



26 August 2011

**THE MANAGER  
COMPANY ANNOUNCEMENTS OFFICE  
ASX LIMITED**

Dear Sirs

**re : Phosphagenics Limited**

**HALF-YEARLY REPORT : APPENDIX 4D**

Enclosed for release to the market is the Company's Appendix 4D Report for the half-year ended 30 June 2011 inclusive of the signed Financial Report of the Company for that period.

Yours faithfully  
Phosphagenics Limited

Mourice Garbutt  
Company Secretary  
poh\asx\half-yearly report 30 06 11

**About Phosphagenics Limited**

Phosphagenics is commercialising drug delivery applications based on its novel transdermal (drugs administered via skin) TPM® – Targeted Penetration Matrix technology. TPM® is a patient friendly and cost effective system used to deliver proven pharmaceutical and nutraceutical products.

The lead product advancing through clinical trials is an oxycodone matrix system for the relief of chronic pain.

Phosphagenics' shares are listed on the Australian Securities Exchange (POH) and its ADR – Level 1 program in the US is with The Bank of New York Mellon (PPGNY).

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

# Phosphagenics Limited

(ABN 32 056 482 403)

## Appendix 4D

### Half Year Report for the period ended on 30 June 2011

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Section 4 Audit Alert

## **SECTION 2 : HIGHLIGHTS OF RESULTS, DIVIDENDS & ANALYSTS INFORMATION**

The following comment is to be read in conjunction with the summarised results report:

For the six months ended 30 June 2011, the Company returned an after tax loss of \$4.382 million (2010: \$0.550 million). The principal activity of Phosphagenics and its controlled entities for the half year period was the continued development of the Company's intellectual property on which \$0.337 million (2010: \$0.764 million) was expensed. From commercialising these activities the Company earned \$1.204 million from the sale of goods (2010: \$0.398 million).

During the period, the Company continued to advance the commercialisation of its unique patented delivery technology with achievement of the following milestones:

### *Oxycodone*

- Completion of preclinical studies for the proprietary TPM/oxycodone transdermal matrix patch system. The collaborative agreement between Phosphagenics and 3M has yielded a 5-fold improvement in the delivery of Oxycodone through human skin.
- Phosphagenics completed a Phase 1B clinical study of the proprietary oxycodone transdermal matrix patch systems in 2010. The results of the trial established that after a single dose the matrix patch delivered oxycodone into the blood stream in a reproducible, consistent and sustained manner.
- Phosphagenics is now working with the global company – 3M (USA) to optimise and carry out large scale GMP development of the TPM/oxycodone matrix patch system. Following the patch optimisation and commercial scale-up of the patch, Phosphagenics will commence Phase 2/3 clinical trials in Australia by Q4 2011. The Phosphagenics/3M collaboration also yielded positive result in May 2011, when the TPM/oxycodone patch was further improved to deliver 5-fold greater Oxycodone through the skin. The improvement to the TPM/oxycodone pain patch bodes well for Phosphagenics commercial prospects with the TPM/oxycodone pain patch and is encouraging from a commercialisation perspective, while also seen as a significant positive step forward in the commercialisation pathway for Phosphagenics world-first pain patch.

### *ELIXIA® BodyShaper Cellulite Contour Crème™*

- Highlighting the success of the ELIXIA® range launch in 1H 2011 was the immense initial sales success of the ELIXIA® BodyShaper Cellulite Contour Crème™. The ELIXIA® range was well-received by consumers, retailers and the media alike – with Myer and TVSN stocking the range shortly after launch, sales have approached \$1 million, indicating that consumers are warming to the prospect of using skin care products that deliver results and are scientifically proven to work.
- Phosphagenics completed all the necessary formulation and development work for TPM/AOD formulation. The product was tested in a human focus group during Q1 2011. Twice daily application of BodyShaper Cellulite Contour Crème™ successfully reduced the visible appearance of cellulite over the 8 week treatment period, and also had positive effects on skin parameters such as elasticity and hydration.

As at 30 June 2011 funds in hand totalled \$6.328 million (2010: \$8.433 million); refer to the Statement of Cash Flow. At 30 June 2011 Shareholders Equity totalled \$42.038 million (2010: \$49.811 million); refer to the Statement of Changes in Equity.

To examine in detail the information referred to above please visit the Company's website at: [www.phosphagenics.com](http://www.phosphagenics.com) or contact the Company by telephone +613 9565 1119 or by facsimile +613 9565 1151

# Appendix 4D

## PHOSPHAGENICS LIMITED

ABN 32 056 482 403

### Half Year Report Period Ended 30 June 2011

(Previous Corresponding Period: Half year ended 30 June 2010)

The Appendix 4D should be read in conjunction with the most recent Financial Report

#### Results for announcement to the market

		\$A'000	\$A'000
		6 months 30 June 2011	6 months 30 June 2010
Revenues from ordinary activities	(Down 68%)	1,663	5,140
(Loss) from ordinary activities after tax attributable to members	(Up 697%)	(4,382)	(550)
Net (Loss) for the period attributable to members	(Up 697%)	(4,382)	(550)

Dividends (distributions)	Amount per security	Franked amount per security
6 months ended 30 June 2011 N/A	-	N/A ¢
6 months ended 30 June 2010 N/A	-	N/A ¢
Record date for determining entitlements to the dividend	N/A	

#### Net Tangible Assets Per Security

Net tangible assets per security (with the comparative figure for the previous corresponding period):

	30 June 2011	30 June 2010
Net tangible assets per security	1.07 Cents	1.27 Cents

***Brief explanation necessary to enable the figures above to be understood:***

For the six months ended 30 June 2011, the Company returned an after tax loss of \$4.382 million (2010: \$0.550 million). The principal activity of Phosphagenics and its controlled entities for the half year period was the continued development of the Company's intellectual property on which \$0.337 million (2010: \$0.764 million) was expensed. From commercialising these activities the Company earned \$1.204 million from the sale of goods (2010: \$0.398 million).

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As at 30 June 2011 funds in hand totalled \$6.328 million (2010: \$8.433 million); refer to the Statement of Cash Flow. At 30 June 2011 Shareholders Equity totalled \$41.988 million (2010: \$49.811 million); refer to the Statement of Changes in Equity.

To examine in detail the information referred to above please visit the Company's website at [www.phosphagenics.com](http://www.phosphagenics.com) or contact the Company by telephone +613 9565 1119 or by facsimile +613 9565 1151

### **SECTION 3 : STATUTORY SECTION 320 ACCOUNTS**

The Financial Report for the half-year period ended 30 June 2011, as attached, is inclusive of:

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# Phosphagenics Limited

ABN 32 056 482 403

Condensed Financial Report  
for the half year ended 30 June 2011

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## Directors' Report

The Directors of Phosphagenics Limited submit their report for the half-year ended 30 June 2011.

### DIRECTORS

The names and particulars of the Directors of Phosphagenics Limited in office at any time during or since the end of the period:

#### Currently in Office

**JONATHAN LANCELOT ADDISON (AGED 59 YEARS) BEC (TAS), ASIC, CFTP (SNR) AICD  
INDEPENDENT DIRECTOR SINCE NOVEMBER 2002, CHAIRMAN SINCE MAY 2010  
LAST RE-ELECTED MAY 2011**

Mr Addison has over 30 years in the investment management industry, including wide experience in superannuation, and insurance. Currently, in addition to holding a number of Board positions he is an Investment Advisor to the Meat Industry Employee Superannuation Fund (MIESF). Previously he was the Fund Manager/CEO, of the Fund.

MIESF, a self-administered industry superannuation fund established in 1981 which operates nationally, currently holds 21,800,000 shares in Phosphagenics Limited. Prior to his appointment to MIESF, Mr Addison was a Director and Asset Consultant within the corporate finance section of PricewaterhouseCoopers and in this role was responsible for establishing an investment consulting practice with clients ranging from superannuation funds to insurance funds and funds managers. Prior to that, Mr Addison held a number of investment management and consulting positions in both the public and private sectors.

In recent years Mr Addison has spoken at a number of economics and investment related conferences both in Australia and overseas.

Mr Addison also holds Non-Executive Directorships with, African Enterprise International, (In October 2010 he was elected International Chairman), African Enterprise (Australia) Limited, African Enterprises New Zealand Limited, Hawksbridge Limited, Global Masters Fund Limited, TPCG Limited and Athelney Trust plc. Mr Addison stepped down as the Chairman of the Company's Audit, Compliance and Corporate Governance Committee in May 2010 as he is now Chairman of the Board.

**HARRY ROSEN (AGED 64 YEARS) BA , LLB  
EXECUTIVE DIRECTOR APPOINTED TO THE BOARD IN JUNE 1999  
APPOINTED CHIEF EXECUTIVE OFFICER DECEMBER 2005  
LAST RE-ELECTED MAY 2004\***

Mr Rosen is one of the founders of Betatene Limited and Denehurst Limited, two formerly ASX listed companies which commercialised significant research and development. Betatene is the world's largest producer of natural beta carotene. After the purchase of Betatene Limited by Henkel Corporation, Mr Rosen served as Vice President, Corporate Development. As a Vice President of Henkel Corporation, he worked for a number of years in the U.S. in the nutrition and health care industries.

Mr Rosen has consulted to many technology companies assisting them with the commercialisation of new technologies. He has had significant experience in the areas of seed capital raising, stock exchange listings, taxation and corporate law. Mr Rosen graduated from the Australian National University (BA-Psychology) and Melbourne University (LLB).

\* As Chief Executive Officer Mr Rosen is not required to retire by rotation.

**DON CLARKE (AGED 57 YEARS) LLB (HONS)  
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010**

Mr Don Clarke has been a partner of law firm Minter Ellison since 1988. He serves in the Melbourne Private Equity & Capital Markets group, predominantly advising ASX listed companies across a range of industries with emphasis on technology and manufacturing.

Mr Clarke is also the Deputy Chairman of Webjet Limited and a Director of Circadian Technologies Limited. He previously served on the Board of Calzada Limited (formerly Metabolic Pharmaceuticals Limited).

Mr Clarke was appointed as the Chairman of the Company's Audit, Compliance and Corporate Governance Committee in August 2010.

**STUART JAMES (AGED 62 YEARS) BA (HONS)  
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010**

Mr Stuart James has held a number of high profile executive positions during his career and has extensive experience in the oil, health, pharmaceutical and financial services sectors. Following a 25 year career with Shell, both in Australia and internationally, Mr James' past roles have included Managing Director of Australian Financial Services for Colonial Group and Managing Director of Colonial State Bank (formerly the State Bank of NSW).

Mr James' most recent executive role was as CEO of the Mayne Group, including Mayne Health and Mayne Pharma. He is a Member of the Supervisory Board of Wolters Kluwer NV. Mr James is Chairman of Pulse Health Ltd, Progen Pharmaceuticals Ltd, Prime Financial Group Ltd and a Non-Executive Director of Greencross Ltd.

Mr James is a member of the Company's Audit, Compliance and Corporate Governance Committee.

**DR SANDRA WEBB (AGED 65 YEARS) BPHARM, PHD, DIP LAW  
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010**

Dr Sandra Webb rejoins Phosphagenics, having served with the company as Pharmaceutical Development Advisor from February 2005 to June 2006. Dr Webb is a Director of Ground Zero Pharmaceuticals Pty Limited. She previously served on the Boards of AusBiotech Limited, Amrad Corporation Limited and Quintiles Pty Limited.

An experienced biopharmaceutical professional, Dr Webb has a strong track record of achievements in the commercial world of drug development. As founding Managing Director of Quintiles Australia, she successfully grew the company as the leading commercial research organisation in Australia. Under her stewardship Quintiles Australia was the most profitable subsidiary of the worldwide Quintiles Transnational Inc.

Dr Webb is a member of the Company's Audit, Compliance and Corporate Governance Committee.

**DR ESRA OGRU (AGED 36 YEARS) BSC (HONS) PHD  
EXECUTIVE DIRECTOR SINCE OCTOBER 2005  
JOINT CHIEF EXECUTIVE OFFICER SINCE MAY 2010  
LAST RE-ELECTED MAY 2009**

Dr Ogru is responsible for the management of the operations in Australia and internationally. She achieves this through leadership of a team of experienced pharmaceutical scientists and chemists and strategic collaborations.

In this role, Dr Ogru has developed commercial opportunities for both the Company's nutraceutical division and pharmaceutical technologies, such as transdermal drug delivery and drug enhancement platforms for disease and chronic pain management.

Dr Ogru has many years of operational experience in commercial aspects of the industry and has publications in peer-reviewed journals.

**FORMER DIRECTORS:**

None

## PRINCIPAL ACTIVITIES

The principal activities of the Company are the production, sale and licensing of products for the nutraceutical and pharmaceutical industries.

## RESULTS

For the six months ended 30 June 2011, the Company returned an after tax loss of \$4.382 million (2010: \$0.550 million). The principal activity of Phosphagenics and its controlled entities for the half year period was the continued development of the Company's intellectual property on which \$0.337 million (2010: \$0.764 million) was expensed. From commercialising these activities the Company earned \$1.204 million from the sale of goods (2010: \$0.398 million).

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## DIVIDENDS

The Directors have not recommended the payment of any dividends and no dividends were declared, paid or reinvested in the period to 30 June 2011.

## OPERATING AND FINANCIAL REVIEW

At the end of June 2011, the company held \$6.3 million in cash and cash equivalents. Closing cash was 25% below the amount held at June 2011 of \$8.4 million. During March 2011, Phosphagenics raised gross \$7.55 million through the placement of 83.90 million shares at 9 cents per share to institutions, professional and sophisticated investors. The funds will be primarily used to advance the clinical development and manufacturing of the Company's core development product – the world's first oxycodone pain patch, and to fund product rollouts of its new cosmetic range, including its new anti-cellulite cream.

Revenues for the year of \$1.3 million decreased by 73% from \$4.8 million in 2010, due mainly to a one-time payment to Phosphagenics in March 2010 of approximately \$1.09m (US\$1 million) and the issuance to Phosphagenics of 1.44 million shares in ProPhase Labs common stock which based on market price at the contract signing date was valued at approximately \$3.185 million. These shares are recognised as an available-for-sale investment at 30 June 2011. Product sales increased year on year by 203%, mainly due to the increase of ELIXIA® sales. The operating loss after income tax was \$4.4 million, an increase from \$0.6 million in 2010. For further details refer to the attached Financial Statements and notes.

A number of R&D milestones were achieved in 2011 including:

### *Oxycodone*

Completion of preclinical studies for the proprietary TPM/oxycodone transdermal matrix patch system. The collaborative agreement between Phosphagenics and 3M has yielded a 5-fold improvement in the delivery of Oxycodone through human skin.

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*Commercial Agreements*

Phosphagenics signed an agreement with CSL to evaluate TPM® delivery technology.

Phosphagenics extended the exclusive agreement with Métier Tribeca LLC, (“Métier”) to enable Métier to launch a further six premium cosmetic products utilising the TPM® delivery technology, under its brand name Le Métier de Beauté. This is yet another example of one of Phosphagenics’ partners experiencing success using scientifically validated TPM® delivery technology to produce commercial return on investment using innovative technology in their products.

Phosphagenics had signed an agreement with a private US-based company, to evaluate the TPM technology in combination with steroids. The collaborator advised that the FDA had approved the IND application in Q1 2011, clearing the way for Phase 1 clinical trials that commenced earlier in 2011 to test for safety and efficacy, the results of the studies are expected by Q3 2011.

Phosphagenics also advanced the collaborative development with a global dermatology company to jointly develop a prescription drug to treat acne. Phosphagenics has undertaken formulation development studies for a new product that combines Phosphagenics’ TPM® delivery technology and an anti-acne drug. The first phase is in-progress that aims to establish it’s stability profile and finalise the commercial product prior to clinical trials. The dermatological collaboration partner will pay for all development costs of the project.

Phosphagenics signed a non-exclusive license agreement with a prestige New York hair care company in Q2 2011, to initiate the first US hair care product sales using TPM® technology by the end of Q4 2011. The company will collaborate with Phosphagenics to develop a new range of hair care products for the US, UK and Australian markets, which account for over 15% of the global, \$67 billion hair care sector.

**Looking Forward**

Clinical trials have clearly shown TPM® technology can be used to safely deliver active agents into the blood stream, or the dermis, without causing irritation or erythema.

Phosphagenics announced the completion of several successful Phase 1 trials for its proprietary TPM/oxycodone (Targeted Penetration Matrix) transdermal patch system which delivered oxycodone in therapeutic doses in a consistent and sustained manner. This trial was conducted over 10 days.

In parallel to applying its proprietary delivery technology for use in pharmaceuticals, which have the potential to generate high value products, but which are subject to stringent regulatory requirements and long product development timelines, Phosphagenics is leveraging the research and development already undertaken to apply the TPM® delivery technology to cosmetic and personal care products. The TPM® delivery technology is well suited to products in this growing market, as products can be brought to market relatively quickly and with relatively low expenditure. Phosphagenics aims to generate cash from the sale of cosmeceutical products, which can be used to support research to develop the more costly, but higher value generating, pharmaceutical products.

In 2011 Phosphagenics will continue to develop and launch its own brand of personal care products (Elixia®) into the Australian and South East Asian markets through pharmacies, department stores and infomercials. Phosphagenics will continue to expand the cosmetics business globally through the relationship with Le Métier de Beauté in the USA.

### **SIGNIFICANT CHANGES IN STATE OF AFFAIRS**

During the period to 30 June 2011 there was no significant change in the state of affairs of the consolidated entity other than that referred to in the half-year report or notes thereto.

### **SIGNIFICANT EVENTS AFTER BALANCE DATE**

There has not been any matter or circumstance, other than that referred to in the half-year report and notes thereto, that has arisen since the end of the financial year, that has significantly affected, or may significantly affect, the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in future financial years.

### **LIKELY DEVELOPMENTS AND FUTURE RESULTS**

Disclosure of information regarding likely developments in the operations of the consolidated entity in future financial years and the expected results of those operations is likely to result in unreasonable prejudice to the consolidated entity. Accordingly this information has not been disclosed in this report.

### **ROUNDING**

The amounts contained in this report and in the financial report have been rounded to the nearest \$1,000 (unless stated otherwise) under the option available to the Company under ASIC Class Order 98/0100. The Company is an entity to which the Class Order applies.

### **REGISTERED OFFICE**

11 Duerdin Street, Clayton, Victoria 3168

Signed in accordance with a resolution of the Board of Directors:



Jonathon Lancelot Addison  
Chairman and Independent Director

Dated this 26<sup>th</sup> day of August 2011



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## Auditor's Independence Declaration to the Directors of Phosphagenics Limited

In relation to our review of the financial report of Phosphagenics Limited for the half-year ended 30 June 2011, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

A handwritten signature in black ink that reads 'Ernst &amp; Young' in a cursive, script font.

Ernst & Young

A handwritten signature in black ink that reads 'David Petersen' in a cursive, script font.

David Petersen  
Partner  
26 August 2011

## Consolidated Statement of Comprehensive Income

for the half-year ended 30 June 2011

	Notes	Consolidated	
		30 June 2011 \$'000	30 June 2010 \$'000
<b>Revenue</b>			
Sale of goods	3a	1,204	398
Licences	3a	124	4,241
Finance revenue	3a	105	203
<b>Total Revenue</b>		1,433	4,842
Cost of sales		(518)	(98)
<b>Gross Profit</b>		915	4,744
Income from government grants	3a	84	161
Other income	3a	146	137
Employee and Directors benefits expenses	3b	(1,849)	(1,839)
Occupancy and communications expenses		(102)	(120)
Consulting and professional expenses		(560)	(782)
Administration expenses		(667)	(416)
Research expenses		(1,194)	(764)
Impairment of available-for-sale investment		(727)	(1,308)
Other expenses	3c	(428)	(363)
Loss before income tax		(4,382)	(550)
Income tax/(expense)		-	-
Loss after income tax		(4,382)	(550)
<b>Other Comprehensive Income</b>			
Foreign currency translation		(3)	(7)
Income tax/(expense) on items of other comprehensive income		-	-
<b>Other comprehensive loss for the period, net of tax</b>		(3)	(7)
<b>Total comprehensive loss for the period</b>		(4,385)	(557)
<b>Loss per share from continuing operations attributable to the ordinary equity holders of the parent:</b>			
Basic loss per share		(0.56 cents)	(0.07 cents)
Diluted loss per share		(0.56 cents)	(0.07 cents)

## Consolidated Statement of Financial Position

as at 30 June 2011

		<b>Consolidated</b>	
	<b>Notes</b>	<b>30 June 2011 \$'000</b>	<b>31 December 2010 \$'000</b>
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash and cash equivalents	5	6,328	2,740
Trade and other receivables		758	305
Inventories		708	522
Other current assets		219	157
<b>Total Current Assets</b>		<b>8,013</b>	<b>3,724</b>
<b>Non-current assets</b>			
Intangible assets		47,023	47,046
Plant and equipment		1,190	1,298
Available-for-sale investment		1,113	1,700
<b>Total Non-Current Assets</b>		<b>49,326</b>	<b>50,044</b>
<b>TOTAL ASSETS</b>		<b>57,339</b>	<b>53,768</b>
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables		1,267	816
Provisions		254	115
<b>Total Current Liabilities</b>		<b>1,521</b>	<b>931</b>
<b>Non-current liabilities</b>			
Deferred tax liabilities		13,830	13,830
<b>Total Non-Current Liabilities</b>		<b>13,830</b>	<b>13,830</b>
<b>TOTAL LIABILITIES</b>		<b>15,351</b>	<b>14,761</b>
<b>NET ASSETS</b>		<b>41,988</b>	<b>39,007</b>
<b>EQUITY</b>			
Contributed equity	10	184,204	176,905
Accumulated losses		(171,406)	(167,024)
Reserves		29,190	29,126
<b>TOTAL EQUITY</b>		<b>41,988</b>	<b>39,007</b>

## Consolidated Statement of Cash Flow

for the half-year ended 30 June 2011

	Notes	Consolidated	
		30 June 2011 \$'000	30 June 2010 \$'000
<b>Cash flows from operating activities</b>			
Receipts from customers and related parties		973	1,731
Receipts of government grants		84	161
Payments to suppliers and employees		(4,795)	(4,528)
<b>Net cash used in operating activities</b>		<b>(3,738)</b>	<b>(2,636)</b>
<b>Cash flows from investing activities</b>			
Interest received		69	209
Purchase of plant and equipment		(42)	(9)
<b>Net cash from investing activities</b>		<b>27</b>	<b>200</b>
<b>Cash flows from financing activities</b>			
Proceeds from share issues	10	7,299	-
<b>Net cash from financing activities</b>		<b>7,299</b>	<b>-</b>
Net increase/(decrease) in cash and cash equivalents		3,588	(2,436)
Cash and cash equivalents at beginning of the period		2,740	10,869
<b>Cash and cash equivalents at the end of the period</b>	<b>5</b>	<b>6,328</b>	<b>8,433</b>

## Consolidated Statement of Changes in Equity

for the half-year ended 30 June 2011

	Consolidated				Total
	Contributed Equity	Employee Benefits Reserve	Business Combination & Foreign Currency Translation Reserve	Accumulated Losses	
	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Balance at 1 January 2011</b>	176,905	1,305	27,821	(167,024)	39,007
Loss for the period	-	-	-	(4,382)	(4,382)
Other comprehensive income	-	-	(3)	-	(3)
Total comprehensive income for the half year	176,905	1,305	27,818	(171,406)	34,625
<b>Transactions with owners in their capacity as owners</b>					
Issue of shares	7,551	-	-	-	7,551
Transaction costs on share issue	(252)	-	-	-	(252)
Share based payments	-	67	-	-	67
<b>Balance at 30 June 2011</b>	<b>184,204</b>	<b>1,372</b>	<b>27,818</b>	<b>(171,406)</b>	<b>41,988</b>
<b>Balance at 1 January 2010</b>	176,905	992	27,841	(155,749)	49,989
Loss for the period	-	-	-	(550)	(550)
Other comprehensive income	-	-	(7)	-	(7)
Total comprehensive income for the half year	176,905	992	27,834	(156,299)	49,432
<b>Transactions with owners in their capacity as owners</b>					
Employee equity settled benefits	-	109	-	-	109
Share based payments	-	270	-	-	270
<b>Balance at 30 June 2010</b>	<b>176,905</b>	<b>1,371</b>	<b>27,834</b>	<b>(156,299)</b>	<b>49,811</b>

# Notes to the Financial Statements

for the half-year ended 30 June 2011

## 1. BASIS OF PREPARATION AND ACCOUNTING POLICIES

### Basis of preparation

This general purpose condensed financial report for the half year ended 30 June 2011 has been prepared in accordance with AASB 134 *Interim Financial Reporting* and the *Corporations Act, 2001*.

The half-year financial report does not include all notes of the type normally included within the annual financial report and therefore cannot be expected to provide as full an understanding of the financial performance, financial position and financing and investing activities of the consolidated entity as the full financial report.

It is recommended that the half-year financial report be read in conjunction with the annual report for the year ended 31 December 2010 and be considered together with any public announcements made by Phosphagenics Limited during the half-year ended 30 June 2011 in accordance with the continuous disclosure obligations of the ASX Listing rules.

The accounting policies and methods of computation are the same as those adopted in the most recent annual financial report and this condensed financial report has been prepared on the historical cost basis.

## 2. OPERATING SEGMENTS

### Identification of reportable segments

The group has identified its operating segments based on the internal reports that are reviewed and used by the chief executive officer and the management team (the chief operating decision makers) in assessing the performance and in determining the allocation of resources.

The operating segments are identified by management based on the group's risks and returns that are affected predominantly by differences in the products and services provided. The reportable segments are based on aggregated operating segments determined according to the nature of the products and services provided, with each reportable segment representing a strategic business unit that offers different products and serves different markets.

### Types of products and services

#### Nutraceuticals

Nutraceuticals is the use of vitamins and nutritious products to improve human health. The nutraceutical business is developing active ingredients for the following market segments:

- Dietary Supplements - e.g. vitamin capsules & tablets. Phosphagenics is using its patented technology to orally deliver dietary supplements aimed at improving bioavailability and efficacy.
- Functional Foods and Beverages - e.g. nutritionally enhanced foods. Functional foods are an expanding nutraceutical market division, aimed at improving the nutritional benefits of everyday foods.
- Personal care products. Discovery research at Phosphagenics has shown that  $\alpha$ -tocopheryl phosphate (TP) is a natural molecule with increased activity over standard Vitamin E ( $\alpha$  tocopherol). TP has scientifically proven anti-inflammatory properties, it reduces redness, protects against UV induced photo damage, and also helps to heal and prevent acne. The structure of TP allows it to act as a penetration enhancer, increasing dermal absorption compared to tocopherol acetate and  $\alpha$ -tocopherol, allowing it to penetrate deeper into the skin for increased action. TP is also able to increase the penetration of molecules formulated in the same cream.

In 2010 Phosphagenics launched its own brand of cosmetic products in Australia (Elixia®) which were initially sold exclusively through Pulse Pharmacies. In April 2011 Elixia® was relaunched in Australia with an expanded product range. The distribution channels were also expanded to include Myer, TVSN and online sales through the Elixia website. Phosphagenics' nutraceutical business is a revenue-generating growth business. The route to market for Phosphagenics' nutraceutical products is through partnering with companies that have established distribution networks within the relevant market segments.

#### Pharmaceuticals

Phosphagenics' pharmaceutical segment is focused on:

- Drug delivery – enhancing the delivery of existing drugs orally or through the skin, utilising Phosphagenics' delivery technology TPM™
- Drug enhancement – augmenting the biological activity of existing drugs by adding a phosphate group to the chemical structure of the drug

The route to market for Phosphagenics' pharmaceutical products is through partnering with larger pharmaceutical companies at the appropriate stage in a product's development so as to maximise return on the Company's research and development investment.

The core competencies of the pharmaceutical business are generation of pharmaceutical intellectual property and translation of this knowledge base into commercially viable product candidates for the treatment of human conditions and disease.

Phosphagenics' strategy is to capitalise on its proprietary technology through joining its resources and development capabilities with co-development partners or licensees.

The objective of any development or marketing agreement entered into is to generate revenues from three sources:

- milestone payments and development fees during the pre-marketing phases of product development;
- royalties on product sales by partners; and
- manufacturing and supply of product to partners, predominantly of the phosphorylated delivery compound.

Phosphagenics choice of development products is based on market opportunity and the overall commercial viability of each individual drug candidate, including assessment of the current and expected competition for the product, the cost, timing and degree of difficulty to commercialise the product, the patent status of the drug compound and the market size of the product to be developed.

**Accounting policies and inter-segment transactions**

The accounting policies used by the Group in reporting segments internally are the same as those contained in note 1 to the accounts and in the prior period.

The following table presents revenue and profit information regarding business reportable for the half-year periods ended 30 June 2011 and 30 June 2010.

<b>Half-year ended 30 June 2011</b>	<b>Nutraceuticals \$'000</b>	<b>Pharmaceuticals \$'000</b>	<b>Total Group \$'000</b>
<b>Revenue</b>			
Sales and Royalties	1,325	2	1,327
Grant income		84	84
Total segment revenue	<u>1,352</u>	<u>86</u>	1,411
Other revenue			106
Total revenue and grant income per statement of comprehensive income			<u>1,517</u>
<b>Result</b>			
Segment result			(4,382)
<b>Segment assets</b>			
Segment operating assets	<u>799</u>	<u>1,047</u>	1,846
Unallocated assets			8,470
Intangible assets			47,023
Total assets per the statement of financial position			<u>57,339</u>
<b>Half-year ended 30 June 2010</b>	<b>Nutraceuticals \$'000</b>	<b>Pharmaceuticals \$'000</b>	<b>Total Group \$'000</b>
<b>Revenue</b>			
Sales and Royalties	398	4,241	4,639
Grant income		161	161
Total segment revenue	<u>398</u>	<u>4,402</u>	4,800
Other revenue			203
Total revenue and grant income per statement of comprehensive income			<u>5,003</u>
<b>Result</b>			
Segment result			(550)
<b>Segment assets</b>			
Segment operating assets	<u>799</u>	<u>934</u>	1,733
Unallocated assets			10,287
Intangible assets			54,728
Total assets per the statement of financial position			<u>66,748</u>

**Segment net operating profit after tax reconciliation to the statement of comprehensive income**

The executive management committee meets on a monthly basis to assess the performance of each segment by analysing the segment's net operating profit before tax. A segment's net operating profit before tax excludes non operating income and expense such as dividends received, fair value gains and losses, gains and losses on disposal of assets and impairment charges.

<b>Reconciliation of segment net operating profit before tax to net profit/loss before tax</b>	<b>2011</b>	<b>2010</b>
	<b>\$'000</b>	<b>\$'000</b>
Segment net operating profit/(loss) before tax	(4,382)	(550)
Other operating loss from continuing activities	-	-
Total net profit before tax per the statement of comprehensive income	<u>(4,382)</u>	<u>(550)</u>

### 3. REVENUES AND EXPENSES

	<b>Consolidated</b>	
	<b>30 June 2011</b>	<b>30 June 2010</b>
	<b>\$'000</b>	<b>\$'000</b>
<b>a) Revenue &amp; Income</b>		
Sales revenue	1,204	398
Income from Export Market Development Grant	84	161
Income from Licences – ProPhase Labs <sup>1</sup>	-	4,241
Income from Licences - Other	124	-
	<u>1,412</u>	<u>4,800</u>
Interest revenue	105	203
<b>Total finance revenue</b>	<u>105</u>	<u>203</u>
Other income	146	137
<b>Total revenue and income</b>	<u>1,663</u>	<u>5,140</u>
 <sup>1</sup> The licence revenue relates to a one-time payment to Phosphagenics of approximately \$1.09m (US\$1 million) and the issuance to Phosphagenics of 1.44 million shares in ProPhase Labs common stock which based on market price at the contract signing date was valued at approximately \$3.185 million. These shares are recognised as an available-for-sale investment at 30 June 2011.		
<b>b) Salaries and employee benefits expense</b>		
Salaries and wages	(1,713)	(1,600)
Superannuation	(127)	(130)
Employee equity settled benefits	9	(109)
<b>Total salaries and employee benefits expense</b>	<u>(1,849)</u>	<u>(1,839)</u>
<b>c) Other expenses</b>		
Net foreign exchange gains/(losses)	96	94
Depreciation	(128)	(146)
Amortisation	(33)	(33)
Operating lease rental expenses	(165)	(180)
Travel	(116)	(61)
Other	(82)	(37)
<b>Total other expenses</b>	<u>(428)</u>	<u>(363)</u>
<b>d) Seasonality of Operations</b>		
Phosphagenics Limited operations are not affected by seasonality		

#### 4. DIVIDENDS PAID AND PROPOSED

There were no dividends declared or paid during the half year ended 30 June 2011. (2010: NIL)

#### 5. CASH AND CASH EQUIVALENTS

	Consolidated	
	30 June 2011 \$'000	31 December 2010 \$'000
For the purposes of the half-year condensed statement of cash flows, cash and cash equivalents are comprised of the following:		
Cash at bank and in hand	2,202	2,565
Short-term deposits	4,126	175
	6,328	2,740
Total Cash and Cash Equivalents	6,328	2,740

#### 6. SHARE BASED PAYMENTS

The Group provides benefits to service providers in the form of share-based payments. Employees render services in exchange for rights over shares (equity-settled transactions). There are currently two schemes in place to provide these benefits to employees, being the Employee Share Option Plan (ESOP) and the Employee Conditional Rights Scheme (ECRS).

- The ESOP is designed to align participants' interests with those of shareholders by increasing the value of the Company's shares. Share options carry no rights to dividends and no voting rights. For options granted under the terms of the ESOP a service period was determined as the most appropriate criteria to attach to the options given Phosphagenics is still commercialising its products. There are no other services or performance criteria attached to share based payment options issued under the terms of the ESOP.
- The ECRS allows eligible employees to be granted Rights to acquire Shares at no cost. The purpose of the Scheme is to provide a long term incentive to staff as part of a focus to more closely link overall remuneration to the achievement of performance benchmarks, to encourage direct involvement and interest in the performance of the Company and to enable the acquisition of a long term equity interest in the Company by its staff. All employees, including executive and non-executive Directors, and any individual whom the Board determines to be an eligible participant for the purposes of the Scheme, are eligible to participate in the Scheme.

Fair values under both methods are calculated using a Binomial model. Options and Rights will be settled in ordinary shares of Phosphagenics Limited and vested options/rights lapse if unexercised after the expiry date.

In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of Phosphagenics Limited.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled (the vesting period), ending on the date on which the relevant party becomes fully entitled to the award (the vesting date).

During the six months ended 30 June 2011 no share options were granted under the ESOP (2010: NIL).

During the six months ended 30 June 2011, a total of 5,800,000 Rights with a fair value of \$0.07 were granted on 31 May 2011 under the ECRS (2010: Nil) which will vest based upon achievement of certain performance objectives.

During the six months ended 30 June 2011, 1,000,000 options with a fair value of \$0.06 million were granted to non-employees (2010: 15,000,000) which vested at the grant date of 25 May 2011.

The following table lists the inputs to the model used for the half-year ended 30 June 2011.

	<b>Consolidated</b>		
	<b>30 June 2011 ECRS</b>	<b>30 June 2011 Other</b>	<b>30 June 2010 Other</b>
Dividend yield (%)	0.00%	0.00%	0.00%
Expected volatility (%)	60%	61%	61%
Risk-free interest rate (%)	4.87%	4.75%	5.30%
Option life (years)	3.6 years	3 years	3 years
Exercise price (\$)	Nil	17.0 cents	14.2 cents

## 7. INVENTORIES

During the half-year ended 30 June 2011, as a result of new product releases, the Group wrote-down inventory which was recognised as an expense of \$43,676 (2010: NIL).

## 8. PLANT & EQUIPMENT

### Acquisitions and disposals

During the half-year ended 30 June 2011, the Group acquired assets with a cost of \$20,066 (2010: \$10,560).

## 9. COMMITMENTS AND CONTINGENCIES

### Lease Commitments

At 30 June 2011 the Group has commitments of \$85,045 (2010: \$405,853) relating to non-cancellable operating leases over the office and manufacturing facilities, which expire in 2011.

## 10. CONTRIBUTED EQUITY

	<b>Consolidated</b>	
	<b>(No. '000's)</b>	<b>(\$'000's)</b>
<b>Issued and paid up capital</b>		
Fully paid ordinary shares carry one vote per share and carry the right to receive dividends		
Movement in ordinary shares on issue:		
At 1 January 2011	739,696	176,905
Issue of shares	83,897	7,551
Exercise of options	-	-
Transaction costs on share issue	-	(252)
At 30 June 2011	<b>823,593</b>	<b>184,204</b>
At 1 January 2010	739,696	176,905
Issue of shares	-	-
Exercise of options	-	-
Transaction costs on share issue	-	-
At 30 June 2010	<b>739,696</b>	<b>176,905</b>

During March 2011, Phosphagenics raised gross \$7.55 million through the placement of 83.90 million shares at 9 cents per share to institutions, professional and sophisticated investors. The funds will be primarily used to advance the clinical development and manufacturing of the Company's core development product - the world's first oxycodone pain patch, and to fund product rollouts of its new cosmetic range, including its new anti-cellulite cream.

## 11. EVENTS AFTER THE BALANCE SHEET DATE

No events occurred between the balance sheet date and the date when these financial statements were authorised for issue.

## Directors' Declaration

In accordance with a resolution of the directors of Phosphagenics Limited, we state that:

In the opinion of the directors:

- (a) the financial statements and notes of the consolidated entity are in accordance with the *Corporations Act 2001*, including:
  - (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2011 and the performance for the half-year ended on that date of the consolidated entity.
  - (ii) complying with Accounting Standards AASB 134: *Interim Financial Reporting* and *Corporations Regulations 2001*; and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

On behalf of the Board



Jonathon Lancelot Addison  
Chairman and Independent Director

Melbourne  
26th August 2011



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To the members of Phosphagenics Limited

## Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Phosphagenics Limited, which comprises the condensed statement of financial position as at 30 June 2011, the condensed statement of comprehensive income, condensed statement of changes in equity and condensed statement of cash flows for the half-year ended on that date, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the half-year end.

### Directors' Responsibility for the Half-Year Financial Report

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

### Auditor's Responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the consolidated entity's financial position as at half-year and its performance for the half-year ended on that date; and complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*. As the auditor of Phosphagenics Limited and the entities it controlled during the half-year, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### Independence

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration.

### Conclusion

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half-year financial report of Phosphagenics Limited is not in accordance with the *Corporations Act 2001*, including:

- a) giving a true and fair view of the consolidated entity's financial position as at 30 June 2011 and of its performance for the half-year ended on that date; and
- b) complying with Accounting Standard AASB 134 *Interim Financial Reporting* and the *Corporations Regulations 2001*.



*Ernst & Young*

Ernst & Young

A handwritten signature in black ink, appearing to read 'David Petersen'. The signature is fluid and cursive, with a long horizontal stroke extending to the right.

David Petersen  
Partner  
Melbourne  
26 August 2011

**SECTION 4 : AUDIT ALERT**

*As at 30 June 2011 and as the date of this Report there are no matters of dispute or qualification or likely dispute or qualification.*