PHOSPHAGENICS

21 February 2012

Company Announcement

Appendix 4E Report and Financial Report December 2011

HIGHLIGHTS

Phosphagenics Limited (ASX: POH; OTCQX: PPGNY) today releases its consolidated Appendix 4E and audited Financial Report for the year ended 31 December 2011. The consolidated operating loss before impairment of intangible assets and income tax was $12.7 million, an increase from the $5.9 million consolidated operating loss for the financial year ended 31 December 2010.

Financial Results

The key points to note in the 2011 financial results are:

- The Company's consolidated cash reserves at 31 December 2011 were $27.2 million (31 December 2010 – $2.7 million).
- Revenues for the year totalled $3.2 million, of which $2.5 million came from product sales.
- For the first time, the Company booked amortisation charges relating to acquired patent assets, amounting to $2.32 million for 2011.
- Operating expenses, excluding amortisation and impairment charges totalled $13.1 million in 2011, compared to $9.8 million in 2010.
- Net profit after tax for the year was $1.1 million as compared to a net loss after tax in 2010 of $11.3 million. The 2011 result included the reversal of a $13.8 million deferred tax liability (thereby giving rise to an income tax benefit) upon the company electing to form a tax consolidated Group.

In commenting on the gains made in 2011 and the activities programmed for 2012 Phosphagenics CEO, Dr Esra Ogru, commented:

"2012 will be a big and exciting year for Phosphagenics. We remain focused and we will continue to advance our clinical TPM/oxycodone program into phase 3 clinical trials as well as expanding our Elixia and BioElixia skin care line nationally and internationally. The successful capital raising in 2011 has put Phosphagenics in a strong cash position, allowing it to further develop and advance its novel platform technology across multiple markets".

Phosphagenics Limited
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About Phosphagenics

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
www.elixia.com.au

Rule 4.3

Appendix 4E

Preliminary final report
Period ending on or after 31 December 2011

Introduced 1/1/2003. Origin: Appendix 4B

Name of entity

Phosphagenics Limited

The following information must be given to ASX under listing rule 4.3.

1.

ABN or equivalent company reference	Year ended: current period	previous corresponding period
32 056 482 403	31 December 2011	31 December 2010

Results for announcement to the market

				$A'000
2.1 Revenues from ordinary activities	down	38%	to	3,171
2.3 Profit (loss) from ordinary activities after tax attributable to members	up	110%	to	1,106
2.4 Net profit (loss) for the period attributable to members	Up	110%	to	1,106

2.4 Dividends (distributions)	Amount per security	Franked amount per security
Final dividend Interim dividend In Specie Dividend	-¢ -¢ -¢	-¢ -¢ -¢
Previous corresponding period: Final dividend Interim dividend In Specie Dividend	-¢	-¢

2.5 Record date for determining entitlements to the dividend	N/A

2.6 Brief explanation of any of the figures in 2.1 to 2.4 necessary to enable the figures to be understood.

At the end of December 2011, the company held $27.2 million in cash and cash equivalents. Closing cash was significantly higher than the amount held at December 2010 of $2.7 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. A further $27.2 million gross was raised from October to December 2011 through the issue of 193.97 million shares via private placements and a share purchase plan. 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 the continued product rollout of its cosmetic range, including its anti-cellulite cream.

Revenues for the year of $3.2 million decreased by 38% from $5.1 million in 2010, due mainly to a one-time payment in 2010 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. Product sales increased year on year by 500%, to $2.5 million mainly due to the rollout of the Elixia cosmetics product range and increases sales of Vital ET.

Net profit after tax for the year was $1.1 million as compared to a net loss after tax in 2010 of $11.3 million. During 2011 the company elected to form a tax consolidated group, with effect from 1 July 2009. Phosphagenics Limited is the head entity of the tax consolidated group, and as a result the tax base of intangible assets was reset such that the deferred tax liability of $13.8 million was reversed during the period, giving rise to an income tax benefit of the same amount.

The operating loss before impairment of intangible assets and income tax was $12.7 million, an increase from $5.9 million in 2010. For the first time, the Company booked amortisation charges relating to acquired patent assets, amounting to $2.32 million for 2011. For further details refer to the attached Financial Statements and notes.

Research & development

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

<u>Body Shaper</u>

Phosphagenics conducted international trials that showed the reduction in the appearance of cellulite in women of up to 40 % in 4 weeks and 56% in 8 weeks.

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Phosphagenics, in partnership with 3M, developed a patch which produced a 5 fold improvement in delivering oxycodone through the skin, as compared with the original prototype in in-vitro trials. The patch has been used in human pharmacokinetic trials which commenced during the final quarter of 2011.

<u>Physician's Survey</u>

Extera Partners , a well known U.S. consulting group, conducted a physician's survey that suggested that if an oxycodone twice a week patch were available, such as the one being developed by Phosphagenics, their prescribing intentions would indicate a market of in excess of $1 billion for that product.

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- Phosphagenics partnered with Mastitis Australia to develop a new technology for the global dairy market. The platform TPM technology was used to deliver an all natural formula targeting mastitis.
- Phosphagenics entered an agreement with an unnamed global dermatological company to trial its delivery technology in formulation development studies relating to the treatment of acne.
- Phosphagenics finalised a number of agreements to stock and sell Elixia products in Australia. Agreements were reached with Myer, TVSN (Foxtel Shopping Channel), Priceline and Terry Whites Pharmacies.
- Phosphagenics reached an agreement with Sungate Supplies Pte Ltd to supply Elixia (Bio Elixia) products exclusively to AS Watson stores in Asia.
- Phosphagenics licensed TPM/Diclofenac, its topical non steroidal pain formulation, to Themis Medicare Pvt Ltd. They may manufacture and sell this formulation in India.

Looking Forward

In the year ahead Phosphagenics will focus its attention on preparing IND (“investigational new drug”) documentation to enable the commencement of Phase 3 trials in the second half of the year. The pain advisory board will recommend the way forward which they believe will best facilitate the objective of gaining FDA approval for our product. As the trials progress we expect to generate considerable interest from large Pharmaceutical companies.

We also believe that 2012 will see continued expansion of the Elixia and Bio Elixia brands in Australia and overseas. Globally we are confident of being able to reach deals to launch in new geographic regions including U.S.A and Europe. In Australia we should see increased brand awareness and sales.

In the area of mass market licensing we remain confident of completing agreements in the area of cosmetics and/ or dermatology during the year.

In the areas of animal health we are hopeful that trial results will help to facilitate deals with major global players.

This year the focus will remain strongly on Oxycodone and Elixia but we expect to consummate other deals and collaborations.

3. A statement of financial performance together with notes to the statement, prepared in compliance with AASB 1018 or the equivalent foreign accounting standard:

See attached Consolidated Statement of Comprehensive Income

4. A statement of financial position together with notes to the statement. The statement may be condensed but must report as line items each significant class of asset, liability, and equity element with appropriate sub-totals:

See attached Consolidated Statement of Financial Position

5. A statement of cash flows together with notes to the statement. The statement of cash flows may be condensed but must report as line items each significant form of cash flow and comply with the disclosure requirements of AASB 1026 Statement of Cash Flows, or for foreign entities, the equivalent foreign accounting standard:

See attached Consolidated Statement of Cash Flow

6. Details of individual and total dividends or distributions and dividend or distribution payments. The details must include the date on which each dividend or distribution is payable, and (if known) the amount per security of foreign sourced dividend or distribution:

N/A

+ See chapter 19 for defined terms.

7. Details of any dividend or distribution reinvestment plans in operation and the last date for the receipt of an election notice for participation in any dividend or distribution reinvestment plan:

N/A

8. A statement of retained earnings showing movements:

	Current period $A'000	Previous corresponding period $A'000
Retained profits (accumulated losses) at the beginning of the financial period	(167,024)	(155,749)
Net profit (loss) attributable to members	1,106	(11,275)
Net transfers from (to) reserves	-	-
Net effect of changes in accounting policies	-	-
Dividends and other equity distributions paid or payable	-	-
Retained profits (accumulated losses) at end of financial period	**(165,918)**	**(167,024)**

9. Net tangible assets per security with the comparative figure for the previous corresponding period.

	Current period	Previous corresponding Period
Net tangible assets per security	2.8 cents	0.8 cents

+ See chapter 19 for defined terms.

10. Details of entities over which control has been gained or lost during the period:

10.1 Name of the entity.	N/A
10.2 The date of the gain or loss of control.	N/A

	Current period	Previous corresponding period
10.3 Where material to an understanding of the report – the contribution of such entities to the reporting entity's profit from ordinary activities during the period and the profit or loss of such entities during the whole of the previous corresponding period.	N/A	N/A

11. Details of associates and joint venture entities including the name of the associate or joint venture entity and details of the reporting entity's percentage holding in each of these entities and – where material to an understanding of the report - aggregate share of profits (losses) of these entities, details of contributions to net profit for each of these entities, and with comparative figures for each of these disclosures for the previous corresponding period.

Name of entity	% Holding	Aggregate Share of profit (losses)		Contribution to net profit	
		Current period $'000	Previous corresponding Period $'000	Current period $'000	Previous corresponding Period $'000
Vital Health Sciences Pty Ltd	100	N/A	N/A	(2,505)	(1,791)
Phosphagenics Inc	100	N/A	N/A	(658)	(505)

12. Any other significant information needed by an investor to make an informed assessment of the entity's financial performance and financial position:

N/A

13. For foreign entities, which set of accounting standards is used in compiling the report (e.g. International Accounting Standards).

International Financial Reporting Standards

14. A commentary on the results for the period. The commentary must be sufficient for the user to be able to compare the information presented with equivalent information for previous periods. The commentary must include any significant information needed by an investor to make an informed assessment of the entity's activities and results, which would include but not be limited to discussion of the following:

14.1 The earnings per security and the nature of any dilution aspects:

Basic earnings per share 0.13 cents (2010: (1.52))
Diluted earnings per share 0.13 cents (2010: (1.52))

14.2 Returns to shareholders including distributions and buy backs:

N/A

14.3 Significant features of operating performance:

N/A

14.4 The results of segments that are significant to an understanding of the business as a whole:

Refer to Preliminary financial statements

14.5 A discussion of trends in performance:

N/A

14.6 Any other factors which have affected the results in the period or which are likely to affect results in the future, including those where the effect could not be quantified:

N/A

15. A statement as to whether the report is based on accounts which have been audited or subject to review, are in the process of being audited or reviewed, or have not yet been audited or reviewed.

The accounts of the Company have been audited.

Note: If the +accounts have been audited or subject to review, the audit report should be provided with the report.

16. If the accounts have not yet been audited or subject to review and are likely to be subject to dispute or qualification, a description of the likely dispute or qualification:

N/A

17. For all entities, if the accounts are subject to audit dispute or qualification, a description of the dispute or qualification.

N/A

Note: The audit report or review must be provided as part of the report.

Signed by Company Secretary:

Name: Mourice Garbutt

Date: 21 February 2012

+ See chapter 19 for defined terms.

Phosphagenics Limited

ABN 32 056 482 403

Annual Financial Report

for the year ended 31 December 2011

Contents

Directors' Report

Your directors submit their report for the year ended 31 December 2011.

DIRECTORS

The names and details of the Company's directors in office during the financial year and until the date of this report are as follows. Directors were in office for this entire period unless otherwise stated.

NAMES, QUALIFICATIONS, EXPERIENCE AND SPECIAL RESPONSIBILITIES

Currently in Office

JONATHAN LANCELOT ADDISON (AGED 59 YEARS) BEC (TAS), ASIC, CFTP (SNR)
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.

Directors' Report (continued)

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 was appointed Joint CEO of Phosphagenics in April 2010. Her responsibilities include involvement in setting strategic direction, management of operations and financing activities for the company. She also plays an active role in driving key commercial negotiations, development programs and corporate activity. She achieves this through strong leadership of an experienced pharmaceutical development team and strategic collaborations.

Dr Ogru has many years experience in the pharmaceutical and biotechnology industries working in development and senior management roles. She is currently the chair of the Australian Biotechnology Victorian Committee and also is the member for the Victorian Biotechnology Council.

DON CLARKE (AGED 58 YEARS) LLB (HONS)
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010
ELECTED MAY 2011

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 63 YEARS) BA (HONS)
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010
ELECTED MAY 2011

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.

Directors' Report (continued)

DR SANDRA WEBB (AGED 66 YEARS) BPHARM, PHD, DIP LAW
INDEPENDENT DIRECTOR APPOINTED AUGUST 2010
ELECTED MAY 2011

Dr Sandra Webb rejoined 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 and Chair of the Advisory Board of Knightsbridge Lawyers & Patent Attorneys. 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.

DIRECTORSHIPS OF OTHER LISTED COMPANIES

Directorships of other listed companies held by Directors in the three years immediately before the end of the financial year are as follows:

NAME	COMPANY	PERIOD OF DIRECTORSHIP
Jonathan Addison	Global Masters Fund Limited	Since 19 April 2005
Don Clarke	Circadian Technologies Limited	Since 1 September 2005
	Webjet Limited	Since 10 January 2008
	Calzada Limited (formerly Metobolic Pharmaceuticals Ltd)	From 12 April 2007 to 23 November 2009
Stuart James	Wolters Kluwer NV	Since 26 April 2006
	Pulse Health Limited	Since 7 November 2007
	Prime Financial Group Limited	Since 16 May 2006
	Progen Limited	Since 1 July 2009
	Greencross Limited	Since 30 October 2009

COMPANY SECRETARY

Mourice Garbutt FCIS, Honorary Justice of the Peace in Victoria

Mr Garbutt, through his professional corporate secretarial and compliance service company, provides secretarial, clerical and corporate governance support to client companies in Australia many of which are listed on the ASX Limited. Fees are charged on normal commercial terms.

PRINCIPAL ACTIVITIES

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

Directors' Report (continued)

OPERATING AND FINANCIAL REVIEW

At the end of December 2011, the company held $27.2 million in cash and cash equivalents. Closing cash was significantly higher than the amount held at December 2010 of $2.7 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. A further $27.2 million gross was raised from October to December 2011 through the issue of 193.97 million shares via private placements and a share purchase plan. 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 the continued product rollout of its cosmetic range, including its anti-cellulite cream.

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Directors' Report (continued)

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FUTURE DEVELOPMENTS

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.

ENVIRONMENTAL REGULATIONS

The Company is registered with relevant authorities to use certain compounds in the manufacture of goods. All waste chemicals are disposed of using accredited service providers with notification to the relevant authorities.

DIVIDENDS

The Directors have not recommended the payment of any dividends and no dividends were declared, paid or reinvested in the year to 31 December 2011.

Directors' Report (continued)

SHARE OPTIONS

Share options convertible to ordinary shares on issue at at the date of this report.

Issuing entity	Australian stock exchange listed	shares under option No.	Class of shares	Exercise price $	Expiry date
Phosphagenics Ltd	unquoted	1,100,000	Ordinary	$0.26	06 June 2012
Phosphagenics Ltd	unquoted	5,000,000	Ordinary	$0.14	31 Mar 2013
Phosphagenics Ltd	unquoted	1,450,000	Ordinary	$0.15	17 Aug 2013
Phosphagenics Ltd	unquoted	1,000,000	Ordinary	$0.15	14 May 2014
Phosphagenics Ltd	unquoted	1,950,000	Ordinary	$0.15	17 June 2014
Phosphagenics Ltd	unquoted	2,650,000	Ordinary	$0.13	30 June 2018
Total		**13,150,000**			

The holders of share options do not have voting rights or ability to participate in any share or rights issue. Since the end of the financial year no options have been issued or exercised.

ROUNDING OF AMOUNTS

The amounts contained in this report and in the financial report have been rounded to the nearest $1,000 (where rounding is applicable and where noted ($'000)), under the option available to the company under ASIC Class Order 98/0100. The company is an entity to which the Class Order applies.

INDEMNIFICATION OF OFFICERS AND AUDITORS

During the financial year, the Company paid a premium in respect of a contract insuring its Directors and Officers against a liability, other than a wilful breach of duty, of a nature that is required to be disclosed under section 300(8) of the *Corporations Act 2001*. In accordance with section 300(9) of the *Corporations Act 2001*, further details have not been disclosed due to confidentiality provisions contained in the insurance contract.

DIRECTORS' MEETINGS

The number of meetings of directors (including meetings of committees of directors) held during the year and the number of meetings attended by each director were as follows:

Directors	Board of Directors		Share Allotment committee		Audit, Compliance and Corporate Governance committee	
	Held	Attended	Held	Attended	Held	Attended
Non-executive directors						
Addison, J L	8	8	-	-	5	5
Clarke, D	8	8	-	-	5	5
James, S	8	8	-	-	5	4
Webb, S	8	8	-	-	5	5
Executive directors						
Rosen, H	8	8	-	-	-	-
Ogru, E	8	8	-	-	-	-

(i) During the year allotments of shares were carried out by resolutions of the Board of Directors

(ii) The Audit, Compliance and Corporate Governance Committee has also been mandated by the Board of Directors to carry out the functions of a Remuneration Committee

Directors' Report (continued)

Committee Membership

For all committees, any two Directors constitutes a quorum. All Directors are eligible to sit on the share allotment committee. The Audit, Compliance and Corporate Governance committee comprises of Independent Directors; D Clarke (chairman), J L Addison, S James and S Webb. Mr Clarke was appointed chairman in August 2010 and continues to remain in this role

Directors Shareholdings

During the reporting period 9,957 shares were issued by the Company to directors at 14 cents per share under a Share Purchase Plan. During the reporting period 5,800,000 rights were awarded to directors under the Employee Conditional Rights Scheme. As at the date of this report, the interests of the directors in the shares and options of Phosphagenics Limited were:

Directors	Number of ordinary shares	Number of rights over ordinary shares	Number of options over ordinary shares
Non-executive directors			
Addison, J L	22,473	750,000	-
Clarke, D	35,484	350,000	-
James, S	-	350,000	2,400,000
Webb, S	111,000	350,000	-
Executive directors			
Rosen, H	64,226,436	2,000,000	-
Ogru, E	5,711,610	2,000,000	-
Total	**70,107,003**	**5,800,000**	**2,400,000**

The number of rights held by directors, as shown above, are those Performance Rights as approved by shareholders at the 2011 Annual General Meeting ("AGM") per the terms of the Employee Conditional Rights Scheme as established by shareholders at the AGM – refer notes below on Remuneration Report for details of the terms and milestones.

The number of existing non-quoted options over unissued ordinary shares as acquired by Mr James by way of an off-market transaction on 30 June 2011,at a cost of $0.035 each, have an exercise price of $0.142 each and expire on 31 March 2013.

Directors' Report (continued)

REMUNERATION REPORT (AUDITED)

This remuneration report for the year ended 31 December 2011 outlines the remuneration arrangements of the Company and the Group in accordance with the requirements of the *Corporations Act 2001* (the Act) and its regulations. This information has been audited as required by section 308(3C) of the Act.

For the purposes of this report, key management personnel (KMP) of the Group are defined as those persons having authority and responsibility for planning, directing and controlling the major activities of the Company and the Group, directly or indirectly, including any director (whether executive or otherwise) of the parent company, and includes the seven executives in the Group receiving the highest remuneration.

Details of Key Management Personnel	Position
Non-executive directors	
Addison, J L	Chairman and Independent Director
Clarke, D	Independent Director
James, S	Independent Director
Webb, S	Independent Director
Executive directors	
Rosen, H	President and Chief Executive Officer
Ogru, E	Joint Chief Executive Officer
Other Key management personnel	
Banti, F	President Phosphagenics Inc, (resigned 29 July 2011)
Gavin, P	Vice President - R&D
Arnott, A	Chief Financial Officer
Butala, D	Vice President – Bioanalytical & CMC
Harrison, K	IP Manager
Kyriakou, K	General Manager – Personal Care
Libinaki, R	Vice President - Nutraceuticals

There were no other changes to KMP after the reporting date and before the date the financial report was authorised for issue.

Remuneration Committee

The remuneration committee, part of the Audit, Compliance and Corporate Governance committee, is responsible for determining and reviewing remuneration arrangements for the directors and executives. The Remuneration Committee assesses the appropriateness of the nature and amount of remuneration of executives on a periodic basis by reference to relevant employment market conditions with the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality, high performing director and executive team.

Remuneration Principles and Strategies

The performance of the Company depends upon the quality of its directors and executives. Attempts to prosper include attracting, motivating and retaining highly skilled directors and executives. The broad remuneration philosophy is to ensure a remuneration package properly reflects the person’s duties and responsibilities and that remuneration is competitive in attracting, retaining and motivating people of the highest quality.

In accordance with best practice corporate governance, the structure of non-executive director and executive remuneration is separate and distinct.

Directors' Report (continued)

Non executive director remuneration

Objective
The board seeks to set aggregate remuneration at a level that provides the Company with the ability to attract and retain directors of the highest calibre, whilst incurring a cost that is acceptable to shareholders.

Structure
The constitution and the ASX listing rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. The latest determination was at the annual general meeting held on 29 January 2004 when shareholders approved an aggregate remuneration of $300,000 per year.

The amount of aggregate remuneration sought to be approved by shareholders and the fee structure is reviewed periodically. The board considers advice from external consultants as well as the fees paid to non-executive directors of comparable companies when undertaking the annual review process. A review was conducted in February 2012 resulting in a 10.5% increase to remuneration of non-executive directors, effective 1 March 2012.

From 1 March 2012 each non-executive director receives a base fee of $42,000 (previously $38,000) for being a director of the Group. The non-executive directors do not receive retirement benefits, nor do they participate in any short term incentive programs. The remuneration of non-executive directors for the period ending 31 December 2011 and 31 December 2010 is detailed in the tables within this report.

Executive remuneration

Objective
The Group aims to reward executives with a level and mix of remuneration commensurate with their position and responsibilities so as to align the interests of executives with those of shareholders to retain executives at the Company to ensure that total remuneration is competitive by market standards.

Structure
In determining the level and make-up of executive remuneration, the board engages external consultants as needed to provide independent advice. The process consists of a review of company and individual performance, relevant comparative remuneration in the market and internally, and where appropriate, external advice on policies and practices.

Remuneration packages contain the following key elements:

- Fixed remuneration (base salary, superannuation and non-monetary benefits).
- Variable remuneration long term incentive (rights issued under the Employee Conditional Rights Scheme (ECRS) and previously under the Employee Share Option Plan (ESOP))

Executive directors' remuneration was reviewed in December 2011 resulting in a 23% increase for Dr Esra Ogru commencing in January 2012, with no change to Mr Harry Rosen's remuneration. Additionally, in June 2011, the Remuneration Committee approved and paid a short term cash bonus to Dr Esra Ogru.

Fixed remuneration

Objective
Fixed remuneration is reviewed annually by the board of directors. The process consists of a review of company and individual performance, relevant comparative remuneration externally and internally and, where appropriate, external advice on policies and practices. As noted above, the committee has access to external advice independent of management.

Structure
Executives are given the opportunity to receive their fixed (primary) remuneration in a variety of forms including cash and fringe benefits such as motor vehicles. It is intended that the manner of payment chosen will be optimal for the recipient without creating undue cost for the Group. Apart from termination benefits which accrue under statute such as unpaid annual leave, long service leave and superannuation benefits, there are no post employment retirement benefits.

Directors' Report (continued)

Variable remuneration long term incentive plan

Objective

The objective of the long term incentive plan is to reward staff in a manner that aligns remuneration with the creation of shareholder wealth and to ensure that all staff, including executives, views their relationship with the Group as a long-term one. As such the long term incentive plan has been offered to all staff who meet the minimum service criteria.

Structure

Employee Share Option Plan

The long term incentive plan grants to executives are delivered in the form of share options under the Employee Share Option Plan (ESOP). The share options will vest over differing periods depending on the offer conditions, with no opportunity to retest. Executives are able to exercise the share options after vesting and before the options lapse.

Where a participant ceases employment prior to the vesting of their share options, the share options are forfeited unless cessation of employment is due to retirement or death. In the event of a change of control of the Group, the performance period end date will be brought forward to the date of the change of control and awards will vest over this shortened period.

Employee Conditional Rights Scheme

The ECRS allows eligible employees to be granted Performance Rights to acquire Shares at no cost. The purpose of the Scheme, and the performance conditions within, 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.

The Scheme will be administered by the Board, with all objectives, determinations, approvals or opinions made or given by the Board in its absolute discretion.

Under the terms of the ECRS, the rights will vest if certain non-market or market conditions are fulfilled. One of the key overriding conditions of the Scheme is that if the 10 day Volume Weighted Average Price is not less than $0.35 at any time prior to 31 December 2014, then 100% of the Performance Rights will vest. Alternatively, vesting of the Rights is conditional on Phosphagenics achieving the following conditions:

Milestone 1 (16.5% of Rights awarded if achieved by 30 Jun 2012) - Completion of recruitment for the clinical trial of the Oxycodone patch, Submission of an IND for the Oxycodone patch, and gross revenues from global sales of all non-prescription products of the Company of not less than $10 million.

Milestone 2 (16.5% of Rights awarded if any two of the following achieved by 31 Dec 2013) - Completion of the clinical trial of the oxycodone patch on time and on budget and the Board determines to continue the development and commercialisation of the patch, gross revenues from the commercialisation of the Company's TPM technology for use in or in connection with dermatology products of not less than $1million, and gross revenues from global sales of all non-prescription products of the Company of not less than $20million.

Milestone 3 (34% of Rights awarded if any two of the following achieved by 31 Dec 2014) - Completion of all pivotal human clinical trials of the oxycodone patch, gross revenues from the commercialisation of the Company's TPM technology for use in or in connection with the dermatology products of not less than $2million, and gross revenues from global sales of all non-prescription products of the Company of not less than $30million

Milestone 4 (34% of Rights awarded if either of the following achieved by 31 Dec 2015) - NDA (or equivalent) registration of the oxycodone patch or commercial agreement for the marketing and sale of the oxycodone patch, or gross revenues from global sales of all non-prescription products of the Company of not less than A$40million.

The Groups current remuneration policies provide a significant degree of linkage between an executive's variable long term incentive remuneration and the overall financial performance of the Group. Given the position of the Group and its stage of development, the remuneration is aimed at retaining key individuals to ensure the success of current and future product development and successful commercialisation of products, which will in turn impact future profitability of the Group and shareholder wealth.

Directors' Report (continued)

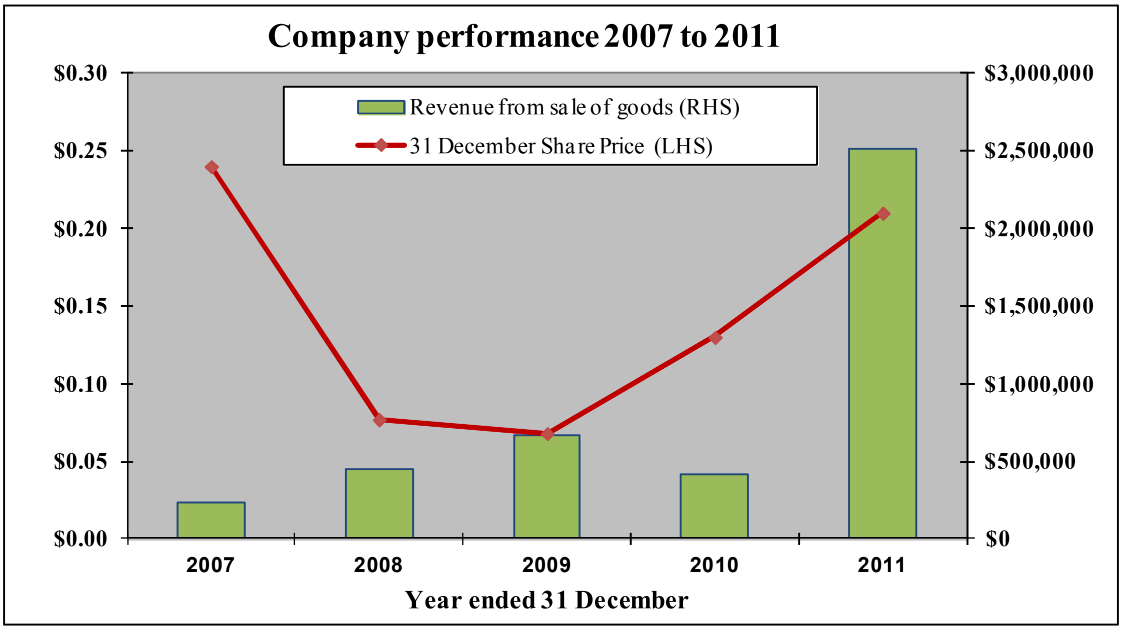
Employment contracts

No executives have fixed term contracts with the Group. The company or the executive may terminate employment by providing four weeks written notice. On termination, any long term incentive plan (ESOP) options or (ECRS) rights that have vested are available to be exercised. Any options or rights that have not yet vested will be forfeited. The company may terminate employment at any time without notice if serious misconduct has occurred. Where termination with cause occurs the executive is only entitled to that portion of remuneration that is fixed, and only up to the date of termination. On termination with cause, any unvested options or rights will immediately be forfeited.

Company performance and its link to long-term incentives

The financial performance measures driving long-term incentive vesting and payment outcomes are revenues from the sale of goods and Company share price. Because of the stage of the Company's development, earnings per share and other profitability based measures do not accurately reflect performance over the past five years.

The following chart shows Phosphagenics Limited's annual revenues from the sale of goods and year end share price over the five-year period from 1 January 2007 to 31 December 2011.



Options granted during the year to key management personnel

No options were awarded during the year to key management personnel and no options vested during the year.

Performance Rights granted during the year to key management personnel

9,750,000 ECRS Rights were awarded to key management personnel during the year, of which nil vested.

Remuneration of key management personnel

Aggregates	2011 $	2010 $
Short-Term Benefits	1,568,076	1,482,034
Post-Employment	115,125	108,968
Share Based Payment	95,119	-
Termination	275,742	-
Totals	**2,054,062**	**1,591,002**

Directors' Report (continued)

Remuneration of key management personnel (continued)

2011	Short – Term		Post-Employment	Share Based Payment	Termination Benefits	Total	Performance Related
	Salary & Fees	Cash Bonus	Superannuation	Performance Rights			
	$	$	$	$	$	$	%
Non-executive directors							
Addison, J L	34,862	-	3,138	9,575	-	47,575	20.1%
Clarke, D	34,580	-	3,112	4,455	-	42,147	10.6%
James, S	34,580	-	3,112	4,455	-	42,147	10.6%
Webb, S	34,580	-	3,112	4,455	-	42,147	10.6%
Executive directors							
Rosen, H	271,765	-	24,459	25,455	-	321,679	7.9%
Ogru, E *	222,703	50,000	20,043	25,455	-	318,201	23.7%
Other Key management personnel							
Banti, F **	146,383	-	-	-	275,742	422,125	-
Gavin, P	135,433	-	12,189	5,385	-	153,007	3.5%
Arnott, A ***	92,520	-	-	1,077	-	93,597	1.2%
Butala, D	140,254	-	12,623	5,385	-	158,262	3.4%
Harrison, K	117,783	-	10,600	2,692	-	131,075	2.1%
Kyriakou, K	123,960	-	11,156	4,038	-	139,154	2.9%
Libinaki, R	128,673	-	11,581	2,692	-	142,946	1.9%
Totals	**1,518,076**	**50,000**	**115,125**	**95,119**	**275,742**	**2,054,062**	

* E Ogru was paid a once off cash bonus in June 2011 in recognition of outstanding performance during the previous 12 month period.
** F Banti resigned on 29 July 2011
*** A Arnott is employed under contract, with no fixed period. Either party may terminate the agreement at any time by giving the other party 14 days notice in writing.

Directors' Report (continued)

Remuneration of key management personnel (continued)

2010	Short – Term		Post-Employment	Total	Performance Related
	Salary & Fees	Cash Bonus	Superannuation		
	$	$	$	$	%
Non-executive directors					
Vizard, A L	29,052	-	2,615	31,667	-
Addison, J L	34,862	-	3,138	38,000	-
Mills, J	23,242	-	2,092	25,334	-
Ashton, M R D	25,756	-	-	25,756	-
Clarke, D	11,527	-	1,037	12,564	-
James, S	11,527	-	1,037	12,564	-
Webb, S	11,527	-	1,037	12,564	-
Executive directors					
Rosen, H	284,909	-	22,706	307,615	-
Ogru, E	222,701	-	19,506	242,207	-
Other Key management personnel					
Banti, F	185,576	-	-	185,576	-
Hodges, A	95,547	-	8,599	104,146	-
Gavin, P	125,229	-	11,271	136,500	-
Arnott, A	21,360	-	-	21,360	-
Butala, D	136,500	-	12,285	148,785	-
Harrison, K	79,511	-	7,156	86,667	-
Kyriakou, K	110,000	-	9,900	119,900	-
Libinaki, R	73,208	-	6,589	79,797	-
Totals	**1,482,034**	**-**	**108,968**	**1,591,002**	**-**

Directors' Report (continued)

Option holdings of key management personnel

2011	01 Jan 11 Balance No.	Award Date	Fair value per option at award Date	Exercise Price	Expiry Date	Net other change No.	31 Dec 11 Balance No.	Vested No.
Non Executive Directors								
Addison, J.L	-	-	-	-	-	-	-	-
Clarke, D	-	-	-	-	-	-	-	-
James, S	-	-	-	-	-	2,400,000	2,400,000	2,400,000
Webb, S	-	-	-	-	-	-	-	-
Executive Directors								
Rosen, H	-	-	-	-	-	-	-	-
Ogru, E	-	-	-	-	-	-	-	-
Key Management Personnel								
Banti, F [1]	2,650,000	1-Jul-08	$0.096	0.13	30-Jun-18	(2,650,000)	-	-
Gavin, P	400,000	22-May-06	$0.091	0.23	22-May-11	(400,000)	-	-
	100,000	18-Aug-08	$0.053	0.15	17-Aug-13	-	100,000	100,000
	300,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	300,000	300,000
Arnott, A	-	-	-	-	-	-	-	-
Butala, D	250,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	250,000	250,000
Harrison, K	-	-	-	-	-	-	-	-
Kyriakou, K	-	-	-	-	-	-	-	-
Libinaki, R	400,000	22-May-06	$0.091	0.23	22-May-11	(400,000)	-	-
	100,000	18-Aug-08	$0.053	0.15	17-Aug-13	-	100,000	100,000
	150,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	150,000	150,000
Totals	**4,350,000**	-	-	-	-	**(1,050,000)**	**3,300,000**	**3,300,000**

1. F Banti is no longer a key management personnel due to his resignation on 29 July 2011, although his options remain exercisable

2010	01 Jan 11 Balance No.	Award Date	Fair value per option at award Date	Exercise Price	Expiry Date	Net other change No.	31 Dec 11 Balance No.	Vested No.
Non Executive Directors								
Addison, J.L	-	-	-	-	-	-	-	-
Clarke, D	-	-	-	-	-	-	-	-
James, S	-	-	-	-	-	-	-	-
Webb, S	-	-	-	-	-	-	-	-
Executive Directors								
Rosen, H	-	-	-	-	-	-	-	-
Ogru, E	-	-	-	-	-	-	-	-
Key Management Personnel								
Banti, F	2,650,000	1-Jul-08	$0.096	0.13	30-Jun-18	-	2,650,000	2,650,000
Hodges A [1]	300,000	18-Aug-08	$0.053	0.15	17-Aug-13	(300,000)	-	-
	300,000	18-Jun-09	$0.095	0.15	17-Jun-14	(300,000)	-	-
Gavin, P	400,000	22-May-06	$0.091	0.23	22-May-11	-	400,000	400,000
	100,000	18-Aug-08	$0.053	0.15	17-Aug-13	-	100,000	100,000
	300,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	300,000	300,000
Arnott, A	-	-	-	-	-	-	-	-
Butala, D	250,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	250,000	250,000
Harrison, K	-	-	-	-	-	-	-	-
Kyriakou, K	-	-	-	-	-	-	-	-
Libinaki, R	400,000	22-May-06	$0.091	0.23	22-May-11	-	400,000	400,000
	100,000	18-Aug-08	$0.053	0.15	17-Aug-13	-	100,000	100,000
	150,000	18-Jun-09	$0.095	0.15	17-Jun-14	-	150,000	150,000
Totals	**4,950,000**	-	-	-	-	**(600,000)**	**4,350,000**	**4,350,000**

Directors' Report (continued)

Option holdings of key management personnel *(continued)*

1. A Hodges options lapsed upon his resignation on 29th July 2010.

All options granted to key management personnel have been issued in accordance with the provisions of the Employee Share Option Plan (ESOP).

Performance Rights holdings of key management personnel

2011	01 Jan 11 Balance No.	Award date	Performance Rights awarded during the year No.	Fair value per performance right at award date	31 Dec 11 Balance No.	Not Vested No.	% of Remuneration consisting of Performance rights
Non Executive Directors							
Addison, J.L	-	1-May 2011	750,000	$0.07	750,000	750,000	20.1%
Clarke, D	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
James, S	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
Webb, S	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
Executive Directors							
Rosen, H	-	1-May 2011	2,000,000	$0.07	2,000,000	2,000,000	7.9%
Ogru, E	-	1-May 2011	2,000,000	$0.07	2,000,000	2,000,000	8.0%
Key Management Personnel							
Banti, F	-	-	-	-	-	-	-
Gavin, P	-	3-Oct-2011	1,000,000	$0.07	1,000,000	1,000,000	3.5%
Arnott, A	-	3-Oct-2011	200,000	$0.07	200,000	200,000	1.2%
Butala, D	-	3-Oct-2011	1,000,000	$0.07	1,000,000	1,000,000	3.4%
Harrison, K	-	3-Oct-2011	500,000	$0.07	500,000	500,000	2.1%
Kyriakou, K	-	3-Oct-2011	750,000	$0.07	750,000	750,000	2.9%
Libinaki, R	-	3-Oct-2011	500,000	$0.07	500,000	500,000	1.9%
Totals	**-**		**9,750,000**	**-**	**9,750,000**	**9,750,000**	

All performance rights granted to key management personnel have been issued in accordance with the provisions of the Employee Conditional Rights Scheme (ECRS).

No performance rights have lapsed during the year.

No performance rights vested or were exercised during the year.

No performance rights were issued prior to 1 January 2011.

All performance rights expire on 30 June 2016.

Directors' Report (continued)

Shareholdings of Key Management Personnel

2011	01 Jan 11 Balance No.	Granted as remuneration No.	Net other change No.	31 Dec 11 Balance No.
Non Executive Directors				
Addison, J.L	19,000	-	3,473	22,473
Clarke, D	30,000	-	5,484	35,484
James, S	-	-	-	-
Webb, S	110,000	-	1,000	111,000
Executive Directors				
Rosen, H	64,226,436	-	-	64,226,436
Ogru, E	5,711,610	-	-	5,711,610
Key Management Personnel				
Banti, F	-	-	-	-
Gavin, P	99,000	-	-	99,000
Arnott, A	-	-	-	-
Butala, D	-	-	-	-
Harrison, K	-	-	-	-
Kyriakou, K	-	-	-	-
Libinaki, R	344,451	-	-	344,451
Totals	**70,540,497**	**-**	**9,957**	**70,550,454**

2010	01 Jan 10 Balance No.	Granted as remuneration No.	Net other change No.	31 Dec 10 Balance No.
Non Executive Directors				
Vizard, A.L	177,758	-	(177,758)	-
Addison, J.L	19,000	-	-	19,000
Mills, J	694,057	-	(694,057)	-
Ashton, M R D	263,043	-	(263,043)	-
Clarke, D	-	-	30,000	30,000
James, S	-	-	-	-
Webb, S	-	-	110,000	110,000
Executive Directors				
Rosen, H	64,226,436	-	-	64,226,436
Ogru, E	5,711,610	-	-	5,711,610
Key Management Personnel				
Banti, F	-	-	-	-
Hodges, A	52,420	-	(52,420)	-
Gavin, P	99,000	-	-	99,000
Arnott, A	-	-	-	-
Butala, D	-	-	-	-
Harrison, K	-	-	-	-
Kyriakou, K	-	-	-	-
Libinaki, R	344,451	-	-	344,451
Totals	**71,587,775**	**-**	**(1,047,278)**	**70,540,497**

Directors' Report (continued)

NON-AUDIT SERVICES

The Directors are satisfied that the provision of non-audit services, during the year, by the auditor (or by another person or firm on the auditor's behalf) is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. Details of amounts paid or payable to the auditor for non-audit services provided during the year by the auditor are outlined in note 6 to the financial statements.

AUDITOR'S INDEPENDENCE DECLARATION

The auditor's independence declaration is included on page 19 of the financial report.

CHANGES IN STATE OF AFFAIRS

During the financial year there was no significant change in the state of affairs of the consolidated entity other than that referred to in the financial statements or notes thereto.

SUBSEQUENT EVENTS

There has not been any matter or circumstance, other than that referred to in the financial statements or 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.

Signed in accordance with a resolution of the Directors made pursuant to s.298(2) of the *Corporations Act 2001*.

Jonathan Lancelot Addison
Chairman

21 February 2012
Melbourne

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Auditor's Independence Declaration to the Directors of Phosphagenics Limited

In relation to our audit of the financial report of Phosphagenics Limited for the financial year ended 31 December 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.

Ernst & Young

Ernst & Young

David Petersen
Partner
21 February 2012

Corporate Governance Statement

CORPORATE GOVERNANCE PRACTICES AND CONDUCT

The board of directors of Phosphagenics Limited is responsible for establishing the corporate governance framework of the Group having regard to the ASX Corporate Governance Council (CGC) published guidelines as well as its corporate governance principles and recommendations. The board guides and monitors the business and affairs of Phosphagenics Limited on behalf of the shareholders by whom they are elected and to whom they are accountable.

The table below summarises the Company's compliance with the CGS's recommendations.

Principle	Recommendation	Comply Yes/No	Reference/ explanation	ASX Listing Rule/ Recommendation
1	**Lay solid foundations for management and oversight**			
1.1	Companies should establish the functions reserved to the board and those delegated to senior executives and disclose those functions.	Yes	Page 21	*ASX LR 1.1*
1.2	Companies should disclose the process for evaluating the performance of senior executives.	Yes	Page 22	*ASX LR 1.2*
1.3	Companies should provide the information indicated in the guide to reporting on Principle 1.	Yes		*ASX LR 1.3*
2	**Structure the board to add value**			
2.1	A majority of the board should be independent directors.	Yes	Page 21	*ASX LR 2.1*
2.2	The chair should be an independent director.	Yes	Page 21	*ASX LR 2.2*
2.3	The roles of chair and chief executive officer should not be exercised by the same individual.	Yes	Page 21	*ASX LR 2.3*
2.4	The board should establish a nomination committee.	No	Page 22	*ASX LR 2.4*
2.5	Companies should disclose the process for evaluating the performance of the board, its committees and individual directors.	Yes	Page 11, 23	*ASX LR 2.5*
2.6	Companies should provide the information indicated in the guide to reporting on Principle 2.	Yes		*ASX LR 2.6*
3	**Promote ethical and responsible decision-making**			
3.1	Companies should establish a code of conduct and disclose the code or a summary of the code as to: ► The practices necessary to maintain confidence in the company's integrity. ► The practices necessary to take into account their legal obligations and the reasonable expectations of their stakeholders. ► The responsibility and accountability of individuals for reporting and investigating reports of unethical practices.	Yes	Website	*ASX CGC 3.1*
3.2	Companies should establish a policy concerning diversity and disclose the policy or a summary of that policy. The policy should include requirements for the board to establish measurable objectives for achieving gender diversity for the board to assess annually both the objectives and progress in achieving them.	Yes	Website	*ASX CGC 3.2*
3.3	Companies should disclose in each annual report the measurable objectives for achieving gender diversity set by the board in accordance with the diversity policy and progress towards achieving them.	Yes	Page 27	*ASX CGC 3.3*
3.4	Companies should disclose in each annual report the proportion of women employees in the whole organisation, women in senior executives positions and women on the board.	Yes	Page 27	*ASX CGC 3.4*
3.5	Companies should provide the information indicated in the guide to reporting on Principle 3	Yes		*ASX LR 3.5*

Principle	Recommendation	Comply Yes/No	Reference/ explanation	ASX Listing Rule/ Recommendation
4	**Safeguard integrity in financial reporting**			
4.1	The board should establish an audit committee.	Yes	Page 23	*ASX LR 4.1*
4.2	The audit committee should be structured so that it: - Consists only of non-executive directors - Has at least three members - Consists of a majority of independent directors - Is chaired by an independent chair, who is not chair of the board	Yes	Page 23	*ASX LR 4.2* *ASX LR 12.7*
4.3	The audit committee should have a formal charter.	Yes	Page 23	*ASX LR 4.3*
4.4	Companies should provide the information indicated in the Guide to reporting on Principle 4.	Yes		*ASX LR 4.4*
5	**Make timely and balanced disclosure**			
5.1	Companies should establish written policies designed to ensure compliance with ASX listing rule disclosure requirements and to ensure accountability at a senior executive level for that compliance and disclose those policies or a summary of those policies.	Yes	Page 23	*ASX LR 5.1*
5.2	Companies should provide the information indicated in the guide to reporting on Principle 5.	Yes		*ASX LR 5.2*
6	**Respect the rights of shareholders**			
6.1	Companies should design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose their policy or a summary of that policy.	Yes	Page 25	*ASX LR 6.1*
6.2	Companies should provide the information indicated in the guide to reporting on Principle 6.	Yes		*ASX LR 6.2*
7	**Recognise and manage risk**			
7.1	Companies should establish policies for the oversight and management of material business risks and disclose a summary of those policies.	Yes	Page 25	*ASX LR 7.1*
7.2	The board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The board should disclose that management has reported to it as to the effectiveness of the company's management of its material business risks	Yes	Page 24 & 25	*ASX LR 7.2*
7.3	The board should disclose whether it has received assurance from the chief executive officer [or equivalent) and the chief financial officer [or equivalent] that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.	Yes	Page 25	*ASX LR 7.3*
7.4	Companies should provide the information indicated in the guide to reporting on Principle 7.	Yes		*ASX LR 7.4*
8	**Remunerate fairly and responsibly**			
8.1	The board should establish a remuneration committee.	Yes	Page 27	*ASX LR 8.1*
8.2	The remuneration committee should be structured so that it consists of a majority of independent directors, is chaired by an independent chair, and has at least three members.	Yes	Page	
8.3	Companies should clearly distinguish the structure of nonexecutive directors' remuneration from that of executive directors and senior executives.	Yes	Page 10 & 27	*ASX LR 8.2*
8.4	Companies should provide the information indicated in the Guide to reporting on Principle 8.	Yes		*ASX LR 8.3*

Corporate Governance Statement (continued)

The Companies corporate governance practices were in place throughout the year ended 31 December 2011.

Board functions

The board seeks to identify the expectations of the shareholders, as well as other regulatory and ethical expectations and obligations. In addition, the board is responsible for identifying areas of significant business risk and ensuring arrangements are in place to adequately manage those risks. To ensure that the board is well equipped to discharge its responsibilities it has established guidelines for the nomination and selection of directors and for the operation of the board. The responsibility for the operation and administration of the Group is delegated, by the board, to the Chief Executive Officer and the executive management team. The board ensures that this team is appropriately qualified and experienced to discharge their responsibilities and has in place procedures to assess the performance of the Chief Executive Officer and the executive management team. Whilst at all times the board retains full responsibility for guiding and monitoring the Group, in discharging its stewardship it makes use of sub-committees. Specialist committees are able to focus on a particular responsibility and provide informed feedback to the board. To this end the board has established Share Allotment and Audit, Compliance and Corporate Governance Committees.

The Directors in office at the date of this statement, their skills, experience, expertise and period of directorship are detailed in the Directors' Report. In respect of the attendance at Board and Committee Meetings, shareholders are referred to the table of Meeting Attendance contained on page 7.

Structure of the Board

The skills, experience and expertise relevant to the position of director held by each director in office at the date of the annual report are included in the directors' report. Directors of Phosphagenics Limited are considered to be independent when they are independent of management and free from any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement.

In the context of director independence, "materiality" is considered from both the Group and individual director perspective. The determination of materiality requires consideration of both quantitative and qualitative elements. An item is presumed to be quantitatively immaterial if it is equal to or less than 5% of the appropriate base amount. It is presumed to be material (unless there is qualitative evidence to the contrary) if it is equal to or greater than 10% of the appropriate base amount. Qualitative factors considered include whether a relationship is strategically important, the competitive landscape, the nature of the relationship and the contractual or other arrangements governing it and other factors that point to the actual ability of the director in question to shape the direction of the Group's loyalty.

In accordance with the definition of independence above, and the materiality thresholds set, the following directors of Phosphagenics Limited are considered to have the following status:

Name	Position and status	Term in Office
Non-executive directors		
Addison, J L	Chairman and Independent Director	9 years
Clarke, D	Independent Director	1.5 years
James, S	Independent Director	1.5 years
Webb, S	Independent Director	1.5 years
Executive directors		
Rosen, H	Chief Executive Officer	12 years
Ogru, E	Joint Chief Executive Officer	6 years

The board recognises the Corporate Governance Council's recommendation that the Chair should be an independent director.

Corporate Governance Statement (continued)

Composition of the Board

The Company's Constitution provides for the appointment of a minimum of three Directors and up to a maximum of eight. At the date of this report, the Company has six Directors comprising two Executive and four Non-Executive Directors. The Chairman of the Board and the Chairman of the Board's Committees' are Non-Executive Directors.

In February 2011 the Board of Directors undertook a review of the status of each Director and reached the opinion that each current Director, apart from Mr Rosen and Dr Ogru, could be classified as a Non-Executive Director. In addition, this assessment has concluded, Mr Addison, Mr Clarke, Mr James, and Ms Webb qualified as Independent Directors. A further review was undertaken in February 2012 and the Board of Directors reached the opinion that status of each director has not changed since February 2011.

Board Responsibilities

The responsibility for the operation and administration of the Company is delegated by the Board to the specifically identified outsourced service providers. The Board ensures that this team of service providers is appropriately qualified and experienced to discharge their responsibilities and has in place procedures to assess their performance.

The Board is responsible for ensuring that management's objectives and activities are aligned with the expectations and risks identified by the Board. The Board has a number of mechanisms in place to ensure this is achieved. In addition to the establishment of specific committees referred in this statement, these mechanisms include the following:

- Implementation of operating plans and budgets by management and Board monitoring of progress against budget – this includes the establishment and monitoring of key performance indicators (both financial and non-financial) for all significant business processes;
- Procedures to allow Directors, in the furtherance of their duties, to seek independent professional advice at the company's expense;
- The review and approval of acquisitions and disposals of businesses and assets, and the approval of contracts and financing arrangements within defined limits; and
- The appointment of an outsourced service provider, which is responsible for managing the Company's public image and communication with shareholders.

In conjunction with an ongoing review of the Board Charter, the Board will consider its responsibilities and delegated authorities to ensure they comply with best practice corporate governance.

Nomination and Membership

Subject to the provisions of the Company's Constitution, Board composition and selection criteria for Directors are addressed by the full Board. Accordingly, a Nomination and Membership Committee has not been established.

The Constitution provides for events whereby Directors may be removed from the Board. Similarly shareholders have the ability to nominate, appoint and remove Directors. The Constitution also provides for the regular rotation of Directors, which ensures that Directors seek re-election by shareholders at least once every three years.

Independent Professional Advice

Directors, in carrying out their duties as Directors or as members of Board Committees, may, after prior consultation with the Chairman, seek independent professional advice at the expense of the Company. If appropriate, such advice will be available to all Directors.

Corporate Governance Statement (continued)

Timely and Balanced Disclosure

The Board of Directors has established written policies and procedures designed to ensure compliance and at each meeting of the Board of Directors and specifically monitors the Company's activities and disclosures. On average there are between six and ten Board meetings a year. The Board of Directors has endorsed the principles of best corporate governance practice as set out by the Council.

Performance

The performance of the board and key executives is reviewed periodically against both measurable and qualitative indicators. The performance criteria against which directors and executives are assessed are aligned with the financial and non-financial objectives of Phosphagenics Limited.

Trading Policy

A Company Share Trading policy was adopted by the Board of Directors in May 2010 and amended by a resolution of directors in December 2010. Under the Company's Share Trading Policy, an executive or director must not trade in any securities of the Company at any time when they are in possession of unpublished, price-sensitive information in relation to those securities; during a blackout period or outside the Executive Trading Windows period without the permission of the Approving Officer. The Directors are permitted to deal in securities in which they have a relevant interest without restriction for any period other than the last day in each half or full year reporting period until six weeks after the release to the ASX of the announcements by the Company of its full year or half year results and six weeks after the date of the Company's annual general meeting. Directors are required to wait at least two business days after the release of any market sensitive announcement by the Company so that the market has had time to absorb the information.

As required by the ASX listing rules, the Company notifies the ASX of any transaction conducted by directors in the securities of the Company.

Board of Directors and its Committees

The Board of Directors is responsible for the overall governance of the Company inclusive of its strategic development and the direction and the control of operations of the Company. Whilst the Board retains overall responsibility, it has established certain committees to assist in carrying out its responsibilities. Such committees include the audit, compliance and corporate governance committee and the share allotment committee.

Audit, Compliance and Corporate Governance Committee

It is the board's responsibility to ensure that an effective internal control framework exists within the entity. This includes internal controls to deal with both the effectiveness and efficiency of significant business processes, the safeguarding of assets, the maintenance of proper accounting records, and the reliability of financial information as well as non-financial considerations such as the benchmarking of operational key performance indicators.

The board has delegated responsibility for establishing and maintaining a framework of internal control and ethical standards to the audit, compliance and corporate governance committee. The committee also provides the board with additional assurance regarding the reliability of financial information. A committee charter has been approved by the board.

The committee, as at the date of this statement, comprises four Non-Executive Independent Directors; Mr D Clarke (Chairman), Mr J Addison, Mr S James and Dr S Webb. The Company's Auditors are invited to attend meetings and to participate in committee discussions. The Group CFO and Company Secretary attends committee meetings.

Corporate Governance Statement (continued)

The duties of the Committee include:

- The review of the Audit Programme and all matters relevant to the financial affairs of the Company's activities together with the production of Statutory Financial Reports inclusive of the Reports and Declarations by Directors.
- To review and advise on procedures in place to record the Company's activities and to ensure the safety of the Company's records and assets.
- To review Internal Control Procedures and the Auditor's Management letter.
- To review the half-yearly and yearly reports to the ASX Limited together with a review of the scope and quality of the annual statutory audit and the half-year audit review.
- To monitor Compliance with the provisions of the *Corporations Act 2001*, Australian Securities and Investment Commission guidelines and practice notes, ASX Listing Rules, taxation requirements and all regulatory bodies.
- Carry out the functions of the Remuneration Committee.
- Group Risk management

Share Allotment Committee

Any two Directors will constitute a quorum for this committee, which deals with the allotment of new shares or grant or exercise of options.

Internal Control Framework and Ethical Standards

The Board of Directors seeks to identify the expectations of shareholders as well as other regulatory and ethical expectations and obligations.

These matters are undertaken by the full Board together with the audit, compliance and corporate governance committee. In respect of the ethical standards, the full Board regularly discusses the maintenance by the Company of appropriate ethical standards in line with the Council’s recommendations.

Risk

The board acknowledges the Revised Supplementary Guidance to Principle 7 issued by the ASX in June 2008 and has continued its proactive approach to risk management. The identification and effective management of risk, including calculated risk-taking is viewed as an essential part of the company's approach to creating long-term shareholder value.

In recognition of this, the Board determines the company's risk profile and is responsible for overseeing and approving risk management strategy. The audit, compliance and corporate governance committee reviews policies, internal compliance and internal control.

The audit, compliance and corporate governance committee oversees the assessment of the effectiveness of risk management and internal compliance and control. The tasks of undertaking and assessing risk management and internal control effectiveness are delegated to management through the Chief Executive Officer and Chief Financial Officer, including responsibility for the day to day design and implementation of the company's risk management and internal control system.

Management reports to the audit, compliance and corporate governance committee on the company’s key risks and the extent to which it believes these risks are being adequately managed. The reporting on risk by management is a standing agenda item at monthly Board meetings.

Corporate Governance Statement (continued)

Business Risk

The main areas of business risk, which are considered on an ongoing basis by the Board are;

- Failure to develop commercial products from the company's research and development
- Ability to raise capital or generate free cash flow to fund future research and development activities
- Failure to market the company's products
- General economic factors including those affecting interest and exchange rates
- Changes in Corporations and Taxation Law

CEO and CFO certification

In accordance with section 295A of the *Corporations Act*, the Chief Executive Officer and Chief Financial Officer have provided a written statement to the board that:

- Their view provided on the Company's financial report is founded on a sound system of risk management and internal compliance and control which implements the financial policies adopted by the board
- The Company's risk management and internal compliance and control system is operating effectively in all material respects

The board agrees with the views of the ASX on this matter and notes that due to its nature, internal control assurance from the Chief Executive Officer and Chief Financial Officer can only be reasonable rather than absolute. This is due to such factors as the need for judgement, the use of testing on a sample basis, the inherent limitations in internal control and because much of the evidence available is persuasive rather than conclusive and therefore is not and cannot be designed to detect all weaknesses in control procedures. In response to this, internal control questions are required to be completed by the key management personnel in support of these written statements.

Remuneration

The Board is responsible for determining and reviewing compensation arrangements for the directors themselves, the Chief Executive Officer and executive team. A Compensation (Remuneration) Committee has not been separately established, rather the function is performed by the Audit, Compliance and Corporate Governance Committee.

It is the Company's objective to provide maximum stakeholder benefit from the retention of a high quality Board and executive team by remunerating directors and key executives fairly and appropriately with reference to relevant employment market conditions. For a full discussion of the Company's remuneration philosophy and framework and the remuneration received by directors and executives in the current period please refer to the remuneration report, which is contained within the directors' report.

Shareholder communication policy

Phosphagenics' objective is to promote effective communication with its shareholders at all times. Phosphagenics Limited is committed to:

- Ensuring that shareholders and the financial markets are provided with full and timely information about Phosphagenics' activities in a balanced and understandable way.
- Complying with continuous disclosure obligations contained in applicable the ASX listing rules and the *Corporations Act* in Australia.
- Communicating effectively with its shareholders and making it easier for shareholders to communicate with Phosphagenics Limited.

To promote effective communication with shareholders and encourage effective participation at general meetings, information is communicated to shareholders:

- Through the release of information to the market via the ASX
- Through the distribution of the annual report and Notices of Annual General Meeting
- Through shareholder meetings and investor relations presentations
- Through letters and other forms of communications directly to shareholders
- By posting relevant information on Phosphagenics website www.phosphagenics.com.

Corporate Governance Statement (continued)

The Company's website www.phosphagenics.com has a dedicated Investor Relations section for the purpose of publishing all important company information and relevant announcements made to the market. The Company has also established an e-mail directory for the direct distribution of announcements made to the ASX.

The external auditors are required to attend the Annual General Meeting and are available to answer any shareholder questions about the conduction of the audit and preparation of the audit report.

Annual Reports are provided to all share and option holders who have elected to receive the Report.

At the meetings of shareholders, Directors are subject to questioning by shareholders about the Directors' stewardship of the Company's affairs and it is shareholders who ultimately vote upon the financial statements and reports, the election of Directors, appointment of Auditors and any matters of Special Business.

Diversity

The Group recognises the value contributed to the organisation by employing people with varying skills, cultural backgrounds, ethnicity and experience. Phosphagenics believes its diverse workforce is the key to its continued growth, improved productivity and performance.

We actively value and embrace the diversity of our employees and are committed to creating an inclusive workplace where everyone is treated equally and fairly, and where discrimination, harassment and inequity are not tolerated. While Phosphagenics is committed to fostering diversity at all levels, gender diversity has been and continues to be a priority for the Group.

To this end, the Group supports and complies with the recommendations contained in the ASX *Corporate Governance Principles and Recommendations*. The Group has established a diversity policy outlining the board's measurable objectives for achieving diversity. This is assessed annually to measure the progress towards achieving those objectives. The diversity policy is available in the corporate governance section on the Group's website.

Broadly, the Groups measurable objectives are as follows:

- Phosphagenics' state and re-state where necessary that there are no forms of discrimination / bias in considering anyone for a position with the Group, i.e. on grounds of gender; age; physical appearance; origins; race; religion; marital status; sexual preference; pregnancy or likely pregnancy; political leanings; disabilities;
- All new appointments or promotion / career enhancement and remuneration be on the basis of merit and ability to carry out the work responsibilities;
- Within the broad ambit of ensuring that the Group's activities are best developed and to ensure harmony of working within the group that there be flexibility in working hours to enable domestic / private lives to allow for a balance between career and family obligations;
- Consideration be given to job sharing

The table below outlines the diversity within Phosphagenics Limited.

Level	Male		Female		Total
	Number	%	Number	%	
Board	4	67%	2	33%	6
Key Management personnel	3	50%	3	50%	6
Other staff	9	37%	15	63%	24
Total	16	44%	20	56%	36

Signed in accordance with a resolution of the Directors.

Jonathan Lancelot Addison
Chairman
21 February 2012
Melbourne

Consolidated statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2011	Note	2011 $'000	2010 $'000
Revenue			
Sale of goods		2,516	419
Licences	3a	228	4,386
Finance revenue		427	314
Total revenue		3,171	5,119
Cost of sales		(1,040)	(44)
Gross profit		2,131	5,075
Income from government grants	3b	1,236	161
Other income		143	187
Employee and Directors benefits expenses		(4,003)	(3,491)
Occupancy and communications expenses		(511)	(511)
Consulting and professional expenses		(933)	(1,412)
Administration expenses		(1,997)	(868)
Research expenses		(4,924)	(2,969)
Impairment of acquired intangible assets		-	(7,660)
Amortisation of acquired intangible assets		(2,389)	(67)
Impairment of available-for-sale investment		(706)	(1,449)
Other expenses	3c	(771)	(570)
Loss before income tax		(12,724)	(13,573)
Income tax benefit	4	13,830	2,298
Profit / (loss) after income tax		1,106	(11,275)
Other Comprehensive Income			
Foreign currency translation	15	(2)	(20)
Income tax/(expense) on items of other comprehensive income		-	-
Other comprehensive income for the period, net of tax	15	(2)	(20)
Total comprehensive income for the period		1,104	(11,295)
Profit / (loss) per share from continuing operations attributable to the ordinary equity holders of the parent:			
Basic profit / (loss) per share	16	0.13 cents	(1.52 cents)
Diluted profit / (loss) per share	16	0.13 cents	(1.52 cents)

The above Statement of comprehensive income should be read in conjunction with the accompanying notes

Consolidated statement of financial position

AS AT 31 DECEMBER 2011	Note	2011 $'000	2010 $'000
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents	21a	27,196	2,740
Trade and other receivables	7	2,376	417
Inventories	8	964	522
Other current assets		223	45
TOTAL CURRENT ASSETS		30,759	3,724
NON-CURRENT ASSETS			
Plant and equipment	9	1,161	1,298
Intangible assets	10	44,657	47,046
Available-for-sale investment	11	-	1,700
TOTAL NON-CURRENT ASSETS		45,818	50,044
TOTAL ASSETS		76,577	53,768
LIABILITIES			
CURRENT LIABILITIES			
Trade and other payables	12	3,358	816
Provisions	13	244	115
TOTAL CURRENT LIABILITIES		3,602	931
NON-CURRENT LIABILITES			
Provisions	13	29	-
Deferred tax liability	4	-	13,830
TOTAL NON-CURRENT LIABILITIES		29	13,830
TOTAL LIABILITIES		3,631	14,761
NET ASSETS		72,946	39,007
EQUITY			
Issued capital	14	209,546	176,905
Reserves	15	29,318	29,126
Accumulated losses		(165,918)	(167,024)
TOTAL EQUITY		72,946	39,007

The above Statement of financial position should be read in conjunction with the accompanying notes

Consolidated statement of cash flow

FOR THE YEAR ENDED 31 DECEMBER 2011	Note	2011 $'000	2010 $'000
OPERATING ACTIVITIES			
Receipts from customers		2,439	1,833
Receipt of government grants		105	161
Payments to suppliers and employees		(11,837)	(10,334)
Net cash used in operating activities	21(b)	**(9,293)**	**(8,340)**
INVESTING ACTIVITIES			
Interest received		216	342
Proceeds from available-for-sale investments		971	-
Purchase of plant and equipment		(79)	(131)
Net cash from investing activities		**1,108**	**211**
FINANCING ACTIVITIES			
Proceeds from issues of shares	14	34,707	-
Costs of issue of shares		(2,066)	
Net cash from financing activities		**32,641**	**-**
Net decrease in cash and cash equivalents		24,456	(8,129)
Cash and cash equivalents at the beginning of period		2,740	10,869
CASH AND CASH EQUIVALENTS AT THE END OF PERIOD	21(a)	**27,196**	**2,740**

The above Statement of cash flows should be read in conjunction with the accompanying notes

Consolidated statement of changes in equity

	Issued Capital $’000	Employee Benefits Reserve $’000	Other Benefits Reserve $’000	Business Combination & Foreign Currency Translation Reserve $’000	Accumulated Losses $’000	Total $’000
Balance at 1 January 2011	176,905	1,057	248	27,821	(167,024)	39,007
Profit / (loss) for the period	-	-	-	-	1,106	1,106
Other comprehensive income	-	-	-	(2)	-	(2)
Total comprehensive income for the period	-	-	-	(2)	1,106	1,104
Transactions with owners in their capacity as owners:						
Issue of share capital	34,707					34,707
Transaction costs	(2,066)					(2,066)
Employee equity settlement benefits	-	136	-	-	-	136
Share based payments	-	-	58	-	-	58
Balance at 31 December 2011	**209,546**	**1,193**	**306**	**27,819**	**(165,918)**	**72,946**

	Issued Capital $’000	Employee Benefits Reserve $’000	Other Benefits Reserve $’000	Business Combination & Foreign Currency Translation Reserve $’000	Accumulated Losses $’000	Total $’000
Balance at 1 January 2010	176,905	947	45	27,841	(155,749)	49,989
Loss for the period	-	-	-	-	(11,275)	(11,275)
Other comprehensive income	-	-	-	(20)	-	(20)
Total comprehensive income for the period	-	-	-	(20)	(11,275)	(11,295)
Transactions with owners in their capacity as owners:						
Employee equity settlement benefits	-	110	-	-	-	110
Share based payments	-	-	203	-	-	203
Balance at 31 December 2010	**176,905**	**1,057**	**248**	**27,821**	**(167,024)**	**39,007**

The above Statement of changes in equity should be read in conjunction with the accompanying notes.

Notes to the consolidated financial statements

YEAR ENDED 31 DECEMBER 2011

1. CORPORATE INFORMATION

The consolidated financial statements of Phosphagenics Limited for the year ended 31 December 2011 was authorised for issue in accordance with a resolution of the Directors on 21st February 2012.

Phosphagenics Limited (the parent) is a company limited by shares incorporated in Australia whose shares are publicly traded on the Australian Stock Exchange ("ASX").

The nature of the operations and principal activities of the Group are described in the directors' report.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Table of Contents

Basis of Preparation of the financial report

The financial report is a general-purpose financial report, which has been prepared in accordance with the requirements of the *Corporations Act 2001,* Australian Accounting Standards, and other authoritative pronouncements of the Australian Accounting Standards Board. The financial report has also been prepared on a historical cost basis, with the exception of Available-for-sale financial assets which are carried at fair value.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars ($'000) unless otherwise stated.

(a) Compliance with IFRS

The financial report also complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) New Accounting Standards and Interpretations

(i) Changes in accounting policy and disclosures.

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended Australian Accounting Standards and AASB Interpretations as of 1 January 2011:

- AASB 124 *Related Party Disclosures (amendment)* effective 1 January 2011
- AASB 132 *Financial Instruments: Presentation (amendment)* effective 1 February 2010

The adoption of the standards or interpretations is described below:

AASB 124 Related Party Transactions (Amendment)

The AASB issued an amendment to AASB 124 that clarifies the definitions of a related party. The new definitions emphasise a symmetrical view of related party relationships and clarifies the circumstances in which persons and key management personnel affect related party relationships of an entity. In addition, the amendment introduces an exemption from the general related party disclosure requirements for transactions with government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The adoption of the amendment did not have any impact on the financial position or performance of the Group.

AASB 132 Financial Instruments: Presentation (Amendment)

The AASB issued an amendment that alters the definition of a financial liability in AASB 132 to enable entities to classify rights issues and certain options or warrants as equity instruments. The amendment is applicable if the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The amendment has had no effect on the financial position or performance of the Group because the Group does not have these type of instruments.

Other amendments resulting from Improvements to AASBs to the following standards did not have any impact on the accounting policies, financial position or performance of the Group:

- AASB 7 *Financial Instruments – Disclosures*
- AASB 101 *Presentation of Financial Statements*
- AASB 127 *Consolidated and Separate Financial Statements*
- AASB 134 *Interim Financial Statements*

The following interpretation and amendments to interpretations did not have any impact on the accounting policies, financial position or performance of the Group:

- AASB 3 *Business Combinations* (Contingent consideration arising from business combination prior to adoption of AASB 3 (as revised in 2008))
- AASB 3 *Business Combinations* (Un-replaced and voluntarily replaced share-based payment awards)
- AASB Int 13 *Customer Loyalty Programmes* (determining the fair value of award credits)

  AASB Int 19 *Extinguishing Financial Liabilities with Equity Instruments* *(ii) Accounting Standards and Interpretations issued but not yet effective.*

The following standards and interpretations have been issued by the AASB but are not yet effective for the period ending 31 December 2011:

Reference	Title	Summary	Application date of standard	Impact on Group financial report	Application date for Group
AASB 2011-5	Amendments to Australian Accounting Standards – Extending Relief from Consolidation, the Equity Method and Proportionate Consolidation [AASB 127, AASB 128 & AASB 131]	This Standard makes amendments to: ▶ AASB 127 *Consolidated and Separate Financial Statements* ▶ AASB 128 *Investments in Associates* ▶ AASB 131 Interests in Joint Ventures to extend the circumstances in which an entity can obtain relief from consolidation, the equity method or proportionate consolidation, and relates primarily to those applying the reduced disclosure regime or not-for-profit entities.	1 July 2011	Some of these amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2012
AASB 2011-9	Amendments to Australian Accounting Standards – Presentation of Other Comprehensive Income [AASB 101]	This Standard requires entities to group items presented in other comprehensive income on the basis of whether they are potentially reclassifiable to profit or loss subsequently (reclassification adjustments).	1 July 2012	These amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2013
AASB 2011-4	Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements [AASB 124]	This Standard makes amendments to remove individual key management personnel disclosure requirements from AASB 124.	1 July 2013	These amendments are likely to have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2014

Reference	Title	Summary	Application date of standard	Impact on Group financial report	Application date for Group
AASB 1053	Application of Tiers of Australian Accounting Standards	This Standard establishes a differential financial reporting framework consisting of two Tiers of reporting requirements for preparing general purpose financial statements: (a) Tier 1: Australian Accounting Standards (b) Tier 2: Australian Accounting Standards - Reduced Disclosure Requirements Tier 2 comprises the recognition, measurement and presentation requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements. The following entities apply Tier 1 requirements in preparing general purpose financial statements: (a) For-profit entities in the private sector that have public accountability (as defined in this Standard) (b) The Australian Government and State, Territory and Local Governments The following entities apply either Tier 2 or Tier 1 requirements in preparing general purpose financial statements: (a) For-profit private sector entities that do not have public accountability (b) All not-for-profit private sector entities (c) Public sector entities other than the Australian Government and State, Territory and Local Governments. Consequential amendments to other standards to implement the regime were introduced by AASB 2010-2.	1 July 2013	Phosphagenics Limited (the parent) is a company limited by shares and the shares are publicly traded on the Australian Stock Exchange therefore the Group has public accountability and will apply the Tier 1 requirements in preparing general purpose financial statements.	1 January 2014

Reference	Title	Summary	Application date of standard	Impact on Group financial report	Application date for Group
AASB 9	Financial Instruments	AASB 9 includes requirements for the classification and measurement of financial assets. It was further amended by AASB 2010-7 to reflect amendments to the accounting for financial liabilities. These requirements improve and simplify the approach for classification and measurement of financial assets compared with the requirements of AASB 139. The main changes are described below. (a) Financial assets that are debt instruments will be classified based on (1) the objective of the entity's business model for managing the financial assets; (2) the characteristics of the contractual cash flows. (b) Allows an irrevocable election on initial recognition to present gains and losses on investments in equity instruments that are not held for trading in other comprehensive income. Dividends in respect of these investments that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument. (c) Financial assets can be designated and measured at fair value through profit or loss at initial recognition if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities, or recognising the gains and losses on them, on different bases. (d) **Where the fair value option is used for financial liabilities the change in fair value is to be accounted for as follows:** ► The change attributable to changes in credit risk are presented in other comprehensive income (OCI) ► The remaining change is presented in profit or loss If this approach creates or enlarges an accounting mismatch in the profit or loss, the effect of the changes in credit risk are also presented in profit or loss. Consequential amendments were also made to other standards as a result of AASB 9, introduced by AASB 2009-11	1 January 2013	These amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2013

Reference	Title	Summary	Application date of standard	Impact on Group financial report	Application date for Group
AASB 10	Consolidated Financial Statements	AASB 10 establishes a new control model that applies to all entities. It replaces parts of AASB 127 *Consolidated and Separate Financial Statements* dealing with the accounting for consolidated financial statements and UIG-112 *Consolidation – Special Purpose Entities*. The new control model broadens the situations when an entity is considered to be controlled by another entity and includes new guidance for applying the model to specific situations, including when acting as a manager may give control, the impact of potential voting rights and when holding less than a majority voting rights may give control. This is likely to lead to more entities being consolidated into the group. Consequential amendments were also made to other standards via AASB 2011-7 and amendments to AASB 127.	1 January 2013	These amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2013
AASB 12	Disclosure of Interests in Other Entities	AASB 12 includes all disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and structures entities. New disclosures have been introduced about the judgements made by management to determine whether control exists, and to require summarised information about joint arrangements, associates and structured entities and subsidiaries with non-controlling interests.	1 January 2013	These amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2013

Reference	Title	Summary	Application date of standard	Impact on Group financial report	Application date for Group
AASB 13	Fair Value Measurement	AASB 13 establishes a single source of guidance under AASB for determining the fair value of assets and liabilities. AASB 13 does not change when an entity is required to use fair value, but rather, provides guidance on how to determine fair value when fair value is required or permitted. Application of this definition may result in different fair values being determined for the relevant assets. AASB 13 also expands the disclosure requirements for all assets or liabilities carried at fair value. This includes information about the assumptions made and the qualitative impact of those assumptions on the fair value determined. Consequential amendments were also made to other standards via AASB 2011-8.	1 January 2013	Some of these amendments may have an impact on the Group; however the Group has not yet assessed the impact.	1 January 2013
AASB 119	Employee Benefits	The main change introduced by this standard is to revise the accounting for defined benefit plans. The amendment removes the options for accounting for the liability, and requires that the liabilities arising from such plans is recognized in full with actuarial gains and losses being recognized in other comprehensive income. It also revised the method of calculating the return on plan assets. Consequential amendments were also made to other standards via AASB 2011-10.	1 January 2013	These amendments are unlikely to have an impact on the Group as Phosphagenics do not currently have any defined benefit plans in place; however the Group has not yet assessed the full impact.	1 January 2013

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of Phosphagenics Limited and its subsidiaries as at and for the period ended 31 December each year ('the Group').

Subsidiaries are all those entities over which the Group has the power to govern the financial and operating policies so as to obtain benefits from their activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether a group controls another entity.

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

In preparing the consolidated financial statements, all intercompany balances and transactions, income and expenses and profit and losses resulting from intra-group transactions have been eliminated in full.

Investments in subsidiaries held by Phosphagenics Limited are accounted for at cost in the separate financial statements of the parent entity less any impairment charges.

(d) Operating Segments

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity), whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available. Management will also consider other factors in determining operating segments such as the existence of a line manager and the level of segment information presented to the board of directors.

Operating segments that meet the quantitative criteria as prescribed by AASB 8 are reported separately. However, an operating segment that does not meet the quantitative criteria is still reporting separately where information about the segment would be useful to users of the financial statements.

Information about other business activities and operating segments that are below the quantitative criteria are combined and disclosed in a separate category for "all other segments".

(e) Significant accounting judgements, estimates and assumptions

The carrying amounts of certain assets and liabilities are often determined based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of certain assets and liabilities within the next annual reporting period are:

Impairment of intangibles with indefinite useful lives

The Group determines whether intangible assets with indefinite useful lives, and intangible assets not yet available for use, are impaired at least on an annual basis. This requires an estimation of the recoverable amount of the cash-generating unit to which the goodwill is allocated. The assumptions used in this estimation of recoverable amount and the carrying amount of intangibles with indefinite useful lives are discussed in note 10.

During the reporting period, certain intangible assets previously assessed as having indefinite useful lives were reassessed as having finite useful lives. As such these intangible assets have begun being amortised over the remaining expiry period of the patents.

Share-based payment transactions

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. The fair value is determined by using the Binomial method taking into account the terms and conditions upon which the instruments were granted, as discussed in note 5. The accounting estimates and assumptions relating to equity-settled share-based payments would have no impact on the carrying amounts of assets and liabilities with the next annual reporting period but may impact expenses and equity.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Development costs

An intangible asset arising from development expenditure on an internal project is recognised only when Phosphagenics can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the development and the ability to measure reliably the expenditure attributable to the intangible asset during its development. Any expenditure so capitalised is amortised over the period of expected future benefit from the related project on a straight line basis. The carrying value of capitalised developments costs not yet available for use is tested for impairment annually at 31 December.

Certain development costs relate to patents which were reassessed as having finite lives during the period. These costs have begun being amortised over their remaining useful lives which ranges between 9 to 12 years.

(f) Cash and cash equivalents

Cash and short term deposits in the statement of financial position comprise cash at bank and in hand and short-term deposits with an original maturity of six months or less, that are readily convertible to known amounts of cash and which are subject to an insignificant rate of change in value.

For the purposes of the consolidated statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

(g) Provisions and employee benefits

General

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

When the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the reporting date. The discount rate used to determine the present value reflects the current market assessments of the time value of money and the risks specific to the liability. The increase in the provision resulting from the passage of time is recognised in finance costs.

Employee leave benefits

Wages, salaries and, annual leave.

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within twelve months of the reporting date are recognised in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for non-accumulating sick leave are recognised when the leave is taken and are measured at the rates paid or payable.

Long service leave

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

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Government grants

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate.

Income is also recognised where there is a reasonable assurance that a cash benefit will arise under the R&D tax incentive from eligible expenditure incurred during the period.

(i) Income Tax and other taxes

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities based on the current period's taxable income. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised:

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in the statement of comprehensive income.

Tax consolidation legislation

During the year Phosphagenics Limited and its wholly-owned Australian controlled entities elected to form a tax consolidation group as of 1 July 2009. As a result the tax base of intangible assets was reset such that the deferred tax liability of $13,830,498 was reversed during the period.

The head entity, Phosphagenics Limited and the controlled entities in the tax consolidated group continue to account for their own current and deferred tax amounts. The Group has applied the Group allocation approach in determining the appropriate amount of current taxes and deferred taxes to allocate to members of the tax consolidated group.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

In addition to its own current and deferred tax amounts, Phosphagenics Limited also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group.

(j) Other taxes

Revenues, expenses and assets are recognised net of the amount of GST except:

- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority is classified as part of operating cash flows. Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

(k) Intangible assets

Intangible assets acquired separately or in a business combination are initially measured at cost. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is recognised in profit or loss in the year in which the expenditure was incurred.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful life and tested for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for prospectively by changing the amortisation period or method, as appropriate, which is a change in accounting estimate. The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed each reporting period to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is accounted for as a change in an accounting estimate and is thus accounted for on a prospective basis.

Research and Development costs

Research costs are expensed as incurred. An intangible asset arising from development expenditure on an internal project is recognised only when Phosphagenics can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the development and the ability to measure reliably the expenditure attributable to the intangible asset during its development. Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortisation and accumulated impairment losses. Any expenditure so capitalised is amortised over the period of expected benefit from the related project.

The carrying value of an intangible asset arising from development expenditure is tested for impairment annually when the asset is not yet available for use, or more frequently when an indication of impairment arises during the reporting period.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(k) Intangible assets *(continued)*

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the profit and loss when the asset is derecognised.

(l) Impairment of non- financial assets

Intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

The Group conducts an annual review of asset values, which is used as a source of information to assess for any indicators of impairment. External factors, such as changes in expected future processes, technology and economic conditions, are also monitored to assess for indicators of impairment. If any indication of impairment exists, an estimate of the asset's recoverable amount is calculated.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. Recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that have previously been impaired are tested for possible reversal of the impairment whenever events or changes in circumstances indicate that the impairment may have reversed.

(m) Investments and other financial assets

Investments and other financial assets in the scope of AASB 139 *Financial Instruments: Recognition and Measurement* are categorised as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired or originated. Designation is re-evaluated at each reporting date, but there are restrictions on reclassifying to other categories.

When financial assets are recognised initially, they are measured at fair value, plus, in the case of assets not at fair value through profit or loss, directly attributable transaction costs.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Investments and other financial assets *(continued)*

Available-for-sale financial assets
Available-for-sale financial assets are those non-derivative financial assets, principally equity securities, that are designated as available-for-sale or are not classified as any of the three preceding categories. After initial recognition available-for-sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is recognised in profit or loss.

The fair value of investments that are actively traded in organised financial markets are determined by reference to quoted market bid prices at the close of business on the reporting date.

(n) Trade and other payables

Trade payables and other payables are carried at amortised costs and are not discounted due to their short term nature. They represent liabilities for goods and services provided to the Group prior to the end of the financial year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services. The amounts are not secured and are usually paid within 30 days of recognition.

(o) Share-based payment transactions

The Group provides benefits to its employees, including Key Management Personnel (KMP), in the form of share-based payments, whereby employees render services in exchange for shares or rights over shares (equity-settled transactions). There is currently two plans in place to provide these benefits being the Employee Share Option Plan (ESOP), and the Employee Conditional Rights Scheme (ECRS) which provides benefits to key management personnel.

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).

The charge to the statement of comprehensive income for the period is the cumulative amount as calculated above less the amounts already charged in previous periods. There is a corresponding entry to equity.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new award are treated as if they were a modification of the original award, as described in the previous paragraph.

In reporting periods where a net loss is reported, options are considered anti-dilutive and therefore are excluded in the calculation of diluted earnings per share. Where a net profit is reported, options are considered dilutive and therefore included in the calculation of diluted earnings per share.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(p) Leases

Leases where the lessor retains substantial risks and reward of ownership are classified as operating leases. Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

(q) Inventories

Inventories including raw materials, work in progress and finished goods are valued at the lower of cost and net realisable value. Costs incurred in bringing each product to its present location and condition are accounted for as follows:

Raw materials
Purchase cost on a first-in, first-out basis. The cost of purchase comprises the purchase price including, import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities), transport, handling and other costs directly attributable to the acquisition of raw materials. Volume discounts and rebates are included in determining the cost of purchase.

Finished goods and work-in-progress
Cost of direct materials, labour and a proportion of variable and fixed manufacturing overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

(r) Trade and other receivables

Trade receivables, which generally have thirty to sixty day terms, are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less an allowance for impairment.

Collectability of trade receivables is reviewed on an ongoing basis. Individual debts that are known to be uncollectible are written off when identified. An impairment provision is recognised when there is objective evidence that the Group will not be able to collect the receivable. Financial difficulties of the debtor, default payments or debts more than ninety days overdue are considered objective evidence of impairment. The amount of the impairment loss is the receivable carrying amount compared to the present value of estimated future cash flows, discounted at the original effective interest rate.

(s) Plant and Equipment

Plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a diminishing value basis as follows:

Computer Equipment – 33% p.a.
Plant and equipment – 20% p.a.
Office Equipment - 20% p.a.

The assets' residual values, useful lives and amortisation methods are reviewed, and adjusted if appropriate, at each reporting period. When no future economic benefits are expected to arise from the continued use of an item of property, plant and equipment, it is derecognised. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the statement of comprehensive income in the year the item is derecognised.

Notes to the consolidated financial statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable taking into account contractually defined terms of payment and excluding taxes or duty. The following specific recognition criteria must also be met before revenue is recognised:

Sale of goods
Revenue from the sale of goods is recognised when the Group has transferred to the buyer the significant risks and rewards of ownership of the goods and the costs in respect of the transaction can be reliably measured. Risks and rewards are considered passed to the buyer at the time of delivery of the goods to the customer.

Royalties
Royalty revenue is recognised on an accrual basis in accordance with the substance of the relevant agreement.

Interest income
Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset) to the net carrying amount of the financial asset.

(u) Issued capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

(v) Foreign currency translation

Functional and presentation currency
Both the functional and presentation currency of Phosphagenics Limited and its Australian subsidiaries is Australian dollars ($). The United States subsidiaries functional currency is United States Dollars which is translated to the presentation currency.

Transactions and balances
Transactions in foreign currencies are initially recorded in the functional currency by applying the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the reporting date. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Translation of Group Companies functional currency to presentation currency
The results of the United States subsidiary are translated into Australian Dollars as at the date of each transaction. Assets and liabilities are translated at exchange rates prevailing at reporting date. Exchange variations resulting from the translation are recognised in the foreign currency translation reserve in equity.
On consolidation, exchange differences arising from the translation of the net investment in the United States subsidiary are taken to the foreign currency translation reserve. If the United States subsidiary were sold, the proportionate share of exchange differences would be transferred out of equity and recognised in the statement of comprehensive income.

(w) Earnings per share

Basic earnings per share is calculated as net profit or loss attributable to members of the parent divided by the weighted average number of ordinary shares. Where the Group generates a loss attributable to members of the parent, basic and diluted earnings per share are the same as a loss attributable to members of the parent cannot be further diluted.

Notes to the consolidated financial statements

3. OTHER REVENUE AND EXPENSES

	2011 $'000's	2010 $'000's
(a) Licences		
Licences – ProPhase Labs[1]	-	4,241
Licences – Other	228	145
Total	**228**	**4,386**

[1] The licence revenue relates to a one-time payment to Phosphagenics of approximately $1.09 million (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 $3.149 million. These shares were recognised as an available-for-sale investment at 31 December 2010, and sold in October 2011 for US$ 936,000.

	2011 $'000's	2010 $'000's
(b) Government Grants		
Export markets development grant[1]	105	161
R&D tax incentive credit[2]	1,131	-
Total	**1,236**	**161**

[1] The Export markets development grant relates to monies received as a partial offset for expenses incurred by Phosphagenics in developing its overseas markets

[2] The R&D tax incentive credit is the estimated cash payment anticipated to be received as a 45% offset of eligible expenditure incurred in developing the Company's products through research and development activities undertaken from 1 July 2011 to 31 December 2011.

	2011 $'000's	2010 $'000's
(c) Other Expenses		
Net foreign exchange gains/(losses)	72	(91)
Depreciation	(261)	(300)
Loss on sale of available-for-sale investments	(163)	-
Travel	(326)	(124)
Other	(93)	(55)
Total	**(771)**	**(570)**

4. INCOME TAXES

	2011 $'000's	2010 $'000's
Major components of income tax expense are:		
Current income tax	-	-
Deferred income tax		
Relating to origination and reversal of temporary differences	(13,830)	(2,298)
Income tax expense recorded in the statement of comprehensive income	(13,830)	(2,298)
The prima facie income tax expense/(benefit) on pre-tax accounting profit from operations reconciles to the income tax expense in the financial statements as follows:		
Accounting (loss) before income tax	(12,724)	(13,573)
Income tax expense calculated at 30% (2010: 30%)	(3,817)	(4,072)
Non-deductible expenses	270	558
Derecognition of deferred tax liability from formation of tax consolidated group	(13,830)	-
Research & development deduction	-	(223)
Unused tax losses and tax offsets not recognised as deferred tax assets	3,547	1,439
Income tax benefit reported in income statement	(13,830)	(2,298)
Deferred tax liabilities comprise:		
Intellectual property	-	13,830

Notes to the consolidated financial statements

4. INCOME TAXES (continued)

Unrecognised deferred tax balances		
The following items have not been brought to account as deferred tax assets:		
Tax losses not recognised	20,435	16,891
Temporary differences not recognised	-	-
Total	**20,435**	**16,891**

Tax Losses

Deferred tax assets have not been recognised in respect of carried forward tax losses.

Tax consolidation

(i) Members of the tax consolidated group and the tax sharing arrangement

Phosphagenics Limited and its 100% owned Australian resident subsidiaries formed a tax consolidated group with effect from 1 July 2009. Phosphagenics Limited is the head entity of the tax consolidated group. As a result the tax base of intangible assets was reset such that the deferred tax liability of $13,830,498 was reversed during the period.

(ii) Tax effect accounting by members of the tax consolidated group
Measurement method adopted under AASB Interpretation 1052 Tax Consolidation Accounting

The head entity and the controlled entities in the tax consolidated group continue to account for their own current and deferred tax amounts. The Group has applied the Group allocation approach in determining the appropriate amount of current taxes and deferred taxes to allocate to members of the tax consolidated group. The current and deferred tax amounts are measured in a systematic manner that is consistent with the broad principles in AASB 112 *Income Taxes.*

5. 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.

Options held by directors of the parent and its subsidiaries were acquired as part of the original subscriptions for shares in Phosphagenics Limited in 1999. Subsequently, all options granted to key management personnel have been issued in accordance with the provisions of the Employee Share Option Plan (ESOP). All rights granted to key management personnel have been issued in accordance with the provisions of the Employee Conditional Rights Scheme (ECRS).

Notes to the consolidated financial statements

5. SHARE BASED PAYMENTS (continued)

Summary of options granted as share based payments

The following table illustrates the number (No.) and weighted average exercise prices (WAEP) of, and movements in, share options issued during the year.

Item	2011 Options No.	2011 WAEP $	2010 Options No.	2010 WAEP $
Outstanding at beginning of the year	25,450,000	$0.17	12,350,000	$0.18
Granted during the year	1,000,000	$0.17	15,000,000	$0.14
Forfeited during the year	(11,100,000)	$0.14	(900,000)	$0.15
Exercised during the year	-	-	-	-
Expired during the year	(2,200,000)	$0.24	(1,000,000)	$0.22
Outstanding at end of the year	**13,150,000**	**$0.15**	**25,450,000**	**$0.16**
Exercisable at end of the year	13,150,000	$0.15	15,450,000	$0.17

When a participant in the employee share option plan ceases employment prior to the vesting of their share options, the share options are forfeited unless cessation of employment is due to retirement or death.

A service period was determined as the most appropriate criteria to attach to the options given Phosphagenics is still developing its products for commercialisation. There are no other service or performance criteria attached to share based payment options.

1,000,000 Options were granted during the reporting period to consultants in recognition of corporate advisory services performed during the year.

The outstanding balance as at 31 December 2011 is represented by:

Issuing entity	Australian stock exchange listed	shares under option No.	Class of shares	Exercise price $	Expiry date
Phosphagenics Ltd	unquoted	1,100,000	Ordinary	$0.26	06 June 2012
Phosphagenics Ltd	unquoted	5,000,000	Ordinary	$0.14	31 Mar 2013
Phosphagenics Ltd	unquoted	1,450,000	Ordinary	$0.15	17 Aug 2013
Phosphagenics Ltd	unquoted	1,000,000	Ordinary	$0.15	14 May 2014
Phosphagenics Ltd	unquoted	1,950,000	Ordinary	$0.15	17 June 2014
Phosphagenics Ltd	unquoted	2,650,000	Ordinary	$0.13	30 June 2018
Total		**13,150,000**			

Summary of performance rights granted as share based payments

The following table illustrates the number (No.) and weighted average exercise prices (WAEP) of, and movements in, performance rights issued during the year.

Item	2011 Performance Rights No.	2011 WAEP $	2010 Options No.	2010 WAEP $
Outstanding at beginning of the year	-	-	-	-
Granted during the year	17,400,000	0.00	-	-
Forfeited during the year	-	-	-	-
Exercised during the year	-	-	-	-
Expired during the year	-	-	-	-
Outstanding at end of the year	**17,400,000**	**0.00**	-	-
Exercisable at end of the year	Nil	-	-	-

Notes to the consolidated financial statements

5. SHARE BASED PAYMENTS (continued)

When a participant in the ECRS ceases employment prior to the vesting of their performance rights, the performance rights are forfeited unless cessation of employment is due to retirement or death.

The outstanding balance as at 31 December 2011 is represented by:

Issuing entity	Australian stock exchange listed	Performance Rights No.	Class of shares	Exercise price $	Expiry date
Phosphagenics Ltd	unquoted	17,400,000	Ordinary	$0.00	30 June 2016
Total		**17,400,000**			

Option pricing model

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 year ended 31 December 2011 no share options were granted under the ESOP (2010: NIL).

During the year ended 31 December 2011 a total of 17,400,000 share rights with a fair value of $0.07 were granted under the ECRS (2010: Nil) which will vest based upon achievement of certain performance objectives.

During the year ended 31 December 2011 a total of 1,000,000 options with a fair value of $0.06 were granted to non-employees (2010: 15,000,000) which vested at the grant date of 25 May 2011.

Model Inputs	2011 Rights	2011 Options	2010 Options
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
Option Exercise price $	Nil	$0.170	$0.142
Weighted Average Share price at measurement date	$0.155	$0.145	$0.109

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur.

The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may not necessarily be the actual outcome.

Notes to the consolidated financial statements

6. REMUNERATION OF AUDITORS

The auditor of Phosphagenics Ltd (the parent), and the Group is Ernst & Young.

Amounts received or due and receivable by Ernst & Young	2011 $	2010 $
Audit or review of the financial report	91,005	83,845
Other non audit services	-	-
Taxation services	63,300	33,716
Total	**154,305**	**117,561**

7. TRADE AND OTHER RECEIVABLES

Current	2011 $'000	2010 $'000
Trade receivables	644	30
Allowance for impairment loss	(8)	-
	636	30
Other receivables	1,448	116
Goods and services tax (GST) recoverable	292	271
Total	**2,376**	**417**

Trade receivables are non interest bearing and are generally 45 day terms or as specified in contracts or agreements.

Allowance for impairment loss
A provision for impairment is recognised when there is objective evidence (such as the probability of insolvency or significant financial difficulty of the debtor) that the Group may not be able to collect all the amounts due under the original terms of the invoice. Impaired debts are derecognised when they are assessed as uncollectible. Debts totalling $8,170 were deemed impaired at 31 December 2011.

At 31 December, the ageing analysis of trade receivables is as follows:

Period	Total	Neither past due or impaired	Past due but not impaired		
			31-60 days	61-90 days	90+ days
	$'000	$'000	$'000	$'000	$'000
31 December 2011	636	238	159	224	15
31 December 2010	30	-	27	3	-

Other balances within trade and other receivables do not contain impaired assets and are not past due. It is expected that these other balances will be received when due.

Fair value and credit risk
Due to the short term nature of these receivables, their carrying value is assumed to approximate their fair value. The maximum exposure to credit risk is the fair value of receivables.

8. INVENTORIES

	2011 $'000	2010 $'000
Raw materials (at cost)	739	283
Finished goods (at cost or net realisable value)	225	239
Total inventories at the lower of cost and net realisable value	964	522

During 2011, $93,530 (2010: $nil) was recognised as an expense for inventories written off or a provision raised for inventories adjusted to their net realisable value. This is recognised in cost of sales.

Notes to the consolidated financial statements

9. PLANT AND EQUIPMENT

2011	Plant and equipment at cost $'000	Total $'000
Year ended 31 December 2011		
At 1 January 2011 net of accumulated depreciation and impairment	1,298	1,298
Additions	90	90
Capital Work in progress	34	34
Disposals	-	-
Depreciation charge for the year	(261)	(261)
At 31 December 2010, net of accumulated depreciation and impairment	1,161	1,161
At 31 December 2011		
Cost	2,690	2,690
Accumulated depreciation and impairment	(1,529)	(1,529)
Net carrying value	1,161	1,161

2010	Plant and equipment at cost $'000	Total $'000
Year ended 31 December 2010		
At 1 January 2010 net of accumulated depreciation and impairment	1,445	1,445
Additions	153	153
Disposals	-	-
Depreciation charge for the year	(300)	(300)
At 31 December 2010, net of accumulated depreciation and impairment	1,298	1,298
At 31 December 2010		
Cost	2,566	2,566
Accumulated depreciation and impairment	(1,268)	(1,268)
Net carrying value	1,298	1,298

Notes to the consolidated financial statements

10. INTANGIBLE ASSETS

2011	Intellectual Property $000	Development costs $000	Total $000
Balance at 1 January 2011 net of accumulated amortisation and impairment	45,577	1,469	47,046
Additions internally developed	-	-	-
Provision for impairment	-	-	-
Amortisation	(2,322)	(67)	(2,389)
Balance at 31 December 2011 net of accumulated amortisation and impairment	43,255	1,402	44,657
At 31 December 2011			
Cost (gross carrying amount)	121,362	3,295	124,657
Accumulated amortisation and impairment	(78,107)	(1,893)	(80,000)
Net carrying amount	43,255	1,402	44,657

2010	Intellectual Property $000	Development costs $000	Total $000
Balance at 1 January 2010 net of accumulated amortisation and impairment	52,062	2,310	54,372
Additions internally developed	-	400	400
Provision for impairment	(6,485)	(1,175)	(7,660)
Amortisation	-	(66)	(66)
Balance at 31 December 2010 net of accumulated amortisation and impairment	45,577	1,469	47,046
At 31 December 2010			
Cost (gross carrying amount)	121,362	3,295	124,657
Accumulated amortisation and impairment	(75,785)	(1,826)	(77,611)
Net carrying amount	45,577	1,469	47,046

Impairment Testing

Intellectual Property
Intellectual property assets cost represent the fair value of patents acquired by the Company at 31 December 2004.

Certain intellectual property assets, acquired patents, are deemed to have a finite life and are amortised from the date significant revenues are earned over the remaining patent life. Up until 30 June 2011 Phosphagenics Limited was yet to earn significant revenues from acquired patent assets, therefore these assets had not yet been amortised. However with significant revenues commencing during the reporting period, amortisation of these patents commenced from 1 July 2011. These assets are tested for impairment where an indicator of impairment arises.

Notes to the consolidated financial statements

10. INTANGIBLE ASSETS (continued)

Intangible assets with an indefinite life or not available for use are tested for impairment at least annually at 31 December, or earlier where an indicator of impairment arises. The recoverable amount has been determined by calculation of the value in use being the present value of future cash flows expected to be derived from intangible assets, excluding expansionary activities, finance costs and income tax.

Asset recoverable amounts (value in use) are calculated using discounted cash flow methodology, and applying sensitivity analysis to various input assumptions.

Key assumptions of these valuations include:

- management opinion on future cash flows on a product by product basis
- different residual lifetime of acquired patents
- allocation of products' value to underlying patents
- probability adjustments (ranging from 0.4275 to 1.00) to individual cash flows, reflecting various types of risks
- no terminal value

The pre-tax discount rate used was 20%, based on:

- the required rates of return on listed companies in a similar business
- the indicative rates of return required by suppliers of venture capital
- the Groups current level of financial gearing

Recoverable amounts were assessed from an individual patent asset perspective. Based on the recoverable amounts, no impairment exists for intangible assets with an indefinite useful life for the year ended 31 December 2011 (2010: $7.66 million).

Development costs
Development expenditure on an internal project is recognised as an intangible asset only when Phosphagenics can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the development and the ability to measure reliably the expenditure attributable to the intangible asset during its development.

Capitalised development costs relating to patents are amortised from the date significant revenues are carried over the remaining patent life.

Development expenditure is tested for impairment annually, when the asset is not yet available for use, or more frequently when an indication of impairment arises during the reporting period. At 31 December 2011 zero development costs were impaired and recognised as an expense (2010: Nil).

11. AVAILABLE-FOR-SALE INVESTMENT

	2011 $'000's	2010 $'000's
Share – US listed		
Fair value at acquisition date	-	3,149
Impairment	-	(1,449)
Shares – at fair value	**-**	**1,700**

Available-for-sale investments consisted of investments in ordinary shares, and therefore have no fixed maturity date or coupon rate. At 31 December 2010 the fair value of US listed available-for-sale investments had been determined directly by reference to published price quotations in an active market.

During October 2011, the total amount of US listed shares (1,440,000 shares) were sold for USD 0.65 per share, yielding USD 936,000.

Notes to the consolidated financial statements

12. CURRENT TRADE AND OTHER PAYABLES

	2011 $'000	2010 $'000
Trade payables	1,997	548
Accrued expenses	1,123	92
Goods and services tax (GST) payable	29	2
Other	209	174
Total	**3,358**	**816**

Due to the short-term nature of these payables, their carrying value is assumed to approximate their fair value.

Trade payables are non-interest bearing and are generally settled on 30 day terms.

Other payables are non-trade payables and non-interest bearing.

There was $29,882 of related party payables included in trade payables at 31 December 2011. Don Clarke, a director, is a partner of law firm Minter Ellison. Minter Ellison provided professional services to the Group during the year, of which $29,882 remained outstanding at 31 December 2011. These services were provided on normal commercial terms.

13. PROVISIONS

CURRENT	2011 $'000	2010 $'000
Annual leave benefits	166	98
Long service leave benefits	78	17
Total	244	115

NON CURRENT	2011 $'000	2010 $'000
Long service leave benefits	29	-

14. ISSUED CAPITAL

Fully paid ordinary shares	2011 No. '000's	2011 $'000	2010 No. '000's	2010 $'000
Balance at beginning of year	739,696	176,905	739,696	176,905
Issue of shares	277,869	34,707	-	-
Exercise of options	-	-	-	-
Capital raising costs	-	(2,066)	-	-
Balance at end of year	1,017,565	209,546	739,696	176,905

Fully paid ordinary shares carry one vote per share and carry the right to dividends.

Share options

As at close of business on 31 December 2011 there were a total of 13,150,000 unexercised unquoted options issued as share based payments, of which 13,150,000 options are fully vested and can be exercised at any time up to the date of expiry.

As at close of business on 31 December 2011 there were a total of 17,400,000 unexercised unquoted rights issued as share based payments, of which nil are fully vested, and therefore cannot yet be exercised.

Share options and share rights carry no rights to dividends and no voting rights. For further details of share based payments refer to note 5.

Notes to the consolidated financial statements

15. RESERVES

	2011 $'000	2010 $'000
Reserves		
Business combination	27,812	27,812
Employee equity-settled benefits	1,192	1,056
Other equity-settled benefits	307	249
Foreign Currency Translation Reserve	7	9
	29,318	29,126
Business combination reserve		
Balance at beginning of year	27,812	27,812
Balance at end of year	27,812	27,812
The business combinations reserve is used to record fair value adjustments relating to the business combination		
Employee equity-settled benefits reserve		
Balance at beginning of year	1,056	946
Share based payment expense	136	110
Balance at end of year	1,192	1,056

The employee share option and share plan reserve is used to record the value of equity benefits provided to employees and Directors as part of their remuneration. For further details refer to note 5 in the Financial Statements.

	2011 $'000	2010 $'000
Other equity-settled benefits reserve		
Balance at beginning of year	249	46
Share based payments	58	203
Balance at end of year	307	249

The other equity-settled benefits reserve is used to record the value of equity benefits provided to suppliers as part of their remuneration.

	2011 $'000	2010 $'000
Foreign Currency Translation Reserve		
Balance at beginning of year	9	29
Foreign Currency Translation	(2)	(20)
Balance at end of year	7	9

The foreign currency translation reserve is used to record the translation from Phosphagenics Inc.'s functional currency into Phosphagenics Ltd's reporting currency.

Notes to the consolidated financial statements

16. EARNINGS PER SHARE

Basic earnings per share

Basic earnings per share is calculated by dividing the net profit / (loss), from continuing operations attributable to ordinary equity holders of the parent for the year, by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share

Diluted earnings per share is calculated by dividing the net profit / (loss) attributable to ordinary shareholders by the weighted average number of ordinary shares on issue during the year (adjusted for the effects of dilutive options).

There are no instruments (e.g., share options) excluded from the calculation of diluted earnings per share that could potentially dilute basic earnings per share in the future.

There have been no transactions involving ordinary shares or potential ordinary shares that would significantly change the number of ordinary shares or potential ordinary shares outstanding between the reporting date and the date of completion of these financial statements.

Profit / (loss) used in calculating earnings per share	**2011 $'000's**	**2010 $'000's**
Net Profit / (loss) from continuing operations attributable to ordinary equity holders for the calculation of basic and diluted earnings per share	1,106	(11,275)

Weighted average number of shares	**2011 No. '000's**	**2010 No. '000's**
Weighted average number of ordinary shares for the purposes of basic earnings per share	833,035	739,696
Effect of dilution:		
Share options	13,776	22,352
Performance rights	5,736	-
Weighted average number of ordinary shares adjusted for the effect of dilution	852,548	762,048

Information on the classification of securities

Options quoted on the ASX and options granted to employees and other service providers are considered to be potential ordinary shares and have been included in the determination of diluted earnings per share to the extent they are dilutive. These options have not been included in the determination of basic earnings per share.

17. COMMITMENTS FOR EXPENDITURE

Operating Leases

Non-cancellable operating leases relate to the rent of commercial property used for business operations.

Non-cancellable operating lease payments	**2011 $'000's**	**2010 $'000's**
Within 1 year	336	226
After 1 year but not more than 5 years	249	-
After more than 5 years	-	-
Total minimum lease payments	585	226

Notes to the consolidated financial statements

18. SEGMENT INFORMATION

Identification of reportable segments

The group has indentified its operating segments based on the internal reports that are reviewed and used by the Chief Executive Officer and his 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 α-tocopheryl phosphate (TP) is a natural molecule with increased activity over standard Vitamin E (α 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 α-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 April 2010 Phosphagenics launched its own brand of cosmetic products in Australia (Elixia®) sold through Myer, Priceline, TVSN, Pulse Pharmacies, and other retail outlets. 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.

Notes to the consolidated financial statements

18. SEGMENT INFORMATION (continued)

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

Accounting policies used by the Group in reporting segments are contained in note 2 to the accounts.

Major customers

The Group has an expanding number of customers to which it provides products and services. The most significant client accounts for 32% (2010: 58%) of external revenue within the nutraceuticals operating segment. The next most significant client accounts for 18% (2009: 27%) of external revenue within the nutraceuticals operating segment.

Business segments

2011	Nutraceuticals $'000's	Pharmaceuticals $'000's	Unallocated $'000's	Total Group $'000's
Revenue				
Sales and Royalties	2,738	6	-	2,744
Grant Income	105	-	1,131	1,236
Total segment revenue	**2,843**	**6**	**1,131**	**3,980**
Net operating profit/(loss) after tax	**(2,609)**	**(1,513)**	**5,228**	**1,106**
Interest revenue	**-**	**-**	427	427
Depreciation and amortisation	(2,546)	(67)	(37)	(2,650)
Segment assets	**3,023**	**878**	**72,676**	**76,577**
Capital Expenditure	-	-	90	90
Segment liabilities	**645**	**1,562**	**1,424**	**3,631**
Cash flow information				
Net cash flow from Operating activities	(2,260)	(741)	(6,292)	(9,293)
Net cash flow from investing activities	-	971	137	1,108
Net cash flow from financing activities	-	-	32,641	32,641

Notes to the consolidated financial statements

18. SEGMENT INFORMATION (continued)

2010	Nutraceuticals $'000's	Pharmaceuticals $'000's	Unallocated $'000's	Total Group $'000's
Revenue				
Sales and Royalties	554	4,251	-	4,805
Grant Income	-	161	-	161
Total segment revenue	**554**	**4,421**	**-**	**4,966**
Net operating profit/(loss) after tax	**(5,821)**	**(2,154)**	**(3,300)**	**(11,275)**
Interest revenue	**-**	**-**	314	314
Depreciation and amortisation	(280)	(66)	(20)	(366)
Segment assets	**799**	**1,055**	**51,914**	**53,768**
Capital Expenditure	-	132	21	153
Segment liabilities	**242**	**281**	**14,238**	**14,761**
Cash flow information				
Net cash flow from Operating activities	(1,297)	(3,495)	(3,548)	(8,340)
Net cash flow from investing activities	-	(82)	293	211
Net cash flow from financing activities	-	-	-	-

i) Segment revenue reconciliation to the statement of comprehensive income

Reconciliation of revenue	**2011 $'000**	**2010 $'000**
Total segment revenue	3,980	4,966
Other revenue from continuing activities	427	314
Total revenue	4,407	5,280

Revenue from external customers by geographical locations is detailed below. Revenue is attributed to geographic location based on the location of the customers.

Revenue by geographical location	**2011 $'000**	**2010 $'000**
Australia	3,205	566
United States	733	4,714
Other	469	-
Total revenue	4,407	5,280

ii) 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 after tax. A segment's net operating profit after 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. Income tax expenses are calculated as 30% (2010:30%) of the segment's net operating profit.

Notes to the consolidated financial statements

18. SEGMENT REVENUE (continued)

Reconciliation of segment net operating profit after tax to net profit/loss before tax	2011 $'000	2010 $'000
Segment net operating profit/(loss) after tax	(4,122)	1,431
Other operating loss from continuing activities	(8,602)	(15,004)
Net loss on disposal of plant and equipment	-	-
Total net profit before tax per the statement of comprehensive income	(12,724)	(13,573)

iii) Segment assets reconciliation to the statement of financial position

In assessing the segment performance on a monthly basis, the executive management committee analyses the segment as described above and its relation to the segment assets. Segment assets are those operating assets of the entity that the management committee views as directly attributing to the performance of the segment. These assets include plant and equipment, receivables, inventory and intangibles and exclude available-for-sale assets, derivative assets and deferred tax assets.

Reconciliation of segment operating assets to total assets	2011 $'000	2010 $'000
Segment operating assets	3,901	1,854
Other operating assets from continuing activities		
Intangibles	44,657	47,046
Cash & cash equivalents	27,196	2,740
All other operating assets from continuing activities	823	2,128
Total assets per the statement of financial position	76,577	53,768

The analysis of the location of non-current assets other than financial instruments, deferred tax assets, pension assets is as follows

Non-current assets by geographical location	2011 $'000	2010 $'000
Australia	45,816	48,344
United States	2	1,700
Total assets	45,818	50,044

iv) Segment liabilities reconciliation to the statement of financial position

Segment liabilities include trade and other payables and debt. The Group has a centralised finance function that is responsible for raising debt and capital for the entire operations. Each entity or business uses this central function to invest excess cash or obtain funding for its operations.

Reconciliation of segment operating liabilities to total liabilities	2011 $'000	2010 $'000
Segment operating liabilities	2,207	523
Deferred tax liabilities	-	13,830
Other operating liabilities from continuing activities	1,424	408
Total liabilities per the statement of financial position	3,631	14,761

Notes to the consolidated financial statements

19. RELATED PARTY DISCLOSURE

The consolidated financial statements include the financial statements of Phosphagenics Limited and the subsidiaries listed in the following table.

Entity	Country of Incorporation	2011 Equity Interest	2010 Equity Interest	2011 Investment $'000	2010 Investment $'000
Vital Health Sciences Pty Ltd	Australia	100%	100%	27,111	27,111
Preform Technologies Pty Ltd	Australia	100%	100%	-	-
Adoil Pty Ltd	Australia	100%	100%	-	-
Phosphagenics Inc.	USA	100%	100%	-	-

Other transactions with key management personnel

The loss from operations includes no items of revenue and expense that resulted from transactions other than remuneration or equity holdings, with specified directors or their personally-related entities.

Don Clarke is a partner of law firm Minter Ellison. Minter Ellison provided professional services to the Group totalling $70,362 (2010: $2,970) during the year. These services were provided on normal commercial terms.

Performance Rights holdings of key management personnel

2011	01 Jan 11 Balance No.	Award date	Performance Rights awarded during the year No.	Fair value per performance right at award date	31 Dec 11 Balance No.	Not Vested No.	% of Remuneration consisting of Performance rights
Non Executive Directors							
Addison, J.L	-	1-May 2011	750,000	$0.07	750,000	750,000	20.1%
Clarke, D	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
James, S	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
Webb, S	-	1-May 2011	350,000	$0.07	350,000	350,000	10.6%
Executive Directors							
Rosen, H	-	1-May 2011	2,000,000	$0.07	2,000,000	2,000,000	7.9%
Ogru, E	-	1-May 2011	2,000,000	$0.07	2,000,000	2,000,000	8.0%
Key Management Personnel							
Banti, F	-	-	-	-	-	-	-
Gavin, P	-	3-Oct-2011	1,000,000	$0.07	1,000,000	1,000,000	3.5%
Arnott, A	-	3-Oct-2011	200,000	$0.07	200,000	200,000	1.2%
Butala, D	-	3-Oct-2011	1,000,000	$0.07	1,000,000	1,000,000	3.4%
Harrison, K	-	3-Oct-2011	500,000	$0.07	500,000	500,000	2.1%
Kyriakou, K	-	3-Oct-2011	750,000	$0.07	750,000	750,000	2.9%
Libinaki, R	-	3-Oct-2011	500,000	$0.07	500,000	500,000	1.9%
Totals	**-**		**9,750,000**	**-**	**9,750,000**	**9,750,000**	

All performance rights granted to key management personnel have been issued in accordance with the provisions of the Employee Conditional Rights Scheme (ECRS).

Notes to the consolidated financial statements

19. RELATED PARTY DISCLOSURE (continued)

Option holdings of key management personnel

2011	01 Jan 11 Balance No.	Granted as remuneration No.	Options Exercised No.	Net other change No.	31 Dec 11 Balance No.	Vested No.	Not Vested No.
Non Executive Directors							
Addison, J.L	-	-	-	-	-	-	-
Clarke, D	-	-	-	-	-	-	-
James, S	-	-	-	2,400,000	2,400,000	2,400,000	-
Webb, S	-	-	-	-	-	-	-
Executive Directors							
Rosen, H	-	-	-	-	-	-	-
Ogru, E	-	-	-	-	-	-	-
Key Management Personnel							
Banti, F	2,650,000	-	-	(2,650,000) [1]	-	-	-
Gavin, P	800,000	-	-	(400,000)	400,000	400,000	-
Arnott, A	-	-	-	-	-	-	-
Butala, D	250,000	-	-	-	250,000	250,000	-
Harrison, K	-	-	-	-	-	-	-
Kyriakou, K	-	-	-	-	-	-	-
Libinaki, R	650,000	-	-	**(400,000)**	250,000	250,000	-
Totals	**4,350,000**	**-**	**-**	**(1,050,000)**	**3,300,000**	**3,300,000**	**-**

1. F Banti is no longer a key management personnel due to his resignation on 29 July 2011, although his options remain exercisable

2010	01 Jan 10 Balance No.	Granted as remuneration No.	Options Exercised No.	Net other change No.	31 Dec 10 Balance No.	Vested No.	Not Vested No.
Non Executive Directors							
Addison, J.L	-	-	-	-	-	-	-
Clarke, D	-	-	-	-	-	-	-
James, S	-	-	-	-	-	-	-
Webb, S	-	-	-	-	-	-	-
Executive Directors							
Rosen, H	-	-	-	-	-	-	-
Ogru, E	-	-	-	-	-	-	-
Key Management Personnel							
Banti, F	2,650,000	-	-	-	2,650,000	2,650,000	-
Hodges, A	600,000	-	-	(600,000) [1]	-	-	-
Gavin, P	800,000	-	-	-	800,000	800,000	-
Arnott, A	-	-	-	-	-	-	-
Butala, D	250,000	-	-	-	250,000	250,000	-
Harrison, K	-	-	-	-	-	-	-
Kyriakou, K	-	-	-	-	-	-	-
Libinaki, R	650,000	-	-	-	650,000	650,000	-
Totals	**4,950,000**	**-**	**-**	**(600,000)**	**4,350,000**	**4,350,000**	**-**

1. A Hodges options lapsed upon his resignation on 29th July 2010.

All options granted to key management personnel have been issued in accordance with the provisions of the Employee Share Option Plan (ESOP).

Notes to the consolidated financial statements

19. RELATED PARTY DISCLOSURE (continued)

Shareholdings of Key Management Personnel

2011	01 Jan 11 Balance No.	Granted as remuneration No.	Net other change No.	31 Dec 11 Balance No.
Non Executive Directors				
Addison, J.L	19,000	-	3,473	22,473
Clarke, D	30,000	-	5,484	35,484
James, S	-	-	-	-
Webb, S	110,000	-	1,000	111,000
Executive Directors				
Rosen, H	64,226,436	-	-	64,226,436
Ogru, E	5,711,610	-	-	5,711,610
Key Management Personnel				
Banti, F	-	-	-	-
Gavin, P	99,000	-	-	99,000
Arnott, A	-	-	-	-
Butala, D	-	-	-	-
Harrison, K	-	-	-	-
Kyriakou, K	-	-	-	-
Libinaki, R	344,451	-	-	344,451
Totals	**70,540,497**	**-**	**9,957**	**70,550,454**

2010	01 Jan 10 Balance No.	Granted as remuneration No.	Net other change No.	31 Dec 10 Balance No.
Non Executive Directors				
Vizard, A.L	177,758	-	(177,758)	-
Addison, J.L	19,000	-	-	19,000
Mills, J	694,057	-	(694,057)	-
Ashton, M R D	263,043	-	(263,043)	-
Clarke, D	-	-	30,000	30,000
James, S	-	-	-	-
Webb, S	-	-	110,000	110,000
Executive Directors				
Rosen, H	64,226,436	-	-	64,226,436
Ogru, E	5,711,610	-	-	5,711,610
Key Management Personnel				
Banti, F	-	-	-	-
Hodges, A	52,420	-	(52,420)	-
Gavin, P	99,000	-	-	99,000
Arnott, A	-	-	-	-
Butala, D	-	-	-	-
Harrison, K	-	-	-	-
Kyriakou, K	-	-	-	-
Libinaki, R	344,451	-	-	344,451
Totals	**71,587,775**	**-**	**(1,047,278)**	**70,540,497**

Notes to the consolidated financial statements

19. RELATED PARTY DISCLOSURE (continued)

Transactions with other related parties

During the year, Vital Health Sciences Pty Ltd repaid $90,048 (2010: loaned $2,677,000) and Phosphagenics Inc. Borrowed $561,730 (2010: $516,488) from Phosphagenics Ltd (the parent entity). The loan is non trading in nature.

Phosphagenics Inc has insufficient net assets to repay the inter company loan balance to Phosphagenics Ltd (the parent entity). At 31 December 2011 Phosphagenics Ltd recognised an impairment of $521,604 (2010: $1,269,191) against the inter company loan with Phosphagenics Inc.

No amounts were provided for doubtful debts relating to debts due from related parties at reporting date (2010: Nil).

20. SUBSEQUENT EVENTS

There has not been any matter or circumstance, other than that referred to in the financial statements or 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.

21. NOTES TO THE CASH FLOW STATEMENT

(a) Reconciliation of cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents includes cash on hand and in banks and investments in money market instruments, net of outstanding bank overdrafts. Cash and cash equivalents at the end of the financial year, as shown in the statement of cash flows, is reconciled to the related items in the statement of financial position as follows:

	2011 $'000	2010 $'000
Cash at Bank	1,064	2,565
Short Term Deposits	26,132	175
	27,196	2,740

(b) Reconciliation of net loss after tax to net cash flows from operations

	2011 $'000	2010 $'000
Net Profit / (loss) after tax	1,106	(11,275)
Adjustments for:		
Revenue from licence fees received as shares	-	(3,149)
Depreciation, disposal and amortisation of non-current assets	2,650	366
Impairment of acquired intangible assets	-	7,660
Impairment of available-for-sale asset	706	1,449
Loss on disposal of available-for-sale asset	163	-
ESOP Expense	-	110
ECSR Expense	136	-
Other share based payments	58	203
Capitalisation of development expenses	-	(400)
Interest received	(216)	(342)
Changes in assets and liabilities:		
(Increase)/ decrease in trade receivables and other receivables	(1,959)	(13)
(Increase)/decrease in inventories	(442)	(464)
(Increase)/decrease in other current assets	(178)	172
(Decrease)/increase in deferred tax liability	(13,830)	(2,298)
(Decrease)/increase in trade payables and other payables	2,355	(378)
(Decrease)/increase in provisions	158	19
Net cash (used in) operating activities	(9,293)	(8,340)

Notes to the consolidated financial statements

22. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments comprise of cash and short-term deposits. Various financial instruments such as trade receivables and trade payables arise directly from operations. The Group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates.

The Group does not enter into, or trade, financial instruments including derivative financial instruments, for speculative purposes and manages its exposure to key financial risks, including interest rate and currency risk in accordance with the principals of prudent financial management. The objective of this is to support the delivery of the Group's financial targets whilst protecting future financial security.

Primary responsibility for identification and control of financial risks rests with the Audit Committee under the authority of the Board. The Board reviews and agrees policies for managing each of the risks including foreign exchange risk, interest rate risk and future cash flow forecast projections.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity instrument are disclosed in note 2 to the financial statements.

(b) Risk exposures and responses

Interest rate risk

The consolidated entity is only exposed to interest rate risk relating to cash at bank as it has no borrowings. At reporting date the Group has the following financial assets (no financial liabilities at 31 December 2011 or 31 December 2010) exposed to Australian Variable Interest Rates;

	2011 $'000	2010 $'000
Financial Assets		
Cash and cash equivalents	27,196	2,740

The following sensitivity analysis is based on the interest rate risk exposures in existence at 31 December 2011. If interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax loss and equity would have been affected as follows;

	Post Tax Loss Higher/(Lower)		Equity Higher/(Lower)	
	2011 $'000	2010 $'000	2011 $'000	2010 $'000
Judgements of reasonably possible movements:				
+ 1% (100 basis points)	272	27	-	-
-.5% (50 basis points)	(136)	(14)	-	-

The movements in profit are due to higher/lower interest income from variable rate term deposits and cash balances. There is no equity movement as there are no financial assets or financial liabilities which are designated as cash flow hedges. The sensitivity is higher in 2011 in comparison to 2010 due to the significantly higher cash and cash equivalents balance.

Foreign Currency Risk

The Group has transactional currency exposures principally due to its operations in the United States. Such exposure arises from sales or purchases by an operating unit in currencies, principally US dollars, other than the Groups presentation currency.

Approximately 44% of sales and royalties (2010: 90%) are denominated in currencies other than the presentation currency of the Group (Australian dollars), whilst approximately 89% (2010: 96%) of costs are denominated in the Groups presentation currency. At 31 December 2011 the Group had the following exposure to US dollar foreign currency not designated in cash flow hedges:

Notes to the consolidated financial statements

22. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

	2011 $'000	2010 $'000
Financial Assets		
Cash and cash equivalents	207	17
Trade and other receivables	306	-
	513	17
Financial Liabilities		
Trade and other payables	(543)	(10)
Net Exposure	(30)	75

(b) Risk exposures and responses

At 31 December 2011, had the Australian Dollar moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows;

	Post Tax Loss Higher/(Lower)		Equity Higher/(Lower)	
	2011 $'000	2010 $'000	2011 $'000	2010 $'000
Judgements of reasonably possible movements:				
Consolidated				
AUD/USD +10%	1	(2)	-	-
AUD/USD -5%	0	1	-	-

Credit risk management

Credit risk arises from the financial assets of the Group comprising cash and cash equivalents and trade and other receivables. Credit risk refers to the risk the counterparty will default on its contractual obligations resulting in financial loss to the Group. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral where appropriate, as a means of mitigating the risk of financial loss from defaults.

Group exposure to, and the credit ratings of, counterparties are continuously monitored and the aggregate value of transactions concluded are with approved counterparties. The Group does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics. The credit risk on liquid funds and financial instruments is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies. The Group measures credit risk on a fair value basis.

The carrying value of financial assets recorded in the financial statements, net of any allowances for losses, represents the Groups maximum exposure to credit risk. Maturity analysis of financial assets and liabilities based on management's expectations as follows;

Year Ended 31 December 2011	≤ 6 Months $'000	6-12 Months $'000	1-5 Years $'000	>5 Years $'000	Total $'000
Financial Assets					
Cash and cash equivalents	27,196	-	-	-	27,196
Trade and other receivables	928	-	-	-	928
	28,124	-		-	28,124
Financial Liabilities					
Trade and other payables	(3,358)	-	-	-	(3,358)
	(3,358)	-	-	-	(3,358)
Net Exposure	**24,766**	**-**	**-**	**-**	**24,766**

Notes to the consolidated financial statements

22. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(b) Risk exposures and responses

Liquidity risk management
Liquidity risk arises from the financial liabilities of the group and the group's subsequent ability to meet their obligations to repay their financial liabilities as and when they fall due. The Group continuously monitors cash flows and matches the maturity profiles of financial assets and liabilities.

Year Ended 31 December 2011	≤ 6 Months $'000	6-12 Months $'000	1-5 Years $'000	>5 Years $'000	Total $'000
Liquid financial assets					
Cash and cash equivalents	27,196	-	-	-	27,196
Trade and other receivables	928	-	-	-	928
	28,124	-		-	28,124
Financial liabilities					
Trade and other payables	(3,358)	-	-	-	(3,358)
	(3,358)	-	-	-	(3,358)
Net inflow/(outflow)	**24,766**	**-**	**-**	**-**	**24,766**

Year Ended 31 December 2010	≤ 6 Months $'000	6-12 Months $'000	1-5 Years $'000	>5 Years $'000	Total $'000
Liquid financial assets					
Cash and cash equivalents	2,740	-	-	-	2,740
Trade and other receivables	305	-	-	-	305
	3,045	-		-	3,045
Financial liabilities					
Trade and other payables	(816)	-	-	-	(816)
	(816)	-	-	-	(816)
Net inflow/(outflow)	**2,229**	**-**	**-**	**-**	**2,229**

Fair Value
Due to the short term nature of the financial instruments, their carrying value is assumed to approximate their fair value. The Group uses quoted market price in estimating the fair value of the available for sale investments, which is considered a level 1 in fair value hierarchy. There are currently no financial instruments with fair value estimated based on a level 2 or level 3 in the hierarchy.

Quoted market price represents the fair value determined based on quoted prices on active markets as at the reporting date without any deduction for transaction costs. The fair value of the available-for-sale financial investments are based on quoted market prices.

Capital Management
Management's objective is to ensure the entity continues as a going concern with the ability to fund future research and development requirements and commercialise the Groups products. Management also aim to maintain a capital structure that ensures the lowest cost of capital available and deliver optimal long term returns to shareholders.

Notes to the consolidated financial statements

23. INFORMATION RELATING TO PHOSPHAGENICS LIMITED ('the parent entity')

	2011 $'000	2010 $'000
Current assets	30,095	3,031
Total assets	76,137	50,989
Current liabilities	3,325	734
Total liabilities	3,354	734
Contributed equity	209,546	176,905
Accumulated losses	(138,262)	(128,179)
Employee equity benefits reserve	1,192	1,056
Other equity-settled benefits reserve	307	249
Total shareholder's equity	72,783	50,031
Loss of the parent entity	(10,083)	(11,801)
Total comprehensive income of the parent entity	(10,083)	(11,801)
Guarantees entered into by the parent entity in relation to the debts of its subsidiaries	-	-
Contingent liabilities of the parent entity	-	-
Contractual commitments by the parent equity for the acquisition of property, plant or equipment.	(584)[1]	(226)[1]

1. Non-cancellable operating leases relating to the rent of commercial property used for business operations.

Directors' Declaration

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

1. In the opinion of the directors:

    (a) The financial statements and notes of Phosphagenics Limited for the financial year ended 31 December 2011 are in accordance with the *Corporations Act 2001*, including:

        (i) Giving a true and fair view of its financial position as at 31 December 2011 and performance

        (ii) Complying with Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*

    (b) The financial statements and notes also comply with International Financial Reporting Standards as disclosed in note 2(a)

    (c) There are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable

2. This declaration has been made after receiving the declarations required to be made to the Directors in accordance with section 295A of the *Corporations Act 2001* for the financial year ended 31 December 2011.

On behalf of the Board

Jonathan Lancelot Addison
Chairman

21 February 2012

Melbourne

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Independent auditor's report to the members of Phosphagenics Limited

Report on the financial report

We have audited the accompanying financial report of Phosphagenics Limited, which comprises the consolidated statement of financial position as at 31 December 2011, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, 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 year's end or from time to time during the financial year.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal controls as the directors determine are necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 2a, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards*.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

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

Independence

In conducting our audit 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.

Opinion

In our opinion:

a. the financial report of Phosphagenics Limited is in accordance with the *Corporations Act 2001*, including:

   i giving a true and fair view of the consolidated entity's financial position as at 31 December 2011 and of its performance for the year ended on that date; and

   ii complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and

b. the financial report also complies with *International Financial Reporting Standards* as disclosed in Note 2a.

Report on the remuneration report

We have audited the Remuneration Report included in pages 9 to 17 of the directors' report for the year ended 31 December 2011. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Opinion

In our opinion, the Remuneration Report of Phosphagenics Limited for the year ended 31 December 2011, complies with section 300A of the *Corporations Act 2001*.

Ernst & Young

Ernst & Young

David Petersen
Partner
Melbourne
21 February 2012