



North  
Australian  
Diamonds  
Limited  
ABN 86 009 153 119

ASX Announcement  
31<sup>st</sup> October 2005

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## Quarterly Activities Report for 3 months ended 30 September 2005

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### Exploration Highlights

#### MERLIN, Northern Territory

- ◆ In excess of 5,000 carats of diamonds recovered from the sorthouse tailings to date.
- ◆ Largest diamonds recovered being 14.21ct and 10.27ct.
- ◆ Yellow diamonds represent 5% of the tailings diamond population.
- ◆ Largest yellow diamond is 3.16ct good quality gem
- ◆ A High Pressure Grinding Roll crusher is currently undertaking test work on both at surface reject ore stockpiles and primary kimberlite ore.
- ◆ Dewatering of pits is continuing with a view to taking additional test samples of primary kimberlite.
- ◆ NADL's Kimberley based DMS plant has been disassembled and relocation of the plant to Merlin has commenced.
- ◆ Exploration at Merlin is focussed on the follow-up of alluvial diamonds in streams to the south of Merlin.

#### NORTH KING GEORGE JV, Western Australia

- ◆ Results received from sampling of 10 priority gravity targets with 4 samples reporting positive for diamonds and 5 samples reporting positive for indicator minerals.

#### KIMBERLEY REGIONAL EXPLORATION, Western Australian

- ◆ Narrie tenement granted allowing follow-up sampling program to commence.

### Corporate Highlights

- ◆ On 30 September 2005 the company completed a share placement of 133,158,188 ordinary fully paid shares at a price of 2.8 cents each to raise \$3.72 million. The placement was made to Montagu and Baker Young Stockbrokers and sophisticated investors.
- ◆ During the quarter the company advised that the company's change of name and status approved by shareholders at a meeting held on 27 June 2005 had been registered by the Australian Securities and Investment Commission.
- ◆ On 19 August 2005 the company announced the placement of 20,598,000 ordinary fully paid shares at a price of 3 cents each and that an agreement in principle had been reached with Knightsbridge Corporate for the advanced sale of \$500,000 of rough diamonds from the Merlin diamond operation.
- ◆ The Company is continuing in its executive search for a new Chief Executive Officer.

## MERLIN MINING LEASE & ASSOCIATED EXPLORATION TENEMENTS

### Merlin Diamond Mine – MLN 1154

Processing of the Merlin x-ray sorthouse tailings is continuing, being the first step in a staged approach to evaluate and redevelop the Merlin diamond mine which ceased open pit production in 2003. The Merlin Mining Lease contains 11 of the 13 known kimberlite pipes in the Merlin field (of which 9 were subject to open-pit operations by previous holders), producing approximately 500,000 carats of diamonds at an average value of US\$108 per carat. Two pipes with potential economic ore grades remain to be evaluated. In line with world increases in diamond prices a recent revaluation of Merlin goods indicates a 30% increase in price to approximately US\$140 per carat. The Company completed the acquisition of the lease from Argyle Diamond Mines in late 2004.

### Inferred and Indicated Resources

The combined **Indicated** and **Inferred Resources** being **19.1Mt** at a grade of **17.3cpht** for a total of **3.3Mcts**. **Over 50% of the total resource is in the Indicated category.**

	<b>Indicated</b>	<b>Inferred</b>	<b>Total</b>		
<b>Southern Cluster</b>					
PalSac	4,015,000t	2,713,000t	6,728,000t	@ 20cpht	
Launfal	730,000t	510,000t	1,240,000t	@ 22cpht	
Excalibur	464,000t	309,000t	773,000t	@ 34cpht	
Tristam		410,000t	410,000t	@ 18cpht	
			<b>9,151,000t</b>	<b>@ 21.4cpht</b>	<b>(1,955,000cts)</b>
<b>Central Cluster</b>					
Gawain	868,000t	1,252,000t	2,120,000t	@ 30cpht	
Ywain	68,000t	105,000t	173,000t	@ 60cpht	
			<b>2,293,000t</b>	<b>@ 32.3cpht</b>	<b>(740,000cts)</b>
<b>Northern Cluster</b>					
Gareth	125,000t	143,000t	268,000t	@ 22cpht	
Kaye	1,498,000t	1,335,000t	2,833,000t	@ 9cpht	
Ector	2,357,000t	2,221,000t	4,578,000t	@ 7cpht	
			<b>7,679,000t</b>	<b>@ 8.3cpht</b>	<b>(634,000cts)</b>
<b>Total</b>	<b>19.1Mt</b>	<b>17.3cpht average</b>		<b>3.3 million carats</b>	

*Inferred and indicated resource grades are based on a bottom screen size of 1.2mm*

### Processing of Sorthouse Tailings

The x-ray sorted tails (sorthouse rejects) were deposited in Ywain pit on cessation of previous mining operations. This pit has been dewatered and some 5,000 tonnes of these tailings have been excavated and transported to the processing plant site where processing is continuing. In addition there is a portion of the tailings that is too heavily contaminated with country rock to be able to be treated by the screening plant in its current configuration. This contaminated material has been stockpiled for processing at a later date. Processing hours have been extended with a view to completing the processing of the majority of the tailings by year end. To date, a total of 1,200 tonnes have been processed.

### Diamond Recovery

Diamond recoveries now exceed 5,000cts, with some 5% of the diamonds being yellow. The grade of the tailings is in excess of 5 carats per tonne inline with initial projections. The diamond recoveries lag behind the processing of the tailings. The largest diamond recovered to date is a clear white 14.21ct gem quality stone. A second large near gem quality stone has also been recovered this being 10.27ct. These large diamonds are a characteristic of the Merlin diamond field. The largest yellow diamond is gem quality and 3.16ct. These yellow diamonds are non-fluorescing and were not previously recovered in large numbers from the Merlin 'Run-of-Mine' production. Details of the recoveries are as follows;

<b>Carats Recovered</b>				<b>Diamonds Recovered</b>			
-25+10mm	-10+4mm	-4+1mm	<b>Total</b>	-25+10mm	-10+4mm	-4+1mm	<b>Total</b>
14.21	517	4,641	<b>5,172.21</b>	1	1,174	62,489	<b>63,664</b>

Now that recoveries have exceeded 5,000cts a parcel is being cleaned and prepared for valuation.



*Photo 1: Selection of cleaned Merlin diamonds*

### **Test Work**

A primary jaw crusher is working in conjunction with a High Pressure Grinding Roll crusher to crush samples taken from the at surface ore stockpiles remaining from previous mining operations. These stockpiles include cyclone floats, trommel rejects and 'Run of Mine' oversize. These samples will be processed through the onsite DMS plant for diamond recovery over the coming weeks. This testwork is aimed at identifying procedures for the improved liberation of diamonds from the kimberlite during processing, which the Company believes contributed to reduced overall diamond recoveries. These liberation related losses appear to be a consequence of the increased competency of the kimberlite with depth. In addition, the work will provide information on recoverable grade which will enable much of this surface material to be incorporated into the Inferred Resource category as well as processing requirements.

Dewatering of selected pits is continuing with a view to obtaining samples of primary kimberlite to be used for processing and diamond liberation and recovery testwork. Ywain pit has been dewatered, Kaye is underway and dewatering of Gawain pit is to commence shortly. This work will continue into the new year.

### **Relocation of Kimberley DMS Plant**

NADL's wholly owned DMS plant currently located in the company's North Kimberley project area has been disassembled in readiness for transport to the Merlin project area. In its current configuration the plant has the capacity to process 100,000tpa. The current test work being undertaken at Merlin will enable the design of an appropriate front-end to this plant with a view to increasing it's capacity to 300,000 – 400,000tpa.

### **Drill Program**

A drill program is planned to investigate the geometry of a number of the Merlin kimberlite pipes at depth. This drilling will also provide kimberlite material for microdiamond analysis and grade assessment. Previous drilling on some of the pipes in the Merlin field has demonstrated significant enlargement of the pipes at the base of the Bukalara Sandstone which is generally at a depth of 100m below surface. It is anticipated that this program will commence late in the year.

## **MERLIN EXPLORATION**

The Merlin Orbit properties consist of nine tenements surrounding the mining lease of the former Merlin Diamond Mine totalling approximately 3,000km<sup>2</sup>, encompassing the currently known extent of the Merlin kimberlite field.

### **New Targets**

A review of the Merlin exploration sampling data has identified 25 indicator mineral and diamond anomalies of which 17 are considered to be high priority exploration targets. Most of these have not previously been investigated in detail.

In the previous reporting period follow-up sampling and ground inspection was carried out on 16 of the geophysical targets and 14 of the indicator mineral anomalies resulting in the collection of 14 loam, 17

gravel and 84 soil samples. These samples were despatched to the Company's Perth laboratory for analysis. Results are still awaited for this sampling program.

Access to the areas to the south of Merlin is being prepared to allow follow-up bulk sampling to be undertaken. Previous bulk samples in this area have reported significant numbers of alluvial diamonds, which were interpreted to be shedding from a second local source, south of the Merlin pipe clusters.

## **NORTH KIMBERLY PROJECTS, Western Australia.**

### **Seppelt Project**

The Seppelt Project comprises a number of related kimberlite dykes, blows and pipes constrained within a narrow corridor over a strike length of some 6km. No additional work was undertaken in this area during the quarter.

## **RIO TINTO JOINT VENTURES**

### **Kimberley Data Base**

The Company has an exclusive diamond licensing agreement with Rio Tinto Exploration Pty Ltd (RTE) over the majority of its extensive Kimberley diamond database. The Kimberley diamond database contains information relating to approximately 13,000 sample sites. The data has been accumulated over a 30 year period and includes SEM probe as well as indicator-mineral and diamond recovery data.

### **Narrie Anomaly**

The first exploration target to be identified from the database was secured by a tenement application in 2004. This exploration licence was granted in late September and a follow-up exploration program is now planned for the coming quarter. Previously limited follow-up sampling in this area has confirmed the presence of kimberlitic chromite with probe analysis indicating the source rock has good diamond bearing potential. The recovery of a single +0.3mm microdiamond associated with the chromite supports this analysis.

## **OTHER**

### **North King George Falcon™ System Joint Venture, Western Australia**

Diamond Mines Australia Pty Ltd, (DMA) a wholly owned subsidiary of Gravity Diamonds Limited, are in a 50/50 joint venture with the Company to follow-up the results of the Falcon™ survey that was funded by DMA. The Company is managing the field program on behalf of the joint venture.

### **Follow-up of Anomalies**

The follow-up of 5 priority targets and 5 moderate priority targets was completed in the previous reporting period with the collection of a total of 47 loam, 10 stream, 11 rock and 9 soil samples. These targets were selected from the 25 priority targets which were sampled in 2004. Results are pending for 19 of the stream/loam samples. Positive results received to date include 3 samples reporting single microdiamonds, one sample reporting a macrodiamond and 5 samples reporting positive for indicator minerals. Microprobe analyses are pending on the samples which contained indicator minerals. Results will be fully assessed when all analyses are received.

### **AKD Joint Venture - E80/1590, Western Australia**

No follow-up sampling was done on this tenement during the reporting period.

## **DE BEERS JOINT VENTURE**

### **Arnhem Land Northern Territory – Striker Earning 100%**

The Company has a farm-in agreement with De Beers Exploration Australia Limited (DBAE) to earn 100% interest in tenements with a total project area of 13,500km<sup>2</sup> in the Arnhem Land region of the Northern Territory. The Company has made application for a further 4 tenements which brings a total area of 7,700km<sup>2</sup> in which the Company has 100% interest. The project area now covers twenty-seven separate tenements of which 18 are in joint venture with De Beers.

Work programs have been submitted for two of the tenements, totalling 1,400km<sup>2</sup> that are available for immediate exploration. Heritage clearances and final meetings with Traditional Owners scheduled to take place this year have been delayed until next year.

The Company considers these tenements to be highly prospective for diamond-bearing kimberlites and other minerals. Regionally the area is situated within stable platform Proterozoic-aged sediments in close proximity to a major crustal trough, a setting geologically analogous to the Merlin kimberlite field which is located some 400km to the south. Initial exploration will include the taking of traditional indicator mineral and diamond stream samples, as well as the interpretation of photo and satellite imagery and aeromagnetic data sets.

## **CORPORATE**

### **Rough Diamond Advance Sale:**

Under the terms of the advance diamond purchase agreement entered into with Knightsbridge Corporate (Knightsbridge), Knightsbridge will pay the company \$500,000 for the purchase of a selection of rough gem quality diamonds from the Merlin Mine. The purchase will be at a 16% discount to an independently assessed value and delivery will be made when sufficient stones become available. Knightsbridge have a further right to purchase any single diamond with an independently assessed value greater than A\$580,000 at a fair market value. The advance payment to the company will also be fully or partly convertible into equity under certain conditions.

### **Australian Golfields NL – Litigation: Refer Appendix 5B – Note 1 (attached)**

On October 11 2000, the company (having obtained leave from the court) filed proceedings against AFN (in liquidation) for:

- (a) A Declaration that the company has suffered loss and damage as claimed:
- (b) A Declaration that in respect of any indebtedness on the Company's part by reason of the receipt of funds from AFN, that any obligation to repay those amounts have been set-off and fully extinguished at law in equity; and
- (c) A Declaration that the liquidators of AFN are bound to accept the proof of debt of the applicant having made due allowance for the amounts set off therein.

It is Senior Counsel's opinion that the repudiatory breach by AFN will give rise to substantial issues of set-off and counter claim which will bear on any obligation by the Company to repay the amounts advanced. The right set-off for the counter claim by AFN makes the future sacrifice of economic benefits unlikely, however this is contingent on the outcome of future court proceedings. The parties have been attending to pre-trial directions and the matter has now been listed for trial in the Supreme Court of Western Australia on 21 November 2005.

Tom Reddcliffe  
Chief Executive Officer

*The information in this report, which relates to mineral resources, is based on information compiled by Mr Tom Reddcliffe, a full time employee of the company. Mr Reddcliffe has relevant experience in relation to the mineralisation being reported on to qualify as a competent person as defined in the Australasian Code for Reporting of Identified Mineral Resources and Ore Reserves. He has consented to the inclusion of this information in the form and context in which it appears in this report.*

# Appendix 5B

## Mining exploration entity quarterly report

Introduced 1/7/96. Origin: Appendix 8. Amended 1/7/97, 1/7/98, 30/9/2001.

Name of entity

North Australian Diamonds Limited

ABN

86 009 153 119

Quarter ended ("current quarter")

30 September 2005

### Consolidated statement of cash flows

	Current quarter \$A '000	Year to date (12 months) \$A '000
<b>Cash flows related to operating activities</b>		
1.1 Receipts from product sales and related debtors		
1.2 Payments for		
(a) exploration and evaluation	(722)	(722)
(b) development		
(c) production		
(d) administration	(396)	(396)
1.3 Dividends received		
1.4 Interest and other items of a similar nature received	10	10
1.5 Interest and other costs of finance paid	(2)	(2)
1.6 Income taxes paid		
1.7 Other (provide details if material)		
<b>Net Operating Cash Flows</b>	(1,110)	(1,110)
<b>Cash flows related to investing activities</b>		
1.8 Payment for purchases of:		
(a)prospects – Merlin Orbit		
(b)equity investments		
(c) other fixed assets	(81)	(81)
1.9 Proceeds from sale of:		
(a)prospects		
(b)equity investments		
(c)other fixed assets		
1.10 Loans to other entities		
1.11 Loans repaid by other entities		
1.12 Other – Security deposits		
<b>Net investing cash flows</b>	(81)	(81)
1.13 Total operating and investing cash flows (carried forward)	(1,191)	(1,191)

**Appendix 5B**  
**Mining exploration entity quarterly report**

1.13	Total operating and investing cash flows (brought forward)	(1,191)	(1,191)
	<b>Cash flows related to financing activities</b>		
1.14	Proceeds from issues of shares, options, etc.	4,356	4,356
1.15	Proceeds from sale of forfeited shares		
1.16	Proceeds from borrowings	25	25
1.17	Repayment of borrowings	(25)	(25)
1.18	Dividends paid		
1.19	Other (proceeds from forward sales of diamonds)	250	250
	<b>Net financing cash flows</b>	<b>4,606</b>	<b>4,606</b>
	<b>Net increase (decrease) in cash held</b>	<b>3,415</b>	<b>3,415</b>
1.20	Cash at beginning of quarter/year to date	339	339
1.21	Exchange rate adjustments to item 1.20		
1.22	<b>Cash at end of quarter</b>	<b>3,754</b>	<b>3,754</b>

**Payments to directors of the entity and associates of the directors**  
**Payments to related entities of the entity and associates of the related entities**

		Current quarter \$A'000
1.23	Aggregate amount of payments to the parties included in item 1.2	117
1.24	Aggregate amount of loans to the parties included in item 1.10	

1.25 Explanation necessary for an understanding of the transactions

Remuneration

**Non-cash financing and investing activities**

2.1 Details of financing and investing transactions which have had a material effect on consolidated assets and liabilities but did not involve cash flows

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2.2 Details of outlays made by other entities to establish or increase their share in projects in which the reporting entity has an interest

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**Financing facilities available**

*Add notes as necessary for an understanding of the position.*

+ See chapter 19 for defined terms.

	Amount available \$A'000	Amount used \$A'000
3.1 Loan facilities	Refer Note 1	\$2,200
3.2 Credit standby arrangements		

**Estimated cash outflows for next quarter**

	\$A'000
4.1 Exploration and evaluation	1,200
4.2 Development	
<b>Total</b>	<b>1,200</b>

**Reconciliation of cash**

Reconciliation of cash at the end of the quarter (as shown in the consolidated statement of cash flows) to the related items in the accounts is as follows.	Current quarter \$A'000	Previous quarter \$A'000
5.1 Cash on hand and at bank	154	339
5.2 Deposits at call	3,600	
5.3 Bank overdraft		
5.4 Other (provide details)		
<b>Total: cash at end of quarter (item 1.22)</b>	<b>3,754</b>	<b>339</b>

**Changes in interests in mining tenements**

	Tenement reference	Nature of interest (note (2))	Interest at beginning of quarter	Interest at end of quarter
6.1 Interests in mining tenements relinquished, reduced or lapsed	E80/2917-20 E80/2461	Lapsed Reduced	100% 15 Blocks	- 8 Blocks
6.2 Interests in mining tenements acquired or increased	EL24500	Acquired	-	116 Blocks

**Appendix 5B**  
**Mining exploration entity quarterly report**

**Issued and quoted securities at end of current quarter**

*Description includes rate of interest and any redemption or conversion rights together with prices and dates.*

	Total number	Number quoted	Issue price per security (see note 3) (cents)	Amount paid up per security (see note 3) (cents)
7.1 <b>Preference +securities</b> <i>(description)</i>				
7.2 Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs, redemptions				
7.3 <b>+Ordinary securities</b>	817,217,552	817,217,552		
7.4 Changes during quarter (a) Increases through issues (b) Decreases through returns of capital, buy-backs	154,256,188	154,256,188		
7.5 <b>+Convertible debt securities</b> <i>(description)</i>				
7.6 Changes during quarter (a) Increases through issues (b) Decreases through securities matured, converted				
7.7 <b>Options</b> <i>(description and conversion factor)</i>	139,999,771 20,500,000	139,999,771	<i>Exercise price</i> 15 cents 7.5 cents	<i>Expiry date</i> 30/11/05 31/07/08
7.8 Issued during quarter				
7.9 Exercised during quarter				
7.10 Expired during quarter	2,000,000	-	12 cents	31/10/05
7.11 <b>Debentures</b> <i>(totals only)</i>				
7.12 <b>Unsecured notes</b> <i>(totals only)</i>				

+ See chapter 19 for defined terms.

## Compliance statement

- 1 This statement has been prepared under accounting policies which comply with accounting standards as defined in the Corporations Act or other standards acceptable to ASX (see note 4).
- 2 This statement does give a true and fair view of the matters disclosed.



Sign here: ..... Date: 31 October 2005  
(~~Director~~/Company secretary)

Print name: KEVIN R. HART

## Notes

- 1 The quarterly report provides a basis for informing the market how the entity's activities have been financed for the past quarter and the effect on its cash position. An entity wanting to disclose additional information is encouraged to do so, in a note or notes attached to this report.
- 2 The "Nature of interest" (items 6.1 and 6.2) includes options in respect of interests in mining tenements acquired, exercised or lapsed during the reporting period. If the entity is involved in a joint venture agreement and there are conditions precedent which will change its percentage interest in a mining tenement, it should disclose the change of percentage interest and conditions precedent in the list required for items 6.1 and 6.2.
- 3 **Issued and quoted securities** The issue price and amount paid up is not required in items 7.1 and 7.3 for fully paid securities.
- 4 The definitions in, and provisions of, *AASB 1022: Accounting for Extractive Industries* and *AASB 1026: Statement of Cash Flows* apply to this report.
- 5 **Accounting Standards** ASX will accept, for example, the use of International Accounting Standards for foreign entities. If the standards used do not address a topic, the Australian standard on that topic (if any) must be complied with.

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**Appendix 5B**  
**Mining exploration entity quarterly report**

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**NOTE 1**

**SECTION 3**

Australian Gold Fields NL (In Liquidation) ('AGF') had an obligation to underwrite a pro-rata offer by the Company to raise a minimum amount of \$7.5 million by prospectus with the shares to be offered at a price at least equal to 12.5 cents ('AGF's Underwriting Obligation').

Due to delays requested by AGF in proceeding with the rights issue, AGF provided interim funding of \$2.2 million to the Company pending completion of the rights issue. AGF has a funding obligation in the order of \$3.0 million. Repayment of the advance was not to the detriment of the Company or any of its controlled entities until at the earliest after 12 December 1998 and only out of the proceeds of a rights issue ('AGF's Funding Obligation').

The Company obtained the opinion of Senior Counsel that both AGF's Underwriting and Funding obligations are valid and enforceable. The then Administrators of AGF denied liability in respect of both such obligations.

On 25 August 1998, the Company advised the then Administrators of AGF that AGF's continuing failure to comply with its Underwriting Obligation was a repudiatory breach which the Company accepted, and reserved all its rights against AGF including a claim for all the loss and damages suffered by the Company as a result of the breach which the Company accepted.

It is Senior Counsel's opinion that the repudiatory breach by AGF will give rise to substantial issues of set-off and counter claim which will bear on any obligation by the Company to repay the amounts advanced.

The Company has lodged with the liquidator of AGF a formal proof of debt claiming the sum of \$11,566,621 being the loss and damage suffered by the Company as a consequence of the failure of AGF to comply with its Underwriting Obligation.

On 8<sup>th</sup> September 2000, the Company lodged an application in the Supreme Court of Western Australia seeking leave to commence proceedings against AGF.

Following grant of leave, the Company has filed and served a writ seeking:

- (a) A Declaration that it has, by reason of the breach, alternatively repudiation of the Residual Underwriting Commitment, suffered loss and damage, as set out in the Company's Proof of Debt, of the amount of \$11,566,621.
- (b) A Declaration that in respect of any indebtedness on its part by reason of the receipt of funds from AGF, that the obligation to repay such amounts has been set off and fully extinguished against its damages claim, being amounts totalling \$2,328,580.
- (c) A Declaration that the liquidators of AGF accept the proof of debt of the Company having made due allowance for amount set off, being an amount of \$9,238,041.
- (d) Costs.

The writ relates to the non-performance of the obligations of AGF pursuant to an Underwriting Agreement and Residual Underwriting Agreement entered into with the Company on the 2<sup>nd</sup> December 1996 and subsequent interim funding monies advanced to Striker up until 6<sup>th</sup> March 1998.

The parties have been attending to pre-trial directions and the matter has now been listed for trial in the Supreme Court of Western Australia on 21 November 2005.

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+ See chapter 19 for defined terms.