

Appendix 4E
For the year ended 31 December 2022

DroneShield Limited
ABN 26 608 915 859

1. Reporting period

The financial information contained in the attached consolidated financial report is for the year ended 31 December 2022. The previous corresponding period was the year ended 31 December 2021.

Results for announcement to the market				
	Up/ Down	% Movement		2022 \$
Revenue from continuing activities	Up	59%	to	16,886,081
Loss from continuing activities after tax attributable to members	Down	82%	to	(949,301)
Net loss attributable to members	Down	82%	to	(949,301)
Dividends: No dividends are being proposed or have been paid	Nil	Nil		Nil

Additional information:

2. Commentary related to the above results

Refer to Directors Report in the attached Annual Report.

3. Net Tangible Assets/(Liabilities) per share:

31 December 2022: \$0.04; 31 December 2021: \$0.04

4. There was no change of control during the year

5. There were no payments of dividends during the year

6. There is no dividend reinvestment plan in operation

7. There are no associates or joint venture entities

8. This report is based on the consolidated financial report which has been audited by HLB Mann Judd Assurance (NSW) Pty Ltd.

Further information regarding the company and its business activities can be obtained by visiting the company's website at www.droneshield.com

For personal use only



DRONESHIELD

Annual Report

For the Year Ended
31 December 2022



Image: DroneShield customer order ready for dispatch

DroneShield Limited (ASX:DRO)

ASX Release

ABN 26 608 915 859

Table of Contents

Corporate Information	2
Chairman's Review	3
About DroneShield	4
Board of Directors and Executives	7
Corporate Governance Statement	9
Directors' Report	19
Directors' Report- Remuneration Report (audited).....	24
Auditor's Independence Declaration	31
Consolidated Statement of Profit or Loss and Other Comprehensive Income	32
Consolidated Statement of Financial Position	33
Consolidated Statement of Changes in Equity	34
Consolidated Statement of Cash Flows	35
1. Summary of Significant Accounting Policies	36
2. Critical accounting judgements, estimates and assumptions	42
3. Revenue.....	43
4. Other income	43
5. Product development expense.....	44
6. Sales and customer service expense	44
7. Corporate and support expense.....	44
8. Corporate governance expense.....	44
9. Options issued	45
10. Income taxes relating to continuing operations	47
11. Cash and cash equivalents	47
12. Trade and other receivables	47
13. Inventories	48
14. Other investments.....	48
15. Plant, equipment and intangible assets	49
16. Right-of-use asset.....	50
17. Provisions	50
18. Other liabilities	50
19. Lease liabilities.....	51
20. Borrowings.....	51
21. Contributed equity.....	51
22. Shares and options	52
23. Earnings (loss) per share	52
24. Key Management Personnel disclosures and related party transactions.....	53
25. Parent entity financial information	53
26. Financial risk management	54
27. Contingent liabilities	55
28. Commitments.....	55
29. Remuneration of auditor	56
30. Segment information.....	56
31. Reconciliation from loss after income tax to net cash outflow from operating activities	58
32. Events after the reporting date.....	58
Directors' Declaration	59
Independent Auditor's Report.....	60
Shareholder Information.....	64

Corporate Information

Directors & Management

Peter James Independent Non-Executive Chairman
Jethro Marks Independent Non-Executive Director
Oleg Vornik CEO and Managing Director

Registered Office

Level 5, 126 Phillip Street
Sydney, NSW 2000
Australia

Telephone: +61 2 9995 7280

Email: info@dronesield.com
Website: www.dronesield.com

Auditors

HLB Mann Judd Assurance (NSW) Pty Ltd
Level 5, 10 Shelley Street
Sydney, NSW 2000
Australia

Bankers

Commonwealth Bank of Australia
309-315 George Street
Sydney NSW 2000
Australia

Westpac
275 Kent Street
Sydney NSW 2000
Australia

PNC Bank
1405 P Street, NW
Washington DC 20005
United States of America

Solicitors

Baker & McKenzie LLP
452 Fifth Avenue
New York NY 10018
United States of America

K&L Gates
1601 K Street, NW
Washington DC 20006
United States of America

MinterEllison
Level 11 Constitution Place
1 Constitution Avenue
Canberra City ACT 2601
Australia

Steinepreis Paganin
16 Milligan Street
Perth WA 6000
Australia

Share Registry

Automic Registry Services
Level 5, 126 Phillip St
Sydney, NSW 2000
Australia

Enquiries (within Australia): 1300 288 664
Enquiries (outside Australia): +61 2 9698 5414

Stock Exchange Listing

DroneShield Limited (ASX code DRO) shares are quoted on the Australian Securities Exchange.

For personal use only

Chairman's Review



*Peter James,
Independent Non-
Executive Chairman*

Dear Fellow Shareholders,

2022 has seen DroneShield Ltd ("DroneShield" or the "Company") produce another leap in results, with 2023 shaping to be a truly transformational year for the business.

Highlights for 2022 and 2023 to date included:

- 2022 Revenue of \$16.9 million (in addition to R&D incentives and other grants). This is an approximately 60% increase on 2021 revenues, and continues the trend of the Company generating record revenues each year of its existence.
- \$15.6 million of 2022 cash receipts, another all-time record.
- Record \$11 million order received in December followed by another \$11 million order from a different Government customer in January 2023, as well as numerous smaller contracts.
- Strong bank balance of approximately \$22 million as of date of this report, including completion of \$10.9 million placement this month, which received exceptional institutional investor support.
- Record \$24 million contract backlog at the start of the year, and a strong sales pipeline with over \$200 million¹ in active project discussions for 2023 opportunities (risk unweighted).
- Substantial tailwinds for the defence industry with growing geopolitical tensions, with an increase in Government spending in Australia and in other markets.

The Ukrainian war, where DroneShield has been deployed since the start in February 2022 on the Ukrainian side, has clearly demonstrated the potential of drones and counterdrone systems on the battlefield, coupled with significant non-military use cases for intelligence community, airports, prisons, border security, stadiums, and other facilities. Nefarious use of drones is a global and rapidly rising threat, with DroneShield providing proven market leading suite of solutions, directly and via its network of 100+ in-country partners globally.

DroneShield has continued to ramp up its mass production capabilities, across supply chain, inventory and deployment aspects, with the goal of immediate or short-term fulfilment of customer orders, including anticipated record-size orders.

The Australian Government continues to strongly encourage the growth of the domestic defence industry. The current \$3.9 million Electronic Warfare contract has been progressing well and a subsequent, larger, contract is expected in 2023.

The U.S. Government and military market is expected to be the single largest opportunity for DroneShield, being the largest counterdrone customer in the world. During 2022, DroneShield continued to solidify its position in that market, led by its Virginia office, securing both significant repeat sales to existing customers and adding new customers. The US business is led by a seasoned ex-military veteran team, experienced in scaling US Government sales and the associated steps towards larger purchases. The US DoD recommended DroneShield solutions for a rollout across its bases nationwide during the year, as part of the SAIC consortium.

DroneShield continues to actively engage with strategic primes, including welcoming a \$3.7 million investment from Epirus, a defence technology unicorn based in California, developing software-defined directed energy systems. The counterdrone industry continues to consolidate as it rapidly grows, as evidenced by Texas-based Highlander Partners acquiring Black Sage, Liteye Systems and DZYNE, in the last 6 months. DroneShield is well-positioned strategically in this environment.

At the macro level, international tensions and greyzone warfare (which C-UAS, Electronic Warfare (EW) and related areas are a key part of) continue to rise, driving increases in security and national defence budgets. The Company currently offers its products in over 100 countries and the diversity of its pipeline is one of its key strengths.

On behalf of the Board, I would like to thank our executive team for their significant contributions for the past year.

I would also like to thank our fellow shareholders for your support and look forward to continued growth of the Company.

Peter James
Independent Non-Executive Chairman



*DroneGun at the Brazil Presidential
Inauguration in January 2023*

¹ Necessarily, not all (and there can be no assurance that any) of the Company's sales opportunities will result in sales.

About DroneShield

DroneShield (ASX:DRO) provides Artificial Intelligence based platforms for protection against advanced threats such as drones and autonomous systems. It offers customers bespoke counterdrone (or counter-UAS) and electronic warfare solutions and off-the-shelf products designed to suit a variety of terrestrial, maritime or airborne platforms. The customers include military, intelligence community, Government, law enforcement, critical infrastructure, and airports globally.

History of DroneShield

Founded on 10 January 2014, the DroneShield business began as DroneShield LLC in the U.S. On 4 November 2015, DroneShield Limited was incorporated in Australia for the primary purpose of listing on the ASX and engaging in the business of offering products manufactured by DroneShield globally, as well as managing and operating DroneShield's business.

DroneShield Limited listed on the ASX on 22 June 2016, raising \$7 million on a \$20 million valuation in an oversubscribed initial public offer ('IPO'). In February 2023, its last capital raise, DroneShield raised \$10.9 million via a placement.

DroneShield has grown from a small start-up to a global leader in C-UAS detection and mitigation.



Business Model and Products

Affordable consumer-grade drones ("UAS") have become popular around the world, but they present unique and frequent threats to privacy, physical security and public safety in a wide variety of environments. DroneShield offers products that detect and defeat such drones to civil infrastructure operators, militaries, and other government and commercial users globally. DroneShield's distribution channels focus on third party distributors, as well as direct relationships with various key customers. With offices in Australia and the United States, DroneShield has an experienced salesforce with distribution partners across over 100 countries. The end-users of DroneShield's products come from a diverse array of global sectors, including the following:

- Defence and intelligence agencies.
- Airports and other civil defence users.
- Utilities such as power plants, electricity grids and gas pipelines.
- Ports and other critical infrastructure asset owners.
- Intelligence and national security agencies.
- Prisons.
- Stadiums and other public event venues and organisers.
- Media production sites.
- Real estate owners including hotels, commercial offices and manufacturing plants.
- Executive protection including ultra-high net worth individuals and government officials.

DroneShield offers a comprehensive solution to drone threats with a suite of detection and countermeasure products.

The main product range is as follows:




	<ul style="list-style-type: none"> • Portable rifle shape drone disruptor, causing the drone (or swarm) to safely land, or fly back to the starting point (potentially identifying the pilot) • 7kg weight, no backpack • Best-in-breed effective range • Released in early 2018 • Existing sales globally
	<ul style="list-style-type: none"> • Pistol shaped compact drone disruptor • Best-in-breed effective range • Released in mid-2019 • Only 2kg weight including battery • Unique patented design • Suitable for mobile deployments, patrols, law enforcement and special forces • Existing sales globally

DroneGun Tactical™

DroneGun MKIII™

For personal use only

For personal use only

 <p>RfPatrol MKII™</p>	<ul style="list-style-type: none"> • Body-worn drone detection device • Best-in-breed detection range • Can be used with a directional accessory (DAU™) to determine direction of the threat as well as vehicle kit • Completely passive (no RF emissions) • MKII version launched in mid-2020 • Deployments include global military and intelligence customers • Receives quarterly software updates via a SaaS model
 <p>DroneSentry™</p>	<ul style="list-style-type: none"> • Integrated detect-and-defeat system • Best-in-breed detection and defeat range • Includes radiofrequency direction finders, radars and cameras in a modular manner, with an integrated DroneCannon™ drone disruptor • Utilises DroneShield proprietary DroneSentry-C2™ counterdrone software command-and-control engine • The camera includes DroneOptID™, DroneShield proprietary AI computervision software to detect and track drone targets • Successfully deployed in multiple locations globally, in full or modular forms, across military and Government customer base • Receives quarterly software updates via a SaaS model
 <p>DroneSentry-X™</p>	<ul style="list-style-type: none"> • Integrated detect-and-defeat counterdrone solution • Best-in-breed detection and defeat range • Deployable on a vehicle, ship or fixed site platforms • Existing customers include US Government agencies and other Government and military departments globally • Receives quarterly software updates via a SaaS model

Underpinning all DroneShield's detection products is the Company's proprietary software engine RFAI™, with quarterly software updates on a subscription basis.

The second subscription software product, DroneSentry-C2™, is the Company's Command-and-Control platform on its DroneSentry™ multi-sensor system. It is an intuitive interface with a comprehensive reporting suite, which can combine a number of customer sites deploying both DroneShield's and third-party sensor hardware. An optional additional module to DroneSentry-C2™ is DroneOptID™, the company's optical/thermal AI-based detection engine

Image: DroneSentry-C2™



Artificial Intelligence R&D Defence Contracts

- During the year, DroneShield progressed two R&D contracts with the Australian Department of Defence (DoD):
- \$3.8 million, 2-year contract in AI applied in Electronic Warfare domain (following on a \$600,000, 6-month contract in 2020) – due for completion mid-2023, with a larger follow-on contract expected on completion.
 - \$800,000 1-year contract in AI applied in computervision domain with Defence Innovation Hub. The contract was successfully completed at the end of 2022 and DroneShield is currently in discussions for a follow-up contract.

Additional, and larger, contracts, are anticipated with the Australian DoD, as well as potentially the U.S. Department of Defense.

Revenue Model and Recurring Cashflows

DroneSentry™, DroneSentry-X™ and RfPatrol™ products have a recurring revenue element which it charges for RFAI™ quarterly updates to the drone libraries of the products. Over time, DroneShield expects to build a robust recurring revenue line as more products requiring library updates are sold.

DroneSentry-C2™, the command-and-control software for DroneShield and third-party sensors, is offered on a subscription basis (via on-prem or secure cloud solution). Within that, DroneOptID™ offers a third subscription product, as an add-on to DroneSentry-C2™.

Additionally, DroneShield offers lease options of its product range to its in-country partners and end customers (where possession and use of a particular product is lawful for that customer according to local laws). The lease periods vary from weekly, to multi-year. Leasing may be suitable for event-based requirements, product evaluations without a commitment to purchase, or for customers who have a preference to lease vs outright purchase. The Company is currently shortlisted for a large U.S. Government “Counterdrone as a service” project, expected to be structured as a long-term lease of its equipment. The tender result is expected to be known this year.

The Company does not believe that leasing would cannibalise its sales, as leasing appeals to a different set of customers and utilises different deployment opportunities. Further, the Company believes that leasing is complementary to its sales efforts as it will promote customer awareness of DroneShield’s products and their applications.

Finally, defence and Government agency markets are typically of a recurring nature, with repeat contracts following initial successful deployments. DroneShield has received repeat customer orders globally on that basis.

For personal use only

Board of Directors and Executives



Peter James; Independent Non-Executive Chairman

Mr. James has over 30 years' experience in the Technology, Telecommunications and Media Industries, and has extensive experience as Chair, Non-Executive Director and Chief Executive Officer across a range of publicly listed and private companies. He is currently Chair of ASX-listed companies Macquarie Telecom, Ansarada and Halo Food Co. Most recently, Mr. James was the chair of Nearmap, which was sold to Thoma Bravo (US private equity firm) for \$1.06 billion, in December 2022.

Mr. James joined the Board of DroneShield on 1 April 2016. Mr. James is an experienced business leader with significant strategic and operational expertise. He is a Fellow of the Australian Institute of Company Directors, a Fellow of the Australian Computer Society and holds a BA degree with Majors in Computer Science and Business.



Oleg Vornik; CEO and Managing Director

Mr. Vornik is an experienced senior executive with previous roles at the Royal Bank of Canada, Brookfield, Deutsche Bank and ABN AMRO.

Prior to becoming the CEO of DroneShield, Mr. Vornik was its Chief Financial Officer. His previous experience includes the Sydney office of the Royal Bank of Canada as well as with Brookfield Asset Management, Deutsche Bank and ABN AMRO in Australia and New Zealand. Mr. Vornik holds a BSc (Mathematics) and BCom (Hons) from the University of Canterbury, New Zealand and has completed a business program with Columbia University in New York.

After co-leading the Company in the role of the Chief Financial Officer for over a year, Mr. Vornik was appointed as the CEO and Managing Director of DroneShield on 24 January 2017. Mr. Vornik does not hold any other public company directorships.



Jethro Marks; Independent Non-Executive Director

Mr. Marks is a Sydney-based CEO and co-founder of The Nile Group, an eCommerce retail, services, logistics and outsourcing business. Over 17 years Mr. Marks has led, and continuously grown, the business at the forefront of digital commerce, marketing and international logistics, while competing with the largest retailers globally. Mr. Marks brings to the Board extensive commercial experience in successfully scaling a multinational business.

The Nile Group's global supply chain and award-winning logistics capability has extended to most consumer goods categories in multiple countries, and today carries 32 million products. This capability has extended to provisioning international logistics support to multinational brands and technology companies.

Mr. Marks graduated from the University of Auckland, with a Bachelor of Commerce (Honours).

Mr. Marks joined the Board on 16 January 2020. Mr. Marks does not hold any other public company directorships.



Matt McCrann; CEO, DroneShield LLC (USA)

Mr McCrann is an experienced business development executive, having previously built and led business units for enterprises delivering innovative technology to military, intelligence, public safety, and law enforcement communities worldwide. Mr McCrann brings to DroneShield more than 15 years of experience in the Defense and National Security sector with significant roles spanning Sales, Operations, and Engineering.

Mr McCrann has industry certifications and specialised training in RF and wireless communications and is a member of numerous industry and government organisations including; National Defense Industrial Association (NDIA), Armed Forces Communications and Electronics Association (AFCEA), Association of the United States Army (AUSA), and American Correctional Association (ACA).

For personal use only



Angus Bean; Chief Technology Officer

With a background in Industrial Design and Mechanical Engineering, Angus Bean brings a wealth of knowledge in product development through to production management. Mr. Bean merges the various fields of mechanical hardware, electronics, software, digital interface and technology.

Mr. Bean joined DroneShield early in 2016, since then has been a driving force in DroneShield's technology team, working to build the team and the technology to deliver on key projects and milestones. Previous to DroneShield, Mr. Bean was the Development Lead for Australia's largest and most prominent industrial design and engineering consultancy.

Over his career, Mr. Bean has adopted both a collaborative and leadership role on a number of projects which have attracted multiple Australian and International Awards in Innovation, Consumer Electronics, Defence and Cyber Security. Mr. Bean holds a BDesign in Industrial Design (First Class Hon) from the University of Technology Sydney.



Carla Balanco; CFO and Company Secretary

Mrs. Balanco is a member of Chartered Accountants Australia & New Zealand (CA ANZ). She holds an Honours in Accounting from the University of Johannesburg and an Honours in Accounting Science from the University of South Africa.

Mrs. Balanco started her career working for Chartered firms Crowe Horwath and HLB Mann Judd in the audit division. She moved on from Chartered to gain experience working in Commercial and Business Development roles.

Since joining DroneShield in 2018, she has spearheaded improvements to critical systems and internal controls and has been instrumental in scaling the Company's financial management systems. Today, as CFO and Company Secretary, Mrs. Balanco oversees statutory reporting, management reporting, payroll, treasury, administration, and compliance for the global DroneShield Group of companies.

Mrs. Balanco was selected as a finalist in the 2021 ADM's Women in Defence Awards and 2020 Australian Defence Industry Awards.



Lyle Halliday; Chief Operating Officer

Mr Halliday joined DroneShield as an experienced Systems Engineer in 2020 with a background in medical device product development. Since then, he has taken his experience in risk management, cybersecurity, requirements management, quality assurance and regulatory compliance and applied this to business operations.

Mr Halliday is responsible for implementation of processes to ensure customer expectations are met with respect to product quality, delivery and continuous improvement. His engineering experience spans electrical, mechanical, manufacturing and software engineering, allowing him to work across all aspects of business operations.

Mr Halliday is a University Medallist of the Australian National University where he studied a Bachelor of Systems Engineering (Research and Development).



Tom Branstetter, U.S. Director of Business Development

Tom is a U.S. Navy veteran and former Navy SEAL. Upon separation from active duty in 2010, he began work as a high-threat protective officer for the U.S. government.

Tom now serves as the Director of Business Development for DroneShield's U.S. operations focusing on overall growth across DoD and other federal agencies. Tom's responsibilities include identifying and developing new business opportunities as well as expanding brand presence. Additional areas of focus include leading cross-functional teams and managing existing partnerships.

Tom holds a Bachelor of Arts degree in Entrepreneurship. He and his family reside in Northern Virginia.

For personal use only

Corporate Governance Statement

The Board of the Company (“**Board**”) recognises the importance of establishing a comprehensive system of control and accountability as the basis for the administration of corporate governance.

To the extent relevant and practical, the Company has adopted a corporate governance framework that is consistent with *The Corporate Governance Principles and Recommendations (4th Edition)* as published by ASX Corporate Governance Council (“**Recommendations**”).

The Board has adopted the following suite of corporate governance policies and procedures which are contained with the Company’s **Corporate Governance Plan**, a copy of which is available on the Company’s website at <https://www.droneshield.com/investors>.

- Board Charter
- Corporate Code of Conduct
- Public Sector Code of Conduct
- Audit and Risk Committee Charter
- Remuneration Committee Charter
- Nomination Committee Charter
- Continuous Disclosure Policy
- Risk Management Policy
- Remuneration Policy
- Trading Policy
- Diversity Policy
- Shareholder Communications Strategy
- Whistleblower Protection Policy
- Anti-bribery and Anti-Corruption Policy
- Performance Evaluation Procedures
- Skills Matrix

The Board is committed to administering the policies and procedures with openness and integrity, pursuing the true spirit of corporate governance commensurate with the Company’s needs.

The Company is pleased to report that its practices are largely consistent with the Recommendations of the ASX Corporate Governance Council and sets out below its compliance and departures from the Recommendations for the year ended 31 December 2022.

In the context of the Company’s nature, scale and operations, the Board considers that the current corporate governance regime is an efficient, practical and cost-effective method of directing and managing the Company. As the Company’s activities develop in size, nature and scope, the implementation of additional corporate governance policies and structures will be reviewed and considered.

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Principle 1: Lay solid foundations for management and oversight		
Recommendation 1.1 A listed entity should have and disclose a board charter setting out: a) the respective roles and responsibilities of its board and management; and b) those matters expressly reserved to the board and those delegated to management.	Yes	The Board is responsible for the corporate governance of the Company. The Company has adopted a Board Charter which sets out, amongst other things, the specific responsibilities of the Board, the roles and responsibilities of the Chairman, Board and management, as well as the matters expressly reserved for the decision of the Board and those delegated to management. A copy of the Company’s Board Charter is contained in its Corporate Governance Plan which is available on the Company’s website at: https://www.droneshield.com/investors The Company is committed to the circulation of relevant materials to Directors in a timely manner to facilitate Directors’ participation in Board discussions on a fully informed basis. The Company intends to regularly review the balance of responsibilities between the Board and

For personal use only

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION												
		management to ensure that the division of functions remains appropriate to the needs of the Company.												
<p>Recommendation 1.2</p> <p>A listed entity should:</p> <p>(a) undertake appropriate checks before appointing a Director or senior executive, or putting someone forward for election, as a Director; and</p> <p>(b) provide security holders with all material information relevant to a decision on whether or not to elect or re-elect a Director.</p>	Yes	<p>The Company's Corporate Governance Plan requires the Board to undertake appropriate checks as to the character, experience, education, criminal record and bankruptcy history of the candidate before appointing a person or putting forward to security holders a candidate for election, as a Director.</p> <p>All material information relevant to a decision on whether to elect or re-elect a Director will be provided to security holders in any notice of meeting pursuant to which the resolution to elect or re-elect such Director will be voted on.</p>												
<p>Recommendation 1.3</p> <p>A listed entity should have a written agreement with each Director and senior executive setting out the terms of their appointment.</p>	Yes	Each Director and senior executive of the Company is party to a written agreement with the Company which sets out the terms and conditions of that Director's or senior executive's appointment.												
<p>Recommendation 1.4</p> <p>The company secretary of a listed entity should be accountable directly to the board, through the chair, on all matters to do with the proper functioning of the board.</p>	Yes	The Board Charter outlines the role, responsibility and accountability of the Company Secretary. The Company Secretary is accountable directly to the Board, through the Chair, on all matters relating to the proper functioning of the Board. The Chairman and the Company Secretary co-ordinate the Board agenda.												
<p>Recommendation 1.5</p> <p>A listed entity should:</p> <p>(a) have and disclose a diversity policy;</p> <p>(b) through its board or a committee of the board set measurable objectives for achieving gender diversity in the composition of its board, senior executives and workforce generally; and disclose in relation to each reporting period:</p> <p>a. the measurable objectives set for that period to achieve gender diversity;</p> <p>b. the entity's progress towards achieving those objectives; and</p> <p>c. either:</p> <p>(A) the respective proportions of men and women on the board, in senior executive positions and across the whole workforce (including how the entity has defined "senior executive" for these purposes); or</p> <p>(B) if the entity is a "relevant employer" under the Workplace Gender Equality Act, the entity's most recent "Gender Equality Indicators", as defined in and published under that Act.</p> <p>If the entity was in the S&P / ASX 300 Index at the commencement of the reporting period, the measurable objective for achieving gender diversity in the composition of its board should be to have not less than 30% of its Directors of each gender within a specified period.</p>	<p>Yes</p> <p>No</p> <p>N/A</p> <p>N/A</p> <p>Yes</p>	<p>The Company has adopted a Diversity Policy which identifies gender diversity as a key area of focus for the Company. While the Company is committed to gender diversity in its workplace, the Board believes that the Company is not yet of a size where it is appropriate to implement formal measurable objectives for achieving gender diversity.</p> <p>Whilst the Board previously adopted a tiered approach to the implementation, this approach has been revisited given the stage of development that the Company remains in. As the Company's workforce continues to grow, this will be re-assessed at the appropriate times.</p> <p>A copy of the Company's Diversity Policy is contained in its Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors</p> <p>During the reporting period (i.e., the year ended 31 December 2022), the respective proportions of men and women in the following roles were as follows:</p> <table border="1"> <thead> <tr> <th></th> <th>Men</th> <th>Women</th> </tr> </thead> <tbody> <tr> <td>Board</td> <td>100%</td> <td>0%</td> </tr> <tr> <td>Senior executives</td> <td>75%</td> <td>25%</td> </tr> <tr> <td>Across the whole organisation</td> <td>81%</td> <td>19%</td> </tr> </tbody> </table>		Men	Women	Board	100%	0%	Senior executives	75%	25%	Across the whole organisation	81%	19%
	Men	Women												
Board	100%	0%												
Senior executives	75%	25%												
Across the whole organisation	81%	19%												
<p>Recommendation 1.6</p>	Yes	The performance of the Board as a group and of individual Directors will be assessed each year for all												

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
<p>A listed entity should:</p> <p>(a) have and disclose a process for periodically evaluating the performance of the board, its committees and individual Directors; and</p> <p>(b) disclose for each reporting period, whether a performance evaluation has been undertaken in the reporting period in accordance with that process during or in respect of that period.</p>		<p>future years. The Remuneration Committee (the function of which is currently performed by the full Board) is responsible for evaluating the performance of the Board and individual Directors on an annual basis.</p> <p>The process for this is set out in the Company's Performance Evaluation Procedures policy which is contained in its Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>Given the small composition of the Board, the Board will undertake an evaluation of the Board and individual Director performance during FY23.</p>
<p>Recommendation 1.7</p> <p>A listed entity should:</p> <p>(a) have and disclose a process for periodically evaluating the performance of its senior executives at least once every reporting period; and</p> <p>(b) disclose in relation to each reporting period, whether a performance evaluation has been undertaken in the reporting period in accordance with that process during or in respect of that period.</p>	Yes	<p>The Managing Director of the Company is responsible for evaluating the performance of senior executives on an annual basis.</p> <p>The process for this is set out in the Company's Performance Evaluation Procedures policy which is contained in its Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>A formal performance evaluation of senior executives was undertaken during the 2022 financial year.</p>
Principle 2: Structure the board to be effective and add value		
<p>Recommendation 2.1</p> <p>The board of a listed entity should have a nomination committee which:</p> <p>(i) has at least three members, a majority of whom are independent Directors; and</p> <p>(ii) is chaired by an independent Director, and disclose:</p> <p>(iii) the charter of the committee;</p> <p>(iv) the members of the committee; and</p> <p>(v) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or</p> <p>if it does not have a nomination committee, disclose that fact and the processes it employs to address board succession issues and to ensure that the board has the appropriate balance of skills, experience, independence and knowledge of the entity to enable it to discharge its duties and responsibilities effectively.</p>	<p>No</p> <p>Yes</p> <p>N/A</p> <p>N/A</p> <p>Yes</p>	<p>Due to its size, the Board has determined that the function of the Nomination Committee is most efficiently carried out with full Board participation and accordingly, the Board has elected not to establish a separate Nomination Committee at this stage. As a result, the duties that would ordinarily be assigned to the Nomination Committee under the Nomination Committee Charter are carried out by the full Board.</p> <p>A copy of the Nomination Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>The Board devotes time at Board meetings on at least an annual basis to discuss Board succession issues. Where appropriate, all members of the Board are involved in the Company's nomination process, to the maximum extent permitted under the Corporations Act and ASX Listing Rules.</p> <p>The Board also conducts an annual review of the Company's Board Skills Matrix (in accordance with Recommendation 2.2) to ensure the Board maintains an appropriate balance of skills, experience, independence and knowledge to discharge its duties and responsibilities effectively.</p>
<p>Recommendation 2.2</p> <p>A listed entity should have and disclose a board skill matrix setting out the mix of skills and</p>	Yes	<p>The Board of the Company is comprised of Directors with a broad range of technical, commercial, financial</p>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
diversity that the board currently has or is looking to achieve in its membership.		<p>and other skills, experience and knowledge relevant to overseeing the business of a drone security company.</p> <p>The Company had developed a Board Skills Matrix which is used as a tool to assess the appropriate and ideal balance of skills, experience, independence and diversity necessary for the Board to discharge its duties and responsibilities effectively.</p> <p>A summary of the collective skills, experience, independence and diversity of the Board is set in Annexure C of the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p>
<p>Recommendation 2.3</p> <p>A listed entity should disclose:</p> <p>(a) the names of the Directors considered by the board to be independent Directors;</p> <p>(b) if a Director has an interest, position or relationship of the type described in Box 2.3 but the board is of the opinion that it does not compromise the independence of the Director, the nature of the interest, position or relationship in question and an explanation of why the board is of that opinion; and</p> <p>(c) the length of service of each Director</p>	Yes	<p>During the 2022 financial year, the Independent Directors of the Company were:</p> <ul style="list-style-type: none"> - Mr. Peter James (Non-Executive Chairman); and - Mr. Jethro Marks (Non-Executive Director). <p>Mr. Oleg Vornik, the Managing Director, was not considered to be independent during his tenure due to his executive role as Managing Director of the Company.</p> <p>The Board has determined the independence of each of the Company's Directors in line with the guidance set out by the ASX's Corporate Governance Council and have not formed an opinion contrary to those guidelines.</p> <p>The Directors who held office during and after the 2022 financial year have served continuously since their respective dates of appointment unless otherwise noted below:</p> <ul style="list-style-type: none"> - Mr. Peter James: appointed 1 April 2016; - Mr. Oleg Vornik: appointed 24 January 2017; and - Mr Jethro Marks: appointed 16 January 2020.
<p>Recommendation 2.4</p> <p>A majority of the board of a listed entity should be independent directors.</p>	Yes	<p>The Board Charter requires that, where practical the majority of the Board will be independent.</p> <p>During the 2022 financial year, the following two of the Company's three Directors were considered to be Independent Directors:</p> <ul style="list-style-type: none"> - Mr. Peter James (Non-Executive Chairman); and - Mr. Jethro Marks (Non-Executive Director).
<p>Recommendation 2.5</p> <p>The chair of the board of a listed entity should be an independent Director and, in particular, should not be the same person as the CEO of the entity.</p>	Yes	<p>The Chairman, Mr. Peter James is an Independent Non-Executive Director and is not the same person as the Managing Director of the Company.</p>
<p>Recommendation 2.6</p> <p>A listed entity should have a program for inducting new Directors and for periodically reviewing whether there is a need for existing Directors to undertake professional development</p>	Yes	<p>The Company's program for the induction of new Directors is tailored for each new Director (depending on their personal requirements, background skills, qualifications and experience) and includes the provision of a formal letter of appointment and an induction package containing sufficient information to</p>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
to maintain the skills and knowledge needed to perform their role as a Director effectively.		<p>allow the new Director to gain an understanding of the business of the Company, and the roles, duties and responsibilities of Directors and the Executive team.</p> <p>All Directors are encouraged to undergo continual professional development and, subject to prior approval by the Chairman, all Directors may have access to various resources and professional development training to address any skills gaps.</p>
Principle 3: Instil a Culture of acting Lawfully, Ethically and Responsibly		
Recommendation 3.1 A listed entity should articulate and disclose its values.	Yes	The Company's values are disclosed in the Corporate Code of Conduct which is contained in the Company's Corporate Governance Plan and available on the Company's website at: https://www.droneshield.com/investors .
Recommendation 3.2 A listed entity should: <ul style="list-style-type: none"> (a) have and disclose a code of conduct for its Directors, senior executives and employees; and (b) ensure that the board or a committee of the board is informed of any material breaches of that code. 	Yes	The Company has adopted a Corporate Code of Conduct which applies to Directors, employees and contractors of the Company. <p>The Corporate Code of Conduct is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> The Board is informed of any material breaches of the Corporate Code of Conduct.
Recommendation 3.3 A listed entity should: <ul style="list-style-type: none"> (a) have and disclose a whistleblower policy; and (b) ensure that the board or a committee of the board is informed of any material incidents reported under that policy. 	Yes	The Company has adopted a Whistleblower Policy which is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors . <p>Clause 7 of the Whistleblower Policy provides that the board is informed of any material incidents reported.</p>
Recommendation 3.4 A listed entity should: <ul style="list-style-type: none"> (a) have and disclose an anti-bribery and corruption policy; and (b) ensure that the board or committee of the board is informed of any material breaches of that policy. 	Yes	The Company has adopted an anti-bribery and anti-corruption (ABC) policy which applies to all officers, employees, and contractors who represent the Company. <p>The ABC policy is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> Clause 8.2 of the ABC Policy provides that all material breaches of the ABC Policy must be reported immediately to the Board.

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Principle 4: Safeguard the integrity of corporate reports		
<p>Recommendation 4.1 The board of a listed entity should:</p> <p>(a) have an audit committee which:</p> <p>(i) has at least three members, all of whom are non-executive Directors and a majority of whom are independent Directors; and</p> <p>(ii) is chaired by an independent Director, who is not the chair of the board,</p> <p>and disclose:</p> <p>(iii) the charter of the committee;</p> <p>(iv) the relevant qualifications and experience of the members of the committee; and</p> <p>(v) in relation to each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or</p> <p>(b) if it does not have an audit committee, disclose that fact and the processes it employs that independently verify and safeguard the integrity of its financial reporting, including the processes for the appointment and removal of the external auditor and the rotation of the audit engagement partner.</p>	<p>No</p> <p>Yes</p> <p>N/A</p> <p>N/A</p> <p>Yes</p>	<p>Due to the current size of the Company, the Board has determined that the function of the Audit and Risk Committee is most efficiently carried out with full Board participation and accordingly, the Company has elected not to establish a separate Audit and Risk Committee at this stage. As a result, the duties that would ordinarily be assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter are carried out by the full board.</p> <p>The Audit and Risk Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>The Board devotes time on at least an annual basis to consider the robustness of the various internal control systems it has in place to safeguard the integrity of the Company's financial reporting.</p> <p>In addition, following the completion of each half year review and annual audit review, the Company's external auditors confer with the Board on any matters identified during the course of the audit that have the potential to increase the Company's exposure to risks of material misstatements in its financial reports.</p> <p>The full Board also assumes responsibility for recommendations to security holders on the appointment and removal of the external auditor. Audit partner rotations will be enforced in accordance with the relevant guidelines.</p>
<p>Recommendation 4.2 The board of a listed entity should, before it approves the entity's financial statements for a financial period, receive from its CEO and CFO a declaration that the financial records of the entity have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.</p>	Yes	<p>Prior to the execution of the financial statements of the Company, the Company's Managing Director and Chief Financial Officer provide the Board with written assurances that the financial records of the Company have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the Company and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively in all material aspects.</p>
<p>Recommendation 4.3 A listed entity should disclose its process to verify the integrity of any periodic corporate report it releases to the market that is not audited or reviewed by an external auditor.</p>	Yes	<p>The Board ensures that any periodic corporate report the Company releases to the market that has not been subject to audit or review by an external auditor discloses the process taken to verify the integrity of its content.</p>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
Principle 5: Make timely and balanced disclosure		
Recommendation 5.1 A listed entity should have and disclose a written policy for complying with its continuous disclosure obligations under listing rule 3.1.	Yes	The Company has adopted a Continuous Disclosure Policy which details the processes and procedures which have been adopted by the Company to ensure that it complies with its continuous disclosure obligations as required under the ASX Listing Rules and other relevant legislation. The Company's Continuous Disclosure Policy is contained within the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors .
Recommendation 5.2 A listed entity should ensure that its board receives copies of all material market announcements promptly after they have been made.	Yes	The Company Secretary ensures the Board is provided with copies of all material market announcements promptly after they have been made.
Recommendation 5.3 A listed entity that gives a new and substantive investor or analyst presentation should release a copy of the presentation materials on the ASX Market Announcements Platform ahead of the presentation.	Yes	Pursuant to the Company's Continuous Disclosure Policy ahead of any new and substantive investor or analyst presentation, a copy of the presentation materials must be released to ASX (even if the information in the presentation would not otherwise require market disclosure). The Company's Continuous Disclosure Policy is contained within the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors .
Principle 6: Respect the rights of security holders		
Recommendation 6.1 A listed entity should provide information about itself and its governance to investors via its website.	Yes	Shareholders can access information about the Company and its governance (including its constitution and adopted corporate governance policies) from the Company's website https://www.droneshield.com/investors . The Company will regularly update the website and contents therein as deemed necessary.
Recommendation 6.2 A listed entity should have an investor relations program that facilitates effective two-way communication with investors.	Yes	The Company has adopted a Shareholder Communications Strategy which aims to promote and facilitate effective two-way communication with investors. The Strategy outlines a range of ways in which information is communicated to Shareholders, including via its website, through announcements released to the ASX, its annual report and general meetings. Shareholders are also welcome to contact the Company or its registrar, Automic Registry Services, via email or telephone. The Company's Shareholder Communications Strategy is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors .

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
<p>Recommendation 6.3</p> <p>A listed entity should disclose how it facilitates and encourages participation at meetings of security holders.</p>	Yes	<p>As noted above, the Company's Shareholder Communications Strategy is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors. Shareholders will be encouraged to participate at all general meetings of the Company by written statement contained in every Notice of Meeting sent to shareholders prior to each meeting.</p> <p>The Company intends to accommodate shareholders who are unable to attend general meetings in person by accepting votes by proxy. Further, any material presented to shareholders at the meeting will be released to the ASX immediately prior to the commencement of the meeting for the benefit of those shareholders who are unable to attend in person. The Company will also announce to the ASX the outcome of each meeting immediately following its conclusion.</p> <p>At each general meeting, shareholders will be given an opportunity to ask questions in relation to the resolutions put to shareholders at that meeting, and in respect of the Company's business and operations generally.</p> <p>At each AGM, shareholders will also be invited by the Chairman to ask questions of the Company's external auditor and the Board in relation to the annual financial report of the Company and the conduct of the audit.</p>
<p>Recommendation 6.4</p> <p>A listed entity should ensure that all substantive resolutions at a meeting of security holders are decided by a poll rather than by a show of hands.</p>	Yes	<p>The Company's Shareholder Communications Strategy provides that all substantive resolutions at a meeting of security holders will be decided by a poll rather than a show of hands.</p>
<p>Recommendation 6.5</p> <p>A listed entity should give security holders the option to receive communications from, and send communications to, the entity and its security registry electronically.</p>	Yes	<p>Shareholders have the option of electing to receive all shareholder communications by e-mail and can update their communication preferences with the Company's registrar, Automic Registry Services, at any time.</p> <p>Security holders can also register with the Company at info@droneshield.com to receive email notifications following the release of a material announcement to the ASX.</p>
<p>Principle 7: Recognise and manage risk</p>		
<p>Recommendation 7.1</p> <p>The board of a listed entity should:</p> <ul style="list-style-type: none"> (a) have a committee or committees to oversee risk, each of which: <ul style="list-style-type: none"> (i) has at least three members, a majority of whom are independent Directors; and (ii) is chaired by an independent Director, and disclose: <ul style="list-style-type: none"> (iii) the charter of the committee; (iv) the members of the committee; and (v) as at the end of each reporting period, the number of times the committee met throughout the period and the 	<p>No</p> <p>Yes</p> <p>N/A</p> <p>N/A</p>	<p>Due to its size, the Board has determined that the function of the Audit and Risk Committee is most efficiently carried out with full Board participation and accordingly, the Company has elected not to establish a separate Audit and Risk Committee at this stage.</p> <p>As a result, the duties that would ordinarily be assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter are carried out by the full Board.</p> <p>The Audit and Risk Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website https://www.droneshield.com/investors.</p>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
<p>individual attendances of the members at those meetings; or</p> <p>(b) if it does not have a risk committee or committees that satisfy (a) above, disclose that fact and the process it employs for overseeing the entity's risk management framework.</p>	Yes	The Board devotes time on at least an annual basis to fulfil the roles and responsibilities associated with overseeing risk and maintaining the Company's risk management framework and associated internal compliance and control procedures.
<p>Recommendation 7.2</p> <p>The board or a committee of the board should:</p> <p>(a) review the entity's risk management framework at least annually to satisfy itself that it continues to be sound and that the entity is operating with due regard to the risk appetite set by the board; and</p> <p>(b) disclose in relation to each reporting period, whether such a review has taken place.</p>	No	The Board, in carrying out the duties typically assigned to the Audit and Risk Committee under the Audit and Risk Committee Charter, will undertake a review of the Company's risk management framework in line with its Risk Management Policy.
<p>Recommendation 7.3</p> <p>A listed entity should disclose:</p> <p>(a) if it has an internal audit function, how the function is structured and what role it performs; or</p> <p>(b) if it does not have an internal audit function, that fact and the processes it employs for evaluating and continually improving the effectiveness of its governance, risk management and internal control processes.</p>	<p>N/A</p> <p>Yes</p>	Due to the current size of the Company and the manageable scale of its operations, the Board, in carrying out the duties typically assigned to the Audit & Risk Committee under the Audit & Risk Committee Charter, have determined that the Company's existing risk management processes and internal controls are sufficiently robust and as such, no internal audit committee is required at this stage.
<p>Recommendation 7.4</p> <p>A listed entity should disclose whether it has any material exposure to environmental or social risks and, if it does, how it manages or intends to manage those risks.</p>	Yes	<p>The Company's Risk Management Policy details the Company's risk management systems which assist in identifying and managing potential or apparent business, economic, environmental and social sustainability risks (where appropriate).</p> <p>All material risks are announced to the market, in accordance with the requirements of the ASX listing rules and otherwise.</p>
Principle 8: Remunerate fairly and responsibly		
<p>Recommendation 8.1</p> <p>The board of a listed entity should:</p> <p>(a) have a remuneration committee which:</p> <p>(i) has at least three members, a majority of whom are independent Directors; and</p> <p>(ii) is chaired by an independent Director,</p> <p>and disclose:</p> <p>(iii) the charter of the committee;</p> <p>(iv) the members of the committee; and</p> <p>(v) as at the end of each reporting period, the number of times the committee met throughout the period and the individual attendances of the members at those meetings; or</p> <p>(b) if it does not have a remuneration committee, disclose that fact and the processes it employs for setting the level and composition of remuneration</p>	<p>No</p> <p>Yes</p> <p>N/A</p> <p>N/A</p> <p>Yes</p>	<p>Due to the size of the Board and the scale of the Company's operations, the Board have determined that the function of the Remuneration Committee is most efficiently carried out with full Board participation (to the extent permitted under the Corporations Act and ASX Listing Rules), and accordingly has elected not to establish a separate Remuneration Committee at this stage.</p> <p>As a result, the duties that would ordinarily be assigned to the Remuneration Committee under the Remuneration Committee Charter are carried out by the full Board.</p> <p>The Remuneration Committee Charter is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p>

PRINCIPLES AND RECOMMENDATIONS	COMPLY (YES/NO)	EXPLANATION
for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive.		The Board devotes time on at least an annual basis to fulfil the roles and responsibilities associated with setting the level and composition of remuneration for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive.
<p>Recommendation 8.2</p> <p>A listed entity should separately disclose its policies and practices regarding the remuneration of non-executive Directors and the remuneration of executive Directors and other senior executives.</p>	Yes	<p>The Company's general policies and practices regarding the remuneration of Non-Executive and Executive Directors and other senior employees are set out in the Remuneration Policy which is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>Further information regarding the remuneration practices of the Company is contained in the Remuneration Report on pages 24 to 30.</p>
<p>Recommendation 8.3</p> <p>A listed entity which has an equity-based remuneration scheme should:</p> <ul style="list-style-type: none"> (i) have a policy on whether participants are permitted to enter into transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme; and (ii) disclose that policy or a summary of it. 	Yes	<p>The Company's Remuneration Committee (the function of which is currently performed by the full Board) is responsible for the review and approval of any equity-based remuneration schemes offered to Directors and Employees of the Company.</p> <p>Further, in accordance with the Remuneration Committee Charter, the Remuneration Committee (the function of which is currently performed by the full Board) is also responsible for granting permission, on a case-by-case basis, for scheme participants to enter transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme.</p> <p>During the 2022 financial year, the Board of the Company authorised the issue of securities to employees under its Incentive Option Plan. To date, no participant to the Incentive Option Plan has sought (or been granted) approval to enter into transactions (whether through the use of derivatives or otherwise) which limit the economic risk of participating in the scheme.</p> <p>The Company's policy in this regard is set out in the Company's Remuneration Committee Charter, a copy of which is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p> <p>The Company also has a Securities Trading Policy that prohibits Directors, Officers and employees from entering into transactions or arrangements which limits the economic risk of participating in unvested entitlements under any equity-based remuneration scheme.</p> <p>A copy of the Securities Trading Policy is contained in the Company's Corporate Governance Plan which is available on the Company's website at: https://www.droneshield.com/investors.</p>

Directors' Report

Your Directors present their report for DroneShield Limited (the "Company") and its controlled entities ("the Group") for the year ended 31 December 2022.

Directors

The names of the Company's Directors in office during the year and until the date of this report are set out below. Directors were in office for this entire period unless otherwise stated. Details of the current members of the Board, including their experience, qualifications, special responsibilities and term of office are included on page 7 of the Annual Report.

Name	Position	Effective date
Directors		
Peter James	Independent Non-Executive Chairman	Appointed as Independent Non-Executive Chairman 1 April 2016. Served as Executive Chairman from 2 December 2016. Returned to Independent Non-Executive Chairman 24 January 2017.
Oleg Vornik	Executive Director, CEO and Managing Director	Appointed as CEO and Managing Director 24 January 2017.
Jethro Marks	Independent Non-Executive Director	Appointed 16 January 2020.

Meetings of Directors

Name	Meetings eligible to attend	Meetings attended
Directors		
Peter James	12	12
Oleg Vornik	12	12
Jethro Marks	12	12

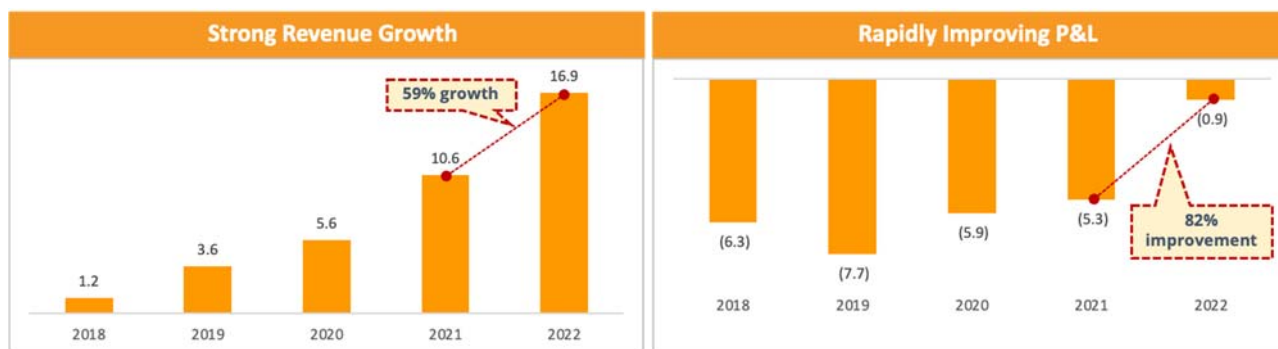
For personal use only

Review of Operations and Financial Results

The Company recorded another record results year by a substantial margin, with revenues up 59% to \$16.9 million, while cash receipts from sales and grants have risen to \$15.6 million, as the counterdrone industry continues to rapidly grow and defence and security budgets rise with an increasing uncertainty globally, underscored by the Ukraine war.

DroneShield has also continued to rapidly improve its bottom-line, closing the 2022 year with a net P&L of only (\$949k) – an 82% improvement over previous year, as the Company continues rapid trajectory to profitability.

This performance has continued a string of record years for the business since its listing in 2016. The closing cash and term deposits balance as at 31 December 2022 was \$10.3 million. Approximate bank balance as of the date of this report is \$20.5 million, providing a strong base for working capital acquisition for rapid order fulfilment.



Highlights during the year have included:

- [Record \\$11 million order](#) received in December followed by [another \\$11 million order](#) from a different Government customer on 9 January 2023, as well as numerous smaller contracts. The Ukraine situation continues to drive the requirement for counterdrone equipment, following initial successful sale of the Company's equipment to Ukraine at the start of the war. Importantly, this is expected to be a permanent increase in requirement, to be sustained after the Ukraine war ends, as militaries and Government agencies around the world are seeking to establish inventory of counterdrone systems, usually from little or no existing stock of such systems.
- Entering 2023 with a record order backlog of \$24 million in cash receipts (committed contract payments due to be paid this year), and a \$200 million² in sales pipeline.
- [Recommendation by the Joint Counter-small Unmanned Aircraft Systems Office](#) (JCO) for a rollout across US Department of Defense nationwide, expected to commence this year.
- [Successful completion](#) of \$800k Australian DoD Defence Innovation Hub project.
- [Selection](#) for the Australian DoD Intelligence, Surveillance, Reconnaissance and Electronic Warfare (ISREW) Standing Panel, exposing DroneShield to a number of additional opportunities in those sectors.
- Collaboration agreement with The Australian Missile Corp Corporation (AMC), as the \$1bn Guided Weapons and Explosive Ordnance (GWEO) enterprise enters the next phase.
- [Successful completion](#) of a key Canadian military exercise.
- [SBIR project](#) awarded by US DoD with partner Quantum Research International.
- [Initial paid US civilian airport deployment](#) – a reference case and pathway to further sales.
- 5-year Contract Framework with the State of Texas, enabling a more streamlined purchasing process.
- Initial U.S. General Services Administration (GSA) order to a Homeland Security agency for a DroneSentry™ variant.
- Paid permanent deployment at a major tier 1 airport in Asia-Pacific, and selection as a short-listed tendered for a major nation-wide deployment in another Asia-Pacific country.
- [\\$3.7 million investment from Epirus Inc](#) in November, a high-growth U.S. defense technology company developing software-defined directed energy systems.

² Necessarily, not all (and there can be no assurance that any) of the Company's sales opportunities will result in sales.

- [Deployment](#) by Swiss Police for protection of Davos 2022.
- [Deployment](#) at IRONMAN Texas 2022.
- New partnership [XRG](#), for Extended Reality C-UAS training, as well as partnerships with Nearmap, Trakka, and a further collaboration strengthening with Thales.
- Launch of a [dedicated testing facility](#) in Australia.
- High-profile DroneGun deployment at [Brazil presidential inauguration](#) (held in early January 2023).
- Participation at a number of industry events as the world starts to re-open following the pandemic, including Global SOF (Special Operator Forces) event in Budapest, Army USA (AUSA) in Washington DC and Land Forces in Brisbane.
- Continued move to a SaaS model, via three subscription products:
 - Quarterly updates to Artificial Intelligence (AI) engine software running on hardware of RfPatrol™, DroneSentry-X™ and RfOne™.
 - Quarterly firmware updates to the camera AI engine DroneOptID™.
 - DroneSentry-C2™ Command-and-Control and analytics software.
- [Reaching](#) UK MOD SAPIENT compliance.
- Commencement of Sydney-based manufacturing of drone smart jammers, following receipt of the first exemption permit of its kind to undertake advanced testing and manufacturing of the Company's Electronic Warfare and counterdrone portfolio in Australia by the Australian Communications and Media Authority (ACMA), the regulator of the communications spectrum nationally. This permit accelerates the development and optimisation of advanced Artificial Intelligence-powered electronic warfare and counter-terrorism technologies here in Australia.

Principal Activities

The principal activity of the Company is the development, commercialisation and sales of hardware and software technology for drone detection and security.

Significant Changes in the State of Affairs

Other than discussed in the Review of Operations above, there have been no significant changes in the state of affairs of the Company during the year ended 31 December 2022.

Significant Events after the Balance Date

Subsequent to 31 December 2022, the following occurred;

- In January 2023, the Company received a new purchase order for approximately \$11 million from a government agency customer.
- In February 2023, the Company issued 36,266,666 shares in a share placement. The issue price was \$0.30, and the total cash received from the placement of shares was \$10,880,000. Under the terms of the Placement, brokers participating in the Placement will receive a commission on the funds raised.
- As of close of 28 February 2023, the Company will be admitted into the MSCI Global Micro Cap Index.

Likely developments and expected results of operations

Refer to the Chairman's Review to shareholders, on page 3, for further information on likely developments and expected results of the Group.

Environmental regulation

The Group's operations are not subject to any significant environmental regulation under either Commonwealth or State legislation. The Board considers that adequate systems are in place to manage the Group's obligations and is not aware of any breach of environmental requirements as they relate to the Group.

Dividends

No dividends were declared or paid to shareholders during the financial year (2021: \$nil).

Insurance of officers

During or since the end of the financial year the Company has paid, or agreed to pay, premiums to insure persons who are, or have been, an officer of the Company, or any past, present or future Director or officer of the Company. The contracts prohibit disclosure of the amount of the premium paid. The liabilities insured include costs and expenses that may be incurred in defending civil or criminal proceedings that may be brought against the officers in their capacity as officers of entities of the Group.

Proceedings on behalf of the Company

No proceedings have been brought or intervened in on behalf of the Group with leave of the Court under section 237 of the *Corporations Act 2001*.

Non-audit services

The Company may decide to employ the auditor on assignments additional to their statutory audit duties where the auditor's expertise and experience with the Company and/or the Group are important.

Details of the amounts paid or payable to the auditor (HLB Mann Judd Assurance (NSW) Pty Ltd) for audit and non-audit services provided during the year are outlined in Note 29 of the financial statements.

The Board of Directors has considered the position and is satisfied that the provision of non-audit services is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The Directors are satisfied that the provision of non-audit services provided by the auditor did not compromise the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services have been reviewed by the Board to ensure they do not impact the objectives and impartiality of the auditor;
- none of the services undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*, including review or auditing the auditor's own work, acting in a management or decision-making capacity for the Group, acting as advocate for the Group or jointly sharing economic risks and rewards.

Auditor's Independence Declaration

A copy of the auditor's independence declaration as required under the Section 307C of the *Corporations Act 2001* is set out on page 31.

For personal use only

Directors' Report- Remuneration Report (audited)

Executive remuneration governance

The Board reviews and approves the remuneration policy to enable the Company to attract and retain executives and Directors who will create value for shareholders having consideration to the amount deemed to be commensurate for a company of its size and level of activity as well as the relevant Directors' time, commitment and responsibility. The Board is also responsible for reviewing any employee incentive and equity-based plans including the appropriateness of performance hurdles and total payments proposed.

Remuneration committee

Due to the size and nature of the existing Board and the magnitude of the Company's operations, the Company does not currently have a Remuneration Committee. In accordance with the Company's Corporate Governance Plan, which is available on the Company's website <https://www.droneshield.com/investors>, the full Board currently carries out the duties that would ordinarily be assigned to the Remuneration Committee under the written terms of reference for that committee.

The Board will devote time on an annual basis to fulfil the roles and responsibilities associated with setting the level and composition of remuneration for Directors and senior executives and ensuring that such remuneration is appropriate and not excessive. The Managing Director of the Company is responsible for evaluating the performance of senior executives on an annual basis. The Board of Directors is responsible for overseeing the Managing Director's performance evaluations. This evaluation is based on specific criteria, including the business performance of the Company, whether strategic objectives are being achieved and the development of management and personnel.

Directors' remuneration

The remuneration of an Executive Director is decided by the Board, without the affected Executive Director participating in that decision-making process.

The total maximum remuneration of Non-Executive Directors is initially set by the Board and subsequent variation is by ordinary resolution of shareholders in general meeting in accordance with the Constitution, the *Corporations Act 2001* and the ASX Listing Rules, as applicable.

The determination of Non-Executive Directors' remuneration within that maximum will be made by the Board having regard to the inputs and value to the Company of the respective contributions by each Non-Executive Director. The current amount has been set at an amount not to exceed \$500,000 per annum.

In addition, a Director may be paid fees or other amounts (i.e. subject to any necessary shareholder approval, non-cash performance incentives such as options) as the Directors determine where a Director performs special duties or otherwise performs services outside the scope of the ordinary duties of a Director.

Directors are also entitled to be paid reasonable travelling, hotel and other expenses incurred by them respectively in or about the performance of their duties as Directors.

The Group's remuneration policy for Executive Directors (including the Managing Director) and senior management is designed to promote superior performance and long-term commitment to the Group. Executives receive a base remuneration which is market related and may also be entitled to performance-based remuneration at the ultimate discretion of the Board.

Overall remuneration policies are subject to the discretion of the Board and can be changed to reflect competitive market and business conditions where it is in the interests of the Group and the Company's shareholders to do so.

Executive remuneration framework

The Group's reward policy reflects the benefits of aligning executive remuneration with shareholders' interests and to retain appropriately qualified executive talent for the benefit of the Group. The main principles of the policy are:

- (a) remuneration is reasonable and fair, taking into account the Group's obligations at law, the competitive market in which the Group operates and the relative size and scale of the Group's business;
- (b) individual reward should be linked to clearly specified performance targets which should be aligned to the Group's short term and long-term performance objectives; and
- (c) executives should be rewarded for both financial and non-financial performance.

The total remuneration of Executive Directors (including the Managing Director) and other senior managers consist of the following:

- (a) Salary – Executive Directors and senior managers may receive a fixed sum payable monthly in cash;
- (b) Short term incentive – Executive Directors and nominated senior managers are eligible to participate in a profit participation plan if deemed appropriate. The Board may at its discretion award bonuses for exceptional performance in relation to each person’s pre-agreed Key Performance Indicators;
- (c) Post-employment benefits – this refers to superannuation schemes; and
- (d) Long term incentives – Executive Directors may participate in share option schemes with the prior approval of shareholders. Executives may also participate in employee share option schemes, with any option issues generally being made in accordance with thresholds set in plans approved by shareholders. The Board, however, considers it appropriate to retain the flexibility to issue options to executives outside of approved Employee Option Plans in exceptional circumstances.

KMP remuneration disclosures in detail

The Directors and other Key Management Personnel (“KMP”) of the Company during or since the end of the financial year were:

Name	Position	Effective date
Non-Executive Directors		
Peter James	Independent Non-Executive Chairman	Appointed as Independent Non-Executive Chairman 1 April 2016. Served as Executive Chairman from 2 December 2016. Returned to Independent Non-Executive Chairman 24 January 2017.
Jethro Marks	Independent Non-Executive Director	Appointed 16 January 2020.
Executive Director		
Oleg Vornik	Executive Director, Managing Director and CEO	Appointed as CEO and Managing Director 24 January 2017.

Directors' Report- Remuneration Report *continued*

Shareholdings of KMP

The number of shares in the Company and subsidiary held during the financial year by each Director of DroneShield and other KMP (of which there are none), including their personally related entities, are set out in the following table:

31 December 2022	Opening balance (Number)	(a) Received during the year on exercise of options (Number)	(b) Other changes during the year (Number)	Balance at 31 December 2022 (Number)
Non-Executive Directors				
Peter James	10,052,522	132,500	(883,334)	9,301,688
Jethro Marks	583,333	83,333	-	666,666
Executive Director				
Oleg Vornik	16,827,022	250,000	(1,766,666)	15,310,356
Total	27,462,877	465,833	(2,650,000)	25,278,710

Notes

- The options exercised during the year were exercised at \$0.65 per share, using a limited recourse loan provided by the Company. The loan is interest free and due for repayment by 18 March 2027. The loan is non-recourse except against the shares issued on exercise of the options and are held by the Directors.
- Shares sold during the year to cover tax liability associated with vesting of DroneShield options.

31 December 2021	Opening balance (Number)	(a) Received during the year on exercise of options (Number)	(b) Other changes during the year (Number)	Balance at 31 December 2021 (Number)
Non-Executive Directors				
Peter James	3,452,522	6,600,000	-	10,052,522
Jethro Marks	83,333	500,000	-	583,333
Executive Director				
Oleg Vornik	4,370,022	12,400,000	57,000	16,827,022
Total	7,905,877	19,500,000	57,000	27,462,877

Notes

- The options exercised by Jethro Marks during the year were exercised at \$0.25 per share, using a limited recourse loan provided by the Company. The loan is interest free and due for repayment by June 2026. The loan is non-recourse except against the shares issued on exercise of the options and are held by Jethro Marks. The options exercised by Peter James and Oleg Vornik were Performance Options, which vested during the year.
- Shares purchased during the year.

Directors' Report- Remuneration Report *continued*

Share options held by KMP

31 December 2022	Opening balance (Number)	Granted as compensation (Number)	Options lapsed (Number)	(a) Options exercised (Number)	Balance at 31 December 2022 (Number)	Vested Options December 2022 (Number)	Unvested Options December 2022 (Number)
Non-Executive Directors							
Peter James	662,500	5,000,000	(397,500)	(132,500)	5,132,500	132,500	5,000,000
Jethro Marks	166,667	1,000,000	-	(83,333)	1,083,334	83,334	1,000,000
Executive Director							
Oleg Vornik	1,250,000	10,000,000	(750,000)	(250,000)	10,250,000	250,000	10,000,000
Total	2,079,167	16,000,000	(1,147,500)	(465,833)	16,465,834	465,834	16,000,000

Notes

- (a) The options exercised during the year were exercised at \$0.65 per share, using a limited recourse loan provided by the Company. The loan is interest free and due for repayment by 18 March 2027. The loan is non-recourse except against the shares issued on exercise of the options and are held by the Directors.

31 December 2021	Opening balance (Number)	Granted as compensation (Number)	Options lapsed (Number)	(a) Options exercised (Number)	Balance at 31 December 2021 (Number)	Vested Options December 2021 (Number)	Unvested Options December 2021 (Number)
Non-Executive Directors							
Peter James	7,262,500	6,600,000	(6,600,000)	(6,600,000)	662,500	-	662,500
Jethro Marks	166,667	500,000	-	(500,000)	166,667	83,333	83,334
Executive Director							
Oleg Vornik	13,650,000	12,400,000	(12,400,000)	(12,400,000)	1,250,000	250,000	1,000,000
Total	21,079,167	19,500,000	(19,000,000)	(19,500,000)	2,079,167	333,333	1,745,834

Notes

- (a) The options exercised by Jethro Marks during the year were exercised at \$0.25 per share, using a limited recourse loan provided by the Company. The loan is interest free and due for repayment by June 2026. The loan is non-recourse except against the shares issued on exercise of the options and are held by Jethro Marks. The options exercised by Peter James and Oleg Vornik were Performance Options, which vested during the year.

Directors' Report- Remuneration Report *continued*

Performance based remuneration granted and exercised during the year

	31 December 2022		31 December 2021	
	(a) Value granted \$	(b) Value exercised \$	(a) Value granted \$	(b) Value exercised \$
Non-Executive Directors				
Peter James	1,175,000	13,515	1,122,000	1,122,000
Jethro Marks	235,000	2,429	33,179	33,179
Executive Directors				
Oleg Vornik	2,350,000	25,499	2,232,000	2,232,000
Total	3,760,000	41,443	3,387,179	3,387,179

Notes

- (a) The value at grant date is calculated using the Black-Scholes Model.
 (b) The value of the options exercised is calculated using the Black-Scholes Model.

Terms and conditions of the share-based payment arrangements

The terms and conditions of each grant of options affecting remuneration in the current or a future reporting period are as follows:

Class of Options issued during 2022	Number of Options	Grant date	Vesting date	Expiry date	Exercise Price	Value per option at grant date \$	Performance achieved	% Vested during 2022
Performance Options	16,000,000	26-Apr-22	29-Apr-27	29-Apr-27	-	0.24	No	0%

Class of Options issued during 2021	Number of Options	Grant date	Vesting date	Expiry date	Exercise Price	Value per option at grant date \$	Performance achieved	% Vested during 2021
Performance Options	12,400,000	26-May-21	16-Aug-21	31-Aug-24	-	0.22	Yes	100%
Performance Options U	6,600,000	27-May-21	16-Aug-21	31-Aug-24	-	0.22	Yes	100%
	500,000	26-May-21	27-May-21	27-May-24	0.25	0.07	Yes	100%

Directors' Report- Remuneration Report *continued*

Remuneration details of KMP

31 December 2022	Salary and fees \$	Movement in employee provisions \$	Cash incentive \$	Post- employment benefits \$	Share based payments (options) \$	Total \$
Non-Executive Directors						
Peter James	99,993	-	-	-	93,442	193,435
Jethro Marks	50,000	-	-	-	32,977	82,977
Executive Director						
Oleg Vornik (a)	306,195	(10,022)	-	24,430	195,463	516,066
Total	456,188	(10,022)	-	24,430	321,882	792,478

31 December 2021	Salary and fees \$	Movement in employee provisions \$	Cash incentive \$	Post- employment benefits \$	Share based payments (options) \$	Total \$
Non-Executive Directors						
Peter James	99,993	-	45,455	-	210,440	355,888
Jethro Marks	50,000	-	-	-	36,022	86,022
Executive Director						
Oleg Vornik (a)	307,369	63,727	150,000	22,631	419,107	962,834
Total	457,362	63,727	195,455	22,631	665,569	1,404,744

The relative proportions of remuneration that are linked to performance and those that are fixed are as follows:

	Fixed		Performance	
	2021	2022	2021	2022
Non-Executive Directors				
Peter James	28%	52%	72%	48%
Jethro Marks	58%	60%	42%	40%
Executive Director				
Oleg Vornik	41%	62%	59%	38%

The performance component of remuneration received by Directors relates to share options. The issue of share options to Directors is subject to shareholder approval. Remuneration in the form of DroneShield share options is used as a tool to align KMP remuneration with shareholder interests.

The employment agreement of the Executive Director during the year included the following key terms:

Name	Positions held during the year	Key terms of employment agreement
Oleg Vornik	CEO and Managing Director	<ul style="list-style-type: none"> - Remuneration of \$300,000p.a. plus superannuation - Eligible to participate in short term incentive program - Eligible to participate in long term incentive program - A notice period of 3 months, except in defined circumstances - No fixed term

Directors' Report- Remuneration Report *continued*

Advisory Board remuneration

For the year-ended 2022 and 2021, there was no Advisory Board.

End of Remuneration Report.

This Directors' Report is made in accordance with a resolution of Directors.



Peter James
Independent Non-Executive Chairman
Sydney, NSW
27 February 2023

For personal use only

Auditor's Independence Declaration

To the directors of DroneShield Limited:

As lead auditor for the audit of the consolidated financial report of DroneShield Limited for the year ended 31 December 2022, I declare that, to the best of my knowledge and belief, there have been no contraventions of:

- (a) the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- (b) any applicable code of professional conduct in relation to the audit.

This declaration is in relation to DroneShield Limited and the entities it controlled during the period.



Sydney, NSW
27 February 2023

N J Guest
Director

hlb.com.au

HLB Mann Judd Assurance (NSW) Pty Ltd ABN 96 153 077 215

Level 5, 10 Shelley Street Sydney NSW 2000 Australia

T: +61 (0)2 9020 4000 **E:** mailbox@hlbnsw.com.au

Liability limited by a scheme approved under Professional Standards Legislation.

HLB Mann Judd is a member of HLB International, the global advisory and accounting network.

For personal use only

Consolidated Statement of Profit or Loss and Other Comprehensive Income

	Note	31 December 2022 \$	31 December 2021 \$
Revenue	3	16,886,081	10,598,124
Other income	4	272,254	345,687
Cost of sales		(4,976,034)	(2,849,001)
Product development expense	5	(6,616,104)	(5,569,604)
Sales and customer service expense	6	(3,302,029)	(2,832,455)
Corporate and support expense	7	(3,689,389)	(4,253,768)
Corporate governance expense	8	(787,730)	(669,222)
Share based payment expense	9	(715,881)	(1,168,041)
Loss before income tax		(2,928,832)	(6,398,280)
Income tax benefit	10	1,979,531	1,087,833
Loss after income tax		(949,301)	(5,310,447)
Other comprehensive income:			
<i>Items that may be reclassified to profit or loss</i>			
Adjustments on translation of foreign controlled entity		97,420	136,376
Total comprehensive loss for the period		(851,881)	(5,174,071)
Basic loss per share	23	(0.002)	(0.013)
Diluted loss per share	23	(0.002)	(0.013)

The above Consolidated Statement of Profit or Loss and Other Comprehensive Income should be read in conjunction with the accompanying notes.

Consolidated Statement of Financial Position

	Note	31 December 2022 \$	31 December 2021 \$
ASSETS			
Current assets			
Cash and cash equivalents	11	10,143,861	9,419,235
Trade and other receivables	12	8,316,648	859,131
Inventories	13	3,733,416	6,915,939
Other investments	14	75,000	75,000
Total current assets		22,268,925	17,269,305
Non-current assets			
Plant, equipment and intangible assets	15	2,436,271	1,028,471
Right-of-use assets	16	458,956	-
Other investments	14	42,900	42,900
Total non-current assets		2,938,127	1,071,371
Total assets		25,207,052	18,340,676
LIABILITIES			
Current liabilities			
Trade payables		564,231	478,382
Provisions	17	427,235	408,631
Other liabilities	18	4,555,326	1,566,894
Lease liabilities	19	526,045	152,985
Borrowings	20	70,052	56,584
Total current liabilities		6,142,889	2,663,476
Non-current liabilities			
Provisions	17	64,760	54,995
Lease liabilities	19	-	38,802
Total non-current liabilities		64,760	93,797
Total liabilities		6,207,649	2,757,273
Net assets		18,999,403	15,583,403
EQUITY			
Contributed equity	21	40,535,156	36,983,156
Reserves		5,088,141	5,299,211
Accumulated losses		(26,623,894)	(26,698,964)
Total equity		18,999,403	15,583,403

The above Consolidated Statement of Financial Position should be read in conjunction with the accompanying notes.

For personal use only

Consolidated Statement of Changes in Equity

	Contributed equity \$	Options reserve \$	Foreign currency translation reserve \$	Accumulated losses \$	Total equity \$
Balance at 1 January 2021	37,283,293	7,777,980	(12,168)	(25,459,672)	19,589,433
Transfer from option reserve to accumulated losses	-	(3,771,018)	-	3,771,018	-
<i>Transactions with owners in their capacity as owners:</i>					
Net share-based payments movement	-	1,168,041	-	-	1,168,041
Equity transaction costs	(300,137)	-	-	300,137	-
	<u>(300,137)</u>	<u>1,168,041</u>	<u>-</u>	<u>300,137</u>	<u>1,168,041</u>
Exchange difference on translation of foreign operations	-	-	136,376	-	136,376
Loss for the period	-	-	-	(5,310,447)	(5,310,447)
Total comprehensive loss for the period	<u>-</u>	<u>-</u>	<u>136,376</u>	<u>(5,310,447)</u>	<u>(5,174,071)</u>
Balance at 31 December 2021	<u>36,983,156</u>	<u>5,175,003</u>	<u>124,208</u>	<u>(26,698,964)</u>	<u>15,583,403</u>
Balance at 1 January 2022	36,983,156	5,175,003	124,208	(26,698,964)	15,583,403
Transfer from option reserve to accumulated losses	-	(1,024,371)	-	1,024,371	-
<i>Transactions with owners in their capacity as owners:</i>					
Net share-based payments movement	-	715,881	-	-	715,881
Contributions of equity, net of transaction costs	3,552,000	-	-	-	3,552,000
	<u>3,552,000</u>	<u>715,881</u>	<u>-</u>	<u>-</u>	<u>4,267,881</u>
Exchange difference on translation of foreign operations	-	-	97,420	-	97,420
Loss for the period	-	-	-	(949,301)	(949,301)
Total comprehensive loss for the period	<u>-</u>	<u>-</u>	<u>97,420</u>	<u>(949,301)</u>	<u>(851,881)</u>
Balance at 31 December 2022	<u>40,535,156</u>	<u>4,866,513</u>	<u>221,628</u>	<u>(26,623,894)</u>	<u>18,999,403</u>

The above Consolidated Statement of Changes in Equity should be read in conjunction with the accompanying notes.

For personal use only

Consolidated Statement of Cash Flows

	Note	31 December 2022 \$	31 December 2021 \$
Cash flows from operating activities			
Receipts from customers		13,533,039	13,444,547
Payments to suppliers and employees		(17,465,446)	(21,060,606)
Other receipts		75,548	79,200
Research and Development Tax and other incentives received		2,090,914	1,227,121
Net cash flows used in operating activities	31	(1,765,945)	(6,309,738)
Cash flows from investing activities			
Purchase of plant and equipment		(832,175)	(467,452)
Net cash flows used in investing activities		(832,175)	(467,452)
Cash flows from financing activities			
Interest income on cash deposits		19,097	35,827
Proceeds from share and option issue		3,700,000	-
Payments for lease liabilities		(641,231)	(122,033)
Net cash flows from (used in) financing activities		3,077,866	(86,206)
Cash and cash equivalents at beginning of period		9,419,235	16,170,872
Net increase (decrease) in cash and cash equivalents		479,746	(6,863,396)
Exchange rate adjustments to balances held in foreign currencies		244,880	111,759
Cash and cash equivalents at the end of the year	11	10,143,861	9,419,235

The above Consolidated Statement of Cash Flows should be read in conjunction with the accompanying notes.

For personal use only

Notes to the Financial Statements

Corporate Information

The consolidated financial report of DroneShield Limited (“the Company”) and its controlled entities (“DroneShield” or “the Group”) for the year ended 31 December 2022 was authorised for issue in accordance with a resolution of the Directors on 27 February 2023.

DroneShield Limited is a company incorporated in Australia, limited by shares which are publicly traded on the ASX.

The principal activity of the Company is the development, commercialisation and sales of hardware and software technology for drone detection and security.

Statement of compliance

These consolidated financial statements are general purpose financial statements which have been prepared in accordance with the *Corporations Act 2001*, Accounting Standards and Interpretations, and comply with other requirements of the law.

Accounting Standards are Australian Accounting Standards (“AAS”). Compliance with AAS ensures that the financial statements and notes of the Group comply with International Financial Reporting Standards (“IFRS”).

The financial statements comprise the consolidated financial statements of the Group. For the purposes of preparing the consolidated financial statements, the Group is a for-profit entity.

1. Summary of Significant Accounting Policies

(a) Basis of preparation

The consolidated financial statements have been prepared on the basis of historical cost as explained in the accounting policies below.

The consolidated financial statements are presented in Australian dollars (“AUD”), unless otherwise noted, which is also the functional currency of the Company. The principal accounting policies are set out below.

Going Concern

This consolidated financial report has been prepared on the basis that the Group will continue to meet its commitments and can therefore continue normal business activities and realise assets and settle liabilities in the ordinary course of business.

For the year ended 31 December 2022, the Group incurred a loss after income tax of \$949,301 and net cash outflows from operating activities of \$1,765,945, with cash on hand and term deposits at 31 December 2022 of \$10,261,761. At 31 December 2022, the Group had net assets of \$18,999,403 and an excess of current assets over current liabilities of \$16,126,036.

The Group’s ability to continue as a going concern beyond this period is dependent on the availability of existing cash assets and term deposits as well as generating revenues from operations. A cash flow forecast for the next 12 months prepared by management has indicated that the Group will have sufficient cash on hand and cash generated from sales opportunities to be able to meet its debts as and when they are due, and therefore the financial statements have been prepared on a going concern basis. Subsequent to year-end, cash of \$10,880,000 was received from a share placement. Refer to Note 32 for further details on the share placement.

(b) Principles of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (i.e. subsidiaries). Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity.

Intercompany transactions, balances and unrealised gains on transactions between Group companies (if any) are eliminated. Accounting policies of all companies in the Group are consistent.

For personal use only

Notes to the Financial Statements *continued*

(c) Foreign currency translation

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the re-measurement of monetary items at year end exchange rates are recognised in profit or loss.

On consolidation, assets and liabilities have been translated into AUD at the closing rate at the reporting date. Income and expenses have been translated into AUD at the average rate over the reporting period. Exchange differences on consolidation are charged or credited to other comprehensive income and recognised in the foreign currency translation reserve in equity.

(d) Revenue recognition

The Group recognises revenue from the following major sources:

- Sale of hardware
- Subscription services
- Services

Revenue is measured based on the consideration specified in a contract with a customer. The Group recognises revenue when it transfers control of a product or service to a customer.

Sale of hardware

The Group sells hardware to distributors and directly to customers. Sales-related warranties associated with hardware can be purchased separately and they serve as an assurance that the products sold comply with agreed-upon specifications. Accordingly, the Group accounts for warranties in accordance with AASB 137 Provisions, Contingent Liabilities and Contingent Assets.

For sales of hardware to distributors, revenue is recognised when control of the hardware has transferred, being when the hardware has been shipped to the distributor's specified location (delivery) and collected from Customs by the distributor. Following delivery, the distributor has full discretion over the manner of distribution and price to sell the hardware, has the primary responsibility when on-selling the goods and where there is a risk of obsolescence and loss in relation to the goods. A receivable is recognised by the Group when the hardware is delivered to the distributor as this represents the point in time at which the right to consideration becomes unconditional, as only the passage of time is required before payment is due.

Contracts with customers have a variable sales element, dependent on volume sold. Currently, revenue from sales is fixed with no variable consideration. Contracts do not include financing components.

For sales directly to customers, revenue is recognised when control of the hardware has transferred to the customer, being at the point the hardware is delivered to the customer. Delivery occurs when the goods have been shipped to the customer's specified location. A receivable is recognised by the Group when the hardware is delivered to the customer as this represents the point in time at which the right to consideration becomes unconditional, as only the passage of time is required before payment is due.

As shipping income is directly related to the sale of hardware, it is not seen as a separate performance obligation and is recognised as and when the related hardware sale is recognised.

When the customer or distributor initially places the order, the customer or distributor is invoiced and the transaction price of the invoice at that point is recognised by the Group as deferred revenue, until control of the hardware has transferred to the customer or distributor and revenue is recognised.

Outside of warranties, customers do not have the right to return hardware sold therefore no "right to returned goods asset" is recognised.

Subscription services

The Group provides a subscription service for software updates. Such services are recognised as a performance obligation satisfied over time.

The transaction price allocated to these services is recognised as deferred revenue at the time of the initial sales transaction and is released on a straight-line basis over the period of service.

Notes to the Financial Statements *continued*

Services

The Group provides services for research and training. Such services are recognised as a performance obligation satisfied over time.

The transaction price allocated to these services is recognised as deferred revenue at the time of the initial sales transaction and is released on a straight-line basis over the period of service.

Interest income

Interest income and expenses are reported on an accrual basis using the effective interest method.

Government grant income

Income from government grants is recognised at their fair value in profit and loss when there is reasonable assurance that the grant will be received, and the Group will comply with attached conditions.

(e) Income tax

The income tax expense/ (income) for the year comprises current income tax expense/ (income) and deferred tax expense/ (income).

Current tax and deferred tax are recognised as an expense/ (income) except to the extent that they relate to a business combination or are recognised directly in equity or other comprehensive income. Current tax liabilities/ (assets) are therefore measured at the amounts expected to be paid to/ (received from) the relevant taxation authority.

Deferred income tax expense reflects movements in deferred tax assets and deferred tax liability balances during the year as well as unused tax losses.

Current and deferred income tax expense/ (income) is recognised in equity instead of profit or loss when the tax relates to items that are credited or charged directly to equity.

Except for business combinations, no deferred income tax is recognised from the initial recognition of an asset or liability where there is no effect on accounting or taxable profit or loss.

Deferred tax liabilities/ (assets) are calculated at the tax rates that are expected to apply to the period when the liability is settled (asset is realised), and their measurement also reflects the manner in which management expects to settle the carrying amount of the related liability/ (recover the assets).

Deferred tax assets relating to temporary differences and unused tax losses are recognised only to the extent that it is probable that future taxable profit will be available against which the benefits of the deferred tax asset can be utilised.

Deferred tax assets and liabilities are offset only when the Group has a right and intention to set off current tax assets and liabilities from the same taxation authority.

The research and development tax incentive claim is recognised as income tax revenue in the period in which it is received.

(f) Goods and services and other value-added taxes ("GST")

Revenue, expenses and assets are recognised net of the amount of associated GST, except where the amount of GST incurred is not recoverable from the taxation authority, in which case it is recognised as part of the acquisition cost of an asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included as part of other receivables or payables in the statement of financial position.

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 authority is classified as operating cash flows.

For personal use only

Notes to the Financial Statements *continued*

(g) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits with terms of less than three months, together with other short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

(h) Trade and other receivables

Trade and other receivables are stated at their cost less an allowance for impairment of receivables. These receivables are unsecured.

Payment for hardware sales and subscription services are due from the customer on the date the invoice is issued. Contracts do not include financing components.

Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default.

The Group applies the AASB 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables. To measure the expected credit losses, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The expected loss rates are based on the payment profiles of sales over a period of 36 months before 31 December 2022 or 1 January 2023 respectively and the corresponding historical credit losses experienced within this period.

(i) Trade and other payables

Trade and other payables are liabilities for goods and services provided to the Group prior to the end of the financial period which are unpaid. These amounts are unsecured and generally payable within 30 days of recognition.

(j) Inventories

Inventories are stated at the lower of cost and net realisable value. Costs of ordinarily interchangeable items are assigned using the average cost method. Net realisable value is the estimated selling price in the ordinary course of business less any applicable selling expenses.

(k) Leases

The Group recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, and subsequently at cost less accumulated depreciation and impairment losses and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate.

The lease liability is subsequently increased by the interest cost on the lease liability and decreased by the lease payment made. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in the estimate of the amount expected to be payable under a residual value guarantee, or as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

The Group has applied judgement to determine the lease term for some lease contracts in which it is a lessee that include renewal options. The assessment of whether the Group is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and right-of-use assets recognised.

For short-term leases (lease term of 12 months or less) and leases of low-value assets the Group will recognise a lease expense on a straight-line basis.

For personal use only

Notes to the Financial Statements *continued*

(l) Employee benefits

Wages, salaries and annual leave

Liabilities for wages and salaries, including non-monetary benefits expected to be settled within 12 months, are recognised in other payables. Annual leave is recognised in provisions and is measured using the remuneration rate expected to apply at the time of settlement.

Long service leave

The liability for long service leave is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using interest rates on national government bonds with terms to maturity that match, as closely as possible, the estimated future cash outflows.

Post-employment benefits

The Group makes fixed percentage contributions for all Australian resident employees to complying third party superannuation funds and recognises the expense as they become payable.

(m) Provisions, contingent liabilities and contingent assets

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated.

No liability is recognised if an outflow of economic resources as a result of present obligations is not probable. Such situations are disclosed as contingent liabilities, unless the outflow of resources is remote, in which case no liability is disclosed.

(n) Contributed equity

Costs directly attributable to the issue of new shares are shown as a deduction from the equity proceeds net of any income tax benefit.

(o) Plant and equipment

Plant and equipment (including fittings and furniture) are initially recognised at acquisition cost.

Depreciation is recognised on a straight-line basis to write down the cost less estimated residual value of plant and equipment. The following useful lives are applied:

Office equipment	2 – 5 years
Plant & equipment	2 – 5 years
Demonstration equipment	2 years
Vehicles and trailers	8 years

Depreciation will commence for self-constructed assets once the asset is available for use.

Material residual value estimates and estimates of useful life are updated as required, but at least annually.

Gains or losses arising on the disposal of property, plant and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognised in profit or loss within other income or other expenses.

(p) Intangible assets

Intangible assets relate to purchased computer software. Amortisation is recognised on a straight-line basis over an estimated useful economic life of 5 years. The estimated useful economic life is reviewed at the end of each reporting period with the effect of any changes in estimate being accounted for on a prospective basis.

For personal use only

Notes to the Financial Statements *continued*

(q) Earnings per share

Basic earnings per share is computed by dividing net earnings by the weighted average number of ordinary shares outstanding during each period.

Dilutive earnings per share is computed by dividing net earnings by the dilutive weighted average number of ordinary shares assuming the conversion of all dilutive potential ordinary shares.

(r) Research and development

Research is the original and planned investigation undertaken with the prospect of gaining new knowledge and understanding. Development is the application of research findings to a plan or design for the production of new or substantially improved processes or products prior to the commencement of commercial production. Research costs are expensed as they are incurred.

(s) Share-based payments

Share based compensation benefits are provided to employees via an Employee Option Plan. Information in relation to this plan is set out in Note 9.

The fair value of options granted is recognised as an employee benefits expense with a corresponding increase in equity. The total amount to be expensed is determined by reference to the fair value of the options granted, which includes any market performance conditions and the impact of any non-vesting conditions but excludes the impact of any service and non-market performance vesting conditions.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each period, the entity revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision of original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

(t) Impairment of assets

Assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely dependent of the cash inflows from other assets or other groups of assets (cash generating units).

(u) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, is the CEO.

(v) Comparative disclosures

Where appropriate, comparative disclosures have been reclassified/amended to be consistent with the current year's presentation.

(w) New accounting standards and interpretations

DroneShield has adopted all of the new, revised or amended Accounting Standards and interpretations issued by the Australian Accounting Standards Board (AASB) that are mandatory for the current reporting period. There has been no material impact on the Group on the adoption of these new standards.

There are no new Accounting Standards or interpretations that have been published, but not yet mandatory, that are expected to have a material impact on the Group.

For personal use only

Notes to the Financial Statements *continued*

2. Critical accounting judgements, estimates and assumptions

In the application of the Group's accounting policies, which are described in Note 1, the Directors are required to make judgements, estimates and assumptions in the preparation of the financial statements about matters that are not readily available from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis.

The judgements, estimates and assumptions that have a significant risk of causing a material adjustment to items (refer to the respective notes) within the next financial year are discussed below.

Licence and patent expenses

There is a degree of judgement required in respect of the capitalisation of patent costs and the future commercial application thereof. The Directors have adopted a prudent approach and all patent costs incurred have been expensed.

Share based payments

The Group measures the cost of equity settled transactions by reference to the fair value of the equity instruments at the date they are granted. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liability within the next annual reporting period but may impact profit or loss and equity. Details of the key assumptions used are set out in Note 9.

Inventories

Management estimates the net realisable values of inventories, taking into account the most reliable evidence available at each reporting date. The future realisation of these inventories may be affected by future technology or other market-driven changes that may reduce future selling prices.

Demonstration Units

Management reviews its estimate of the useful lives of demonstration assets at each reporting date, based on the expected utility of these assets. Uncertainties in these estimates relate to technical obsolescence that may change the utility of certain items.

Leases

Management estimates the Group's incremental borrowing rate which is used as the discount rate to calculate the present value of the lease payments that are not paid at the commencement date.

Judgement is also applied by management to determine the lease term for some lease contracts, in which it is a lessee, that include renewal options. The assessment of whether the Group is reasonably certain to exercise such options impacts the lease term, which significantly affects the amount of lease liabilities and right-of-use assets recognised.

For personal use only

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
3. Revenue		
Hardware sales	14,452,915	7,208,348
Services revenue	1,529,857	2,833,003
Shipping revenue	488,526	231,672
Subscription revenue	331,232	189,081
Warranty revenue	4,193	4,193
Total revenue from sales	16,806,723	10,466,297
<p>The Group derives its revenue from the transfer of goods and services over time and at a point in time. This is consistent with the revenue information that is disclosed for each reportable segment (see Note 30).</p>		
Timing of revenue recognition		
At a point in time		
Hardware sales including shipping income		
<i>direct sales</i>	7,938,000	3,854,433
<i>distributors</i>	7,003,441	3,585,587
Over time		
Subscription services		
<i>direct sales</i>	270,280	88,170
<i>distributors</i>	60,952	100,911
Services revenue		
<i>direct sales</i>	1,464,750	2,767,231
<i>distributors</i>	65,107	65,772
Warranty revenue		
<i>distributors</i>	4,193	4,193
Total revenue from sales	16,806,723	10,466,297
Other revenue		
Interest revenue	19,098	35,827
Sublease revenue	60,260	96,000
Total other revenue	79,358	131,827
Total revenue	16,886,081	10,598,124
4. Other income		
Awards and incentives revenue	111,382	269,170
Net foreign exchange gains	160,872	76,517
Total other gains	272,254	345,687

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
5. Product development expense		
Consultants	490,565	434,727
Other	1,200,069	1,130,060
Payroll	4,764,823	3,967,312
Travel, accommodation and meals	160,647	37,505
Total product development expense	6,616,104	5,569,604
6. Sales and customer service expense		
Marketing and advertising	76,447	139,860
Other	575,727	820,875
Payroll	2,325,673	1,683,332
Travel, accommodation and entertainment	324,182	188,388
Total sales and customer service expense	3,302,029	2,832,455
7. Corporate and support expense		
Legal	159,645	344,091
Office costs and communication	681,482	1,019,318
Other	774,438	424,964
Payroll	1,434,754	1,529,157
Professional expenses	563,294	908,625
Travel, accommodation and entertainment	75,776	27,613
Total corporate and support expense	3,689,389	4,253,768
8. Corporate governance expense		
ASX fees	93,953	94,746
Audit	77,365	84,916
Board expenses	212,993	195,449
Insurance	237,801	163,893
Other	94,970	56,850
Professional expenses	70,648	73,368
Total corporate governance expense	787,730	669,222

Notes to the Financial Statements *continued*

9. Options issued

During the year ended 31 December 2022, a number of options were issued to Directors, management and other employees of the Group. In addition to this, a number of options did not meet the vesting conditions during the period. Using the Black-Scholes Model, the fair value of each option is as set out below and based on the following criteria/assumptions. The options below were issued at various dates between January and December 2022.

Options Issued 31 December 2022	Class X Options	Class Y Options	Class Z Options	Class AA Options	Class AB Options	Performance ¹ Options	Other Options ²	Total option expense for the year ³
No of new options	14,650,000	850,000	100,000	600,000	500,000	25,000,000		
Expiry (years)	2.01	5.00	0.25	2.98	3.01	4.87		
Exercise price (\$)	0.25	0.25	0.20	0.30	0.20	-		
Average vesting period (years)	0.00	0.00	0.00	0.00	0.00	4.87		
Underlying volatility	54.4%	54.4%	54.4%	54.4%	54.4%	n/a		
Average risk-free interest rate	0.72%	1.54%	3.29%	3.26%	3.01%	n/a		
Average calculated fair value of each option (\$)	0.0349	0.0719	0.0107	0.1059	0.1900	0.2188		
Total expense recorded for the period ended 31 December 2022 (\$)	511,224	61,157	1,067	63,561	95,000	675,265	(691,393)	715,881

¹ Zero Price Performance Options ("Performance Options") are subject to the following vesting conditions being satisfied: DroneShield achieving \$50,000,000 of revenue or customer cash receipts; or automatic vesting in the event that DroneShield is subject to a takeover or other change of control transaction. As there is no exercise price and no near-term expectations of dividends for DroneShield, the value of the option (excluding the impact of vesting conditions) determined using Black-Scholes is equivalent to the price of a DroneShield share. The value of the Options is based on the spot price of a DroneShield share on the date at which the options were issued. Based on the sales pipeline and existing orders, management estimate that the options will vest within the expiry period. At this stage, the vesting period is assumed to be five years, which will be reviewed against updated pipeline and forecasts each six months.

² \$691,393 comprises of a credit for Tranche 2 Performance Options (issued in 2019) and a vesting expense for Class Q options (issued in 2019 and 2020). The expense recognised in prior periods for Tranche 2 Performance Options was credited due to the vesting conditions not being met within 3 years from the date of issue of the Tranche 2 Performance Options. Refer to 2021 Annual Report for details of options issued in prior periods.

³ During the year, limited-recourse loans were issued to certain employees and directors, where the company provided interest free loans for conversion of options previously issued by the company. In total, 14,315,833 options were converted into ordinary shares, at various exercise prices. The loans are due for repayment within 5 years from the date of inception. The loans are non-recourse except against the shares issued on exercise of the options and are held by the participant to which the loan relates. Non-recourse loans issued are treated as a modification of the option under the Accounting Standards. No additional expense has been recognised in relation to these modifications.

Notes to the Financial Statements *continued*

9. Options issued (*continued*)

During the year ended 31 December 2021, a number of options were issued to Directors, management and other employees of the Group as well as to brokers participating in the share placement that occurred in August 2020. In addition to this, a number of options did not meet the vesting conditions during the period. Using the Black-Scholes Model, the fair value of each option is as set out below and based on the following criteria/assumptions. The options below were issued at various dates between January and December 2021.

Options Issued 31 December 2021	Class T Options	Class U Options	Class V ¹ Options	Class W Options	Performance ² Options	Other Options ³	Total option expense for the year ⁴
No of new options	3,570,000	500,000	5,000,000	450,000	21,459,384		
Expiry (years)	0.35	3.01	3.00	3.00	3.37		
Exercise price (\$)	0.20	0.25	0.25	0.20	0		
Average vesting period (years)	0.00	0.00	0.00	0.00	0.33		
Underlying volatility	70.0%	70.0%	70.0%	70.0%	n/a		
Average risk-free interest rate	0.05%	0.14%	0.10%	0.14%	n/a		
Average calculated fair value of each option (\$)	0.0204	0.0664	0.0600	0.0651	0.1780		
Total expense recorded for the period ended 31 December 2021 (\$)	65,125	33,179	-	29,213	3,354,000	(2,313,476)	1,168,041

¹ Class V options were issued to brokers as part of the August 2020 capital raise and included as part of share transaction costs which is treated as a deduction from equity of \$300,137.

² 19,000,000 of the Zero Price Performance Options (Performance Options) was issued to Directors. The vesting conditions were satisfied and the options were exercised into shares on 16 August 2021. 2,459,384 of the Performance Options was issued to management and employees. These options automatically lapsed, during the year, as the vesting conditions attached to Tranche 1 Performance Options, issued in 2018, were satisfied.

³ \$2,313,476 comprises of a credit for Tranche 1 Performance Options (issued in 2018) and a vesting expense for Tranche 2 Performance Options and Class Q options (issued in 2019 and 2020). The expense recognised in prior periods for Tranche 1 Performance Options was credited due to the vesting conditions not being met within 36 months from the date of issue of the Tranche 1 Performance Options. Refer to 2020 Annual Report for details of options issued in prior periods.

⁴ During the year, limited-recourse loans were issued to certain employees and directors, where the company provided interest free loans for conversion of options previously issued by the company. In total, 6,886,666 options were converted into ordinary shares, at various exercise prices. The loans are due for repayment within 5 years from the date of inception. The loans are non-recourse except against the shares issued on exercise of the options and are held by the participant to which the loan relates. Non-recourse loans issued are treated as a modification of the option under the Accounting Standards. No additional expense has been recognised in relation to these modifications.

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
10. Income taxes relating to continuing operations		
The components of tax recognised in profit or loss include:		
Current tax	-	-
Deferred tax	-	-
Research and Development Tax Incentive	(1,979,531)	(1,087,833)
Total tax benefit	(1,979,531)	(1,087,833)
The income tax for the year can be reconciled to the accounting profit as follows:		
Income tax benefit calculated at 25% (2021: 27.5%)	(732,208)	(1,759,527)
Tax effect of amounts which are not deductible	178,970	321,211
Research and Development Tax Incentive	(1,979,531)	(1,087,833)
Effect of unused tax losses not recognised as deferred tax assets	553,238	1,438,316
Income tax benefit recognised in profit or loss (relating to continuing operations)	(1,979,531)	(1,087,833)
The tax rate used for the 2022 reconciliations above is the corporate tax rate of 25% (2021:27.5%) payable by DroneShield Limited on taxable profits under Australian tax law.		
The Company has unused tax losses of \$11,344,498 (2021: \$12,255,676). The benefit of these losses will only be recognised where it is probable that future taxable profit will be available against which the benefit of the deferred tax asset can be utilised. The deferred tax asset not recognised in relation to these tax losses is \$2,836,124 (2021: \$3,370,311).		
11. Cash and cash equivalents		
Cash at bank and in hand	9,290,829	5,660,677
Short-term deposits	853,032	3,758,558
Total cash and cash equivalents	10,143,861	9,419,235
12. Trade and other receivables		
Trade receivables	6,625,276	259,031
GST receivable	222,429	130,054
Deferred revenue (see Note 18)	31,478	131,278
Prepayments	1,437,465	338,768
Total trade and other receivables	8,316,648	859,131

Age of receivables that are past due but not impaired.

>120 days	9,559	-
-----------	-------	---

Payment for hardware sales and subscription services are due from the customer as per the terms specified in the contract.

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
13. Inventories		
Raw materials	2,403,734	5,980,558
Finished goods	<u>1,329,682</u>	<u>935,381</u>
Total Inventory	<u>3,733,416</u>	<u>6,915,939</u>
14. Other investments		
Current	75,000	75,000
- Term Deposits		
Non-current		
- Term Deposits	<u>42,900</u>	<u>42,900</u>
Total Other investments	<u>117,900</u>	<u>117,900</u>

For personal use only

Notes to the Financial Statements *continued*

15. Plant, equipment and intangible assets

	Development equipment \$	Demonstration equipment \$	Office equipment \$	Plant & equipment \$	Vehicles and trailers \$	Intangible assets (software) \$	Total \$
Balance at 1 Jan 21	129,714	175,247	115,303	274,656	138,989	40,206	874,115
Additions	142,005	62,084	122,471	114,051	49,706	14,785	505,102
Disposals	-	25,774	8,164	-	-	(2,159)	31,779
Transfer from (to) inventory	(174,356)	229,898	-	-	-	-	55,542
Depreciation/amortisation	-	(174,087)	(96,089)	(96,908)	(21,805)	(14,610)	(403,499)
Exchange differences	-	(27,039)	(13,675)	-	6,146	-	(34,568)
Balance at 31 Dec 21	97,363	291,877	136,174	291,799	173,036	38,222	1,028,471
Additions	634,581	-	95,483	7,384	-	4,247	741,695
Disposals	-	(116,030)	(11,542)	-	(44,463)	-	(172,035)
Transfer from (to) inventory	(187,962)	1,387,807	-	-	-	-	1,199,845
Depreciation/amortisation	-	(128,495)	(106,559)	(101,597)	(22,367)	(13,674)	(372,692)
Exchange differences	-	4,273	860	-	5,854	-	10,987
Balance at 31 Dec 22	543,982	1,439,432	114,416	197,586	112,060	28,795	2,436,271

	Cost \$	Accumulated Depreciation \$	Carrying Value \$
Development equipment	543,982	-	543,982
Demonstration equipment	2,030,428	(590,996)	1,439,432
Office equipment	395,063	(280,647)	114,416
Plant & equipment	514,526	(316,940)	197,586
Vehicles and trailers	155,654	(43,594)	112,060
Intangible assets (software)	79,902	(51,107)	28,795
Balance at 31 December 2022	3,719,555	(1,283,284)	2,436,271
Development equipment	97,363	-	97,363
Demonstration equipment	917,027	(625,150)	291,877
Office equipment	319,859	(183,685)	136,174
Plant & equipment	520,183	(228,384)	291,799
Vehicles and trailers	198,434	(25,398)	173,036
Intangible assets (software)	75,655	(37,433)	38,222
Balance at 31 December 2021	2,128,521	(1,100,050)	1,028,471

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
16. Right-of-use asset		
Balance at 1 January	-	236,973
Additions	949,790	-
Depreciation	(557,465)	(105,322)
Impairment	66,631	(131,651)
Balance at 31 December	458,956	-
<p>The Group leases various assets including offices and storage units. The contractual lease terms range from 1 to 4 years.</p> <p>The total cash outflow for leases, including short-term leases was \$641,231. (2021: \$625,298).</p> <p>The maturity analysis of lease liabilities is presented in Note 19.</p>		
Amounts recognised in profit and loss		
Depreciation expense on right-of-use assets	557,465	105,322
Expense relating to short-term leases	22,967	440,499
Impairment expense on right-of-use assets	-	131,651
Interest expense on lease liabilities	56,707	10,441
Reversal of impairment on right-of-use assets	(66,631)	-
17. Provisions		
Current		
- Annual leave	427,235	408,631
Non-current		
- Long-service leave	64,760	54,995
Total provisions	491,995	463,626
18. Other liabilities		
Accrued expenses	478,285	310,511
Deferred Revenue		
- Hardware sales	1,606,250	571,293
- Subscription services	1,664,521	398,333
- Services	-	282,579
- Shipping	-	4,178
- Other revenue	780,970	-
Sublease bonds	25,300	-
Total other liabilities	4,555,326	1,566,894

Notes to the Financial Statements *continued*

	31 December 2022 \$	31 December 2021 \$
19. Lease liabilities		
Amounts due for settlement within 12 months	526,045	152,985
Amounts due for settlement after 12 months	-	38,802
Total lease liabilities	526,045	191,787

These liabilities were measured at the present value of the remaining lease payments, discounted using the weighted average incremental borrowing rate of 6.07% - 9.00%.

20. Borrowings**Unsecured borrowing at amortised cost**

Insurance Premium Finance	70,052	56,584
Total borrowings	70,052	56,584
Amount due for settlement within 12 months	70,052	56,584
Amount due for settlement after 12 months	-	-

21. Contributed equity

	No. of shares (Note a)	\$
Balance at beginning of period (1 January 2022)	418,226,152	36,983,156
Shares issued following options exercised during period (Note b)	14,315,833	-
Share placement (Note c)	18,500,000	3,700,000
Transaction costs in relation to shares issued from share placement	-	(148,000)
Balance at end of period (31 December 2022)	451,041,985	40,535,156

Note a: The number of shares disclosed is the number of shares in DroneShield Limited.

Note b: During the year, 14,315,833 options were exercised using limited-recourse loans, where the company provided interest free loans for conversion of options previously issued by the company into shares. The loans are due for repayment within 5 years from the date of inception. The loans are nonrecourse except against the shares issued on exercise of the options and are held by the participant to which the loan relates.

Note c: In November 2022, the Company issued 18,500,000 shares in a share placement. The issue price was \$0.20 per share and the total cash received from the placement of shares was \$3,700,000.

Notes to the Financial Statements *continued*

22. Shares and options

	Number of Shares	Number of Unlisted Options
Opening balances at 1 January 2022	418,226,152	24,115,834
Share placement	18,500,000	-
Options exercised	14,315,833	(14,315,833)
Options lapsed	-	(15,745,000)
Options issued to Directors, Management and Employees	-	41,700,000
Closing balance at 31 December 2022	451,041,985	35,755,001

Unlisted Options

41,700,000 Unlisted Options were issued to Directors, Management and employees during the year to 31 December 2022. These Options are subject to various vesting conditions relating to length of employment with the Company and performance of the Company. See Note 9 for further details.

	31 December 2022 \$	31 December 2021 \$

23. Earnings (loss) per share

(a) Basic earnings (loss) per share

Total basic earnings (loss) per share attributable to the ordinary equity holders of the company	(0.002)	(0.013)
--------------------------------------------------------------------------------------------------	---------	---------

(b) Dilutive earnings per share

Dilutive earnings (loss) per share attributable to the ordinary equity holders of the company	(0.002)	(0.013)
-----------------------------------------------------------------------------------------------	---------	---------

(c) Weighted average number of shares used as the denominator

Weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share	429,980,471	397,919,239
------------------------------------------------------------------------------------------------------------------------	-------------	-------------

Options

Unlisted Options on issue (refer to Note 22) are not included in the calculation of diluted earnings per share because they are considered to be antidilutive for the period ended 31 December 2022. These options and shares could potentially dilute basic earnings per share in future periods.

Notes to the Financial Statements *continued*

24. Key Management Personnel disclosures and related party transactions

	31 December 2022 \$	31 December 2021 \$
(a) KMP Compensation		
Cash incentive	-	195,455
Movement in employee provisions	(10,022)	63,727
Post-employment benefits	24,430	22,631
Salaries and fees	456,188	457,362
Share-based payments	321,882	665,569
Total KMP compensation	792,478	1,404,744

Detailed remuneration disclosures are provided in the Remuneration Report on pages 24-30.

(b) Other transactions with related parties

There were no related party transactions during the financial year.

25. Parent entity financial information

The individual financial statements for the accounting parent entity, DroneShield Limited, show the following aggregate amounts:

Statement of financial Position

Current assets	5,126,447	10,383,461
Non-current assets	2,624,992	897,987
Total assets	7,751,439	11,281,448
Current liabilities	2,370,837	1,179,366
Non-current liabilities	64,760	93,797
Total liabilities	2,435,597	1,273,163
Net assets	5,315,842	10,008,285
Share capital	39,212,609	35,660,609
Reserves	4,866,513	5,175,003
Accumulated losses	(38,763,280)	(30,827,327)
Total equity	5,315,842	10,008,285
Loss for the year	(8,960,323)	(13,456,268)
Other comprehensive loss	-	-
Total comprehensive loss	(8,960,323)	(13,456,268)

DroneShield LLC and DroneShield Corporation Pty Ltd are legal subsidiaries of DroneShield Limited and are 100% owned by DroneShield Limited.

Notes to the Financial Statements *continued*

26. Financial risk management

The Group's financial instruments consist mainly of deposits with banks, accounts receivable and payable and inter-entity loans.

The Directors' overall risk management strategy seeks to assist the Group in meeting its financial targets whilst minimising potential adverse effects on financial performance.

Credit risk

With respect to credit risk arising from other financial assets, which comprise cash and cash equivalents, trade and other receivables and other investments, the Company's exposure to credit risk arises in the form of default of the counter party, with a maximum exposure equal to the carrying amount of these instruments. Management has considered impairment, with none noted at 31 December 2022.

Since the Company trades only with recognised parties, there is no requirement for collateral security.

The maximum exposure to credit risk at the balance date is as follows:

	31 December 2022	31 December 2021
	\$	\$
Cash and cash equivalents	10,143,861	9,419,235
Other investments	117,900	117,900
Trade and other receivables	6,879,183	520,363

Liquidity risk

The Company's policy is to maintain a comfortable level of liquidity through the continual monitoring of actual and forecast cash flows and the maturity profile of term deposits, and the raising of additional capital as required.

Foreign exchange risk

The Company operates from Australia and the U.S., and accordingly transactions currently occur in a mix of AUD, GBP and USD. Cash and cash equivalents used to fund working capital are held in USD and AUD bank accounts.

Transactional currency exposures arise from sales or purchases in currencies other than the Company's functional currency. For example, the Company is exposed to transactional exposure in respect of non-functional currencies on foreign currency denominated sales contracts entered into by DroneShield Limited in Australia.

Additionally, the Company is exposed to foreign currency exchange risk when capital is raised in AUD and transferred to the U.S. entity. The Company closely monitors foreign currency movements at such times but does not use hedging instruments to manage such risk.

Foreign currency denominated financial assets and liabilities which expose the Company to currency risk are disclosed below. The amounts shown are translated into AUD at the closing rate.

	31 December 2022	31 December 2021
	\$	\$
Cash	4,839,648	2,410,035
Trade and other receivables	6,614,195	332,726
Total financial assets	11,453,843	2,742,761
Other liabilities	(186,060)	(24,939)
Provisions	-	(33,066)
Trade and other payables	(225,618)	(353,239)
Total Financial liabilities	(411,678)	(411,244)

Notes to the Financial Statements *continued*

26. Financial risk management (*continued*)

Foreign exchange risk

The following table, expressed in AUD, indicates DroneShield's sensitivity to movements in exchange rates on the profit or loss, based on the AUD strengthening/ weakening against the USD by 10%:

	31 December 2022 \$	31 December 2021 \$
+ 10%	(1,007,918)	(193,520)
- 10%	1,143,766	136,452

Exposure to foreign currency varies during the year depending on the volume of transactions. Nonetheless, the analysis above is considered to be representative of the Group's exposure to currency risk.

Financial instrument composition and maturity analysis

The table below reflects the undiscounted contractual settlement terms for financial liabilities.

Contractual maturities of financial liabilities	Less than 6 months \$	6-12 Months \$	Between 1 and 2 years \$	Between 2 and 5 years \$	Total contractual cash flows \$	Carrying amount (assets)/ liabilities \$
As at 31 December 2021						
Accrued expenses	310,511	-	-	-	310,511	310,511
Borrowings	47,973	8,611	-	-	56,584	56,584
Lease liabilities	74,192	78,793	38,802	-	191,787	191,787
Trade and other payables	478,382	-	-	-	478,382	478,382
Total	911,058	87,404	38,802	-	1,037,264	1,037,264
As at 31 December 2022						
Accrued expenses	478,285	-	-	-	478,285	478,285
Borrowings	60,727	9,325	-	-	70,052	70,052
Lease liabilities	300,903	225,142	-	-	526,045	526,045
Trade and other payables	564,231	-	-	-	564,231	564,231
Total	1,404,146	234,467	-	-	1,638,613	1,638,613

27. Contingent liabilities

As at 31 December 2022 there were no contingent liabilities.

28. Commitments

At 31 December 2022, contractual agreements existed to pay suppliers \$2,354,271 for the manufacturing of inventory to deliver on orders received (2021: \$1,210,769).

Notes to the Financial Statements *continued*

29. Remuneration of auditor

During the year, the following fees were paid or payable for services provided by the auditor, HLB Mann Judd Assurance (NSW) Pty Limited and its related practices:

	31 December 2022 \$	31 December 2021 \$
Audit and assurance services	76,353	112,348
Taxation and other services	14,036	39,489
Total Auditor's remuneration	90,389	151,837

30. Segment information

The Group operates in one operating segment, being the development and commercialisation of hardware and software technology for drone detection and security.

This operating segment is monitored by the Group's chief operating decision maker and strategic decisions are made on the basis of adjusted segment operating results. The chief operating decision maker of the Group is the CEO.

The following tables present certain information regarding geographical segments for the years ended 31 December 2022 and 31 December 2021.

Segment performance 31 December 2022	USA \$	Australia \$	Elimination \$	Total \$
Hardware sales including shipping income				
- <i>direct sales</i>	7,180,891	757,109	-	7,938,000
- <i>distributors</i>	1,732,536	5,270,905	-	7,003,441
Subscription services				
- <i>direct sales</i>	152,759	117,521	-	270,280
- <i>distributors</i>	8,783	52,169	-	60,952
Services revenue				
- <i>direct sales</i>	71,706	1,393,044	-	1,464,750
- <i>distributors</i>	-	65,107	-	65,107
Warranty revenue				
- <i>distributors</i>	-	4,193	-	4,193
Total revenue from sales	9,146,675	7,660,048	-	16,806,723
Other revenue	-	79,358	-	79,358
Total revenue	9,146,675	7,739,406	-	16,886,081
Depreciation	(268,046)	(647,655)	-	(915,701)
Loss after income tax expense	3,322,828	(4,272,129)	-	(949,301)
Assets and liabilities				
Segment assets	6,539,065	27,613,170	(8,945,183)	25,207,052
Segment liabilities	(6,873,124)	(8,279,708)	8,945,183	(6,207,649)

Notes to the Financial Statements *continued*

30. Segment information (continued)

Segment performance 31 December 2021	USA \$	UK \$	Australia \$	Elimination \$	Total \$
Hardware sales including shipping income					
- <i>direct sales</i>	2,858,605	-	995,828	-	3,854,433
- <i>distributors</i>	1,273,927	-	2,311,660	-	3,585,587
Subscription services					
- <i>direct sales</i>	7,078	-	81,092	-	88,170
- <i>distributors</i>	28,881	-	72,030	-	100,911
Services revenue					
- <i>direct sales</i>	84,454	-	2,682,777	-	2,767,231
- <i>distributors</i>	36,872	-	28,900	-	65,772
Warranty revenue					
- <i>distributors</i>	-	-	4,193	-	4,193
Total revenue from sales	4,289,817	-	6,176,480	-	10,466,297
Other revenue	-	-	131,827	-	131,827
Total revenue	4,289,817	-	6,308,307	-	10,598,124
Depreciation	(50,152)	(2,648)	(455,139)	-	(507,939)
Loss after income tax expense	2,083,416	299,475	(7,693,338)	-	(5,310,447)
Assets and liabilities					
Segment assets	563,594	-	21,809,715	(4,032,633)	18,340,676
Segment liabilities	(4,314,724)	(3,176)	(2,472,006)	4,032,633	(2,757,273)

Notes to the Financial Statements *continued*

31. Reconciliation from loss after income tax to net cash outflow from operating activities

	31 December 2022 \$	31 December 2021 \$
Operating loss for the year after tax	(949,301)	(5,310,447)
Annual and long service leave entitlement	18,486	277,876
Awards and incentives revenue - Paycheck Protection Program ("PPP")	-	(129,883)
Bad debts	-	8,218
Depreciation	915,701	507,939
Effects of foreign currency translation	(153,168)	13,105
Intercompany loan	6,886	-
Interest income on cash deposits	(19,098)	(35,827)
Inventory impairment expense	(1,315)	211,945
Loss on disposal of fixed asset	56,006	25,051
Right-of-use asset impairment reversal	(66,631)	131,651
Share option expense	715,881	1,168,041
Transfers from fixed assets	222,797	-
<i>Change in operating assets and liabilities</i>		
Decrease/(Increase) in trade and other receivables	(7,557,316)	2,166,203
Decrease/(Increase) in inventory	1,982,678	(4,897,660)
(Decrease)/increase in trade and other payables	85,849	(405,981)
(Decrease)/increase in borrowings	13,468	-
(Decrease)/increase in other liabilities	2,963,132	(39,969)
Net cash flows from (used in) operating activities	(1,765,945)	(6,309,738)

32. Events after the reporting date

Subsequent to 31 December 2022, the following occurred;

- In January 2023, the Company received a new purchase order for approximately \$11 million from a government agency customer.
- In February 2023, the Company issued 36,266,666 shares in a share placement. The issue price was \$0.30, and the total cash received from the placement of shares was \$10,880,000. Under the terms of the Placement, brokers participating in the Placement will receive a commission on the funds raised.
- As of close of 28 February 2023, the Company will be admitted into the MSCI Global Micro Cap Index.

Directors' Declaration

1. In the opinion of the Directors:
 - (a) the consolidated financial statements and notes set out on pages 32 to 58 are in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the Group's financial position as at 31 December 2022 and of its performance for the financial year ended on that date; and
 - (ii) complying with Australian Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements; 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.
2. The notes to the consolidated financial statements include a statement of compliance with International Financial Reporting Standards.
3. The Directors have been given the declarations by the Chief Executive Officer and the Chief Financial Officer for the year ended 31 December 2022 required by section 295A of the *Corporations Act 2001*.

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



Peter James
Independent Non-Executive Chairman

Sydney, NSW
27 February 2022

For personal use only



Independent Auditor's Report to the Members of DroneShield Limited

REPORT ON THE AUDIT OF THE FINANCIAL REPORT

Opinion

We have audited the financial report of DroneShield Limited ("the Company") and its controlled entities ("the Group"), which comprises the consolidated statement of financial position as at 31 December 2022, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Group's financial position as at 31 December 2022 and of its financial performance for the year then ended; and
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* ("the Code") that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report of the current period. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matters below to be the key audit matters to be communicated in our report.

hlb.com.au

HLB Mann Judd Assurance (NSW) Pty Ltd ABN 96 153 077 215

Level 5, 10 Shelley Street Sydney NSW 2000 Australia

T: +61 (0)2 9020 4000 E: mailbox@hlbnsw.com.au

Liability limited by a scheme approved under Professional Standards Legislation.

HLB Mann Judd is a member of HLB International, the global advisory and accounting network.

For personal use only

Key Audit Matter	How our audit addressed the key audit matter
Revenue recognition (Note 3)	
<p>The Group recognised total revenue from sales of \$16,806,723 during the year ended 31 December 2022 (2021: \$10,466,297).</p> <p>We focussed on this area as a key audit matter due to the judgements involved in applying AASB 15 <i>Revenue from Contracts with Customers</i>.</p>	<p>Our audit procedures included but were not limited to the following:</p> <p>We reviewed management's revenue recognition accounting policy to assess whether it complied with AASB 15.</p> <p>We reviewed a sample of revenue transactions recorded during the year along with management's assessments and reviewed contracts and other documentation in relation to these to assess whether revenue recognised was in accordance with the requirements of AASB 15.</p> <p>We also reviewed disclosures in the financial statements to assess whether they are in accordance with AASB 15.</p>
Existence and Valuation of inventory (Note 13)	
<p>At 31 December 2022, the Group held inventory with a carrying value of \$3,733,416 (2021: \$6,915,939).</p> <p>As detailed in note 1 of the financial statements, inventories are valued at the lower of cost and net realisable value. Significant judgement is involved in estimating the net realisable value of inventory as it requires estimating the future sales volumes and prices for specific inventory lines.</p> <p>We focussed on this area as a key audit matter due to the material value of this balance.</p>	<p>Our audit procedures included but were not limited to the following:</p> <p>We attended the year-end stocktake and observed the count procedures and controls.</p> <p>We agreed the physical inventory count records to the accounting inventory listing at year-end.</p> <p>We tested a sample of inventory items to assess whether the carrying value was recorded at lower of cost or net realisable value in accordance with AASB 102 <i>Inventories</i>.</p> <p>We reviewed and tested management's assessment of inventory obsolescence.</p> <p>We reviewed the accounting policies adopted by the Group for inventory, and the disclosures in the financial report to ensure they meet the requirements of accounting standards.</p>
Share Based Payments (Note 9)	
<p>In the current and previous periods, the Company has issued a number of share options to directors and management.</p> <p>As detailed in note 1 of the financial statements, and in accordance with AASB 2: <i>Share Based Payment</i>, the fair value of the options at grant date are determined by management, and utilised to account for the share based payment expense and options issued.</p> <p>The key assumptions used in determining the fair value of the options are set out in Note 9 to the financial statements.</p> <p>We considered this to be a key audit matter due to the complexity and significant management estimation and judgement involved in determining the fair value of the share based payments issued.</p>	<p>Our audit procedures included but were not limited to the following:</p> <p>We reviewed and verified the key terms of the options issued as shared based payments during the year, to the supporting agreements and documentation.</p> <p>We reviewed the fair valuation calculation for the options, with reference to the methodology utilised and the key assumptions adopted in the valuation.</p> <p>We tested the accuracy of the recorded share-based payment expense for the period in the statement of profit or loss and option reserve.</p> <p>We assessed the accuracy of the Group's disclosures of the share based payment arrangement and options on issue in the financial statements with reference to the requirements of accounting standards.</p>

For personal use only



Information Other than the Financial Report and Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the information included in the Group's annual report for the year ended 31 December 2022, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

For personal use only

- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the directors, we determine those matters that were of most significance in the audit of the financial report of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

REPORT ON THE REMUNERATION REPORT

Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 24 to 30 of the directors' report for the year ended 31 December 2022.

In our opinion, the Remuneration Report of DroneShield Limited for the year ended 31 December 2022 complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

HLB Mann Judd

HLB Mann Judd Assurance (NSW) Pty Ltd
Chartered Accountants

Sydney, NSW
27 February 2023



N J Guest
Director

For personal use only

Shareholder Information

Holdings distribution at 24 February 2023

Holding Ranges	Holders	Total Shares	% Issued Share Capital
1 - 1,000	182	37,012	0.01%
1,001 - 5,000	3,158	9,974,207	2.05%
5,001 - 10,000	1,923	15,137,253	3.11%
10,001 - 100,000	3,724	126,225,676	25.90%
100,000 - over	544	335,934,503	68.94%
Total	9,531	487,308,651	100.00%

The shareholders are entitled to one vote for each share held.

Twenty largest shareholders at 24 February 2023

Position	Holder Name	Shares Held	% Issued Share Capital
1	BNP PARIBAS NOMINEES PTY LTD <IB AU NOMS RETAILCLIENT DRP>	44,159,329	9.06%
2	BETA GAMMA PTY LTD	21,500,000	4.41%
3	CITICORP NOMINEES PTY LIMITED	20,289,110	4.16%
4	EPIRUS INC	18,500,000	3.80%
5	Carla Balanco	8,450,000	1.73%
6	Oleg Vornik	8,077,022	1.66%
7	Angus Bean	7,385,621	1.52%
8	BNP PARIBAS NOMINEES PTY LTD ACF CLEARSTREAM	7,071,082	1.45%
9	Peter James	6,301,688	1.29%
10	MR PAUL JONATHAN SHAW & MRS BEATRICE SHAW	5,582,157	1.15%
11	S R BENNETT PTY LTD <D&S BENNETT PTY LTD SF A/C>	5,352,783	1.10%
12	HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	4,831,330	0.99%
13	P & B SHAW FT CB PTY LTD	3,434,775	0.70%
14	MR SHENCHEN GU	3,162,289	0.65%
15	BLACKWOOD CONSULTING PTY LTD <ROGER CAMPBELL FAMILY A/C>	3,095,351	0.64%
16	WARBONT NOMINEES PTY LTD <UNPAID ENTREPOT A/C>	2,825,278	0.58%
17	AZOTH LLC	2,483,333	0.51%
18	MR BARRY MARTIN LAMBERT	2,333,333	0.48%
19	BNP PARIBAS NOMS PTY LTD <DRP>	2,150,277	0.44%
20	SUPERHERO SECURITIES LIMITED <CLIENT A/C>	2,133,067	0.44%
Total		179,117,825	36.76%
	Balance of register	308,190,826	63.24%
	Total issued capital	487,308,651	100.00%

The number of unquoted equity securities on issue as at 31 December 2022 was 35,755,001 held by 41 holders.

509 holders held less than a marketable parcel of DRO securities, based on the closing market price as at 31 December 2022 of \$0.22.