

TERMS OF ISSUE OF CONVERTIBLE NOTES

1 Definitions and Interpretation

In these Terms unless the context or subject matter otherwise indicates or requires:

- (a) **Company** means Incremental Oil and Gas Ltd ABN 66 138 145 114;
- (b) **Conversion Price** means the amount equal to \$0.20 per Share.
- (c) **Corporations Act** means the *Corporations Act 2001* (Cth).
- (d) **Maturity Date** means 2 July 2011;
- (e) **Noteholder** means in relation to any of the Notes at any time, the person registered as the holder of those Notes;
- (f) **Notes** means the secured convertible Notes issued by the Company, convertible into Shares, subject to these conditions
- (g) **Share** means an ordinary fully paid share in the Company;
- (h) **Terms** means these terms of issue of Notes; and
- (i) the singular includes the plural, a reference to any gender includes the other genders, a reference to a person includes a body corporate, and vice versa respectively.

2 Qualifications

- (a) In order to qualify to be a Noteholder, a person must satisfy the requirements of section 708(8) of the Corporations Act (*Sophisticated investors*).
- (b) The Noteholder may not sell, transfer or otherwise assign any Note or any Share issued on conversion of the Notes for a period of one year after the date of issue of the Notes, except to a person who has complied with clause 2(a).

3 Redemption by the Company

- (a) At any time prior to the Conversion Date, the Company may redeem the Notes for the face value of the Note .
- (b) The Company must give Noteholders not less than 30 days prior written notice of its intention to redeem the Notes.
- (c) A notice given under clause 3(b) is irrevocable.
- (d) After receiving notice under clause 3(b), any Noteholder or Noteholders may elect by notice in writing to convert their Notes into Shares instead of the Company redeeming those Notes under clause 3(a).
- (e) A notice given under clause 3(d) is irrevocable.
- (f) Unless redeemed or converted earlier in accordance with this deed, the Company shall convert all of the Notes on the Maturity date.

- (g) Any Noteholder or Noteholders may elect by notice in writing given not less than 7 days prior to the Maturity Date to redeem their Notes on the Maturity date instead of the Company converting those Notes into Shares under clause 3(f).
- (h) All payments made by the Company under this deed (whether in redeeming Notes or paying interest) must be in immediately available funds.

4 Redemption by Noteholder

Notwithstanding anything contained above, Noteholders will be entitled at any time by giving notice in writing to the Company at its registered office, to require the Company to redeem a Note for its total issue price immediately upon demand in the event that:

- (a) any order is made, an effective resolution is passed or a petition is presented for the winding-up of the Company;
- (b) a receiver is appointed or an encumbrancer takes possession of any property or undertaking of the Company;
- (c) the Company enters into any arrangement or composition with its creditors or proposes to do so;
- (d) a resolution is passed pursuant to section 436A of the Corporations Law for the purpose of placing the Company under external administration; or
- (e) the Company becomes insolvent or is deemed to be insolvent pursuant to section 459C of the Corporations Law.

5 Conversion

- (a) Any Noteholder or Noteholders may elect to convert their Notes into Shares at any time prior to the Maturity Date or the relevant Notes being redeemed otherwise.
- (b) Upon conversion under clause 3(d), 3(g) or 5(a), each Noteholder is deemed to authorise the Company to register it as the holder of Shares and to be bound by the constitution of the Company.
- (c) Notes may only be converted in whole;

6 Interest

Notes shall bear interest of 10% per annum, a compounded monthly, on their face value payable by the Company on the Conversion Date or upon redemption.

7 Shares to rank equally

Each Share issued upon conversion of the Notes will, as from the Conversion Date, rank in all respects pari passu with the then issued Shares of the Company.

8 Issues of New Shares

Where the Company determines that new shares in the Company are to be offered for cash subscription to the shareholders of the Company, the Noteholder will be entitled to participate in that offer in the same manner in all respects as if the date of the offer was the Conversion Date of the Notes and the Noteholder held the Shares that it would hold upon its Notes being converted into Shares. Any cash or other entitlements accruing to holders of Shares in respect of fractions shall be disregarded.

9 Capital Reconstruction

9.1 Effect of Reconstruction

If a reconstruction (including consolidation, subdivision, reduction or return) of the issued capital of the Company occurs, the basis for conversion of the Notes will be reconstructed in the same proportion as the issued capital of the Company is reconstructed and in a manner which will not result in any additional benefits being conferred on the Noteholder which are not conferred on the shareholders of the Company (subject to the same provisions with respect to rounding of entitlements as sanctioned by the meeting of shareholders approving the reconstruction) but in all other respects the terms for conversion of the Notes will remain unchanged.

9.2 Compliance with Income Tax Assessment Act

If the application of the provisions of clause 9.1 would have the effect that the terms of the Notes would not comply with the provisions of section 82SA(1) of the Income Tax Assessment Act 1936, and if, immediately prior to the capital reconstruction, the terms of the Notes did comply with the provisions of section 82SA(1) of the Income Tax Assessment Act, then the basis of conversion will not be reconstructed under clause 9.1.

10 Allotment of Shares

- (a) Where the Notes are converted to Shares, the Company will allot the Shares to the Noteholder, on the Conversion Date.
- (b) The Company will, after allotment, send to the Noteholder certificates for the number of Shares issued on conversion of the Convertible Note.

11 Security

- (a) The Notes will be secured by first ranking security over all of the issued capital of Incremental Oil and Gas LLC.
- (b) The security shall be held in a security trust for the benefit of the Noteholders.
- (c) The Company shall not grant any other security in respect of its shares in Incremental Oil and Gas LLC.

12 Governing Law

The governing law of these Terms is that of Western Australia.