



## **NOTICE OF GENERAL MEETING**

Notice is given that a general meeting of Lodestone Exploration Limited ABN 20 075 877 075 (**Company**) will be held at the offices of Stanley Yeates & Associates, Level 1, 101 Edward Street, Brisbane on Friday 26 June 2009 and will commence at 10.00 am Brisbane time (**Meeting**).

The Meeting is being convened to:

- approve the Company's entry into the Tambo Gas Farmin Agreement and Coal Farmin Agreement;
- approve a change in the name of the Company to Lodestone Energy Limited;
- approve the issue of options to Mr Grahame Baker, a recent addition to the Board;
- ratify a past issue of shares and options to key investors in the Company and approve a further issue of shares and options to them; and
- approve the adoption of a Performance Rights Plan and the issue of Performance Rights to Directors under the plan.

The Explanatory Memorandum accompanying this Notice provides additional information on the matters to be considered at the Meeting to enable the shareholders to make an informed decision regarding the Resolutions. The Explanatory Memorandum is intended to be read in conjunction with, and forms part of, this Notice.

Words that are defined in the Explanatory Memorandum have the same meaning when used in this Notice, unless the context requires otherwise.

### **Items of business**

#### **1. Resolution 1 – Approval of Gas Farmin Agreement**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act and Listing Rule 10.1 , and for all other purposes, the performance by the Company of its obligations under the Gas Farmin Agreement, the terms and conditions of which are summarised in the Explanatory Memorandum, be approved.*

#### **Voting exclusion statement**

The Company will disregard any votes cast on Resolution 1 by:

- Tambo; and
- any of its associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Tambo or any of its associates.

**2. Resolution 2 – Approval of Coal Farmin Agreement**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act and Listing Rule 10.1 , and for all other purposes, the performance by the Company of its obligations under the Coal Farmin Agreement, the terms and conditions of which are summarised in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 2 by:

- Tambo; and
- any of its associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Tambo or any of its associates.

**3. Resolution 3 – Approval of change of name**

To consider and, if thought fit, pass the following resolution as a special resolution:

*That the name of the Company be changed from Lodestone Exploration Limited to Lodestone Energy Limited and that the constitution of the Company be amended by deleting Lodestone Exploration Limited wherever it appears and inserting Lodestone Energy Limited in its place.*

**4. Resolution 4 – Approval of issue of options to Grahame Baker**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.11 and for all other purposes, the grant of 2,000,000 options to Mr Grahame Baker, a Director, or his nominee, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 4 by:

- Mr Baker; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Baker or any of his associates.

**5. Resolution 5 – Ratification of issue of Placement Shares and Placement Options**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That for the purposes of Listing Rule 7.4 and for all other purposes, the issue of 9,000,000 Placement Shares and 9,000,000 Placement Options to the parties, for the purposes and on the terms described in the Explanatory Memorandum, be ratified.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 5 by:

- any person who participated in the issue, being Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd; and
- any of their associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy for a person who is entitled to vote in accordance with the directions on the Proxy Form; or
- it is cast by the person chairing the Meeting as a proxy for a person who is entitled to vote in accordance with a direction on the Proxy Form to vote as their proxy decides.

**6. Resolution 6 – Approval of proposed further issue of Placement Shares and Placement Options**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That for the purposes of Listing Rule 7.1, Listing Rule 7.2 Exception 13 and for all other purposes, the proposed issue of up to 11,000,000 Placement Shares and 11,000,000 Placement Options to the parties, for the purposes and on the terms described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 6 by:

- any person who is to participate in the issue, being Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd, and any person who might obtain a benefit if Resolution 6 is passed (except a benefit solely in the capacity of a security holder); and
- any of their associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy for a person who is entitled to vote in accordance with the directions on the Proxy Form; or
- it is cast by the person chairing the Meeting as a proxy for a person who is entitled to vote in accordance with a direction on the Proxy Form to vote as their proxy decides.

**7. Resolution 7 – Approval of Performance Rights Plan**

To consider and, if thought fit, pass the following resolution as an ordinary resolution:

*That for the purposes of section 195(4) and section 200E of the Corporations Act and Exception 9(b) of Listing Rule 7.2, the Performance Rights Plan, the terms and conditions of which are summarised in the Explanatory Memorandum, and the issue of securities pursuant to the Performance Rights Plan, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 7 by:

- a Director, being Mr Martin Ackland, Mr Greg Baynton, Mr John McCawley, Mr Bill Stubbs, Mr Lance Grimstone and Mr Grahame Baker; and
- any associate of a Director.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy for a person who is entitled to vote in accordance with the directions on the Proxy Form; or
- it is cast by the person chairing the Meeting as a proxy for a person who is entitled to vote in accordance with a direction on the Proxy Form to vote as their proxy decides.

**8. Resolution 8 – Approval of issue of Performance Rights to Mr Martin Ackland**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 2,000,000 Performance Rights to Mr Martin Ackland, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 8 by:

- Mr Ackland; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Ackland or any of his associates.

**9. Resolution 9 – Approval of issue of Performance Rights to Mr Greg Baynton**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 2,000,000 Performance Rights to Mr Greg Baynton, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 9 by:

- Mr Baynton; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Baynton or any of his associates.

**10. Resolution 10 – Approval of issue of Performance Rights to Mr John McCawley**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 2,000,000 Performance Rights to Mr John McCawley, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 10 by:

- Mr McCawley; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr McCawley or any of his associates.

**11. Resolution 11 – Approval of issue of Performance Rights to Mr Bill Stubbs**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 2,000,000 Performance Rights to Mr Bill Stubbs, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 11 by:

- Mr Stubbs; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Stubbs or any of his associates.

**12. Resolution 12 – Approval of issue of Performance Rights to Mr Lance Grimstone**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 4,000,000 Performance Rights to Mr Lance Grimstone, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 12 by:

- Mr Grimstone; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Grimstone or any of his associates.

**13. Resolution 13 – Approval of issue of Performance Rights to Mr Grahame Baker**

Subject to Resolution 7 being approved, to consider and, if thought fit, pass the following resolution as an ordinary resolution:

*For the purposes of Chapter 2E of the Corporations Act, Listing Rule 10.14 and for all other purposes, the grant of 2,000,000 Performance Rights to Mr Grahame Baker, a Director, for no consideration and otherwise on the terms and conditions described in the Explanatory Memorandum, be approved.*

***Voting exclusion statement***

The Company will disregard any votes cast on Resolution 13 by:

- Mr Baker; and
- any of his associates.

However, the Company need not disregard a vote if:

- it is cast by a person as a proxy appointed by writing that specifies how the proxy is to vote on the proposed resolution; and
- it is not cast on behalf of Mr Baker or any of his associates.

**BY ORDER OF THE BOARD**

Leni Stanley  
Company Secretary  
15 May 2009

## NOTES TO THE NOTICE OF EXTRAORDINARY GENERAL MEETING

### Eligibility to vote

A person's entitlement to vote at the Meeting will be determined by reference to the number of Shares registered in the name of that person (reflected in the register of members) as at 7:00pm (Sydney time) on Wednesday, 24 June 2009.

### Proxy votes and corporate representatives

A member who is entitled to attend and cast a vote at the Meeting is entitled to appoint a proxy. A form of appointment of proxy is enclosed with this Notice.

The proxy need not be a member of the Company. A member who is entitled to cast two or more votes may appoint two proxies and may specify the proportion or number of votes each proxy is appointed to exercise. If no such specification is given and two proxies are appointed, each may exercise half of the votes to which that member is entitled.

All Proxy Forms will need to be lodged with the Company no later than 10.00 am (Brisbane time) on Wednesday 24 June 2009, being 48 hours before commencement of the Meeting. Any Proxy Form received after that time will not be valid for the Meeting.

If you wish to appoint a proxy and are entitled to do so, then complete the enclosed Proxy Form in accordance with the instructions on it and return it to the Company's share registry by the deadline for lodgement as follows:

- by using the enclosed **reply paid envelope**;
- by **post or fax** to the Company's share registry as follows:

Lodestone Exploration Limited  
C/- Link Market Services Limited  
Locked Bag A14  
Sydney South NSW 1235  
Facsimile: (02) 9287 0309; or

- by **delivery** to Link Market Services Limited at Level 12, 680 George Street, Sydney NSW 2000.

A corporation may elect to appoint a representative in accordance with the Corporations Act in which case the Company will require written proof of the representative's appointment, which must be lodged with or presented to the Company no later than 48 hours before commencement of the Meeting.

If you have any queries on how to cast your votes then please call the Company Secretary, Leni Stanley, on (07) 3221 6022 during business hours.



## Lodestone Exploration Limited

ABN 20 075 877 075

[www.lodestonex.com](http://www.lodestonex.com)

### EXPLANATORY MEMORANDUM

This Explanatory Memorandum has been prepared for the information of shareholders in relation to the business to be conducted at the general meeting of the Company to be held at the offices of Stanley Yeates & Associates, Level 1, 101 Edward Street, Brisbane on Friday 26 June 2009 at 10.00 am Brisbane time. This Explanatory Memorandum should be read in conjunction with the Notice.

The Meeting is being convened to:

- approve the Company's entry into the Tambo Gas Farmin Agreement and Coal Farmin Agreement;
- approve a change in the name of the Company to Lodestone Energy Limited;
- approve the issue of options to Mr Grahame Baker, a recent addition to the Board;
- ratify a past issue of shares and options to key investors in the Company and approve a further issue of shares and options to them; and
- approve the adoption of a Performance Rights Plan and the issue of Performance Rights to Directors under the plan.

A number of words and terms used in this Explanatory Memorandum have defined meanings, which are set out in the Definitions section at the end of this document.

#### Resolution 1 and 2 – Approval of Gas and Coal Farmin Agreements

##### *Introduction*

Pursuant to Resolutions 1 and 2, shareholder approval is sought for the performance by the Company of its obligations under the Coal Farmin Agreement between the Company, Lodestone Coal and Tambo and the Gas Farmin Agreement between the Company, Lodestone CSG and Tambo (collectively the **Farmin Agreements**).

Resolutions 1 and 2 are not conditional on each other. This means that both Resolutions 1 and 2 may be approved, only one of Resolutions 1 and 2 may be approved or neither may be approved.

The terms of the Farmin Agreements differ in some respects and so a separate summary of each agreement is set out below. Following these summaries, this Explanatory Memorandum explains why shareholder approval of Resolutions 1 and 2 is required, and summarises the reasons why the Board recommends shareholders vote in favour of these Resolutions.

In accordance with the requirements of the Listing Rules, the Company engaged MBA Petroleum Consultants as an independent expert to report whether in its opinion each Farmin Agreement is fair and reasonable to the Company's eligible shareholders. **The Independent Expert has concluded that that the Farmin Agreements are fair and reasonable to the Eligible Shareholders.** The independent Expert's Report accompanies this Explanatory Memorandum.

## Summary of Gas Farmin Agreement

### *Overview*

On 10 December 2008 the Company, Lodestone CSG and Tambo entered into the Gas Farmin Agreement. Lodestone CSG is a wholly owned subsidiary of the Company. Tambo is a company controlled by Mr Greg Baynton, a Director.

Under the Gas Farmin Agreement, Lodestone CSG has a right to earn up to a 50% interest in Authority to Prospect (**ATP**) 1020, a tenement prospective for gas (the **Gas Tenement**) by undertaking exploration activities, and incurring exploration expenditure, to the value of \$5 million over a period of four years (**Earning Period**).

The Gas Tenement covers a largely unexplored region of the Surat-Eromanga Basin sequence in Southern Central Queensland.

### *Conditions precedent*

The Gas Farmin Agreement is subject to the following conditions:

- The Company's Eligible Shareholders approving the performance by the Company of its obligations under the Gas Farmin. The reason why this approval is required is described later in this Explanatory Memorandum.
- The Independent Expert's Report stating that the transaction the subject of the Gas Farmin Agreement is fair and reasonable to Eligible Shareholders.

### *Earning Obligation*

Under the Gas Farmin Agreement Lodestone CSG may earn up to a 50% interest in the Gas Tenement by undertaking exploration activities, and incurring exploration expenditure, to the value of \$5 million over the Earning Period (**Earning Obligation**). The Gas Tenement is currently held by Tambo. Tambo applied for the Gas Tenement, and will contribute the Gas Tenement to the Gas Farmin Agreement.

The Gas Farmin Agreement provides that for each \$1 million that Lodestone CSG spends satisfying its total Earning Obligation, it is entitled to be transferred a 10% interest in the Gas Tenement.

If Lodestone CSG satisfies all of its Earning Obligation within the Earning Period, Lodestone CSG and Tambo will enter into an unincorporated joint venture. Lodestone CSG and Tambo will each have a 50% interest in the joint venture and Lodestone CSG will be the initial operator. If Lodestone CSG satisfies at least one stage, but not all stages, of its Earning Obligation a joint venture between the parties will also be established but Tambo will be the initial operator. Upon the formation of the joint venture Tambo must contribute its share of the further exploration and permit obligations in respect of the Gas Tenement.

If Lodestone CSG fails to satisfy at least one stage of its Earning Obligation by the end of the Earning Period, it will not acquire any interest in the Gas Tenement and will be deemed to have withdrawn from the Gas Farmin Agreement.

### *Parties' obligations during Earning Period*

During the Earning Period, Lodestone CSG has the sole exclusive right to access and explore the Gas Tenement at Lodestone CSG's sole risk and cost, including the right to determine the nature and content of exploration programmes and budgets. In carrying out such exploration

activities, Lodestone must abide by the terms of the Gas Tenement and not do anything to breach, or cause any other party to breach, the terms and conditions of the Gas Tenement.

Lodestone CSG must satisfy the minimum expenditure obligations for the Gas Tenement required under applicable petroleum legislation until Lodestone CSG withdraws from the Gas Farmin Agreement, the Earning Period expires, or Lodestone CSG satisfies its Earning Obligation (whichever occurs first). The minimum expenditure obligations are currently anticipated to amount to approximately \$3.1million per annum. Lodestone CSG is otherwise under no obligation to undertake exploration or incur exploration expenditure during the Earning Period.

Provided Lodestone CSG has satisfied all obligations imposed by the applicable petroleum legislation in respect of the Gas Tenement (including expenditure conditions but excluding relinquishment obligations), Lodestone CSG may withdraw from the Gas Farmin Agreement by notice to Tambo at any time prior to undertaking and incurring the Earning Obligation in full. Upon such withdrawal Lodestone CSG is not obliged to undertake any further work or incur any further liability in respect of the Gas Tenement or to fund any further exploration in or about the Gas Tenement, but will be liable for rehabilitation of land arising from its exploration activities.

### ***Sole risk activities***

At any time after 12 months from the satisfaction of all of the conditions precedent, Tambo may indicate its intention to carry out exploration activities in a specified part of the Gas Tenement within which Lodestone CSG is not currently, and has no immediate plans, to undertake its own exploration activities (a **Sole Risk Proposal**). Within 30 days of receiving a Sole Risk Proposal, Lodestone CSG may elect to undertake the proposed exploration activities within six months, as part of its Earning Obligation, or elect to maintain its then percentage earned interest in the sole risk area by agreeing to pay its proportionate share of the exploration expenditure incurred by Tambo in undertaking the Sole Risk Proposal.

If Lodestone CSG does not elect to undertake the activities proposed in a Sole Risk Proposal or to maintain its earned interest in the sole risk area, Tambo may undertake those activities at its own cost. If it does so, it must, upon the completion of those activities, report on their outcome to Lodestone CSG. Lodestone CSG then has six months in which to elect whether to participate in the sole risk activities up to a maximum of 50% by paying Tambo its proportionate share of the expenditure made by Tambo in completing the sole risk activities, multiplied by four. If Lodestone CSG chooses not to make such a payment, then the relevant area the subject of the Sole Risk Proposal is excluded from the operation of the Gas Farmin Agreement and Tambo will retain a 100% beneficial interest in that area.

The parties have agreed that if any of them proposes to take up, or acquire, or is offered an interest in, any petroleum tenement in an area within 100 kilometres of the boundary of the Gas Tenement, that party must offer to include that interest in the joint venture between the parties.

### ***Guarantee***

The Company has agreed to guarantee the due performance of Lodestone CSG's obligations under the Gas Farmin Agreement. This guarantee will terminate if Lodestone CSG validly transfers its whole interest in the Gas Farmin Agreement to a third party who is not a related body corporate of the Company, in accordance with the requirements of the Gas Farmin Agreement.

### ***Transfer and termination rights***

Lodestone CSG is prohibited from transferring the whole or any part of its interest in the Gas Farmin Agreement except with the prior written consent of Tambo (which must not be unreasonably withheld), unless the transfer is to a related body corporate of the Company

and the Company agrees to guarantee the performance of that entity's obligations, or the transfer is otherwise permitted by the Gas Farmin Agreement.

Tambo is prohibited from transferring any interest in the Gas Tenement except as permitted by the Gas Farmin Agreement. If Tambo wishes to transfer its interest in the Gas Tenement to a third party, Lodestone CSG has a first right of refusal to acquire that interest on the same terms and conditions. If Lodestone CSG does not exercise its right of pre-emption, Tambo may only proceed with the transfer if Lodestone CSG is reasonably satisfied the transferee is of good standing, financial substance and reputation and the transferee has agreed to perform the obligations of Tambo under the Gas Farmin Agreement. Tambo may assign its interest in the Gas Tenement to a related body corporate without the consent of Lodestone CSG subject to certain conditions.

If there is a change in control of Tambo (as defined in the Gas Farmin Agreement), or Tambo becomes insolvent, then Lodestone CSG has the right to acquire the whole of Tambo's interest in the Gas Tenement at a price agreed between Lodestone CSG and Tambo, or failing agreement, at a price determined by an independent valuer appointed in accordance with the Gas Farmin Agreement.

If Tambo commits a material breach of its obligations under the Gas Farmin Agreement then Lodestone CSG may acquire all of Tambo's interest in the Gas Tenement at a price agreed between the parties or failing agreement, as determined by an independent valuer. If Lodestone CSG elects not to acquire Tambo's interests in the Gas Tenement, it may terminate the Gas Farmin Agreement with Tambo.

Tambo may terminate the Gas Farmin Agreement if an insolvency event occurs in relation to Lodestone CSG or Lodestone CSG commits a breach of a material obligation under the Gas Farmin Agreement that is not remedied within 30 business days of Tambo giving notice.

## **Summary of Coal Farmin Agreement**

### ***Overview***

On 10 December 2008 the Company, Lodestone Coal and Tambo entered into the Coal Farmin Agreement. Lodestone Coal is a wholly owned subsidiary of the Company.

Under the Coal Farmin Agreement, Lodestone Coal has a right to earn up to a 50% interest in tenements that are prospective for coal by undertaking exploration activities, and incurring exploration expenditure, to the value of \$5 million over a period of four years (**Earning Period**).

The Coal Tenements cover a largely unexplored region of the Surat-Eromanga Basin sequence, in Southern Central Queensland. There is some overlap between the Coal Tenements and the Gas Tenement that is the subject of the Gas Farmin Agreement although the two areas are not identical.

The Coal Tenements are currently under application by Tambo.

### ***Conditions precedent***

The Coal Farmin Agreement is subject to the following conditions:

- The Company's Eligible Shareholders approving the performance by the Company of its obligations under the Coal Farmin Agreement. The reason why this approval is required is described below.
- The Independent Expert's Report states that the transaction the subject of the Coal Farmin Agreement is fair and reasonable to Eligible Shareholders.

- At least one Coal Tenement that is satisfactory to Lodestone Coal being granted to Tambo by the QDME. The Coal Farming Agreement provides that upon Tambo receiving a notice from the QDME of its intention to grant a Coal Tenement, Tambo must immediately advise Lodestone Coal. Lodestone Coal may then determine whether it considers the tenement is acceptable based on its assessment of the tenement's prospects for commercial exploitation or production of coal, or whether it should be excluded from the agreement. To assist Tambo to secure the grant of each acceptable tenement, Lodestone Coal has agreed to pay any security and rent that is payable for each such tenement.

### ***Earning Obligation***

Under the Coal Farming Agreement Lodestone Coal may earn up to a 50% interest in the Coal Tenements (other than those that the Company excludes from operation of the agreement) by undertaking exploration activities, and incurring exploration expenditure, to the value of \$5 million over the Earning Period (**Earning Obligation**). The Coal Tenements are currently under application by Tambo. Tambo applied for the Coal Tenements, and will contribute the Coal Tenements to the Coal Farming Agreement.

The Coal Farming Agreement provides that for each \$1 million of expenditure that Lodestone Coal spends satisfying its Earning Obligation, it is entitled to be transferred a 10% interest in the Coal Tenements.

Lodestone Coal and Tambo have also applied jointly (in equal shares) for the Joint Coal Tenements. Of the Joint Coal Tenements, EPC1623 has been granted by QDME. The parties have agreed that the Earning Obligation may be applied across both the Coal Tenements and the Joint Coal Tenements. The parties applied for the Joint Coal Tenements after Tambo had applied for the Coal Tenements to which Lodestone Coal is farming in under the Coal Farming Agreement.

If Lodestone Coal satisfies the whole of its Earning Obligation within the Earning Period, Lodestone Coal and Tambo will enter into an unincorporated joint venture in which each has a 50% interest and Lodestone Coal will be the initial operator. If Lodestone Coal satisfies at least one stage, but not all stages, of its Earning Obligation a joint venture between the parties will also be established but Tambo will be the initial operator. Upon the formation of the joint venture Tambo must contribute its share of the further exploration and permit obligations in respect of the Coal Tenements.

If Lodestone Coal fails to satisfy at least one stage of its Earning Obligations by the end of the Earning Period, it will not acquire any interest in the Coal Tenements and is deemed to have withdrawn from the Coal Farming Agreement.

### ***Parties' obligations during Earning Period***

Pending grant of the Coal Tenements, Tambo must do everything reasonably possible to preserve the value of the Coal Tenements and must not, without the prior written consent of Lodestone Coal, withdraw the applications for the Coal Tenements or take any action to prejudice the applications. Lodestone Coal must use its reasonable endeavours to assist Tambo to secure the grant of the Coal Tenements.

During the Earning Period, Lodestone Coal has the sole exclusive right to access and explore the Coal Tenements at Lodestone Coal's sole risk and cost, including the right to determine the nature and content of exploration programmes and budgets. Lodestone Coal's other rights and obligations during the Earning Period are materially the same as those of Lodestone CSG under the Gas Farming Agreement.

### ***Sole risk activities, guarantee and transfer and termination***

The Coal Farmin Agreement contains sole risk, guarantee and transfer and termination provisions materially the same as those described in respect of the Gas Farmin Agreement.

If during the Earning Period Lodestone Coal considers one or several of the Coal Tenements are no longer prospective for commercial exploitation it may provide notice of this to Tambo and such tenements will be excluded from the Coal Farmin Agreement. This will not affect the amount of Lodestone Coal's Earning Obligation.

### **Why shareholder approval of Resolutions 1 and 2 is required**

#### ***Listing Rule 10.1***

Listing Rule 10.1 provides that the Company must ensure that neither it, nor any of its child entities, acquires a substantial asset from a related party unless the acquisition is approved by the Company's shareholders. A substantial asset is defined in Listing Rule 10.2 as an asset whose value, or the value of the consideration for it is, 5% or more of the equity interests of the Company.

Tambo is an entity controlled by Greg Baynton, a Director, and is a related party of the Company for the purposes of Listing Rule 10.1. Lodestone CSG and Lodestone Coal are wholly owned subsidiaries of the Company and are therefore child entities of the Company for the purposes of Listing Rule 10.1. The consideration payable by Lodestone CSG under the Gas Farmin Agreement to acquire a maximum 50% interest in the Gas Tenement is \$5,000,000. The consideration payable by Lodestone Coal to acquire a maximum 50% interest in the Coal Tenements is also \$5,000,000. In each case, the maximum consideration payable by Lodestone CSG or Lodestone Coal represents more than 5% of the equity interests of the Company.

Shareholder approval is therefore required under Listing Rule 10.1 because if either the Coal Farmin Agreement or Gas Farmin Agreement becomes binding on Lodestone CSG and Lodestone Coal respectively, a child entity of the Company will acquire a 'substantial asset' from a related party.

#### ***Chapter 2E of the Corporations Act***

Chapter 2E of the Corporations Act prohibits the Company, or an entity the Company controls, from giving a financial benefit to a related party of the Company, except with the approval of the Company's members. Acquiring an asset from a related party is an example of giving a financial benefit that requires shareholder approval under Chapter 2E.

An approval under Chapter 2E is required because, pursuant to the Farmin Agreements, the Company's wholly owned subsidiaries, Lodestone CSG and Lodestone Coal, will each acquire assets from Tambo, a related party of the Company.

### **Advantages and disadvantages of the Farmin Agreements**

#### ***Advantages and disadvantages of the Gas Farmin Agreement***

The Board considers that the Gas Farmin Agreement will provide the Company with an exciting opportunity to further expand its activities in the energy sector. The Board considers that advantages of the proposal include:

- Under the Gas Farmin Agreement, Lodestone CSG has the exclusive right to determine the nature and content of exploration programs and budgets and is under no obligation to undertake exploration or incur exploration expenditure, except to the extent necessary to satisfy minimum expenditure obligations for the tenement required under applicable petroleum legislation (as described in more detail above).

- Lodestone CSG has a right to withdraw from the Gas Farmin Agreement at any time prior to satisfying its Earning Obligation in full, but retains any Earned Interest that it has at the date of withdrawal.

A potential disadvantage of the Gas Farmin Agreement is that, as described above, Lodestone CSG is obliged under the agreement to satisfy the minimum expenditure obligations for the Gas Tenement. There can be no guarantee that gas reserves will be discovered in the Gas Tenement area or that, if found, these reserves will be able to be commercially exploited. It is therefore possible that even if the Lodestone CSG satisfies its Earning Obligation in full, it may not derive a commercial benefit from doing so. The Board will, however, actively seek to manage this risk.

### ***Advantages and disadvantages of the Coal Farmin Agreement***

The Board considers that the advantages and disadvantages of the Coal Farmin Agreement are materially the same as those for the Gas Farmin Agreement.

### ***Funding of Earning Obligations***

On 5 May 2009 the Company announced that it has entered into a heads of agreement with Mr Oliver Lennox-King to raise \$4.5 million by the placement of Shares for \$1.5 million and the sale of a 2% royalty interest for \$3 million. The Company also announced that it intends to place Shares to raise another \$500,000, bringing the total raising to \$5,000,000. This amount will fund the initial exploration activities of Lodestone CSG and Lodestone Coal under the Farmin Agreements.

When the results of the initial exploration activities are analysed and the Company determines to proceed with further exploration, the Company plans to undertake additional capital raisings to fund the balance of the exploration activities.

### **Independent Expert's Report**

Listing Rule 10.10 provides that a notice of meeting prepared for the purposes of obtaining an approval under Listing Rule 10.1 must include a report from an independent expert as to whether the relevant transaction in respect of which shareholder approval is being sought is fair and reasonable to the Company's eligible ordinary shareholders.

For the purposes of Listing Rule 10.10 the Company engaged MBA Petroleum Consultants to prepare the Independent Expert's Report, which is set out in schedule 1.

**The Independent Expert has concluded that the Farmin Agreements are fair and reasonable to the Eligible Shareholders.**

Shareholders are encouraged to read the Independent Expert's Report carefully.

### **Other information**

In accordance with the requirements of Chapter 2E of the Corporations Act, the following information is provided to shareholders for the purposes of Resolutions 1 and 2:

- The related party to whom a financial benefit will be given if either Resolution 1 or 2 is approved is Tambo. Tambo is a related party of the Company because it is controlled by Mr Greg Baynton, a Director.
- Under the Gas Farmin Agreement, Lodestone CSG has agreed to acquire up to a 50% interest in the Gas Tenement on the terms summarised above. The consideration payable to Lodestone CSG to acquire this interest, and any other amounts payable to or on behalf of Tambo under the Gas Farmin Agreement, constitute the giving of a financial benefit for the purposes of Chapter 2E of the Corporations Act.

- Under the Coal Farmin Agreement, Lodestone Coal has agreed to acquire up to a 50% interest in the Coal Tenements on the terms summarised above. The consideration payable by Lodestone Coal to acquire those interests, and any other amounts payable to or on behalf of Tambo under the Coal Farmin Agreement, constitute the giving of a financial benefit for the purposes of Chapter 2E of the Corporations Act.

### **Directors' interests and recommendations**

None of the Directors, other than Mr Greg Baynton, have an interest in the Farmin Agreements, except in their capacity as shareholders of the Company.

As noted above, Mr Baynton, a Director, controls Tambo, which is a party to the Farmin Agreements. As Mr Baynton has, by virtue of his interests in Tambo, an interest in Resolutions 1 and 2, he makes no recommendation in relation to them.

The Directors, other than Mr Baynton, have considered all the relevant information relating to Resolutions 1 and 2, including the accompanying Independent Expert's Report, which states that, in the opinion of the Independent Expert, the Farmin Agreements are fair and reasonable to the Eligible Shareholders. These Directors **unanimously recommend that you vote in favour of Resolutions 1 and 2** for the following reasons:

- the Directors consider that the area covered by the Gas Tenement and the Coal Tenements is prospective for Surat Basin coal and coal seam gas;
- the Company has also applied for further permits in order to secure a substantial area (including the Gas Tenement and the Coal Tenements), which it considers may be prospective; and
- the ability of the Company to farmin to the Gas Tenement and the Coal Tenements as opposed to a purchase of an interest in them is considered advantageous, as it allows for staged expenditure in line with exploration results.

### **Resolution 3 – Change of name to Lodestone Energy Limited**

#### ***Introduction***

Resolution 3 seeks Shareholder approval for the Company to change its name to Lodestone Energy Limited.

The Directors believe that this name change is appropriate to reflect the Company's ongoing deepening focus on the exploration for energy and resources, notably coal and coal seam gas.

#### ***Name change process***

Section 157 of the Corporations Act requires that the new name must be approved by a special resolution of the shareholders of the Company. A special resolution is a resolution that has been passed by at least 75% of the votes cast by shareholders entitled to vote on the resolution.

If the special resolution to change the Company's name to Lodestone Energy Limited is passed, an application will be lodged with the Australian Securities and Investments Commission (**ASIC**) to change the Company's name.

A certificate of change of name will be issued by ASIC. A copy of this certificate will then be provided to the ASX. The Company anticipates that once ASX has been provided with a copy of the certificate the change of the Company's name on ASX will take effect within a relatively short period of time.

The Company will not make any request to change its ASX trading code "LOD".

### ***Directors' recommendation***

The Directors **unanimously recommend that shareholders vote in favour of Resolution 3.**

### **Resolution 4 – Issue of options to Mr Grahame Baker**

#### ***Introduction***

Pursuant to Resolution 4 shareholder approval is sought for the grant of 2,000,000 options, for no consideration, to Mr Grahame Baker, a Director, or his nominee, on the terms set out below.

Mr Baker was appointed as a Director on 15 April 2009.

#### ***Why is shareholder approval required?***

##### ***Listing Rule 10.11***

Listing Rule 10.11 provides that the Company must not issue, or agree to issue, securities to a related party of Company without first obtaining shareholder approval. As the Company proposes to issue options to Mr Baker (a related party) shareholder approval is therefore required under Listing Rule 10.11 before the options can be issued.

#### ***Chapter 2E of the Corporations Act***

Chapter 2E of the Corporations Act prohibits the Company from giving a financial benefit to related party of the Company, except with the approval of the Company's members. Issuing securities (including options) to a related party is an example of giving a financial benefit that requires shareholder approval under Chapter 2E.

An approval under Chapter 2E is required because, if Resolution 4 is approved, the Company will issue options to Mr Baker, a related party.

#### ***Details of options***

If Resolution 4 is approved the Company will issue to Mr Baker 2,000,000 options, which, if exercised, will entitle him to acquire one Share per option. The options will be issued on the following terms:

- the options will be issued for no consideration;
- each option will, on exercise, entitle the holder to acquire one Share;
- the exercise price is \$0.07 per option;
- each option will have an expiry date of two years from the date of issue; and
- although the options are not being issued under the ESOP, the rules of the ESOP will otherwise apply to the options.

These are materially the same terms as the options issued to the other non-executive directors of the Company pursuant to the approval given by the shareholders at the general meeting of the Company held on 9 September 2008.

#### ***Value of options***

The Board has engaged an independent adviser to prepare a valuation of the options to be granted under Resolution 4. The independent adviser has determined the value of the

options to be issued pursuant to Resolutions 4 to be \$0.057 per option. This value has been derived using both a Black Scholes Option Pricing Model and a Binomial Model Option Pricing Model, assuming the terms set out above and the following additional information:

- share price of \$0.08 (being the closing price of Shares on the ASX on 8 May 2009);
- a risk free rate of 3.49% per annum;
- a volatility factor of 140.8%, which has been determined having regard to the historical trading of the Company's Shares on ASX;
- an expiry date of two years from the date of issue; and
- all other terms and conditions as outlined in this Explanatory Memorandum.

#### ***Why are the options being issued?***

The primary purpose of the grant of the options to Mr Baker under Resolution 4 is not to raise capital but to better align the long-term interests of the Company and Mr Baker by providing an incentive to him to remain with the Company and increase shareholder value.

The issue of options to the other Directors on the same terms as the Options to be issued to Mr Baker was approved at the general meeting of the Company held on 9 September 2008.

#### ***Other information***

For the purposes of Listing Rule 10.13, and for all other purposes, the following information is provided to shareholders in respect of Resolution 4:

- Under Resolution 4, approval is being sought to issue to Mr Baker 2,000,000 options.
- The options will be granted to Mr Baker as soon as practicable after the Meeting, but in any event, no later than one month after the date of the Meeting.
- Because the options are to be issued for no consideration, the Company will not raise any funds from the issue. If any or all of the options are exercised, the funds raised from the issue of Shares to Mr Baker will contribute to the Company's working capital.

Pursuant to Listing Rule 7.2 Exception 14, where an issue is made with the approval of shareholders under Listing Rule 10.11, approval is not required under Listing Rule 7.1.

In accordance with the requirements of Chapter 2E of the Corporations Act, the following additional information is provided to shareholders in respect of Resolution 4:

- Under Resolution 4, the Company will, if the Resolution is approved, be permitted to give Mr Baker, a related party, a financial benefit. The financial benefit to be given is the grant of 2,000,000 options to subscribe for Shares on the terms summarised above.
- If Resolution 4 is passed, the 2,000,000 options issued by the Company would, if exercised, result in the issue of 2,000,000 Shares and existing shareholders' interests in the Company would be diluted by approximately 1.05% (based on Company's issued share capital on 15 May 2009 of 190,409,529 Shares and assuming no other options then on issue are exercised).
- The current annual compensation that Mr Baker is entitled to receive as a Director is set out below in relation to Resolutions 8 to 13.
- The last price that Shares traded on ASX before the finalisation of this Notice was \$0.085 on 13 May 2009. As at this date the lowest and highest price that Shares

traded on ASX in the past 12 months was \$0.01 (on 7 October 2008 and 10 November 2008) and \$0.085 (on 11 May 2009 and 13 May 2009).

### ***Directors' interests and recommendations***

None of the Directors, other than Mr Baker, has an interest in Resolution 4. As the proposed recipient of options under Resolution 4, Mr Baker has an interest in Resolution 4, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Baker, **unanimously recommend that you vote in favour of Resolution 4.**

## **Resolutions 5 and 6 – Approval of share and option placements**

### ***Introduction***

The Company has entered into agreements with Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd pursuant to which:

- the Company issued to Mr Lennox-King 6,750,00 Placement Shares at an issue price of \$0.10 per Placement Share and 6,750,000 Placement Options exercisable at \$0.20 per Placement Option;
- subject to shareholder approval, Mr Lennox-King agreed to subscribe for, and the Company agreed to issue, a further 8,250,000 Placement Shares and Placement Options on the same terms;
- the Company issued to Wealford Investments Limited 1,575,000 Placement Shares at an issue price of \$0.10 per Placement Share and 1,575,000 Placement Options exercisable at \$0.20 per Placement Option;
- subject to shareholder approval, Wealford Investments Limited agreed to subscribe for, and the Company agreed to issue, a further 1,925,000 Placement Shares and Placement Options on the same terms;
- the Company issued to Springtide Capital Pty Ltd 675,000 Placement Shares at an issue price of \$0.10 per Placement Share and 675,000 Placement Options exercisable at \$0.20 per Placement Option; and
- subject to shareholder approval, Springtide Capital Pty Ltd agreed to subscribe for, and the Company agreed to issue, a further 825,000 Placement Shares and Placement Options on the same terms.

Pursuant to Resolution 5, shareholders are requested to ratify the issue of the 9,000,000 Placement Shares and Placement Options that have been issued to Mr Lennox-King and Wealford Investments Limited and Springtide Capital Pty Ltd.

Pursuant to Resolution 6, the Company seeks shareholder approval to issue the additional 11,000,000 Placement Shares and Placement Options that Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd have agreed to subscribe for, subject to shareholder approval being granted.

Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd are not related to each other or the Company.

### ***Why is shareholder approval required?***

Listing Rule 7.1 imposes a limit on the number of equity securities (e.g., Shares or options to subscribe for Shares) that the Company can issue or agree to issue without shareholder approval. In general terms, the Company may not, without shareholder approval, issue or

agree to issue equity securities representing more than 15% of its share capital in a 12 month period.

Securities that are issued with shareholder approval do not reduce the number of equity securities that may be issued by the Company under Listing Rule 7.1.

Under Listing Rule 7.4, shareholder approval can be obtained after the securities are issued if the issue did not breach the 15% limit in Listing Rule 7.1 when made and the Company's members subsequently approve it. The 9,000,000 Placement Shares and Placement Options that have been issued to Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd did not breach the 15% limit. Pursuant to Resolution 5 Shareholders are therefore being asked to approve these issues so that they are not counted towards the Company's 15% limit, giving the Company greater capacity and flexibility to raise additional capital in the future.

Subject to Resolution 6 being passed, the Company has agreed to issue additional Placement Shares and Placement Options to Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd. Under Listing Rule 7.1.5 and Exception 13 of Listing Rule 7.2, an issue of securities is not counted towards the Company's 15% limit under Listing Rule 7.1 if the issue occurs pursuant to an agreement to issue securities that is conditional on shareholders approving the issue before it is made and provided that the securities are not issued without shareholder approval being obtained.

The further issues of Placement Shares and Placement Options to Mr Lennox-King, Wealford Investments Limited and Springtide Capital Pty Ltd are subject to shareholder approval. An approval under Listing Rule 7.1 is required because the Company would, if it were to issue the additional Placement Shares and Placement Options without shareholder approval, exceed the 15% limit in Listing Rule 7.1.

#### ***Terms of Placement Shares and Placement Options***

All Placement Shares will rank equally with all other Shares in the capital of the Company from the date of issue.

The Company will issue to the holder of Placement Shares, for no consideration, a Placement Option for every Placement Share that is issued to them. Each Placement Option entitles the holder on exercise to subscribe for one Share at an exercise price of \$0.20 and to be issued one Piggy-back Option for no consideration. Each Placement Option has a term of two years from its date of issue.

Under the terms of issue of the Placement Options, if the Company's Share price remains above \$0.30 for more than 20 consecutive trading days in the second year of the term of the Placement Options, the holder must exercise the Placement Options within 14 days of that condition being satisfied, or they will expire.

On exercise of a Placement Option, the Placement Option holder will be issued one Share and one Piggy-back Option. The terms of the Piggy-back Options are materially the same as the Placement Options except that:

- on exercise of a Piggy-back Option the Company is required to issue one Share only (i.e., no additional options are issued);
- the exercise price is \$0.50;
- each Piggy-back Option will expire on the first to occur of 30 June or 31 December on or following the second anniversary of the date the Piggy-back Option is issued; and
- if the Company's Share price remains above \$0.70 for more than 20 consecutive trading days in the second year of the term of a Placement Option, the holder must

exercise the Placement Option within 14 days of that condition being satisfied, or it will expire.

The full terms and conditions of the Placement Options and Piggy-back Options are set out in schedules 2 and 3 respectively.

***Additional information regarding the issue of Placement Shares and Placement Options***

Listing Rules 7.3 and 7.5 require the following information to be given to shareholders:

<b>Placement Shares and Placement Options that have been issued (Resolution 5)</b>						
<b>Date of issue</b>	<b>Investor</b>	<b>Security</b>	<b>Issue price</b>	<b>Terms of issue</b>	<b>Number issued</b>	<b>Total capital subscribed</b>
15 May 2009	Wealford Investments Limited	Placement Shares	\$0.10 per Placement Share	Rank equally with existing Shares on issue	1,575,000	\$157,500
15 May 2009	Wealford Investments Limited	Placement Options	Nil	See schedules 2 and 3	1,575,000	Nil
15 May 2009	Mr Lennox-King	Placement Shares	\$0.10 per Placement Share	Rank equally with existing Shares on issue	6,750,000	\$675,000
15 May 2009	Mr Lennox-King	Placement Options	Nil	As set out in schedules 2 and 3	6,750,000	Nil
15 May 2009	Springtide Capital Pty Ltd	Placement Shares	\$0.10 per Placement Share	Rank equally with existing Shares on issue	675,000	\$67,500
15 May 2009	Springtide Capital Pty Ltd	Placement Options	Nil	See schedules 2 and 3	675,000	Nil

<b>Proposed issue of Placement Shares and Placement Options (Resolution 6)</b>						
<b>Date of issue</b>	<b>Investor</b>	<b>Security</b>	<b>Issue price</b>	<b>Terms of issue</b>	<b>Number issued</b>	<b>Total capital subscribed</b>
As soon as practicable, but no later than three months after the Meeting	Wealford Investments Limited	Placement Shares	\$0.10 per Placement Share	To rank equally with existing Shares on date of issue	1,925,000	\$192,500

As above	Wealford Investments Limited	Placement Options	Nil	See schedules 2 and 3	1,925,000	Nil
As above	Mr Lennox-King	Placement Shares	\$0.10 per Placement Share	To rank equally with existing Shares on date of issue	8,250,000	\$825,000
As above	Mr Lennox-King	Placement Options	Nil	As set out in schedules 2 and 3	8,250,000	Nil
As above	Springtide Capital Pty Ltd	Placement Shares	\$0.10 per Placement Share	To rank equally with existing Shares on date of issue	825,000	\$82,500
As above	Springtide Capital Pty Ltd	Placement Options	Nil	As set out in schedules 2 and 3	825,000	Nil

All funds raised from the issues listed above are to be used for the purposes of funding the Company's exploration activities under the Farmin Agreements.

***Effect on issued capital of the Company***

Each Placement Share will be issued with a Placement Option, which, if exercised, will entitle the holder to be issued with a further Share and a Piggy-back Option. Each Piggy-back Option will, if exercised, entitle the holder to be issued with a further Share. As a consequence, for each Placement Share that the Company issues, it may issue up to a further two Shares.

The table below summarises the holdings of Placement Shares that Mr Lennox-King and Wealford Investments Limited will each have if all Placement Shares are issued and each Option and Piggy-back Option is exercised:

Investor	No. of Placement Shares	No. of Placement Options	Maximum no. of Piggy-back Options	Total no. of Shares if all options <sup>1</sup> are exercised	% of total issued Shares <sup>2</sup> assuming all options <sup>1</sup> are exercised
Mr Lennox-King	15,000,000	15,000,000	15,000,000	45,000,000	18.6
Wealford Investments Limited	3,500,000	3,500,000	3,500,000	10,500,000	4.3
Springtide Capital Pty Ltd	1,500,000	1,500,000	1,500,000	4,500,000	1.9
<b>TOTAL</b>	<b>20,000,000</b>	<b>20,000,000</b>	<b>20,000,000</b>	<b>60,000,000</b>	<b>24.8</b>

1 - All Placement Options and Piggy-back Options, but excluding any other options on issue.

2 - Assumes that the total number of Shares on issue is 241,409,529 (being 181,409,529 Shares on issue on 14 May 2009 plus 60,000,000 Shares) and that no other options currently on issue are exercised.

If each of Resolutions 5 and 6 is passed, and 60,000,000 Shares are issued in total, this would dilute shareholders' interests in the Company by approximately 24.8% (based on the Company's issued share capital on 14 May 2009 (being the date prior to the placement issued on 15 May 2009)) of 181,409,529 Shares and assuming no other options then on issue are exercised.

#### ***Director's interests and recommendation***

None of the Directors has an interest in either Resolution 5 or 6. **The Directors unanimously recommend that you vote in favour of Resolutions 5 and 6.**

### **Resolution 7 – Approval of Performance Rights Plan**

#### ***Introduction***

Pursuant to Resolution 7 shareholder approval is sought for the introduction of the Performance Rights Plan and the issue of securities under the Performance Rights Plan.

#### ***Purpose of the Performance Rights Plan***

The purpose of the Performance Rights Plan is to align the interests of participants in the Performance Rights Plan (who may include directors, officers, executives and employees of the Company, and persons engaged by the Company on a contractor basis) with the interests of the Company's shareholders by rewarding participants for creating shareholder value.

#### ***Summary of the Performance Rights Plan***

Under the Performance Rights Plan, the Company may issue eligible participants with Performance Rights. Each Performance Right entitles the holder to subscribe for or be transferred one Share at no consideration, subject to any performance conditions specified by the Board being satisfied.

A Performance Right does not confer an interest in a Share or the usual rights attached to Shares such as dividend and voting rights.

An invitation to participate in the Performance Rights Plan, the particular conditions on which Performance Rights will be granted and the number of Performance Rights to be granted, is at the discretion of the Board.

There is no amount payable on grant of a Performance Right.

The Board may require the payment of an exercise price on exercise of Performance Rights in any offer of the Performance Rights. Currently, there is no plan to require payment of an exercise price on exercise of Performance Rights granted under the Performance Rights Plan.

Performance rights do not confer a right to participate in new issues of capital.

If the Company makes a bonus issue, participants whose Performance Rights have not been exercised will be entitled to an adjustment to the number of Shares that will be issued to them upon exercise of any of those Performance Rights.

In the event of a reorganisation of the issued capital of the Company the number of Shares to which a participant is entitled to on the exercise of a Performance Right will be reconstructed as required by the Listing Rules.

Performance Rights will vest and may be exercised if:

- all applicable performance conditions relating to the Performance Rights have been satisfied;
- an event occurs such as a takeover bid for or winding up of the Company; or
- the Performance Rights otherwise vest in accordance with the Performance Rights Plan (see below regarding cessation of employment).

If a participant dies, is disabled, retires or is made redundant, or in the event of any other reason approved by the Board, and at that time the participant continues to satisfy any other conditions imposed by the Board, the Board may allow the Performance Rights granted to the participant to vest. If no determination is made by the Board within three months after the participant ceases to be an employee, the Performance Rights will lapse.

If a participant ceases to be an employee for any other reason, for example, because their employment is terminated for misconduct, then all Performance Rights held by the participant will lapse immediately.

Unvested Performance Rights will also lapse immediately if the relevant performance conditions attaching to them are not satisfied, if there is an unauthorised transfer of the Performance Rights or if a participant acts fraudulently or dishonestly or is in breach of his or her obligations to the Company or any related body corporate. The last date by which any unvested Performance Rights will lapse is ten years after the date of grant of the Performance Rights.

Performance Rights may not be transferred except with the consent of the Board or, if a participant dies, to the participant's legal personal representative.

Shares issued on exercise of Performance Rights will rank equally with all existing Shares then on issue.

Performance Rights will not be quoted. The Company will apply to ASX for quotation of Shares issued on exercise of Performance Rights.

The Performance Rights Plan will be administered by the Board, who has power to suspend, terminate or amend the plan.

The full terms of the Performance Rights Plan are available from [www.lodestonex.com](http://www.lodestonex.com).

#### ***Why is shareholder approval required?***

Section 195 of the Corporations Act provides that a director of a public company may not vote or be present during meetings of directors when matters in which that director holds a "material personal interest" are being considered.

Subject to Resolutions 8 to 13 being approved, it is proposed that each of the Directors of the Company be issued Performance Rights under the Performance Rights Plan. As consequence, each Director has a material personal interest in the adoption of the Performance Rights Plan and cannot therefore be present at a meeting of the Board at which the Performance Rights Plan is being considered. As every Director of the Company is in this position a meeting of Directors cannot be held to consider whether to adopt the Performance Rights Plan as a quorum of the Board will not be present. In these circumstances section 195(4) of the Corporations Act permits the Board to seek shareholder approval to adopt the Performance Rights Plan. Resolution 7 is being proposed for this purpose.

A Director who ceases to hold office is not permitted by the Corporations Act 2001 (section 200B) to receive a benefit from the Company in connection with their retirement unless the benefit is approved by shareholders under section 200E.

Benefits may arguably be provided under the Performance Rights Plan if Directors cease to hold office, where the Board allows the Performance Rights to vest in the event of the Director's death, disablement, retirement or redundancy. As a result, approval is sought for any benefit that a Director may receive under the Performance Rights Plan on ceasing to hold office with the Company or a related body corporate.

The value of any such benefits cannot be determined at the time of issuing the Notice. The calculation of the value of the benefits would be affected by the number of Performance Rights that vest on the exercise of the discretion by the Board and the market value of the Company's shares at the time the discretion is exercised.

In addition, Listing Rule 7.1 imposes a limit on the number of equity securities (e.g., shares) that the Company can issue without shareholder approval. In general terms, the Company may not, without shareholder approval, issue equity securities representing more than 15% of its share capital in a 12 month period. Unless an exemption applies, an issue of shares by the Company to participants under the Performance Rights Plan will reduce the Company's capacity to issue further securities without requiring shareholder approval under Listing Rule 7.1.

Pursuant to exception 9(b) of Listing Rule 7.2, an issue of securities under an employee incentive scheme that is approved by shareholders will not be taken into account when calculating the maximum number of securities that the Company is permitted to issue within its 15% limit. Resolution 7 is proposed to take advantage of this exception.

#### ***Other information***

Shareholder approval will be required before any Performance Rights can be issued to any Director or related party of the Company under the Performance Rights Plan.

There have been no previous issues of securities under the Performance Rights Plan.

As each of the Directors has an interest in the Performance Rights Plan and the issue of Performance Rights to that Director, the Directors do not consider it appropriate to make a recommendation in relation to Resolution 7.

### **Resolutions 8 to 13 – Approval of issue of Performance Rights to Directors**

#### **Introduction**

Subject to Resolution 7 being passed, pursuant to Resolutions 8 to 13 shareholder approval is sought for the grant by the Company, for no consideration, of:

- 2,000,000 Performance Rights to Mr Martin Ackland (Resolution 8);
- 2,000,000 Performance Rights to Mr Greg Baynton (Resolution 9);
- 2,000,000 Performance Rights to Mr John McCawley (Resolution 10);
- 2,000,000 Performance Rights to Mr Bill Stubbs (Resolution 11);
- 4,000,000 Performance Rights to Mr Lance Grimstone (Resolution 12); and
- 2,000,000 Performance Rights to Mr Grahame Baker (Resolution 13).

The Performance Rights are to be issued pursuant to the Performance Rights Plan on the terms summarised below. Mr Ackland, Mr Baynton, Mr McCawley, Mr Stubbs, Mr Grimstone and Mr Baker are non-executive Directors.

#### ***Why is shareholder approval required?***

*Listing Rule 10.14*

Listing Rule 10.14 provides that the Company must not permit any director, or any associate of a director, to acquire securities under an employee incentive scheme, without the prior approval of its ordinary shareholders. As Mr Ackland, Mr Baynton, Mr McCawley, Mr Stubbs, Mr Grimstone and Mr Baker are non-executive Directors, the proposed issue of Performance Rights to them under the Performance Rights Plan requires the prior approval of the Company's shareholders under Listing Rule 10.14.

#### *Chapter 2E of the Corporations Act*

Chapter 2E of the Corporations Act prohibits the Company from giving a financial benefit to related party of the Company, except with the approval of the Company's members. Agreeing to issue securities to a related party is an example of giving a financial benefit that requires shareholder approval under Chapter 2E.

An approval under Chapter 2E is required in the circumstance because, if any of Resolutions 8 to 13 are approved, the Company will issue Performance Rights to related parties of the Company, being the Directors.

#### **Details of Performance Rights**

The Performance Rights to be granted under each of Resolutions 8 to 13 will be granted on the terms of the Performance Rights Plan that has been summarised above in connection with Resolution 7. They will also be subject to the following performance conditions:

- one half of the Performance Rights that are granted to a participant will vest and become exercisable if the Company's market capitalisation (calculated by multiplying the volume weighted average price of the Company's Shares by the number of fully paid ordinary shares on issue) is \$50 million for a continuous period of five or more trading days; and
- one half of the Performance Rights that are granted to a participant will vest and become exercisable if the volume weighted average price of the Company's Shares is at least \$0.25 for a continuous period of five trading days.

#### **Why are the Performance Rights being issued?**

The Company aims to grow shareholder wealth by pursuing its strategic priorities while minimising costs and cash burn as much as possible. As part of this strategy the Company has kept employee numbers low and has instead relied on the skills and expertise of each of its Directors and the Company's officers.

Consistent with this strategy, the Board has been structured so that it has a depth of expertise in each of the Company's areas of focus, including coal seam gas, coal and precious metals exploration. Particularly as the Company seeks to pursue its current exploration focus and develop itself into a leading participant in the energy sector in Queensland, the Company will continue to place heavy demands on the Board in lieu of engaging additional employees and contractors.

The purpose of the Performance Rights Plan is therefore to reward the Directors and any other participants in the Performance Rights Plan for the successful pursuit of the Company's growth strategy, as measured by tangible improvements in the Company's Share price and market capitalisation, without placing further demands on the Company's cash resources.

Mr Grimstone is to be issued more Performance Rights than the other Directors because he is performing duties for the Company in addition to those of the other Directors.

#### **Other information**

For the purposes of Listing Rule 10.15, the following information is provided to shareholders in respect of Resolutions 8 to 13:

- Under Resolution 8 to 13 approval is being sought to issue each of Mr Ackland, Mr Baynton, Mr McCawley, Mr Stubbs and Mr Baker a maximum of 2,000,000 Performance Rights and Mr Grimstone a maximum of 4,000,000 Performance Rights. An issue of additional Performance Rights to any of them will require a further prior shareholder approval. The maximum number of Shares that may be issued on exercise of these Performance Rights is 14,000,000 Shares.
- The Performance Rights will be granted to each recipient as soon as practicable after the Meeting, but in any event, no later than 12 months after the date of the Meeting.
- Because the Performance Rights are to be issued for no consideration, the Company will not raise any funds from the issue. If any or all of the Performance Rights that vest are exercised, the Company will not raise any additional capital because no consideration is payable for the issue of a Share on exercise of a Performance Right.
- The Company will not provide a loan in connection with the exercise of any Performance Rights.
- As at the date of the Meeting, no Performance Rights will have been issued to any person.
- All Directors may participate in the Performance Rights Plan.

For the purposes of Chapter 2E of the Corporations Act, the following additional information is provided to shareholders in respect of Resolutions 8 to 13:

- Assuming that both vesting conditions attaching to the proposed issue of Performance Rights are satisfied and all Performance Rights are exercised, the value of 2 million Shares (being the maximum number of Shares issued to each participating Director other than Mr Grimstone), 4 million Shares (being the maximum number of Shares issued to Mr Grimstone) and 14 million Shares (being the maximum number of Shares issued to Directors) at varying Share prices is set out in the table below:

Share Price	\$0.085 (Closing price on ASX on 13 May 2009)	\$0.15	\$0.20	\$0.25 (Price at which half of the Performance Rights vest)
Value of 2 million Shares	\$170,000	\$300,000	\$400,000	\$500,000
Value of 4 million Shares	\$340,000	\$600,000	\$800,000	\$1,000,000
Value of 14 million Shares	\$1,190,000	\$2,100,000	\$2,800,000	\$3,500,000

- The current market capitalisation of the Company, assuming a Share price of \$0.085, and a total of 190,409,529 Shares on issue on 15 May 2009 (being the date of finalisation of the Notice) is \$16,184,810. As noted above, one half of the Performance Rights vest if the Company's market capitalisation increases to \$50 million. At the current Share price, and based on the current issued capital, the Company would need to issue an additional 397,825,766 number of Shares to achieve this market capitalisation or, assuming no additional Shares are issued, the Company's share price would need to rise to \$0.263. If the price of Shares were to rise above \$0.085, the number of Shares that would need to be issued to achieve the market capitalisation target would reduce, and vice versa.
- If each of Resolutions 8 to 13 is passed, the 14,000,000 Performance Rights issued by the Company to Directors would, if exercised, result in the issue of 14,000,000

Shares, which would dilute shareholders' interests in the Company by approximately 7.4% (based on the Company's issued share capital on 15 May 2009 (being the date of finalisation of the Notice)) of 190,409,529 Shares and assuming no other options then on issue are exercised.

- Under each of Resolutions 8 to 13 the Company will, if the relevant Resolution is approved, be permitted to give the recipient, a related party, a financial benefit. For each recipient the financial benefit to be given is the grant of that number of Performance Rights described above.
- The annual compensation of each Director for the year ending 30 June 2009 is as follows:

Name	Salary & fees	Non monetary benefits	Post employment and superannuation	Total
Martin Ackland	40,000	25,061	3,600	68,661
Greg Baynton	30,000	25,061	2,700	57,761
John McCawley *1	50,000	25,061	48,100	123,161
Bill Stubbs	30,000	25,061	2,700	57,761
Lance Grimstone	30,000	25,061	2,700	57,761
Grahame Baker *2	6,346	-	571	6,917

\*1 – Mr McCawley was executive an Director from 1 July 2008 to 31 December 2008

\*2 – Mr Baker was appointed a Director on 15 April 2009

### ***Directors' interests and recommendations***

#### ***Resolution 8***

None of the Directors, other than Mr Ackland, has an interest in Resolution 8. As the proposed recipient of Performance Rights under Resolution 8, Mr Ackland has an interest in Resolution 8, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Ackland, have considered all the relevant information relating to Resolution 8 and **unanimously recommend that you vote in favour of it.**

#### ***Resolution 9***

None of the Directors, other than Mr Baynton, has an interest in Resolution 9. As the proposed recipient of Performance Rights under Resolution 9, Mr Baynton has an interest in Resolution 9, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Baynton, have considered all the relevant information relating to Resolution 9 and **unanimously recommend that you vote in favour of it.**

#### ***Resolution 10***

None of the Directors, other than Mr McCawley, has an interest in Resolution 10. As the proposed recipient of Performance Rights under Resolution 10, Mr McCawley has an interest in Resolution 10, and therefore makes no recommendation in relation to it.

The Directors, other than Mr McCawley, have considered all the relevant information relating to Resolution 10 and **unanimously recommend that you vote in favour of it.**

### *Resolution 11*

None of the Directors, other than Mr Stubbs, has an interest in Resolution 11. As the proposed recipient of Performance Rights under Resolution 11, Mr Stubbs has an interest in Resolution 11, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Stubbs, have considered all the relevant information relating to Resolution 11 and **unanimously recommend that you vote in favour of it.**

### *Resolution 12*

None of the Directors, other than Mr Grimstone, has an interest in Resolution 12. As the proposed recipient of Performance Rights under Resolution 12, Mr Grimstone has an interest in Resolution 12, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Grimstone, have considered all the relevant information relating to Resolution 12 and **unanimously recommend that you vote in favour of it.**

### *Resolution 13*

None of the Directors, other than Mr Baker, has an interest in Resolution 13. As the proposed recipient of Performance Rights under Resolution 13, Mr Baker has an interest in Resolution 13, and therefore makes no recommendation in relation to it.

The Directors, other than Mr Baker, have considered all the relevant information relating to Resolution 13 and **unanimously recommend that you vote in favour of it.**

## **Definitions**

**ASX** means ASX Limited, or the stock market operated by it, as the context requires.

**Board** means the board of Directors.

**Business Day** means a day other than a Saturday, Sunday or bank or public holiday in Brisbane, Queensland.

**Coal Farmin Agreement** means the Tambo Coal Project Farmin Agreement dated 10 December 2008 between the Company, Lodestone Coal and Tambo, as amended, the terms of which are summarised in the Explanatory Memorandum.

**Coal Tenements** means Exploration Permits for Coal (**EPC**) 1414, 1415, 1417, 1418, 1481, 1482 and 1484.

**Company** means Lodestone Exploration Limited ACN 075 877 075.

**Corporations Act** means the *Corporations Act 2001* (Cth).

**Director** means a director of the Company.

**Eligible Shareholder** means a shareholder of the Company eligible to vote on the Resolutions.

**ESOP** means the Employee Share Option Plan approved by the shareholders at the extraordinary general meeting of the Company held on 9 September 2008.

**Explanatory Memorandum** means this memorandum, which forms part of and accompanies the Notice.

**Farmin Agreements** means the Gas Farmin Agreement and Coal Farmin Agreement.

**Gas Farmin Agreement** means the Tambo Gas Project Farmin Agreement dated 10 December 2008 between the Company, Lodestone CSG and Tambo, as amended, the terms of which are summarised in the Explanatory Memorandum.

**Gas Tenement** means Authority to Prospect (**ATP**) 1020.

**Independent Expert's Report** means the report of the Independent Expert prepared for the purposes of Listing Rule 10.10 as to whether the transactions pursuant to the Coal Farmin Agreement and Gas Farmin Agreement are fair and reasonable to the Company's Eligible Shareholders, which is attached at schedule 1.

**Independent Expert** means MBA Petroleum Consultants.

**Joint Coal Tenements** means EPC 1622, 1623, 1624, 1625, 1632, 1633, 1644, 1697 and 1719.

**Listing Rules** means the official listing rules of ASX.

**Lodestone Coal** means Lodestone Coal Pty Ltd ACN 134 427 919.

**Lodestone CSG** means Lodestone CSG Pty Limited ACN 134 448 258.

**Meeting** means the extraordinary general meeting of the Company to be held for the purpose of considering the Resolutions.

**Notice** means the notice of meeting of the Company dated 15 May 2009.

**Performance Right** means a right of a participant in the Performance Rights Plan to be issued a Share on the satisfaction of applicable performance conditions and subject to the other terms and conditions of the Performance Rights Plan.

**Performance Rights Plan** means the incentive plan for which the Company is seeking approval under Resolution 7.

**Piggy-back Option** means an option, issued on exercise of a Placement Option, to subscribe for a Share on the terms set out in schedule 3.

**Placement Share** means a share issued by the Company together with a Placement Option.

**Placement Option** means an option to subscribe for a Share and a Piggy-back Option on the terms set out in schedule 2.

**Proxy Form** means a form prepared by the Company for the purposes of the Meeting pursuant to which a member of the Company may appoint one or more proxies to attend the Meeting and vote of the Member's behalf.

**QDME** means the Queensland Department of Minerals and Energy.

**Resolution** means a resolution set out in the Notice.

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

**Tambo** means Tambo Coal & Gas Pty Limited ACN 131 603 766.

**Schedule 1**  
**Independent Expert's Report**

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**Principals: Walter F Muir  
Douglas B Barrenger**

**Technical and Management  
Advisors to the Petroleum Industry**

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15 May 2009

The Directors  
Lodestone Exploration Limited  
Level 1,  
101 Edward Street  
Brisbane QLD 4000

### **Independent Expert's Report - Tambo Coal and Gas Projects**

#### **1.0 Introduction**

MBA Petroleum Consultants (MBA) was commissioned by Lodestone Exploration Limited (Lodestone) to provide an Independent Expert's Report relating to the farm-in agreements covering seven (7) coal applications and one (1) petroleum application exploration tenements lying in the south-eastern Eromanga Basin of Queensland.

The areas are held by Tambo Coal & Gas Pty Ltd (Tambo), a company controlled by Mr Greg Baynton, who is also a director of Lodestone. Lodestone has, therefore, sought an informed and independent opinion on the extent to which the terms and conditions of the two (2) Farm-In Agreements, one being for the potential coal resources, 'Tambo Coal Project Farm-in Agreement', and the other for the potential coal seam gas (CSG) resources, 'Tambo Gas Project Farm-in Agreement', (the agreements) are "fair and reasonable", for the non-associated Lodestone shareholders.

When granted, Tambo will hold a 100% interest in the seven coal permits and the petroleum permit. Tambo has agreed to farm out to Lodestone a 50% interest in relation to the future tenements.

The full portfolio of relevant coal application tenements and Authority to Prospect (ATP) 1020P, comprising the Tambo Coal and Gas Projects, is illustrated in Figure 1. Of the coal application, which number fourteen (14) in total, seven (7) tenements are specifically the subject of the coal farm-in agreement. The other seven (7) coal tenements have been jointly applied for by Tambo and Lodestone, who will each hold a 50% interest when granted. Together with the farm-in permits, a substantial area will be held.

MBA has concluded that the area is at the early stage of exploration and concepts are based on sparse drilling for oil and gas exploration, and stratigraphic and water bores.

MBA considers that the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement are fair and reasonable for the non-associated shareholders of Lodestone. This view is based on a number of factors, such as previous farmout and permit purchases. Although MBA considers that the prospects of Lodestone discovering coal and gas deposits in the tenement areas to be low, substantial coal and substantial gas resources are possible. In addition, under the farm-in agreements, Lodestone has a right to design an exploration program that it considers offers the best prospects of successfully discovering any such deposits. Further, Lodestone may at any time terminate its exploration program without any ongoing obligation to spend further funds on exploration, which limits its financial commitments under the farm-in agreements, and which, subject to various transaction specific provisions, are in a typical form.

## Contents

<b>1.0 Introduction .....</b>	<b>1</b>
<b>2.0 Summary .....</b>	<b>4</b>
<b>3.0 Overview .....</b>	<b>5</b>
<b>4.0 Farm-in Agreement Key Conditions .....</b>	<b>6</b>
<b>5.0 Coal Farm-in Application Tenement Areas .....</b>	<b>8</b>
5.1 Tenement Commitments (Work Programs) and Indicative Costs.....	8
5.2 Exploration Rationale .....	9
<b>6.0 Geology and Stratigraphy.....</b>	<b>9</b>
<b>7.0 Previous Exploration History .....</b>	<b>11</b>
7.1 Previous Exploration History – Coal .....	11
7.1.1 EPC 259 ‘Merivale’ .....	12
7.1.2 EPC 263 ‘Forest Vale’ .....	12
7.1.3 EPC 314 ‘Redford’.....	12
7.1.4 EPC 385 ‘Westgrove’ .....	12
7.1.5 EPC 1017 ‘Bymount’ .....	12
7.1.6 EPC 1018 ‘Injune’ .....	12
7.1.7 EPC 1149 ‘Blackall’ .....	13
7.1.8 EPC 1192.....	13
<b>8.0 Exploration History – Petroleum and Stratigraphic Borehole Data .....</b>	<b>14</b>
8.1 Petroleum Data .....	14
8.2 Resource potential of the Tambo Project Area Eromanga Basin sequence.....	14
<b>9.0 Farm-out and Permit Purchases .....</b>	<b>16</b>
<b>10.0 General Description of Coal Seam Gas .....</b>	<b>16</b>
<b>11.0 Comparison of Gas Contents with Existing Coal Seam Gas Producers .....</b>	<b>18</b>
<b>12.0 Water Disposal.....</b>	<b>19</b>
<b>13.0 Methodology .....</b>	<b>19</b>
<b>MBA has been asked to express an opinion as to whether the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement are fair and reasonable for non-associated shareholders of Lodestone. The methodology that MBA has adopted in forming a view that the farm-in agreements are fair and reasonable has involved an assessment by MBA of the following factors: .....</b>	<b>19</b>
<b>(a) within the areas that are the subject of the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement, the low level of exploration that has been conducted in the past; .....</b>	<b>20</b>
<b>(b) the geology of the tenement areas and the probability of commercial coal and coal seam gas resources being discovered; .....</b>	<b>20</b>

(c) the structure of the farm-in agreements, Lodestone’s obligations to undertake exploration work and its rights of withdrawal; .....	20
(d) Lodestone’s rights to design the exploration program for the tenement areas; and.....	20
(e) the general terms of the farm-in agreements; .....	20
<b>14.0 Conclusion.....</b>	<b>20</b>
<b>15.0 Statements .....</b>	<b>21</b>
15.1. MBA Payment .....	21
15.2. Declaration .....	21
15.3. Qualifications.....	21
<b>16.0 Bibliography .....</b>	<b>22</b>
<b>17.0 Technical Terms .....</b>	<b>23</b>

## 2.0 Summary

- Tambo has applied for seven (7) coal tenements (numbers in the 1400s) (five year terms) and one (1) petroleum tenement (four year term) and will hold 100% interest when granted.
- Lodestone, together with Tambo, has applied for seven (7) coal tenements (numbers in the 1600s). The companies will each hold a 50% interest when granted (five year terms).
- Together, these applications comprise the Tambo Coal Project.
- There are two (2) separate farm-in agreements, one for coal tenements and one for the petroleum tenement.
- Tambo will farm out a 50% interest to Lodestone in coal exploration tenements (applications) for a total expenditure of \$5 million, to be earned in 10%/\$1 million stages over four years (Tambo Coal Project Farm-in Agreement).
- Tambo will farm out a 50% interest to Lodestone in ATP 1020P, recently granted, for a total expenditure of \$5 million, to be earned in 10%/\$1 million stages over four years (Tambo Gas Project Farm-in Agreement).
- Total cost, over four years, of both farm-ins will be \$10 million for Lodestone to earn a 50% interest in both the coal and the petroleum tenements.
- The target formation is the Birkhead Formation of the Eromanga Basin and its stratigraphic equivalent, the Walloon Sub Group of the Surat Basin.
- The Walloon Sub Group contains significant volumes of coal to the east of the Tambo Coal Project with a world-class mine planned by Xstrata (Wandoan), and large coal seam gas resources currently being drilled so as to prove enough volume for up to four (4) 3.5 mega-tonne (Mt) liquid natural gas (LNG) trains, also a world-class asset.
- Both coal and gas will exist in the Tambo Coal Project. Lodestone's objective will be to explore for and discover potentially economic resources of either coal or gas, or both.
- Lodestone aims to discover gas resources from which the revenue could assist with the development of a coal mine in a best case scenario.
- The chance of success for finding a coal deposit is considered low, though large resources are possible.
- The chance of success for finding commercial gas resources is also considered low, though very large resources are possible.
- MBA is satisfied that Lodestone will have reasonable protection should the project be considered unsuccessful before completion of the farm-in deals.

### 3.0 Overview

The Tambo Coal Project comprises a very large area overlying the western margin of the Eromanga Basin and eastern margin of the Surat Basin (Figure 2). There are fourteen (14) applications for coal tenements, seven (7) of which form part of the Tambo Coal Project Farm-in Agreement as well as one recently-granted petroleum release, ATP 1020P, which forms the Tambo Gas Project Farm-in Agreement.

Tambo constructed the original portfolio of permit applications, the seven coal, and one petroleum, with the view to farm out the coal exploration and the CSG exploration. Lodestone reviewed the prospectivity and believes that the total area is significant and warrants further study and investigation, including the drilling of wells and acquisition of seismic.

Together the companies have applied for a further seven (7) coal permits to effectively tie-up a very large exploration area.

The main play is the coal seams of the middle Jurassic coal measures of the Birkhead Formation in the Eromanga Basin and the equivalent (extension) of the Birkhead, the Walloon Sub Group in the Surat Basin.

Lodestone is interested in discovering exploitable coal resources. Coal seam gas is also being targeted in the area of the petroleum application. In recent times there has been significant interest in the coals of the Walloon Sub Group for coal mining with potential at Wandoan for a world class mine (Xstrata), as well as for coal seam gas, which is currently the subject of enormous exploration and reserve growth in preparation for the development of a massive liquid natural gas (LNG) production facility at Gladstone.

The coal exploration tenements that are the subject of the farm-in agreement are listed below in Table 1, and this includes the value of the proposed exploration work program commitment that was submitted with the tenement applications.

Tambo has agreed for Lodestone to progressively earn a 50% interest in the farm-in tenements, in return for 100% funding of exploration by Lodestone, totalling \$5 million for the coal tenements and \$5 million for the petroleum tenement. Therefore, the total farm-in value to earn 50% in both the coal and petroleum tenements is \$10 million.

As each farm-in proceeds, Lodestone will earn a 10% interest in the Coal Farm-in for the expenditure of \$1 million, progressively earning 50% after 5 earning stages. The Gas Farm-in Agreement has the same phases of 10% per \$1 million expenditure.

Lodestone can participate in, and may or may not complete, either or both of the farm-in agreements.

Under the agreements, Lodestone has a 4-year "earning period" within which to achieve the five (5) 10% earning stages in all seven (7) of the combined coal farm-in applications and the petroleum permit.

Overall, the potential commitment to keep the 7 coal farm-in tenements and the one petroleum tenement in good standing over the tenement periods will include the acquisition of up to:

- 63 line kilometers of two dimensional (2D) seismic (63km in the 7 coal permits and 120km in the petroleum permit);
- 140 wells (coal exploration) at 150 to 200m average (23,450 drilling meters in the 7 coal permits); and
- 45 wells in ATP 1020P (gas exploration) at 200m average (9,000 drilling meters) although a lesser number of wells between 200 and 800m may represent substantive compliance under the terms of the grant.

The value of the work programs proposed in the tenement applications (5-year term) for the seven coal applications that form the farm-in agreement amounts to \$8.54 million.

Expenditure on jointly-applied tenements will count towards the earning of interest in the farm-in tenements.

The value of the work programs proposed for ATP 1020P over the initial 4-year term is estimated by the Queensland Department of Mines and Energy (“DME”) (ATP 1020 – Approved initial work program and expenditure) to be \$12.25 million (Table 2). Lodestone will pay up to \$5 million at 100% and then the remainder of the \$7.25 million at 50% (\$3.625 million) for a total of \$8.625 million by Lodestone to fulfil all of the permit commitments as stated in the “Approved Initial Work Program and Expenditure, ATP1020P”.

#### **4.0 Farm-in Agreement Key Conditions**

There are two farm-in agreements, one pertaining to the seven coal applications and the other to the single petroleum permit. These are:

1. Tambo Coal Project Farm-in Agreement between Lodestone Coal Pty Ltd (formerly Lodestone Energy Pty Ltd) and Lodestone Exploration Limited (together, Lodestone) and Tambo Coal & Gas Pty Ltd; and
2. Tambo Gas Project Farm-in Agreement between Lodestone CSG Pty Ltd and Lodestone Exploration Limited (together, Lodestone) and Tambo Coal & Gas Pty Ltd.

Some key points of both of the agreements are:

- The agreements coming into effect are conditional upon:
  - acceptance by a majority of shareholders at a general meeting;
  - Lodestone agreeing that the petroleum and/or some or all of the coal tenements involved are “acceptable tenements”; and
  - that the agreement is independently deemed to be fair and reasonable.
- If the agreement does not proceed due to any “condition precedent” not being met, monies paid by Lodestone for rental on behalf of Tambo (tenement rental costs) are refundable to Lodestone.
- Lodestone can earn a 10% “undivided interest” in the seven coal tenements for each \$1 million spent, and can earn up to 50% (5 stages, each requiring \$1 million expenditure), over an earning period of 4 years.
- Lodestone can earn a 10% “undivided interest” in the ATP 1020P for each \$1 million spent, and can earn up to 50% (5 stages, each requiring \$1 million expenditure), over an earning period of 4 years.
- As the coal tenements are granted by the DME and if Lodestone gives notice to Tambo that the tenements are “acceptable tenements”, Lodestone is required to pay the annual tenement rental amounts. This financial obligation is calculated to be approximately \$87,500 for each coal tenement, and up to approximately \$1,225,000 for 14 permits over Years 1 to 4. These rental costs count favourably towards Tambo’s earning obligation.
- Lodestone will be the Operator of the coal and gas projects and be able to plan and conduct exploration as it sees fit at any time after the commencement date of the agreement. In this capacity, Lodestone is required to maintain the tenements in good standing (compliance obligations).
- In respect of the coal farm-in tenements, by giving written notice, Lodestone can at any time advise Tambo that a tenement is no longer prospective, and that tenement will no longer be part of the agreement. However, Lodestone’s earning obligation does not reduce, and it can still fulfil its earning obligation on the remaining tenements.
- At the fulfilment of each stage of the earning obligation, by giving notice to Tambo, Lodestone would be granted its earned equity in the tenement title (Lodestone is required to do the necessary paperwork and pay the application fees to the DME to so action the transfer of title).

- If by the end of the earning period Lodestone has met all its earning obligations, Tambo and Lodestone would initiate a 50:50 JV, one for the coal permits and one for the petroleum permit.
- If, by the end of the earning period, Lodestone has not met its full earning obligation, yet had met at least stage 1, or other stage, Lodestone's participating interest in either the coal or petroleum Joint Venture would be equivalent to its Earned Interest at the date of expiry of the Earning Period.
- With (not less than) 30 days written notice, Lodestone can withdraw from either agreement at any time without fulfilling its earning obligation.
- Any unmet expenditure obligations would be payable to Tambo on a pro-rata basis (\$1000 per year per sub-block for the coal tenements and \$3,062,500 per year for the ATP 1020P) for the balance of the year in which it withdraws, and Lodestone would equally be entitled to receive repayment of any security amounts and the pro-rata portion of any rental monies paid in advance.

## 5.0 Coal Farm-in Application Tenement Areas

The coal farm-in tenement areas (EPCA 1414, 1415, 1417, 1418, 1481, 1482 and 1484) are contiguous, and coincide with the south-eastern margin of the Eromanga Basin, extending along strike some 150km from just to the north of Mitchell, north and west to the vicinity of Tambo.

The areas are adjoined to the north and south by an additional seven (7) areas applied for jointly by Tambo and Lodestone (EPCA 1621, 1622, 1623, 1624, 1625, 1633, and 1644), which in total extend the entire Tambo Coal Project over more than 300km strike length of this part of the Eromanga Basin.

From the basin margins on the east of the tenement boundaries, the application areas extend down-dip to the south and west for a distance of up to 50km.

Each of the EPC application areas extend over 300 sub-blocks (945km<sup>2</sup>). The applications were originally made for a term of 3 years. Lodestone has confirmed that subsequently a request was made to the DME to extend the terms to be 5 years and this is likely to be accepted.

### 5.1 Tenement Commitments (Work Programs) and Indicative Costs

The work programs for each 'farm-in' application are exactly the same and have an approximate expenditure value of \$1.2 million over 5 years (Table 1).

**Table 1: Tambo Coal Project ' Coal Farm-in' Tenements** (EPCA 1414, 1415, 1417, 1418, 1481, 1482 and 1484)

Tenement (EPCA)	Work Program Budget (A\$'000)					Total
	Year 1	Year 2	Year 3	Year 4	Year 5	
	G&G 4.5km seismic & 150m drilling	4.5km Seismic & 1500m drilling	1000m drilling	700m drilling	G&G	
1414	\$150	\$450	\$240	\$200	\$180	\$1,220
1415	\$150	\$450	\$240	\$200	\$180	\$1,220
1417	\$150	\$450	\$240	\$200	\$180	\$1,220
1418	\$150	\$450	\$240	\$200	\$180	\$1,220
1481	\$150	\$450	\$240	\$200	\$180	\$1,220
1482	\$150	\$450	\$240	\$200	\$180	\$1,220
1484	\$150	\$450	\$240	\$200	\$180	\$1,220
<b>TOTAL</b>	<b>\$1,050</b>	<b>\$3,150</b>	<b>\$1,680</b>	<b>\$1,400</b>	<b>\$1,260</b>	<b>\$8,540</b>

In addition to the work program commitments, annual tenement rent due upon grant will be \$40,000 each in year 1, and a further estimated \$110,000 each over years 2 to 4.

More recently, Tambo and Lodestone jointly applied for another seven (7) coal tenements (EPCA 1621, 1622, 1623, 1624, 1625, 1633 and 1644), each with a 50% working interest (Figure 1). Tambo and Lodestone will share costs equally (50% each) for the commitments on these EPCs. The expenditure on these tenements by Lodestone will count towards its interest earning value.

Table 2 shows the petroleum commitments as detailed by the Department of Mines and Energy under "Approved Initial Work Program and Expenditure, ATP1020P" of the grant document. The document suggests that 8250 metres will be drilled in 45 wells, however, it is possible that fewer holes may be considered substantially compliant, provided total metres and costs are met.

**Table 2: Tambo Gas Project 'Petroleum Farm-in' Tenement** (ATP 1020P – "Approved Initial Work Program and Expenditure" as shown in the grant document)

Period 1	Authorised Activities	Expenditure
Two (2) years: commencing 1 May 2009	<ul style="list-style-type: none"> <li>• Geological &amp; Geophysical Studies</li> <li>• 600km reprocessing</li> <li>• 180km 2D seismic</li> <li>• Drill 20 wells (depth 200m)</li> </ul>	<b>\$8,000,000</b>
Two (2) years commencing 1 May 2011	<ul style="list-style-type: none"> <li>• Drill 15 wells (depth 150m)</li> <li>• Drill 10 wells (depth 200m)</li> <li>• Geological &amp; Geophysical studies</li> </ul>	<b>\$4,250,000</b>
		<b>\$12,500,000</b>

NOTE: Petroleum is a 4-year commitment term rather than year-by-year as shown here

## 5.2 Exploration Rationale

The exploration rationale of Tambo and Lodestone is to explore the southeast Eromanga Basin and western Surat Basin, concentrating on that part of the stratigraphic sequence which effectively represents the Birkhead Formation and its equivalent, the Walloon Sub Group in the adjoining Surat Basin (Figure 3).

The Walloon Sub Group contains numerous and widespread commercial coal resources, ranging in size and scale from quite small (50Mt) to very large (more than 1 billion tonnes).

The Surat and Eromanga Basins are separated by the Nebine Ridge, a structural basement “high” trending north-south and aligned approximately through Morven and Injune (Figure 2).

Both basins contain age-equivalent and lithologically very similar rock sequences, and the lithostratigraphic relationships between the two basins are - for the most part – reasonably well studied and understood.

Lodestone has advised MBA that its objective is to locate large-scale coal resources, together with accompanying coal seam gas fields whose early revenues are sufficient to justify and support the development of an eventual 20 to 30 million tonne per year export mining operation.

To fulfil this objective, it would be necessary to locate gross in-situ coal resources of at least 0.5 billion tonnes. This aggregate resource need not occur as a single deposit, and could be multiple, lesser deposits of smaller tonnage provided all deposits are in sufficiently close proximity to be developed together as a ‘project’.

As ATP 1020P partially overlaps some of the coal tenements, the successful identification of either a coal seam gas field downdip or a coal mining project updip will encourage exploration for the other, and provide further commercial incentives for combined development and exploitation.

## 6.0 Geology and Stratigraphy

Both the Eromanga and the Surat Basins are components of the Great Artesian Basin, a large Jurassic-Cretaceous intra-cratonic basin that covers 1.7 million square kilometres of Eastern Australia. The Eromanga Basin in central Australia covers parts of western Queensland, the Northern Territory, New South Wales and South Australia. The Surat Basin is located to the east of the Eromanga Basin. The North-South oriented Nebine Ridge is a structural basement ‘high’ and defines the boundary between the two basins.

Substantial coal exploration in the past two decades has demonstrated that the Walloon Sub Group in the Surat Basin is sub-divided into three recognisable subunits: the Taroom Coal Measures at the base, the Tangalooma Sandstone Member and the Juandah Coal Measures at the top.

Proven coal resources (measured and indicated status), suited to surface mining operations in the Walloon exceed 4 billion tonnes. All of the known resources are thermal quality, and the coal characteristics and burial history dictate that coking quality coal is not expected to occur in the Surat Basin. Coal production from within the Walloon in the Surat Basin dates from at least as early as 1914, and a number of large-scale commercial operations are currently operating (Wilkie Creek, Kogan Creek and Wandoan – commencing soon; Figure 4), with others planned for the

near-term future (such as Wandoan - Xstrata). All existing mining operations are surface, open-cut mines, and it is unlikely that the Surat Basin coal resources could justify the future development of large-scale underground longwall-style operations particularly as coals are not usually continuous.

The style of the coal deposits is lenticular and many thousands of coal exploration holes have been drilled in the Surat Basin, the majority of which failed to intersect any coal that might be regarded as 'significant' (say, greater than 1m thick). Many holes intersected thin, banded coal seams. It is extremely difficult in most places to correlate between even closely spaced holes.

The nature of the Surat coal deposits is such that it is quite possible to intersect significant coal (greater than 10m thick) in one hole, and then not find a similar thickness in the next hole as little as 1000m (or less) distance away.

To date, only the relatively shallow margins of the Surat Basin have been systematically explored for coal. Recently, the drilling of coal seam gas wells has shown significantly more coal than this exists at depth. Particularly in the past 5 years, significant coal seam gas reserves have been identified and are now being developed for massive LNG plants to be built in Gladstone.

CSG is extracted from both the Juandah and Taroom coal measures with gas contents ranging from 1.15-13.17m<sup>3</sup>/t (DAF). Individual coals within the Walloon Sub Group are typically less than 2m thick. In some places there are 30 or more individual coal seams. In the eastern Surat Basin the Walloon Sub Group is 300 to 350m thick and contains 20 to 30m of net coal. Traditionally, the overall Walloon thickness and the amount of net coal present, are thought to thin towards the west, becoming 150 to 200m Walloon thickness, with 10 to 15m of net coal, on the Roma Shelf.

Also, coal seam gas usually requires net coal intervals of greater than 10m to be viable. If found it would need to be over an area of approximately 100km<sup>2</sup>, a much larger area than required for a significant, mineable resources. This will need to have an average minimum depth of 200m and range from about 100 to 800m (Figure 2). Given the lack of drillhole data it is quite possible that a gas resource could exist. This is more likely to be in the east than in the west. Whether the petroleum application may contain may contain such a resource is quite unknown.

Conventional thinking would expect that the net coal will be even less on the Nebine Ridge and further west into the Eromanga Basin. However, there are some indications that thick coals may be present to the west of the Nebine Ridge.

Lodestone has obtained nearly all data that it can in an attempt to find indications of thick coal sections and resolve the stratigraphy.

Petroleum and stratigraphic bores have been used, though these are quite sparse (Figure 5). In particular, petroleum wells barely recorded any information over the upper 500m of drilled section. So the information within the important depth range of the Walloon and above the Birkhead is of questionable quality.

Therefore, Lodestone has turned to the water wells which are of relatively high density and these have been used as a primary source of widespread data across the tenements.

Water wells would not have had the benefit of a geologist on site, and most penetrated to relatively shallow depths. Lithological data is very variable in its quality and there are only rarely supporting wireline logs. However, they represent more than a century of field observation, sometimes to considerable depths and once collar elevations are corrected to modern topographic mapping standards, they provide an excellent insight into the stratigraphic simplicity of the region.

The Walloon coals are typically high volatile with excellent combustion and burn-out characteristics and ideal for blending with lower-quality thermal coals. Walloon coals are also perhydrous and potentially suited to the production of liquid fuels through gasification or liquefaction.

The Permian coals of the Bandanna (or Rangal) Formation outcrop to the north of the permits and dip to the south beneath the permits. These are not discussed here as they are presently thought to be too deeply buried to be prospective for CSG and are currently not a target of Lodestone.

Coals within the tenement currently thought to belong to the Early Jurassic Evergreen Formation may also be a CSG target of Lodestone.

Westward, the Walloon Sub Group is traditionally thought to gradually change into the Birkhead Formation. In fact, this change is represented by a distinct line on the western Nebine Ridge, which is the geological divide between the Surat and Eromanga Basins (Figure 2). It also seems to coincide with the boundary between the areas of responsibility of two different geological groups, one mapping in the Surat Basin, and the other in the Eromanga Basin

The Surat geological group, concentrated on coal using Surat Basin terminology, mapped from east to west, utilising the extensive coal and petroleum database that extends to just west of the Roma Shelf.

At the same time the Eromanga geological group, concentrated on petroleum exploration and using Eromanga Basin terminology, mapped from west to east, using extensive petroleum data that extends to just east of the Cooper/Eromanga oil and gas fields. Unfortunately, these two data sets did not meet and left a significant gap which was arbitrarily divided. Because of this, the extent and thickness of the Walloon Sub Group coals, and their equivalents in the Birkhead Formation are poorly known west of the Roma Shelf and throughout the Tambo Project.

The geological evolution of the Surat Basin and Eromanga Basin is more or less parallel. While variations in the stratigraphic sequence occur within and between each basin, Jurassic and Cretaceous sedimentary rocks have equivalent facies in both basins.

Exon (1976) suggested that from Late Triassic to Early Jurassic, sedimentation occurred in a cyclic fashion both in the Eromanga and the Surat Basins. Each cycle is associated with grading from deposition initially in high energy environments, and over time and upwards through the section to low energy depositional environment. Braided stream sedimentation was followed by sedimentation in rivers and then swamps, lakes and deltas. Exon (1976) attributes this cyclical depositional mechanism to global sea-level changes caused by periodic climate changes.

The Injune Creek Group is of primary interest here. It is divided to a number of formations. The oldest unit of the Injune Creek Group in Surat Basin is the fluvialite Eurombah Formation consisting of sandstone, minor conglomerate, siltstone and mudstone. The formation is traditionally believed to thin to the west and is not therefore distinguished within the Eromanga Basin. Overlying the Eurombah is the Walloon Sub Group in the Surat Basin.

Jones and Patrick (1981) divided the Walloon Sub Group in the Surat Basin into three units, namely the Taroom Coal Measures at the base, the Tangalooma Sandstone and the Juandah Coal Measures at the top.

Conventional opinion correlates the Walloon Sub-Group with the Birkhead Formation in the Eromanga Basin. The Birkhead Formation consists of sub-labile to labile sandstone and siltstone with minor carbonaceous mudstone and coal. However, while significant coal deposition is evident in the Walloon Sub Group, coal occurrences in the Birkhead Formation are generally regarded to be less common.

The Springbok Sandstone in the Surat Basin overlies the Walloon Subgroup. Traditionally, its equivalent is thought to be the Adori Sandstone in the Eromanga Basin. The Springbok Sandstone was deposited in a low energy fluvial environment and consists of cross-bedded labile sandstone, mudstone and thin coal lenses. Yet the Adori Sandstone, in contrast, is a high energy fluvialite deposit, consisting of sub-labile to labile sandstone with minor pebble bands and coarse sandstone lenses.

In the absence of better data, this stratigraphic correlation would appear sound.

## **7.0 Previous Exploration History**

### ***7.1 Previous Exploration History – Coal***

The relevant part of the Eromanga Basin, which is the subject of a large portion of the Tambo Coal Project, is almost wholly lacking in any previous coal exploration activity.

Historical coal tenements in the Tambo Coal Project region are mostly confined to the western parts of the Surat Basin, and to the Rolleston-Springsure Shelf region to the north in relation to the Permian Bandanna (Rangal) Formation.

The latter is of no relevance to the Tambo project areas.

The following is a brief summary of exploration results obtained from relevant historical tenements held in the Surat Basin, and which covered (more or less) equivalent stratigraphic intervals to that of the Tambo Coal Project.

#### **7.1.1 EPC 259 'Merivale'**

In the late 1970s, EPC 259 'Merivale' covered an area to the north and east of Tambo applications EPCA 1623, and 1624. Exploration was conducted over a period of about 4 years. A total of 10 non-cored holes were drilled, with all but one geophysically logged. Some thin and banded coal seams were located, and two small inferred coal resources were defined (Munya, and Ninderra resources) for an aggregate 35 million tonnes (Mt) in situ.

#### **7.1.2 EPC 263 'Forest Vale'**

The 'Forest Vale' area, EPC 263 was explored briefly in the westernmost part of the Surat Basin between 1979 and 1980/81, and coincides with an area immediately to the north of and adjacent to Tambo application areas EPCA's 1623 and 1624.

Exploration conducted within EPC 263 in the late 1970s and early 1980s included the completion of 6 drill holes, all of which intersected minor shallow coal seams between 40 and 80m depth. These were interpreted as being within the upper Juandah Coal Measures. Seam thicknesses were typically between 0.5 and 1.5m.

#### **7.1.3 EPC 314 'Redford'**

Between 1980 and 1981, CRA Exploration (Pacific Coal Pty Ltd) held title to the 'Redford' area. This is the only historical coal exploration tenement which has any overlap (partial or whole) with any of the current Tambo application areas

Pacific Coal conducted an initial 6-months of scout mapping and ground truthing in an effort to target its exploration effort and ultimately drilled 31 rotary holes, including 8 partially cored holes. Seven (7) holes intersected minor coal seams, up to a maximum thickness of 0.7 metres.

In its final report, Pacific Coal states '*...It was thought that some thickening of the coal horizons in the Birkhead Formation might occur to the northwest, away from the Nebine Ridge. However, the constraint imposed by the southern boundary of the Central Queensland Coal Reserve Area 55D prevented application for potentially more prospective ground in the region of the Chesterton Syncline and other synclinal axes to the northwest.*' (Hewitt, 1981).

Although their tenement area was very large, the drilling campaign completed by Pacific Coal covered only a very small percentage of the tenement area.

#### **7.1.4 EPC 385 'Westgrove'**

The Operator of EPC 385 quoted the existence of coal known from previous work in the central-western part of the tenement (EPC 263 Merivale) as being potentially significant and greater than 1 m in thickness, at depths between 50 to 100m. However, the Operator conducted no additional exploration and relinquished the area as non-prospective for commercial-scale coal resources at that time (Alder, 1982).

#### **7.1.5 EPC 1017 'Bymount'**

This tenement is currently held by Cockatoo Coal and remains current. As such no new data is available.

The area forms part of the Injune coal project mentioned below and contains cumulative coal thickness in excess of 4 metres.

#### **7.1.6 EPC 1018 'Injune'**

This tenement held by Cockatoo Coal remains current and no new data pertaining to recent work is yet available.

The area is more or less coincident with an earlier tenement EPC 259 (see above) dating from the 1970s, and contains the previously-identified Munya and Ninderra inferred resources.

The only company report yet submitted to the DME for this area and now on 'open file' is for 12 sub-blocks that were relinquished, within which no additional work was completed.

#### **7.1.7 EPC 1149 'Blackall'**

This is a current exploration area held by East Energy Resources Limited

The area was the subject of an extensive exploration drilling program in 2008 resulting in an increase in, estimated in ground coal to 500-550 million tonnes.

"Unweathered, significant, coal seams have been discovered as close as 12.77m below ground level." (Eastern Energy Resources, 2008)

#### **7.1.8 EPC 1192**

This is a current exploration area held by Argos (Qld) Pty Ltd.

The area was granted in January 2008. As a current tenement, there are as yet no 'open file' company reports available with which to assess exploration results, potential, or the geology of the area.

The tenement coincides with the known location of the Hendon Park and Cornwall inferred coal resource areas, which lie close to the western boundary of EPC 1192 and adjacent to the neighbouring Tambo tenement, EPCA 1623.

Systematic and comprehensive exploration within EPCA 1623 is quite likely to disclose similar coal resources.

## **8.0 Exploration History – Petroleum and Stratigraphic Borehole Data**

### **8.1 Petroleum Data**

Relevant petroleum and stratigraphic wells are few and spread over an enormous area. These usually penetrate deep into the rock section and have significant datasets. Wells include those listed below:

#### GSQ Tambo 2

- Lies in the northern part of the farm-in area tenements. No significant coal was recorded.

#### Nive River 1

- Currently no records are available for this hole.

#### Valetta 1

- Coal was recorded in the Birkhead Formation.

#### GSQ Augathella 3

- Several thin coals at about 600m.

#### GSQ Augathella 7

- Currently unable to locate the data.

#### AOP Cunno 1

- The well was spudded updip of the tenements near the outcrop of the Hutton Sandstone and the Birkhead has been removed by erosion.

#### AOP Balfour 1

- Coal occurrences were recorded in the Birkhead Formation, with the thickest coal plies being approximately 3m at depths between 615 and 745m. An interval of coal 9 to 10m thick was found at 871-880m depth, supposedly within the Evergreen Formation. Lodestone has questioned the stratigraphic assignment in this hole.

#### GSQ Augathella 1

- Rare, thin coal seams up to a maximum of 0.45m thickness are recorded within the Birkhead Formation.

#### Donnybrook 1

- Includes about 10m of coal in the Walloon section.

#### Don Juan 1

- Includes about 15m of coal in the Walloon section.

BMR 49 and BMR 50, and GSQ Eddystone 49 and 50- Records for these holes are not included in the current version of the QPED database.

In the very few GSQ-drilled stratigraphic bores in the region, some coal has been reliably recorded and it is mostly thin. These were fully-cored holes (from surface), and provide high quality, reliable and accurate descriptions of the sections penetrated, and are also geophysically logged.

### **8.2 Resource potential of the Tambo Project Area Eromanga Basin sequence**

Traditionally, the Eromanga Basin has not been highly regarded as a coal province, and there has been almost no coal exploration conducted previously in the areas now applied for by Tambo.

To date, the entire area is almost totally unexplored.

No significant coal resources have yet been recorded from the project area, or from this part of the Eromanga Basin as a whole, which has been traditionally regarded as having low prospectivity for the discovery of commercial-scale coal resources.

Although there are some reliably documented occurrences of coal from bores drilled, there is, as yet, very little data which could reasonably be classified as high quality (such as Balfour 1) or reliable data from within the tenements to provide support for the existence of any significant coal that might be regarded as a possible future 'mining reserve' or gas reserve.

There is evidence that coal is present, spread over a relatively wide stratigraphic interval, from at least the Hooray Sandstone (re-picked by Lodestone to be within the Birkhead Formation) at the top of the sequence, to the Evergreen Formation.

Indications are that the Birkhead Formation probably provides the most prospective target interval.

Water bore records, although individually of limited reliability, are numerous and widespread, and there are a considerable number of records dating back for the past 100 years that mention an occurrence of coal, coaly shale, minor coal, coaly bands, etc. This at least provides confidence for the presence of suitable lithofacies needed to host substantial coal resources.

Significant resources of coal may be present within the Tambo Project area, though at best are expected to be of a similar nature to those resources known from the Surat Basin.

It remains conceivable that significant shallow (less than 200m depth) coal intervals may have gone unnoticed and unrecorded. This is even more possible at depths below 200m where there is less data.

At this early stage, there are too few holes spaced over too wide an area to draw any significant conclusions from the current well data.

There is an almost total lack of definitive data on which to accurately assess the likelihood for the occurrence of significant coal across the Tambo Coal EPC application areas.

For this reason and over the very large area involved, the chance of successfully outlining a viable commercial coal resource of a scale required to support a large-scale open cut mining operation is regarded as low. For the same reasons, the chance of successfully outlining a viable commercial gas resource of a scale required to support a gas market is regarded as low.

Notwithstanding, the Tambo project coal and gas tenement areas provide leverage to a vast area of the Eromanga Basin and western Surat Basin which is almost totally under-explored for coal, and which undoubtedly contain rock unit equivalents of the commercially productive Walloon Subgroup. There is a high frequency and broad spread of water well data from throughout the subject areas which, in typical Walloon style, make mention of mostly minor coal occurrences, and this lends some support to the possibility of typical Walloon coal deposits which might be present over relatively large areas.

## 9.0 Farm-out and Permit Purchases

There have been several deals revolving around the Gladstone Liquid Natural Gas (GLNG) plants and the Rangal (Fairview/Spring Gully) and Walloon coals lying to the east of the ATP1020P area that have included:

- AGL's \$37 million investment (exploration and appraisal) for a 50% stake of ATP 529P (Galilee Basin);
- 50% of Santos areas (including the Comet Ridge and Walloon Play) to Petronas for \$2,500 million;
- 50% of Origin areas (including the Comet Ridge and Walloon Play) to Conoco-Phillips for \$9,600 million;
- Queensland Gas Company Limited (QGC) purchase of Sydney Gas Limited (dominantly the Lacerta Field) for \$840 million;
- British Gas' purchase of QGC (Walloon Play) for \$5,000 million;
- BG's purchase of Pure Energy for \$670 million and
- Origin's purchase of ATP 788P (Walloon Basin) for \$660 million

Despite the economic down turn very significant prices are still being paid for CSG assets.

In June 2007 Cockatoo Coal Limited Purchased 3,000 km<sup>2</sup> of coal tenements from Metallic Minerals, which included potential coal prospects at Bymount (ECP 1017) and Injune (ECP 1018) for \$4.75 million in cash plus 25 million ASX-listed shares that were valued at \$11.75 million, giving a total value of \$16.5 million plus royalty and share options for future production.

## 10.0 General Description of Coal Seam Gas

(CSG) is a fossil fuel generated in three stages in the life of a sedimentary basin (Coal Mine Methane (CMM) is simply CSG extracted from a coal mine or mine affected coal):

1. Primary Biogenic – by the breakdown of organic matter contained in sediment:
2. Thermogenic – by the progressive expulsion of volatile matter from the coaly material by increasing temperature and pressure, during its increased depth of burial within the sedimentary basin: and
3. Secondary Biogenic – by the action of aerobic bacteria, following uplift and exposure of the seam and the inflow of meteoric water into the seam.

The gas contained in a coal seam can be thermogenic, biogenic, or typically a combination of thermogenic and secondary biogenic. The coal mining process creates a very fractured halo around the void which is much more effective than can be achieved in drill holes.

Gas in coal seams is stored in two main ways:

1. Adsorbed, or bonded, to the coal surfaces of micropores within the coal structure and held by molecular attraction; and
2. Trapped within cleats and fractures of the coal that would normally be occupied by water.

The first of these mechanisms is by far the most important in terms of the volume of gas that can be stored. The process of adsorption allows coal to hold large volumes of gas within its structure, perhaps as much as three times the amount of gas contained in the same gross rock volume (GRV) of a conventional sandstone reservoir.

The volume of gas that can potentially be stored by a particular coal increases asymptotically with depth of burial and increasing hydrostatic pressure.

The amount of gas trapped in fractures within the coal bed is typically not large. However, it may have the effect of displacing water as is believed to be the case at the Scotia and Peat Gas Fields

(Queensland, Australia), where the fields are located in anticlinal traps. This has a number of beneficial effects:

- The permeability to gas is higher;
- Water production and handling is greatly reduced; and
- There is some increase to the gas reserve.

Pressure exerted by the natural water column in the pore space of rocks extending down from the water table is called hydrostatic pressure. The combination of adsorption and hydrostatic pressure causes the gas to be trapped on the coal surfaces within the coal seams. Where the coal seam contains as much gas as it is capable of adsorbing (is fully saturated), the gas pressure is equal to the hydrostatic pressure, but if the coal is not fully saturated, the gas pressure is proportionally less and is known as the desorption pressure. To release adsorbed gas, the hydrostatic pressure must be lowered to and below the gas desorption pressure.

The rate of gas flow through a coal seam is governed by two factors:

1. Gas desorption from the coal micropore structure via a gas concentration gradient, observed as gas bleeding; and
2. Gas migration to the well bore through the fracture system via a pressure gradient, the ease of flow being measured in millidarcies (mD).

Production of CSG requires drilling into the coal seam and installing pumps to remove water and reduce the hydrostatic pressure (draw down) in the coal seam. The adsorbed gas then desorbs and is released within the well bore as the water is pumped off.

The length of the de-watering period and the rate at which gas will flow depends primarily on the permeability of the coal. Production wells in a CSG field are typically drilled in a pattern such that the areas of reduced hydrostatic pressure around each of the wells overlap and reinforce one another. This also reduces the ability of the water to recharge the coal seams.

If permeability within the coal is too high then it is difficult to draw down the reservoir pressure in the coal seam, as water will re-charge as quickly as it is pumped out. Eventually, the pumping will get ahead of the water re-charge. A higher pump rate may overcome the water re-charge, but this requires higher operational costs and the environmental impact of a much larger volume of water that requires disposal. High permeability and water re-charge is a major operational challenge facing operators developing the Jurassic Walloon Coal Measures in the Surat Basin (Queensland), as has also been the case in the development of the Powder River Basin in the USA.

- Ramp Gas
- Massive Water Volumes

Conversely, where permeability within the coal is too low, gas will not be able to flow at economic rates. Low to moderate permeability can be enhanced by the application of completion techniques which include:

- Hydraulically fracturing (fracking) the coal seam to cause a long fracture;
- Cavitating the coal seam to cause a cavity in the seam
- Under-reaming the coal seam to increase the diameter of the hole in the seam;
- Drilling a long high-angle/horizontal hole within the seam;
- Radial Drilling; and
- Roof/Floor Drilling

The choice of a particular technique depends heavily on many factors including the type of coal, its strength, and the degree of banding with non-coal rocks. Fracking works typically in competent seams and where stress properties are favourable, while cavitation is effective where the coal is friable. Both methods have historically been used to effect, particularly in some USA fields.

Under reaming is very effective where permeabilities are already high and the seams are heavily banded. This is being applied in coal seam gas fields within the Walloon Coal Measures, for example.

Long hole in-seam drilling is finding increased application where the seams are reasonably thick and continuous. This technique is also finding increased application in degassing seams ahead of underground mining, where the produced gas can be utilized at the mine site or in the local area. One advantage it has is that it can probably be effective in low permeability seams where other techniques are not. Drilling techniques are being continually refined to improve the performance and reduce the cost of the gas wells.

The depth of burial has a significant effect on coal permeability. As burial increases, the permeability of coal decreases as a result of increased rock weight (geostatic pressure) closing fractures and cleats. Generally, the floor for adequate permeability is about 1,000m and coal seams deeper than this are unlikely to flow gas at economic rates. However, in the Piceance Basin in the USA, there are examples of coals which produce gas at economic rates at depths greater than 1,000m.

Shallow coals have a low capacity to adsorb gas due to the low hydrostatic pressure and to the flushing effects of meteoric water. Most exploration is concentrated on coals that are deeper than 150m below the ground.

### **11.0 Comparison of Gas Contents with Existing Coal Seam Gas Producers**

The concentration of gas held in a particular coal seam is a product of a number of factors, the dominant ones being;

- Rank of the coal – gas concentrations increase with rank such that low rank (high volatile content) coals usually have low to very low concentrations, while high rank (low volatile content) coals can have high to very high concentrations;
- Depth of burial – higher confining pressures accompanying deeper burial allow for higher concentration, up to the maximum value for the coal; and
- Maceral composition of the coal – within the lower to medium rank coals high vitrinite and liptinite (bright coals) usually have higher gas concentrations than coals high in inertinite (dull coals).

Other factors such as geological structure, permeability, seam thickness and extent, gas composition, proximity to infrastructure and gas price can also be critical in making a coal deposit economic for coal bed methane production.

Within Australia and elsewhere, there are coal bed gas operations drawing gas from coals with a wide range of rank. Table 5 shows the average seam gas content, in cubic meters per tonne of coal, of some coal bed gas projects within the Bowen Basin and in the United States. It also shows that, while many have high gas contents, some with low rank coals (notably the Powder River Basin) and low to very low gas contents can be brought into production providing other factors, such as permeability, seam geometry and gas price are favourable.

**Table 5: Comparison of Some CSG Characteristics From Representative Fields.**

Basin	Bowen	Bowen	Bowen	Surat	San Juan	Black Warrior	Powder River
Field	Moranbah	Moura	Peat/Scotia	Walloon CM	Fruitland	Oak Grove	Prairie Dog Creek
Ro*	<1.1	1.0	0.55 - 0.71	0.4 - 0.5	0.5 - 1.5	1.2 - 1.4	0.28 - 0.45
Gas Content (daf)**	12	13	9	5.3	3 – 22	15	2 - 5
Permeability (mD)	1-10	1-10	10-100	10-1000	10-100	1-50	30-500

\*Ro is the mean maximum reflectance of vitrinite in oil, and is a sensitive measure of coal rank; the higher the value the higher the rank.

\*\*daf means dry ash free and is used here as a means of comparing gas contents between coals of different ash and moisture contents.

## 12.0 Water Disposal

Production of large volumes of water can be a significant operational challenge for CSG producers, due to the volume itself, the water chemistry and restrictions on water use.

A number of proven technologies are available and new methods are being explored.

Aside from volume, the main issues associated with the co-produced waters are salinity and chemistry, with high sodium content being one of the main concerns. The ratio of sodium to magnesium and calcium is called the sodium adsorption ratio (SAR). When too high in water used for irrigation it can eventually damage some soil profiles.

The following is a list of methods of disposal that have been used successfully in the US and are being employed or trialed in Australia:

- Surface discharge without treatment (tight water quality requirements);
- Surface supply for stock watering;
- Surface supply for irrigation;
- Aquaculture;
- Static evaporation;
- Spray evaporation;
- Reverse Osmosis/Ion Exchange treatment;
- Re-injection;
- Supply to utility; and
- Treat with gypsum, or other chemicals, to control SAR.

Each of these has its own problems and limitations, or is hampered by high cost. Large evaporation ponds are currently favoured, although some companies are trialling reverse osmosis combined with evaporation ponds and other chemical treatments in order to produce water that may then be used for irrigation.

Water disposal remains a significant challenge for large-scale production of CSG.

## 13.0 Methodology

MBA has been asked to express an opinion as to whether the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement are fair and reasonable for non-associated shareholders of Lodestone. The methodology that MBA has adopted in forming a view

that the farm-in agreements are fair and reasonable has involved an assessment by MBA of the following factors:

- (a) within the areas that are the subject of the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement, the low level of exploration that has been conducted in the past;
- (b) the geology of the tenement areas and the probability of commercial coal and coal seam gas resources being discovered;
- (c) the structure of the farm-in agreements, Lodestone's obligations to undertake exploration work and its rights of withdrawal;
- (d) Lodestone's rights to design the exploration program for the tenement areas;
- (e) the general terms of the farm-in agreements; and
- (f) previous farmout and permit purchases.

## **14.0 Conclusion**

MBA considers that the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement are fair and reasonable to the non-associated shareholders of Lodestone. MBA has formed this conclusion on the following basis:

- (a) the areas the subject of the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement cover a large geographical area of Queensland that has been subject to only limited exploration for coal and coal seam gas;
- (b) the geology of the tenement areas and adjacent areas suggests that the probability of Lodestone discovering commercial coal and coal seam gas resources is low, however there is a possibility of large coal resources, and very large coal seam gas resources, being present in the tenement areas;
- (c) in contrast to normal acquisition, under the farm-in agreements, Lodestone will not purchase an interest in the tenement areas upfront, but will progressively earn the right to be transferred (in 10% parcels) up to a 50% interest in the tenement areas through undertaking exploration activities and incurring exploration expenditure. Lodestone may withdraw from the agreements at any time, which means it can limit its financial commitment and exposure to the tenement areas and is not required to make an large up-front commitment of capital (in contrast to a typical acquisition);
- (d) Lodestone has a right to design the exploration program for the tenement areas to target those areas that it considers offer the best prospects for success;
- (e) the terms of the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement are broadly consistent with market practice; and
- (f) there have been a number of acquisitions of coal and coal seam gas resources to the east of the areas the subject of the Tambo Coal Project Farm-in Agreement and the Tambo Gas Project Farm-in Agreement, which indicate that interest in coal seam gas assets in the region, and the prices paid for such assets, remain high.

## **15.0 Statements**

### **15.1. MBA Payment**

MBA has received a fee of \$60,000, GST exclusive, for this opinion.

### **15.2. Declaration**

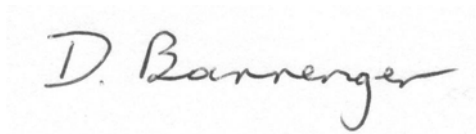
MBA Petroleum Consultants has not had and, at the date of this report, does not have any relationship with Lodestone, or its subsidiary companies. A fee will be received for the preparation of this report and this is not contingent on the outcome of the Report. No other benefit will be received by MBA. Neither Wal Muir nor Doug Barrenger has any pecuniary or other interest which could be regarded as capable of affecting their ability to provide an unbiased opinion.

### **15.3. Qualifications**

Douglas Barrenger

Doug Barrenger received a BSc degree (geology) from the Australian National University and a Graduate Diploma in Computing Science from the Queensland University of Technology. He has more than 25 years of experience in the petroleum industry and has undertaken all facets of geological work, from wellsite and operations geology to prospect evaluation, risk analysis, reserve assessment, basin analysis, portfolio valuation and project management for both operated permits and new-venture roles and for development and exploration projects. He has worked on all Australian petroleum basins, including coal seam gas, and has overseas experience in SE Asia and Italy as an employee and as a consultant and has written numerous Independent Expert Reports and acreage valuations. Doug is a founding partner of MBA Petroleum Consultants, a member of the Petroleum Exploration Society of Australia and a twenty-year, Active Member of the American Association of Petroleum Geologists (number 330431).

Yours sincerely

A handwritten signature in black ink that reads "D. Barrenger". The signature is written in a cursive style with a long horizontal stroke at the end.

Doug Barrenger  
Partner

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Tambo Coal Project Farm-in Agreement between Lodestone Energy Pty Ltd and Lodestone Exploration Limited (together, Lodestone) and Tambo Coal & Gas Pty Ltd.; and

Tambo Gas Project Farm-in Agreement between Lodestone CSG Pty Ltd and Lodestone Exploration Limited (together, Lodestone) and Tambo Coal & Gas Pty Ltd.

Tambo Coal and Gas Pty Limited, 27 April 2009: Clarification of matters relating to Tambo Gas Farm-in Agreement Dated 10 December 2008 – Letter

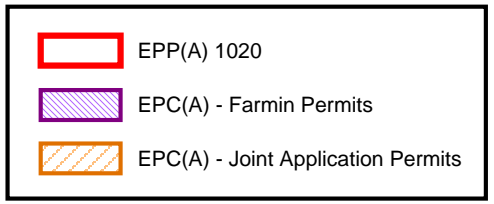
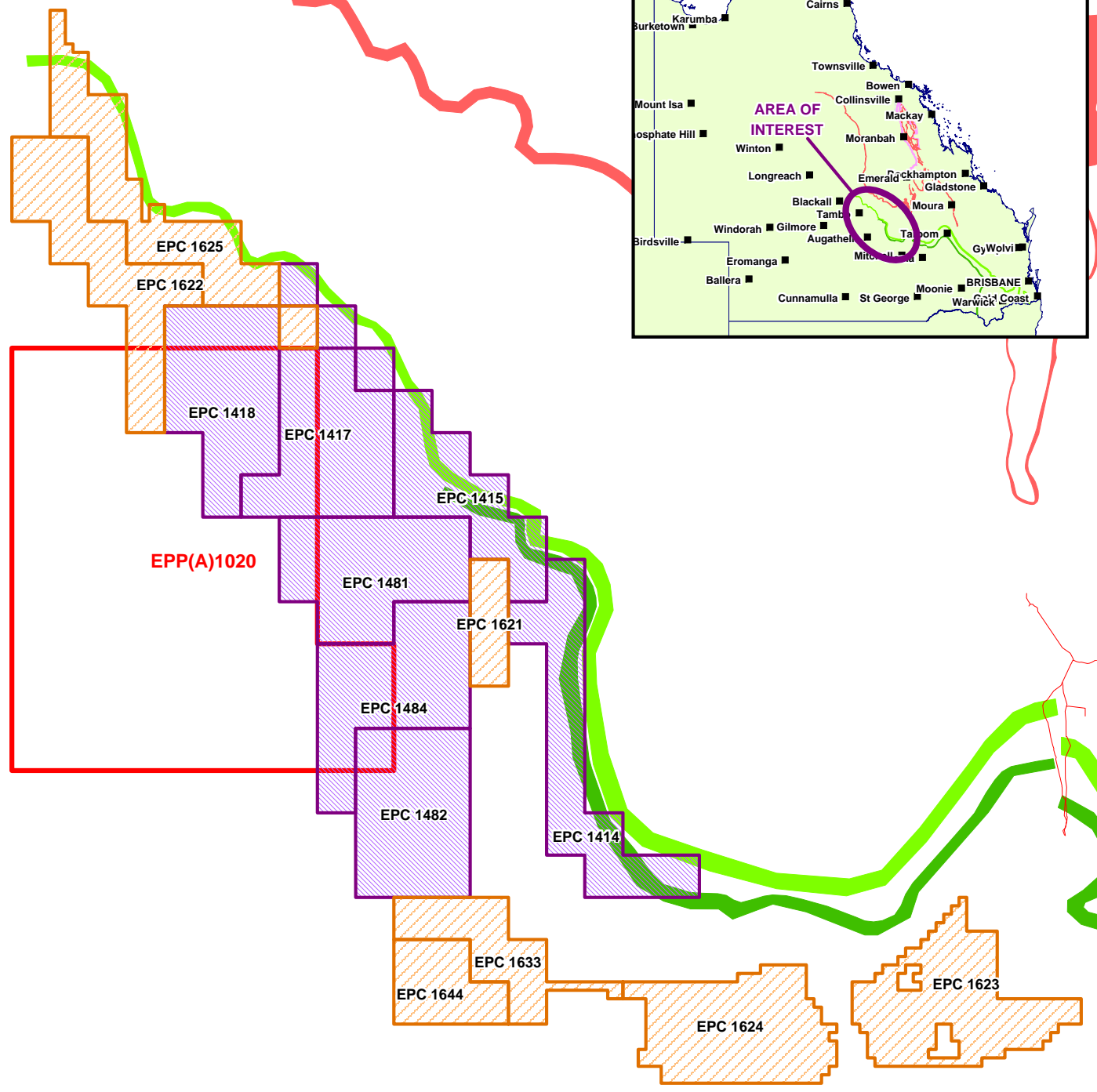
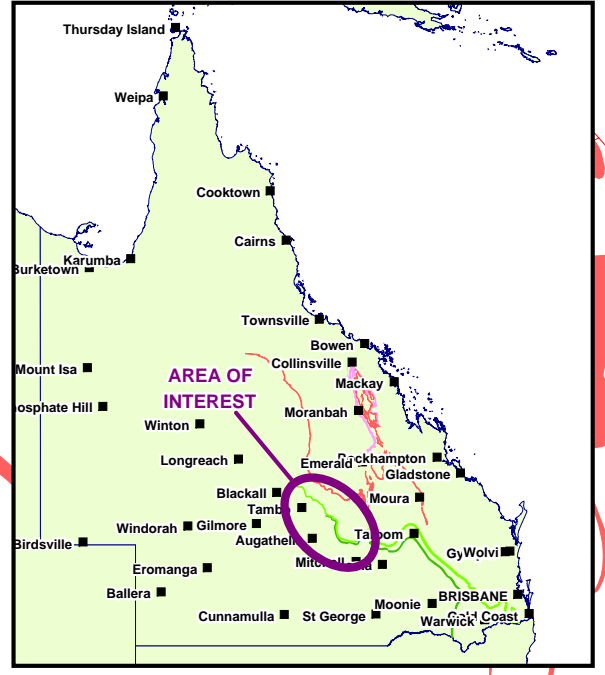
Tambo Coal and Gas Pty Limited, 27 April 2009: Clarification of matters relating to Tambo Coal Farm-in Agreement Dated 10 December 2008 – Letter

## 17.0 Technical Terms

2P Reserves	means the sum of proved reserves plus probable reserves, as defined by the Society of Petroleum Engineers.
Adsorption means	the attraction exerted by the surface of coal for a liquid or gas with which there is contact.
Areal Extensive	means occurring over a large area
Ash	means the inorganic residue after burning coal.
ATP	means Authority to Prospect
Basin	means a segment of the earth's crust that has down-warped and in which sediments have accumulated.
Bcf	means Billion cubic feet ( $10^9$ cubic feet).
Bituminous Coal	means coal that contains between 15% and 20% volatile matter.
CSG	means coal seam gas. This generally refers to non-mine-affected coal. There are some areas that may be pre-drained using surface-drilled holes, ahead of mining, and these can be classed as CSG. As mining approaches it can be expected that the effect of fracturing of the coal reservoir will 'felt' by the well. See CMM below.
Cleat	means a joint or system of joints along coal fractures.
CMM	means coal mine methane. It is extracted by drill holes within the mine draining gas immediately ahead of mining, as gas in the ventilation stream and extracted from goafs and from the voids after mine closure. It is established within the mine-affected area (the mining extraction process causes the surrounding rock, above and below, to fracture significantly). Fractures may extend up to 160m above and 70m below the mined area. The lateral extent is quite short.
CO <sub>2</sub>	means carbon dioxide.
Coal Rank	Is the thermal maturity of the coal. Usually expressed in terms of the maturation of the vitrinite maceral and symbolized as Ro or Vro. It is the mean of the maximum reflectance measurements made on the vitrinite under oil. The higher the value the higher the coal rank (thermal maturity).
Core	means a cylindrical piece of rock taken as a sample.
CSG	means Coal Seam Gas, also known as coal bed methane (CBM), or coal seam methane (CSM), or natural gas contained within coals.
DAF	means dry ash free. All coals contain ash and moisture. It can be useful to recalculate coal parameters such as gas content to an equivalent of clean coal, dry and ash free. The clean-coal parameters can be compared from seam to seam or even basin to basin.
Desorption	means the process of the loss of gas previously adsorbed on coal face.
Fracture	means any break in a rock caused by mechanical stress.
Gas-in-Place or GIP	means a technical estimate of potential gas volumes contained within a defined area. Gas in place or total gas includes all gas types, whether recoverable or not.
Goaf	The cavity behind the longwall is called the goaf, goff or gob. If this gas is not drained from the goaf area it has the potential to flow in significant quantities into the current working areas and cause a safety hazard.
GJ	means a Gigajoule ( $10^9$ joules).

Hydrostatic	means head pressure exerted by a fluid at rest.
Joule	is a unit of energy.
Km	is a Kilometre.
Km <sup>2</sup>	is a square kilometer.
Longwall mining	is a form of underground coal mining where a long wall (typically about 250-400 m long) of coal is mined in a single slice (typically 1-2 m thick). The longwall "panel" (the block of coal that is being mined) is typically 3-4 km long and 250-400 m wide.
Mcf	is a thousand cubic feet (10 <sup>3</sup> cubic feet).
mD	means a milli-Darcy (unit measurement of permeability).
mm	means to millimeters.
MMcf	means a million cubic feet (10 <sup>6</sup> cubic feet).
mmscf/d	means a million standard cubic feet (10 <sup>6</sup> cubic feet) per day.
moisture	means in coals, inherent water that makes up part of the coal.
MW or Megawatt	equals one million watts of power and is a unit for measuring electricity.
MWh	is a Megawatt hour.
psi	means pounds-per-square-inch and is an imperial unit of pressure.
Resource	A resource implies a potentially recoverable amount of gas.
Tcf	means Trillion cubic feet (10 <sup>12</sup> cubic feet).
ton	is an imperial unit used for weight measurements. A short ton (USA) is equivalent to 2000 pounds A long ton is equivalent of 2240 pounds.
tonne	is a metric unit used for weight measurements. It is equivalent to 1000 kilograms.
Ventilation	refers to in-mine ventilation of gasses that escape into the mine shafts. The build-up of methane should not normally exceed 2% of the air mix. This requires the ventilation through the mine shafts at an appropriate volume

# FIGURES



**LODESTONE**  
Location Map - Petroleum Permit and EPC Applications

Author: DB Date: 27-03-2009  
Drafted: JW Date: 27-03-2009

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FIGURE 01

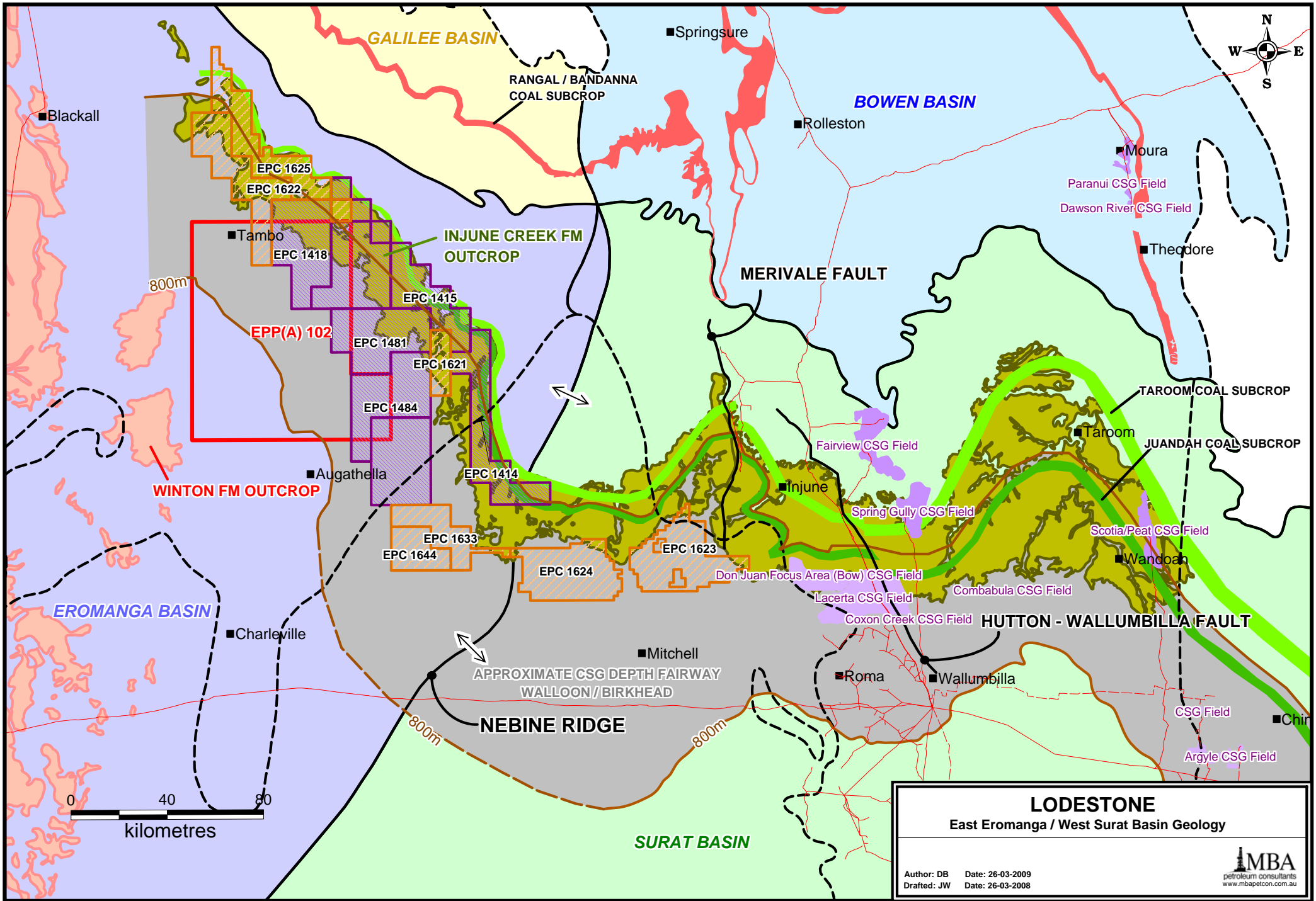
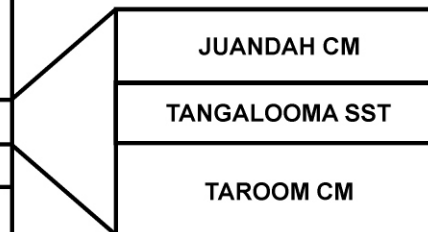
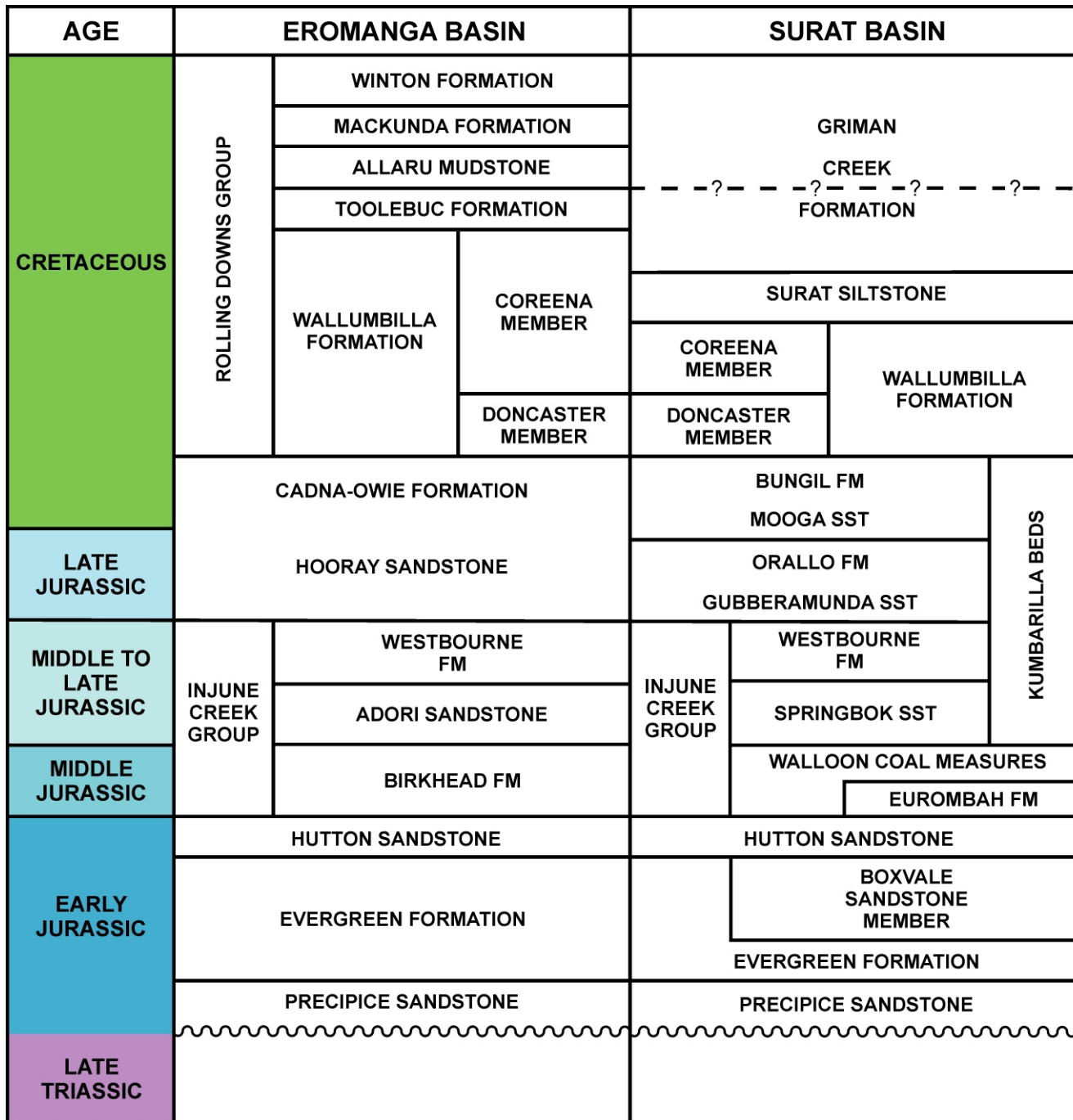


FIGURE 02

**LODESTONE**  
East Eromanga / West Surat Basin Geology

Author: DB Date: 26-03-2009  
Drafted: JW Date: 26-03-2008

  
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**LODESTONE**  
EROMANGA - SURAT STRATIGRAPHY

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Author: JW    Date: 27-03-2009  
Drafted: WR    Date: 27-03-2009

  
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FIGURE 3

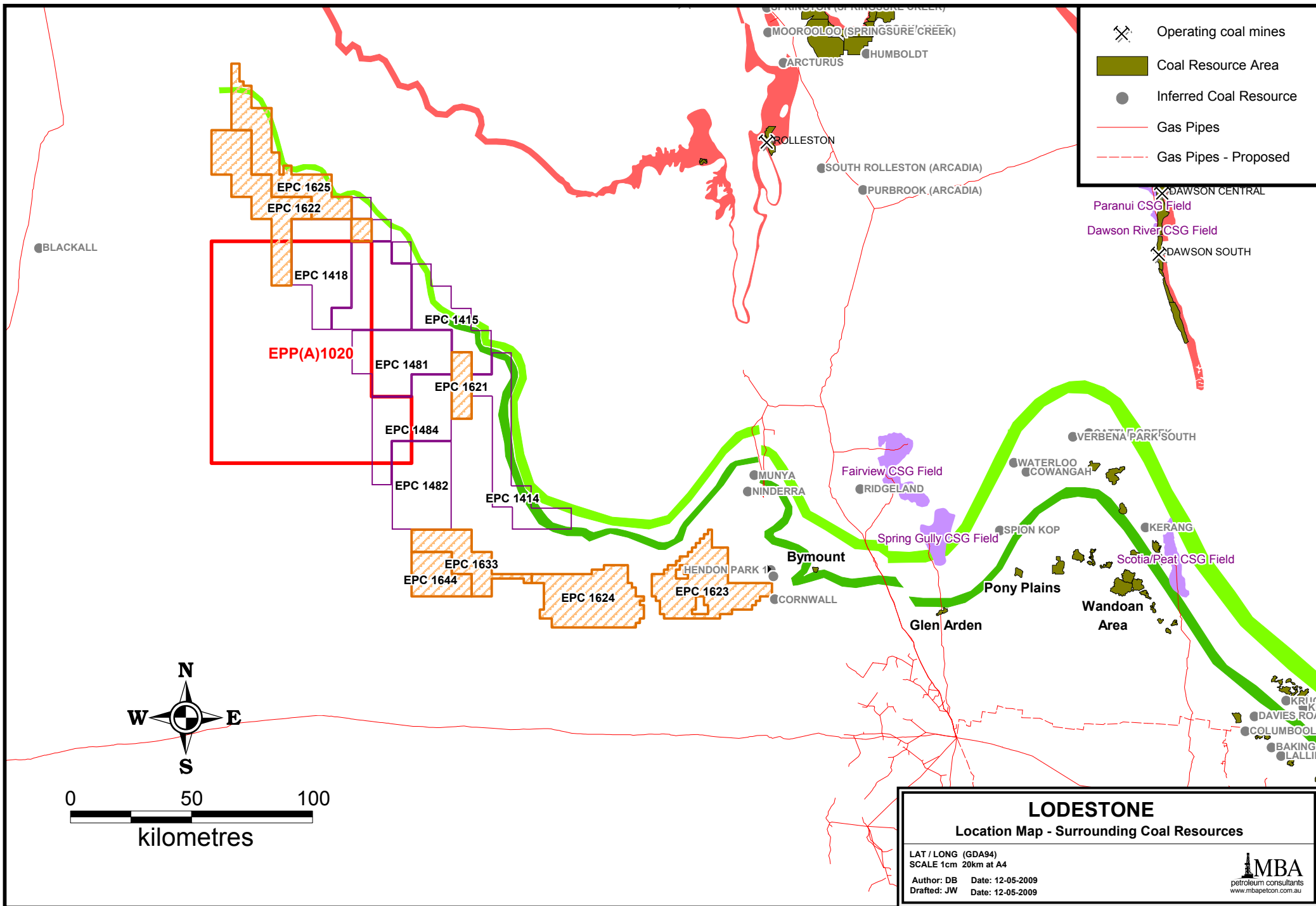


FIGURE 04



**Schedule 2**

**Terms of Placement Options**

## Conditions of Options

### Entitlement to Shares and Piggy-back Options

- 1 Subject to these Conditions, each Option confers on the Option Holder an entitlement to subscribe for and be issued:
  - (a) one Share, credited as fully paid, at the Exercise Price; and
  - (b) one Piggy-back Option.

### Exercise Price

- 2 The Exercise Price is A\$0.20 per Option.

### Exercise of Options by Option Holder

- 3 Subject to clause 10:
  - (a) Options may be exercised by the Option Holder at any time during the Exercise Period; and
  - (b) the Exercise Period commences on the date of issue of an Option and ends on the second anniversary of the date of issue of the Option.

### Lapse of Options

- 4 Subject to clause 10, Options not exercised during the Exercise Period automatically lapse.
- 5 On an Option lapsing, all rights of the Option Holder in respect of the Option cease and no consideration or compensation will be payable for or in relation to that lapse.

### Procedure for exercise of Options by Option Holder

- 6 Subject to these Conditions, Options may be exercised during the Exercise Period by the Option Holder:
  - (a) lodging with the Company a Notice of Exercise signed by the Option Holder; and
  - (b) paying to the Company the Exercise Price in respect of the Options exercised.

An exercise of Options will only be valid and effective once the Company has received, in cleared funds, the full amount of the Exercise Price payable.

- 7 Unless otherwise determined by the Board in its absolute discretion, a Notice of Exercise, once lodged with the Company, is irrevocable and by giving a Notice of Exercise the Option Holder:

- (a) agrees to subscribe for that number of Shares (and an equivalent number of Piggy-back Options) equivalent to the number of Options exercised in the Notice of Exercise;
  - (b) agrees to be bound by the constitution of the Company on the issue of Shares; and
  - (c) without limiting any other clause in these Conditions, must pay the Exercise Price in respect of the Options exercised within 14 days of lodging the Notice of Exercise with the Company.
- 8 Options must be exercised in minimum parcels of 10,000 Options but the Board may, in its absolute discretion, accept an exercise of Options that does not comply with this clause.
- 9 Subject to clause 10, the exercise of some Options only does not affect the Option Holder's right to exercise other Options at a later time.

#### **Accelerated Exercise Period**

- 10 If, at any time in the period commencing on the first anniversary of the date of issue of the Options, the Company's VWAP is equal to or exceeds A\$0.30 for more than 20 consecutive Trading Days (**Trading Condition**):
- (a) the Company must notify the Option Holder that the Trading Condition has been satisfied; and
  - (b) the Option Holder has a period of 14 days from the date the Company gives notice that the Trading Condition is satisfied (**Accelerated Exercise Period**) to validly exercise some or all of the unexercised Options held by the Option Holder.

All Options that are unexercised at the end of the Accelerated Exercise Period automatically lapse.

#### **Obligation of the Company on exercise of Option**

- 11 Subject to these Conditions, on exercise of an Option the Company must issue to the Option Holder:
- (a) one Share, credited as fully paid; and
  - (b) one Piggy-Back Option,
- and, within 10 Business Days (or such other period as is required by the Listing Rules) after the date of exercise of the Option, issue (or cause to be issued) to the Option Holder a holding statement or other appropriate evidence of title for each Share and Piggy-back Option that is issued.
- 12 If the Option Holder exercises only some of the Options held by the Option Holder the Company must issue (or cause to be issued) a holding statement or other appropriate evidence of title for each remaining Option held by the Option Holder.

#### **Quotation of Options and Shares**

- 13 Options and Piggy-back Options will not be quoted on ASX.

- 14 The Company will apply for the quotation by ASX of Shares issued upon exercise of Options within the time period required by the Listing Rules.

### **Rights attaching to Shares**

- 15 Shares issued on the exercise of Options will rank equally in all respects with all existing Shares on and from the date of issue.

### **Rights attaching to Options**

- 16 Options do not confer on the Option Holder:
- (a) any entitlement to attend or vote at meetings of the Company;
  - (b) any entitlement to share in dividends declared or paid by the Company; or
  - (c) the right to participate in any new issues of securities by the Company.
- 17 The Option Holder will be given at least seven Business Days' notice (or such other period of notice as is required by the Listing Rules) of the record date (as defined in the Listing Rules) of a new issue of securities by the Company to enable the Option Holder to exercise any Options then capable of exercise and participate in the issue.
- 18 In the event of a Pro-rata Issue (other than a Bonus Issue) to the holders of Shares, the Exercise Price of Options will be amended to take into account the effect of the Pro-rata Issue as set out in the Listing Rules. Other than as provided by this clause and clause 18, Options do not confer on the Option Holder the right to a change in the Exercise Price or a change in the number of Shares over which Options can be exercised.
- 19 In the event of any reorganisation of the issued capital of the Company (including, without limitation, a consolidation, sub-division, reduction or return of capital), the rights of the Option Holder will be amended to the extent necessary to comply with the Listing Rules applying to a reorganisation of capital at the time of the reorganisation.

### **Transfer of Options**

- 20 Options are transferrable in accordance with the Corporations Act and the Company's constitution.

### **Purpose of issue of Shares on exercise of Options**

- 21 Any Shares issued to the Option Holder on exercise of Options are not offered or issued by the Company for the purpose of the Option Holder selling or transferring them, or granting, issuing or transferring any interest in, or granting options over.

### **Interpretation and compliance with law**

- 22 These Conditions will be interpreted and applied in a manner that is consistent with the Listing Rules. If any of these Conditions are inconsistent

with the requirements of the Listing Rules, they may be amended by the Company to comply with the Listing Rules. The Company must advise the Option Holder of any such amendments.

- 23 Notwithstanding any other clause of these Conditions, an Option may not be exercised, and the Company must not issue Shares on exercise of an Option, if to do so:
- (a) would contravene the Corporations Act or the Listing Rules because any necessary shareholder or regulatory approval of the issue of the Shares has not been given; or
  - (b) would contravene the local laws of, or the rules or requirements of any regulatory or statutory body in, an Option Holder's country of residence or in the opinion of the Board compliance with those local laws, rules or requirements would be impractical or result in any unnecessary or unreasonable burden on or expense for the Company in the circumstances.

The Company must use its best endeavours to obtain any shareholder or regulatory approval referred to in paragraph (a) of this clause.

## Notices

- 24 In these Conditions a notice (including a Notice of Exercise) will be deemed to have been duly given:
- (a) where delivered, on the date of delivery or, if delivery is not effected within a Business Day, at the commencement of the next Business Day;
  - (b) where sent by prepaid post, two Business Days after posting;
  - (c) where sent by facsimile, upon successful transmission, provided that if the facsimile is not received during a Business Day, it will be deemed to be received at the commencement of the next Business Day; and
  - (d) where sent by electronic mail, when the sender's computer indicates that the message has been received and that it has not bounced.
- 25 The address for notices to the Company is:
- (a) postal address: c/- Stanley Yeates & Associates, GPO Box 363, Brisbane QLD 4001;
  - (b) street address: c/- Stanley Yeates & Associates, Level 1, 101 Edward Street, Brisbane QLD 4000;
  - (c) facsimile: (07) 3221 6625; or
  - (d) electronic mail: [leni.stanley@sya.com.au](mailto:leni.stanley@sya.com.au),

or as otherwise notified by the Company. Notices should be addressed to the Company Secretary.

The address for notices to the Option Holder is to the Option Holder's registered address or to a facsimile number notified to the Company by the Option Holder.

## Definitions

26 In these Conditions:

**ASX** means ASX Limited.

**Board** means the board of directors of the Company from time to time.

**Bonus Issue** has the meaning given in the Listing Rules.

**Business Day** has the meaning given in the Listing Rules.

**Company** means Lodestone Exploration Limited ACN 075 877 075.

**Conditions** means the terms and conditions of the Options set out in this document.

**Corporations Act** means the *Corporations Act 2001* (Cth).

**Exercise Period** means the period specified in clause 3(b).

**Exercise Price** means the amount payable by the holder of an Option on the exercise of the Option, as set out in clause 2.

**Listing Rules** means the official listing rules of ASX.

**Notice of Exercise** means, as the case requires, a duly completed and executed notice of exercise of an Option or Piggy-back Option by the Option Holder in such form (if any) as required by the Board from time to time.

**Option** means an option to subscribe for a Share on the terms set out in these Conditions.

**Option Holder** means a person who is the valid holder of an Option.

**Piggy-back Option** means an option to subscribe for Shares on the terms set out in the Schedule.

**Pro-rata Issue** has the meaning given in the Listing Rules.

**Security Interest** means a mortgage, charge, pledge, lien or other encumbrance of any nature.

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

**Trading Day** has the meaning given in the Listing Rules.

**VWAP** means the daily volume weighted average market price of all Shares on ASX's trading platform but excluding all off-market trades and any other trades that the Board determines to exclude on the basis that the trades are not fairly reflective of supply and demand.

**Schedule 3**

**Terms of Piggy-back Options**

# Schedule: Conditions of Piggy-back Options

## Entitlement to Shares

- 1 Subject to these Conditions, each Piggy-back Option confers on the Option Holder an entitlement to subscribe for and be issued one Share, credited as fully paid, at the Exercise Price.

## Exercise Price

- 2 The Exercise Price is A\$0.50 per Piggy-back Option.

## Exercise Period

- 3 Subject to clause 11, the Exercise Period for a Piggy-back Option:
  - (a) commences on the date the Company issues the Piggy-back Option; and
  - (b) ends on:
    - (i) if the second anniversary of the date of issue of the Piggy-back Option is either 30 June or 31 December, on that day; or
    - (ii) in all other cases, on the next to occur of 30 June or 31 December following the day that is the second anniversary of the date of issue of the Piggy-back Option.

## Exercise of Piggy-back Options by Option Holder

- 4 Subject to clause 11 Piggy-back Options may be exercised by the Option Holder at any time during the Exercise Period.

## Lapse of Piggy-back Options

- 5 Subject to clause 11, Piggy-back Options not exercised during the Exercise Period automatically lapse.
- 6 On a Piggy-back Option lapsing, all rights of the Option Holder in respect of the Piggy-back Option cease and no consideration or compensation will be payable for or in relation to that lapse.

## Procedure for exercise of Piggy-back Options by Option Holder

- 7 Subject to these Conditions, Piggy-back Options may be exercised during the Exercise Period by the Option Holder:
  - (a) lodging with the Company a Notice of Exercise signed by the Option Holder;
  - (b) paying to the Company the Exercise Price in respect of the Piggy-back Options exercised; and

- (c) providing written confirmation that the Option Holder is a person to whom an offer of Shares can be made without disclosure under Chapter 6D of the Corporations Act.

An exercise of Piggy-back Options will only be valid and effective once the Company has received:

- (d) the full amount of the Exercise Price payable in cleared funds; and
- (e) such documents or other evidence that it reasonably requires to be satisfied that the Option Holder is a person to whom an offer of Shares can be made without disclosure under Chapter 6D of the Corporations Act.

- 8 Unless otherwise determined by the Board in its absolute discretion, a Notice of Exercise, once lodged with the Company, is irrevocable and by giving a Notice of Exercise the Option Holder:
- (a) agrees to subscribe for that number of Shares equivalent to the number of Piggy-back Options exercised in the Notice of Exercise;
  - (b) agrees to be bound by the constitution of the Company on the issue of Shares; and
  - (c) without limiting any other clause in these Conditions, must pay the Exercise Price in respect of the Piggy-back Options exercised within 14 days of lodging the Notice of Exercise with the Company.
- 9 Piggy-back Options must be exercised in minimum parcels of 10,000 Piggy-back Options but the Board may, in its absolute discretion, accept an exercise of Piggy-back Options that does not comply with this clause.
- 10 Subject to clause 11, the exercise of some Piggy-back Options only does not affect the Option Holder's right to exercise other Piggy-back Options at a later time.

#### **Accelerated Exercise Period**

- 11 If, at any time in the period commencing on the first anniversary of the date of issue of a Piggy-back Option, the Company's VWAP is equal to or exceeds A\$0.70 for more than 20 consecutive Trading Days (**Trading Condition**):
- (a) the Company must notify the Option Holder that the Trading Condition has been satisfied; and
  - (b) the Option Holder has a period of 14 days from the date the Company gives notice that the Trading Condition is satisfied (**Accelerated Exercise Period**) to exercise that Piggy-back Option. If the Piggy-back Option remains unexercised at the end of the Accelerated Exercise Period it automatically lapses.

#### **Obligation of the Company on exercise of Piggy-back Option**

- 12 Subject to these Conditions, on exercise of a Piggy-back Option the Company must issue to the Option Holder one Share, credited as fully paid

and, within 10 Business Days (or such other period as is required by the Listing Rules) after the date of exercise of the Piggy-back Option, issue (or cause to be issued) to the Option Holder a holding statement or other appropriate evidence of title for each Share that is issued.

- 13 If the Option Holder exercises only some of the Piggy-back Options held by the Option Holder the Company must issue (or cause to be issued) a holding statement or other appropriate evidence of title for each remaining Piggy-back Option held by the Option Holder.

#### **Quotation of Piggy-back Options and Shares**

- 14 Piggy-back Options will not be quoted on ASX.
- 15 The Company will apply for the quotation by ASX of Shares issued upon exercise of Piggy-back Options within the time period required by the Listing Rules.

#### **Rights attaching to Shares**

- 16 Shares issued on the exercise of Piggy-back Options will rank equally in all respects with all existing Shares on and from the date of issue.

#### **Rights attaching to Piggy-back Options**

- 17 Piggy-back Options do not confer on the Option Holder:
- (a) any entitlement to attend or vote at meetings of the Company;
  - (b) any entitlement to share in dividends declared or paid by the Company; or
  - (c) the right to participate in any new issues of securities by the Company.
- 18 The Option Holder will be given at least seven Business Days' notice (or such other period of notice as is required by the Listing Rules) of the record date (as defined in the Listing Rules) of a new issue of securities by the Company to enable the Option Holder to exercise any Piggy-back Options then capable of exercise and participate in the issue.
- 19 In the event of a Pro-rata Issue (other than a Bonus Issue) to the holders of Shares, the Exercise Price of Piggy-back Options will be amended to take into account the effect of the Pro-rata Issue as set out in the Listing Rules. Other than as provided by this clause and clause 20, Piggy-back Options do not confer on the Option Holder the right to a change in the Exercise Price or a change in the number of Shares over which Piggy-back Options can be exercised.
- 20 In the event of any reorganisation of the issued capital of the Company (including, without limitation, a consolidation, sub-division, reduction or return of capital), the rights of the Option Holder will be amended to the extent necessary to comply with the Listing Rules applying to a reorganisation of capital at the time of the reorganisation.

### **Transfer of Piggy-back Options**

- 21 Piggy-back Options are transferrable in accordance with the Corporations Act and the Company's constitution.

### **Purpose of issue of Shares on exercise of Piggy-back Options**

- 22 Any Shares issued to the Option Holder on exercise of Piggy-back Options are not offered or issued by the Company for the purpose of the Option Holder selling or transferring them, or granting, issuing or transferring any interest in, or granting options over them.

### **Interpretation and compliance with law**

- 23 These Conditions will be interpreted and applied in a manner that is consistent with the Listing Rules. If any of these Conditions are inconsistent with the requirements of the Listing Rules, they may be amended by the Company to comply with the Listing Rules. The Company must advise the Option Holder of any such amendments.
- 24 Notwithstanding any other clause of these Conditions, an Option may not be exercised, and the Company must not issue Shares on exercise of an Option, if to do so:
- (a) would contravene the Corporations Act or the Listing Rules because any necessary shareholder or regulatory approval of the issue of the Shares has not been given; or
  - (b) would contravene the local laws of, or the rules or requirements of any regulatory or statutory body in, an Option Holder's country of residence or in the opinion of the Board compliance with those local laws, rules or requirements would be impractical or result in any unnecessary or unreasonable burden on or expense for the Company in the circumstances.

The Company must use its best endeavours to obtain any shareholder or regulatory approval referred to in paragraph (a) of this clause.

### **Notices**

- 25 In these Conditions a notice (including a Notice of Exercise) will be deemed to have been duly given:
- (a) where delivered, on the date of delivery or, if delivery is not effected within a Business Day, at the commencement of the next Business Day;
  - (b) where sent by prepaid post, two Business Days after posting;
  - (c) where sent by facsimile, upon successful transmission, provided that if the facsimile is not received during a Business Day, it will be deemed to be received at the commencement of the next Business Day; and

- (d) where sent by electronic mail, when the sender's computer indicates that the message has been received and that it has not bounced.

26 The address for notices to the Company is:

- (a) postal address: c/- Stanley Yeates & Associates, GPO Box 363, Brisbane QLD 4001;
- (b) street address: c/- Stanley Yeates & Associates, Level 1, 101 Edward Street, Brisbane QLD 4000;
- (c) facsimile: (07) 3221 6625; or
- (d) electronic mail: [leni.stanley@sya.com.au](mailto:leni.stanley@sya.com.au),

or as otherwise notified by the Company. Notices should be addressed to the Company Secretary.

The address for notices to the Option Holder is to the Option Holder's registered address or to a facsimile number notified to the Company by the Option Holder.

## Definitions

27 Terms defined in the Option Conditions have the same meaning in these Conditions, except that:

**Conditions** means the terms and conditions set out in this document.

**Exercise Period** means the period specified in clause 3 of these Conditions.

**Exercise Price** means the amount payable by the holder of a Piggy-back Option on the exercise of the Piggy-back Option, as set out in clause 2.

**Option Holder** means a person who is the valid holder of a Piggy-back Option.

**Option** means an option to subscribe for Shares and Piggy-back Options.

**Option Conditions** means the terms and conditions of the Options.

**Piggy-back Option** means an option to subscribe for a Share on the terms set out in these Conditions.