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Klondike Source Limited

ABN 64 087 595 980

Annual Report 2004

KLONDIKE SOURCE LIMITED

ABN 64 087 595 980

DIRECTORS

Patrick J D Elliott (Chairman)

Colin M Thomas

Raymond J Soper

CEO

Robert G Adamson

SECRETARY

Robert J Waring

REGISTERED AND ADMINISTRATION OFFICE

Level 10, 80 Arthur Street, North Sydney, NSW 2060

Telephone: (02) 9957 3199

Facsimile: (02) 9954 4011

Email: info@klondikesource.com.au

Web: www.klondikesource.com.au

SHARE REGISTRY

Registries Limited

Level 2, 28 Margaret Street

SYDNEY NSW 2000

PO Box R67

Royal Exchange

SYDNEY NSW 1223

Telephone: (02) 9290 9600

Facsimile: (02) 9279 0664

AUDITORS

Barnes Dowell James

BANK

Westpac Banking Corporation

STOCK EXCHANGE LISTING AND NSX CODE

The Company's shares are quoted on the official list of the Stock Exchange of Newcastle Limited and trade under NSX code KSL.

SHARE CAPITAL

At 31 December 2004: 31,504,900 fully paid ordinary shares, 4,075,100 options issued to Founders, Directors, seed capital subscribers and consultants, and 1,300,000 Employee Incentive Plan options.

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CHAIRMAN'S LETTER

The Initial Public Offer (IPO) by Klondike Source Limited closed on 27 February 2004, having raised \$1.84 million. On 19 March 2004 the Company was admitted to the list of the Stock Exchange of Newcastle. Support for the IPO was Australia-wide with 166 new shareholders joining our patient founding and seed capital investors in the quest to discover the hard rock gold potential of the world famous Klondike Goldfield.

Our proposed diamond drill program got underway in early June; six holes were completed by September. We embarked on this program with high expectations as these were the first holes ever to be drilled in the headwaters of the creeks that produced (and continue to produce) significant quantities of placer gold. Although initial encouragement was provided by the alteration and other features visible in the core, the assays from the first four holes reported only slightly anomalous levels of gold. However, the last two holes intersected several intervals of low-grade gold mineralisation in association with arsenopyrite. We think this represents a weak mineralizing episode that is somewhat later than the principal gold event which is inferred to be the source of the alluvial gold.

Shareholders may recall that in the Prospectus, it was stated that three outcomes were possible. One; we could be lucky and encounter potentially economic gold mineralisation in our initial holes. Two; we would gain valuable geological information that might offer new understandings of the geology and point to styles of mineralisation different to our initial expectations. Or three; our work might endorse the long-held Canadian view that there is no gold left in the Klondike hinterland.

Our results are clearly in the second category. While Pogo-style mineralisation has been shown to be unlikely, we have on the other hand found evidence for more than one period of primary gold mineralisation. When considered with the past gold production of 13 million ounces (plus current production of ~50,000 annual ounces), this confirms that the Klondike goldfield does have considerable potential to host significant hard rock gold mineralisation.


While the Board believes this outcome provides encouragement for continuing exploration in the Klondike district, it considers that the Company would best utilise its current resources by offering other explorers the opportunity to farm in to the venture by funding the next stages of exploration.

Late in the year, the Company terminated the PacRim/KSL Consolidation Agreement as PacRim had failed to carry out its obligations. Accordingly, the proposed issue of 11.975 million shares did not proceed and the Company's share capital and board composition is unchanged, and we have reverted to the original joint venture in which KSL (after funding the 2004 program) has earned an interest of 56%.

In addition to farming out the Klondike project, the Company is seeking and considering proposals for interests in other high-quality exploration opportunities. Our objective is either to contribute technical know-how and exploration expenditure to generate drill targets of important economic potential, or to use our existing resources to participate in a suitable seed capital opportunity.

The Board of KSL is mindful of its major responsibilities not only to corporate governance as an Australian-listed company but also as an environmentally responsible gold exploration company in Canada's Yukon Territory.

We look forward to materially advancing the Company's goals in 2005.



P J D Elliott
Chairman

13 April 2005

DIRECTORS' REPORT

Your Directors present their report on the consolidated entity consisting of Klondike Source Limited and the entity it controlled at the end of, and during the year ended 31 December 2004.

Directors

The following persons were directors of Klondike Source Limited during the whole of the financial year and up to the date of this report:

Patrick J D Elliott (Chairman)

Colin M Thomas

Raymond J Soper

Robert G Adamson (alternate director for C M Thomas)

Directors' qualifications and experience

Patrick J D Elliott

Non-Executive Chairman

Pat Elliott has over 30 years experience in investment, financial and industrial management, having previously been employed by Consolidated Goldfields Australia Limited, Morgan Grenfell Australia Limited and Natcorp Investments Limited. He is currently a director of Argonaut Resources Ltd (Chairman), Magnesium International Limited (Deputy Chairman) and Australia Oriental Minerals NL (Chairman).

Colin M Thomas

Technical Director

Colin Thomas is a graduate of St Andrews University, Scotland. He joined the then international natural resources consulting group, Robertson Research group in 1970, after 10 years in regional mapping for Government Geological Surveys in Africa (Tanzania and Botswana). He has specialised in regional and district geological studies for precious and base metals, uranium and diamonds, having undertaken significant projects for (among others) Newmont Australia, CRA/RTZ, Freeport Australia, Mobil Minerals Australia, Hindustan Copper Ltd (Indian government corporation) and BP Minerals NZ. In addition, he has major experience in the assessment and valuation of mineral exploration properties for equity fund raising. He is a director of RobSearch Australia, a wholly Australian owned natural resources, safety and environmental risk management and project consultancy, which commenced business as the Australian coal/mineral resources consultancy arm of the Robertson Research group PLC in 1970.

Raymond J Soper

Non-executive Director

Ray Soper is a mining engineer and company director, with 33 years experience in the mining industry. He has worked with MIM Holdings, Renison Goldfields, McKinsey and Co, Peko-Wallsend Ltd, Lachlan Resources and Resource Finance Corporation in the fields of mining, mineral economics, mining finance, exploration, technology development and related activities. He is a director of Continental Minerals Corporation (TSX Venture), GTN Resources Ltd, Huntley Investment Company Limited, Paradigm Gold Limited and PlatSearch NL.

Robert G Adamson

Alternate Director for C M Thomas, Chief Executive Officer

Bob Adamson has over 35 years experience in exploration, initially with the CRA/RTZ group, followed by 14 years with the Newmont group. He was subsequently General Manager for BP Minerals NZ and then Managing Director of Cluff Pacific Resources and a Director of Cluff Zimbabwe (owner/operator of the largest gold mine in that country, the Freda Rebecca). Whilst with Newmont, he made major contributions to the discovery of the Telfer gold deposit in 1972. For the past ten years he has been an independent consultant and associated with RobSearch Australia. He is a director of Southern Cross Exploration NL.

DIRECTORS' REPORT

Directors' Remuneration

	Directors' Fees	Consulting Fees	Superannuation	Options	TOTAL
P J D Elliott	15,000	-	1,350	23,931	40,281
C M Thomas	-	48,000	-	15,705	63,705
R J Soper	5,000	6,501	450	15,705	27,656
	20,000	54,501	1,800	55,341	131,642

The value of options granted has been calculated using the Black & Scholes valuation methodology.

In addition, certain consulting fees were paid to companies related to the directors (refer to note 23).

Executive Officer's Remuneration

	Consulting Fees	Options	TOTAL
R G Adamson	76,183	15,594	91,777
	76,183	15,594	91,777

The value of options granted has been calculated using the Black & Scholes valuation methodology.

Directors' interests in shares and options

The relevant interest of each director in the share capital of the Company as at the date of this report is as follows:

2004			PJD Elliott	CM Thomas	RJ Soper	RG Adamson
Ordinary shares			2,500,000	1,750,050	1,117,540	296,750
Options						
	Exercise price	Expiry date				
	20 cents per share	31.12.2007	2,195,000	875,000	450,000	125,000
	25 cents per share	31.12.2007	1,250,000	2,195,000	2,195,000	200,000
	30 cents per share	31.12.2007	-	800,000	800,000	-
	20 cents per share	20.04.2009	600,000	-	-	400,000
2003			PJD Elliott	CM Thomas	RJ Soper	RG Adamson
Ordinary shares			2,500,000	1,750,050	1,117,540	296,750
Options						
	Exercise price	Expiry date				
	20 cents per share	31.12.2007	2,195,000	875,000	450,000	125,000
	25 cents per share	31.12.2007	1,250,000	2,195,000	2,195,000	200,000

The following options were issued to directors or executives during the year.

			PJD Elliott	CM Thomas	RJ Soper	RG Adamson
Options						
	Exercise price	Expiry date				
	30 cents per share	31.12.2007	-	800,000	800,000	-
	20 cents per share	20.04.2009	600,000	-	-	400,000

Principal activities

The principal activity of the consolidated entity is the exploration for economic hardrock gold deposits in the Klondike area of Canada.

Results

The net result of operations after applicable income tax expense of the consolidated entity for the year ended 31 December 2004 was a loss of \$711,725 (2003: loss of \$381,805).

DIRECTORS' REPORT

Dividends

No dividends were either paid or declared for the year (2003 – nil).

The directors do not recommend the payment of a dividend in respect of the financial year ended 31 December 2004.

Review of operations

The Company's shares commenced trading on the Stock Exchange of Newcastle Limited (NSX) on 19 March 2004 after successfully completing the IPO which raised A\$1,841,000 through the issue of 18,420,000 shares at 10 cents per share.

On 2 September 2004, the Company completed a program of six deep diamond drill holes (totalling 1,537 metres) within joint venture claims located near the centre of the Klondike Goldfield. This was the first such drilling ever conducted in the central part of the goldfield. The holes tested areas of anomalous gold and arsenic soil geochemistry identified by surveys carried out by the Company during 2000 and 2001. Further soil geochemistry surveys were conducted during the 2004 field season, and 382 new claims were staked.

The holes drilled mainly quartz mica schist (the Klondike Schists) and minor chloritic and carbonaceous schists. Although mineralisation of economic potential was not intersected (best: 0.95 g/t gold over 1.2 metres in DDH04-06), the new lithologic, structural, geochemical and petrographic data derived from core logging and sampling have considerably advanced knowledge of the goldfield's geology.

The western holes (DDH04-05 and 06) show a widespread low-temperature hydrothermal alteration event followed by limited deposition of veinlets of carbonate-clay-chlorite, and weakly auriferous arsenopyrite and other sulphides. Alteration and gold-arsenic mineralisation increase toward a broad aeromagnetic 'low' located northwest of the holes. The magnetic anomaly is interpreted as a buried, probably intrusive body that has been strongly altered by the hydrothermal event seen in the drill core. This is thought to be a weakly mineralised epithermal episode that differs from, and is rather later than the main gold mineralising event in the district. Evidence for the earlier event, which is the likely primary source for most of the alluvial gold, is provided by the widespread carbonate-(sulphide) alteration that occurs (with variable intensity) in all the drill holes.

The Company presently holds 490 claims outright and has earned a 56% interest in 443 claims of the Klondike Joint Venture. Exploration expenditure in the 2004 field season has ensured that the majority of the joint venture claims are in good standing for the next five years.

During March 2005, the Company was advised that a Whitehorse legal firm holds a judgement against PacRim Resources Ltd (PRL) for CAN\$13,532 and a Writ of Seizure and Sale to be enforced by the Yukon Sheriff's Office against 375 Klondike Joint Venture claims of which PRL is the registered holder. We are advised that the writ attaches only to PRL's interest in the claims and a sale cannot be forced until the writ has been registered for one year.

In January 2004, the Yukon Territory Government announced an extension to March 2007, of the Territory's Mineral Exploration Tax Credit which offers a tax credit up to 25% on eligible exploration expenditures. KSL Exploration (Yukon) anticipates a rebate of approximately AUS\$123,500 under this scheme for work carried out in the 2004 field program.

The information in this report that relates to Exploration Results, Mineral Resources or Ore Reserves is based on information compiled by Robert Adamson who is a Member of the Australasian Institute of Mining and Metallurgy. Mr Adamson is a technical consultant to the Company. Mr Adamson has sufficient experience which is relevant to the style of mineralisation and type of deposit under consideration and to the activity which he is undertaking to qualify as a Competent Person as defined in the 2004 Edition of the "Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves". Robert Adamson consents to the inclusion in the report of the matters based on his information in the form and context in which it appears.

DIRECTORS' REPORT

Significant changes in the state of affairs

Other than undertaking the Initial Public Offering (IPO) and the termination of the agreement with PacRim Resources Limited (PRL) to acquire its interest in the Klondike Joint Venture claims there were no significant changes in the state of affairs of the consolidated entity during the financial year.

Matters subsequent to the end of the financial year

There were at the date of this report no matters or circumstances which have arisen since 31 December 2004 that have significantly affected or may significantly affect:

- i) the operations of the consolidated entity,
- ii) the results of those operations, or
- iii) the state of affairs of the consolidated entity

in the financial years subsequent to 31 December 2004.

Likely developments

The 2004 drilling results, together with regional mapping and aeromagnetic data recently published by the Yukon and the Canadian Geological Surveys are being interpreted and assessed as guides to major bedrock gold mineralisation.

The Company is actively seeking to farm out a part interest in the exploration of its wholly owned and joint venture Klondike claims.

In the longer-term, the Company is hoping to identify other precious and base metal exploration and evaluation targets which are perceived to offer outstanding opportunities.

At this stage, it is not possible to postulate likely developments from any of these exploration activities. As the consolidated entity's areas of interest are at an early stage of exploration, it is not possible to postulate likely developments.

Directors' benefits

During the year no director of the Company has received or become entitled to receive a benefit (other than a benefit included in the notes to the accounts) by reason of a contract made by the Company or a related corporation with the director or with a firm of which he is a member, or with a company in which he has a substantial financial interest.

Share Options

Particulars of options granted over unissued shares:

There are 15,375,100 options granted by the Company over unissued ordinary shares. No shares have been issued in the period as the result of the exercise of options. Full details of options on issue are shown in Note 20.

Meetings of Directors

Attendance at directors' meetings during the year:

	Eligible to attend	Attended
Patrick J D Elliott	8	6
Colin M Thomas	8	8
Raymond J Soper	8	8

Directors Messrs Soper and Elliott are members of the Company's Audit Committee, which met once during the year. The Committee was set up to review the Company's financial systems, accounting policies and annual financial statements.

DIRECTORS' REPORT

Environment

Klondike Source Limited, through its subsidiary, KSL Exploration (Yukon) Limited, holds exploration tenements in the Yukon Territory of Canada that are subject to various governmental statutes and guidelines for environmental impacts in relation to exploration activities. These provide for the satisfactory rehabilitation of the areas of exploration. There have been no material known breaches of the licence conditions.

Directors' and auditors' indemnification

The Company has not, either during or since the end of the financial period, in respect of any person who is or has been an officer or auditor of the Company or a related body corporate, indemnified or made any relevant agreement for indemnifying against a liability incurred as an officer, including costs and expenses in successfully defending legal proceedings.

During or since the financial period, the Company has not paid or agreed to pay a premium in respect of a contract insuring against a liability incurred as an officer for the costs or expenses to defend legal proceedings.

Auditor

Barnes Dowell James holds office in accordance with section 327 of the Corporations Act 2001.

This report is made in accordance with a resolution of the directors.



Colin M Thomas

Director

Sydney

4 April 2005

STATEMENTS OF FINANCIAL PERFORMANCE

for the year ended 31 December 2004

	Note	Consolidated		Parent Entity	
		2004	2003	2004	2003
		\$	\$	\$	\$
Revenue from ordinary activities	2	45,640	866	45,592	866
Administration costs		(152,616)	(112,715)	(122,114)	(108,893)
Borrowing cost	3	(246)	(2,651)	(246)	(2,651)
Consultants fees		(128,757)	(169,180)	(128,757)	(166,229)
Depreciation	3	(2,859)	(1,537)	(906)	(1,537)
Diminution of loans to controlled entity	3	-	-	(560,588)	(151,342)
Directors fees		(20,000)	(37,101)	(20,000)	(37,101)
Exploration property provision	12	(750,000)	-	-	-
Foreign exchange gains (losses)	3	224,794	(2,477)	126,863	-
Office rent	3	(26,568)	(49,428)	(26,568)	(49,428)
Other expenses from ordinary activities		(24,695)	(7,582)	(24,695)	(5,595)
Loss from ordinary activities before income tax expense		(835,307)	(381,805)	(711,419)	(521,910)
Income tax (expense) benefit	4	123,582	-	-	-
Net loss from ordinary activities after income tax expense	21	(711,725)	(381,805)	(711,419)	(521,910)
Basic and diluted loss per share (cents)		(2.55)	(3.14)		

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

STATEMENTS OF FINANCIAL POSITION

at 31 December 2004

		Consolidated		Parent Entity	
	Note	2004 \$	2003 \$	2004 \$	2003 \$
CURRENT ASSETS					
Cash Assets	9	729,963	364,570	717,491	351,453
Receivables	10	210,946	33,757	45,095	24,878
TOTAL CURRENT ASSETS		940,909	398,327	762,586	376,331
NON-CURRENT ASSETS					
Receivables	11	-	-	467,345	499,069
Deferred Exploration and Evaluation Expenditure	12	448,190	486,447	164,281	-
Investments	13	-	-	855	855
Plant and equipment	14	13,605	660	2,440	528
TOTAL NON-CURRENT ASSETS		461,795	487,107	643,921	500,452
TOTAL ASSETS		1,402,704	885,434	1,397,507	876,783
CURRENT LIABILITIES					
Payables	15	162,659	317,412	157,462	309,067
Other Current Liabilities	16	1,220	-	1,220	-
Interest bearing liabilities	17	32,000	-	32,000	-
TOTAL CURRENT LIABILITIES		195,879	317,412	190,682	309,067
NON-CURRENT LIABILITIES					
Interest bearing liabilities	18	-	32,000	-	32,000
TOTAL NON-CURRENT LIABILITIES		-	32,000	-	32,000
TOTAL LIABILITIES		195,879	349,412	190,682	341,067
NET ASSETS		1,206,825	536,022	1,206,825	535,716
SHAREHOLDERS' EQUITY					
Contributed equity	19	3,007,518	1,624,990	3,007,518	1,624,990
Accumulated losses	21	(1,800,693)	(1,088,968)	(1,800,693)	(1,089,274)
TOTAL EQUITY		1,206,825	536,022	1,206,825	535,716

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

STATEMENTS OF CASH FLOWS

for the year ended 31 December 2004

		Consolidated		Parent Entity	
	Note	2004	2003	2004	2003
		\$	\$	\$	\$
CASH FLOWS FROM OPERATING ACTIVITIES					
Payment to suppliers (inclusive of GST)		(271,716)	(177,774)	(365,873)	(169,243)
Interest received		45,640	866	45,592	866
Interest paid		(246)	-	(246)	-
NET CASH (OUTFLOWS) FROM OPERATING ACTIVITIES	29	(226,322)	(176,908)	(320,527)	(168,377)
CASH FLOWS FROM INVESTING ACTIVITIES					
Expenditure on plant and equipment		(15,804)	-	(2,818)	-
Expenditure on mining interests (exploration)		(775,009)	(1,161)	(164,281)	-
Loans to controlled entity		-	-	(528,864)	61,454
NET CASH INFLOWS / (OUTFLOWS) FROM INVESTING ACTIVITIES		(790,813)	(1,161)	(695,963)	61,454
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from issue of shares		-	111,980	-	111,980
Application monies received pursuant to IPO		1,503,000	338,000	1,503,000	338,000
Proceeds from long term borrowing		-	2,000	-	2,000
Share issue costs		(120,472)	-	(120,472)	-
NET CASH INFLOWS FROM FINANCING ACTIVITIES		1,382,528	451,980	1,382,528	451,980
NET INCREASE / (DECREASE) IN CASH HELD		365,393	273,911	366,038	345,057
Cash at the beginning of the financial year		364,570	90,659	351,453	6,396
CASH AT THE END OF THE FINANCIAL YEAR	29	729,963	364,570	717,491	351,453

The above statements of cash flows should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

This general purpose financial report has been prepared in accordance with Accounting Standards, other authoritative pronouncements of the Australian Accounting Standards Board, Urgent Issues Group Consensus Views and the Corporations Act 2001.

It is prepared in accordance with the historical cost convention, except for certain assets which, as noted, are at valuation. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year. Comparative information is reclassified where appropriate to enhance comparability.

Impact of Adopting Australian Equivalent to International Financial Reporting Standards

The consolidated entity will be required to prepare financial statements that comply with Australian equivalents to International Financial Reporting Standards ("A-IFRS") for annual reporting periods beginning on or after 1 January 2005. Accordingly, the consolidated entity's first half-year report prepared under A-IFRS will be for the half-year reporting period ending 30 June 2005, and its first annual financial report prepared under A-IFRS will be for the year ending 31 December 2005.

The consolidated entity has recently commenced the process of evaluating the impact of A-IFRS on the consolidated entity and consequently has not yet finalised how it is going to manage the transition to A-IFRS. The directors expect to complete the impact study and commence a plan to prepare the consolidated entity to be A-IFRS compliant shortly.

While no decision has yet been made as to the policy alternatives to be applied or the extent to which it will affect the consolidated entity, the directors have identified the following as being the key accounting policy differences expected to arise on transitioning to A-IFRS. This does not represent an exhaustive list of the differences that will arise, and further analysis may change the consolidated entity's assessment of the importance or otherwise of the various differences.

(a) First-time adoption of A-IFRS

On first-time adoption of A-IFRS, the consolidated entity will be required to restate its comparative balance sheet such that the comparative balances presented comply with the requirements specified in the A-IFRS. That is, the balances that will be presented in the financial report for the half-year ending 30 June 2005 and year ending 31 December 2005 may not be the balances that will be presented as comparative numbers in the financial report for the following half year, and year end, as a result of the requirement to retrospectively apply the A-IFRS. In addition, certain assets and liabilities may not qualify for recognition under A-IFRS, and will need to be derecognised. Required adjustments on first-time adoption are to be made against opening retained earnings (1 January 2005).

(b) Capitalised Exploration and Development Expenditure

An A-IFRS on extractive industries has not yet been issued. Consequently, the consolidated entity is unable to determine the change in policies and related impacts, if any, that may arise on adoption of A-IFRS on its extractive-related operations and balances at reporting date.

(c) Impairment testing

Under A-IFRS all current and non-current assets will be subject to impairment testing. The consolidated entity will be required to test the values attributed to assets where impairment is indicated. Such testing will require the consolidated entity to identify the smallest group of assets generating independent cash inflows, called cash generating units ("CGUs"), and determine the recoverable amount for each CGU. Recoverable amounts are determined using the higher of either value in use calculated using reliable estimates of future discounted cash flows, or fair values. Where the carrying amount of a CGU exceeds the recoverable amount, an impairment loss exists which will be recognised in the statement of income. The consolidated entity has not yet determined the impact, if any, of any impairment which may be required. It is not practicable to determine the impact of the change in accounting policy for future financial reports, as any impairment or reversal thereof will be affected by future conditions.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(d) Income tax

The consolidated entity currently recognises deferred taxes by accounting for the differences between accounting profit and taxable income, which give rise to 'permanent' and 'timing' differences. Under A-IFRS, deferred taxes are measured by reference to the 'temporary differences' determined as the difference between the carrying amount and tax base of assets and liabilities recognised in the balance sheet. As A-IFRS has a wider scope than the entity's current accounting policies, it is likely that the amount of deferred taxes recognised in the balance sheet will increase.

Adjustments to the recognised amounts of deferred taxes will also result as a consequence of adjustments to the carrying amounts of assets and liabilities resulting from the adoption of other A-IFRS. The likely impact of these changes on deferred tax balances has not currently been determined.

(e) Financial assets and financial liabilities

Under current Australian CAAP, financial assets and financial liabilities are recognised at cost, at fair value, or at net market value. On adoption of A-IFRS, the consolidated entity will be required to classify these financial instruments into various specified categories. The classification of the instrument will affect the instrument's subsequent measurement - at amortised cost using the effective interest rate method, fair value with movements recognised through equity or fair value recognised through the profit and loss. The consolidated entity is evaluating the different options available, but has not made any determination at reporting date of the accounting to be adopted, and consequently, the impact of the change on the financial statements cannot yet be quantified.

Borrowings

Loans are recorded at an amount equal to the net proceeds received. Interest expense is recognized on an accruals basis.

Cash

For the purposes of the statement of cash flows, cash includes cash on hand and in banks, and money market investments readily convertible to cash within two working days, net of outstanding bank overdrafts.

Exploration and Evaluation Expenditure

Exploration and evaluation expenditure incurred by or on behalf of the Company is accumulated separately for each area of interest. Such expenditure comprises net direct costs and an appropriate portion of related overhead expenditure, but does not include general overheads or administrative expenditure not having a specific nexus with a particular area of interest.

Each area of interest is limited to a size related to known or probable mineral resource capable of supporting a mining operation.

Exploration expenditure for each area of interest, other than that acquired from the purchase of another mining company, is written off as incurred, except that it is carried forward provided that one of the following conditions is met:

- such costs are expected to be recouped through successful development and exploitation of the area of interest or, alternatively, by its sale; or
- exploration activities in the area of interest have not yet reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves, and active and significant operations in relation to the area are continuing.

A provision is raised against exploration expenditure where the directors are of the opinion that the carried forward net cost may not be recoverable. The increase in the provision is charged against the results for the year.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Exploration expenditure which no longer satisfies the above policy is written off. When an area of interest is abandoned, any expenditure carried forward in respect of that area is written off firstly against any existing provision for that expenditure, with any remaining balance being charged to earnings. The provision against exploration expenditure is reversed when recoupment out of revenue to be derived from the relevant area of interest/mineral resource or from the sale of that area of interest, is assured and the asset is transferred to another class or sold.

Expenditure is not carried forward in respect of any area of interest/mineral resource unless the Company's rights of tenure to that area of interest are current.

Foreign Currency Translation

Foreign currency transactions are initially translated into Australian currency at the rate of exchange at the date of translation. At balance date, amounts payable and receivable in foreign currencies are translated to Australian currency at rates of exchange current at that date. Resulting exchange differences are brought to account in determining the profit or loss for the year.

Goods and Services Tax

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

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

The net amount of GST recoverable from, or payable to, the taxation authorities is included as part of other receivables or other payables.

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

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 accounts and when items are taken into account in determining taxable income, the net related taxation benefit or liability, calculated at 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.

Joint Ventures

Interests in joint ventures are brought to account by including in the respective classifications, the share of individual assets employed, and liabilities and expenses incurred.

Leases

Operating lease payments, where the lessor effectively retains substantially all of the risks and benefits of ownership of the leased items, are included in the determination of the operating profit in equal instalments over the lease term.

Principles of Consolidation

The consolidated financial statements incorporate the assets and liabilities of all entities controlled by Klondike Source Limited ("Company") as at 31 December 2004 and the results of all entities for the year then ended. Klondike Source Limited and its controlled entities together are referred to in this financial report as the consolidated entity. The effect of all transactions between entities in the consolidated entity are eliminated in full. Outside equity interests in the results and equity of controlled entities are shown separately in the consolidated profit and loss statement and balance sheet respectively.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Where control of an entity is obtained during a financial year, its results are included in the consolidated profit and loss statement from the date on which control commenced. Where control of an entity ceases during a financial year, its results are only included for that part of the year during which control existed. There are no associated companies.

Property, Plant and Equipment

Property, plant and equipment are included at cost. Depreciation is provided on a straight line basis on all property, plant and equipment at rates calculated to write off the cost, less estimated residual value at the end of the useful lives of the assets, over those estimated useful lives.

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

Plant and equipment 5 – 8 years

Receivables

Trade and other receivables are recorded at amounts due less any allowance for doubtful debts.

Restoration, Rehabilitation and Environmental Expenditure

Restoration, rehabilitation and environmental costs necessitated by exploration and evaluation activities are accrued at the time of those activities, and treated as exploration and evaluation expenditure.

Revenue Recognition

Interest revenue is recognized on a proportional basis taking into account the interest rates applicable to the financial assets. All revenue is stated net of GST.

Trade and Other Creditors

These amounts represent liabilities for goods and services provided to the company prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

2. REVENUE

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Revenue from operating activities				
Interest received	45,640	866	45,592	866
Total revenue	45,640	866	45,592	866

3. OPERATING LOSS FROM ORDINARY ACTIVITIES BEFORE INCOME TAX EXPENSE

The operating loss from ordinary activities before income tax expense has been determined after charging the following expenses:

Borrowing costs	246	2,651	246	2,651
Depreciation	2,859	1,537	906	1,537
Diminution of loan to controlled entity	-	-	560,588	151,342
Foreign exchange losses (gains)	(224,794)	2,477	(126,863)	-
Rent	26,568	49,428	26,568	49,428

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
4. INCOME TAX				
Loss from ordinary activities before income tax expense	711,725	381,805	711,419	521,910
Income tax (expense) benefit calculated @ 30% (2003 – 30%)	213,518	114,542	213,426	156,573
Future income tax benefits not brought to account in respect of current year	(213,518)	(114,542)	(213,426)	(156,573)
Corporate tax refund	123,582	-	-	-
Income tax (expense) benefit attributable to operating loss	123,582	-	-	-
Future income tax benefits not recognised calculated at 30% (2003 - 30%) in respect of:				
Revenue Losses	286,198	201,461	286,198	201,461
Timing differences	265,781	44,503	265,781	44,503
Total future tax benefits not recognised	551,979	245,964	551,979	245,964

The benefit for tax losses and timing differences will only be obtained if:

- (i) the consolidated entity derives future assessable income of a nature and of an amount sufficient to enable the benefit from the deductions for the losses to be realised;
- (ii) the consolidated entity continues to comply with the conditions for deductibility imposed by the law; and
- (iii) no changes in tax legislation adversely affect the consolidated entity in realising the benefit from the deductions for the losses.

No franking credits are available for subsequent years.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

5. REMUNERATION OF DIRECTORS AND EXECUTIVE OFFICERS

Directors' Remuneration

	Directors' Fees	Consulting Fees	Superannuation	Options	TOTAL
P J D Elliott	15,000	-	1,350	23,931	40,281
C M Thomas	-	48,000	-	15,705	63,705
R J Soper	5,000	6,501	450	15,705	27,656
	20,000	54,501	1,800	55,341	131,642

The value of options granted has been calculated using the Black & Scholes valuation methodology.

In addition, certain consulting fees were paid to companies related to the directors (refer to note 26).

Executive officers' Remuneration

	Consulting Fees	Options	TOTAL
R G Adamson	76,183	15,594	91,777
	76,183	15,594	91,777

The value of options granted has been calculated using the Black & Scholes valuation methodology.

6. REMUNERATION OF AUDITORS

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Total amounts receivable by the auditors of the Company for:				
Audit of the Company's accounts	9,025	3,000	9,025	3,000
Other services – IPO Accountant's Report	-	2,000	-	2,000
	9,025	5,000	9,025	5,000

7. FINANCIAL REPORTING BY SEGMENTS

The consolidated entity operates predominantly in the one industry and in one geographical area, namely Canadian mineral exploration and evaluation.

8. EARNINGS PER SHARE

Basic and diluted	2004	2003
Weighted average number or shares used in basic and diluted earnings per share	27,923,777	12,208,263
Basic and diluted earning per share (cents per share)	(2.55)	(3.14)

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

9. CASH ASSETS

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Cash at Bank	47,473	364,570	35,001	351,453
Deposits at call	82,490	-	82,490	-
Bank Bills	600,000	-	600,000	-
	729,963	364,570	717,491	351,453

10. RECEIVABLES - CURRENT

Other debtors	18,927	33,757	18,927	24,878
Security deposit	20,000	-	20,000	-
Corporate taxes receivable	134,614	-	-	-
GST debtor	37,271	-	6,034	-
Interest receivable	134	-	134	-
	210,946	33,757	45,095	24,878

11. RECEIVABLES – NON-CURRENT

Loan to controlled entity	-	-	1,179,275	650,411
Less provision for diminution	-	-	(711,930)	(151,342)
	-	-	467,345	499,069

12. DEFERRED EXPLORATION AND EVALUATION EXPENDITURE

Deferred exploration costs	1,198,190	486,447	164,281	-
Less provision for diminution	(750,000)	-	-	-
	448,190	486,447	164,281	-
Deferred exploration costs brought forward	486,447	487,734	-	-
Costs incurred during the year	775,009	1,161	164,281	-
Provision for diminution	(750,000)	-	-	-
Abandoned areas written off	-	-	-	-
Exchange rate fluctuation	(63,266)	(2,448)	-	-
Deferred exploration costs carried forward	448,190	486,447	164,281	-

The above amounts represent costs of exploration areas of interest carried forward as an asset in accordance with the accounting policy set out in Note 1. The ultimate recoupment of deferred exploration and evaluation expenditure in respect of an area of interest carried forward is dependent upon the discovery of commercially viable reserves and the successful development and exploitation of the respective areas or alternatively sale of the underlying areas of interest for at least their carrying value. Amortisation, in respect of the relevant area of interest, is not charged until a mining operation has commenced.

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

13. INVESTMENTS

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Investment in controlled entity				
Investment in KSL Exploration (Yukon) Limited (Incorporated in Canada – 100% owned (2003 - 100% owned))	-	-	855	855

14. PROPERTY PLANT AND EQUIPMENT

Plant and Equipment

Cost	18,115	2,197	4,882	2,065
Accumulated Depreciation	(4,510)	(1,537)	(2,442)	(1,537)
	13,605	660	2,440	528

Reconciliations of the carrying amount of each class of property, plant and equipment at the beginning and end of the current financial year are set out below.

Plant and Equipment

Carrying amount at 1 January 2004	660	2,319	528	2,065
Additions	15,804	-	2,818	-
Depreciation	(2,859)	(1,537)	(906)	(1,537)
Exchange rate fluctuation	-	(122)	-	-
Carrying amount at 31 December 2004	13,605	660	2,440	528

15. CURRENT PAYABLES

Trade creditors and accruals	162,659	312,412	157,462	304,067
Application monies refundable - IPO	-	5,000	-	5,000
	162,659	317,412	157,462	309,067

16. OTHER CURRENT LIABILITIES

Unearned interest	1,220	-	1,220	-
	1,220	-	1,220	-

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

17. CURRENT INTEREST BEARING LIABILITIES

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Convertible note (Refer Note 26)	<u>32,000</u>	<u>-</u>	<u>32,000</u>	<u>-</u>

18. NON-CURRENT INTEREST BEARING LIABILITIES

Convertible note (Refer Note 26)	<u>-</u>	<u>32,000</u>	<u>-</u>	<u>32,000</u>
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19. SHARE CAPITAL

Issued Capital

31,504,900 fully paid ordinary shares
(2003 – 13,094,900)

	3,150,490	1,309,490	3,150,490	1,309,490
Application monies received	-	338,000	-	338,000
Less share issue costs	<u>(142,972)</u>	<u>(22,500)</u>	<u>(142,972)</u>	<u>(22,500)</u>
	<u>3,007,518</u>	<u>1,624,990</u>	<u>3,007,518</u>	<u>1,624,990</u>

Movement in issued capital

	Number	\$
Shares on issue 1 January 2004	13,094,900	1,309,490
Issued for cash pursuant to IPO	<u>18,410,000</u>	<u>1,841,000</u>
Shares on issue 31 December 2004	<u>31,504,900</u>	<u>3,150,490</u>

20. OPTIONS

Expiry Date	Exercise Price	Issued 1 Jan 04	Granted	Exercised	Lapsed	Issued 31 Dec 04
31 Dec 07	0.20	6,487,500	-	-	-	6,487,500
31 Dec 07	0.25	5,487,600	500,000	-	-	5,487,600
31 Dec 07	0.30	-	1,600,000	-	-	1,600,000
20 Apr 09	0.20	-	1,300,000	-	-	1,300,000
		<u>11,975,100</u>	<u>3,400,000</u>	<u>-</u>	<u>-</u>	<u>15,375,100</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

21. ACCUMULATED LOSSES

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Accumulated losses at the beginning of the financial year	(1,088,968)	(707,163)	(1,089,274)	(567,364)
Net loss for the year	(711,725)	(381,805)	(711,419)	(521,910)
Retained losses at the end of the financial year	<u>(1,800,693)</u>	<u>(1,088,968)</u>	<u>(1,800,693)</u>	<u>(1,089,274)</u>

22. CONTINGENT LIABILITIES

There are no contingent liabilities.

23. COMMITMENTS

Exploration Tenement Expenditure Requirements

In order to maintain the consolidated entity's tenements in good standing with Canadian mining authorities, the Company will be required to incur exploration expenditure under the terms of each claim.

Payable not later than one year	21,557	67,068	-	-
Payable later than one year, but not later than two years	50,372	58,283	-	-
	<u>71,929</u>	<u>125,351</u>	<u>-</u>	<u>-</u>

It is likely that variations to the terms of the current and future tenement holdings, the granting of new tenements and changes in tenement areas at renewal or expiry, will change the expenditure commitment to the consolidated entity from time to time.

24. JOINT VENTURES

The consolidated entity continues exploration in the Klondike Joint Venture (which it manages) with PacRim Resources Limited (PRL). The consolidated entity has earned a 56% participating interest in the joint venture and can earn additional interest by contributing expenditure in the event PRL elects dilution.

25. LEASE COMMITMENTS

Payable not later than one year	22,120	26,544	22,120	26,544
Payable later than one year, but not later than two years	-	22,120	-	22,120
	<u>22,120</u>	<u>48,664</u>	<u>22,120</u>	<u>48,664</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

26. RELATED PARTY DISCLOSURES

The directors in office during the year were Patrick J D Elliott, Colin M Thomas, Raymond J Soper and Robert G Adamson (alternate director for Colin M Thomas).

Interests in the shares and options of the Company held by current directors and their director-related entities are:

2004			PJD Elliott	CM Thomas	RJ Soper	RG Adamson
Ordinary shares			2,500,000	1,750,050	1,117,540	296,750
Options	Exercise price	Expiry date				
	20 cents per share	31.12.2007	2,195,000	875,000	450,000	125,000
	25 cents per share	31.12.2007	1,250,000	2,195,000	2,195,000	200,000
	30 cents per share	31.12.2007	-	800,000	800,000	-
	20 cents per share	20.04.2009	600,000	-	-	400,000

Shares held by directors included those held by the directors and their director-related entities, including the spouses of such directors and relatives of such directors. All shares and options were issued or granted on terms no more favourable than to other shareholders.

Klondike Source Limited issued a convertible note during the year ended 31 December 2003 to Poduta Pty Limited, a company in which Mr Colin Thomas is a director and has a significant financial interest. The interest rate imposed is the rate of interest per annum actually paid by Mr Colin Thomas, a Director of the Noteholder (Poduta Pty Limited), in respect of a loan by Citibank Mortgage Power to Mr Colin Thomas. The note is convertible into new shares of Klondike at the option of the holder, or repayable on 30 June 2005. The Noteholder may require the Issuer to repay all or part of the amount owing to the Noteholder by issue of such number of new shares at the applicable issue price as equals the amount to be repaid. The issue price is 10 cents per share if the shares are issued prior to listing of the Issuer on a recognised Stock Exchange. If the shares are issued after the listing of the Issuer on a recognised stock exchange, the issue price shall not be less than the greater of 20 cents, if the recognised stock exchange is the Australian Stock Exchange (ASX) or in the case of a recognised stock exchange other than the ASX, the issue price on listing, or the weighted average price of a share on the stock exchange over the Stock Exchange trading days immediately preceding the date of issue.

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Maximum amount available	70,000	70,000	70,000	70,000
Amount drawn down at balance date	32,000	32,000	32,000	32,000

Mr C M Thomas is a director and has a significant financial interest in RobSearch Pty Limited, a company that provides geological and administration services to the Company. A portion of costs has been deferred and is payable to RobSearch when the Company completes a successful IPO or equivalent raising to raise a minimum of \$2.5 million or a like amount is spent by way of expenditure by joint venture partners of the Company's exploration properties. Services provided by RobSearch were under normal commercial terms and conditions.

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Amounts paid during year	76,145	13,375	76,145	13,375
Amounts deferred during year	14,250	8,025	14,250	8,025
Deferred amount at balance date	114,050	99,800	114,050	99,800

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

27. SUBSEQUENT EVENTS

There were at the date of this report no matters or circumstances which have arisen since 31 December 2004 that have significantly affected or may significantly affect:

- i) the operations of the consolidated entity,
- ii) the results of those operations, or
- iii) the state of affairs of the consolidated entity

in the financial years subsequent to 31 December 2004.

28. FINANCIAL INSTRUMENTS

- (a) The Company receives interest on its cash balance and at balance date was exposed to a floating weighted average interest rate on cash balances of 4.75% (2003 - 4.25%). As surplus funds become available, they are deposited in its cash management account and are exposed to receiving a floating rate, which varies according to the amount of funds deposited. All other financial assets are non-interest bearing.
- (b) Net fair value of financial assets and liabilities: the net fair value of cash and cash equivalents and non-interest bearing financial assets and financial liabilities approximates their carrying value.
- (c) The consolidated entity's exposure to interest rate risk and the effective weighted average interest rate for each class of financial assets and financial liabilities is set out in the following table:

	Notes	Floating interest rate	Fixed interest maturing in:			Non-interest bearing	Total
			1 year or less	over 1 to 5 years	more than 5 years		
		\$	\$	\$	\$	\$	\$
2004							
Financial assets							
Cash		129,963	600,000	-	-	-	729,963
Receivables	10	-	-	-	-	210,946	210,946
		<u>129,963</u>	<u>600,000</u>	<u>-</u>	<u>-</u>	<u>210,946</u>	<u>940,909</u>
Weighted average interest rate		5.25%					
Financial liabilities							
Payables	15	-	-	-	-	162,659	162,659
Convertible notes	17	32,000	-	-	-	-	32,000
		<u>32,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>162,659</u>	<u>194,659</u>
Weighted average interest rate		7.59%					
Net financial assets (liabilities)		<u>97,963</u>	<u>600,000</u>	<u>-</u>	<u>-</u>	<u>48,287</u>	<u>746,250</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

28. FINANCIAL INSTRUMENTS (Continued)

	Notes	Floating interest rate	Fixed interest maturing in:			Non-interest bearing	Total
			1 year or less	over 1 to 5 years	more than 5 years		
		\$	\$	\$	\$	\$	\$
2003							
Financial assets							
Cash		364,570	-	-	-	-	364,570
Receivables	10	-	-	-	-	33,757	33,757
		<u>364,570</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>33,757</u>	<u>398,327</u>
Weighted average interest rate		4.75%					
Financial liabilities							
Payable	15	-	-	-	-	317,412	317,412
Convertible notes	18	32,000	-	-	-	-	32,000
		<u>32,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>317,412</u>	<u>349,412</u>
Weighted average interest rate		7.59%					
Net financial assets (liabilities)		<u>332,570</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(283,655)</u>	<u>48,915</u>

NOTES TO THE FINANCIAL STATEMENTS

31 December 2004

29. RECONCILIATION OF LOSS FROM ORDINARY ACTIVITIES AFTER INCOME TAX TO NET CASH OUTFLOW FROM OPERATING ACTIVITIES.

(a) Reconciliation of loss from ordinary activities after income tax to net cash outflows from operating activities as follows:

	Consolidated		Parent Entity	
	2004	2003	2004	2003
	\$	\$	\$	\$
Operating (loss) after income tax	(711,725)	(381,805)	(711,419)	(521,910)
Depreciation	2,859	1,537	906	1,537
Provision for exploration properties	750,000	-	-	-
Diminution of loans to controlled entity	-	-	560,588	151,342
Unrealised foreign exchange loss	63,266	2,570	-	-
Change in operating assets and liabilities:				
- Decrease / (Increase) in receivables	(42,575)	(19,051)	(20,217)	(12,279)
- Increase / (Decrease) in accounts payable	(153,533)	219,841	(150,385)	212,933
- Corporate taxes receivable	(134,614)	-	-	-
Net cash outflow from operating activities	<u>(226,322)</u>	<u>(176,908)</u>	<u>(320,527)</u>	<u>(168,377)</u>
(b) Cash on hand comprises:				
Cash at banks	<u>729,963</u>	<u>364,570</u>	<u>717,491</u>	<u>351,453</u>

30. DETAILS OF CONTROLLED ENTITIES.

Company	Country of Incorporation and Operation	Percentage of Equity Held	
		2004	2003
KSL Exploration (Yukon) Ltd	Canada	100%	100%

DIRECTORS' DECLARATION

The directors declare that the financial statements and notes set out on pages 7 to 23:

- (a) comply with Accounting standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
- (b) give a true and fair view of the company's and consolidated entity's financial position as at 31 December 2004 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date.

In the directors' opinion:

- (a) the financial statements and notes are in accordance with the Corporations Act 2001; and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

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

Dated at SYDNEY this 4th day of April 2005

On behalf of the Board

A handwritten signature in black ink, appearing to read 'C. Thomas'.

Colin M Thomas
Director

INDEPENDENT AUDIT REPORT

BARNES DOWELL JAMES

CHARTERED ACCOUNTANTS

4 April 2005

Klondike Source Limited
Level 10, 80 Arthur Street
NORTH SYDNEY NSW 2060

Partners
C H Barnes FCA
A J Dowell CA
M W James CA

Associate
M A Nakkan CA

North Sydney
Level 13, 122 Arthur St
North Sydney NSW 2060

Manly
Level 5, 22 Central Ave
Manly National Building
Manly NSW 2095

Correspondence
PO Box 1664
North Sydney NSW 2059

Telephone
(02) 9956 8500
Facsimile
(02) 9929 7428
email:
bdj@bdj.com.au

SCOPE

We have audited the financial report of Klondike Source Limited and controlled entity for the financial year ended 31 December 2004 as set out on pages 2 to 24.

The financial report includes the consolidated financial statements of the consolidated entity comprising the company and the entities it controlled at the year's end or from time during the financial year. The company's directors are responsible for the financial report. We have conducted an independent audit of this financial report in order to express an opinion on it to the members of the company.

Our audit has been conducted in accordance with Australian Standards to provide reasonable assurance whether the financial report is free of material misstatement. Our procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial report, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion whether, in all material respects, the financial report is presented fairly in accordance with Accounting Standards and other mandatory professional reporting requirements in Australia and statutory requirements so as to present a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and performance as represented by the result of their operations and their cash flows.

The audit opinion expressed in this report has been formed on the above basis.

AUDIT OPINION

In our opinion, the financial report of Klondike Source Limited is in accordance with:

(a) the Corporations Act 2001, including:

- (i) Giving a true and fair view of the company's and consolidated entity's financial position as at 31 December 2004 and of their performance for the year ended on that date: and
- (ii) Complying with Accounting Standards in Australia and the Corporations Regulations 2001: and

(b) other mandatory professional reporting requirements in Australia.

BARNES DOWELL JAMES
Chartered Accountants



.....
A.J. DOWELL
Partner

SHAREHOLDER INFORMATION

Information relating to shareholders at 31 March 2005

Substantial Shareholders	Number of Shares	%
Panstyn Investments Pty Ltd	2,500,000	7.93
Mr Glenn Tetley	2,000,000	6.35
Poduta Pty Ltd	1,750,000	5.56

Distribution of Shareholders - Analysis of Holdings as at 31 March 2005

Security Classes	Holdings Ranges	Holders	Total Units	%
Fully Paid Ordinary	1 - 1,000	2	100	0.00
	1,001 - 5,000	0	0	0
	5,001 - 10,000	1	6,000	0.3
	10,001 - 100,000	147	7,653,500	24.3
	100,001 and over	47	23,755,300	75.4
Totals		193	31,504,900	100.00

As at 31 March 2005 there was one shareholder with an unmarketable share parcel of less than 10,000 shares at the prevailing share price of 5 cents.

Top 20 Holdings as at 31 March 2005

Holder Name	Balance at 31-03-2005	%
Panstyn Investments Pty Ltd	2,500,000	7.94
Mr Glenn Tetley	2,000,000	6.35
Poduta Pty Ltd	1,750,000	5.56
Ipseity Pty Ltd	1,117,490	3.55
Baron Nominees Pty Limited	1,000,000	3.17
Yandal Investments Pty Ltd	1,000,000	3.17
Sunshore Holdings Pty Ltd	1,000,000	3.17
Henley Park Estate Pty Ltd	1,000,000	3.17
Australian Heritage Group Pty Ltd	1,000,000	3.17
Redcliff Pty Ltd	625,000	1.98
John M Clark Engineering Pty Ltd	625,000	1.98
Wildfire Investments Pty Ltd	500,000	1.59
Mr Ronald Hugh Beevor & Mrs Fiona Mary Beevor	500,000	1.59
WHI Securities Pty Ltd	500,000	1.59
Eureka Capital Partners Pty Ltd	500,000	1.59
Jaspon Holdings Pty Ltd	500,000	1.59
K Biggs Enterprises Pty Limited	400,000	1.27
National Nominees Limited	400,000	1.27
Mr John P Tuite	400,000	1.27
Mr Paul Antony Young & Mrs Lorraine Young	375,000	1.19
Total of top 20 holders	17,692,490	56.16
Other holdings	13,812,410	43.84
Total Issued Capital	31,504,900	100.00

SHAREHOLDER INFORMATION

Restricted Securities

Each of the Directors of the Company has entered into a voluntary restriction agreement, in respect of their Shares totalling 5,664,340, for a period of 24 months from 19 March, 2004, or, for 12 months, if after that time, the Company's Shares achieve a weighted average market price over two months of not less than 40 cents. This has been agreed between KSL and Newcastle Stock Exchange Limited.

Options on issue including holders of more than 20%

Expiry Date	Exercise Price \$	Number of Holders	Total Issued	Holders of more than 20%	
31/12/07	0.20	16	6,487,500	P J D Elliott	33.83%
31/12/07	0.25	10	5,487,600	R J Soper	36.97%
				C M Thomas	36.97%
31/12/07	0.30	2	1,600,000	R J Soper	50.00%
				C M Thomas	50.00%
20/04/09	0.20	5	1,300,000	P J D Elliott	46.15%
				R G Adamson	30.77%

Voting Rights

There are no restrictions on voting rights. On a show of hands every member present in person or by proxy shall have one vote and upon a poll each share shall have one vote. Where a member holds shares which are not fully paid, the number of votes to which that member is entitled on a poll in respect of those part paid shares shall be that fraction of one vote which the amount paid up bears to the total issued price thereof. Option holders have no voting rights until the options are exercised.

Five-year Summary of Performance Table (Consolidated)

		2000	2001	2002	2003	2004
Gross Revenue	\$	8,693	3,721	2,222	866	45,640
Net profit/(loss) before tax	\$	(169,581)	(218,363)	(195,054)	(381,307)	(835,307)
Total assets	\$	708,239	741,729	595,418	855,434	1,402,704
Total liabilities	\$	69,475	78,828	127,571	349,412	195,879
Shareholders' funds	\$	638,764	662,901	467,847	536,022	1,206,825
Earnings per share (loss)	Cents	(5.00)	(2.00)	(1.63)	(3.14)	(2.55)

The company has not paid any dividends in the period.

CORPORATE GOVERNANCE

Statement of Corporate Governance

The Directors of KSL are responsible to the Shareholders for the performance of the Company in both the short and the longer term and seek to balance these sometimes competing objectives in the best interests of the Company as a whole. Their principal focus is to enhance the interests of the Shareholders and ensure that the Company, including its controlled entity, is properly managed. The Board draws on relevant best practice principles, particularly those issued by the ASX Corporate Governance Council in March 2004. At its October 2004 meeting, the Board examined the KSL corporate governance practices compared to the best practice principles proposed by the ASX Corporate Governance Council. While KSL will align itself with the principles proposed by ASX, it is mindful that there may be some instances where compliance is not practicable for a company of KSL's current small size. The following paragraphs set out the Company's position relative to each of the 10 principles contained in the ASX Corporate Governance Council's report.

Principle 1: Lay solid foundations for management and oversight

The Company has not yet formalised and disclosed the functions reserved to the Board and those delegated to management. However, the Company has a small Board of three Directors (two Non-Executive Directors plus an Executive Director) and a small management team, so roles and functions have to be flexible to meet specific requirements.

Principle 2: Structure the Board to add value

The Company currently does not comply with a number of the recommendations within this area as the position of Chairman is separate from Executive Director. The Company does not comply with the recommendation that a majority of directors are independent, because two are substantial shareholders and one is an Executive Director. The Company does not have a Board nomination committee.

Two of the Company's three directors are non-executives, and none of the non-executives have undertaken "material" consultancy work for the Company within the past three years. Each Director of the Company has the right to seek independent professional advice at the expense of the Company. Prior approval of the Chairman is required, but this will not be unreasonably withheld.

Principle 3: Promote ethical and responsible decision-making

The Company has a policy concerning trading in its securities by Directors, management, staff and significant consultants which is set out in the Annual Report. The Company does not have a formal code of conduct, again reflecting the Company's size and the close interaction of individuals throughout the organisation.

Principle 4: Safeguard integrity in financial reporting

The Company is reviewing its procedures to ensure compliance with the recommendations set out under this principle.

Senior management confirms that the financial reports represent a true and fair view and are in accordance with relevant accounting standards. The Chief Executive and Company Secretary state in writing to the Board that the company's financial reports are complete and present a true and fair view, in all material respects, of the financial condition and operational results of the company and Group, and are in accordance with relevant accounting standards.

The Company has an Audit Committee and is reviewing its charter, and the written charter will be approved by the Board.

The Audit Committee consists of the two non-executive Directors, Messrs Elliott and Soper. These directors have the applicable expertise and skills for this Committee. This structure does not meet the ASX's guidance regarding independence, in that it should have a majority of independent directors (Mr Elliott is a substantial shareholder) and have at least three members. The audit committee reports to the Board after each committee meeting. In conjunction with the full board, the committee reviews the performance of the external auditors (including scope and quality of the audit).

Principle 5: Make timely and balanced disclosure

The Company, its Directors and staff are very aware of the NSX's continuous disclosure requirements and operate in an environment where strong emphasis is placed on full and appropriate disclosure to the market. Whilst the Company does not have formal written policies regarding disclosure, it uses strong informal systems underpinned by experienced individuals.

Principle 6: Respect the rights of shareholders

All significant information disclosed to the NSX is posted on the Company's website as soon as it is disclosed to the NSX. When analysts are briefed on aspects of the Group's operations, the material used in the presentation is released to the NSX and posted on the Company's website. Procedures have also been established for reviewing whether any price sensitive information has been inadvertently disclosed, and if so, this information is also immediately released to the market.

Whilst the Company does not have a communications strategy to promote effective communication with shareholders, as it believes this is excessive for small companies, the Company does communicate regularly with shareholders.

The Company has requested the external auditor to attend general meetings.

CORPORATE GOVERNANCE

Principle 7: Recognise and manage risk

The Company is a small exploration company and does not believe that there is significant need for formal policies on risk oversight and management of risk.

Risk management arrangements are the responsibility of the Board of Directors and senior management collectively.

Principle 8: Encourage enhanced performance

The Company does not have a Remuneration Committee and when required, the Board reviews performance matters and remuneration. There has been no formal performance evaluation of the Board during the past financial year, although its composition is reviewed at a Board meeting at least annually. The directors work closely with management and have full access to all the Company's files and records.

Principle 9: Remunerate fairly and responsibly

Directors believe that the size of the Company makes individual salary negotiation more appropriate than formal remuneration policies. The Board will seek independent external advice and market comparisons as necessary. In accordance with Corporations Act requirements, the Company discloses the fees or salaries paid to all Directors, plus the officers actively involved in the management of the Company. The Company has an Employee Share Option Plan.

Principal 10: Recognise the legitimate interests of stakeholders

Due to the Company's size and relative level of operational activity which makes legal compliance a less onerous task than with larger companies, the Company does not have a formal code of conduct to guide compliance with legal and other obligations. The Board of Directors continues to review the situation to determine the most appropriate and effective operational procedures.

Conflict of Interests

The Directors, either as employees of, or consultants to, the Company or through controlled entities connected with them, may provide services to the Company. In accordance with accepted corporate governance practice, the Directors concerned have declared their interests in those transactions with the Company and took no part in decisions relating to them.

Securities Trading and Trading Windows Policy

Directors, employees and key consultants must consult with the Chairman or an Executive Director or the Chief Executive Officer before dealing in Shares of the Company. Purchases or sales in the Company Shares by Directors, employees and key consultants may not be carried out other than in the "window", the window being the period commencing one day following and ending ten days following the date of an announcement of the Company leading, in the opinion of the Board, to an informed market. However, Directors, employees and key consultants are prohibited from buying or selling KSL shares at any time while exploration drilling is being carried out or if they are aware of price sensitive information that has not been made public.

Shareholder Communication

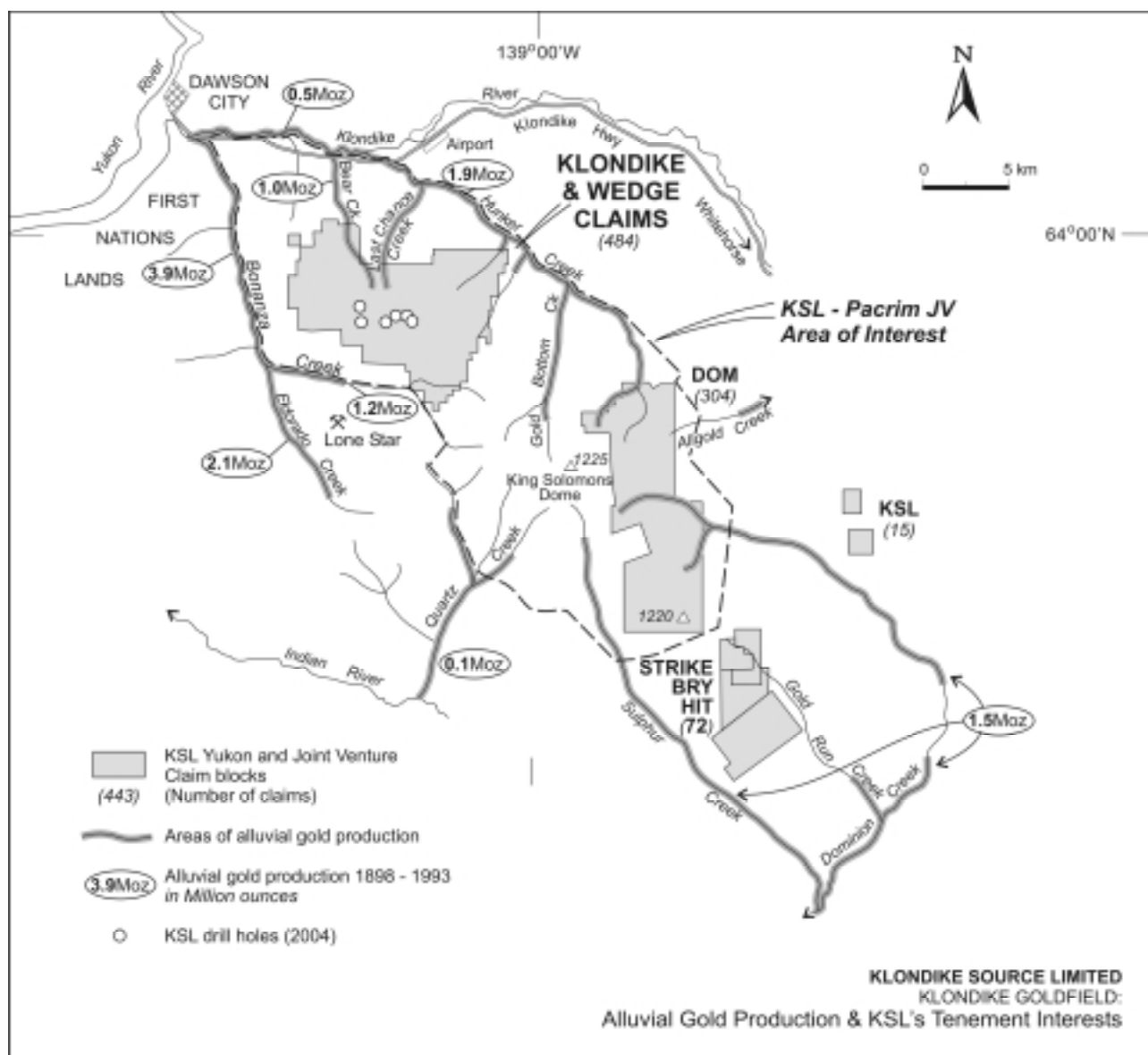
The Directors are keen to ensure that all Shareholders are kept fully informed. All announcements will be available on the Company's web site (www.klondikesource.com.au) after release to NSX.

Community Relations in the Yukon

The Company will respect the legitimate rights and titles of the First Nations people and the concerns of the local communities who are likely to be interested in or affected by the Klondike Source Project. The Canadian Government and the First Nations people of the region have formally agreed as to which area are First Nations lands (Settlement Lands) and which are not. All of the tenements in which KSL has an interest fall outside any Settlement Lands and consequently the Directors do not anticipate any native title concerns. The Company seeks to work constructively and in consultation with interested groups in accordance with Yukon and Canadian law.

Dividend Policy

Any determination as to the payment of dividends by the Company will be at the discretion of the Directors and will depend upon the availability of distributable earnings, the operating results and financial condition of KSL, future capital requirements, general business and financial conditions and other factors considered relevant by the Directors. No assurances in relation to the payment of future dividends, or the franking credits attached to such dividends, can be given to Shareholders.



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Klondike Source Limited

Level 10, 80 Arthur Street, North Sydney, NSW 2060

Telephone: 02 – 9957 3199

Facsimile: 02 – 9954 4011

Email: info@klondikesource.com.au

Website: www.klondikesource.com.au