



A.R.B.N. 082 338 789

**ANNUAL REPORT
2005**

CORPORATE DIRECTORY

Directors

Richard Andrew Payne (Non Executive Chairman)
Robert John Parry (Chief Executive Officer)
Geoffrey David Hann (Chief Financial Officer)
Thomas George Folliard (Non Executive Director)
Trevor Flugge (Non Executive Director)

President

Robert John Parry

Secretary

Geoffrey David Hann

Registered Office in United States

780 North Water Street
City of Milwaukee, Milwaukee County
WISCONSIN USA 53202

Principal Place of Business in United States

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Registered Office in Australia

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AUSTRALIA

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Auditors in Australia

PKF
Level 10, 1 Margaret Street
Sydney NSW 2000
AUSTRALIA

Auditors in United States

S.W. Scampini, S.C
W188 N11707 Maple Road
Germantown,
WISCONSIN USA 53022

Attorneys in United States

Godfrey & Kahn, SC
780 North Water Street
Milwaukee,
WISCONSIN USA 53202

Share Registry

Computershare Registry Services Pty Ltd
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Australian Stock Exchange

ZBB Energy Corporation is a company incorporated in Wisconsin, USA. The Company's shares are listed on the Australian Stock Exchange (Home Exchange is Perth, Western Australia). Trading code is ZBB

Your Directors present their report on the Company and its controlled entities for the financial year ended 30 June 2005.

BOARD OF DIRECTORS

The names and details of the directors of the Company in office during the financial year and until the date of this report are as follows. Directors have been in office since the start of the financial year to the date of this report unless otherwise stated

Richard Andrew Payne (Chairman) B.Juris (Hons), LLB Age 50

Richard Payne is an Australian commercial lawyer and the principal of the legal firm Richard Payne & Associates. Mr Payne has practised in the corporate and commercial areas of law for over 23 years. He has had extensive experience in advising public and private companies and in acting as a director of public and private companies. He is a Director of Australian Ethanol Limited and the Broome International Airport group of companies.

Robert John Parry (Chief Executive Officer) B.Acct. FCPA Age 54

Robert Parry is a Fellow of the Australian Society of Certified Practising Accountants. He was a foundation Director of ZBB (Australia) Ltd, which was the foundation company in 1982 for the ZBB group. He became Managing Director in 1987 and has been the Chief Executive Officer for the group since that date.

Mr Parry has extensive international experience in corporate management, finance and technology acquisition and transfer.

Geoffrey David Hann (Chief Financial Officer and Company Secretary) B.Bus. CPA Age 44

Geoffrey Hann has been Company Secretary and Chief Financial Officer of ZBB Technologies, Ltd. and its subsidiaries since 1992 and has been a director of ZBB since 1998. Mr. Hann holds a Bachelor degree in Business Studies with a triple major in Accounting, Finance and Business Administration from Churchlands College of Advanced Education (Edith Cowen University) in Western Australia. He is an Associate of CPA Australia. Mr. Hann has an extensive financial management background, including four years with the Western Australian power utility, SECWA, where he was specifically responsible for project evaluation and analysis work and as Company Secretary/Finance Director for a Western Australian industrial investment company. Prior to that Mr. Hann spent two years gaining international experience in banking and financial analysis working for the Midland Banking Group in the United Kingdom.

Thomas George Folliard (Non Executive Director) CPA Age 60

Thomas Folliard has been President of Corporate Development Resources, Inc. (Milwaukee, WI) since 1995, a firm that assists middle-market businesses in the areas of financial and business strategy, capital raising, retrenchment, and business acquisitions and divestitures. Prior to founding Corporate Development Resources, Mr. Folliard was a Managing Director of Robert W. Baird & Co. Incorporated ("Baird") (Milwaukee, WI) and was a founder, the President, and a member of the investment committee of Baird Capital Partners, Baird's venture capital activity.

Prior to his employment with Baird in 1989, Mr. Folliard was Vice President of Finance, Treasurer and Controller (CFO) of Bucyrus-Erie Company (South Milwaukee, WI), a NYSE-listed, multi-division manufacturer of mining, aerospace and industrial products. Mr. Folliard, a CPA, received an undergraduate degree from the Wharton School of the University of Pennsylvania, and an MBA from the University of Chicago. He has served as a director of several privately owned, early and later stage growth companies.

Trevor Flugge (Non Executive Director) - Appointed 28 March 2005 AO Age 58

Trevor Flugge is a director of Wesfarmers Limited. He is the Chairman of Australian Wool Services Limited (AWS) and IBT Education Limited, and a member of the Rabobank Food & Agribusiness Advisory Board. He is also a director of AWS subsidiaries TWC Holdings Pty Limited and The Woolmark Company Pty Ltd. He is a past President of the Grains Council of Australia, a past director of the Grains Research and Development Corporation and a former Chairman of AWB Limited. Trevor received the Monash University/Rabobank Agribusiness Leader of the Year award in 1998 and in 1997 was awarded the Farrer Memorial Medal for his contribution to agriculture.

PRINCIPAL ACTIVITIES

The principal activities of the economic entity during the financial year was the development, manufacture and sale of energy storage systems based upon the company's proprietary zinc-bromine battery technology.

OPERATING RESULTS

The consolidated loss of the economic entity for the financial year ended 30 June 2005 was \$2,298,699 (2004: \$4,011,626).

DIVIDENDS

No dividends were paid or declared since the start of the financial year. No recommendation for payment of a dividend has been made.

REVIEW OF OPERATIONS

The most significant event for the Company during the year was the Company's successful Initial Public Offering (IPO) and the subsequent listing of the Company's shares on the Australian Stock Exchange in March 2005. With this change in status of becoming a "listed entity" also comes necessary changes in our reporting requirements as well as other compliance and governance issues. To this effect, long term shareholders will notice a difference in the style of accounting and reporting from previous years.

Upon listing on the ASX the Company appointed a new non-executive director, Mr Trevor Flugge, whose appointment increases the number of non-executive directors to three. Mr Flugge is a very experienced company director who sits on the Boards of a number of prominent Australian public companies and we are fortunate to have his experience available to us at this time. Further additions may be made to the Board in the coming year as the Company continues its expansion program.

During the year the Sydney based accounting firm, PKF, were appointed as auditors to the Company. This move to an Australian based auditor is in line with the Company now adopting Australian accounting and reporting principles in compliance with the rules for ASX listing and ASIC approvals for the issuance of our prospectus as a part of our IPO process. The appointment is also timely as we undertake further changes in our financial reporting requirements with the adoption of International Financial Reporting Standards in the coming year.

The main business activity apart from the IPO process was firmly focussed on the undertaking of our major contract to design and deliver four 500kWh energy storage systems for the California Energy Commission. This contract was barely a month or so old at the start of the year and provided a full twelve months for the design and manufacturing stage to be undertaken prior to the first system being ready for in-house testing towards the end of 2005. New designs were established, new vendors for component supply have been identified and secured adding greater flexibility in our "supply chain" and overall improvements have been successfully incorporated on our manufacturing and assembly lines. The result to date is a radical new configuration for our storage modules and a 25% increase in rated energy from our standard containerised system, from 400kWh to 500kWh. With this new module now firmly locked into production the Company will commence its marketing initiatives based upon this first "utility scale" system. Focus is also presently on the processes for implementing quality control procedures and achieving international product certifications.

Early commercial activity is also being undertaken in China, another rapidly expanding economy with an increasing demand for utility scale power management assets. During the year the Company entered into a joint venture arrangement to commence the process for initial export sales to this region and with the intention of establishing a relationship with an appropriate China based partner to locally source components and sub-assemble modules and with the aim of achieving certain local manufacturing in China as a cost effective alternative for the Company in the future. Initial presentations have been made in China during the year and specific proposals are currently being reviewed. The commercial intent for the Company in this coming year is to secure a contract for the sale of an initial system similar in size and application to the California Energy Commission system. Other commercial opportunities are also now under discussion and evaluation. In the United States recent legislative changes in the State of Texas have been enacted to include "energy storage" technologies in the definition of energy efficiency products and thereby allow for systems such as ZBB's to qualify for cost rebates under that States energy efficiency program. Continued focus on renewable energies also focuses on the role for energy storage as a facilitator for the greater uptake of these generating technologies. ZBB is firmly committed to tailoring its products to meet this market sector. Finally, the increased public awareness of energy matters in general brought about in the main by rising fuel costs, globally, is also having the effect of focussing attention on alternative energy management solutions, of which ZBB's energy storage technology is clearly one gaining attention.

Our financial results for the year saw an improvement in revenues, primarily driven by the effect of the current contract with the California Energy Commission. This was "balanced out" however by the Board's decisions to directly write off or significantly adjust the carrying value of certain intangible items from the previous year's Balance Sheet in accordance with new accounting standards.

The Company has begun the expansion program outlined in its prospectus issued in early 2005. New manufacturing equipment has been ordered, new marketing initiatives have commenced, increases have occurred with staffing levels including certain new key hiring's

The Company is committed to its energy storage business and has a strong belief in its future.

FINANCIAL PERFORMANCE

Profitability

The consolidated loss of the economic entity for the financial year ended 30 June 2005 was \$2,298,699. (2004: \$4,011,626).

Financial Position

Cash on hand at 30 June 2005 for the Economic Entity was \$1,096,752 (2004: \$392,190). Cash on hand at 30 June 2005 for the Parent Entity was \$875,169 (2004: \$137,466).

SIGNIFICANT CHANGES IN STATE OF AFFAIRS

Other than as disclosed elsewhere in this financial report, no significant changes in the state of affairs of the company occurred during the year.

SUBSEQUENT EVENTS

Subsequent to the close of the financial year the Company in July 2005 participated in an international battery convention in China as a first step in marketing its products into this region. A proposal for the introduction of a China based joint venture partner has been submitted to interested parties in that country.

In July 2005, the Company announced that legislative changes made by the State of Texas would enable buyers of the Company's energy storage systems to qualify for "energy efficiency" rebates from the State. Subsequently, the Company has received and is considering a proposal from a Texas based consortium seeking marketing and distribution opportunities for the Company's products. To date no final agreement has been made on this proposal.

FUTURE DEVELOPMENTS, PROSPECTS AND STRATEGIES

The economic entity expects to continue to commercialise its energy storage products and increase the present status and level of operations over the course of the next few years.

ENVIRONMENTAL ISSUES

The company's operations are not regulated by any significant environmental regulation under a law of the Commonwealth or of a State or Territory.

REMUNERATION REPORT

Remuneration of the Non-Executive Directors is approved by the Board and set in aggregate within the maximum amount approved by the shareholders from time to time. The fees have been determined by the Board having regard to industry practice and the need to obtain appropriately qualified independent persons.

Remuneration and terms and conditions of employment for the Executive Directors and Senior Executives are reviewed annually having regard to performance and relative comparative information, and are approved by the Board which may seek independent professional advice, as required. In this respect, consideration is given to normal commercial rates of remuneration for similar levels of responsibility. To 30 June 2005 emoluments comprise salaries and there is not a separate performance-based component.

The aggregate amount of remuneration payable to Non-Executive Directors is currently \$200,000. The following table details the remuneration payable to the Company's Non-Executive Directors commencing from 1 January 2005. At the date of this report none of these Directors fees have been paid.

Name	Salary	Directors Fees	Non-cash Benefits	Bonuses	Profit Share	Super-annuation Payments	Other Termination Payments	Value of Shares and Options Granted	Sign-on Payments
	\$	\$	\$	\$	\$	\$	\$	\$	\$
Richard Payne	-	65,000	-	-	-	-	-	-	-
Thomas Folliard	-	50,000	-	-	-	-	-	-	-
Trevor Flugge	-	50,000	-	-	-	-	-	-	-

The current executive Directors were paid the following remuneration for the financial year to 30 June 2005:

Managing Director, Mr Robert Parry was paid a salary of US\$187,620.

The Finance Director and Company Secretary, Mr Geoffrey Hann was paid a salary of US\$160,000.

Disclosures related to equity instruments

Options provided as remuneration

No options were granted to Directors during the year as part of remuneration packages.

Interests of Directors

At the date of this report the following beneficial and non beneficial interests were held by Directors:

Directors	Ordinary Shares	Listed Options	Unlisted Options
Richard Payne	1,452,500	27,500	516,000
Robert Parry	6,132,000	46,000	-
Geoffrey Hann	660,050	68,700	-
Trevor Flugge	-	-	-
Thomas Folliard	72,000	-	516,000

Listed Options are exercisable at A\$0.50 and expire on 15 December 2007. Unlisted Options are exercisable at prices between US\$0.25 cents and US\$0.33 cents each at varying dates between 1 January 2006 and 31 March 2008.

RELATED PARTY TRANSACTIONS

During the financial year the following related party transactions occurred in addition to the transactions disclosed elsewhere in the financial statements.

Richard Payne & Associates, a legal firm associated with Richard Payne, has provided general legal services to the Company. The Company has paid \$64,715 in fees (inclusive of GST) to Richard Payne & Associates under normal commercial terms and conditions.

By a lease dated 31 October 2001 between the Barrington Street Partnership (in respect of which Robert Parry, Geoffrey Hann and Richard Payne comprise 3 of the 4 partners) as landlord, ZBB Technologies Limited as tenant and the Company as guarantor, as varied by a deed of variation between such parties dated 15 June 2002, the premises at 240 Barrington Street, Bibra Lake, Western Australia are leased by ZBB Technologies Limited for a period of 5 years commencing 1 November 2001. The current rental is \$54,600 per annum based on an independent rental valuation in June 2004. ZBB Technologies Limited has 2 options of renewal, each of 5 years and an option to buy the property at any time during the term or any extended term after 31 July 2006 at the then current market value.

EMPLOYMENT CONTRACTS

Robert Parry has entered into an employment agreement with ZBB to act as Chief Executive Officer for a period expiring on 30 June 2008 on normal commercial terms and conditions and is paid a remuneration package totalling US\$187,620 per annum exclusive of any options granted to him.

If the Company terminates the employment agreement prior to its expiration for any reason other than for cause, the Company must pay the employee his annual remuneration for the greater of 18 months or the remaining term of the agreement and all unvested options shall vest and become immediately exercisable. Subject to the foregoing provision, on the expiration of the term of the agreement, the Company shall pay the employee an amount equal to the employee's annual remuneration for a further period of 18 months in 18 equal consecutive monthly instalments commencing on the date of such expiration.

The employment agreement contains covenants prohibiting the employee competing with the Company during his employment and at any time during 18 months following termination for any reason and a requirement for the employee to keep all information strictly confidential.

Geoffrey Hann has entered into an employment agreement with the Company to act as Chief Financial Officer for a period expiring on 31 December 2005 on normal commercial terms and conditions and is paid a remuneration package totalling US\$160,000 per annum exclusive of any options granted to him.

If the Company terminates the employment agreement prior to its expiration for any reason other than for cause, the Company must pay the employee his annual remuneration for the greater of 18 months or the remaining term of the agreement and all unvested options shall vest and become immediately exercisable. Subject to the foregoing provision,

on the expiration of the term of the agreement, the Company shall pay the employee an amount equal to the employee's annual remuneration for a further period of 18 months in 18 equal consecutive monthly instalments commencing on the date of such expiration.

The employment agreement contains covenants prohibiting the employee competing with the Company during his employment and at any time during 18 months following termination for any reason and a requirement for the employee to keep all information strictly confidential.

EMPLOYEES

The economic entity employed 20 employees as at 30 June 2005.

MEETINGS OF DIRECTORS

During the financial year, 3 Directors meetings and 1 audit committee meeting were held. The number of meetings attended by each Director during the year is as follows:

	DIRECTORS' MEETINGS		AUDIT COMMITTEE MEETINGS	
	Number of Meetings Held While in Office	Number of Meetings Attended While in Office	Number of Meetings Held While in Office	Number of Meetings Attended While in Office
Mr R.A. Payne	3	3	2	2
Mr R.J. Parry	3	3	-	-
Mr G.D. Hann	3	3	2	2
Mr T.G. Folliard	3	3	2	2
Mr T.Flugge	1	1	-	-

NON RELATED PARTY OPTIONS

As at balance date there are 5,361,903 options (1,787,301 pre 1 for 3 split) with an expiry date of 31 January 2006 and an exercise price of A\$0.25 issued and outstanding. These options are not listed.

At 30 June 2005 there are 1,875,000 options with an expiry date of 10 December 2007 and an exercise price of A\$0.50 issued and outstanding. These options are not listed.

At 30 June 2005 there are 3,000,000 options with an expiry date of 15 December 2007 and an exercise price of A\$0.50 issued and outstanding. These options are listed on the ASX.

At 30 June 2005 there are 5,341,000 options with an expiry date of 15 December 2007 and an exercise price of A\$0.25 issued and outstanding. These options are not listed.

PROCEEDINGS ON BEHALF OF COMPANY

No person has applied for leave of Court to bring proceedings on behalf of the Company or intervene in any proceedings to which the Company is a party for the purpose of taking responsibility on behalf of the Company for all or any part of those proceedings.

The Company was not a party to any such proceedings during the year.

NON-AUDIT SERVICES

The Board of Directors, in accordance with advice from the audit committee, is satisfied that the provision of non-audit services during the year is compatible with the general standard of independence for auditors imposed by the Corporations Act 2001. The Directors are satisfied that the services disclosed below did not compromise the external auditor's independence for the following reasons:

- all non-audit services are reviewed and approved by the audit committee prior to commencement to ensure they do not adversely affect the integrity and objectivity of the auditor; and
- the nature of the services provided do not compromise the general principles relating to auditor independence as set out in the Institute of Chartered Accountants in Australia and CPA Australia's Professional Statement F1: Professional Independence.

The following fees for non-audit services were paid/payable to the external auditors during the year ended 30 June 2005:

	\$
Due diligence service	72,970
Technical assistance re accounting principles and financial reports	10,000
	<u>82,970</u>

AUDITOR'S INDEPENDENCE DECLARATION

The lead auditor's independence declaration for the year ended 30 June 2005 has been received and can be found on page 7 of the Directors' Report.

INDEMNIFICATION OF OFFICERS AND DIRECTORS

Due to the high cost, the Company has not taken out any directors and officers insurance. In December 2004 the Company entered into Deeds of Indemnity and Access with persons who are Officers or Directors of the economic entity indemnifying such persons against liability incurred by them in their capacity as an Officer or Director, including costs and expenses of defending legal proceedings and providing them with access to company records where a claim is made or threatened against such Officer or Director.

Signed in accordance with a resolution of the Board of Directors.



Robert John Parry
Director and Chief Executive Officer
Milwaukee, 30 September 2005



Geoffrey David Hann
Director and Chief Financial Officer



Chartered Accountants
& Business Advisers

NSW Partnership
ABN 83 236 985 726

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Sydney NSW 2000

DX 10173 Sydney Stock Exchange NSW

Tel: 61 2 9251 4100

Fax: 61 2 9240 9821

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Liability is limited by the Accountants
Scheme, approved under the
Professional Standards Act 1994 (NSW)

**Lead auditor's independence declaration
Under section 307C of the Corporations Act 2001**

To the Directors of ZBB Energy Corporation

I declare that, to the best of my knowledge and belief, in relation to the audit for the year ended 30 June 2005, there have been:

- i. no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- ii. no contraventions of any applicable code of professional conduct in relation to the audit.

A stylized, handwritten-style logo for PKF, rendered in black ink.

PKF

A handwritten signature in black ink, which appears to read 'Bruce Gordon'.

B R Gordon
Partner

Sydney
Dated: 30 September 2005

CORPORATE GOVERNANCE STATEMENT

Unless disclosed below, all the best practice recommendations of the ASX Corporate Governance Council have been applied for the entire financial year ended 30 June 2005.

Board Composition

The skills, experience and expertise relevant to the position of each Director who is in office at the date of the annual report and their term of office are detailed in the Directors' Report.

The names of independent Directors of the Company are:

Richard Andrew Payne
Thomas George Folliard
Trevor Flugge

When determining whether a non-executive Director is independent the Director must not fail any of the following materiality thresholds:

- less than 10% of company shares are held by the Director and any entity or individual directly or indirectly associated with the Director;
- no sales are made to or purchases made from any entity or individual directly or indirectly associated with the Director; and
- none of the Director's income or the income of an individual or entity - directly or indirectly associated with the Director is derived from a contract with any member of the economic entity other than income derived as a Director of the entity.

Independent Directors have the right to seek independent professional advice at the Company's expense in the furtherance of their duties as Directors. Written approval must be obtained from the Chairman prior to incurring any expense on behalf of the Company.

As the whole Board only consists of five members, the Board carries out the role of Nomination Committee because it is a more efficient mechanism than a separate nomination committee.

Trading Policy

The Company's policy regarding Directors and employees trading in its securities is set by the Board of Directors. The policy restricts Directors and employees from acting on material information until it has been released to the market and adequate time has been given for this to be reflected in the securities' prices.

Audit Committee

The names and qualifications of those appointed to the Audit Committee and their attendance at meetings of the Committee are included in the Directors' Report.

Performance Evaluation

Due to the size and nature of the Company to date, the Board does not conduct an evaluation of its performance.

Remuneration Policies

The remuneration policy, which sets the terms and conditions for the Chief Executive Officer and other senior executives, was developed by the Board. All executives receive a base salary. The remuneration committee reviews executive packages annually by reference to company performance, executive performance, comparable information from industry sectors and other listed companies and independent advice. The performance of executives is measured against criteria which is based on the forecast growth of the Company's profits and shareholders value. The policy is designed to attract the highest calibre executives and reward them for performance which results in long-term growth in shareholder value. Executives are also entitled to participate in the employee share and option arrangements.

The amount of remuneration for all Directors including the two executives, including all monetary and non-monetary components, are detailed in Note 18 to the financial report. All remuneration paid to executives is valued at the cost to the company and expensed. Shares given to executives are valued as the difference between the market price of those shares and the amount paid by the executive. Options are valued using the Black-Scholes methodology.

The Board expects that the remuneration structure implemented will result in the Company being able to attract and retain the best executives to run the economic entity. It will also provide executives with the necessary incentives to work to grow long-term shareholder value.

The payment of bonuses, stock options and other incentive payments are reviewed by the Board annually as part of the review of executive remuneration and a recommendation is put to the Board for approval. All bonuses, options and incentives must be linked to predetermined performance criteria. The Board can exercise its discretion in relation to approving incentives, bonuses and options. Any changes must be justified by reference to measurable performance criteria.

ZBB Energy Corporation ABN 92 082 338 789 and Controlled Entities

STATEMENTS OF FINANCIAL PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2005

	Note	Economic Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
Sales Revenue	2	1,682,261	162,501	1,682,261	104,011
Cost of Sales		(479,647)	(269,259)	(1,682,261)	(104,011)
Gross Profit/(Loss)		1,202,614	(106,758)	-	-
Other Revenue	2	28,685	-	28,446	-
Selling and Administration Expenses		(2,463,708)	(3,350,795)	(803,926)	(2,334,130)
Depreciation and Amortisation Expenses		(314,792)	(335,493)	(2,249)	(846)
Intellectual Property Written-Off		(467,429)	-	-	-
Borrowing Costs Expenses		(284,069)	(218,580)	(193,499)	(185,948)
Loss from Ordinary Activities Before Income Tax		(2,298,699)	(4,011,626)	(971,228)	(2,520,924)
Income Tax Relating to Ordinary Activities	3	-	-	-	-
Loss from Ordinary Activities After Income Tax Expense Attributable to Members of the Parent Entity		(2,298,699)	(4,011,626)	(971,228)	(2,520,924)
Net exchange difference on translation of financial report of self-sustaining foreign operations	16	(518,486)	(302,643)	337,235	-
Total revenues, expenses and valuation adjustments attributable to members of the parent entity and recognised directly in equity		(518,486)	(302,643)	337,235	-
Total changes in equity other than those resulting from transactions with owners as owners		(2,817,185)	(4,314,269)	(633,993)	(2,520,924)
Basic earnings per share (cents per share)	4	(6.8)	(13.0)		
Diluted earnings per share (cents per share)	4	(6.8)	(9.5)		

The accompanying notes form part of these financial statements.

ZBB Energy Corporation ABN 92 082 338 789 and Controlled Entities

STATEMENTS OF FINANCIAL POSITION AS AT 30 JUNE 2005

	Note	Economic Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
CURRENT ASSETS					
Cash assets	5	1,096,752	392,190	875,169	137,466
Receivables	6	46,528	1,361,321	-	4,179,720
Inventories	7	2,854,254	2,940,826	-	-
TOTAL CURRENT ASSETS		3,997,534	4,694,337	875,169	4,317,816
NON-CURRENT ASSETS					
Investments	8	250,000	-	12,596,135	7,797,282
Plant and Equipment	9	539,813	691,837	2,585	3,158
Intangibles	10	2,420,271	2,711,091	-	-
TOTAL NON-CURRENT ASSETS		3,210,084	3,402,928	12,598,720	7,800,440
TOTAL ASSETS		7,207,618	8,097,265	13,473,889	12,117,626
CURRENT LIABILITIES					
Payables	11	207,604	600,352	42,070	1,404,542
Interest bearing liabilities	12	77,071	4,145,192	-	3,113,533
Provisions	13	80,342	1,246,342	8,728	1,181,979
TOTAL CURRENT LIABILITIES		365,017	5,991,886	50,798	5,700,054
NON-CURRENT LIABILITIES					
Interest bearing liabilities	14	-	85,105	-	-
TOTAL NON-CURRENT LIABILITIES		-	85,105	-	-
TOTAL LIABILITIES		365,017	6,076,991	50,798	5,700,054
NET ASSETS		6,842,601	2,020,274	13,423,091	6,417,572
EQUITY					
Contributed Equity	15	26,250,436	18,610,924	26,250,436	18,610,924
Accumulated Losses	16	(16,664,732)	(14,366,033)	(13,036,914)	(12,065,686)
Reserves	16	(2,743,103)	(2,224,617)	209,569	(127,666)
TOTAL EQUITY		6,842,601	2,020,274	13,423,091	6,417,572

The accompanying notes form part of these financial statements.

ZBB Energy Corporation ABN 92 082 338 789 and Controlled Entities

STATEMENTS OF CASH FLOWS FOR THE YEAR ENDED 30 JUNE 2005

	Note	Economic Entity		Parent Entity	
		2005 \$	2004 \$	2005 \$	2004 \$
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers		3,083,626	162,501	5,861,981	104,011
Payments to suppliers and employees		(4,502,103)	(3,612,710)	(5,021,910)	(2,258,733)
Interest received		28,685	-	28,446	-
Borrowing costs		(284,069)	(218,580)	(193,499)	(185,948)
Net cash (used in) operating activities		(1,673,861)	(3,668,789)	675,018	(2,340,670)
CASH FLOWS FROM INVESTING ACTIVITIES					
(Payments) for joint venture equity investment		(250,000)	-	(250,000)	-
Proceeds from sale of plant and equipment		-	13,802	-	-
(Payments) for purchase of plant and equipment		-	-	(1,676)	(4,126)
(Payments) for controlled entities investment		-	-	(4,548,853)	-
(Payments) for purchase of intangibles assets		(339,377)	-	-	-
Net cash (used in) / provided by investing activities		(589,377)	13,802	(4,800,529)	(4,126)
CASH FLOWS FROM FINANCING ACTIVITIES					
Proceeds from issue of shares		9,053,881	2,932,716	9,053,881	2,932,730
Payments for share issue expenses		(1,414,369)	-	(1,414,369)	-
Proceeds from borrowings		-	896,589	-	1,139,330
Repayment of borrowings		(4,153,226)	-	(3,113,533)	(1,739,828)
Net cash provided by financing activities		3,486,286	3,829,305	4,525,979	2,332,232
Net increase / (decrease) in cash held		1,223,048	174,318	400,468	(12,564)
Cash at beginning of financial year		392,190	217,872	137,466	150,031
Effect of exchange rates on cash holdings in foreign currencies		(518,486)	-	337,235	-
Cash at end of financial year	5	1,096,752	392,190	875,169	137,467

The accompanying notes form part of these financial statements.

NOTES TO AND FORMING PART OF THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Accounting

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

The financial statements for the year ended 30 June 2004 were prepared in accordance with the United States Generally Accepted Accounting Policies.

On 23 December 2004 ZBB Energy Corporation issued a Prospectus and was subsequently listed on the Australian Stock Exchange on 30 March 2005.

The Company is now reporting under the Corporations Act 2001 and consequently the financial statements must be prepared in accordance with Australian Accounting Standards. The financial statements for the year ended 30 June 2005, and the comparative information for the year ended 30 June 2004, have been prepared on this basis.

The financial report covers the economic entity of ZBB Energy Corporation and controlled entities, and ZBB Energy Corporation as an individual parent entity. ZBB Energy Corporation is a listed public company, incorporated and domiciled in the United States.

The financial report has been prepared on an accruals basis and is based on historical costs and does not take into account changing money values or, except where stated, current valuations of non-current assets. Cost is based on the fair values of the consideration given in exchange for assets. The financial report has been expressed in Australian dollars, \$A.

The following is a summary of the material accounting policies adopted by the economic entity in the preparation of the financial report. The accounting policies have been consistently applied, unless otherwise stated.

(b) Principles of Consolidation

The consolidated financial statements are those comprising ZBB Energy Corporation and its controlled entities ("ZBBE Group"), which ZBB Energy Corporation controlled from time to time during the reported period. The Corporation is developing an advanced energy storage system.

The financial statements of controlled entities are prepared for the same reporting period as ZBB Energy Corporation using consistent accounting policies. Adjustments are made to bring into line any dissimilar accounting policies which may exist.

All intercompany balances and transactions, and unrealised profits arising from intra-economic entity transactions, have been eliminated in full.

(c) Income Tax

The ZBBE Group adopts the liability method of tax-effect accounting whereby the income tax expense is based on the profit from ordinary activities adjusted for any permanent differences.

Timing differences, which arise due to the different accounting periods in which items of revenue and expense are included in the determination of pre-tax accounting profit and taxable income, are brought to account as either a provision for deferred income tax or an asset described as a future income tax benefit at the rate of income tax applicable to the period in which the benefit will be received or the liability will become payable.

The amount of benefits brought to account or which may be realised in the future is based on the assumptions that no adverse changes will occur in income taxation legislation and the anticipation that the ZBBE Group will derive sufficient future assessable income to enable the benefit to be realised and comply with the conditions of deductibility imposed by the law.

A future income tax benefit is only carried forward as an asset where realisation of the benefit can be regarded as being assured beyond reasonable doubt.

(d) Plant and Equipment

Each class of Plant and equipment is carried at cost or fair value less, where applicable, any accumulated depreciation. The carrying amount of plant and equipment is reviewed annually by Directors to ensure it is not in excess of the recoverable amount from these assets. The recoverable amount is assessed on the basis of the expected net cash flows, which will be received from the assets' employment and subsequent disposal. The expected net cash flows have not been discounted to their present values in determining recoverable amounts.

Depreciation

Depreciation is provided on all fixed assets. The depreciable amount of all fixed assets is depreciated on a straight line basis over their useful lives to the ZBBE Group commencing from the time the asset is held ready for use.

The depreciation rates used for each class of depreciable assets are:

Class of Fixed Asset	Depreciation Rate
Plant and Equipment	2 – 10 years
Office Equipment	3 – 8 years

(e) Foreign Currencies

Translation of foreign currencies

Transactions in foreign currencies are converted to local currency.

Amounts payable to and by the entities controlled by ZBB Energy Corporation that are outstanding at the balance date and are denominated in foreign currencies have been converted to local currency using rates of exchange ruling at the end of the financial year.

Translation of financial reports of overseas operations

All overseas operations are deemed self-sustaining as each is financially and operationally independent of ZBB Energy Corporation. The financial reports of overseas operations are translated using the current rate method and any exchange differences are taken directly to the foreign currency translation reserve.

(f) Leases

A distinction is made between finance leases which effectively transfer from the lessor to the lessee substantially all the risks and benefits incidental to ownership of leased non-current assets, and operating leases under which the lessor effectively retains substantially all such risks and benefits.

Finance leases are capitalized. A leased asset and liability is established at the present value of minimum lease payments. Lease payments are allocated between the principal component of the lease liability and the interest expense.

Leased assets are amortised on a straight line basis over the term of the lease, or where it is likely that the ZBBE Group will obtain ownership of the asset, the life of the asset. Leased assets held at the reporting date are being amortised over periods ranging from 3 to 22 years.

Lease payments for operating leases, where substantially all the risks and benefits remain with the lessor, are charged as expenses in the periods in which they are incurred.

(g) Investments

Non-current investments are measured on the cost basis. The carrying amount of non-current investments is reviewed annually by Directors to ensure it is not in excess of the recoverable amount of these investments. The recoverable amount is assessed from the quoted market value for listed investments or the underlying net assets for other non-listed investments.

The expected net cash flows from investments have not been discounted to their present value in determining the recoverable amounts.

Interests in Joint Ventures

The economic entity's share of the assets, liabilities, revenues and expenses of joint venture operations are included in the appropriate items of the consolidated Statements of Financial Performance and Financial Position. Details of the economic entity's interests are shown in Note 8.

The economic entity's interests in joint venture entities are brought to account using the equity method of accounting in the consolidated financial statements. The parent entity's interests in joint venture entities are brought to account using the cost method.

(h) Intangibles

Prototype and Development Costs

Certain prototype and development costs relating to the ZBBE Group's flow and non flow technology are capitalised and are amortised over the period during which benefits are expected to be received. This is taken as being 20 years.

Goodwill

Goodwill represents the excess of the purchase consideration over the fair value of identifiable net assets acquired at the time of acquisition of a business or shares in a controlled entity.

Goodwill is amortised by the straight line method over the period during which benefits are expected to be received or written off when the benefits are no longer expected to be received. This is taken as being 20 years.

(i) Cash

For the purposes of the Statement of Cash Flows, cash includes cash at bank and deposits at call which are readily available to cash on hand, and are subject to an insignificant risk of change in value, net of outstanding bank overdrafts.

(j) Inventories

Inventories are valued at the lower of cost and net realisable value.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

- Raw materials – purchase cost of direct material
- Finished goods and work-in-progress – purchase cost of direct material plus direct labour plus a proportion of manufacturing overheads.

The ZBBE Group has a policy of installing test units on site at prospective customers. These units can be installed in some cases exceeding one year. As it is the ZBBE Group's intention that these units be sold to these customers or "returned" to stock they are included as inventories.

(k) Revenue Recognition

Revenue relating to contract sales is recognised in proportion to the work performed.

(l) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office. In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense. Receivables and payables in the Statement of Financial Position are shown inclusive of GST.

(m) Employee entitlements

Wages, salaries and annual leave

Liabilities for wages, salaries and annual leave are recognised, and are measured as the amount unpaid at the reporting date at current pay rates in respect of employees' services up to that date.

Economic Entity		Parent Entity	
2005	2004	2005	2004
\$	\$	\$	\$

NOTE 2 - PROFIT FROM ORDINARY ACTIVITIES

The following revenue and expense items are relevant in explaining the financial performance for the period:

(a) Operating Revenue

Sales revenue	1,682,261	162,501	1,682,261	104,011
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(b) Other Revenue

Interest received from other persons	28,685	-	28,446	-
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(c) Expenses

Cost of sales	479,647	269,259	1,682,261	104,011
Amortisation of goodwill	74,015	74,015	-	-
Amortisation of prototype and development costs	88,753	88,753	-	-
Write-off of Intellectual Property	467,429	-	-	-
Depreciation	152,024	172,725	2,249	846
Borrowing costs	284,069	218,580	193,499	185,948

NOTE 3 - INCOME TAX

The *prima facie* tax on the loss from ordinary activities before income tax is reconciled to the income tax expense in the accounts as follows:

Prima facie tax benefit on the loss from ordinary activities before income tax at 30% (2004:32.71%)

	689,610	1,312,203	291,368	824,594
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Less:

Tax effect of permanent differences:

Non-deductible amortisation	(48,776)	-	-	-
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Timing differences and tax losses not brought to account as future income tax benefits

	(640,834)	(1,312,203)	(291,368)	(824,594)
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The taxation benefits will only be obtained if:

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

Tax losses at 30%	5,174,318	4,484,708	3,474,817	3,183,449
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	Economic Entity		Parent Entity	
	2005 \$	2004 \$	2005 \$	2004 \$
NOTE 4 - EARNINGS PER SHARE				
Earnings used in the calculation of basic EPS	(2,298,699)	(2,699,423)		
Earnings used in the calculation of dilutive EPS	(2,298,699)	(2,699,423)		
Weighted average number of ordinary shares outstanding during the year used in calculation of basic EPS	34,121,936	20,741,542		
Options	-	240,000		
Convertible notes	-	7,500,000		
Weighted average number of ordinary shares outstanding during the year used in calculation of dilutive EPS	34,121,936	28,481,542		

NOTE 5 - RECONCILIATION OF CASH AT THE END OF THE YEAR

Reconciliation of cash at the end of the year (as shown in the Statements of Cash Flows) to the related items in the accounts is as follows:

Cash on hand and at bank	1,096,752	392,190	875,169	137,466
Deposits at call	-	-	-	-
	1,096,752	392,190	875,169	137,466

NOTE 6 - RECEIVABLES

Amounts Receivable from Third Parties	46,528	1,361,321	-	1,361,321
Amounts Receivable from Controlled Entities	-	-	-	2,818,399
	46,528	1,361,321	-	4,179,720

NOTE 7 - INVENTORIES

Raw materials - at cost	402,980	259,453	-	-
Work in progress - at cost	46,920	39,014	-	-
Finished goods - at cost	2,404,354	2,642,359	-	-
	2,854,254	2,940,826	-	-

NOTE 8 - INVESTMENTS

Investment in Joint Venture Company	250,000	-	250,000	-
Investment in Controlled Entities	-	-	12,346,135	7,797,282
	250,000	-	12,596,135	7,797,282

Investment in controlled entities comprises:

	Country of incorporation	Beneficial percentage held by economic entity	
		2005 %	2004 %
Parent Entity:			
ZBB Energy Corporation	United States		
Subsidiaries of ZBB Energy Corporation:			
ZBB Technologies, Ltd			
- ordinary shares	Australia	100	100
ZBB Technologies, Inc			
- ordinary shares	United States	100	100

Overseas controlled entities carry on business in the country of incorporation.

Investment in Joint Venture Company

On 30 March 2005 ZBB Energy Corporation announced it had agreed to set up a joint venture company to take its highly-advanced electricity storage for power utilities and renewable energy generators into the Chinese market.

ZBB China Pty Ltd was incorporated with an initial capital of \$510,000 with ZBB Energy Corporation holding 49% of the issued equity with the balance being held by China Century Group Ltd – a newly formed Australian company investing in high growth areas of the Chinese economy. The voting power held by ZBB Energy Corporation is 49%.

Under the joint venture agreement, ZBB China Pty Ltd is being granted an exclusive licence to sell ZBB Energy Corporation's zinc-bromine batteries in China, Macau and Hong Kong subject to ZBB China Pty Ltd achieving the following annual sales objectives on a take or pay basis:

- i) 2 MWh being 4 x 500 kWh (each of 10 x 50 kWh modules) for delivery and installation as initial commercial test units before June 30, 2006.
- ii) 10 MWh (200 x 50 kWh modules) before June 30, 2007.
- iii) 25 MWh (500 x 50 kWh modules) before June 30, 2008.
- iv) 60 MWh (1200 x 50 kWh modules) before June 30, 2009.

At ZBB Energy Corporation's current sales price of US\$400 per kWh the sales targets represent a potential US\$38 million of sales revenue to ZBB Energy Corporation. In the event that ZBB China Pty Ltd is unable to meet these annual sales volumes then the license becomes non-exclusive.

	Economic Entity		Parent Entity	
	2005 \$	2004 \$	2005 \$	2004 \$
Retained earnings attributable to interest in joint venture	-	-	-	-
Reserves attributable to interest in joint venture	-	-	-	-
Share of joint venture entity's results and financial position				
Current Assets	119,060	-	119,060	-
Profit from ordinary activities after income tax expense	-	-	-	-

NOTE 9 - PLANT AND EQUIPMENT

Plant and equipment - at cost	2,273,556	2,273,556	5,680	4,004
Provision for depreciation	(1,733,743)	(1,581,719)	(3,095)	(846)
	<u>539,813</u>	<u>691,837</u>	<u>2,585</u>	<u>3,158</u>
Movements in Carrying Amounts				
Economic Entity:				
Balance at the beginning of the financial year	691,837	864,562	3,158	-
Additions	-	-	1,676	4,004
Disposals	-	-	-	-
Depreciation expense	(152,024)	(172,725)	(2,249)	(846)
Carrying amount at the end of the year	<u>539,813</u>	<u>691,837</u>	<u>2,585</u>	<u>3,158</u>

	Economic Entity		Parent Entity	
	2005 \$	2004 \$	2005 \$	2004 \$
NOTE 10 - INTANGIBLES				
Goodwill	1,480,296	1,480,296	-	-
Provision for amortisation	(800,023)	(726,008)	-	-
	<u>680,273</u>	<u>754,288</u>	-	-
Prototype and development costs	2,183,043	1,771,455	-	-
Provision for amortisation	(443,045)	(354,292)	-	-
	<u>1,739,998</u>	<u>1,417,163</u>	-	-
License fee	-	10,000	-	-
Patents and trademarks	-	457,429	-	-
		<u>467,429</u>		
	<u>2,420,271</u>	<u>2,711,091</u>	-	-

NOTE 11 - ACCOUNTS PAYABLE

Trade creditors	<u>207,604</u>	<u>600,352</u>	<u>42,070</u>	<u>1,404,542</u>
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NOTE 12 - BORROWINGS

Equipment leases (i)	77,071	196,646	-	-
Bank overdrafts (ii)	-	204,246	-	-
Line of credit (iii)	-	630,767	-	-
Project financing (iv)	-	1,134,533	-	1,134,533
Convertible notes (v)	-	1,979,000	-	1,979,000
	<u>77,071</u>	<u>4,145,192</u>	-	<u>3,113,533</u>

(i) The equipment leases are secured by a charge over the manufacturing equipment. The rates are from 5 – 6%, with the final payment due in April 2006.

(ii) The bank overdraft security was in the form of a First Registered Mortgage Debenture over the whole of the assets and undertakings at ZBB Technologies Limited including uncalled capital, if any. The interest was National Australia Bank's Base Lending Rate plus 3.5%.

(iii) The line of credit was secured over the inventory of ZBB Technologies Inc. with maturity on 31 March 2005. The interest rate was 7%.

(iv) The project financing borrowings are secured over the accounts receivable and proceeds from inventory of ZBB Technologies Inc. Accounts receivable relating to these borrowings is \$1,227,343 and is disclosed as trade debtors.

(v) The convertible notes carried an interest rate of 10% but were converted into ordinary shares on 30 March 2005.

NOTE 13 - PROVISIONS

Unearned revenue	-	1,116,603	-	1,116,603
Employee entitlements	80,342	129,739	8,728	65,376
	<u>80,342</u>	<u>1,246,342</u>	<u>8,728</u>	<u>1,181,979</u>

NOTE 14 - BORROWINGS

Equipment leases	-	85,105	-	-
	<u>-</u>	<u>85,105</u>	<u>-</u>	<u>-</u>

NOTE 15 – CONTRIBUTED EQUITY

At balance date there are 150,000,000 authorised shares in the Company with 81,964,626 issued.

Category of Securities	Total Number	Number Quoted	Issue price per security \$	Amount paid \$
Opening balance	20,741,542	Nil		18,610,924
1 for 3 share split	62,224,626	57,557,657		-
Existing options exercised into ordinary new shares	240,000	191,040	0.23	53,881
Ordinary new shares issued by Initial Public Offering	12,000,000	12,000,000	0.50	6,000,000
Ordinary new shares issued on conversion of convertible notes	7,500,000	7,500,000	0.40	3,000,000
Transaction costs arising from placement of shares				(1,414,369)
Total Ordinary Shares	<u>81,964,626</u>	<u>77,248,697</u>		<u>26,250,436</u>

EMPLOYEE/DIRECTOR OPTION PLANS

In 1998 the Company entered into a Key Employees Stock Option Plan (KESOP) whereby a stock option committee comprising three Directors were given the discretion to grant up to 4,800,000 (1,600,000 pre 1 for 3 split) options to key employees of the Company. At 30 June 2005 all 1,600,000 KESOP options had been granted. During the period ended 30 June 2005, no KESOP options were exercised in accordance with their terms and conditions. At 30 June 2005 there remains 255,000 KESOP options with exercise prices of US\$0.50 and exercise dates between 15 March 2006 and 15 March 2008 outstanding.

In 1999 the Company entered into an Outside (Non-Executive) Directors Stock Option Plan (ODSOP) whereby 1,200,000 (400,000 pre 1 for 3 split) options were issued to Non-Executive Directors over a five year period commencing on 2 January 1999. At 30 June 2003, all ODSOP options had been granted. During the period ended 30 June 2005, 240,000 ODSOP options were exercised at US\$0.25 each in accordance with their terms and conditions. At 30 June 2005 there remains 720,000 ODSOP options with prices of US\$0.25 and exercise dates between 2 January 2006 and 2 January 2008 outstanding.

In 2002 the Company established the Company's 2002 Stock Option Plan whereby a stock option committee comprising all Directors was given the discretion to grant up to 10,500,000 (3,500,000 pre 1 for 3 split) options to key employees of the Company at exercise prices to be determined (but in any case not less than US\$0.33 per share) and exercisable at times to be determined by the Company commencing from 1 July 2007. During the period ended 30 June 2005 no 2002 SOP options were exercised in accordance with their terms and conditions. At 30 June 2005 there remains 3,646,867 options with exercise prices of not less than US\$0.33 and exercise dates up to 31 March 2008 outstanding and a further 3,284,627 available to be issued.

During the 2005 financial year the Company established an Employee Option Scheme whereby at the discretion of the Board of the Company, options may be granted to employees and Directors of the Company or any company related to it. The maximum number of options that may be granted in aggregate at any time under this option scheme or under any other employee option or share plan is the number equivalent to 5% of the total number of shares on issue in the Company (as if all options issued under any employee or executive option scheme had been exercised). The options will not be listed nor are they transferable. At the date hereof no options have been issued under this option scheme. Options shall expire 5 years after they are vested in the holder. The exercise price for options issued under this scheme shall be an amount determined by Directors provided that whilst the Company is on the official list of the ASX in no event shall the exercise price be a price less than 10% higher than the weighted average market price for shares on ASX over the last 20 days on which sales in shares were recorded on ASX immediately preceding the date of grant of the option.

NON RELATED PARTY OPTIONS

As at balance date there are 5,361,903 options (1,787,301 pre 1 for 3 split) with an expiry date of 31 January 2006 and an exercise price of A\$0.25 issued and outstanding. These options are not listed.

At 30 June 2005 there are 1,875,000 options with an expiry date of 10 December 2007 and an exercise price of A\$0.50 issued and outstanding. These options are not listed.

At 30 June 2005 there are 3,000,000 options with an expiry date of 15 December 2007 and an exercise price of A\$0.50 issued and outstanding. These options are listed on the ASX.

At 30 June 2005 there are 5,341,000 options with an expiry date of 15 December 2007 and an exercise price of A\$0.50 issued and outstanding. These options are not listed.

	Economic Entity		Parent Entity	
	2005 \$	2004 \$	2005 \$	2004 \$
NOTE 16 - ACCUMULATED LOSSES AND RESERVES				
Accumulated Losses				
Accumulated losses at the beginning of the financial year	(14,366,033)	(6,687,125)	(12,065,686)	(9,544,762)
Net loss attributable to members	(2,298,699)	(4,011,626)	(971,228)	(2,520,924)
Increase in accumulated losses on transition of US GAAP to Australian GAAP	-	(3,667,282)	-	-
Accumulated losses at the end of the year	<u>(16,664,732)</u>	<u>(14,366,033)</u>	<u>(13,036,914)</u>	<u>(12,065,686)</u>
Reserves – Foreign Currency Translation				
Balance at the beginning of the financial year	(2,224,617)	(1,921,974)	(127,666)	(127,666)
Translation differences during the year	(518,486)	(302,643)	337,235	-
Reserves at end of the year	<u>(2,743,103)</u>	<u>(2,224,617)</u>	<u>209,569</u>	<u>(127,666)</u>

The foreign currency translation reserve records exchange differences arising on translation of a foreign controlled subsidiary.

NOTE 17 – CAPITAL AND LEASING COMMITMENTS

OPERATING LEASES

The Company has a lease for premises in Menomonee Falls, Wisconsin that expires on 31 January 2007. The Company also has a lease for premises in Bibra Lake, Western Australia that expires on 31 October 2006.

Future minimum payments due under operating leases are:

- not later than 1 year	250,653
- later than 1 year but not later than 5 years	133,948
	<u>384,601</u>

FINANCE LEASES

The Company leased US\$514,000 of equipment during the year ended 30 June 2002.

Future minimum payments due under capital leases are:

- not later than one year	77,071
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NOTE 18 - REMUNERATION OF SPECIFIED DIRECTORS AND SPECIFIED EXECUTIVES

Determination of remuneration of specified Directors

Remuneration of the Non-Executive Directors is approved by the Board and set in aggregate within the maximum amount approved by the shareholders from time to time. The fees have been determined by the Board having regard to industry practice and the need to obtain appropriately qualified independent persons.

Remuneration and terms and conditions of employment for the Executive Directors and Senior Executives are reviewed annually having regard to performance and relative comparative information, and are approved by the Board which may seek independent professional advice, as required. In this respect, consideration is given to normal commercial rates of remuneration for similar levels of responsibility. To 30 June 2005 emoluments comprise salaries and there is not a separate performance-based component.

The aggregate amount of remuneration payable to Non-Executive Directors is currently \$200,000. The following table details the remuneration payable to the Company's Non-Executive Directors commencing from 1 January 2005. At the date of this report none of these Directors fees have been paid.

Name	Salary	Directors Fees	Non-cash Benefits	Bonuses	Profit Share	Super-annuation Payments	Other Termination Retirement Payments	Value of Shares and Options Granted	Sign-on Payments
	\$	\$	\$	\$	\$	\$	\$	\$	\$
Richard Payne	-	65,000	-	-	-	-	-	-	-
Thomas Folliard	-	50,000	-	-	-	-	-	-	-
Trevor Flugge	-	50,000	-	-	-	-	-	-	-

The current executive Directors were paid the following remuneration for the financial year to 30 June 2005:

Managing Director, Mr Robert Parry was paid a salary of US\$187,620.

The Finance Director and Company Secretary, Mr Geoffrey Hann was paid a salary of US\$160,000.

Disclosures related to equity instruments

Options provided as remuneration

No options were granted to Directors during the year as part of remuneration packages.

Interests of Directors

At the date of this report the following beneficial and non beneficial interests were held by Directors:

Directors	Ordinary Shares	Listed Options	Unlisted Options
Richard Payne	1,452,500	27,500	516,000
Robert Parry	6,132,000	46,000	-
Geoffrey Hann	660,050	68,700	-
Trevor Flugge	-	-	-
Thomas Folliard	72,000	-	516,000

Listed Options are exercisable at A\$0.50 and expire on 15 December 2007. Unlisted Options are exercisable at prices between US\$0.25 cents and US\$0.33 cents each at varying dates between 1 January 2006 and 31 March 2008.

RELATED PARTY TRANSACTIONS

During the financial year the following related party transactions occurred in addition to the transactions disclosed elsewhere in the financial statements.

Richard Payne & Associates, a legal firm associated with Richard Payne, has provided general legal services to the Company. The Company has paid \$64,715 in fees (inclusive of GST) to Richard Payne & Associates under normal commercial terms and conditions.

By a lease dated 31 October 2001 between the Barrington Street Partnership (in respect of which Robert Parry, Geoffrey Hann and Richard Payne comprise 3 of the 4 partners) as landlord, ZBB Technologies Limited as tenant and

the Company as guarantor, as varied by a deed of variation between such parties dated 15 June 2002, the premises at 240 Barrington Street, Bibra Lake, Western Australia are leased by ZBB Technologies Limited for a period of 5 years commencing 1 November 2001. The current rental is \$54,600 per annum based on an independent rental valuation in June 2004. ZBB Technologies Limited has 2 options of renewal, each of 5 years and an option to buy the property at any time during the term or any extended term after 31 July 2006 at the then current market value.

EMPLOYMENT CONTRACTS

Robert Parry has entered into an employment agreement with the Company to act as Chief Executive Officer for a period expiring on 30 June 2008 on normal commercial terms and conditions and is paid a remuneration package totalling US\$187,620 per annum exclusive of any options granted to him.

If the Company terminates the employment agreement prior to its expiration for any reason other than for cause, the Company must pay the employee his annual remuneration for the greater of 18 months or the remaining term of the agreement and all unvested options shall vest and become immediately exercisable. Subject to the foregoing provision, on the expiration of the term of the agreement, the Company shall pay the employee an amount equal to the employee's annual remuneration for a further period of 18 months in 18 equal consecutive monthly instalments commencing on the date of such expiration.

The employment agreement contains covenants prohibiting the employee competing with the Company during his employment and at any time during 18 months following termination for any reason and a requirement for the employee to keep all information strictly confidential.

Geoffrey Hann has entered into an employment agreement with the Company to act as Chief Financial Officer for a period expiring on 31 December 2005 on normal commercial terms and conditions and is paid a remuneration package totalling US\$160,000 per annum exclusive of any options granted to him.

If the Company terminates the employment agreement prior to its expiration for any reason other than for cause, the Company must pay the employee his annual remuneration for the greater of 18 months or the remaining term of the agreement and all unvested options shall vest and become immediately exercisable. Subject to the foregoing provision, on the expiration of the term of the agreement, the Company shall pay the employee an amount equal to the employee's annual remuneration for a further period of 18 months in 18 equal consecutive monthly instalments commencing on the date of such expiration.

The employment agreement contains covenants prohibiting the employee competing with the Company during his employment and at any time during 18 months following termination for any reason and a requirement for the employee to keep all information strictly confidential.

NOTE 19 - SEGMENT REPORTING

ZBB Energy Corporation operated predominantly in the research, development and commercialisation of zinc bromine battery technology in Australia and the United States of America.

Primary Reporting – Geographical Segments

Geographical Segments	Australia		United States		Elimination		Consolidation	
	2005	2004	2005	2004	2005	2004	2005	2004
Sales to customers outside the economic entity	-	61,476	1,682,261	101,025	-	-	1,682,261	162,501
Intersegment sales	-	-	-	-	-	-	-	-
	-	61,476	1,682,261	101,025	-	-	1,682,261	162,501
Segment result	(3,069,989)	(3,332,652)	(910,971)	(841,475)	-	-	(3,980,960)	(4,174,127)
Economic entity's loss							(2,298,699)	(4,011,626)
Segment assets	4,719,243	1,010,137	2,123,358	1,010,137	-	-	6,842,601	2,020,274

NOTE 20 - FINANCIAL INSTRUMENTS

(a) Interest Rate Risk

ZBB Energy Corporation's exposure to interest rate risk, which is the risk that a financial instrument's value will fluctuate as a result of change in the market, interest rate and the effective weighted average interest rate on these financial assets, is as follows:

	Non Interest Bearing \$	2005 Weighted Average Effective Interest Rate %	Floating Interest Rate \$	Non Interest Bearing \$	2004 Weighted Average Effective Interest Rate %	Floating Interest Rate \$
<i>Economic Entity</i>						
Financial Assets						
- Cash	1,096,752		-	392,190		-
- Trade debtors	46,528		-	1,361,321		-
Total Financial Assets	1,143,280		-	1,753,511		-
Financial Liabilities						
- Bank overdraft	-		-	-	13.10	204,246
- Bank lines of credit	-		-	-	7.00	630,767
- Trade creditors and accruals	207,604		-	600,352		-
- Equipment leases	-	8.00	77,071	-	8.00	281,751
- Provisions	80,342		-	1,246,342		-
- Project financing	-		-	-	2.00	1,134,533
- Convertible Notes	-		-	-	10.00	1,979,000
Total Financial Liabilities	287,946		77,071	1,846,694		4,230,297
<i>Parent Entity</i>						
Financial Assets						
- Cash	875,169		-	137,466		-
- Trade debtors	-		-	4,179,720		-
Total Financial Assets	875,169		-	4,317,816		-
Financial Liabilities						
- Trade creditors and accruals	42,070		-	1,404,542		-
- Provisions	8,728		-	1,181,979		-
- Project financing	-		-	-	2.00	1,134,533
- Convertible Notes	-		-	-	10.00	1,979,000
Total Financial Liabilities	50,798		-	2,586,521		3,113,533

ZBB Energy Corporation's accounting policies, including the terms and conditions of each class of financial asset, financial liability and equity instrument, both recognised and unrecognised in the balance sheet are as follows:

Financial Assets

- Trade debtors
Trade debtors are carried at nominal amounts due less any provision for doubtful debts. A provision for doubtful debts is recognised when collection of the full nominal amount is no longer probable.

Financial Liabilities

- Bank Lines of Credit
The bank lines of credit were carried at the principal amount. Interest was charged as an expense as it accrued.
- Trade Creditors and Accruals
Liabilities are recognised for amounts to be paid in future for goods and services received, whether or not billed to ZBB Energy Corporation.

(b) Credit Risk

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date, to recognise financial assets is the carrying amount net of any provisions for doubtful debts, as disclosed in the balance sheet and notes to and forming part of the consolidated financial statements.

ZBB Energy Corporation does not have any material credit risk exposure to any single debtor or group of debtors under financial instruments entered into by it.

(c) Net Fair Values

For assets and other liabilities the net fair value approximates their carrying value. ZBB Energy Corporation has no financial assets or liabilities that are readily traded on organised markets at balance date and has no financial assets where the carrying amount exceeds net fair values at balance date.

The aggregate net fair values and carrying amounts of financial assets and financial liabilities are disclosed in the balance sheet and in the notes to and forming part of the consolidated financial statements.

Economic Entity		Parent Entity	
2005	2004	2005	2004
\$	\$	\$	\$

NOTE 21- AUDITORS' REMUNERATION

Remuneration of the auditor of the parent entity for:

- auditing or reviewing the financial report	47,500	41,302	47,500	34,614
- other services	82,970	767	82,970	-
- other services provided by related practice of auditor	-	-	-	-
	<u>130,470</u>	<u>42,069</u>	<u>130,470</u>	<u>34,614</u>

NOTE 22- CASH FLOW INFORMATION

Reconciliation of cash flow from operations with loss from ordinary activities after income tax

Operating loss from ordinary activities after related income tax	(2,298,699)	(2,699,243)	(971,228)	(2,520,924)
Depreciation	152,024	172,725	2,249	846
Amortisation	630,197	162,588	-	-
Decrease/(increase) in receivables	1,314,793	(37,431)	4,179,720	(2,361,011)
Decrease/(increase) in stock and WIP	86,572	(30,572)	-	-
(Decrease)/increase in payables	(392,748)	173,273	(1,362,472)	1,358,439
(Decrease) in other creditors	-	(97,925)	-	-
(Decrease)/increase in provisions	(1,166,000)	(1,312,203)	(1,173,251)	1,181,979
Net cash (outflow)/Inflow from operating activities	<u>(1,673,861)</u>	<u>(3,668,788)</u>	<u>675,018</u>	<u>(2,340,671)</u>

NOTE 23 - SUBSEQUENT EVENTS

Subsequent to the close of the financial year the Company in July 2005 participated in an international battery convention in China as a first step in marketing its products into this region. A proposal for the introduction of a China based joint venture partner has been submitted to interested parties in that country.

In July 2005 the Company announced that legislative changes made by the State of Texas would enable buyers of the Company's energy storage systems to qualify for "energy efficiency" rebates from the State. Subsequently, the Company has received and is considering a proposal from a Texas based consortium seeking marketing and distribution opportunities for the Company's products. To date no final agreement has been made on this proposal.

NOTE 24 - ADOPTION OF AUSTRALIAN EQUIVALENTS TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

The Company is preparing and managing the transition to Australian Equivalents to International Financial Reporting Standards (AIFRS) effective for the financial years commencing from 1 January 2005. The adoption of AIFRS will be reflected in the Company's financial statements for year ended 30 June 2006. On first time adoption of AIFRS, comparatives for the financial year ended 30 June 2005 are required to be restated. The majority of the AIFRS transitional adjustments will be made retrospectively against retained earnings at 1 July 2004.

The Company's management, with the assistance of external consultants, has assessed the significance of the expected changes and is preparing for their implementation. The impact of the alternative treatments and elections under AASB 1: First Time Adoption of Australian Equivalents to International Financial Reporting Standards has been considered where applicable.

Set out below are the key areas where accounting policies are expected to change on adoption of AIFRS and the best estimate of the quantitative impact of the changes on total equity as at the date of transition and 30 June 2005 and on net loss for the year ended 30 June 2005.

The figures disclosed are management's best estimates of the quantitative impact of the changes as at the date of preparing the 30 June 2005 financial report. The actual effects of transition to AIFRS may differ from the estimates disclosed due to:

- (i) ongoing work being undertaken by the AIFRS project team;
- (ii) potential amendments to AIFRSs and Interpretations thereof being issued by the standard-setters and IFRIC; and
- (iii) emerging accepted practice in the interpretation and application of AIFRS and UIG Interpretations.

Under AASB 2 "Share-based Payments", ZBB Energy Corporation would recognise the fair value of options granted to employees as remuneration as an expense on a pro-rata basis over the vesting period in the Income Statement with a corresponding adjustment to equity. Share-based payment costs are not recognised under AGAAP. Under AASB 1 first-time adoption of Australian equivalent to International Financial Reporting Standards, options granted prior to 7 November 2002 and also options granted and vested prior to 1 January 2005 are not subject to the requirements of AASB 2.

If applied in the current year the impact would have been an expense of \$11,803.

Under AASB 3 "Business Combinations", goodwill is not permitted to be amortised but instead is subject to impairment testing on an annual basis or upon the occurrence of triggers which may indicate a potential impairment. Currently goodwill arising on consolidation is amortised over 20 years. ZBB Energy Corporation has elected not to apply AASB 3 retrospectively to the acquisitions of its subsidiaries and as a result has not written back prior year amortisation, as recognised under AGAAP, as at the date of transition.

The impact of reversing current year amortisation would be a write back of the expense amounting to \$74,015.

Under AASB 138 "Intangible Assets", costs incurred in the research phase of the development of an internally generated intangible asset would be expensed. The ZBB Energy Corporation's current accounting policy allows for the capitalisation of such costs where the future economic benefits are expected beyond reasonable doubt. The Directors are currently reviewing Intangible assets amounting to \$2,420,271 to determine the research component of the Intangible Asset, if any.

Under AASB 121 "The effects of changes in Foreign Exchange Rates" ZBB Energy Corporation will elect to adopt the exemption under this Standard and consequently the cumulative translation differences for all foreign operations will be deemed to be zero at the date of transition. The amount of \$2,743,103 will be transferred to accumulated losses at 1 July 2005

DIRECTORS' DECLARATION

The directors of the company declare that:

1. the financial statements and notes are in accordance with the Corporations Act 2001 and:
 - (i) comply with Accounting Standards and the Corporation Regulations 2001; and
 - (ii) give a true and fair view of the financial position as at 30 June 2005 and of the performance for the year ended on that date of the company and economic entity; and
1. the Chief Executive Officer and Chief Financial Officer have each declared that:
 - (i) the financial records of the company for the financial year have been properly maintained in accordance with section 286 of the Corporations Act 2001;
 - (ii) the financial statements and notes for the financial year comply with the Accounting Standards; and
 - (iii) the financial statements and notes for the financial year give a true and fair view
3. in the directors opinion 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 Board of Directors.



Robert John Parry
Managing Director and Chief Executive Officer
30 September 2005



Chartered Accountants
& Business Advisers

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Liability is limited by the Accountants
Scheme, approved under the
Professional Standards Act 1994 (NSW)

INDEPENDENT AUDIT REPORT TO THE MEMBERS OF ZBB ENERGY CORPORATION

Scope

The financial report and directors' responsibility

The financial report comprises the statement of financial position, statement of financial performance, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for both ZBB Energy Corporation (the company) and the consolidated entity for the year ended 30 June 2005. The consolidated entity comprises both the company and the entities it controlled during that year.

The directors of the company are responsible for the preparation and true and fair presentation of the financial report in accordance with the Corporations Act 2001. This includes the responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

Audit approach

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

We performed procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001, including compliance with Accounting Standards and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the company's and the consolidated entity's financial position, and of their performance as represented by the results of their operations and cash flows.

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

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

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

Independence

In conducting our audit, we followed applicable independence requirements of Australian professional ethical pronouncements and the Corporations Act 2001.

Audit opinion

In our opinion, the financial report of ZBB Energy Corporation 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 30 June 2005 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 financial reporting requirements in Australia.



PKF



B R Gordon
Partner

Sydney
Dated: 30 September 2005

ADDITIONAL INFORMATION FOR THE YEAR ENDED 30 JUNE 2005

The following information is included in accordance with Listing Rules of the Australian Stock Exchange Limited.

1. SHAREHOLDING

(a) Distribution of Shareholders as at 30 September 2005

Size of Holding	Number of Shareholders	Ordinary Shares Held	%
1-1,000	42	33,862	0.04
1,001-5,00	349	1,191,008	1.45
5,001-10,000	313	2,509,340	3.06
10,001-100,000	481	16,951,543	20.68
100,001 and over	143	61,278,873	74.77
Total	1,327	81,964,626	100.00

Shareholders holding less than a marketable parcel: 391

(b) Twenty Largest Security Holders

Name	Number of Fully Paid Ordinary Shares Held	% Held of Issued Ordinary Shares
WA Local Government Superannuation Fund	6,043,458	7.37
Frank Ernest Parry <FEIM Fund A/C>	5,610,000	6.84
Baytree Holdings Limited	5,504,284	6.72
International Finance Trust Company Limited <7506>	1,535,826	1.87
Arcturus Invest Graas	1,490,865	1.82
Multiplex Limited	1,394,001	1.70
Kent Frederick Carter	1,292,500	1.58
Hawkesbridge Limited <LGST A/C>	1,250,000	1.53
China Bridge Finance Limited	1,200,000	1.46
China Century Group Limited	1,200,000	1.46
Geizo Pty Ltd <RA Payne Family A/C>	1,082,000	1.32
Ingrid Anna-Maria Hanselmann	1,014,795	1.24
Preferential Capital Pty Ltd	981,250	1.20
Bernville Pty Ltd	900,000	1.10
Graeme Edward Davey	696,139	0.85
Taavco Limited <No 1 A/C>	681,687	0.83
Ross Stanley Sutherland & Carolyn Anne Sutherland <Joe & Co Group Super Fund A/C>	672,501	0.82
Arellbee Pty Limited	650,000	0.79
Robert John Parry and Geoffrey David Hann	600,000	0.73
Phillip Alan Eidler	600,000	0.73

2. OPTION HOLDING

Distribution of Listed Optionholders as at 30 September 2005

Size of Holding	Number of Option holders	Ordinary Options Held	%
1-1,000	106	103,300	3.44
1,001-5,000	208	558,250	18.61
5,001-10,000	23	192,235	6.41
10,001-100,000	34	942,400	31.41
100,001 and over	7	1,203,815	40.13
Total	378	3,000,000	100.00