development costs to date | 209,422 | - | - | - |
| | ----- | ----- | ----- | ----- |
| | 1,147,816 | 308,687 | 765,450 | 765,450 |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

14 Intangible Assets (Continued)

The ownership of the TLG patent licence and wind rights were transferred from a subsidiary company, Wind Torque Limited, since liquidated, on the 20th January 2002 to Windflow Technology Limited by way of an agreement between the Company, its subsidiary and Mr G Henderson.

The wind rights, at a fair value as determined by the Directors, were transferred to the ownership of the subsidiary company, NZ Windfarms Limited on the 30th June 2005. This fair value was determined to be the original cost to Windflow Technology Limited.

The amortisation over the previous three years applicable to the wind rights has been added back as a recoverable item and separately disclosed within the Statement of Financial Performance for the parent only. There are no taxation implications in regard to this matter.

The TLG patent licence has been retained and continues to be amortised.

15 Subsidiary Companies

NZ Windfarms Limited

The shares of NZ Windfarms Limited are owned 100% by Windflow Technology Limited. The balance date of NZ Windfarms Limited is the 30th June 2005.

Pacific Windfarms Limited

The shares of Pacific Windfarms Limited are owned 100% by Windflow Technology Limited, the Company has not traded since incorporation. The balance date of Pacific Windfarms Limited is the 30th June 2005.

Wind Blades Limited

Windflow Technology Limited has a 50% share holding in Wind Blades Limited. It has been determined that Windflow Technology Limited controls this entity. The balance date of Wind Blades Limited is the 30th June 2005.

16 Commitments

Capital Commitments as at balance date totalled \$572,387.
These are costs associated with the construction of the wind turbines.
(30th June 2004 \$1,604,457.)

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

17 Financial Instruments

Credit Risk

To the extent that the Company has a receivable from another party, there is a credit risk in the event of non performance by that counter party. Financial instruments, which potentially subject the Company to credit risk, principally consist of bank balances, receivables, and term deposits.

The Company monitors the credit quality of its investments and manages its exposure to credit risk.

Concentrations of credit risk

The Company does not have any significant concentrations of credit risk apart from its deposits with a large and reputable bank.

Currency Risk

The Company has exposure to foreign exchange risk as a result of transactions denominated in foreign currencies, arising from normal trading activities.

Such activities are not of a material nature.

Interest Rate Risk

The Company has exposure to interest rate risk to the extent that it invests for a fixed term at fixed rates.

Credit Facilities

The Company has no credit facilities, other than trade creditors.

Fair Values

The estimated fair values of financial instruments do not differ from the carrying values.

18 Significant Events After Balance Date

Repairs have been completed on the prototype turbine at Gebbies Pass and it was reinstalled in August 2005. A claim was lodged with the insurers for the total cost of rebuilding the prototype. The insurers advised in July 2005 that this claim is acceptable. The amount to be claimed has not yet been finalised because the final cost of the repairs has yet to be determined.

There were no other significant events after balance date.

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

19 Related Party Disclosures

All related party transactions are at normal market terms and conditions.
No related party debts have been written off or forgiven.

The Company paid project management fees and fees for services related to the prospectus issues to one Director, Mr K McConnell \$13,309 (2004 \$64,546), and the fees were charged on normal commercial terms.

The amount outstanding at balance date to Mr McConnell, and included within Accounts Payable is \$nil. (2004 \$1,809).

| | 30 th June 2005 | | 30 th June 2004 | |
|--|----------------------------|-------------|----------------------------|-------------|
| | Group | Parent | Group | Parent |
| | \$ | \$ | \$ | \$ |
| 20 Reconciliation of reported deficit with cash flows from operating activities | | | | |
| Net Deficit | (2,027,330) | (1,772,690) | (1,490,360) | (1,386,677) |
| <i>Less Non Cash Items and non operating items:</i> | | | | |
| Amortisation of Licences | 75,038 | 75,038 | 150,076 | 150,076 |
| Amortisation Recovered Wind Rights | - | (217,580) | - | - |
| Depreciation | 331,882 | 238,422 | 287,685 | 249,798 |
| Interest Charged | 459 | 459 | 3,044 | - |
| Prospectus Costs | 347,311 | 229,901 | 83,756 | 83,756 |
| Loss on Investment | - | - | 16,273 | 17,657 |
| | ----- | ----- | ----- | ----- |
| | 754,690 | 326,240 | 540,834 | 501,287 |
| | ----- | ----- | ----- | ----- |
| Cash Flow from Operations before working capital changes | (1,272,640) | (1,446,450) | (949,526) | (885,390) |
| <i>Movements in Working Capital</i> | | | | |
| <i>Increase (Decrease) in accounts payable excluding asset purchases</i> | 20,366 | (59,066) | 242,655 | 188,912 |
| Decrease (Increase) in tax refund | (1,646) | (1,356) | (44) | - |
| Decrease (Increase) in accounts receivable & interest accrued | 34,238 | 4,489 | (52,080) | (8,667) |
| Decrease (Increase) in Work in Progress | (617,601) | (617,601) | (423,196) | (423,196) |
| Decrease (Increase) in prepayments | (268,125) | (268,125) | (352,741) | (352,741) |
| Decrease (Increase) in GST receivable | (10,813) | 165,250 | (59,906) | (59,906) |
| | ----- | ----- | ----- | ----- |
| | (843,581) | (776,409) | (645,312) | (655,598) |
| | ----- | ----- | ----- | ----- |
| Net Cash Flows from Operating Activities | (2,116,221) | (2,222,859) | (1,594,838) | (1,540,988) |
| | ===== | ===== | ===== | ===== |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

21 Prospective Financial Information

In July 2003 the Company registered a prospectus for the issue of shares. The following information is a comparison of the projected financial statements of Windflow Technology Limited from the 2003 Prospectus for the year ended 30th June 2005 with the actual result (parent) from the same period, and from the 2003 Prospectus for the year ended 30th June 2004 with the actual result (parent) for the same period.

Statement of Financial Performance

| | 2003 Proj'ns to 30th June 2005 | Actual to 30th June 2005 | 2003 Proj'ns to 30th June 2004 | Actual to 30th June 2004 |
|---|---|---|---|---|
| | \$ | \$ | \$ | \$ |
| Operating Revenue | | | | |
| Consultancy Fees Received | - | 33,860 | - | 18,387 |
| Grants Received | - | 11,700 | - | 62,165 |
| Interest Received | 60,000 | 93,795 | 4,000 | 177,419 |
| Sale of installed Turbines | 13,500,000 | - | 4,050,000 | - |
| Maintenance Fees Received | 60,000 | - | - | - |
| Sale of Power | 104,000 | 19,938 | 104,000 | 19,526 |
| | ----- | ----- | ----- | ----- |
| | 13,724,000 | 159,293 | 4,158,000 | 277,497 |
| Operating Expenses | | | | |
| Amortisation of Licences & Wind Rights | 183,000 | 75,038 | 183,000 | 150,076 |
| Cost of Sales | - | - | - | 53,841 |
| Engineering Costs | 14,166,000 | 129,576 | 5,468,000 | 82,271 |
| Research and Development Costs | 426,000 | 914,064 | 526,000 | 597,138 |
| Marketing Costs | 320,000 | 211,086 | 154,000 | 89,133 |
| General and Administration Costs | 447,000 | 581,377 | 469,000 | 441,917 |
| Depreciation | 127,000 | 238,422 | 127,000 | 249,798 |
| | ----- | ----- | ----- | ----- |
| | - | 2,149,563 | 6,927,000 | 1,664,174 |
| Less Amortisation of Wind Rights Rec'd | - | 217,580 | - | - |
| | ----- | ----- | ----- | ----- |
| | 15,669,000 | 1,931,983 | 6,927,000 | 1,664,174 |
| | ----- | ----- | ----- | ----- |
| Net Deficit | 1,945,000 | 1,772,690 | 2,769,000 | 1,386,677 |
| Statement of Cash Flows | | | | |
| Opening Balance | 2,413,000 | 263,495 | 165,000 | 93,048 |
| Net cash inflows (outflows) from operating activities | (2,056,000) | (2,222,859) | (2,637,000) | (1,540,988) |
| Net cash inflows (outflows) from investing activities | - | 2,176,665 | (450,000) | (2,853,962) |
| Net cash inflows (outflows) from financing activities | - | 2,909,420 | 5,335,000 | 4,565,397 |
| | ----- | ----- | ----- | ----- |
| Net Increase (Decrease) in cash held | 2,056,000 | 2,863,226 | 2,248,000 | 170,447 |
| | ----- | ----- | ----- | ----- |
| Closing Balance | 357,000 | 3,126,721 | 2,413,000 | 263,495 |
| | ----- | ----- | ----- | ----- |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

Statement of Financial Position

| | 2003 Proj'ns to 30th June 2005 \$ | Actual to 30th June 2005 \$ | 2003 Proj'ns to 30th June 2004 \$ | Actual to 30th June 2004 \$ |
|-------------------------------------|--|--------------------------------------|--|--------------------------------------|
| Shareholder' Equity | | | | |
| Share Capital | 9,415,000 | 12,283,029 | 9,415,000 | 8,980,763 |
| Retained Earnings Account | (6,606,000) | (4,996,390) | (4,661,000) | (3,223,700) |
| | ----- | ----- | ----- | ----- |
| | 2,809,000 | 7,286,639 | 4,754,000 | 5,757,063 |
| Current Liabilities | | | | |
| Accounts Payable | 95,000 | 282,505 | 95,000 | 291,734 |
| Provision for Warranty | 837,000 | - | 203,000 | - |
| | ----- | ----- | ----- | ----- |
| | 932,000 | 282,505 | 298,000 | 291,734 |
| Total Equity and Liabilities | 3,741,000 | 7,569,144 | 5,052,000 | 6,048,797 |
| | ----- | ----- | ----- | ----- |
| Current Assets | | | | |
| Cash on Hand and at Bank | 357,000 | 3,126,721 | 2,413,000 | 263,495 |
| Term Deposits | 200,000 | 16,391 | 200,000 | 2,621,583 |
| Interest Accrued | - | 67 | - | 9,821 |
| Accounts Receivable | - | 10,890 | - | 5,625 |
| Prepayments / Retentions | 1,350,000 | 625,090 | 405,000 | 356,965 |
| GST Refund | 187,000 | - | 76,000 | 105,999 |
| Work in Progress | - | 1,040,797 | - | 423,196 |
| Other Assets | - | 1,356 | - | - |
| | ----- | ----- | ----- | ----- |
| | 2,094,000 | 4,821,312 | 3,094,000 | 3,786,684 |
| Non Current Assets | | | | |
| Fixed Assets | 848,000 | 1,004,786 | 976,000 | 1,171,037 |
| Intangible Assets | 799,000 | 308,687 | 982,000 | 765,450 |
| Advances to Equity Investment | - | 20,777 | - | - |
| Advance to Joint Venture | - | 136,090 | - | 262,969 |
| Advance to Subsidiary | - | 408,631 | - | 62,657 |
| Shares – NZ Windfarms Ltd | - | 846,486 | - | - |
| Shares – Wind Blades Ltd | - | 22,375 | - | - |
| | ----- | ----- | ----- | ----- |
| | 1,647,000 | 2,747,832 | 1,958,000 | 2,262,113 |
| Total Assets | 3,741,000 | 7,569,144 | 5,052,000 | 6,048,797 |
| | ----- | ----- | ----- | ----- |

WINDFLOW TECHNOLOGY LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30TH JUNE 2005 (Continued)

The major variances between the projections and actual are as follows:

The sale of wind turbines had not commenced, as projected, during the 2003, 2004 or 2005 financial year.

In 2005, the engineering costs variance is due to the timing of construction of the wind turbines and the capitalisation policy adopted by the Directors of recording these costs as work in progress.

Additional delays and research and development costs were incurred during the 2005 financial year in order to further meet the stringent operating noise levels required by the Gebbies Pass resource consent. Due to the damage to the turbine at Gebbies Pass, in March 2005, additional research and development costs were incurred during this financial year.

Depreciation did not commence until the installation of the first turbine was completed at Gebbies Pass. The date was determined to be from the 1st July 2003.

22 Contingent Liabilities

As at the 30th June 2005 no contingent liabilities existed. (30th June 2004 nil.)

Audit Report

To the Shareholders of Windflow Technology Limited.

We have audited the financial report on pages 2 to 19. The financial report provides information about the past financial performance and financial position of the company and group as at 30 June 2005. This information is stated in accordance with the accounting policies set out in the Statement of Accounting Policies on pages 5 to 8.

Directors Responsibilities

The directors are responsible for the preparation of a financial report which gives a true and fair view of the financial position of the company and group as at 30 June 2005 and the results of its operations and cash flows for the year ended on that date.

Auditors' Responsibilities

It is our responsibility to express an independent opinion on the financial report presented by the directors and report our opinion to you.

Basis of Opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial report. It also includes assessing:

- the significant estimates and judgements made by the directors in the preparation of the financial report; and
- whether the accounting policies are appropriate to the company and group circumstances, consistently applied and adequately disclosed.

We conducted our audit in accordance with New Zealand Auditing Standards. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to obtain reasonable assurance that the financial report is free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial report.

Other than in our capacity as auditor we have no relationship with, or interests in, the company or its subsidiary.

Unqualified Opinion

We have obtained all the information and explanations we have required.

In our opinion:

- proper accounting records have been kept by the company as far as appears from our examination of those records; and
- the financial report on pages 2 to 19
 - complies with generally accepted accounting practice in New Zealand;
 - gives a true and fair view of the financial position of the company and group as at 30 June 2005 and the results of operations and cash flows for the year ended on that date.

Our audit report was completed on 5 September 2004 and our unqualified opinion is expressed as at that date.

Goldsmit Fox PKF
GOLDSMITH FOX PKF
Christchurch

DIRECTORY

The Directors of Windflow Technology Ltd are:

Barrie Leay, Chairman of Directors
45 Ledbury Rd, Nelson

Barrie Leay is currently Chairman of Ecodyne Limited, a company established to develop environmentally benign forms of power generation, Chairman of Broadband Networks Limited, Chairman of Bio Refineries Limited, Chairman of SwimmingFish Pacific Limited, Director of ThePacific.net, Director of Pantenna Limited Managing Director of e-services Limited, an Internet company involved in energy networks and energy efficiency and founder Chairman of the APEC Energy Business Network in the Asia Pacific region. Barrie has been a leading figure in the reforms of electricity industries and the establishment of competitive electricity markets in New Zealand and other APEC economies.



Keith McConnell, Director
12 Balfour Rd, Auckland



Keith has served as Chief Executive Officer of a number of commercial entities over the last 15 years. These include John Edmond Ltd, Donaghy Downs Pty Ltd, The Power Company Ltd, United Electricity Ltd, Paykel Ltd and most recently Fruehauf Pacific Ltd. His involvement with wind energy first arose during his tenure with The Power Company Ltd where he sponsored a wind testing programme at three sites in Southland. Keith has also been involved in several successful start-up ventures (eg Metering Systems Ltd and Supply Solutions) and has a good understanding of the issues involved in such ventures.

Keith is presently acting in a part time executive role within Windflow by assisting with many of the commercial matters.

Geoff Henderson, Director and Chief Executive Officer
12 Scotston Avenue, Christchurch

A registered mechanical engineer, Geoff Henderson has been involved in wind power engineering for twenty years, including seven years in California and England working at the forefront of wind power technology. During that time he invented the torque limiting gearbox (TLG) system which has been patented in New Zealand, Australia, and the USA. In 1994 he received the Communications Award from the Institution of Professional Engineers (IPENZ) for his contribution to the engineering profession as a proponent of wind power. Geoff is past-chairman of the Canterbury Branch of IPENZ and in 2005 was elected a Fellow of IPENZ. He is also a director of the Aeolian Property Company Ltd and four companies in which Windflow has shares, New Zealand Windfarms Ltd, Wind Blades Ltd, Windpower Otago Ltd and Pacific Windfarms Ltd (non-trading).



Heugh Kelly, Director
Shegadeens Road, R.D. 1, Wellsford

Heugh Kelly is a barrister and solicitor with over 20 years experience of commercial law. Educated at Auckland Grammar School and the University of Auckland, he has been in practice on his own account since 1984. He is a director of the Environmental Defence Society which is a position he has held since 1981 and was a member of the legal committee of the Maruia Society for some years.



The Directors of New Zealand Windfarms Ltd are:



Derek Walker, Director
41A Elmira Ave, Palmerston North

Derek is a professional electrical engineer and a member of the Institute of Directors and the Institute of Management. His association with windfarms began in 1998 with the building of the Tararua Wind Farm when he was CEO of Central Power who funded and built the farm (it has since been sold to TrustPower). Derek's governance experience includes Palmerston North Airport Limited, Palmerston North City Holdings, The Bio Commerce Centre, and the Central Energy Trust.

Vicki Buck, Director
14 Jane Deans Close, Christchurch

Vicki Buck is the Development Manager at Christchurch Polytechnic Institute of Technology. She has an M.A. (Hons) degree and was Mayor of Christchurch from 1989 until she stood down in 1998. Since then she has been heavily involved in establishing two new state schools in Christchurch. She is also a director of Jade Stadium Ltd and Brylton Software Ltd.



Juliet McKee, Director
23A Braithwaite St, Wellington

Juliet is an economist and company director whose board appointments include Warren and Mahoney, NZ Book Council, Marsden School, and the Centre for Corporate and Institutional Governance at Massey University. Previous assignments have been diverse - as a reporter for the BBC in Tunisia, a financial analyst for Shell in Gabon, and 3 year stints with the United Nations in Geneva and the Commonwealth Secretariat in London, among others. She was awarded the Commonwealth Medal in 1990 and the QSO for public services in 1996. She has also been Chairman of the Wellington Branch of the Institute of Directors.

Barrie Leay and Keith McConnell are also Directors of New Zealand Windfarms Ltd.

Staff

| | |
|-----------------------------|--|
| Senior Mechanical Engineer | Warwick Payne |
| Mechanical Engineer/Analyst | Francis Jackson |
| Mechanical Engineer | Gavin Williams |
| Mechanical Engineer/Analyst | Emma Patrick |
| Mechanical Engineer/Analyst | Jamie Wallace |
| Senior Electrical Engineer | Wernher Roding |
| Electrical Engineer | Magnus Koldau |
| Marketing Manager | Chris Freear (Seconded to NZWL as CEO) |
| Office Manager | Terry Moon |
| Procurement Manager | Alan White |
| Marketing Co-ordinator | Sheralee MacDonald |
| Receptionist | Marie Munford |

Solicitor

Guy Mortlock
Mortlocks
137 Armagh St
Christchurch

Accountant

Mike Keyse
HFK Ltd
12 Main North Road
Christchurch

Auditor

Goldsmith Fox PKF
236 Armagh St
Christchurch

Share Registry

BK Registries Ltd
138 Tancred St
Ashburton

Bankers

Kiwibank Limited
Level 12, 155 The Terrace
Wellington

Insurance Brokers

Marsh Limited
Level 4, 233 Cambridge Terrace
Christchurch

Principal Suppliers

| | |
|-----------------------|--|
| Blades | Wind Blades Ltd of Auckland |
| Gearbox | AH Gears Ltd of Auckland |
| Electrical Control | Bremca Ltd of Christchurch |
| Hub | Farra Bros Ltd of Dunedin |
| Generator | Newage International Ltd of UK (Sydney office) |
| Nacelle Assembly | ASCO (NZ) Ltd |
| Pallet | Southern Cross Engineering Ltd of Christchurch |
| Site Works | Smith Crane and Construction of Christchurch |
| Civil/Survey Services | Connell Wagner of Christchurch |

DIRECTORS REVIEW 2005

Windflow Technology Ltd

The past year has seen the wind energy industry in New Zealand move into a rapid growth phase, with wind finally being considered a 'mainstream' electricity generation option. From a base of 168 MW of wind generation in New Zealand, more than a dozen new wind farms (proposed or in the planning stage) announced in the past year are likely to bring the total to over 1000 MW by 2010.

This is a very positive environment for the Windflow group of companies to be moving forward in. Windflow Technology has started our first production run of Windflow 500 turbines and NZ Windfarms Ltd now holds a fully consented world class wind farm site. Although these key events have occurred later than originally planned, we are well on the way to achieving our goals.

NZ Windfarms Ltd



NZ Windfarms Ltd has progressed well during this financial year. A highlight was gaining resource consent for our world class wind site, the Te Rere Hau wind farm on Aeolian Property Company Limited land on the Tararua ranges. The resource consent application for the wind farm was filed in August 2004 and consent was granted by the Palmerston North City Council commissioner in February 2005.

The appeal period closed three weeks later with three parties filing appeals, (one of these being NZ Windfarms' own appeal, which was lodged in order to remove ambiguity from the wording of some of the conditions).

After a successful mediation process with all appellants, the consent was formally signed by the Environment Court Judge on 30 May 2005. Planning is underway for civil works and connection for the first five turbines, with initial site works expected to begin this summer.

As well as having its own board and CEO the necessary documentation has gone through, which effectively splits ownership and assets in preparation for the initial public offering (IPO) later this year. This has capitalised NZWL with significant assets, in particular the resource consent, the carbon credits and the wind rights to develop the Te Rere Hau wind farm. It will also allow Windflow to focus on its core business; being a turbine manufacturer.

Windflow currently holds 100% of the shares in NZ Windfarms. Following the planned IPO, Windflow is expected to retain a holding of 3,000,000 shares, recognising the investment that Windflow has made to date. Before NZWL seeks public investment, Windflow shareholders are being asked to approve the IPO at the AGM. We recommend that you do so, as a successful IPO will mean that NZWL will have enough capital to proceed with the first stages of Te Rere Hau.

In March 2005, NZ Windfarms entered into a 'Memorandum of Understanding' with two of the world's leading wind farm developers for the development of the Te Rere Hau wind farm. The joint venture partners are NP Power Pty Limited and Babcock & Brown Windpower Pty Limited who are developing Lake Bonney and other major wind farms in Australia. Both parties are experienced in wind energy developments, and NP Power has a strong technical understanding of wind energy technology.

The understanding is that the partners will contribute 50% of funds (ie about \$40 million) to the Te Rere Hau project. However the directors would caution shareholders that there is still uncertainty as to whether or not the joint venture will proceed. Entering the formal joint venture agreement is conditional on several critical matters being resolved including the partners completing technical due diligence on the wind farm site and the Windflow 500 turbine. If this joint venture arrangement is confirmed then the timetable for fully developing the site will be much shorter than otherwise, and the funds required for investment in the Te Rere Hau wind farm by NZ Windfarms will also be decreased.

NZ Windfarms was previously awarded a contract for 519,000 carbon credits for the Te Rere Hau wind farm from the Government through its Projects to Reduce Emissions. The contract to give carbon credits in 2009-2013 is conditional on building the \$ 80 million wind farm. Therefore it is not reflected in Windflow's consolidated financial statements as it does not meet the asset recognition requirements of the Financial Reporting Standards.

The Kyoto Protocol came into force in February this year, resulting in an increasing global market for carbon credits. In last year's review we mentioned that we had applied for pre qualification for the Dutch government's tender process for carbon credits. Although we did not pre qualify for this tender, we have submitted an Expression of Interest for Emission Reductions generated by JI projects under the Austrian JI/CDM Programme, and are actively looking at other opportunities in this area. At the time of writing the European carbon market futures (EUA06) were trading at €22.55 (NZ\$39.46) (www.evomarkets.com). While this price does not currently apply to credits from non-European projects (for which the price has been around NZ\$10 to date), it gives an indication of the potential for carbon prices to increase if efficient international trading systems are introduced during the First Commitment Period of the Kyoto Protocol, 2008-2012.

For every \$10 value of a carbon credit, the fully developed and operating wind farm will benefit by \$ 5.19 million over the five year period of the contract.

Windflow Technology Ltd

Engineering Progress

The first significant engineering achievement of the past year was the reduction of a noisy vibration from the prototype gearbox which had caused the turbine to exceed consented sound levels at Gebbies Pass. As reported in the 2004 Annual Report and subsequent newsletters, this innovation has made our gearbox one of the quietest in the industry. We have applied for patents for this quiet gearbox innovation. The Banks Peninsula District Council performed sound monitoring and gave provisional compliance in October 2004 which allowed the prototype to operate on a 24 hour basis.

Operational data showed that the prototype had a better power curve than expected and was generating at full capacity in wind speeds of over 100 km/h (28 m/s). Several improvements were made to the prototype over the next few months and it was performing well until 10 March, when an extreme weather event, a very strong and rapid wind shift, resulted in the gearbox of the prototype being ripped from its holding down bolts and falling to the ground along with the rotor. The wind shift (which was outside the design envelope of the turbine) was part of the frontal system that on the same day spawned tornados that caused unprecedented damage in Greymouth.

We are pleased to be able to report that our insurance company, NZI, has accepted our claim for the damage cause by the extreme wind shift. This is expected to cover 100% of the costs of rebuilding the prototype.

In our March newsletter we included a supplement explaining what happened and what we intended to do to stop it happening again. In brief the remedies, which we have now implemented, involve three modifications to the control system to prevent a recurrence of this event, should a similar wind shift occur. Any one of these modifications on its own could have prevented the event, so the effect of the three of them will be to add three layers of defence against a recurrence.

In addition the bolted joint has also been redesigned to stretch rather than break. This provides a secure "torque-limiting" effect because the new joint has more than ten times the ductile energy absorption of the original joint. While the original joint provided "torque-limiting" by failing completely, this had not been intentionally built into the design, and was therefore not a secure enough feature in such an event.

Painful as it has been, the event has provided a huge amount of learning for the Windflow engineering team and one which we could never have "dialled up" to test the prototype even if we had wanted to.

This event has naturally caused a further delay in certification work on the Windflow 500. It has, however, allowed several modifications to be made which will make the rebuilt prototype more representative of the first production batch of turbines. In-stock parts from one of the first production batch turbines have been used for the rebuild, and means that the first production batch will now consist of five rather than six turbines.

At the time of writing, we are pleased to say that the prototype at Gebbies Pass has been reinstalled (see the photo on the next page) and we are working through the commissioning of the various the design improvements.

In last year's review we mentioned we had claimed against AH Gear's design insurance for costs due to the gearbox thrust ring redesign work in early 2004. At time of writing the insurance company has acknowledged our claim has merit, but we have not settled on a figure. We have also claimed against AH Gear's design insurance for costs due to the failure of the Stage 4 planet bearings in the gearbox in late 2004. We

have decided to wait until the thrust ring claim is settled before finalising and progressing this second claim.



Other highlights

The Windflow 500's ability to maintain frequency control is being acknowledged as a particular advantage in isolated networks, and as such we are investigating the expanding wind-diesel market in the Asia Pacific. The wind-diesel combination is in a growth phase due to rising oil prices and increasing demand for electricity, refrigeration and water desalination in isolated areas. In February 2005, we were awarded a \$130,000 Business Growth from Technology New Zealand to fund half the research which would prove the suitability of the Windflow 500 turbine for use in small, isolated networks such as islands or remote communities. The research will involve refining the torque limiting feature of our unique gearbox to include a dynamic control system that will respond to both the varying demands of a small network and the available wind energy simultaneously. The technology produced will be a wind turbine capable of operating successfully in tandem with a diesel generator, in an isolated situation. It will also help prove the fault ride-through capability of the turbine, an important advantage of our system in grid-connected wind farm applications. We will be starting work on this project later in the year.

Windflow's Electrical Engineer, Wernher Roding, has presented on the turbine's unique frequency and voltage control abilities at national and international conferences. We are finding that, with the increase of wind power in national electricity grids across the world, these attributes are becoming of more interest and importance in the industry.

Given that the prototype was not operational at the time of the May/June Renounceable Rights Issue, we were pleased with the level of uptake which resulted in \$3.3 million of subscriptions. This additional capital will ensure we can build manufacturing capacity and complete the first production batch by this summer for installation as the first stage of the Te Rere Hau wind farm.

The paperwork required to enable American Depositary Receipts (ADR's) to be traded is now being completed which will soon allow investors in the U.S. to invest in Windflow and improve the liquidity and international profile of our shares.

To sum up

Our immediate plan going forward is:

- to gain final confirmation of compliance with sound level requirements at Gebbies Pass
- to continue monitoring and documentation of the Windflow 500 for certification purposes (to IEC WT-01)
- to build capability for the first production batch of five turbines
- to enable NZWL to raise capital to fund the Te Rere Hau wind farm
- to commission five turbines on the Te Rere Hau site in 2006 and establish a track record for the technology

As part of building capability going forward, Windflow is pleased to welcome several new faces to the team: Emma Patrick, Mechanical Engineer/Analyst; Marie Munford, Office Junior; Magnus Koldau, Control and Instrumentation Engineer; and Jamie Wallace, Mechanical Engineer/Analyst.

Finally, we would like to acknowledge the great work of our staff; Chris Freear, Geoff Henderson, Francis Jackson (whom we farewell at the end of September when he returns to South Africa), Sheralee MacDonald, Terry Moon, Warwick Payne, Wernher Roding, and Gavin Wilson over the past year. We would also like to recognise the great contribution of supporting organisations, and component suppliers for the Windflow 500. In particular we acknowledge the ongoing support of Windflow shareholders through participation in the recent Rights Issue and words of encouragement as we move forward. We look forward to much exciting progress in the coming year.



CORPORATE GOVERNANCE

Introduction

The Board of Directors is elected by the shareholders and is responsible for the corporate governance of the Company. The Board is the final body responsible for the decision making within the Company and has the requirement to work to enhance the value of the Company in the interests of the Company and its shareholders.

Corporate Governance encompasses the requirement for the Board to discharge such responsibilities, to be accountable to the shareholders and other stakeholders for the performance of the Company and to ensure that the Company is compliant with laws and standards.

The Board establishes the objectives of the company and is engaged in ongoing strategic planning in order to meet these objectives. It provides an oversight of compliance and risk, it measures and monitors management performance and it sets in place the policy framework within which the Company operates.

The Board monitors financial results and compares them to the budgets and annual plans at the regular monthly meetings.

The following headings reflect the corporate governance principles recommended by the New Zealand Securities Commission in February 2004.

Reference has also been made to the Corporate Governance Best Practice Code (the NZX code).

Board Composition and Membership

As at the 30th June 2005 the Board comprised four Directors. This included a non-executive Chairman, an executive Director (the Chief Executive Officer) and two non-executive Directors.

The Board has a broad base of energy, engineering, financial, legal and other skills, experience and expertise to meet its objectives.

The details and background of the Directors are detailed elsewhere within this Annual Report.

The Chairman is elected by the Board of Directors and it is his role to manage the Board in the most effective manner and to provide a conduit between the Board and the Chief Executive Officer. He has no significant external commitments that conflict with this role.

Procedures for the operation of the Board, including the appointment and removal of Directors, are governed by the Company's Constitution.

The Board held twelve meetings during the financial period ended 30th June 2005. In addition to these formal meetings the Board meets on other occasions to debate strategic and financial deliberations.

Chief Executive Officer Performance Review

The Board is responsible for the evaluation of the Chief Executive officer against his key performance objectives and is responsible for the setting of these objectives on a periodic basis and ensuring that they are an appropriate measure.

Directors' Shareholdings as at the 30th June 2005

There is a Share Option Plan with Mr G Henderson, the Chief Executive Officer, which relates to any royalties payable under the TLG licence. This is detailed within Note 8 of the Notes to the Financial Statements (page 11).

Directors' disclosure of their shareholdings pursuant to Section 148 of the Companies Act 1993 and the NZAX listing rule are shown as at 30 June, 2005 in the list below.

| Director | Shares Held | | |
|-----------------|--------------|--------------------------------|------------------|
| | Beneficially | Interest of Associated Persons | Non-Beneficially |
| Barrie Leay | 28,650 | | |
| Geoff Henderson | 380,000 | 387,025 | |
| Heugh Kelly | 24,500 | | |
| Keith McConnell | 32,166 | | |

Independence of Directors

To be "independent" a Director must, in the opinion of the Board, be removed from any relationship or business that could materially interfere or be reasonably perceived to materially interfere with the exercise of his or her independent judgement.

It has been determined by the Board that of the four Directors all Directors were independent apart from Mr Geoff Henderson and Mr Keith McConnell.

Mr Henderson is the Chief Executive Officer and Mr McConnell has carried out various strategic consultancy exercises on behalf of the Company on a fee paying basis.

All Directors are required to immediately advise if any new relationships would interfere with such independence and so enable the Board to consider and determine the materiality of the relationship.

Board Committees

Due to the size of the Company no Board Committees have been established to assist in the execution of the Board's responsibilities. All such matters are conducted at the regular full Board meetings.

Ethical Standards

Code of Ethics

The Company expects all its employees and Directors to maintain the highest ethical standards.

The Directors support the principles set out in the "Codes of Proper Practice for Directors" issued by the Institute of Directors in New Zealand. Whilst recognizing that the Code expresses principles and does not purport to determine the detailed course of conduct by Directors on any particular matter, the Directors are committed to the highest standards of behaviour and accountability.

Interests Register

In accordance with the Companies Act 1993 the Company maintains an Interest Register in which the particulars of certain transactions and matters involving Directors are recorded. The following table summarises the Directors' interests in entities with which the Company has, or may in future have, transactions:

| Director | Directorship or shareholding (at 24/8/2005) |
|-----------------|--|
| Barrie Leay | New Zealand Windfarms Ltd |
| Geoff Henderson | Aeolian Property Company Ltd Henderson Inventions (TLG Patent) Pacific Windfarms Ltd Wind Blades Ltd Windpower Otago Ltd |
| Heugh Kelly | |
| Keith McConnell | New Zealand Windfarms Ltd Wind Blades Ltd |

Conflicts of Interest

If conflicts of interest do exist at law then the policy of the Board is that Directors must declare their interest and do not exercise their right to vote in respect of such matters.

Insider Trading

Directors and employees of the Company are subject to the limitations on their ability to buy or sell Windflow Technology Limited shares under the NZAX Listing Rules and the Securities Markets Act 1988. No one at Windflow Technology is permitted to, directly or through other persons or entities, buy or sell Windflow Technology shares or advise someone else to buy or sell Windflow Technology shares on the basis of inside information about the Company, its joint venture partners and subsidiaries.

Audit Governance and Independence

The Board approved the reappointment of Goldsmith Fox PKF as Auditors for the year ended 30th June 2005. Shareholders approved the Board setting the remuneration of the Auditors at the Annual General Meeting in November 2004.

The work of the external Auditors is limited to audit and related work only and the Company is committed to auditor independence. The Board annually reviews the independence and objectivity of the external Auditors. No employees, Partners or Directors of the Audit firm hold shares in the Company.

Representatives of the Company's external Auditors, Goldsmith Fox PKF have been invited to the Annual General Meeting.

Directors Remuneration

The current annual Directors fee paid to all Directors within the parent company is \$81,000 per annum, each Director receiving \$18,000 each and the Chairman receiving \$27,000. The Chairman and directors of NZ Windfarms Ltd, are paid at the same rate.

The salary of the Chief Executive Officer as at the 30th June 2005 was \$88,000.

Project management fees totalling \$13,909 were paid to one Director, Mr K McConnell. Refer to note 22 on page 16.

The following table summarises the remuneration for the period to 30 June 2005 of the Directors of Windflow Technology Ltd and New Zealand Windfarms Ltd:

| Name | | Directors Fees | Salary | Other Fees |
|-----------------|----------|----------------|----------|------------|
| Barrie Leay | WTL/NZWL | \$37,500 | | |
| Geoff Henderson | WTL/NZWL | \$16,667 | \$88,000 | |
| Heugh Kelly | WTL/NZWL | \$16,667 | | |
| Keith McConnell | WTL/NZWL | \$32,250 | | \$13,909 |
| Vicki Buck | WTL/NZWL | \$16,750 | | |
| Juliet McKee | NZWL | \$16,750 | | |
| Derek Walker | NZWL | \$23,250 | | |

No other benefits were received by the Directors of the Company. Reimbursements of appropriate costs (mainly travel to meetings) were made.

Reporting and Disclosure

Annual and Interim Reports in accordance with the requirements of the Companies Act 1993, the Financial Reporting Act 1993 and the NZAX Listing Rules are communicated on a periodic basis to all shareholders.

A web site is maintained and contains regular updates to shareholders as well as the Annual and Interim Reports.

The Chief Executive Officer and other Senior Officers have conducted regular information meetings and discussions with shareholders and interested persons.

Risk Management

The Company has a policy of identifying, assessing and managing risks arising from its business direction and also from the strategic environment.

It implements risk management through its business processes of planning, budgeting, investment and project analysis, and operations management.

Shareholder Relations

The Board's policy is to ensure that shareholders are informed of all major and strategic developments affecting the Company's state of affairs.

All major disclosures are posted to the Company's web site on a timely basis. Regular media releases are made and copied to shareholders by email.

Company Secretary

The board has appointed Terry Moon as Company Secretary, effective as of 21st June 2005 to take on the task of co-ordinating all the reporting and compliance requirements of the company throughout the financial year.

OTHER STATUTORY INFORMATION

Employee Remuneration

For the period to 30 June 2005, there were no employees who earned more than \$100,000. The remuneration paid to Geoff Henderson is reported under the heading Director Remuneration.

Directors Indemnity and Insurance

The Company has Directors & Officers Liability Insurance to the sum of \$2,000,000 in the aggregate.

Subsidiaries and Directors Thereof

Windflow has incorporated three subsidiaries. They are Wind Blades Limited, NZ Windfarms Limited and Pacific Windfarms Limited. The Directors of Wind Blades Limited are Peter Brooking, Bruce Tait, Keith McConnell and Geoff Henderson. The Directors of NZ Windfarms Limited are set out on page 22. The sole Director of Pacific Windfarms Limited (which is non-trading) is Geoff Henderson.

SHAREHOLDER INFORMATION

The ordinary shares of Windflow Technology Ltd are listed on the New Zealand Stock Exchange's Alternative Market (NZAX). The information in the disclosures below has been taken from the Company's register at 30th June 2005.

Twenty Largest Ordinary Shareholders

| Shareholder | Address | Shares | % |
|---|----------------|----------------|---------------|
| Geoff Henderson | Christchurch | 380,000 | 5.69 |
| Delane Wycoff | Nebraska, USA | 362,244 | 5.43 |
| Jenny Henderson | Christchurch | 332,237 | 4.98 |
| Mark Mellsoy | Franz Josef | 277,525 | 4.16 |
| Paul Simmons & Esther Simmons | Christchurch | 160,000 | 2.40 |
| Reda Holdings Ltd | Switzerland | 144,977 | 2.17 |
| Andrew Rochford & Sabina Rochford | Warkworth | 85,000 | 1.27 |
| Fitzallan Investments Ltd | Christchurch | 73,500 | 1.10 |
| Victor Holmes & Christine Holmes | South Auckland | 72,555 | 1.09 |
| Simon Stockdale | Auckland | 72,000 | 1.08 |
| Caroline Stockdale | Auckland | 60,000 | 0.90 |
| Sheila Kolstad | Christchurch | 60,000 | 0.90 |
| Geoffrey Robinson & Reihana Robinson | Coromandel | 60,000 | 0.90 |
| David Studholme & Tim & Cherry Armitage | Christchurch | 52,811 | 0.79 |
| Jeanette Fitzsimons | Thames | 50,000 | 0.75 |
| Esther Simmons | Christchurch | 50,000 | 0.75 |
| David Iles | Wellington | 41,500 | 0.62 |
| Aeolian Property Company Ltd | Christchurch | 40,000 | 0.60 |
| Robin Owens & Michael G. Stuart Trustee Co (1999) Ltd | Mt Maunganui | 40,000 | 0.60 |
| Francis Henderson | NSW, Australia | 38,114 | 0.57 |
| TOTALS | | 2452463 | 36.74% |

Distribution of Shareholders

| Holdings Ranges | Number of Holders | Number of Shares | % |
|----------------------|-------------------|------------------|---------------|
| 1 – 1,000 | 93 | 71,231 | 1.07 |
| 1,001 – 5,000 | 354 | 996,979 | 14.94 |
| 5,001 – 10,000 | 200 | 1,322,114 | 19.80 |
| 10,001 – 50,000 | 112 | 2,092,130 | 31.34 |
| 50,001 – 100,000 | 8 | 535,866 | 8.03 |
| 100,001 – 1,000,000 | 6 | 1,656,983 | 24.82 |
| 1,000,001 – and over | 0 | 0 | 0 |
| Totals | 773 | 6,675,303 | 100.00 |

Substantial Security Holders

The following information is given in accordance with Section 26 of the Securities Markets Act 1988. According to notices received, the following persons were substantial security holders in the company at 30th June 2005.

| Shareholder | Number of shares directly held | % |
|------------------------------|--------------------------------|-------|
| Henderson Family Interests – | 767,025 | 11.49 |
| made up of: | | |
| • Geoff Henderson | 380,000 | |
| • Jenny Henderson | 332,237 | |
| • Frank Henderson | 38,114 | |
| • Catherine Henderson | 11,746 | |
| • Jean Henderson | 3,969 | |
| • Jon Henderson | 959 | |
| Delane Wycoff | 362,244 | 5.43 |
| Totals | 1,129,269 | |

The total number of issued voting securities as at 30th June 2005 was 6,675,303.

NOTES

NOTES