

Freshtel

PROSPECTUS 2005

FOR THE OFFER OF 10,000,000 SHARES
AT AN ISSUE PRICE OF \$0.20 TO RAISE
\$2,000,000 (WITH THE ABILITY TO ACCEPT
OVERSUBSCRIPTIONS FOR UP TO
A FURTHER \$1,000,000).

THIS PROSPECTUS ALSO INCLUDES AN
OFFER OF SHARES AND PERFORMANCE
SHARES TO THE SHAREHOLDERS IN
FRESHTEL AUSTRALIA PTY LTD.

IMPORTANT INFORMATION

This is an important document that should be read in its entirety. If you do not understand it you should consult your professional advisers without delay. The securities offered by this Prospectus should be considered speculative.

IMPORTANT NOTICE

This Prospectus is dated 4 March 2005 and was lodged with the Australian Securities and Investments Commission (**ASIC**) on that date. ASIC and its officers take no responsibility for the contents of this Prospectus or the merits of the investment to which the Prospectus relates.

The expiry date of this Prospectus is 5.00pm WST on that date which is 13 months after the date this Prospectus is lodged with ASIC (**Expiry Date**).

No securities may be issued on the basis of this Prospectus after the Expiry Date.

The distribution of this Prospectus in jurisdictions outside Australia may be restricted by law and persons who come into possession of this Prospectus should seek advice on and observe any of these restrictions. Failure to comply with these restrictions may violate securities laws. Applicants who are resident in countries other than Australia should consult their professional advisers as to whether any governmental or other consents are required or whether any other formalities need to be considered and followed.

This Prospectus does not constitute an offer in any place in which, or to any person to whom, it would not be lawful to make such an offer.

It is important that investors read this Prospectus in its entirety and seek professional advice where necessary. The securities that are the subject of this Prospectus should be considered speculative.

WEB SITE—ELECTRONIC PROSPECTUS

A copy of this Prospectus can be downloaded from the website of Freshtel Holdings Limited at www.freshtelholdings.com. Any person accessing the electronic version of this Prospectus for the purpose of making an investment in the Company must be an Australian resident and must only access the Prospectus from within Australia.

The Corporations Act prohibits any person passing on to another person an application form unless it is attached to a hard copy of this Prospectus or it accompanies the complete and unaltered version of this Prospectus. Any person may obtain a hard copy of this Prospectus free of charge by contacting the Company.

EXPOSURE PERIOD

This Prospectus will be circulated during the Exposure Period. The purpose of the Exposure Period is to enable this Prospectus to be examined by market participants prior to the raising of funds. Potential investors should be aware that this examination may result in the identification of deficiencies in the Prospectus and, in those circumstances, any application that has been received may need to be dealt with in accordance with Section 724 of the Corporations Act.

Applications for securities under this Prospectus will not be accepted by the Company until after the expiry of the Exposure Period. No preference will be conferred on persons who lodge applications prior to the expiry of the Exposure Period.

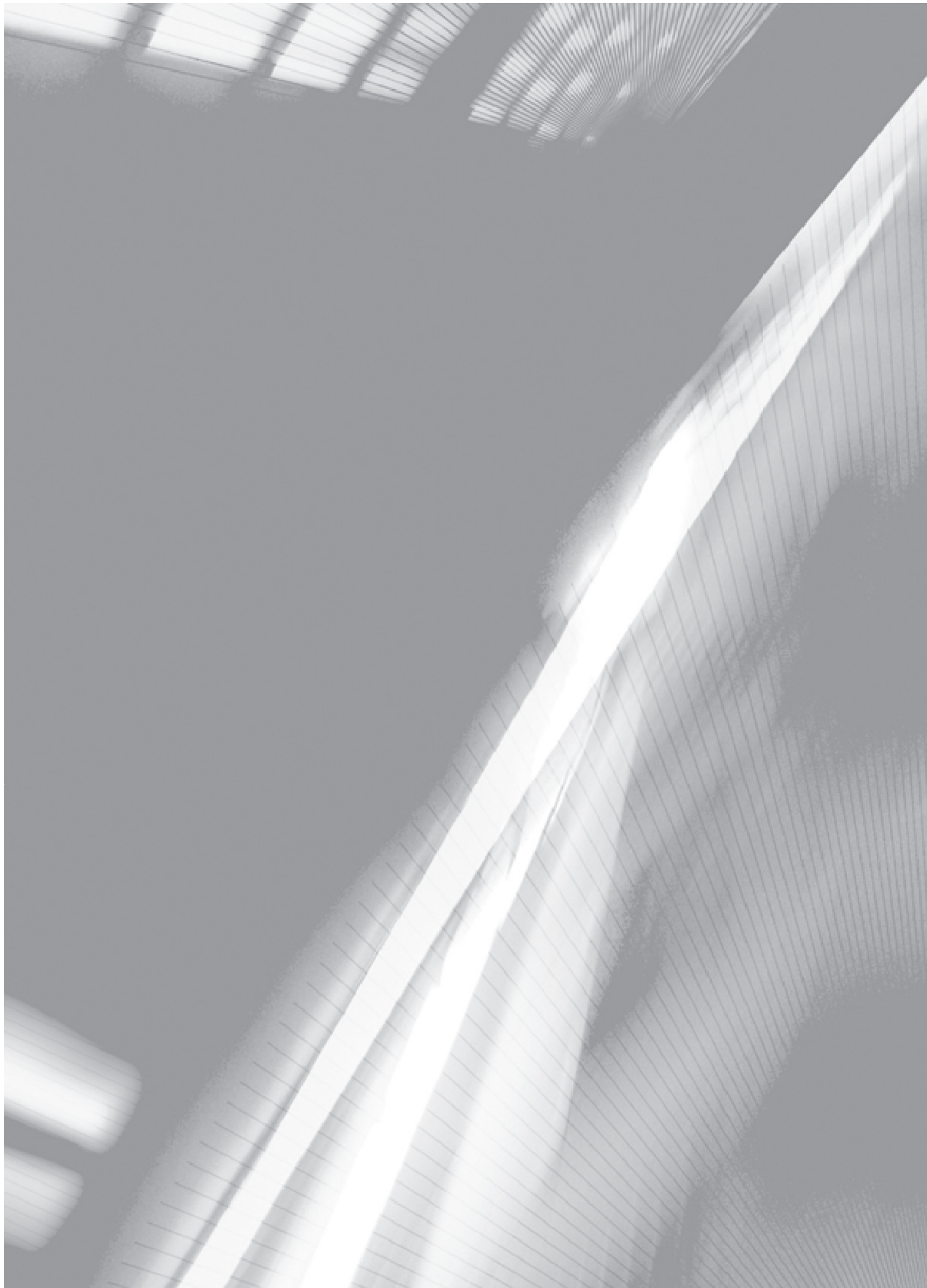
SUMMARY OF IMPORTANT DATES

Lodgement of Prospectus with ASIC	4 March 2005
Opening Date	11 March 2005
Closing Date	8 April 2005
Expected Date of Dispatch of Holding Statements	15 April 2005
Expected Date of Listing on ASX	22 April 2005

The above dates are indicative only and may change without notice. The Company reserves the right to extend the Closing Date or close the Offer early without notice.

“... we are moving into a new field of technology that has the potential to reshape the way we can communicate the world over ...”

Les Taylor, Chairman



Contents

1	Chairman's Letter	4
2	Investment Highlights	6
3	Overview of the Offer	7
4	Details of the Offer	8
5	The Freshtel Business	11
6	Board of Directors	22
7	Risk Factors	24
8	Independent Accountant's Report	26
9	Summary of Material Contracts	36
10	Additional Information	41
11	Glossary	48
12	Directors' Authorisation	50
13	Directory	53

1

Chairman's Letter



Dear Investor,

I would like to take this opportunity to congratulate you on your consideration to invest in the emerging Voice over Internet Protocol (VoIP) market. I am truly excited as we are moving into a new field of technology that has the potential to reshape the way we can communicate the world over. Freshtel is positioning itself as a market leader in product and service offerings for this emerging sector both in Australia and overseas.

VoIP uptake around the world is growing at a remarkable rate. There has been limited use of VoIP in Australia until recently, with its use being largely confined to enthusiasts and early adopters. During the last 18 months, however, there has been increasing interest in the use of VoIP. We expect this trend to continue, as broadband Internet prices continue to fall, increasing the number of potential VoIP subscribers. The Board believes that the consumer market will embrace VoIP in the coming years.

Freshtel Australia has already developed high quality hardware and software VoIP solutions for home and business use. The capital raised from this Prospectus will enable us to launch these services into a rapidly growing global market.

Our expertise in the technology, research and development of VoIP comes from our experienced and knowledgeable team, allowing us to create the products and services that will enable Freshtel to grow on a domestic and global front.

I take great pleasure in welcoming the new Board of Directors.

Mr Michael Carew, Executive Director and CEO, is the founder of Freshtel Australia. Michael planned and orchestrated the development of Freshtel products and is the major shareholder of Freshtel Australia.

Mr Peter Warner, our new Executive Commercial Director, has worked with some of Australia's leading businesses including Zurich Insurance, Fuji Xerox, Adobe and the Commonwealth Bank.

Mr Sebastian Filzek, Non-Executive Director and CTO, has been instrumental in the development of Freshtel's strategic direction and product development since its inception. Sebastian has been developing Internet technologies and electronic systems for over 15 years, and his portfolio of work in both of these areas is an asset to the Company.

Mr David Elbourn, Non-Executive Director and CFO, is a chartered accountant who has worked with international chartered accountants Coopers and Lybrand and is currently a partner in his own firm. David's expertise and experience with rapidly growing businesses has contributed to the financial strategy of Freshtel from its beginning. David will continue to oversee the financial strategy and control of the Company.

We look forward to welcoming you as a shareholder in Freshtel, and to becoming part of the future in Internet Telephony.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Les Taylor'. The signature is fluid and cursive, written in a professional style.

LES TAYLOR
CHAIRMAN
4 March 2005



2

Investment Highlights

THE VOIP OPPORTUNITY

- VoIP technology enables telephone calls over computer networks such as the Internet.
- Substantially reduces call costs.
- Ability to grow and interoperate with IT systems.
- Technology capable of replacing conventional telephone systems.

LARGE AND RAPIDLY GROWING GLOBAL MARKET

- Global VoIP traffic in 2003 estimated at 22 billion minutes, 12% of all voice traffic.¹
- Worldwide VoIP sales estimated at \$4.9 billion for 2004, growing to \$15.1 billion by 2007.¹
- By 2009, VoIP revenue projected to be \$32 billion—12% of total telephony revenue of \$260 billion.¹
- In USA, VoIP subscribers expected to grow from 131,000 at year-end 2003 to 17.5 million by year-end 2008.¹
- 180,000 subscribers to Freshtel in 12 months since launch in January 2004.

ADVANCED TECHNOLOGY

- Freshtel products allow free calls over Internet or low cost calls to conventional telephones.
- Integrated products—softphone, hardware and call termination service—offer a ‘one-stop’ VoIP solution for customers and a competitive advantage for Freshtel.
- Easy to configure and use.
- Excellent sound quality.
- Based on open standards to allow interoperation with other providers.
- One of the first to market.

MARKET-LEADING PRODUCTS

- **Firefly softphone**
Allows quick and easy entry to VoIP. Provides all the cost advantages of VoIP without the need for any specialised hardware.
- **USB hardware phone**
Plugs into the USB port of a PC. Feels like a conventional telephone.
- **LAN phone**
Plugs into a local area network—no PC required. Looks and works like a conventional desktop telephone (due for release 2005).
- **Analogue Telephone Adaptor (ATA)**
Quickly and easily converts a conventional telephone into a VoIP telephone (due for release 2005).
- **VoiceStream Call Termination Service**
Enables calls to be made from a VoIP telephone to a traditional telephone at reasonable call rates.
- **White Label Systems**
Un-branded turnkey VoIP solutions that can be licensed globally.

EXPERIENCED TEAM

- The Board offers years of experience in business practices, financial management and product development.
- The Freshtel management team includes key personnel from a broad cross-section of the business world.
- The Freshtel R&D team embodies a wealth of talent and knowledge in VoIP product development.

3

Overview of the Offer

3.1 IMPORTANT NOTICE

This section is not intended to provide full information for investors intending to apply for Shares offered pursuant to this Prospectus. This Prospectus should be read and considered in its entirety.

3.2 SUMMARY OF THE OFFER

By this Prospectus, the Company invites investors to apply for up to 10,000,000 Shares at an issue price of \$0.20 per Share to raise \$2,000,000.

In addition, the Company may also accept oversubscriptions of a further \$1,000,000 through the issue of up to 5,000,000 Shares at \$0.20 each.

This Prospectus also includes an offer of Shares and Performance Shares to the shareholders in Freshtel Australia.

3.3 INDICATIVE TIMETABLE

Lodgement of Prospectus with ASIC	4 March 2005
Opening Date	11 March 2005
Closing Date	8 April 2005
Expected date of Dispatch of Holding Statements	15 April 2005
Expected Date of Listing on ASX	22 April 2005

The above dates are indicative only and may change without notice. The Company reserves the right to extend the Closing Date or close the Offer early without notice.

3.4 OBJECTIVE

The purpose of this raising is to raise sufficient funds to enable the Company to fund ongoing research and development and working capital to fund the growth of the business in both the domestic and global markets.

On completion of the Offer, the Board believes the Company will have sufficient working capital to carry out these objectives.

3.5 USE OF PROCEEDS

The funds raised from the Offer (assuming only the minimum subscription of \$2,000,000 is raised), together with existing cash reserves of approximately \$2.2 million, are intended to be applied as follows:

Description	Amount
Hardware manufacturing	\$500,000
Research and development	\$1,500,000
Domestic and global commercialisation	\$500,000
Expenses of Offer	\$336,010
General working capital	\$1,363,990
Total	\$4,200,000

Any funds raised over the minimum subscription of \$2,000,000 will be applied towards research and development and general working capital.

3.6 CAPITAL STRUCTURE

The capital structure of the Company following completion of the Offer is summarised below:

Shares	Number
Shares on issue at date of this Prospectus	17,748,500
Shares offered in capital raising	10,000,000
Shares to be issued to Freshtel Australia Shareholders	56,100,000
Total Shares on issue at completion of the Offer¹	83,848,500
Performance Shares	
Performance Shares to be issued to Freshtel Australia Shareholders	93,900,000
Options	
Options on issue at date of this Prospectus	5,165,000

¹ Notes:
Assumes that only the minimum subscription of \$2,000,000 is raised.

4

Details of the Offer

4.1 THE OFFER

By this Prospectus, the Company offers for subscription 10,000,000 Shares at an issue price of \$0.20 per Share to raise \$2,000,000.

In addition, the Company may also accept oversubscriptions of up to a further \$1,000,000 through the issue of up to 5,000,000 Shares at \$0.20 each. The Shares offered under this Prospectus will rank equally with the existing Shares on issue.

4.2 APPLICATION FOR SHARES

An application for Shares by an investor must be made using the Application Form.

Payment for the Shares must be made in full at the issue price of \$0.20 per Share. An application for Shares must be for a minimum of 10,000 Shares and thereafter in multiples of 2,000 Shares. Completed Application Forms and accompanying cheques must be mailed or delivered to:

Computershare Investor Services Pty Limited
GPO Box D182
Perth WA 6840

OR

Computershare Investor Services Pty Limited
Level 2, 45 St Georges Terrace
Perth WA 6000

Cheques should be made payable to 'Freshtel Holdings Ltd—Share Offer Account' and crossed 'Not Negotiable'. Completed Application Forms must reach the Share Registry by no later than the Closing Date.

4.3 OFFER TO SHAREHOLDERS IN FRESHTEL AUSTRALIA

This Prospectus incorporates an offer of Shares and Performance Shares to the shareholders in Freshtel Australia.

Under the terms of the Share Sale Agreement, the Company has agreed to issue the shareholders in Freshtel Australia 56,100,000 Shares, 33,900,000 Class A Performance Shares, 30,000,000 Class B Performance Shares and 30,000,000 Class C Performance Shares. The material terms and conditions of the Performance Shares are set out in Section 10.5.2.

To apply for Shares and Performance Shares under this Prospectus, each of the shareholders in Freshtel Australia must complete the 'Freshtel Application Form'.

4.4 ALLOTMENT

Subject to ASX granting approval for the Company to be admitted to the Official List, allotment of Shares offered by this Prospectus will take place as soon as practicable after the Closing Date. Prior to allotment, all application monies shall be held by the Company in trust. The Company, irrespective of whether the allotment of Shares takes place, will retain any interest earned on the application monies.

The Directors reserve the right to allot Shares in full for any application or to allot any lesser number or to decline any application. Directors may in their discretion give preference to Shareholders in accepting applications under the public offer. Where the number of Shares allotted is less than the number applied for, or where no allotment is made, the surplus application monies will be returned by cheque to the applicant within seven (7) days of the allotment date.

4.5 MINIMUM SUBSCRIPTION

The minimum amount to be raised pursuant to this Prospectus is \$2,000,000.

If the minimum amount has not been raised within four months after the date of this Prospectus, all applications will be dealt with in accordance with the Corporations Act.

4.6 ASX LISTING

The Company will apply to ASX within seven (7) days after the date of this Prospectus for admission to the Official List and for Official Quotation of the Shares offered under this Prospectus. If ASX does not grant permission for Official Quotation of the Shares within three (3) months after the date of this Prospectus, or such longer period as is permitted by the Corporations Act, none of the Shares offered by this Prospectus will be allotted or issued. In these circumstances, all applications will be dealt with in accordance with the Corporations Act.

4.7 APPLICANTS OUTSIDE AUSTRALIA

This Prospectus does not, and is not intended to, constitute an offer in any place or jurisdiction, or to any person to whom, it would not be lawful to make such an offer or to issue this Prospectus. The distribution of this Prospectus in jurisdictions outside Australia may be restricted by law and persons who come into possession of this Prospectus should seek advice on and observe any such restrictions. Any failure to comply with such restrictions may constitute a violation of applicable securities law. No action has been taken to register or qualify the Shares or otherwise permit a public offering of the securities that are the subject of this Prospectus in any jurisdiction outside Australia.

It is the responsibility of applicants outside Australia to obtain all necessary approvals for the allotment and issue of the Shares pursuant to this Prospectus. The return of a completed Application Form will be taken by the Company to constitute a representation and warranty by the applicant that all relevant approvals have been obtained.

4.8 UNDERWRITER

The Offer is not underwritten.

4.9 CHESS

The Company will apply to participate in the Clearing House Electronic Subregister System (**CHESS**). CHESS is operated by ASX Settlement and Transfer Corporation Pty Ltd (**ASTC**), a wholly owned subsidiary of ASX, in accordance with the Listing Rules and the ASTC Settlement Rules.

Under CHESS, the Company will not issue certificates to investors. Instead, Share and Option holders will receive a statement of their holdings in the Company. If an investor is broker sponsored, ASTC will send a CHESS statement.

4.10 RISK FACTORS

Prospective investors in the Company should be aware that subscribing for securities that are the subject of this Prospectus involves a number of risks. These risks are set out in Section 7 of this Prospectus and investors are urged to consider those risks carefully (and if necessary, consult their professional adviser) before deciding whether to invest in the Company.

The risk factors set out in Section 7, and other general risks applicable to all investments in listed securities not specifically referred to, may in the future affect the value of the Shares.

Accordingly, an investment in the Company should be considered speculative.

4.11 PRIVACY ACT

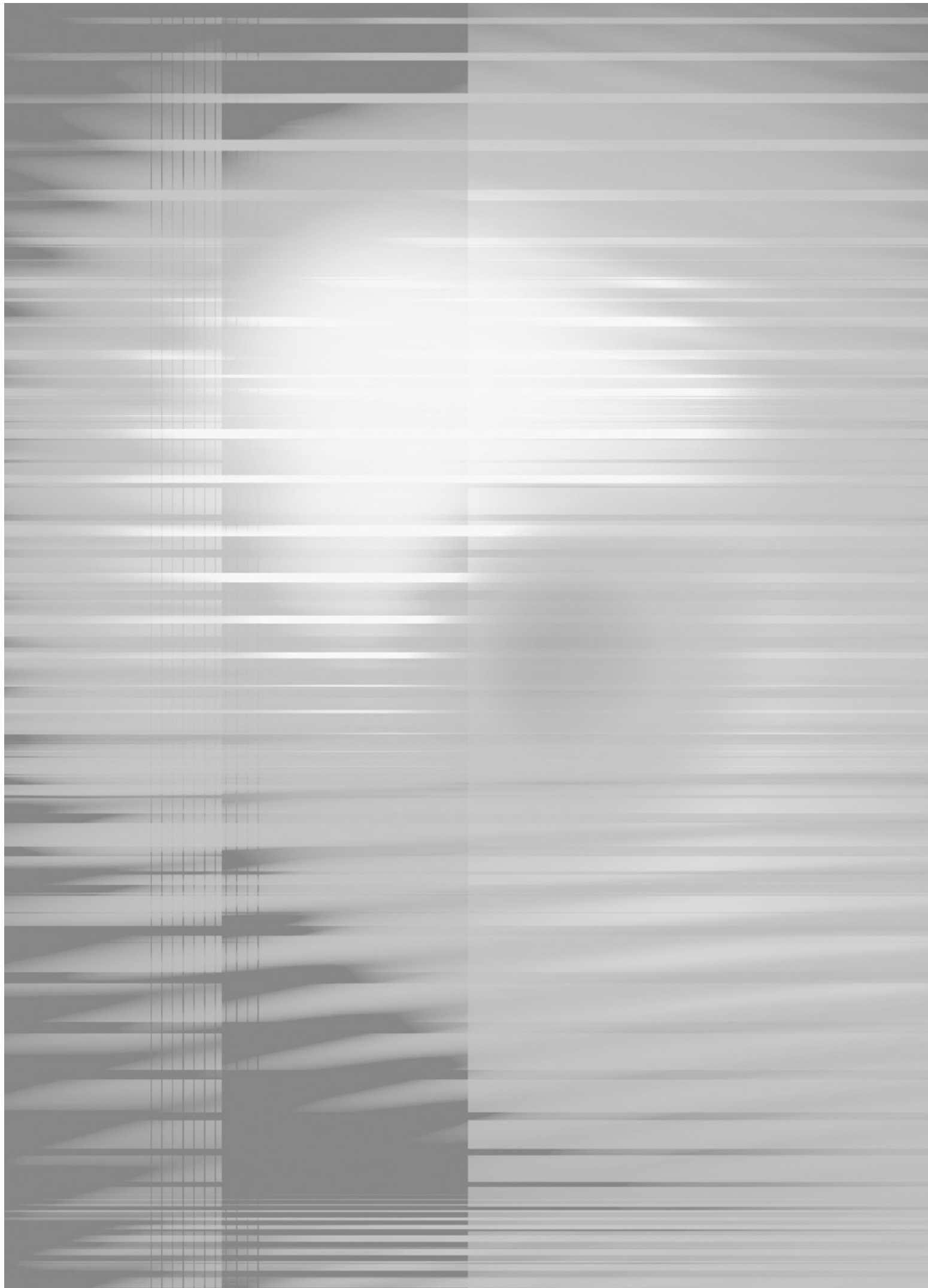
If you complete an Application Form, you will be providing personal information to the Company (directly or by the Share Registry). The Company collects, holds and will use that information to assess your application, service your needs, facilitate distribution payments and corporate communications to you as a Shareholder, and carry out administration. The information may also be used from time to time and disclosed to persons inspecting the register, bidders for your securities in the context of takeovers, regulatory bodies, including the Australian Taxation Office, authorised securities brokers, print service providers, mail houses and the Share Registry.

You can access, correct and update the personal information that we hold about you. Please contact the Company or the Share Registry if you wish to do so at the relevant contact numbers set out in this Prospectus.

Collection, maintenance and disclosure of certain personal information is governed by legislation including the Privacy Act 1988 (as amended), the Corporations Act and certain rules such as the ASTC Settlement Rules. If you do not provide the information required on the Application Form, the Company may not be able to accept or process your application.

4.12 FINANCIAL FORECASTS

The Directors have considered the matters set out in ASIC Policy Statement 170 and believe that they do not have a reasonable basis to forecast future earnings on the basis that the operations of the Company are inherently uncertain. Accordingly, any forecast or projection information would contain such a broad range of potential outcomes and possibilities that it is not possible to prepare a reliable best estimate forecast or projection.



The Freshtel Business

5.1 BACKGROUND ON THE COMPANY

The Company was incorporated on 20 October 2004.

Following a seed raising of approximately \$2.2 million that was completed in late November 2004, the Company entered into an agreement with Freshtel Australia and its shareholders, under which the Company agreed to acquire all of the issued shares in Freshtel Australia in return for the issue of securities in the Company to the Freshtel Australia shareholders (**Acquisition**).

At a general meeting of Shareholders held on 17 January 2005, approval was obtained to proceed with the Acquisition and the Company is now seeking to raise funds to facilitate a listing on ASX.

5.2 BACKGROUND ON FRESHTEL AUSTRALIA

Established in 2002, Freshtel Australia is an Australian Internet telephony company developing and marketing Voice over Internet Protocol (**VoIP**) telephony products and services. VoIP (or **IP Telephony**) is a technology that allows voice telephone calls to be made over an IP network such as the Internet, rather than the traditional Public Switched Telephone Network (**PSTN**).

Freshtel Australia comprises three separate channels and an internal research and development (**R&D**) arm. Each channel has its own brand and performs a different business function.

- **Freshtel Pty Limited** retails VoIP services using the Firefly **softphone**.
- **Virbiage Pty Limited** manufactures and sells VoIP handsets and other hardware.
- **Voicestream Networks Pty Limited** provides wholesale call termination and turnkey VoIP software services.

These channels are backed up by **Freshtel R&D Pty Limited**, a dedicated VoIP R&D business.

5.3 THE VOIP MARKET

VoIP technology can be considered a 'disruptive technology' owing to its potentially substantial impact on the telecommunications sector. Its strategic impact has led analysts and market commentators to question the long-term ongoing viability of traditional telecommunications companies. This is due to both

the savings incurred by using Internet-based telephony and the ongoing ability of VoIP devices to interoperate and grow with existing computer systems, allowing increased workflow and efficiency.

VoIP users reap the efficiencies associated with lower port and operational costs. Additionally, using VoIP eliminates the need for separate voice and data networks and enables infrastructure consolidation. At the consumer level, with broadband penetration rapidly increasing in the developed world, the price advantages of IP telephony are now being carried over to the home.

The benefits of VoIP are well-recognised and have led to many predictions of rapid growth in the sector, such as that:¹

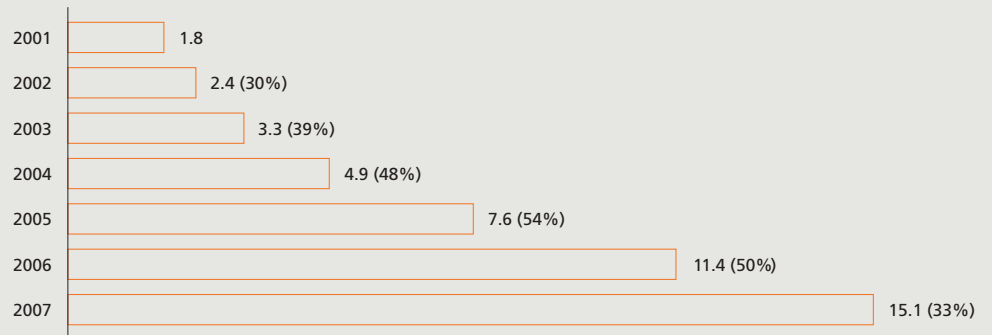
- VoIP will account for over 12% of all telephony revenues by 2009, contributing \$32 billion to a total worldwide telephony market of \$260 billion.
- Global IP telephony equipment revenues will total \$4.9 billion by the end of 2004, growing by 48% over 2003, and will exceed \$15 billion by 2007. In Australia, IP telephony hardware revenue is set to reach \$679 million by 2006, following the world trend.
- VoIP will grow steadily over the following four years, rising from 6.5 million lines in 2004 to 19.2 million lines in 2007, with the rise of VoIP following the growth of broadband Internet services.
- Broadband adoption, new broadband appliances and VoIP subscribers will increase.
- VoIP subscribers will grow from 131,000 at year-end 2003 to almost 1 million subscribers by year-end 2004 and 17.5 million US households by year-end 2008.

5.4 TECHNOLOGY OVERVIEW

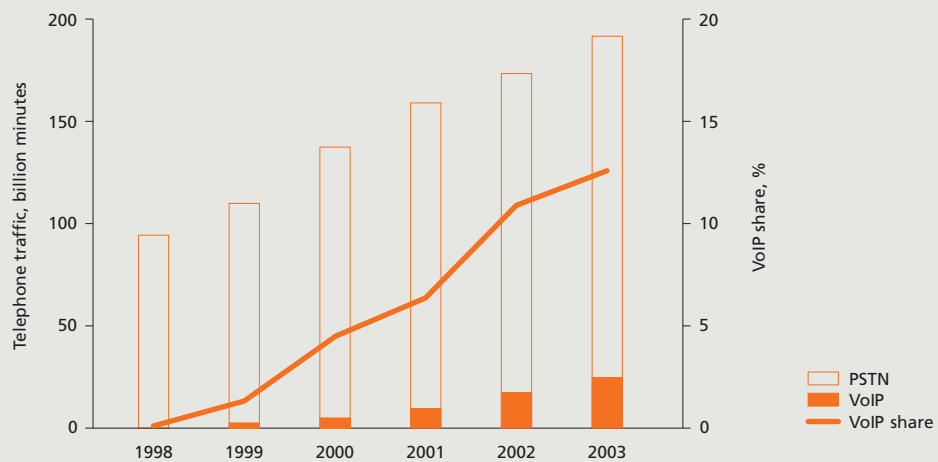
Central to the Freshtel Australia business is Firefly, the software that makes VoIP possible. Firefly uses a number of new and innovative technologies to provide a high-quality and resilient service. It is specifically designed to run over a broadband Internet connection, with or without a Network Address Translation (**NAT**) firewall.

¹Source: Budde Report.

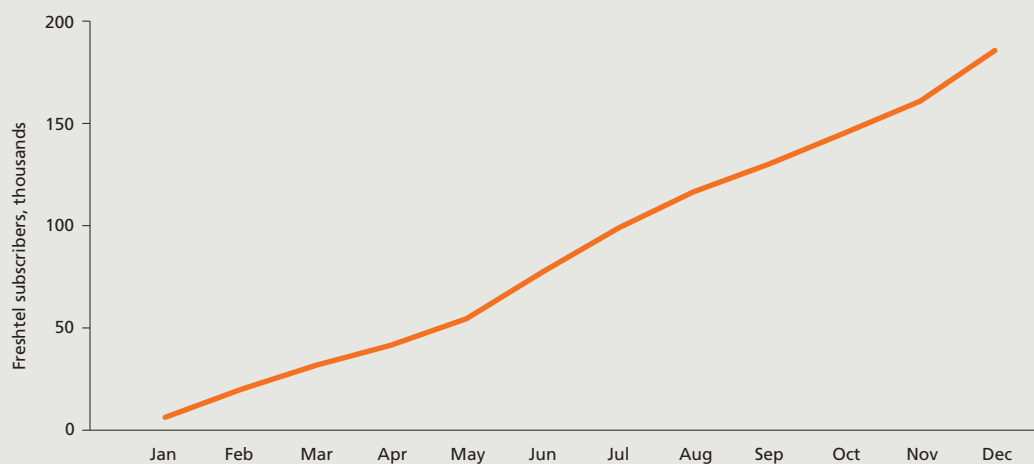
The Freshtel Business



Worldwide IP telephony equipment revenues 2001–2007, billion US\$ (% growth).
Source: Budde Report



International VoIP and PSTN Traffic 1998–2003. Compound annual growth rates—PSTN: 12%, VoIP: 177%.
Source: Budde Report



Freshtel subscriber growth 2004.

The Freshtel Business

5.4.1 THE TROUBLE WITH NAT

NAT is a significant problem with many existing VoIP systems. NAT is used by the vast majority of broadband modems that employ a firewall system. It can and does interfere with many standard VoIP processes. This can be circumvented in several ways to give the user access to a VoIP system; however, most fixes require configuration changes to the user's modem or router, which invariably involves a call to the helpdesk of the user's Internet Service Provider (ISP). These helpdesk calls are generally quite involved, and not all users are easily able to make the required changes to their equipment.

Any VoIP system requires a **protocol**—a special set of rules used to send and receive data across a communication network. Freshtel Australia's earliest launch into VoIP involved use of the H.323 protocol direct to the user. This approach caused problems for helpdesk staff since the users being targeted were those with a broadband connection, and therefore most likely to use a NAT modem or router.

5.4.2 A NEW APPROACH

The new FireFly softphone is based on the Inter-Asterisk eXchange 2 (IAX2) and SIP protocols instead of H.323. Since both IAX2 and the Firefly network are highly compatible with existing NAT equipment, no set-up or configuration changes to the user's modem or router are required. IAX2 is also an open-standard protocol, allowing Firefly to interoperate with

other VoIP systems such as **Asterisk** and allow one user to call another user with a different VoIP provider. Firefly is one of the first commercial softphones using IAX2.

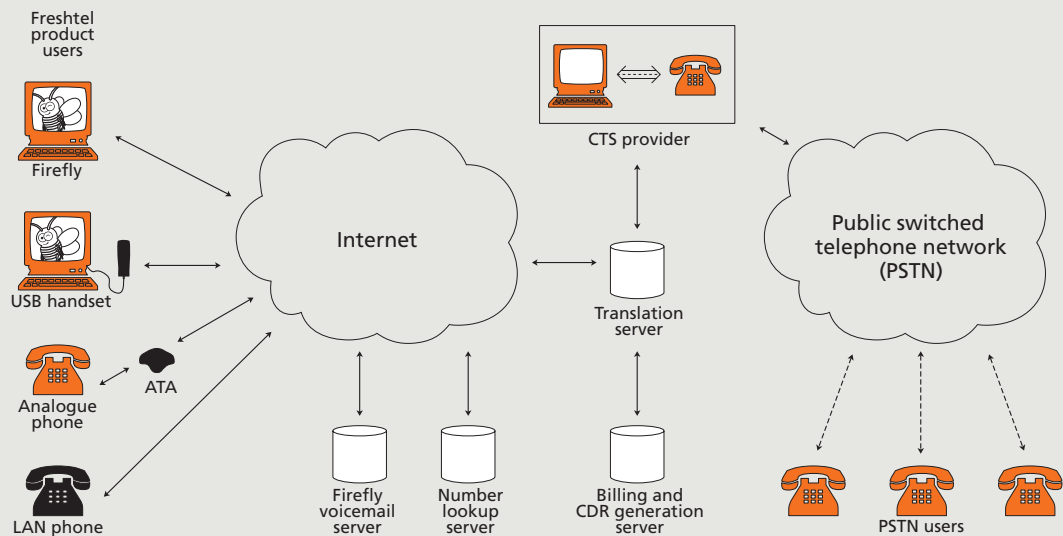
Freshtel Australia launched a telephony service using Firefly in January 2004. By the end of December 2004 there were more than 180,000 registered accounts running Firefly, with currently more than 5,000 new subscribers each week. All users are currently supported entirely via a single e-mail and VoIP helpdesk staffed by two employees, illustrating the effectiveness and ease-of-use of the Firefly system.

5.4.3 PEER-TO-PEER TELEPHONY

Firefly enables users to make calls to other Firefly users using a peer-to-peer calling strategy. Firefly users can also call traditional telephones (landline and mobile). Each Firefly user is assigned a custom Firefly telephone number. These numbers are 'simulated'; that is, they do not map onto the traditional telephone system. They are used solely to make calls to other Firefly users. Users of Firefly also have access to a fully-featured voicemail system, which can take messages when the user is offline or on another call.

Firefly works best over a broadband Internet connection, but can also operate using a standard dial-up modem. A Firefly call requires 24 kb/s of bandwidth in each direction, so calls may be made using a 33.6 kb/s modem connection.

The Freshtel Business



A simplified overview of how Freshtel VoIP technology works.

Protocol and codec translation

Since the majority of Call Termination Service (CTS) providers cannot interconnect directly to Firefly using the IAX2 protocol, IAX2 needs to be translated to H.323 or ISDN before being passed on to Freshtel's CTS providers (Comindico and Powertel). This translation is done by the VoiceStream translation servers.

The translation servers are currently located in Comindico's Sydney Point of Presence (PoP) and in Freshtel Australia's Melbourne data centre. The translators have been designed with speed, efficiency and scalability in mind.

Firefly also makes use of a new codec called iLBC, which compresses the voice information of a telephone call to reduce the amount of bandwidth required. This codec has some major advantages over the more traditional G.729 codec. iLBC offers the same voice quality as G.729 but degrades more gracefully when exposed to the packet loss and jitter that tend to occur on the Internet. Hence end-users are more likely to retain high call quality even when there is congestion over their Internet connection. The translation servers can also convert between numerous codec and signalling standards, including G.729 and G.711.

Making a Firefly-to-Firefly (on-net) call

A Firefly user dials another Firefly number. The Firefly software running on the user's PC contacts the Number Lookup Server (NLS) and finds out if the person they have called is online. If they are online then the NLS performs a 'handshake' between the parties and then leaves them to carry on a peer-to-peer call.

Making a Firefly-to-traditional (off-net) call

A Firefly user dials a standard telephone number. The Firefly software running on the user's PC contacts the NLS and finds out that the dialled number is part of the traditional (off-net) telephone network. The Firefly software then connects to the translation server, where the Firefly protocol is converted to a more traditional H.323 protocol or ISDN PRI before being passed on to our CTS providers for routing to the off-net telephone.

Billing and call detail records

As a telephone call passes through the VoiceStream translation server, information is also sent to the billing and Call Detail Record (CDR) generation server. Billing records are then made available to Firefly users online or as a PDF document. The billing system also has the ability to generate RADIUS packets for real time data feeds.

The Freshtel Business

5.5 EXISTING PRODUCTS

5.5.1 FIREFLY VOIP SOFTPHONE

The Firefly softphone was released in early 2004. It is a richly-featured softphone with instant messaging and voicemail for home, businesses and other organisations. Firefly lets anyone with a microphone and speakers or a **USB** handset communicate around the world.

Telephone calls to other Firefly users anywhere in the world are free, as are instant messaging to other Firefly users and the personal voicemail box. Calls can also be made to traditional telephones both nationally and internationally at competitive calling rates.

5.5.2 VIRBIAGE HARDWARE

FT102 USB Handset

The FT102 USB handset is Freshtel Australia's market-entry VoIP telephone, retailing currently at \$129 bundled with a CD ROM and \$10 worth of call credit. The FT102 handset is a small, easy-to-use VoIP telephone that runs on a Windows PC and gives the user basic VoIP telephony services.

Features and specifications

- easy-to-read **LCD** screen
- no external power required
- no sound card required
- very high sound quality
- light and comfortable to use
- no additional Windows drivers required
- feels like a conventional phone
- USB 1.1 compliant
- 1.2 metre curly cord, stretches to over 2 metres
- runs off power supplied via USB
- detects as a USB audio device and a human interface device for the LCD/keypad
- dimensions approximately 40 × 120 × 15 mm³

FT201 LAN Phone

The FT201 **LAN** (Local Area Network) telephone is currently in development, with manufacturing planned to commence in the second quarter of 2005. The FT201 is a fully-featured IAX/SIP-capable VoIP LAN phone and is the first in a new series of IAX compatible phones. The LAN phone is a stand-alone VoIP handset targeted at the residential, SME and

corporate markets. It has rich functionality and is expected to have an initial retail price of \$174.95.

Features and specifications

- VLAN support
- voice activity detection
- comfort noise generation
- multi-line support
- power over Ethernet (802.3af)
- easy configuration via DHCP
- backlit graphical LCD display
- configurable on-screen display
- phone-to-PC interface available via **XML**
- dual 10/100 Mb/s Ethernet
- IAX2 and SIP signalling
- codecs: iLBC, GSM, Speex, G.726, G.729AB and G.711 (μA-Law)
- G.165 32 ms echo canceller
- hardware Ethernet switching
- Linux-powered for robust and secure operation
- USB port for optional wireless connectivity.

Analogue Telephone Adaptor

The Virbiage Analogue Telephone Adaptor (**ATA**) is currently in the final stages of development, with manufacturing planned to commence in the first quarter of 2005. The Virbiage ATA connects standard telephone devices to an IP network, such as the Internet or a corporate network. It will take advantage of Firefly software, allowing Freshtel Australia to produce one of the first ATAs capable of both IAX2 and SIP. The built-in web server allows easy configuration. **DHCP** allows for remote automatic configuration in mass deployments such as an ISP service. The initial retail price is expected to be \$149.95.

Features and specifications

- supports multiple codecs
- designed for use on the VoiceStream network
- allows a standard PSTN telephone handset to be used as a fully-featured VoIP phone
- integrates seamlessly with the Firefly softphone
- delivers high sound quality
- fully approved to all relevant Australian standards
- sleek and modern design
- low entry cost

The Freshtel Business

- capable of auto configuration
- easy-to-use interface
- supports SIP 2.0 and IAX2 VoIP protocols
- TCP, UDP, HTTP, ICMP, DNS, DHCP, RTP and TFTP Internet protocols
- built-in Web server—easy to configure and password-protected
- 10 Mb/s Ethernet port
- analogue phone port
- VLAN and quality-of-service support
- NAT traversal using STUN and symmetric RTP
- advanced SIP features, including SRV DNS support.

5.5.3 GN NETCOM HEADSETS

Freshtel Australia has signed a distribution agreement with GN Netcom, a leading global provider of hands-free communications solutions. This enables Freshtel Australia to market GN Netcom headsets on Freshtel Australia's website together with a Firefly call credit. GN Netcom is currently assessing Firefly as part of their global VoIP strategy.

GN 2200 Omega

The GN 2200 Omega headsets are of commercial quality and are targeted at the small business market. Freshtel Australia currently retails the 2200 Omega at \$119, including \$5 of Freshtel call credit.

GN 9120

The GN9120 is a wireless headset. It uses GN Netcom's unique Smart Power Management technology, which enables the headset to continually assess how far it is from the base. It is also WiFi friendly, effectively using 95 unique channels across the entire 2.4 GHz spectrum without obstruction to the network.

Freshtel Australia currently retails the 9120 at \$395, including \$50 of Freshtel call credit.

5.5.4 CALL TERMINATION SERVICES

Freshtel Australia, through the Freshtel retail brand, provides Call Termination Services (CTS) at competitive rates compared to traditional telephones. CTS take-up has been strong since being launched in May 2004.

CTS charges have the potential to provide significant revenue streams in the VoIP business model.

Most consumers are accustomed to the rates currently charged by their existing telephone company. Using the Freshtel CTS model, consumers can experience reduced rates while still allowing profitable retail and wholesale margins.

Residential 'second line' services offer an additional market entry point, since the uptake of these services is limited by the base line rental charges imposed by current telephone service providers.

The Freshtel CTS service currently uses the Powertel network to route national calls, and the Comindico IP backbone to route calls to international destinations. These two networks can be used redundantly so that, in the event of failure of one network, all calls can be routed via the other network.

As VoIP becomes more accepted and as consumers begin to rely on the services provided by VoIP businesses, the company expects that the industry will most likely become more tightly regulated. Freshtel Australia is actively working with relevant government regulatory bodies to work within existing regulations while shaping future regulations placed on the VoIP industry.

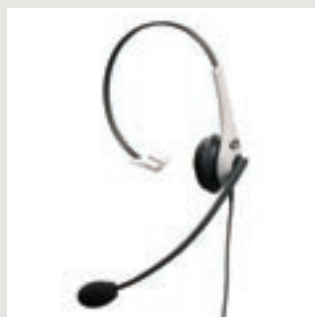
White label product (Voicedot)

The call termination and the associated billing system have been developed to allow for duplication. This will enable licensing to other organisations such as Internet Service Providers (ISPs). Each ISP can then operate their own branded CTS, enabling them to resemble a conventional stand-alone telecommunications service provider. Under current proposals, Freshtel Australia, via its wholly owned subsidiary Voicestream Networks, will derive revenue from the provision of wholesale CTS to these licensed operators.

Voicestream Networks currently has an exclusive reseller agreement covering Australia and New Zealand with Wholesale Communications Group, a major ISP wholesaler, which distributes to more than 220 Australian ISPs. Distribution under this agreement will commence in the first quarter of 2005. (Refer to Section 9.2 for details.)

Freshtel Australia also plans to establish similar arrangements in other countries with significant broadband penetration.

The Freshtel Business



1	2
3	4
5	6

1. Firefly softphone
2. FT102 USB handset
3. FT201 LAN phone
4. Analogue Telephone Adaptor
5. GN 2200 Omega
6. GN 9120

The Freshtel Business

5.6 DEVELOPMENT ROADMAP

5.6.1 FIREFLY

Freshtel Australia's current intention is to further develop the Firefly softphone. Features to be added include:

- **Conferencing**
Enables multi-party conferencing, including adaptive audio control to enhance quality.
- **Transfers**
Enable transfer of a call to another Firefly user.
- **Bluetooth device integration**
Many new mobile phones and PDAs support Bluetooth access, enabling them to be used as an external handset for Firefly.
- **Additional skin interfaces**
Enable new look and feel options, including a gallery of user-submitted designs.
- **Shared contact list**
Enables one common contact group to be shared among multiple users. If one user updates a contact, that change is reflected with other users running Firefly in the same contact group.
- **Message/voicemail distribution lists**
Allow a user to send a single voicemail or text message to a number of people (e.g. for clubs and event organisers).
- **Multiple lines**
Allow multiple incoming phone numbers.
- **Integration with Outlook and CRM packages**
Allows other programs to initiate a call on Firefly to integrate with Customer Relationship Management (CRM) or contact management software.
- **Integration with LAN phone and ATA**
Allows user to manage their phone calls on Firefly, but make or take the call on a Virbiage LAN phone or ATA device.
- **Sending and receiving SMS messages**
Allows Firefly users to exchange SMS text and multimedia messages with standard mobile phones.
- **Video support**
Full video conferencing, including latest video codecs (H.263 and H.264).
- **Port to Linux and Mac**
Development of new versions to support the Linux and Macintosh operating systems.
- **Support for Asian languages**
Addition of native support for non-Roman character sets to enable increased market penetration throughout Asia and the Middle East.

- **PDA version**

A Firefly version optimised for the new generation of WiFi PDA devices, allowing calls to be made and received on a PDA.

- **Call centre version**

A Firefly version with enhancements suited to a distributed call centre environment.

Freshtel Australia expects to implement these developments over the next 24 months.

5.6.2 SERVICES

In addition to further developing the Firefly softphone, Freshtel Australia is committed to further developing and expanding its range of services. Current developments include:

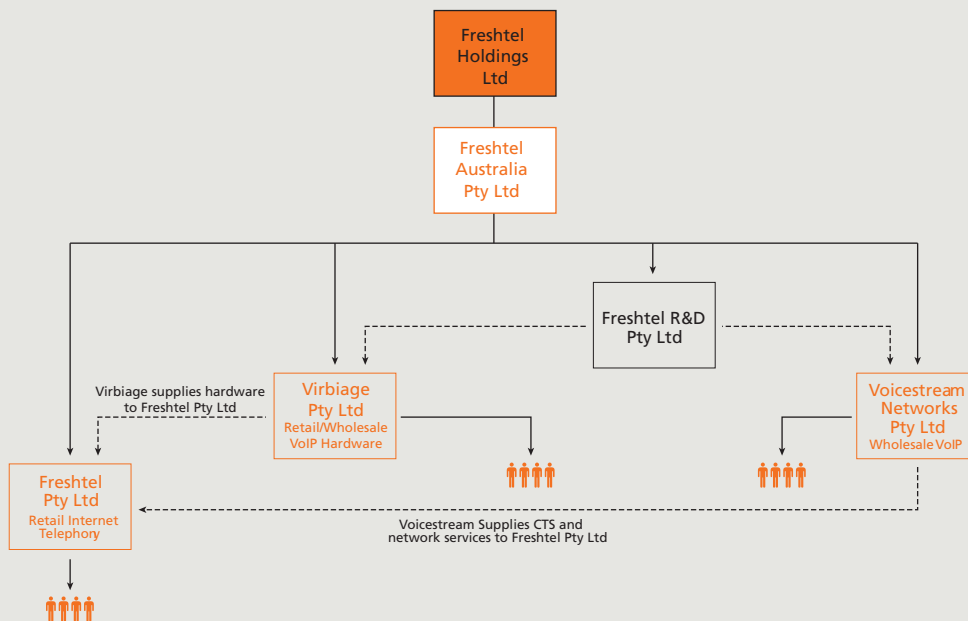
- **Incoming Australian phone numbers**
This is a major step forward, allowing a Firefly softphone to have a 'real' phone number. This service is in the final stages of development and is planned to be commercially available in the first quarter of 2005.
- **Email-to-voice support**
This would allow a user to call their personal Firefly number and have it read the contents of their email inbox. This service is planned for launch in the fourth quarter of 2006.

Planned future services include:

- **Hosted PBX systems**
This would allow integration of Firefly, LAN phones and ATA devices under a single interface to give small and medium business customers a 'one stop' telephony solution.
- **Call centre management software**
This would involve enhancement of the hosted PBX offering, specialised for use in call centres and other call queuing environments.
- **Call cost allocation**
This would allow each call to be costed directly to an existing customer account.
- **Fax services**
This would allow the sending and receiving of faxes from within a Windows or web-based environment.

Freshtel Australia expects to implement these developments over the next 24 months.

The Freshtel Business



5.7 BUSINESS OPERATIONS

5.7.1 BUSINESS STRUCTURE

The Freshtel Australia business is structured into three separate channels and an internal research and development arm. Each channel has its own brand and performs a different business function.

Although the different businesses interoperate very closely, they allow Freshtel Australia to present different commercial strategies to the market.

Virbiage Pty Ltd is a manufacturer and distributor of VoIP hardware such as Internet telephones and analogue telephone adaptors. Virbiage retails these products through its own web site and is in the process of setting up distribution agreements with local Australian and international partners.

Voicestream Networks Pty Ltd runs the Internet telephone network used to route telephone calls. Voicestream provides a wholesale version of the Freshtel Australia retail offering. This wholesale service is targeted at ISPs, which potentially can easily offer telephony services to their existing subscriber base.

Both of these companies supply services to **Freshtel Pty Ltd**, the retail provider of these services. Virbiage and Voicestream are supported by Freshtel R&D, which undertakes all product research and development. Freshtel R&D is currently part of the Australian Government R&D initiative and has already received two research grants.

5.7.2 HARDWARE MANUFACTURERS





Manufacturing of the Virbiage hardware can be undertaken by a number of contract manufacturers. Freshtel Australia is currently in discussions with several contract manufacturers in Australia and China. All Virbiage hardware follows standard design-for-manufacture guidelines to allow Freshtel Australia to contract work to electronics contract manufacturers worldwide. Prototype and short-run manufacture (less than 200 units) is undertaken locally.

Freshtel Australia ultimately plans to choose a contract manufacturer based on its full service offering, which it expects to do by the third quarter of 2005. The contract manufacturer should be able to handle sourcing and inventory management of the common parts, and lead-time management with distributors of specialised components. Freshtel Australia will also favour contract manufacturers that will conduct unit testing and full retail presentation.

5.7.3 LOGISTICS

Logistics is currently handled in-house, with handsets being distributed worldwide via Australia Post and couriers. Freshtel Australia currently charges \$9.95 for delivery, with costs being usually \$4.50–\$12.00. The standard order-to-ship time is 24 hours, with local deliveries being received by the customer within 2–3 days of order approval. International delivery is normally seven days, depending on customs.

The Freshtel Business

BRANDS	PRODUCTS	MARKET
	Firefly softphone Freshtel CTS FT102 FT201 (manufacturing in Q2 2005) Virbiage ATA (manufacturing in Q1 2005) GN Netcom 9120 & 2200	Direct: consumer/SME
	FT102 FT201 (manufacturing in Q2 2005) Virbiage ATA (manufacturing in Q1 2005)	Direct & indirect: retail & wholesale hardware sales
	Firefly under ISP/Telco brand Firefly translation server (under OEM) Billing systems Virbiage hardware (with resellers) CTS (under ISP brand)	Indirect: ISPs and telcos
	Firefly softphone Firefly translation server White label billing systems Hardware design and development	Internal: technology licensing

Freshtel Australia has had discussions with Australia Post logistics. Once volumes are great enough, stock could be warehoused with their post logistics centre, if deemed commercially suitable by the company.

The company intends, during the third quarter of 2005, to organise direct shipping from handset manufacturers to channel partners and/or distribution partners, allowing Freshtel Australia to outsource shipping and distribution costs wherever possible.

5.7.4 DISTRIBUTION CHANNELS

Freshtel Australia (via Voicestream Networks) has secured an exclusive distribution agreement for the Australian and New Zealand markets with Wholesale Communications Group Pty Ltd (WCG), a major wholesaler to the ISP market. WCG currently services more than 250 ISPs. WCG will work to enable each of these ISPs to sell Freshtel Australia VoIP services to their existing user bases. (Refer to Section 9.2 for details.)

Freshtel Australia is also negotiating a series of licensing agreements with hardware vendors, including GN Netcom, as part of its Alliance Programme. The Freshtel Alliance Programme, an internal method of identifying and assessing business partners, is a significant contributor to the success of Freshtel Australia and thus the company is dedicating time and expertise to selecting and managing appropriate partner companies.

Freshtel Australia also has plans to launch its products and services directly in the United Kingdom during 2005. Early discussions have commenced with several parties in regard to alliances and joint ventures.

5.7.5 COMPETITIVE ADVANTAGE AND STRATEGY

Freshtel Australia has built a strong and dedicated team of technologists through Teragen International, its contracted R&D team. The team has developed and continues to develop leading open-standard software and hardware VoIP products.

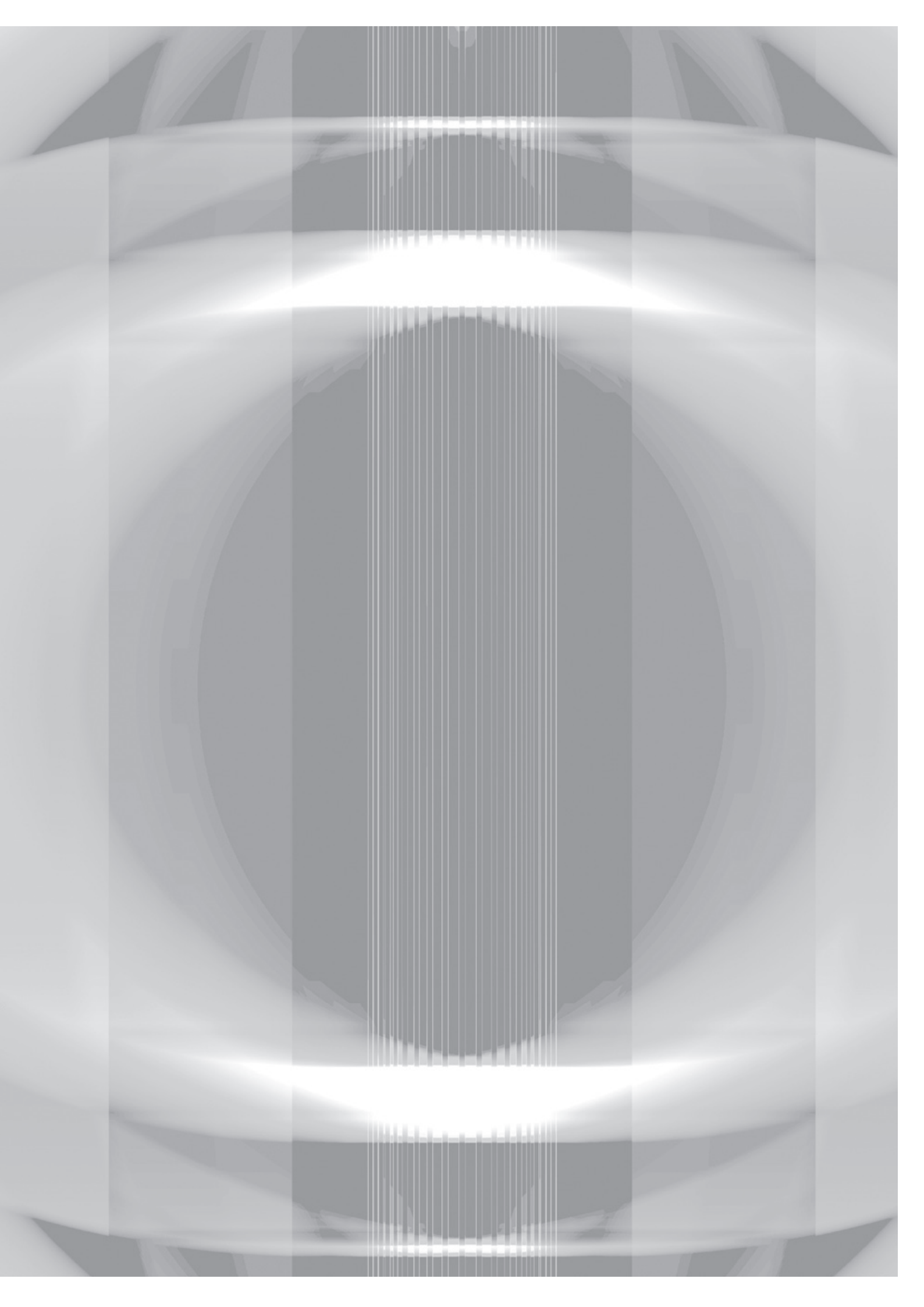
Freshtel Australia is developing a network of business partners interested in aligning their own products with those of Freshtel Australia. These companies include ISPs, value-added resellers and hardware manufacturers.

Freshtel Australia's Firefly softphone was launched in January 2004 and is being used in most countries, with more than 180,000 registered users at the date of this Prospectus.

This uptake has predominantly been by steady growth, with only limited above-the-line marketing activities. Freshtel Australia also provides outgoing calls at competitive rates to landlines across the globe.

A key differentiator in an increasingly fragmented market is the ability to provide hardware, softphone and CTS. Freshtel Australia is ideally placed to provide all three, allowing a fully integrated solution.

Freshtel Australia is a leading exponent of the IAX2 VoIP protocol, and is at the forefront of its development as it becomes an industry standard. Through its work with Asterisk, Freshtel Australia is driving the ongoing development of IAX2 and working on further enhancements of the protocol. As Asterisk rapidly grows in popularity, Freshtel Australia hardware and software systems based on IAX2 and SIP are expected to fill a rapidly expanding VoIP market.



6

Board of Directors

MR DAVID ELBOURN CHIEF FINANCIAL OFFICER

David Elbourn is responsible for the financial control of Freshtel Australia. He is a chartered accountant (ACA) in a boutique accounting firm, Dillon and Elbourn Chartered Accountants, specialising in fast growing SMEs from all over Australia. Clients include companies ranked in *Business Review Weekly's* Fast 100.

David has been the financial advisor to Freshtel Australia since its inception, has personally invested in Freshtel Australia and is a significant shareholder in Freshtel Australia.

MR MICHAEL CAREW CHIEF EXECUTIVE OFFICER AND MANAGING DIRECTOR

Michael Carew has founded and managed several very successful businesses and understands the importance of teamwork and the ability to adapt quickly to take advantage of market change and trends. Michael has always illustrated an innovative approach to the development of products, from inception through design-proofing to sales and marketing. He has considerable experience with product manufacturing processes in Taiwan and mainland China.

Michael is the founder of Freshtel Australia. He has planned and orchestrated the development of Freshtel Australia products and is the major shareholder in Freshtel Australia.

Michael is often sought out by the industry and media for his opinions and insights on the current and future development of the VoIP industry. He was recently appointed as the Chairman of the newly formed Australian VoIP Association (AVOLPA), an industry-driven association.

Michael will spearhead global commercialisation for Freshtel Australia.

MR SEBASTIAN FILZEK CHIEF TECHNOLOGY OFFICER

Sebastian Filzek has been instrumental in the development of Freshtel's strategic direction and products since the company's inception. He has been involved in Internet systems development for over 10 years and electronic design for over 15 years. He has developed many different concepts ranging from software-based systems to computer peripherals. He has been involved in developing several first applications, including the first eCommerce transaction system delivered via a mobile phone and the first commercial classified advertising website in Australia.

Sebastian first became involved with VoIP technology in 1995 and has been working with production VoIP technology since 1998. During this time, he has gathered a great wealth of industry and technical knowledge. He is a significant shareholder in Freshtel Australia.

Sebastian is also a director and shareholder (through his investment company Gluaff Investments Pty Limited, which owns 8%) of Wholesale Communications Group Pty Limited, the company's main wholesale distributor in Australia (see reseller agreement review at Section 9.2).



MR LES TAYLOR
CHAIRMAN

Les Taylor is the former Chief Solicitor and General Counsel of the Commonwealth Bank Group, and has been involved in banking and commercial law in Australia for over 40 years. He was a member of the Business Regulatory Advisory Group established by the Government in 1996 to restructure the Corporations Law in Australia, and remained a member of that body through CLERP 1 to CLERP 5.

Les is a member of the Takeovers Panel, a statutory body with power to adjudicate disputes between corporations in Australia, and a director of Arab Bank Australia, a wholly owned subsidiary of the international banking group Arab Bank PLC. He is Chairman of the Safety, Rehabilitation and Compensation Commission, a statutory authority established by the Federal Government to oversee workers' compensation arrangements for Commonwealth employees, and also has power as the regulator under the Occupational Health and Safety legislation.

During his period as General Counsel of the Commonwealth Bank, Les handled the legal work for the conversion of the Commonwealth Bank from a statutory authority to a public company, and headed the Bank's legal team for the acquisition of the State Bank of Victoria in 1991, as well as the takeover in 2001 of the Colonial Bank Group—the largest takeover in Australia's corporate history. His background and extensive experience in corporate governance and regulatory compliance will be of considerable assistance to the Company.

MR PETER WARNER
COMMERCIAL DIRECTOR

Peter Warner heads the Freshtel Sydney office and is responsible for the corporate finance and global commercialisation of Freshtel Australia. He is a former senior executive with a boutique corporate advisory firm and has worked with Australia's premier business leaders to formulate business strategy and staff development schemes in many of the region's leading corporations, including Unilever, Tricon, Zurich Insurance, Fuji Xerox and Adobe. He was contracted to the Commonwealth Bank of Australia as an Executive Coach/Business Consultant working with the bank's senior executive tier.

Peter has previously managed a parallel career as one of the country's top yachtsmen, accumulating two world titles and over 10 Australian titles, and was a member of the Australian Olympic Sailing Team in the run-up to the 2000 Games.

Peter has also held a senior role with a successful online software development company. In his role as Chief Officer—Development, he oversaw many large contracts and built a vast knowledge of cutting-edge technology applications.

7

Risk Factors

7.1 INTRODUCTION

An investment in the Company is not risk free and prospective new investors should consider the risk factors described below, together with information contained elsewhere in this Prospectus, before deciding whether to apply for Shares.

The following is not intended to be an exhaustive list of the risk factors to which the Company is exposed.

In this section of the Prospectus, a reference to 'Company' also includes a reference to Freshtel Australia (and its subsidiaries).

7.2 ECONOMIC RISKS

General economic conditions, movements in interest and inflation rates and currency exchange rates may have an adverse effect on the Company's activities, as well as on its ability to fund those activities.

7.3 ADDITIONAL REQUIREMENTS FOR CAPITAL

The Company's capital requirements depend on numerous factors. Depending on the Company's ability to generate income from its operations, the Company may require further financing in addition to amounts raised under the capital raising. Any additional equity financing will dilute shareholdings, and debt financing, if available, may involve restrictions on financing and operating activities. If the Company is unable to obtain additional financing as needed, it may be required to reduce the scope of its operations and scale back its expansion and development programmes as the case may be.

7.4 LOSS OF KEY CLIENTS

Freshtel Australia has a number of important client relationships. The loss of one or more key clients is likely to adversely affect the operating results of the Company after the acquisition.

7.5 RELIANCE ON KEY MANAGEMENT

The responsibility of overseeing the day-to-day operations and the strategic management of the Company depends substantially on its senior management and its key personnel. There can be no assurance given that there will be no detrimental impact on the Company if one or more of these employees cease their employment.

7.6 TECHNOLOGICAL DEVELOPMENTS

Freshtel Australia relies on its ability to adapt to technological developments. A failure to adapt to new developments could lead to a loss of opportunities and adversely impact on the Company's operating results and financial position.

7.7 COMPETITION

There is a risk that the Company will not be able to continue to compete profitably in the telecommunications industry in the long term. The potential exists for the nature and extent of the competition to change rapidly, which may cause loss to the Company.

As a strategic response to changes in the competitive environment, the Company may from time to time make research and development, manufacturing, pricing, service or marketing decisions that could have a material effect on the Company's business, results of operations and financial conditions. There can be no certainty that these strategic responses are the correct responses.

There can be no assurance that other parties, incumbent or emerging, in Australia and globally will not develop technologies, software, hardware, services, networks or other products that compete with the Company or supersede the products of the Company.

7.8 MANAGEMENT OF GROWTH

There is a risk that management of the Company will not be able to implement the Company's growth strategy after completion of the listing on ASX. The capacity of the new management to properly implement and manage the strategic direction of the Company may affect the Company's financial performance.

7.9 PROTECTION OF PROPRIETARY TECHNOLOGY

While the Company will continue to use all reasonable endeavours to protect its proprietary technology, there can be no assurance that these measures have been, or will be, sufficient.

7.10 PRODUCT LIABILITY

The Company's contracts with its clients generally contain provisions drafted to limit the Company's exposure to product liability claims. However, it is possible that the limitation of liability provisions may not be effective in certain jurisdictions. Hence there can be no assurance that the Company will not be subject to such claims.

The Company carries (and will continue to carry after the listing on ASX) what the Directors consider to be adequate insurance. However, there can be no assurance that a significant claim, if successful, would not adversely impact on the Company's financial performance.

7.11 SHARE MARKET

Share market conditions may affect the value of the Company's quoted securities regardless of the Company's operating performance. Share market conditions are affected by many factors such as:

- (a) general economic outlook;
- (b) interest rates and inflation rates;
- (c) currency fluctuations;
- (d) changes in investor sentiment towards particular market sectors;
- (e) the demand for, and supply of, capital; and
- (f) terrorism or other hostilities.

7.12 CHANGES TO ACCOUNTING STANDARDS

For reporting periods beginning on or after 1 January 2005, the Company and its subsidiaries must comply with International Financial Reporting Standards (IFRS). The most significant changes to accounting treatment under IFRS as it applies to the Company relates to the accounting for research and development costs, intangible assets being goodwill, share-based payments and taxation.

Intangible Assets

AASB 138 'Intangible Assets' generally requires derecognition of all items that do not qualify as identifiable intangible assets.

Goodwill

Amortisation of goodwill will no longer be permitted under the new standard. At the date of adoption of IFRS, goodwill will be allocated to cash-generating units of the entity and will be impairment-tested on initial adoption of IFRS and annually thereafter.

Any necessary impairment write-down in relation to goodwill will be expensed through the statement of financial performance.

Research and Development

Currently, capitalised items of research costs that have been internally generated must be derecognised under the new standard. Any further research costs must be expensed in the year they are incurred.

Qualifying expenditure in relation to development phase costs may be capitalised and impairment tested annually until the related asset is complete, at which time they will be amortised over the useful life of the related asset. The company must review the amortisation period and the amortisation method at least at the end of each annual reporting period.

Share-Based Payments

Under AASB 2, all share-based payments to employees and third parties in respect of goods and services must be expensed and a corresponding increase in equity be recognised when goods or services are received (or a liability if the goods or services were acquired in a cash-settled share-based transaction). This will result in additional expenses being recorded and therefore lower earnings.

Income Tax

AASB 112 'Income Tax' requires all income tax balances to be calculated using the comprehensive balance sheet liability method. Deferred tax items will be calculated by comparing the difference in carrying amounts to tax bases for all assets and liabilities and multiplying this by the tax rates expected to apply to the period when the asset is realised or the liability settled. Recognition of the resulting amounts is subject to some exceptions, but generally deferred tax balances must be calculated for each item in the statement of financial position. Deferred tax assets will only be recognised where there exists the probability that future taxable profit will be available to recognise the asset.

7.13 RESEARCH AND DEVELOPMENT CAPABILITY

Freshtel Australia has outsourced its whole research and development function to Teragen under the Consultancy Agreement (referred to at Section 9.7 of this Prospectus). The Consultancy Agreement requires Teragen to train internal staff to carry out research and development, the training to be completed within the initial term of the agreement. There is a risk that Teragen could breach the terms of this agreement, leaving the company temporarily without a research and development function until it was able to recruit relevant staff to replace the Teragen consultants.

7.14 GOVERNMENT REGULATION

In Australia the telecommunications industry is governed by legislation. The primary legislation includes:

- the Telecommunications Act 1997;
- the Australian Communications Authority Act 1997;
- the Telecommunications (Transitional Provisions and Consequential Amendments) Act 1997;
- the Trade Practices Amendment (Telecommunications) Act 1997;
- the Telecommunications (Consumer Protection and Service Standards) Act 1999; and
- the Spam Act 2003.

Overseas markets will be subject to similar regulatory requirement. Accordingly, changes to this regulatory environment may impact on Freshtel Australia's operations. Freshtel Australia has recognised the need to have a political lobby group to ensure the interests of the emerging VoIP industry are met. Freshtel Australia is currently in the process of founding the Australian Voice over Internet Protocol Association (AVoIPA) with several other relevant industry bodies.

7.15 INVESTMENT SPECULATIVE

The above list of risk factors ought not to be taken as exhaustive of the risks faced by the Company or by investors in the Company.

The above factors, and others not specifically referred to above, may in the future materially affect the financial performance of the Company and the value of the securities offered under this Prospectus. Therefore, the securities to be issued pursuant to this Prospectus carry no guarantee with respect to the payment of dividends, returns of capital or the market value of those securities.

Potential investors should consider that the investment in the Company is speculative and should consult their professional advisers before deciding whether to apply for Shares.

8

Independent Accountant's Report

4 March 2005
The Board of Directors
Freshtel Holdings Limited
Level 11, 91 York Street
SYDNEY NSW 2000



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Dear Sirs,

1. INTRODUCTION

This Independent Accountant's Report ("Report") has been prepared at the request of the Directors of Freshtel Holdings Limited ("the Company") for inclusion in a Prospectus ("the Prospectus") to be dated on or about 4 March 2005 relating to the issue of 10,000,000 fully paid ordinary shares ("Shares") at an issue price of \$0.20 per share each to raise \$2,000,000. The Company reserves the right to accept oversubscriptions of up to \$1,000,000 through the issue of up to a further 5,000,000 Shares at an issue price of \$0.20 per share.

Expressions defined in the Prospectus have the same meaning in this Report.

2. BACKGROUND

The Company was incorporated on 20 October 2004 as Firstplan Investments Limited. The Company changed its name to Freshtel Holdings Limited on 17 January 2005.

Following a seed raising of approximately \$2.2 million that was completed in November 2004, the Company entered into an agreement with Freshtel Australia Pty Ltd ("Freshtel Australia") and its shareholders, under which the Company agreed to acquire all of the issued Shares in Freshtel Australia in return for the issue of 56,100,000 Shares and 93,900,000 Performance Shares in the Company to the Freshtel Australia shareholders.

At a general meeting of shareholders held on 17 January 2005, approval was obtained to proceed with the acquisition of Freshtel Australia and the Company is now seeking to raise funds to facilitate a listing on the Australian Stock Exchange.

3. SCOPE

PKF Corporate Advisory Services (WA) Pty Ltd has been requested to conduct an independent review of the Historical Statement of Financial Position of the Company as at 30 November 2004, and the Pro-Forma Consolidated Statement of Financial Position of the Company as at 30 November 2004.

The purpose of the Pro-Forma Consolidated Statement of Financial Position is to demonstrate the financial effect on the Company assuming that the following transactions and events had taken place on 30 November 2004:

- The acquisition of 100% of Freshtel Australia via the issue of 56,100,000 Shares and 93,900,000 Performance Shares as approved by the Company's shareholders in a general meeting on 17 January 2005. The value assigned by the Directors to the acquisition of Freshtel Australia is based on the table below.

	No. Issued	Value per Security \$	Total Value \$
Shares	56,100,000	0.20	11,220,000

No value has been assigned to the 93,900,000 Performance Shares as the conversion of the Performance Shares to ordinary shares depends on Freshtel Australia achieving various milestones that cannot be reliably measured. The Performance Shares have been disclosed as a contingent event in Note 17 of this Report.

The Company is acquiring 100% of the issued capital of Freshtel Australia. The Directors' fair value of 100% of the net assets of Freshtel Australia as at 30 November 2004 was \$249,177, resulting in goodwill on the acquisition of Freshtel Australia of \$10,970,823.

Independent Accountant's Report

- The issue of 10,000,000 shares at \$0.20 each to raise \$2,000,000 assuming no oversubscriptions;
- The settlement of capital raising costs incurred by the Company of \$336,010 in relation to the Prospectus comprising:

	\$
ASIC fees	2,010
ASX fees	34,000
Advisers' fees	260,000
Printing	10,000
Miscellaneous	30,000
Total	336,010

As at 30 November 2004, the Company had already incurred \$68,179 of capital raising costs, resulting in a cash payment of \$267,831 for capital raising costs. These costs are recognised directly in equity as a reduction of the share proceeds received in accordance with UIG 23 'Transaction costs arising on the issue of equity instruments'.

- The issue of 665,000 free options to brokers as detailed in the Company's prospectus dated 27 October 2004. The options to be issued by the Company have not been brought to account as an expense. The option terms and conditions are disclosed in Section 10.5.3 of the Prospectus.

Our review of the Historical Statement of Financial Position and Pro-Forma Consolidated Statement of Financial Position of the Company was conducted in accordance with Australian Auditing Standard AUS 902 'Review of Financial Reports' and was limited to such inquiries and procedures as we, in our professional judgement, considered reasonable in the circumstances including:

- a review of work papers, accounting records and other documents prepared by the Company and FreshTel Australia;
- a review of the Directors' assumptions used to compile the Pro-Forma Consolidated Statement of Financial Position as set out in Note 14 of this Report;

- inquiry of Directors, management and others; and
- a review for post balance date events.

Our review was undertaken in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that:

- The Historical Statement of Financial Position of the Company as at 30 November 2004 is not presented fairly in accordance with the measurement requirements, but not the disclosure requirements, of applicable Accounting Standards and other mandatory professional reporting requirements in Australia; and
- The Pro-Forma Consolidated Statement of Financial Position of the Company as at 30 November 2004 is not presented fairly in accordance with the measurement requirements, but not the disclosure requirements, of applicable Accounting Standards and other mandatory professional reporting requirements in Australia, assuming the transactions and events set out in Note 14 of Annexure A had taken place as at 30 November 2004.

These review procedures do not provide all the evidence that would be required in an audit; thus the level of assurance provided is less than given in an audit. We have not performed an audit on the Historical Statement of Financial Position and Pro-Forma Consolidated Statement of Financial Position of the Company set out in Annexure A and accordingly, we do not express an audit opinion on the Historical and Pro-Forma Consolidated Statement of Financial Position of the Company as at 30 November 2004.

4. STATEMENT

4.1 HISTORICAL STATEMENT OF FINANCIAL POSITION OF THE COMPANY

Based on the scope of our review, which is not an audit, nothing has come to our attention that causes us to believe that the Historical Statement of Financial Position of the Company as at 30 November 2004, as set out in Annexure A, is not presented fairly in accordance with the measurement requirements, but not the disclosure requirements, of applicable Accounting Standards and other mandatory professional reporting requirements in Australia.

Independent Accountant's Report

4.2 PRO-FORMA CONSOLIDATED STATEMENT OF FINANCIAL POSITION OF THE COMPANY

Based on the scope of our review, which is not an audit, nothing has come to our attention that causes us to believe that the Pro-Forma Consolidated Statement of Financial Position of the Company as at 30 November 2004, as set out in Annexure A, is not presented fairly in accordance with the measurement requirements, but not the disclosure requirements, of applicable Accounting Standards and other mandatory professional reporting requirements in Australia, on the basis and assumption that the transactions and events set out in Note 14 of Annexure A had taken place as at 30 November 2004.

4.3 INHERENT UNCERTAINTY CONCERNING CARRYING VALUE OF GOODWILL ON ACQUISITION OF FRESHTEL AUSTRALIA

Without qualification to the review opinion expressed in Section 4.2 above, attention is drawn to the following matter. As a result of the acquisition of FreshTel Australia by the Company, goodwill on consolidation of \$10,970,823 arose. As disclosed in Note 1(n) of Annexure A, the ability for the goodwill to be carried forward as an asset depends on FreshTel Australia trading profitably in the future and continuing to sign up customers to use their VoIP software and technology in line with the planned business objectives of the Company.

5. SUBSEQUENT EVENTS

To the best of our knowledge and belief, and based on the work we have performed in relation to the scope of work set out in Section 3 of this Report, there have been no material transactions and events subsequent to 30 November 2004, other than those included in our Report, that would require a comment on or adjustment to, the information referred to in our Report or that would cause the information included in this Report to be misleading.

We have no responsibility to update this Report for events and circumstances occurring after the date of this Report.

6. DECLARATION

PKF Corporate Advisory Services (WA) Pty Ltd is responsible for this Report. This Report is strictly limited to the matters contained herein and is not to be read as extending by implication or otherwise, to any other matter.

PKF Corporate Advisory Services (WA) Pty Ltd does not have any interest that could reasonably be regarded as being capable of affecting its ability to give an unbiased opinion in relation to this matter.

Except for fees relating to this Report and the preparation of an Independent Expert's Report in relation to the planned acquisition of FreshTel Australia, which are based on normal commercial terms, PKF Corporate Advisory Services (WA) Pty Ltd does not have any interest in the Company nor in the outcome of the Capital Raising.

PKF Corporate Advisory Services (WA) Pty Ltd has not made, and will not make, any recommendation through the issue of this Report to potential investors of the Company as to the merits of the investment.

The nature of this report is such that it should be given by an entity that holds an Australian Financial Services licence under the Financial Services Reform Act 2001. PKF Corporate Advisory Services (WA) Pty Ltd is wholly owned by PKF Chartered Accountants and holds the appropriate Australian Financial Services licence.

Consent for the inclusion of this Report in the Prospectus in the form and context in which it appears has been given. At the date of this Report, this consent has not been withdrawn.

Yours faithfully

PKF Corporate Advisory Services (WA) Pty Ltd



IAN P OLSON

Director

Authorised Representative under Proper Authority

Independent Accountant's Report

ANNEXURE A—FINANCIAL INFORMATION STATEMENT OF FINANCIAL POSITION

Set out below is the reviewed Historical Statement of Financial Position of the Company as at 30 November 2004, and the reviewed Pro-Forma Consolidated Statement of Financial Position of the Company as at 30 November 2004 prepared on the basis that the assumptions and events as set out in Note 14 had taken place as at 30 November 2004.

	Notes	Reviewed 30 November 2004 \$	Reviewed Pro-forma Consolidated 30 November 2004 \$
CURRENT ASSETS			
Cash assets	2	2,211,350	3,955,065
Receivables	3	-	196,129
Inventories	4	-	144,246
Other	5	-	47,226
TOTAL CURRENT ASSETS		2,211,350	4,342,666
NON-CURRENT ASSETS			
Other financial assets	6	-	187,500
Property, plant and equipment	7	-	102,261
Intangible assets	8	-	11,381,165
Deferred tax assets	9	-	220,890
TOTAL NON-CURRENT ASSETS		-	11,891,816
TOTAL ASSETS		2,211,350	16,234,482
CURRENT LIABILITIES			
Payables	10	42,393	827,742
Interest bearing liabilities	11	-	30,956
Other liabilities	12	-	245,436
TOTAL CURRENT LIABILITIES		42,393	1,104,134
NON-CURRENT LIABILITIES			
Interest bearing liabilities	11	-	8,800
Deferred tax liabilities		-	422
TOTAL NON-CURRENT LIABILITIES		-	9,222
TOTAL LIABILITIES		42,393	1,113,356
NET ASSETS		2,168,957	15,121,126
EQUITY			
Contributed equity	13	2,200,647	15,152,816
Retained profits / (Accumulated losses)		(31,690)	(31,690)
TOTAL EQUITY		2,168,957	15,121,126

The above statements of financial position should be read in conjunction with the accompanying notes.

Independent Accountant's Report

NOTES TO THE STATEMENTS OF FINANCIAL POSITION

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Statements of Financial Position have been prepared in accordance with Accounting Standards, Urgent Issues Group Consensus Views and other authoritative pronouncements of the Australian Accounting Standards Board and the Corporations Act 2001. The Statements of Financial Position have been prepared on an accruals basis based on historical costs, and, except where stated, do not take into account changing money values or current valuations of non-current assets, unless otherwise stated.

The Statements of Financial Position have been prepared in accordance with the measurement requirements, but not the disclosure requirements, of applicable Accounting Standards and other mandatory professional reporting requirements in Australia.

The following is a summary of the material accounting policies adopted in the preparation and presentation of the Statements of Financial Position. The accounting policies have been consistently applied, unless otherwise stated.

A. PRINCIPLES OF CONSOLIDATION

The financial statements of controlled entities are included from the date control commences until the date control ceases.

Unrealised gains and losses and inter-entity balances resulting from transactions with or between controlled entities are eliminated in full on consolidation.

B. CASH AND CASH EQUIVALENTS

Cash on hand and in banks and short-term deposits are stated at nominal value.

C. RECEIVABLES

Trade receivables are recognised and carried at original invoice amount less a provision for any uncollectible debts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off as incurred.

D. RECOVERABLE AMOUNT

Non-current assets measured using the cost basis are not carried at an amount above their recoverable amount, and where carrying values exceed this recoverable amount, assets are written down.

E. PLANT AND EQUIPMENT

Each class of property, plant and equipment is carried at cost or fair value less, where applicable, any accumulated depreciation. All assets acquired are initially recorded at their cost of acquisition at the date of acquisition, being the fair value of the consideration plus incidental costs directly attributable to the acquisition.

F. DEPRECIATION

All assets, excluding freehold land and buildings, are depreciated over their useful lives. The depreciation rates used for each class of assets are as follows:

Plant and Equipment	5–40%
Motor Vehicles	12.5%

G. RESEARCH AND DEVELOPMENT COSTS

Costs incurred on research and development are deferred to future periods to the extent that they are expected beyond any reasonable doubt to be recovered. Deferred costs will be amortised from the commencement of commercial production of the product to which they relate on a straight-line basis over the period of the expected benefits, which is estimated to be three years.

H. PAYABLES

Liabilities for trade creditors and other amounts are carried at cost, which is the fair value of the consideration to be paid in the future for goods and service received, whether or not billed to the Company.

I. PROVISIONS

Provisions are recognised when the Company has a legal, equitable or constructive obligation to make a future sacrifice of economic benefits to other entities as a result of past transactions or other past events, it is probable that a future sacrifice of economic benefits will be required, and a reliable estimate can be made of the amount of the obligation.

J. CONTRIBUTED EQUITY

Issued and paid-up capital is recognised at the fair value of the consideration received by the Company. Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction of the share proceeds received.

Independent Accountant's Report

K. INCOME TAX

Tax-effect accounting is applied using the liability method whereby income tax is regarded as an expense and is calculated on the accounting profit after allowing for permanent differences. To the extent timing differences occur between the time items are recognised in the financial statements and when items are taken into account in determining taxable income, the net related taxation benefit or liability, calculated at the current rates, is disclosed as a future income tax benefit or a provision for deferred income tax. The net future income tax benefit relating to tax losses and timing differences is not carried forward as an asset unless the benefit is virtually certain of being realised.

L. INVESTMENTS

Non-current investments are measured at cost. The carrying amount of investments is reviewed at each reporting date by the directors to ensure it is not in excess of the recoverable amount of these investments.

M. GOODWILL

Goodwill represents the excess of the cost of acquisition over the fair values of the net assets acquired. Goodwill is amortised over a period of 20 years.

N. RECOVERABLE AMOUNT OF GOODWILL

At a general meeting of the Company held on 17 January 2005, approval was given to acquire 100% of the issued capital of Freshtel Australia. At the date of acquisition, the Directors of the Company have assessed the fair value of the net assets of Freshtel Australia to be \$249,177, comprising:

	\$
Cash assets	11,546
Receivables	196,129
Inventory	144,246
Prepayments	47,226
Plant & equipment	102,261
Investments	187,500
Deferred tax assets	220,890
Intangible assets	410,342
Payables	(785,349)
Other liabilities	(245,436)
Interest bearing liabilities	(39,756)
Deferred tax liabilities	(422)
Net assets	249,177
Consideration	11,220,000
Goodwill on consolidation	10,970,823

Freshtel Australia was established in 2002, and since that time, has undertaken research and development of its VoIP software and hardware technology, and has commenced commercial sales and marketing activities.

The immediate objective of the Directors of the Company is to implement Freshtel Australia's business plan for larger scale sales of their VoIP software and hardware technology. The Directors believe that Freshtel Australia will be successful in achieving its business plan and will trade profitably in the future.

This depends on Freshtel Australia trading profitably in the future and continuing to sign up customers to use their VoIP software and hardware technology, in line with the planned objectives of the Company.

The Directors have considered the carrying value of goodwill arising on consolidation at the date of this Report and believe it to be recoverable.

O. ACQUISITIONS OF ASSETS

The purchase method of accounting is used for all acquisitions of assets regardless of whether equity instruments or other assets are acquired. Cost is measured as the fair value of assets given up, shares issued or liabilities undertaken at the date of acquisition plus incidental costs directly attributable to the acquisition. Where equity instruments are issued in an acquisition, the value of the instruments is their market price as at the acquisition date, unless the notional price at which they could be placed in the market is a better indicator of fair value.

P. INVENTORY

Inventories are valued at the lower of cost and net realisable value. Costs are assigned on a first-in-first-out basis.

Net Realisable Value

Net realisable value is determined on the basis of expected selling price.

Q. INCOME IN ADVANCE

Income in advance consists mainly of call time charges and will be recognised as earned.

Independent Accountant's Report

	Notes	Reviewed 30 November 2004 \$	Reviewed Pro-forma Consolidated 30 November 2004 \$
2. CASH ASSETS			
Cash	15	2,211,350	3,955,065
Total cash assets		2,211,350	3,955,065
3. RECEIVABLES			
Receivables		–	1,681
Other debtors		–	5,062
Unsecured loans		–	12,290
GST refundable		–	41,714
Income tax receivable		–	135,382
Total receivables		–	196,129
4. INVENTORIES			
Stock on hand		–	65,448
Raw materials		–	78,798
Total inventories		–	144,246
5. OTHER ASSETS			
Prepayments		–	47,226
Total other assets		–	47,226
6. OTHER FINANCIAL ASSETS			
Shares in unlisted unit trust—at cost		–	187,500
Total other financial assets		–	187,500
7. PROPERTY, PLANT AND EQUIPMENT			
Plant and equipment at cost		–	81,205
Less: Accumulated depreciation		–	(22,131)
Property improvements at cost		–	1,700
Less: accumulated depreciation		–	(28)
Motor vehicles at cost		–	16,846
Less: accumulated depreciation		–	(4,321)
Research and development equipment at cost		–	31,388
Less: accumulated depreciation		–	(2,398)
Total property, plant and equipment		–	102,261

Independent Accountant's Report

Notes	Reviewed 30 November 2004 \$	Reviewed Pro-forma Consolidated 30 November 2004 \$
8. INTANGIBLES		
Borrowing costs	–	295
Less: accumulated amortisation	–	(136)
Business establishment costs	–	19,340
Less: accumulated amortisation	–	(18,770)
Internet establishment costs	–	2,249
Less: accumulated amortisation	–	(2,249)
Research and development costs	–	546,593
Less: accumulated amortisation	–	(142,084)
Formation expenses	–	5,104
Goodwill on acquisition of Freshtel Australia	–	10,970,823
Total intangibles	–	11,381,165
9. DEFERRED TAX ASSETS		
Future income tax benefit	–	220,890
Total deferred tax assets	–	220,890
10. PAYABLES		
Current		
Accounts payable other creditors	42,393	335,192
Unsecured loans	–	492,550
Total payables	42,393	827,742
11. INTEREST-BEARING LIABILITIES		
Current		
Loans—premium funding	–	4,940
Credit card liabilities	–	22,817
Hire purchase liability	–	4,162
Less: unexpired hire purchase liability	–	(963)
Total current interest-bearing liabilities	–	30,956
Non-current		
Hire purchase liability	–	9,862
Less: unexpired hire purchase liability	–	(1,062)
Total non-current interest-bearing liabilities	–	8,800
12. OTHER LIABILITIES		
Current		
Accrued charges	–	155,000
Income in advance	–	90,436
Total other liabilities	–	245,436
13. CONTRIBUTED EQUITY		
Ordinary shares fully paid	2,200,647	15,152,816
Total contributed equity	2,200,647	15,152,816

Independent Accountant's Report

a) Movements in ordinary shares are as follows:

Date	Details	No. of Notes	Issue Shares	Price	\$
30 November 2004	Balance at 30/11/04		17,748,500		2,200,647
Pro-forma transaction	Issue of shares for the acquisition of Freshtel Australia	14(a)	56,100,000	\$0.20	11,220,000
Pro-forma transaction	Issue pursuant to the Prospectus	14(b)	10,000,000	\$0.20	2,000,000
Pro-forma transaction	Capital raising costs	14(c)	–		(267,831)
Pro-forma 30 November 2004	Pro-forma closing balance		83,848,500		15,152,816

b) Movement in options are as follows

Date	Details	Notes	Number of Options
30 November 2004	Closing balance		4,500,000
Pro-forma transaction	Issue of options to brokers	14(d)	665,000
Pro-forma 30 November 2004	Pro-forma closing balance		5,165,000

The option terms and conditions are disclosed in Section 10.5.3 of the Prospectus.

14. ASSUMPTIONS USED IN PREPARING THE PRO-FORMA STATEMENT OF FINANCIAL POSITION

The Pro-Forma Statement of Financial Position of the Company as at 30 November 2004 has been prepared on the assumption that the following transactions had taken place at that date:

- The acquisition of 100% of Freshtel Australia via the issue of 56,100,000 Shares and 93,900,000 Performance Shares as approved by the Company's shareholders in a general meeting on 17 January 2005. The value assigned by the Directors to the acquisition of Freshtel Australia is based on the table below.

	No. Issued	Value per Security \$	Total Value \$
Shares	56,100,000	0.20	11,220,000

No value has been assigned to the 93,900,000 Performance Shares as the conversion of the Performance Shares to ordinary Shares depends on Freshtel Australia achieving various milestones that cannot be reliably measured. The Performance Shares have been disclosed as a contingent event in Note 17 of this Report.

The Company is acquiring 100% of the issued capital of Freshtel Australia. The Directors' fair value of 100% of the net assets of Freshtel Australia as at 30 November 2004 was \$249,177, resulting in goodwill on the acquisition of Freshtel Australia of \$10,970,823.

Independent Accountant's Report

- b. The issue of 10,000,000 shares at \$0.20 each to raise \$2,000,000 assuming no oversubscriptions;
- c. The settlement of capital raising costs incurred by the Company of \$336,010 in relation to the Prospectus comprising:

	\$
ASIC fees	2,010
ASX fees	34,000
Advisers' fees	260,000
Printing	10,000
Miscellaneous	30,000
Total	336,010

As at 30 November 2004, the Company had already incurred \$68,179 of capital raising costs, resulting in a cash payment of \$267,831 for capital raising costs. These costs are recognised directly in equity as a reduction of the share proceeds received in accordance with UIG 23 'Transaction costs arising on the issue of equity instruments'.

- d. The issue of 665,000 free options to brokers as detailed in the Company's prospectus dated 27 October 2004. The options to be issued by the Company have not been brought to account as an expense. The option terms and conditions are disclosed in Section 10.5.3 of the Prospectus.

15. RECONCILIATION OF CASH

	Notes	Reviewed Pro-Forma 30 Nov 2004 \$
Opening cash balance	2	2,211,350
Pro-forma cash transactions		
Cash acquired from the acquisition of Freshtel Australia		11,546
Funds raised from issue of 10,000,000 shares	14(b)	2,000,000
Capital raising costs	14(c)	(267,831)
Closing cash balance		3,955,065

16. RELATED PARTY TRANSACTIONS

Transactions with Related Parties and Directors' Interests are disclosed in Sections 10.1–10.2 of the Prospectus.

17. CONTINGENT EVENT

The Company has issued to Freshtel Australia shareholders 93,900,000 Performance Shares, which will convert to 93,900,000 Shares should Freshtel Australia meet certain milestones as detailed in Section 10.5.2 of the Prospectus. Should Freshtel Australia achieve the milestones, it will result in an additional 93,900,000 Shares being issued at 20 cents per share, which will therefore increase both goodwill and share capital by \$18,780,000.

18. SUBSEQUENT EVENTS

Subsequent to 30 November 2004 to the date of this report, there has not arisen any event of a material nature likely, in the opinion of the Directors, to affect significantly the operations of the Company or its state of affairs in future years.

19. MATERIAL CONTRACTS

Material contracts are disclosed in Section 9 of the Prospectus.

20. INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

The potential implications for the Company on the introduction of IFRS have been disclosed in Section 7.12 of the Prospectus.

9

Summary of Material Contracts

9.1 SHARE SALE AGREEMENT

On 3 December 2004, the Company, Freshtel Australia and the shareholders in Freshtel Australia entered into a share sale agreement (Share Sale Agreement) pursuant to which the Company agreed to acquire all of the issued shares in Freshtel Australia.

The consideration to be paid by the Company for the acquisition will be satisfied through the allotment and issue of 56,100,000 Shares and 93,900,000 Performance Shares to the Freshtel Australia shareholders. Completion of the transactions contemplated by the Share Sale Agreement is subject to and conditional on:

- (a) the Company obtaining all necessary regulatory and Shareholder approvals required to complete the transactions contemplated by the Share Sale Agreement (including, without limitation, the Company obtaining the necessary spread of Shareholders required under condition 7 of ASX Listing Rule 1);
- (b) the Company and the Freshtel Australia shareholders being reasonably satisfied that after settlement, the Company will be able to meet the requirements of Chapters 1 and 2 of the ASX Listing Rules;
- (c) the Company preparing a prospectus to raise a minimum of \$2,000,000 net of costs pursuant to that prospectus through the issue of new shares at an issue price of \$0.20 each (**Capital Raising**), lodging the prospectus with the ASIC and completing the Capital Raising;
- (d) the Company obtaining Shareholder approval for the appointment of the following persons to the board of directors of the Company:
 - (i) Michael Carew as the new managing director/ chief executive officer;
 - (ii) Peter Warner as an executive director;
 - (iii) David Elbourn as a non-executive director; and
 - (iv) Sebastian Filzek as a non-executive director;
- (e) Michael Carew and Peter Warner (and/or their controlled entities) each entering into executive service agreements or consultancy agreements with the Company securing their services for a minimum term of three years;
- (f) the Company having complied in full with its obligations relating to maintaining the status quo of its business;
- (g) Freshtel Australia having complied in full with its obligations relating to maintaining the status quo of its business;
- (h) the Company entering into the reseller agreement and consultancy agreement (see Sections 9.2 and 9.7);
- (i) the adoption of an employee option plan by the Company (on terms to be agreed);
- (j) during the period commencing on the execution date of the Share Sale Agreement and expiring on the date that the last of the conditions set

in paragraphs (a) to (i) (inclusive) above is satisfied or waived (as the case may be), there not having been:

- (i) any event (or series of events) having or which is likely to have a material adverse effect on the financial position or business prospects of Freshtel Australia or its subsidiaries; or
 - (ii) any material default under the Share Sale Agreement by Freshtel Australia or the Freshtel Australia shareholders; or
 - (iii) any breach of the warranties by Freshtel Australia or the Freshtel Australia shareholders; and
- (k) during the period commencing on the execution date of the Share Sale Agreement and expiring on the date that the last of the conditions set in paragraphs (a) to (i) (inclusive) above is satisfied or waived (as the case may be), there not having been:
- (i) any event (or series of events) having or which is likely to have a material adverse effect on the financial position or business prospects of the Company; or
 - (ii) any material default under the Share Sale Agreement by the Company; or
 - (iii) any breach of the warranties by the Company.

The conditions set out in paragraphs (d), (e) and (h) above have all been satisfied at the date of this Prospectus.

At settlement, Freshtel Australia must confer on the Company title to the Freshtel Australia shares and place the Company in effective possession and control of Freshtel Australia.

In addition to the above, the Warrantors have provided the Company with a number of warranties and representations including without limitation as to the status, financial position, ownership of assets and ownership of intellectual property of Freshtel Australia. Further, each of the Warrantors has agreed to indemnify the Company against any claims arising with respect to a breach of any warranty given, subject to a maximum liability equal to the value of the consideration actually received by each Warrantor.

9.2 RESELLER AGREEMENT BETWEEN WHOLESALE COMMUNICATIONS GROUP AND FRESHTEL AUSTRALIA

On or about 27 January 2005, Wholesale Communications Group Pty Limited (**WCG**) (ACN 109 626 011) and Voicestream Networks Pty Limited (**Voicestream**) (a wholly owned subsidiary of Freshtel Australia) entered into a reseller agreement pursuant to which Voicestream appointed WCG as the exclusive reseller of Freshtel Australia VoIP products in Australia and New Zealand.

The agreement is for an initial period of three years. Voicestream only has the option to renew the term of the agreement for two further terms of three years

Summary of Material Contracts

by giving written notice to WCG not later than six months prior to the end of any three year term. Either party may terminate the agreement at the end of any three year term by giving six months notice in writing to the other party.

The arrangement between the parties is exclusive whereby WCG must not enter into competing arrangements with third parties by selling any other VoIP products or services that are similar to or competitive with the Freshtel Australia VoIP Products. WCG must:

- (a) market and resell Freshtel Australia VoIP products to the wholesale market, being Internet services providers and voice/data services providers, but not to end users or retailers;
- (b) market and sell all commercially realistic products offered to it by Voicestream, including any upgrades or modifications of those products and then enter into a service level agreement with Voicestream;
- (c) if WCG is selling or marketing a product or service that becomes competitive with a Voicestream product as a direct consequence of Voicestream entering into new markets or developing new products, market and offer for sale commercially realistic Voicestream products before and in preference to the products and services of any other party;
- (d) act reasonably in assessing whether a product is commercially realistic, and where it is assessed as not commercially realistic, notify Voicestream in writing as soon as practicable after the assessment has been made, but in any case, within 30 business days of receipt of the product;
- (e) market and offer for sale Voicestream hardware products to service providers before and in preference to the hardware products of any other party; and
- (f) on or before the 7th day of each quarter, provide a written report outlining projected sales for that quarter.

Voicestream must:

- (a) modify, change or improve products and make them available to WCG and incorporate into the Voicestream products, the benefits resulting from such product modifications. This obligation does not apply to wholesalers who are agents or resellers of Voicestream (or any of its related entities) branded products;
- (b) not sell its Freshtel Australia VoIP products to wholesalers;
- (c) where it sells a non-Voicestream branded product to a retailer for the retailer to market under the retailer's brand (White Label Solution), offer to the retailer any supporting network services provided by WCG;
- (d) not (and must ensure that its related entities do not) knowingly sell hardware to WCG customers unless otherwise agreed in writing with WCG; and
- (e) not itself, or allow any person to, market Firefly as a retail brand.

WCG can only use the trademarks, logos and brand names of Voicestream in accordance with Voicestream's written policies or instructions.

Either party may terminate on the occurrence of the following:

- (a) the other party breaches and does not remedy the breach;
- (b) the other party becomes subject to any form of insolvency;
- (c) the other party ceases or threatens to cease conducting business in the normal manner; or
- (d) the other party enters into or proposes to enter into a scheme, composition or arrangement with any of that party's creditors.

Sebastian Filzek, a director of the Company, is also a director and (indirectly) a shareholder of WCG.

9.3 EMPLOYMENT AGREEMENT WITH MICHAEL CAREW

With effect from 6 December 2004, Freshtel Australia Pty Ltd entered into an employment agreement with Mr Michael Carew. Under the terms of this agreement, Mr Carew has been appointed to the role of Chief Executive Officer. His remuneration is \$180,000 per annum plus superannuation. Additional cash compensation of \$200 per day is payable for any related overseas business travel.

Mr Carew is also entitled to an annual performance bonus equivalent to 1.5% of the net profit of Freshtel Holdings Limited (up to a maximum of \$60,000 per annum).

As an employee he is also entitled to participate in the Employee Share Option Plan.

The employment contract is subject to termination by either party on three months' notice, and restraint of trade provisions apply post termination.

9.4 EMPLOYMENT AGREEMENT WITH PETER WARNER

With effect from 6 December 2004, Freshtel Australia entered into an employment agreement with Mr Peter Warner. Under the terms of this agreement, Mr Warner has been appointed to the role of Commercial Director. His remuneration is \$120,000 per annum plus superannuation. Additional cash compensation of \$200 per day is payable for any related overseas business travel.

Mr Warner is also entitled to an annual performance bonus equivalent to 1.5% of the net profit of Freshtel Holdings Limited (up to a maximum of \$60,000 per annum).

As an employee he is also entitled to participate in the Employee Share Option Plan.

The employment contract is subject to termination by either party on three months' notice, and restraint of trade provisions apply post termination.

Summary of Material Contracts

9.5 JOINT VENTURE AGREEMENT

On or about 10 September 2002, Freshtel Australia and Freshwater Technology Investments Pty Limited (FTI) as trustee of the Freshwater Technology Investments Unit Trust (FTIUT) entered into a joint venture agreement pursuant to which FTI agreed to provide Freshtel Australia with capital of not less than \$200,000 for the development of an IP phone. In return for the capital investment, FTIUT is to receive a share of the revenue from the sale by Freshtel Australia of the IP phone.

FTI has provided \$312,500 to Freshtel Australia and in return for this investment, Freshtel Australia has agreed to pay FTIUT US\$1.00 per IP phone sold worldwide. After FTIUT has received a total amount of not less than US\$1,500,000, Freshtel Australia may elect to pay an amount equal to the capital investment (i.e. AUD\$312,500) to buy out FTIUT's future rights to receive any further payments for IP phone sales. All ownership and proprietary rights (including any intellectual property rights) in the IP phone remain with Freshtel Australia.

The joint venture agreement terminates at the expiration of seven years from the date of the agreement.

9.6 LOAN AGREEMENT AND CHARGE

On 3 December 2004, the Company and Freshtel Australia entered into a loan agreement pursuant to which the Company agreed to advance \$1,275,000 to Freshtel Australia.

The material terms of the agreement are as follows:

- (a) interest on advances is payable annually in arrears at the rate of 8% per annum;
- (b) any advances must be repaid within 12 months (if the Company is not admitted to the official list of ASX by 30 April 2005) or within five years (if the Company is admitted to the official list of ASX by 30 April 2005); and
- (c) all advances made under the agreement are secured by a fixed and floating charge over the assets and undertakings of Freshtel Australia.

Both the loan agreement and charge are otherwise on ordinary commercial terms.

9.7 CONSULTANCY AGREEMENT BETWEEN FRESHTEL R&D, TERAGEN INTERNATIONAL AND GLUAFF INVESTMENTS

On 4 January 2005, Freshtel R&D Pty Limited (formerly Virbiage Pty Limited) (Freshtel R&D) (a wholly owned subsidiary of Freshtel Australia) entered into a consultancy agreement with Teragen International Pty Limited (Teragen) and Gluaff Investments Pty Limited (Gluaff) (Consultancy Agreement).

Teragen and Gluaff are both wholly owned by Sebastian Filzek, a director and shareholder of Freshtel Australia. Gluaff is the company through which Mr Filzek holds his shares in Freshtel Australia. Teragen is a research and development services company.

Freshtel R&D is a VoIP telephony provider and has engaged Teragen, a consultancy company, to provide research and development services in relation to the VoIP market. The agreement sets out terms under which Freshtel R&D engages Teragen to carry out research and development services.

The agreement is for a period of three years.

Freshtel R&D engages Teragen on a project-by-project basis under a specific work request. Services must be provided by approved employees. Each work request specifies a description of the services provided, a timetable by which services are to be provided and an estimate of the cost of having the services provided.

During the term of the agreement, Teragen must provide training to up to three Freshtel R&D employees such that by the end of the term, they are able to provide the services to the same standard as Teragen employees. If Teragen terminates the agreement prior to the end of the three year term, Teragen must complete any outstanding work request and, as soon as reasonably practicable after the termination date, fully train three Freshtel R&D employees to the required standard.

Freshtel R&D can terminate for failure to perform the services, insolvency of Teragen, change of control of Teragen, or if the actions of Teragen cause a material adverse effect on Freshtel R&D's business. Either party can terminate the agreement for unremedied breach.

In addition to its other remedies on termination, if Freshtel R&D terminates the agreement (other than as a result of a change in control of Teragen), Freshtel R&D may issue a divestment notice to Gluaff. The divestment notice may require Gluaff to transfer all shares it holds in Freshtel Australia (or any successor of the company) to a person nominated by Freshtel R&D, or enter into a buyback agreement in respect of those shares.

In consideration for the services provided under the Consultancy Agreement, Teragen is currently paid about \$85,000 per month. This is anticipated to increase to approximately \$120,000 per month as demand for Teragen's services increases.

Teragen adopts an 'agile development' approach to its R&D project work. This approach gives Freshtel greater flexibility in relation to its R&D requirements. Agile development allows Freshtel to reassess its requirements on a periodic basis throughout the life of an R&D project in light of the outcomes achieved by Teragen as the project progresses. This also allows Freshtel to adapt its R&D pipeline to changing market conditions. Because of the fluid nature of this method of development, the cost associated with agile development projects is difficult to forecast accurately.

The following table sets out a list of current projects being undertaken by Teragen for Freshtel. The table includes an estimated timetable and cost to completion based on current project parameters. Cost is based on an average daily rate of \$750 per person-day. The Company estimates typical commercial rates from other service providers for the type of work being undertaken by Teragen to be at least \$1500 per day.

Summary of Material Contracts

Project description	Estimated labour (person-days)	Estimated cost (\$)	Commencement date
DEVELOP ATA	292	219,000	June 2004
A hardware product that connects a consumer's analogue phone to the Internet to enable VoIP services. Currently, all Firefly users access the VoiceStream Network via the Firefly softphone, which requires a computer with microphone and speakers. The ATA will enable Freshtel users to use their current analogue phone to make VoIP and CTS calls. The ATA will need to have comparable talk quality with configurable mechanisms.			
DESIGN WEB SITE	245	183,750	September 2004
Freshtel requires a new public 'telco' site to promote its products and services. The site will need to enhance the promotion of Freshtel products and VoIP services, sign-up processes of new customers and maintenance of user information.			
DEVELOP FIREFLY 2	620	465,000	November 2004
Firefly is the ongoing development of communication concepts and features in Freshtel's VoIP softphone application. Firefly 1 has a respectable feature set and service quality in comparison to its market competitors. Freshtel intends to rebuild the softphone to enhance its competitive advantage, since the current softphone prevents implementation of future functionality.			
ENHANCE VOICESTREAM NETWORK	220	165,000	September 2004
Freshtel runs a VoIP network for customers, allowing Firefly customers to interact with and terminate calls to the PSTN. Development of the network should enhance redundancy and prevent failures, ensuring carrier grade service. Customers will have PSTN numbers, enabling Freshtel to deliver a complete phone line solution (inbound and outbound). The platform needs to have a provisioning interface, which will provision numbers based on their address. With its global expansion, Freshtel will need to operate and adhere to other country's telecommunication regulations.			
DEVELOP LAN PHONE	218	163,500	September 2004
The FT201 is a fully featured phone with the benefits of VoIP technology. This stand-alone phone needs to operate without the aid of a computer. Freshtel wants to target business customers and hence requires the phone to have business functionality.			
DEVELOP VOICEDOT	132	99,000	January 2005
Voicedot is a turnkey VoIP platform allowing companies to provide a range of telecommunications services. Voicedot is targeted at larger companies that require a much more involved setup and integration process, which will entail full customisation.			
DEVELOP VOICEDOT LITE	194	145,500	January 2005
Voicedot Lite is targeted at smaller companies requiring lower VoIP entry costs, which will entail little customisation. This project will require more development as it involves building one system to cater for all users, with minimal setup and maintenance time and costs.			
RESEARCH LICENSED CARRIER STATUS	30	22,500	February 2005
Investigate the benefits and obligations of becoming a licensed Australian carrier. Freshtel's PSTN providers are currently restricting functionality because Freshtel is not a licensed carrier. Becoming a carrier will enable Freshtel to deliver more features to its customers.			
DEVELOP OUTSOURCED PBX	384	288,000	February 2005
A system to minimise costs for SMEs to implement and maintain their own PBX.			



Additional Information

10.1 DISCLOSURE OF INTERESTS

Directors are not required under the Company's Constitution to hold any Shares. As at the date of this Prospectus, the Directors have relevant interests in securities in the Company as follows:

Director	No. of Shares
Mr Les Taylor	Nil
Mr Michael Carew	200,000
Mr Peter Warner	Nil
Mr Sebastian Filzek	200,000
Mr David Elbourn	250,000

Upon completion of the acquisition of Freshtel Australia, the Directors will have relevant interests in Shares and Performance Shares in the Company as follows:

Director	No. of Shares	No. of Performance Shares
Mr Les Taylor	Nil	Nil
Mr Michael Carew	21,340,959	35,385,668
Mr Peter Warner	350,587	586,812
Mr Sebastian Filzek	10,297,979	16,901,965
Mr David Elbourn	7,156,046	11,559,318

10.2 REMUNERATION

The Company's Constitution provides that the remuneration of non-executive Directors will be not more than the aggregate fixed sum determined by Shareholders in general meetings. The aggregate remuneration has been set at an amount of \$200,000 per annum.

Fees paid to executive Directors (Mr Michael Carew and Mr Peter Warner) are separate from the fees paid to non-executive Directors.

10.3 FEES AND BENEFITS

Other than as set out below or elsewhere in this Prospectus, no:

- Director or proposed Director of the Company;
- person named in this Prospectus as performing a function in a professional advisory or other capacity in connection with the preparation or distribution of this Prospectus;
- promoter of the Company; or
- underwriter,

has, or had within two years before lodgement of this Prospectus with ASIC, any interest in:

- the formation or promotion of the Company;
- any property acquired or proposed to be acquired by the Company in connection with its formation or promotion or in connection with the offer of securities under this Prospectus; or
- the offer of securities under this Prospectus,

and no amounts have been paid or agreed to be paid and no benefits have been given or agreed to be given to any of those persons as an inducement to become, or to qualify as, a director of the Company or for services rendered in connection with the formation or promotion of the Company or the offer of securities under this Prospectus.

Steinepreis Paganin has acted as the solicitors to the Company in relation to the Offer and has been involved in due diligence enquiries on legal matters involving the Company. The Company estimates it will pay Steinepreis Paganin approximately \$35,000 for these services. Subsequently, fees will be charged in accordance with normal charge-out rates. During the 24 months preceding lodgement of this Prospectus with ASIC, Steinepreis Paganin has received fees of approximately \$20,000 for other legal services provided to the Company.

Nova Legal & Advisory Pty Ltd has acted as the solicitors to Freshtel Australia to the transaction and has been involved in due diligence enquiries on legal matters involved Freshtel Australia. Freshtel Australia estimates it will pay Nova Legal & Advisory Pty Ltd approximately \$120,000 for these services. Subsequently, fees will be charged in accordance with normal charge-out rates. During the 24 months preceding lodgement of this Prospectus with ASIC, Nova Legal & Advisory Pty Ltd has not received any other fees.

Walker Herceg has acted as the solicitors to Freshtel Australia in relation to the Offer. Freshtel Australia estimates it will pay Walker Herceg approximately \$90,000 for these services. Subsequently, fees will be charged in accordance with normal charge-out rates. During the 24 months preceding lodgement of this Prospectus with ASIC, Walker Herceg has not received any other fees.

PKF Corporate Advisory Services (WA) Pty Ltd has acted as the independent accountant in relation to the Offer and has prepared the Independent Accountant's Report set out in Section 8 of this Prospectus.

Additional Information

The Company estimates it will pay PKF Corporate Advisory Services (WA) Pty Ltd approximately \$15,000 for these services. During the 24 months preceding lodgement of this Prospectus with ASIC, PKF Corporate Advisory Services (WA) Pty Ltd has received fees of \$16,712 for other services provided to the Company.

10.4 CONSENTS

Each of the parties referred to in this section:

- (a) does not make, or purport to make, any statement in this Prospectus other than those referred to in this section; and
- (b) to the maximum extent permitted by law, expressly disclaims and takes no responsibility for any part of this Prospectus other than a reference to its name and a statement included in this Prospectus with the consent of that party as specified in this section.

Steinepreis Paganin has given its written consent to being named as the solicitors to the Company in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

Nova Legal & Advisory Pty Ltd has given its written consent to being named as the solicitors to Freshtel Australia in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

Walker Herceg has given its written consent to being named as the solicitors to Freshtel Australia in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

Buchan Consulting Pty Ltd has given its written consent to being named as the corporate enquiries contact for the Company in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

Computershare Investor Services Pty Ltd has given its written consent to being named as the share registry for the Company in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

WHK Greenwoods Pty Ltd has given its written consent to being named as the auditor for the Company in this Prospectus and has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

PKF Corporate Advisory Services (WA) Pty Ltd has given its written consent to being named as the Independent Accountant in this Prospectus and to

the inclusion of the Independent Accountant's Report set out in Section 8 of this Prospectus. PKF Corporate Advisory Services (WA) Pty Ltd has not withdrawn its consent prior to the lodgement of this Prospectus with ASIC.

Paul Budde Communications Pty Ltd has given its written consent to all statements by it or said to be based on statements by it in the form and context in which they are included, and has not withdrawn this consent prior to lodgement of this Prospectus with ASIC. These statements are in Sections 2 and 5.3.

10.5 RIGHTS ATTACHING TO SECURITIES

10.5.1 ORDINARY SHARES

The following are the more important rights, privileges and liabilities attaching to the Shares offered for subscription by this Prospectus:

- (a) subject to any special rights or restrictions for the time being attached to any class or classes of Shares in the Company (at present there are none), at a general meeting every Shareholder present in person or by proxy, representative or attorney will have a vote on a show of hands and, on a poll, one vote for each Share held;
- (b) each Shareholder will be entitled to receive notice of, and to attend and vote at, general meetings of the Company and to receive all notices, accounts and other documents required to be furnished to Shareholders under the Constitution or the Corporations Act;
- (c) subject to any special rights of the holders of any Shares as to a dividend (at present there are none), any dividend declared shall be payable on all Shares in proportion to the number of Shares held by the Shareholders irrespective of the amount paid up or credited as paid up in respect of such Shares;
- (d) subject to the rights of holders of Shares with special rights in a winding up (at present there are none), on a winding-up of the Company all monies and property that are to be legally distributed among holders of Shares will be distributed so that, to the greatest extent possible, the amount distributed is in proportion to the Shares held by Shareholders respectively, irrespective of the amounts paid up or credited as paid up in respect of the Shares. At the commencement of the winding-up, Shares classified by ASX as restricted shares shall rank on a return of capital after all other Shares; and
- (e) subject to the Constitution and the Corporations Act, Shares are freely transferable.

Additional Information

10.5.2 PERFORMANCE SHARES

Under the terms of the Share Sale Agreement, the Company has agreed to issue the shareholders in Freshtel Australia 56,100,000 Shares, 33,900,000 Class A Performance Shares, 30,000,000 Class B Performance Shares and 30,000,000 Class C Performance Shares. The material terms and conditions of the Performance Shares are set out below.

Class A Performance Shares

1. Rights Attaching to the Class A Performance Shares

- 1.1 **(Shares)** Each Class A Performance Share is a share in the capital of the Company.
- 1.2 **(General Meetings)** The Class A Performance Shares shall confer on the holder (**Holder**) the right to receive notices of general meetings and financial reports and accounts of the Company that are circulated to shareholders. Holders have the right to attend general meetings of shareholders of the Company.
- 1.3 **(No Voting Rights)** The Class A Performance Shares do not entitle the Holder to vote on any resolutions proposed at a general meeting of shareholders of the Company.
- 1.4 **(No Dividend Rights)** The Class A Performance Shares do not entitle the Holder to any dividends.
- 1.5 **(No Rights on Winding Up)** The Class A Performance Shares do not confer on the Holder any right to participate in the surplus profits or assets of the Company upon winding up of the Company.
- 1.6 **(Not Transferable)** The Class A Performance Shares are not transferable.
- 1.7 **(Reorganisation of Capital)** If at any time the issued capital of the Company is reconstructed, all rights of a Holder will be changed to the extent necessary to comply with the applicable ASX Listing Rules at the time of reorganisation.
- 1.8 **(Application to ASX)** The Class A Performance Shares will not be quoted on ASX. However, upon conversion of the Class A Performance Shares, the Company must within seven (7) days after the conversion, apply for the official quotation of the shares arising from the conversion on ASX.
- 1.9 **(No other Rights)** The Class A Performance Shares give the Holders no rights other than those expressly provided by these terms and those provided at law where such rights at law cannot be excluded by these terms.

2. Conversion of the Class A Performance Shares

- 2.1 **(Conversion on Achievement of Milestone)** Following the issue of the Class A Performance Shares, if the Company and its subsidiaries, on a consolidated basis, achieve a net profit available to entity shareholders of at least \$6,000,000 (as determined by the Company's auditors) in any calendar or financial year (**Milestone**), each Class A Performance Share will automatically convert into one (1) fully paid ordinary share in the capital of the Company (**Share**).
- 2.2 **(Lapse if Milestone is not Achieved)** If the Milestone is not achieved by the date the Company announces to ASX its audited financial results for the year ending 31 December 2007 (**End Date**), every 100,000 Class A Performance Shares will convert into one (1) Share (rounded up to the nearest whole number).
- 2.3 **(Conversion Procedure)** Upon the Milestone being achieved or the End Date occurring (whichever occurs first), the Class A Performance Shares will automatically convert into Shares in accordance with term 2.1 or 2.2 (as the case may be) and the Company will issue each Holder with a new holding statement for the Shares.
- 2.4 **(Ranking of Shares)** The Shares into which the Class A Performance Shares will convert will rank pari passu in all respects with existing Shares.

Additional Information

Class B Performance Shares

1. Rights Attaching to the Class B Performance Shares

- 1.1 **(Shares)** Each Class B Performance Share is a share in the capital of the Company.
- 1.2 **(General Meetings)** The Class B Performance Shares shall confer on the holder (Holder) the right to receive notices of general meetings and financial reports and accounts of the Company that are circulated to shareholders. Holders have the right to attend general meetings of shareholders of the Company.
- 1.3 **(No Voting Rights)** The Class B Performance Shares do not entitle the Holder to vote on any resolutions proposed at a general meeting of shareholders of the Company.
- 1.4 **(No Dividend Rights)** The Class B Performance Shares do not entitle the Holder to any dividends.
- 1.5 **(No Rights on Winding Up)** The Class B Performance Shares do not confer on the Holder any right to participate in the surplus profits or assets of the Company upon winding up of the Company.
- 1.6 **(Not Transferable)** The Class B Performance Shares are not transferable.
- 1.7 **(Reorganisation of Capital)** If at any time the issued capital of the Company is reconstructed, all rights of a Holder will be changed to the extent necessary to comply with the applicable ASX Listing Rules at the time of reorganisation.
- 1.8 **(Application to ASX)** The Class B Performance Shares will not be quoted on ASX. However, upon conversion of the Class B Performance Shares, the Company must within seven (7) days after the conversion, apply for the official quotation of the shares arising from the conversion on ASX.
- 1.9 **(No other Rights)** The Class B Performance Shares give the Holders no rights other than those expressly provided by these terms and those provided at law where such rights at law cannot be excluded by these terms.

2. Conversion of the Class B Performance Shares

- 2.1 **(Conversion on Achievement of Milestone)** Following the issue of the Class B Performance Shares, notwithstanding the earlier conversion of any Class A Performance Shares, if the Company and its subsidiaries, on a consolidated basis, achieve a net profit available to entity shareholders of at least \$8,000,000 (as determined by the Company's auditors) in any calendar or financial year (**Milestone**), each Class B Performance Share will automatically convert into one (1) fully paid ordinary share in the capital of the Company (**Share**).
- 2.2 **(Lapse if Milestone is not Achieved)** If the Milestone is not achieved by the date the Company announces to ASX its audited financial results for the year ending 31 December 2007 (**End Date**), every 100,000 Class B Performance Shares will convert into one (1) Share (rounded up to the nearest whole number).
- 2.3 **(Conversion Procedure)** Upon the Milestone being achieved or the End Date occurring (whichever occurs first), the Class B Performance Shares will automatically convert into Shares in accordance with term 2.1 or 2.2 (as the case may be) and the Company will issue each Holder with a new holding statement for the Shares.
- 2.4 **(Ranking of Shares)** The Shares into which the Class B Performance Shares will convert will rank *pari passu* in all respects with existing Shares.

Additional Information

Class C Performance Shares

1. Rights Attaching to the Class C Performance Shares

- 1.1 **(Shares)** Each Class C Performance Share is a share in the capital of the Company.
- 1.2 **(General Meetings)** The Class C Performance Shares shall confer on the holder (**Holder**) the right to receive notices of general meetings and financial reports and accounts of the Company that are circulated to shareholders. Holders have the right to attend general meetings of shareholders of the Company.
- 1.3 **(No Voting Rights)** The Class C Performance Shares do not entitle the Holder to vote on any resolutions proposed at a general meeting of shareholders of the Company.
- 1.4 **(No Dividend Rights)** The Class C Performance Shares do not entitle the Holder to any dividends.
- 1.5 **(No Rights on Winding Up)** The Class C Performance Shares do not confer on the Holder any right to participate in the surplus profits or assets of the Company upon winding up of the Company.
- 1.6 **(Not Transferable)** The Class C Performance Shares are not transferable.
- 1.7 **(Reorganisation of Capital)** If at any time the issued capital of the Company is reconstructed, all rights of a Holder will be changed to the extent necessary to comply with the applicable ASX Listing Rules at the time of reorganisation.
- 1.8 **(Application to ASX)** The Class C Performance Shares will not be quoted on ASX. However, upon conversion of the Class C Performance Shares, the Company must within seven (7) days after the conversion, apply for the official quotation of the shares arising from the conversion on ASX.
- 1.9 **(No other Rights)** The Class C Performance Shares give the Holders no rights other than those expressly provided by these terms and those provided at law where such rights at law cannot be excluded by these terms.

2. Conversion of the Class C Performance Shares

- 2.1 **(Conversion on Achievement of Milestone)** Following the issue of the Class C Performance Shares, notwithstanding the earlier conversion of any Class A Performance Shares or Class B Performance Shares, if the Company and its subsidiaries, on a consolidated basis, achieve a net profit available to entity shareholders of at least \$10,000,000 (as determined by the Company's auditors) in any calendar or financial year (**Milestone**), each Class C Performance Share will automatically convert into one (1) fully paid ordinary share in the capital of the Company (**Share**).
- 2.2 **(Lapse if Milestone is not Achieved)** If the Milestone is not achieved by the date the Company announces to ASX its audited financial results for the year ending 31 December 2007 (**End Date**), every 100,000 Class C Performance Shares will convert into one (1) Share (rounded up to the nearest whole number).
- 2.3 **(Conversion Procedure)** Upon the Milestone being achieved or the End Date occurring (whichever occurs first), the Class C Performance Shares will automatically convert into Shares in accordance with term 2.1 or 2.2 (as the case may be) and the Company will issue each Holder with a new holding statement for the Shares.
- 2.4 **(Ranking of Shares)** The Shares into which the Class C Performance Shares will convert will rank pari passu in all respects with existing Shares.

Additional Information

10.5.3 OPTIONS

The material terms and conditions of the Options are as follows:

- (a) each Option entitles the holder to one (1) Share in the Company;
- (b) the Options are exercisable at any time on or prior to 5.00pm (Western Standard Time) on 31 December 2007 by completing an Option exercise form and delivering it together with the payment for the number of Shares in respect of which the Options are exercised to the registered office of the Company;
- (c) the Option exercise price is \$0.20 per Option;
- (d) an Option does not confer the right to a change in exercise price or a change in the number of underlying securities over which the Option can be exercised;
- (e) subject to the Corporations Act and the Company's Constitution, the Options are freely transferable;
- (f) all Shares issued upon exercise of the Options will rank *pari passu* in all respects with the Company's then issued Shares;
- (g) there are no participating rights or entitlements inherent in the Options and holders will not be entitled to participate in new issues of capital offered to Shareholders during the currency of the Options. However, the Company will ensure that for the purposes of determining entitlements to any such issue, the record date will be at least seven (7) Business Days after the issue is announced. This will give Option holders the opportunity to exercise their Options prior to the date for determining entitlements to participate in any such issue; and
- (h) if at any time the issued capital of the Company is reconstructed, all rights of an Option holder are to be changed in a manner consistent with the Corporations Act and the Listing Rules.

10.6 CORPORATE GOVERNANCE

The Directors monitor the business affairs of the Company on behalf of Shareholders and intend to formally adopt a corporate governance policy designed to encourage Directors to focus their attention on accountability, risk management and ethical conduct.

10.7 EXPENSES OF THE OFFER

The total expenses of the Offer are estimated to be approximately \$336,010 and are expected to be applied towards the items set out in the table below:

Item of Expenditure	Amount (\$)
ASIC fees	\$2,010
ASX fees	\$34,000
Advisers' fees	\$260,000
Printing	\$10,000
Miscellaneous	\$30,000
TOTAL	\$336,010

10.8 LITIGATION

As at the date of this Prospectus, the Company is not involved in any legal proceedings and the Directors are not aware of any legal proceedings pending or threatened against the Company.



11

Glossary

Where the following terms are used in this Prospectus they have the following meanings:

A\$ or \$ means an Australian dollar.

Acquisition means the acquisition by the Company of Freshtel Australia, as described in Section 9.1.

Application Form means the application form attached to or accompanying this Prospectus.

ASIC means the Australian Securities and Investments Commission.

ASTC means ASX Settlement and Transfer Corporation Pty Ltd.

Asterisk means an open source computer program that runs on Linux and provides a complete PBX in software.

ASX means Australian Stock Exchange Limited.

ATA means Analogue Telephone Adaptor, a device that allows a conventional analogue telephone to be used in a VoIP system.

Board means the board of Directors as constituted from time to time.

Budde Report means 'Global-Telecoms & IT—Overview and Statistics', 2005, produced by Paul Budde Communications Pty Limited.

Business Day means a week day when trading banks are ordinarily open for business in Perth, Western Australia.

CDR means Call Detail Record, a file containing information about recent VoIP calls such as the identities of sources and destinations, call duration and the amount billed for each call.

CHES means Clearing House Electronic Sub-register System, which is operated by ASTC, a wholly owned subsidiary of ASX.

Closing Date means the closing date for receipt of Application Forms under this Prospectus, being 5.00pm (WST) on 8 April 2005 (unless the Offer is extended or closed early).

Codec means a compression/decompression algorithm, which reduces the size of a data file.

Company means Freshtel Holdings Limited (ACN 111 460 121).

Constitution means the constitution of the Company.

Corporations Act means the Corporations Act 2001 (Cth).

CTS means Call Termination Service, which allows calls to be made from a VoIP telephone to a conventional telephone.

DHCP means Dynamic Host Configuration Protocol, a communications protocol that enables automated assignment of IP addresses in a computer network.

Directors means the directors of the Company at the date of this Prospectus.

Exposure Period means the period of seven (7) days after the date of lodgement of this Prospectus, which period may be extended by ASIC by not more than seven (7) days pursuant to Section 727(3) of the Corporations Act.

Freshtel Australia means Freshtel Australia Pty Ltd (ABN 14 094 928 248) and may include its wholly owned subsidiaries, as the context requires.

Freshtel Application Form means the application form attached to or accompanying this Prospectus and titled 'Freshtel Application Form'. **Freshtel R&D** means Freshtel R&D Pty Ltd (ABN 31 107 224 448) (formerly Virbiage Pty Ltd).

Holder means an owner of shares.

IAX or IAX2 mean the Inter-Asterisk eXchange protocols, which provide control and transmission of streaming media over IP networks.

IFRS means International Financial Reporting Standards.

IP means Internet Protocol, the method or protocol by which data is sent from one computer to another on the Internet.

ISDN means Integrated Services Digital Network, an international standard for sending voice and data over a telephone line.

ISP means Internet Service Provider.

LAN means Local Area Network, a group of computers and associated devices sharing a common communications line or wireless link and typically sharing the resources of a single processor or server within a small geographic area.

LCD means Liquid Crystal Display, a technology used for displays in many electronic devices.

Listing Rules means the official Listing Rules of ASX.

NAT means Network Address Translation, the translation of an IP address used within one network to a different IP address known within another network.

NLS means Number Lookup Server.

Offer means the invitation to investors to apply for Shares pursuant to this Prospectus and, where the context requires, includes the offer of Shares and Performance Shares to the shareholders in Freshtel Australia.

Official List means the Official List of ASX.

Official Quotation means official quotation by ASX in accordance with the Listing Rules.

Option means an option to subscribe for a Share subject to the terms and conditions set out in Section 10.5.3 of this Prospectus.

PBX means Private Branch eXchange, a telephone system within an enterprise that switches calls between enterprise users on local lines while allowing all users to share one or more external telephone lines.

PC means Personal Computer.

PDF means Portable Document Format, a file format created using Adobe Acrobat or similar that has captured all the elements of a printed document as an electronic image that can be viewed, navigated, printed, or forwarded to someone else.

Performance Share means a share issued on the material terms and conditions set out in Section 10.5.2.

PoP means Point of Presence, an access point from one place to the rest of the Internet.

PRI means Primary Rate Interface, a method of delivery for ISDN services.

Prospectus means this prospectus.

Protocol means a special set of rules used to send and receive data across a communication network.

PSTN means Public Switched Telephone Network, the world's collection of interconnected voice-oriented public telephone networks.

R&D means Research and Development.

RADIUS means Remote Authentication Dial-In User Service, a client/server protocol and software that enables remote access servers to communicate with a central server to authenticate dial-in users and authorise their access to the requested system or service.

Share means a fully paid ordinary share in the capital of the Company.

Share Sale Agreement means the share sale agreement entered into between the Company, Freshtel Australia and each of the shareholders in Freshtel Australia, a summary of which is set out in Section 9.1 of this Prospectus.

Shareholder means a holder of Shares.

SIP means Session Initiation Protocol, an IETF standard protocol for initiating an interactive user session that involves multimedia elements.

SME means Small-to-Medium Enterprise, a legally independent company with no more than 500 employees.

SMS means Short Message Service, a service for sending short messages to mobile phones.

Softphone means software that can communicate voice information over a computer network, emulating the functions of a conventional telephone.

USB means Universal Serial Bus, a standardised plug-and-play interface between a computer and add-on devices.

Virbiage means Virbiage Pty Limited (ACN 112 682 774).

Voicestream Networks means Voicestream Networks Pty Ltd (ACN 111 334 108).

VoIP means Voice over Internet Protocol, a system for communicating voice information using the Internet Protocol.

Warrantor means each of:

- (a) MD&MA Pty Limited (as trustee of the Carew Family Trust);
- (b) Mantroz Pty Limited (as trustee for the Elbourn Family Trust); and
- (c) Gluaff Investments Pty Limited.

WiFi means a device conforming to the IEEE 802.11b standard for wireless networks.

WST means Western Standard Time, Perth, Western Australia.

XML means eXtensible Markup Language, a language used to create common information formats and share both the format and the data.

12

Directors' Authorisation



This Prospectus is issued by the Company and its issue has been authorised by a resolution of the Directors.

In accordance with Section 720 of the Corporations Act, each Director has consented in writing to the lodgement of this Prospectus with ASIC.

A handwritten signature in black ink, consisting of a stylized 'M' followed by a horizontal line that tapers to a point on the right.

Mr Michael Carew
Director

For and on behalf of Freshtel Holdings Limited.

FRESHTEL HOLDINGS LIMITED

ACN 111 460 121

Application Form

This Application Form is important. If you are in doubt as to how to deal with it, please contact your stockbroker or professional adviser without delay. You should read the entire prospectus carefully before completing this form. To meet the requirements of the Corporations Act, this Application Form must not be distributed unless included in, or accompanied by, the prospectus.

Registry Use Only

Broker Code

Adviser Code

A I/we apply for

Number of Shares in Freshtel Holdings Limited at A\$0.20 per Share or such lesser number of Shares which may be allocated to me/us

B I/we lodge full Application Money

A\$

C Individual/Joint applications - refer to naming standards overleaf for correct forms of registrable title(s)

Title or Company Name	Given Name(s)	Surname
<input type="text"/>	<input type="text"/>	<input type="text"/>

Joint Applicant 2 or Account Designation
<input type="text"/>

Joint Applicant 3 or Account Designation
<input type="text"/>

D Enter your postal address - Include State and Postcode

Unit	Street Number	Street Name or PO Box /Other Information
<input type="text"/>	<input type="text"/>	<input type="text"/>

City / Suburb / Town	State	Postcode
<input type="text"/>	<input type="text"/>	<input type="text"/>

E Enter your contact details

Contact Name
<input type="text"/>

Telephone Number - Business Hours / After Hours
(<input type="text"/>) <input type="text"/>

F CHESSE Participant

Holder Identification Number (HIN)
X <input type="text"/>

Please note that if you supply a CHESSE HIN but the name and address details on your form do not correspond exactly with the registration details held at CHESSE, your application will be deemed to be made without the CHESSE HIN, and any securities issued as a result of the IPO will be held on the Issuer Sponsored subregister.

Cheque details - Make your cheque or bank draft payable to Freshtel Holdings Limited

Drawer	Cheque Number	BSB Number	Account Number	Amount of cheque
<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	A\$ <input type="text"/>
Drawer	Cheque Number	BSB Number	Account Number	Amount of cheque
<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	A\$ <input type="text"/>

By submitting this Application Form, I/we declare that this application is completed and lodged according to the Prospectus and the declarations/statements on the reverse of this Application form and I/we declare that all details and statements made by me/us (including the declaration on the reverse of this Application Form) are complete and accurate. I/we agree to be bound by the Constitution of the Company.

See back of form for completion guidelines

I P O

How to complete this form

A Shares Applied for

Enter the number of Shares you wish to apply for. The application must be for a minimum of 10,000 Shares. Applications for greater than 10,000 Shares must be in multiples of 2,000 Shares.

B Application Monies

Enter the amount of Application Monies. To calculate the amount, multiply the number of Shares by the price per Share.

C Applicant Name(s)

Enter the full name you wish to appear on the statement of share holding. This must be either your own name or the name of a company. Up to 3 joint Applicants may register. You should refer to the table below for the correct forms of registrable title. Applications using the wrong form of names may be rejected. Clearing House Electronic Subregister System (CHES) participants should complete their name identically to that presently registered in the CHES system.

D Postal Address

Enter your postal address for all correspondence. All communications to you from the Registry will be mailed to the person(s) and address as shown. For joint Applicants, only one address can be entered.

E Contact Details

Enter your contact details. These are not compulsory but will assist us if we need to contact you.

F CHES

Freshtel Holdings Limited (the Company) will apply to the ASX to participate in CHES, operated by ASX Settlement and Transfer Corporation Pty Ltd, a wholly owned subsidiary of Australian Stock Exchange Limited. In CHES, the company will operate an electronic CHES Subregister of security holdings and an electronic Issuer Sponsored Subregister of security holdings. Together the two Subregisters will make up the Company's principal register of securities. The Company will not be issuing certificates to applicants in respect of Shares allotted. If you are a CHES participant (or are sponsored by a CHES participant) and you wish to hold Shares allotted to you under this Application on the CHES Subregister, enter your CHES HIN. Otherwise, leave this section blank and on allotment, you will be sponsored by the Company and allocated a Securityholder Reference Number (SRN).

G Payment

Make your cheque or bank draft payable to Freshtel Holdings Limited in Australian currency and cross it Not Negotiable. Your cheque or bank draft must be drawn on an Australian Bank.

Complete the cheque details in the boxes provided. The total amount must agree with the amount shown in box B.

Cheques will be processed on the day of receipt and as such, sufficient cleared funds must be held in your account as cheques returned unpaid may not be re-presented and may result in your Application being rejected. Pin (do not staple) your cheque(s) to the Application Form where indicated. Cash will not be accepted. Receipt for payment will not be forwarded.

Before completing the Application Form the applicant(s) should read this prospectus to which this application relates. By lodging the Application Form, the applicant agrees that this application for Shares in Freshtel Holdings Limited is upon and subject to the terms of the prospectus and the Constitution of Freshtel Holdings Limited, agrees to take any number of Shares that may be allotted to the Applicant(s) pursuant to the prospectus and declares that all details and statements made are complete and accurate. It is not necessary to sign the Application Form.

Lodgement of Application

Application Forms must be received at the Perth office of Computershare Investor Services Pty Limited by no later than 5pm WST on 8 April 2005. Return the Application Form with cheque(s) attached to:

Computershare Investor Services Pty Limited OR Computershare Investor Services Pty Limited
GPO Box D182 Level 2
PERTH WA 6840 45 St Georges Terrace
PERTH WA 6000

Privacy Statement

Personal information is collected on this form by Computershare Investor Services Pty Limited ("CIS"), as registrar for securities issuers ("the issuer"), for the purpose of maintaining registers of securityholders, facilitating distribution payments and other corporate actions and communications. Your personal information may be disclosed to our related bodies corporate, to external service companies such as print or mail service providers, or as otherwise required or permitted by law. If you would like details of your personal information held by CIS, or you would like to correct information that is inaccurate, incorrect or out of date, please contact CIS. In accordance with the Corporations Act 2001, you may be sent material (including marketing material) approved by the issuer in addition to general corporate communications. You may elect not to receive marketing material by contacting CIS. You can contact CIS using the details provided on the front of this form or E-mail privacy@computershare.com.au

If you have any enquiries concerning your application, please contact the Computershare Investor Services Pty Limited on 1300 557 010.

Correct forms of registrable title(s)

Note that ONLY legal entities are allowed to hold Shares. Applications must be made in the name(s) of natural persons, companies or other legal entities in accordance with the Corporations Act. At least one full given name and the surname is required for each natural person. The name of the beneficial owner or any other registrable name may be included by way of an account designation if completed exactly as described in the examples of correct forms of registrable title(s) below.

Type of Investor	Correct Form of Registration	Incorrect Form of Registration
Individual - Use given name(s) in full, not initials	Mr John Alfred Smith	J.A Smith
Joint - Use given name(s) in full, not initials	Mr John Alfred Smith & Mrs Janet Marie Smith	John Alfred & Janet Marie Smith
Company - Use company title, not abbreviations	ABC Pty Ltd	ABC P/L ABC Co
Trusts - Use trustee(s) personal name(s) - Do not use the name of the trust	Ms Penny Smith <Penny Smith Family A/C>	Penny Smith Family Trust
Deceased Estates - Use executor(s) personal name(s) - Do not use the name of the deceased	Mr Michael Smith <Est John Smith A/C>	Estate of Late John Smith
Minor (a person under the age of 18) - Use the name of a responsible adult with an appropriate designation	Mr John Alfred Smith <Peter Smith A/C>	Peter Smith
Partnerships - Use partners personal name(s) - Do not use the name of the partnership	Mr John Smith & Mr Michael Smith <John Smith & Son A/C>	John Smith & Son
Clubs/Unincorporated Bodies/Business Names - Use office bearer(s) personal name(s) - Do not use the name of the club etc	Mrs Janet Smith <ABC Tennis Association A/C>	ABC Tennis Association
Superannuation Funds - Use the name of trustee of the fund - Do not use the name of the fund	John Smith Pty Ltd <Super Fund A/C>	John Smith Pty Ltd Superannuation Fund

13

Directory

DIRECTORS

Mr Les Taylor (Chairman)
Mr Michael Carew (CEO)
Mr Peter Warner
Mr Sebastian Filzek
Mr David Elbourn (Secretary)

AUSTRALIAN COMPANY NUMBER

111 460 121

REGISTERED AND PRINCIPAL OFFICE

Suite 5, 651 Canterbury Road
SURREY HILLS VIC 3127
Telephone: (03) 9898 0377
Facsimile: (03) 9898 0499

CORPORATE ENQUIRIES

Rebecca Christie
Buchan Consulting Pty Ltd
Suite 1005, Level 10
37 Bligh Street
SYDNEY NSW 2000
Telephone: (02) 9237 2800
Mobile: 0417 382 391
rchristie@bcg.com.au

SHARE REGISTRY

Computershare Investor Services Pty Ltd
Level 2, 45 St Georges Terrace
PERTH WA 6000

INDEPENDENT ACCOUNTANT

PKF Corporate Advisory Services (WA) Pty Ltd
Level 7, BGC Centre
28 The Esplanade
PERTH WA 6000

SOLICITORS TO THE COMPANY

Steinepreis Paganin
Lawyers & Consultants
Level 4, Next Building
16 Milligan Street
PERTH WA 6000

SOLICITORS TO FRESHTEL AUSTRALIA PTY LTD

Nova Legal & Advisory Pty Ltd
Level 13, 60 Margaret Street
SYDNEY NSW 2000

Walker Herceg

Level 22, Australia Square
264 George Street
SYDNEY NSW 2000

AUDITOR

WHK Greenwoods Pty Ltd
Level 15, 309 Kent Street
SYDNEY NSW 2000

