



24 September, 2013

Stephanie Yong
Senior Advisor, Listing Compliance (Sydney)
ASX Compliance Pty Limited
20 Bridge Street NSW 2000

Dear Stephanie,

We respond to your letter originally dated 4 September, 2013 relating to Phoslock Water Solution's (PWS) Financial Statements lodged on 30 August, 2013. These accounts contained a Disclaimer of Opinion relating to one specific matter – approx. \$40,000 of additional inventory was found at our Chinese JV factory during the June 2013 stocktake. PWS was unaware that this was a material audit issue until Wednesday 28 August, 2013, two days before the accounts were scheduled to be signed. The auditors were unable to accept PWS's reasons for the additional inventory by the time that the preliminary accounts were due to be lodged, by close of business on Friday 30 August, 2013.

PWS undertook an internal investigation to find the source of the additional inventory – approximately 20 tons. This resulted in a detailed package of information provided to the auditors at a meeting on 10 September, 2013 attended by PWS Chairman, Managing Director and the two audit partners involved in the PWS audit.

The auditors reviewed the information and state in the new Audit Opinion "A previous audit report with a disclaimer of audit opinion was issued on 30 August, 2013 due to us being unable to obtain sufficient appropriate audit evidence on material movements on inventory. Subsequent to issuing the audit report, management were able to provide us with additional supporting evidence that enabled us to reissue an unqualified audit report".

The same Financial Statements lodged on 30 August, 2013 were re-lodged this morning with a new Audit Report with no Disclaimer of Opinion.

With a new Audit Opinion being provided which has no Disclaimer of Opinion, questions 1 and 2 are now not applicable. However, you have asked PWS Directors to confirm that the Annual Accounts comply with the relevant Accounting Standards, and give a true and fair view of the financial performance and financial position of the Company, which they do.

In relation to question 3 concerning Going Concern, PWS has had a Material Uncertainty Note regarding continuation as a Going Concern Note in its accounts since the 30 June, 2010. PWS provided Note 27 in the 30 June 2013 Financial Statements which covers what PWS is doing in relation to this issue. The A\$1.3m unsecured loan facility or Convertible Notes are due 31 December, 2013. The holder has not advised PWS of their intentions at this stage regarding the conversion of Notes into PHK shares or the request for repayment or the possibility of an extension in this facility. The Company is confident that it will come to an accommodation with the Convertible Note holder (convert into equity or extend the maturity of the Notes), who is also as major shareholder of PWS.

Question 4. PWS believes that its level of operations is sufficient to warrant quotation of the securities on the ASX in accordance with the requirements of listing rule 12.1 (level of entity's operation). PWS is confident that it can convert a meaningful portion of its pipelines projects into sales. It is currently at an advanced stage with one large sale project/sale, however until the contract is officially awarded and signed, is not in a position to confirm details.

Question 5. PWS believes that the financial condition of the Company is sufficient to warrant continued listing on the ASX in accordance with the requirements of listing rule 12.2 (financial condition). PWS is confident that it can convert a meaningful portion of its pipelines projects into sales. It is currently at an advanced stage with one large sale project/sale, however until the contract is officially awarded and signed, is not in a position to confirm details.

Question 6. PWS answered yes to both questions 4 and 5.

Question 7. PHK confirms that it is in compliance with its listing rules and in particular listing rule 3.1 (continuous disclosure).

Yours sincerely,



Robert Schuitema
Managing Director
Phoslock Water Solutions Limited

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4 September 2013

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By Email

Dear Robert

Phoslock Water Solutions Limited (the "Company") – Financial Condition Query

ASX Limited ("ASX") refers to the following:

1. The Company's 2013 full year accounts for the year ended 30 June 2013, lodged with ASX on 30 August 2013 (the "Annual Accounts").
2. The Independent Auditor's Report set out on pages 37 to 38 of the Annual Accounts ("Auditor's Report") which contains a Disclaimer of Opinion (the "Disclaimer") and an Emphasis of Matter, stating the following:

"Basis for Disclaimer of Opinion

Phoslock Water Solutions Limited and its controlled entities' inventory is carried at \$358,457 and trade receivables \$54,742 on the consolidated statement of financial position as at 30 June 2013, and revenue of \$1,313,344 and cost of sales of \$798,919 is included in the consolidated statement of comprehensive income for the year then ended.

We were unable to obtain sufficient appropriate audit evidence to support the completeness, existence and valuation of inventory as at 30 June 2013 due to unsupported material movements of inventory during the year ended 30 June 2013. Consequently we were also unable to obtain sufficient, appropriate audit evidence to support the completeness, existence and valuation of trade receivables at 30 June 2013 and nor were we able to obtain sufficient audit evidence over the completeness, occurrence and accuracy of revenue and cost of sales.

We were unable to satisfy ourselves by alternative means.

As a consequence, we are unable to determine whether any adjustments to the amounts for inventory, receivables, revenue and cost of sales was necessary including the elements making up the statement of comprehensive income, statement of changes in equity and statement of cash flows.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial report.

Emphasis of matter

Uncertainty in Relation to Going Concern

We draw attention to Note 27, in the financial report, which indicates that the consolidated entity incurred a net loss of \$2,060,431 during the year ended 30 June 2013, had accumulated losses totalling \$32,686,216, a net current liability position of \$841,173 and net cash used in operating activities of \$1,178,711 at 30 June 2013. These conditions, along with the other matters set forth in Note 27, indicate the existence of a material uncertainty that may cast significant doubt about the consolidated entity's ability to continue as a going concern and therefore, whether it will be able to realise its assets and discharge its liabilities in the normal course of business."

Relevant Listing Rules and Guidance

- Listing Rule 12.1 – *The level of an entity's operations must, in ASX's opinion, be sufficient to warrant the continued quotation of the entity's securities and its continued listing.*
- Listing Rule 12.2 – *An entity's financial condition (including operating results) must, in ASX's opinion, be adequate to warrant the continued quotation of its securities and its continued listing.*
- Listing Rule 19.11A – *If a listing rule requires an entity to give ASX accounts, the following rules apply:
...
(b)The accounts must be prepared to Australian accounting standards. If the entity is a foreign entity the accounts may be prepared to other standards agreed by ASX.*

Questions for Response

In light of the Auditor's Report, the information contained in the Annual Accounts, and the application of the listing rules stated above, please respond to each of the following questions:

1. Is the Company able to confirm that in the Directors' opinion the Annual Accounts:
 - (a) comply with the relevant Accounting Standards; and
 - (b) give a true and fair view of the financial performance and financial position of the Company?
2. Given the Disclaimer relates to the Auditor's inability to obtain sufficient appropriate audit evidence to support the completeness, existence and valuation of various items as stated in the Auditor's Report, what steps does the Company intend to take to obtain an unqualified audit/review report for future financial periods? Also, on what basis does the Company believe the carrying values to be appropriate? In your response, please address specifically the following items:
 - (a) Inventory

(in your response, please explain why the Auditor has been unable to obtain sufficient appropriate audit evidence in relation to the inventory figure, making specific reference to the unsupported material movements of inventory during the year ended 30 June 2013 and what these material movements related to); and
 - (b) trade receivables.
3. What steps does the Company intend to take to address the going concern issues of the Company? The Company should specifically address the net current liability position and its ability to meet its current debts as and when they fall due, as well as the impact on the Company in the event that the Company fails to renegotiate the unsecured loan facility.

4. Does the Company consider that its level of operations is sufficient to warrant continued quotation of its securities on ASX in accordance with the requirements of listing rule 12.1? In answering this question, please also explain the basis for this conclusion.
5. Does the Company consider that the financial condition of the Company is sufficient to warrant continued listing on ASX in accordance with the requirements of listing rule 12.2? In answering this question, please also explain the basis for this conclusion.
6. If the answer to questions 4 or 5 is "No", please explain what steps the Company has taken, or proposes to take, to warrant continued listing on ASX in accordance with the requirements of listing rules 12.1 and 12.2.
7. Please confirm that the Company is in compliance with the listing rules and, in particular, listing rule 3.1.

Please note the ASX reserves its right under listing rule 18.7A to release this letter and the Company's response to the market. Accordingly, the Company's response should address each question separately and be in a format suitable for release to the market.

Unless the information is required immediately under listing rule 3.1, a response is requested as soon as possible and, in any event by **no later than 9.30 a.m. AEST on Tuesday, 24 September 2013.**

Any response should be sent to me by return email. It should not be sent to the ASX Market Announcements Office.

If you have any queries regarding any of the above, please let me know.

Yours sincerely

(sent electronically without signature)

Stephanie Yong
Senior Adviser, Listings Compliance (Sydney)