2016 ANNUAL REPORT

Phosphagenics

ABN 32 056 482 403

CONTENTS

2016 OPERATIONAL HIGHLIGHTS

Corporate:

- A focus on our core business strategy, to develop and commercialise TPM®, is delivering results
- Significant progress in establishing strategic partnerships
- Resolution of several legacy issues, most significantly the ProPhase arbitration

Human Health:

- Established a successful partnership with Terumo Corporation, supporting the development of multiple TPM® enhanced product opportunities
- Extensive due diligence program with Terumo, resulting in execution of a non-binding term sheet in respect of the TPM®/Oxymorphone patch in Japan (January 2017)
- Successful reformulation of the TPM®/Oxymorphone patch with tesa Labtec GmbH
- R&D progress on a number of new TPM® injectable formulations
- Geographical expansion of the commercialised TPM®/Diclofenac gel

Highlights

2016: A year of continuing progress and achievement

As you know, we intitiated a major business restructure in 2015, and have made significant progress in 2016 towards achieving our core business strategic goal of developing and commercialising TPM®.

The establishment and strengthening of new and existing strategic partnerships, such as the relationship we established with Terumo Corporation in 2016, has been a focus this past year and provides the foundation for future growth and revenue streams for our shareholders.

Animal Health and Nutrition:

- Several trial activities have been completed demonstrating the value of TPM® as a feed additive to improve livestock performance (i.e. weight gain and feed efficiency)
- Studies in newly weaned pigs and poultry showed promising results
- A multi-farm trial initiated in dairy cattle, with completion expected in late 2017
- Results and ongoing studies have generated considerable interest from potential partners within the industry

Production and Personal Care:

- Significant improvements in the production processes as well as production capacity have been achieved
- Development and implementation of improved quality management systems
- Vital ET® product relaunch scheduled for 2017 to reinvigorate existing partnerships as well as identify and develop new sales channels
- Successful resolution of ProPhase arbitration has cleared the way for the sale of the BioElixia® brand

"We continue to engage in multiple active discussions with potential partners for our core TPM® technology across each of our three businesses, and we will continue to seek opportunities that deliver increasing returns for our shareholders."

Chairman's Report

Dear Shareholders,

The 2016 financial year has demonstrated significant progress for Phosphagenics as we have begun executing on our refined business strategy, focusing on developing and commercialising our core TPM® technology with external partnerships.

This has been a productive year for Phosphagenics, across all three business divisions: Human Health, Animal Health and Nutrition, and Production and Personal Care. I would like to highlight to shareholders some of our key achievements in 2016.

In the second quarter we entered a number of agreements with Terumo Corporation, a leading Japanese healthcare company. These agreements encompassed our TPM®/opioid patches and three additional pharmaceutical products. Following an extensive due diligence program, Terumo and Phosphagenics announced in January 2017 the signing of a non-binding term sheet giving Terumo exclusive rights to the TPM®/Oxymorphone patch, in Japan in exchange for an upfront payment. A definitive agreement is currently being negotiated. We believe this is a very important step for our Company, not only in terms of the return if the product is commercialized, but also in terms of the external validation and data package it provides to Phosphagenics towards deals in other markets.

Towards the end of 2016 we announced the successful reformulation of the TPM®/Oxymorphone patch with tesa Labtec GmbH, the German transdermal formulation specialists. The new formulation has enhanced chemical and physical properties technically tailored toward the Japanese and US markets, laying the foundation for future growth opportunities in other markets.

We also reorientated our internal R&D focus in 2016 towards TPM® enhanced injectables. We have several potential valuable assets that can improve the formulation of existing or novel compounds.

The Animal Health and Nutrition division continued to focus on trials assessing the commercial potential of TPM® as a feed additive to improve livestock performance. We now have promising results from studies in pigs and poultry supporting ongoing discussions with potential partners. We have also initiated our first placebo controlled study investigating TPM® in dairy cattle. We believe the collective results from all these studies increase the potential for deals in the Animal Health and Nutrition field.

The Company also made progress in the resolution of several corporate legacy issues in 2016. Significantly, the long awaited verdict in respect of our arbitration with ProPhase Labs Inc. was handed down in November returning the full use and ownership of the disputed license for over-the-counter (OTC) pharmaceutical applications for TPM® to Phosphagenics. No cash damages were awarded to either party. We believe this result provides considerable value for the Company, allowing completion of the sale of the BioElixia® brand and returning a valuable license back to Phosphagenics shareholders.

Additionally, the Board continues to support the pursuit of damages in the Mylan arbitration, given the high potential value of the TPM®/daptomycin product and the contractual breaches that the company believes have resulted in significant loss of its intellectual property and other commercial opportunities.

As we look to the year ahead, I believe Phosphagenics is very well placed to execute on the commercial opportunities that management are developing. We continue to engage in multiple active discussions with potential partners across each of our three businesses, and continue to seek opportunities that deliver increasing returns for our shareholders. We remain committed to our internal R&D program, and are on-track to deliver positive newsflow in 2017 including initial results on a number of TPM® enhanced injectable formulations.

To conclude, I would like to thank all Phosphagenics shareholders for their continued support of the Company as well as the Executive Team and staff for their continued hard work and dedication.

Peter Lankau
Chairman

CEO's Report

Dear Shareholders,

I am pleased to report that 2016 has been a year of progress and achievement for Phosphagenics. We advanced our strategic partnerships, resolved several longstanding legacy issues and strengthened our core proprietary TPM® technology which continues to provide value and commercialisation opportunities for shareholders.

Phosphagenics made significant progress in 2016 in a number of areas. The decision in 2015 to organise the business across three clear business divisions – Human Health, Animal Health and Nutrition, and Production and Personal Care – has been successful in enabling us to clearly focus our business objectives, commercialisation strategies and partnership discussion by division.

The Human Health division achieved some major milestones in 2016, most significantly entering into an exclusive due diligence agreement with Terumo Corporation in May 2016. In January 2017, following extensive due diligence, we were pleased to announce the signing of a non-binding term sheet with Terumo, the first step towards a definitive commercial agreement granting them the exclusive rights to develop, market and sell the TPM®/Oxymorphone patch in Japan. On signing the non-binding term sheet Phosphagenics received a payment of approximately $400,000. Terumo and Phosphagenics are now in the process of negotiating the formal agreement and, additionally, Terumo may consult with the Japanese regulatory agency before this is executed.

A major R&D activity undertaken during 2016 was the reformulation of the TPM®/Oxymorphone patch with tesa Labtec GmbH. The reformulation activity concluded in December with the announcement of the successful development of multiple suitable patch options with the desired commercially targeted attributes. These included attributes designed for both Japanese and non Japanese markets.

During 2016 we ramped up our internal R&D effort focusing on the development and production of TPM® enhanced injectables. TPM® enhanced injectables are attractive targets for a number of reasons, principally that we have the potential to produce multiple valuable assets in a relatively short period of time for a relatively low cost. We have begun work on a number of commercially attractive formulations with clear commercial value associated to their formulation related clinical unmet needs. The development effort is moving forward well and we believe that this has the potential to begin to provide great value for the Company in 2017 and beyond.

The Animal Health and Nutrition business focused its efforts in 2016 on developing the quality data demonstrating the value of TPM® enhanced feed for livestock. The trials undertaken were designed to demonstrate to potential partners the commercial value of TPM® as a feed additive to improve livestock performance. Over the year, Phosphagenics completed multiple studies in pigs and poultry and the announcements of the study results (particularly the results of the poultry study) has generated considerable interest amongst the industry. Phosphagenics management has already met, and continues to meet, with several interested parties. In addition to this, a study to investigate if TPM® as a feed additive in dairy cattle can promote improved fertility and milk quality is progressing well. This major multi-site, placebo controlled study has already reached its half way point and is on track to conclude the in-life portion in 2017.

“ The decision in 2015 to organise the business across three clear business divisions has been successful in enabling us to clearly focus our business objectives, commercialisation strategies and partnerships. ”

The Production and Personal Care business focused its efforts in 2016 on strengthening the quality and protection of TPM® production as well as increasing the manufacturing capacity of the existing plant. The result has been impressive, with a marked improvement in the production process, manufacturing capacity and a marked decrease in the overall “cost-of-goods”. This however coincided with a relatively disappointing sales year for TPM® and Vital ET®. In response a product refresh and relaunch is scheduled by our channel partners for 2017.

From a corporate perspective, Phosphagenics focused considerable effort and resources across two Arbitrations in 2016. A key achievement in 2016 was the completion of the ProPhase arbitration and the handing down of the associated decision. This arbitration between Phosphagenics and ProPhase Labs Inc. had been underway since October 2014 and related to a joint venture between our Company and ProPhase, established in 2010. The arbitration ruling handed down in November 2016 returned the full use and ownership of the licence for OTC pharmaceutical applications for TPM® back to Phosphagenics without cash damages being awarded to either party. We believe the outcome is a good result for the Company, and that the potential OTC pharmaceutical applications of TPM® are significant.

Phosphagenics’ second arbitration arose from a partnership agreement to develop a TPM® enhanced daptomycin injectable with Mylan. This will continue to be a considerable focus for the Company in 2017, both in terms of costs which are estimated at $3,000,000 in 2017 ($5,000,000 in total) and management time. Although the evidence in respect of the damages claim is yet to be filed, the Phosphagenics Board and Management believe that the claims are well founded and the action is necessary to ensure Phosphagenics is adequately compensated for loss and damage. We will endeavor to seek a satisfactory resolution and ensure shareholder interests are balanced against potential legal costs. We remain convinced of the merit of vigorously pursuing this arbitration.

Looking forward, we are well positioned in 2017 to capitalise on the successes and hard work of the past year. We are looking to grow the strong partnership with Terumo, bringing with it associated upfront milestone payments, expertise and valuable additional data. Additionally, multiple active discussions with other potential partners for our TPM® technology continue across each of the three business divisions. Overall, we believe that our business strategy is working and will continue to deliver value generating opportunities for our shareholders.

In the following pages, we provide further detail on the achievements of each business unit during 2016.

I would like to take this opportunity to thank my staff, fellow Board members and shareholders for their support during 2016. I look forward to updating you of our continued progress in the months ahead.

Human Health

Significant progress was made in the Human Health business over the course of 2016, in particular:

- The establishment and consolidation of a number of key partnerships with Terumo Corporation supporting the development of multiple TPM® enhanced product opportunities, including TPM®/ Oxymorphone and TPM®/Propofol;
- The successful conclusion of an extensive due diligence program with Terumo, resulting in the execution of a non-binding term sheet in respect of the TPM®/Oxymorphone patch in Japan (January 2017);
- The successful reformulation of the TPM®/ Oxymorphone patch with tesa Labtec GmbH;
- Progress on a number of new TPM® enhanced injectable formulations, including TPM®/Propofol (Terumo), as well as work towards a portfolio of new injectable products; and
- Further geographical expansion of the commercialised TPM®/Diclofenac gel.

The Terumo partnerships to date focus on the development and commercialisation of four (4) potential product candidates, the TPM®/ Oxymorphone patch, and three other TPM® product opportunities. The most advanced of the non-patch projects is a TPM® enhanced Propofol injectable which is moving rapidly forward with a new formulation identified, a new patent application filed and a development plan instituted. The other two projects are yet to be disclosed.

In parallel with the due diligence assessment of the TPM®/ Oxymorphone patch, Terumo also undertook due diligence on Phosphagenics' TPM®/Oxycodone patch. Terumo's formal exclusive due diligence period in respect of the TPM®/Oxycodone patch expired in February. Phosphagenics is now free to actively discuss this opportunity with other companies that have shown interest in the TPM®/Oxycodone patch.

During 2016 Phosphagenics expanded the license given to Themis Medicare Ltd to sell TPM®/Diclofenac gel in an additional 16 countries. The TPM®/Diclofenac gel is now to sold in India and Georgia through both Themis and Novartis under the trade name Voveran® TPM. There are additional regulatory packages under submission for approval in several more countries under the license. While revenues at present are relatively small, sales growth in 2016 was promising. Further expansion of sales through this channel are being explored and provide a clear opportunity to increase revenue without further development risk. Work to identify additional commercial partners for the existing product as well as other potential product extensions are ongoing.

“ This data package is being used to demonstrate the value potential of TPM® with potential animal feed partners, and the announcement has already generated considerable interest within the industry. ”

Animal Health and Nutrition

The focus of this business in 2016 was on trial activities aimed at consolidating and proving the commercial potential of TPM® as a feed additive in the mind of potential partners.

In December 2016 we announced the completion of our poultry feed efficiency study in broilers. This study was significant as it was the first to monitor TPM®'s performance across an animals full life cycle. The study, undertaken at a large research facility in Australia, tested a broad range of TPM® doses and produced a range of promising results that paralleled our findings from the previous weaner pig study completed in January 2016.

As announced in December, the “TPM® enhanced feed” was able to significantly ($P<0.05$) improve the average live weight (at day 28) and average daily gain (day 0-28) of test broilers. Feed containing 10ppm TPM® was found to be optimal and produced the largest numerical improvement in live weight, average daily gain and feed conversion rate without any significant change in total average feed intake.

This data package is being used to demonstrate the value potential of TPM® with potential animal feed partners, and the announcement has already generated considerable interest within the industry.

Also initiated in 2016 was Phosphagenics' first multi-sited dairy cattle trial. This will continue to be a major focus for the Animal Health and Nutrition business in 2017. This study assesses if TPM® can promote improved milk quality and fertility in dairy cattle. The study is progressing well and has now reached the midpoint of the in-life portion with the conclusion on track for the fourth quarter of 2017.

In March 2017, we also announced the signing of a settlement deed with IAH which resolves contractual issues that had arisen over the past year, with respect to sales of TPM® based animal nutrition products. Phosphagenics and IAH mutually agreed to cease all of their licences. While the details remain confidential, this solution is beneficial for Phosphagenics shareholders as it allows the Company to move forward and focus on new business opportunities.

Production and Personal Care

“ The focus on the fundamentals of this business unit has produced marked improvements... ”

The Production and Personal Care business focused its efforts in 2016 on strengthening the quality, protection and capacity of TPM® production whilst also looking for clear savings in costs and new customers. The development and implementation of an improved quality management system (QMS) further strengthens the Company’s production platform and partnership potential.

The focus on the fundamentals of this business unit has produced marked improvements, in the production process, a 50 fold increase in TPM® manufacturing capacity and in the overall “cost-of-goods” – all resulting in improvements in financial margin and the Company’s ability to respond to any increase in demand associated with existing and new potential partnerships.

Although we saw some promising trends, overall orders for TPM® and Vital ET® did not grow in 2016 mainly due to sales by our former partner Integrated Animal Health Pty Ltd (IAH) not reaching their minimum targets as well as our global Vital ET® distributor, Ashland, working through “overstocking” from prior years. Ashland remain committed to Vital ET® and are planning a potential product refresh and relaunch in 2017. Enthusiasm for the product remains strong and a product refresh is expected to reinvigorate existing partners as well as identify and develop new customer partnerships.

Despite a number of approaches from multiple interested parties, the sale of the BioElixia® brand had to be put on hold pending the outcome of ProPhase arbitration. The successful resolution of the ProPhase arbitration has now allowed the Company to refocus the effort to secure a buyer. Discussions with interested parties are in progress.

The Board

MR PETER LANKAU BS

Independent non-executive director

Chairman of the Board

Member of nomination and remuneration committees

DR GREG COLLIER PhD

Independent non-executive director

Chairman of remuneration committee

Member of nomination and audit and risk committees

DR ROSS MURDOCH PhD

Chief Executive Officer and managing director

Member of nomination committee

DR GEERT CAUWENBERGH PhD

Independent non-executive director

Chairman of nomination committee

Member of remuneration and audit and risk committees

MR DAVID SEGAL BComm, LLB

Non-independent non-executive director

"Looking forward, we are well positioned in 2017 to capitalise on the successes and hard work of the past year."

Phosphagenics Limited

ABN 32 056 482 403

Annual Financial Report

for the year ended 31 December 2016

Contents

Directors' Report

Your directors are pleased to submit this report on Phosphagenics Limited and its controlled entities for the year ended 31 December 2016.

Directors

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

Information on Directors

Currently in Office:

PETER LANKAU BS

Independent non-executive director (appointed April 2015, elected May 2015)

Chairman of the Board

Member of nomination, remuneration and audit and risk committees

Mr Lankau served as President and CEO and Director of US based pain management Company, Endo Pharmaceuticals Inc. from 2005 to 2008. He previously served as the Company's President and Chief Operating Officer and as Senior Vice President, US Commercial Business. While CEO, he led the Company to become an industry leader in specialty pharma, as well as developing its pipeline which included 12 product acquisitions and/or licensing transactions.

More recently, Mr Lankau was Executive Chairman of Nautilus Neurosciences Inc., a commercial stage, private equity-backed, neurology-focused specialty pharmaceutical Company, which sold its business to Depomed Inc. in December 2014 for more than US$50 million. Mr Lankau was Chairman and CEO of Logical Therapeutics Inc., a development stage Company which developed novel compounds for inflammatory disease. Currently Mr Lankau is a Principal in the consulting firm, Lankau Consulting LLC.

Other current directorships of listed entities:
ANI Pharmaceuticals Inc., Cipla Limited

Former directorships of listed entities in last 3 years: None.

Nil ordinary shares in Phosphagenics Limited.

DR ROSS MURDOCH PhD

Chief Executive Officer and managing director (appointed April 2015)

Member of nomination committee

Dr Murdoch joined Phosphagenics as CEO in January 2015 and was appointed as director in April 2015. He has more than 25 years' experience as a leader within the global healthcare, pharmaceutical and biotechnology industries. He has held senior management and executive positions in Australia, the USA and Europe, with responsibility for the strategy, development and commercialisation of products, product portfolios and the building and rebuilding of new and existing businesses.

Highlights of his career include Senior Vice President at Shire Pharmaceuticals (one of the world's leading specialty pharmaceutical companies), based in the USA and Switzerland, where he founded and grew both the Emerging Products Business and Haematology Business, and President and COO of Prana Biotechnology Limited based in Australia.

Dr Murdoch has a BSc degree with honours from Monash University, a PhD in Clinical Pharmacology from the University of Melbourne and additional postgraduate training in Health Economics from Monash University Business School. He is also a Graduate of the Australian Institute of Company Directors.

Nil ordinary shares in Phosphagenics Limited

15,000,000 performance rights in Phosphagenics Limited.

DR GEERT CAUWENBERGH PhD

Independent non-executive director (appointed February 2014, elected May 2014)

Chairman of nomination committee

Member of remuneration and audit and risk committees

Dr Cauwenbergh is very experienced in the life sciences sector, having started his career with Janssen Research Foundation in Belgium in 1979. He moved to the USA in 1994 to take up the role of Vice President Product Development for Johnson & Johnson. Subsequently he was appointed Global Vice President of R&D for Johnson & Johnson Consumer companies worldwide.

In 2001 Dr Cauwenbergh left Johnson & Johnson and founded Barrier Therapeutics, a Company developing drugs to treat skin diseases. In 2008 Barrier Therapeutics was acquired by Stiefel Laboratories. At the time of acquisition the Company's annual revenues had reached approximately US$45 million.

Dr Cauwenbergh is currently President and CEO of NASDAQ-listed Company RXi Pharmaceuticals. In this role he has guided RXi Pharmaceuticals through its initial public offering and helped it successfully prepare and submit its first US FDA Investigational New Drug Application.

Other current directorships of listed entities:
RXi Pharmaceuticals Inc., Moberg Pharma AB

Former directorships of listed entities in last 3 years:
Ablynx NV.

20,000 ordinary shares in Phosphagenics Limited

1,000,000 options in Phosphagenics Limited

DR GREG COLLIER PhD

Independent non-executive director (appointed April 2015, elected May 2015)

Chairman of remuneration and audit and risk committees

Member of nomination committee

Dr Collier has more than 20 years' experience spanning operational, clinical and scientific aspects of pharmaceutical research, development and commercialisation. He has led the planning and execution of multiple commercial transactions including in and out licensing deals and major M&A activities, and he has successfully taken a drug from discovery through to regulatory approval.

Notably, Dr Collier steered ChemGenex Pharmaceuticals Limited from a research-based Company with a market capitalisation of $10 million to a Company with completed clinical trials and regulatory dossiers submitted to the FDA and EMA. In 2011, ChemGenex was sold to Cephalon Inc. (now subsidiary of Teva Pharmaceuticals Industries Limited) for $230 million.

Prior to his commercial pharmaceutical career, Dr Collier had an outstanding academic career resulting in over 150 peer reviewed publications, and senior authorship on 33 patents. Dr Collier was the inaugural Alfred Deakin Professor at Deakin University, and also held positions at Melbourne University, Monash University and the University of Toronto. In 2010, Dr Collier was awarded the Roche Award of Excellence for his contribution to the biotechnology industry.

Dr Collier is currently Executive Chairman of listed drug development Company, Invion Limited.

Other current directorships of listed entities: Invion Limited

Former directorships of listed entities in last 3 years: None.

Nil ordinary shares in Phosphagenics Limited.

DAVID SEGAL BComm, LLB

Non-independent non-executive director (elected 19 May 2016)

Mr Segal was the Investor Relations Manager at Phosphagenics from 2011 to 2015. Prior to this he worked for over 30 years in stockbroking, including setting up, raising capital for and running Trent Securities which was absorbed into Shaw Stockbroking in 1992. Mr Segal has been a shareholder of Phosphagenics since 1999.

Mr Segal has a law/commerce degree from Melbourne University and is a graduate of the Australian Institute of Company Directors

Other current directorships of listed entities: None

Former directorships of listed entities in last 3 years: None.

14,931,281 ordinary shares in Phosphagenics Limited.

Former Directors:

NATHAN DRONA MBA

Independent non-executive director until his retirement on 18 May 2016

Mr Drona had over a 15-year career in international investment banking and a strong background in corporate finance, executing over 25 global banking and M&A engagements in biotech, medical devices and healthcare.

Mr Drona was Chairman of the audit and risk committee and a member of the remuneration committee.

Other current directorships of listed entities: None

Former directorships of listed entities in last 3 years: Alchemia Ltd.

Nil ordinary shares in Phosphagenics Limited

1,000,000 options in Phosphagenics Limited.

Company Secretary

Ms Legg has been the Company Secretary since December 2015 and Chief Financial Officer since January 2013. She holds a Bachelor of Economics from Macquarie University, a Diploma of Law from the Legal Practitioners Board (NSW) and is currently undertaking the Graduate Diploma in Corporate Governance with the Governance Institute of Australia. She is also a member of the Australian Institute of Company Directors.

Operating and Financial Review

Principal Activities

The principal activities of the Company are the development, production, sale and licensing of products incorporating its patented platform technology TPM®, for the pharmaceutical, skin care and animal health and nutrition industries.

Result

The financial report for the financial year ended 31 December 2016, and the results herein, have been prepared in accordance with Australian Accounting Standards.

The consolidated loss after income tax attributable to ordinary shareholders for the financial year ended 31 December 2016 was $17,314,000 (2015: $20,120,000). The net operating cash outflow for the year was $6,412,000 (2015: $8,705,000), with a cash balance at 31 December 2016 of $6,092,000 (2015: $12,395,000).

Dividends

No dividends were paid or declared during the period and no dividends are recommended in respect of the financial year ended 31 December 2016.

Review of Financials

Income statement

The reported net loss after tax was $17,314,000 (2015: $20,120,000).

Total revenue for the year was $1,588,000 (2015: $2,190,000), with sales of Vital ET® by the Company's partner Ashland decreasing to $818,000 (2015: $1,669,000) primarily due to restructuring of their sales force and resetting of commercial targets ahead of the product relaunch in mid-2017. This was partially offset by increased royalties and licence fees of $636,000 (2015: $310,000).

Expenses from continuing operations were $20,587,000 (2015: $24,058,000) and included an intangibles impairment loss of $7,207,000 (2015: $7,837,000). Excluding non-cash expenses (impairment losses, amortisation and depreciation), total other expenses in 2016 were 16% lower at $10,908,000 (2015: $12,953,000), with employee and director expenses 41% lower at $3,428,000 (2015: $5,852,000).

Balance sheet

At the end of December 2016, the Company held $6,092,000 in cash and cash equivalents (2015: $12,395,000). The Company expects to receive a further $2,294,000 (2015: $2,442,000) from the R&D tax incentive scheme on 1 March 2017.

Statement of cash flows

The net operating cash outflow for the year was lower at $6,412,000 (2015: $8,705,000), with similar receipts from customers at $2,140,000 (2015: $1,989,000) and government grants at $2,442,000 (2015: $2,665,000) as in prior years but with lower payments to suppliers and employees at $10,994,000 (2015: $13,519,000).

Net cash inflow from financing activities was nil (2015 nil).

Audit report

The Company's auditor has included an "emphasis of matter" paragraph in the Audit Report relating to the Company's ability to continue as a going concern (refer Note 1(a)(iii)).

Earnings per share

	2016	2015
Basic loss per share	($0.0137)	($0.0159)
Diluted loss per share	($0.0137)	($0.0159)

Review of Operations

Phosphagenics' continues to execute on its strategy of developing and commercialising its TPM® technology to deliver value to shareholders.

The Company made significant progress in 2016, in a number of areas.

Human Health Business

The Human Health Business advanced on multiple fronts in 2016:

- The successful reformulation of the TPM®/Oxymorphone patch with tesa Labtec GmbH
- The establishment and consolidation of several key agreements with Terumo supporting the development of multiple TPM® enhanced product opportunities, including TPM®/Oxymorphone and TPM®/Propofol
- Progress on several new TPM® enhanced injectable formulations, including TPM®/Propofol (Terumo), as well as beginning work on a portfolio of new injectable products.
- Further geographical expansion of the commercialised TPM®/Diclofenac gel.

Terumo Partnership

The Company granted Terumo Corporation a 6-month exclusive option to undertake technical/scientific and commercial due diligence on both the TPM®/Oxymorphone and TPM®/Oxycodone patches for the Japanese market. Following a three-month extension, Phosphagenics announced in January 2017 the signing of a non-binding term sheet with Terumo for TPM®/Oxymorphone patch in Japan. Terumo would

have, upon the signing of a definitive agreement, the exclusive rights to develop, market, and sell the TPM®/Oxymorphone patch in Japan. Phosphagenics has received a non-refundable payment of 35 million JPY (about ~A$400,000) associated with the signing of the term sheet, in exchange for granting exclusive negotiation rights. The 3 month extended exclusivity period granted to Terumo to evaluate the TPM®/Oxycodone patch expired in February 2017 and no further extension has been requested.

Terumo and Phosphagenics will finalise a development plan for the TPM®/Oxymorphone patch and Terumo may consult with the Japanese regulatory agency (Pharmaceutical and Medical Devices Agency) before signing a definitive agreement.

In addition to the TPM®/opioid patches, Phosphagenics is working with Terumo to develop a TPM® enhanced propofol injectable formulation as well as additional products containing the TPM® technology (the specific active ingredients have yet to be named). This work continues to proceed well.

Themis Partnership Expansion

During 2016, Phosphagenics licensed Themis to sell TPM®/Diclofenac gel in an additional 16 countries. The TPM®/Diclofenac gel is presently sold in India through Themis Medicare India under the trade names Instanac® TPM and Aquadol® TPM, and through Novartis under the trade name Voveran® TPM. It is also sold in Georgia through Humanity under the trade name Diclofenac-HUMANITY. There are additional regulatory packages being submitted for approval in several more countries under the licence. Sales continued to grow, with the highest quarter sales for the product in the third quarter of 2016, although revenues remain modest to date. Expansion of sales through this existing channel is being explored as an opportunity to increase revenue without further development risk. Work to identify additional commercial partners for the existing product as well as potential product extensions continue.

Successful TPM® Patch Reformulation

Phosphagenics has previously demonstrated in multiple Phase 1 human trials that a TPM®/Oxymorphone patch can deliver therapeutically relevant concentrations of Oxymorphone. In preparation for submission of an FDA IND, it was noted that the previous patch had adhesion and stability issues that would require significant external expertise to overcome. In May 2015 the Company announced that it would reformulate the TPM®/Oxymorphone patch with tesa Labtec GmbH, (the company associated with the successful development of the most recent TPM®/Oxycodone patch). The reformulation program was designed to ensure that the new formulation would meet broad market requirements including the Japanese pain market, given the relationship between Phosphagenics and Terumo. The reformulation was successfully completed in 2016. The reformulated patch has increased fluid flux in-vitro compared to the previous clinical patch, and has enhanced physical and chemical stability across a range of standard tests. Phosphagenics now has multiple patch candidates that appear to have attributes needed for commercialisation in both Japan and the USA.

TPM® Injectable Products

As promised to shareholders, in 2016 Phosphagenics began exploring other injectable molecules that would benefit from combination with TPM®. A range of candidate molecules with poor solubility were tested independently in the US for compatibility with the TPM® technology. TPM® was found to dissolve most of the molecules tested without the addition of adverse or problematic co-solvents typically used. Work towards the finished formulations and formal development plans for select molecules has initiated. Potential product candidates will be announced when partnerships are finalised.

The collaboration between Phosphagenics and Terumo to develop a TPM® enhanced propofol formulation continues to progress well.

TPM®/Daptomycin injectable

Phosphagenics' first injectable partnership with Agila Specialties Private Limited (Agila) was for the development and commercialisation of a TPM®/Daptomycin injectable. Agila was subsequently acquired by the global generics company, Mylan Incorporated, in 2014. Daptomycin is an antibiotic indicated for the treatment of complicated skin and skin structure infections and staphylococcus aureus bloodstream infections. Sales of the branded daptomycin product "Cubicin" reached around US$1 billion per annum prior to robust competition from generic companies entering the market in September 2016, shown in IMS Health data below.

Product	Company	Q3 2016 $US	Q4 2016 $US
Cubicin	Merck	$263M	$81M
Cubicin RF	Merck	$18M	$26M
Daptomycin	Fresenius	$7M	$70M
Daptomycin	Teva	$5M	$67M
TOTAL		$293M	$245M

Source: IMS Health, National Sales Perspectives, Feb 2017

The TPM®/Daptomycin licencing agreement signed in 2012 forms part of the arbitration dispute with Mylan. To date Mylan has not launched the TPM®/Daptomycin product and Phosphagenics has not been informed by Mylan of either its registration or launch plans. Therefore Phosphagenics is not aware of when it might begin to receive royalty payments it is entitled to under the licencing agreement.

For further information see "Mylan Arbitration" and "Legal" sections below.

Operating and Financial Review (cont.)

Animal Health and Nutrition

The Animal Health and Nutrition business is a large and attractive opportunity for Phosphagenics. The Company has several development programs underway. In 2016 the primary focus was on trial activities aimed to assess the commercial potential of TPM® as a feed additive to improve feed efficiency.

Phosphagenics completed multiple studies assessing TPM® as a feed additive in pigs and poultry.

TPM® was shown to deliver positive improvements in Feed Conversion Rate (FCR) when supplemented in the first 14 days post weaning - a very important time in a pig's life cycle when it is subjected to a number of stresses which are known to impact performance. The performance benefits however appeared to be specific to TPM® offered at this nursery phase in pigs, with the performance (FCR) benefit not extended into pigs supplemented only in later grower / finisher pigs.

A further performance study was carried out in the later part of 2016 in poultry (broilers) to investigate if TPM® could deliver FCR benefits to other species. This was the first single study to monitor TPM® performance across an animal's full life cycle. It found that TPM® as a feed additive has the potential to deliver a commercially viable benefit to livestock producers, with TPM® enhanced feed offering improvements in FCR and average weight gain.

The promising data across multiple livestock species continues to increased interest in the TPM® technology from potential partners.

TPM® is also believed to have the potential to enhance milk quality and conception rates in dairy cattle. To test this the Company initiated a study in dairy cattle in July 2016. This multi-sited, blinded, placebo controlled study will assess milk quality and immune endpoints, during the most critical lactation and production periods, as well as any improvements in fertility, due to TPM® treatment. The study is due to complete in late 2017.

Phosphagenics' partnership with Integrated Animal Health Pty Ltd (IAH) to manufacture and sell animal nutrition products incorporating TPM® in Australia continued into 2016 however it did not result in any sales. The companies entered into a dispute regarding minimum royalty payments and this matter is still on-going.

Production and Personal Care

Phosphagenics continues to produce TPM® products such as TPM® and Vital ET® for commercial sale.

A focus on operational efficiencies, plant improvement and production planning throughout 2016 has delivered substantial improvements in production, order completion, lower operating costs and improved margins. The associated improvement in capacity will support an expanded number of partnerships.

An enhanced quality assurance project was undertaken further strengthening the end-to-end quality and reaffirming that Phosphagenics' standards meet the quality requirements required by partners.

Phosphagenics continues to work closely with Ashland, the global distributor of Vital ET®, with the potential of a product refresh and relaunch in 2017. Although overall orders from Ashland for Vital ET® were down in 2016, enthusiasm for the product remains strong and a refresh will provide the prospect for improved sales over the next few years.

Phosphagenics' direct partner Le Métier de Beauté launched two additional products containing its patented technology: - Vital ET® Recovery Boost Body and Vital ET® Recovery Boost Face. This prestigious brand now has 20 products using the TPM® technology in its range.

The successful resolution of the ProPhase arbitration has allowed the Company to refocus the effort to find a buyer for the BioElixia® brand. Several interested parties have been identified and discussions are in progress.

Legal Matters

Disappointingly for a biotech company, Phosphagenics has spent significant funds on legal expenses to defend the arbitration claim made against it in the ProPhase matter and to lodge a significant arbitration claim against Mylan.

Mylan Arbitration

In 2011-12, Phosphagenics and Agila Specialties Private Limited (Agila) entered into an R&D agreement and commercial licencing agreement to develop a TPM® enhanced injectable daptomycin formulation: Agila being the injectables business of Strides Arcolab, an Indian company listed on the Bombay Stock Exchange (532531) and National Stock Exchange of India (code STAR). In 2013, Mylan Inc. (Mylan) (NASDAQ code MYL: market cap approximately US$22b) announced that it had acquired the Agila injectables business from Strides Arcolab for up to US$1.75 billion. In purchasing Agila, Mylan acquired the TPM®/daptomycin agreements and inherited any associated disputes. In January 2016, Phosphagenics lodged a dispute notice in association with the Agila TPM®/Daptomycin agreements. In accordance with the relevant agreements, the dispute was referred to arbitration in Singapore. The arbitration will be heard by a single arbitrator.

The arbitration notices issued by Phosphagenics assert that Mylan is liable for breaches of several provisions under the two relevant agreements, misrepresentations, breaches of confidence and/or unjust enrichment in relation to intellectual property amongst others. Phosphagenics has lodged multiple individual damages claims of substantial quantum. While an assessment of the quantum has been made, it is important to note that they are preliminary and the ultimate value of the claims remain subject to ongoing refinement having regard

to independent expert input, which is yet to be received in final form. The directors also note that there is no guarantee or certainty in respect of the outcome of these arbitration proceedings and if unsuccessful, the arbitration may not result in any positive result for Phosphagenics and may even result in costs being awarded against Phosphagenics. Similarly, even if successful there is no certainty that the arbitrator will award any quantum of damages and, if a quantum is awarded it may be materially less than the current preliminary estimate.

Mylan reported as part of the Agila acquisition that, at the time of closing they retained up to US$250 million of the Agila purchase price as contingent consideration to settle outstanding matters arising from the acquisition. Although some claims have already been made and settled against this sum it is important to note that Phosphagenics' claims are not limited by the initial amount, nor by any remaining sum, and Mylan remains responsible to meet any additional sum. Mylan have not made any financial counter-claims.

All Phosphagenics costs associated with the litigation to date have been expensed. It remains the intention of the Company to investigate the potential for additional funding to cover the remaining costs of this action. The Company remains confident that suitable funding is available and is actively investigating third party funding and other options to raise funds. The Company will advise shareholders in due course of any suitable developments in this regard. No budgetary inclusion has been made for an adverse cost award or any potential damages awards related to this action. Phosphagenics has retained Corrs Chambers Westgarth, who are highly experienced in intellectual property and arbitration law.

The arbitration process is currently well advanced and in-line with the timetable. The arbitration hearing has been set down for hearing in October 2017. During the arbitration process the TPM®/Daptomycin agreements between Mylan and Phosphagenics remains in force.

ProPhase Arbitration

In November 2016, the arbitration ruling from the American Arbitration Association determined that the full use and ownership of the license for OTC pharmaceutical applications for TPM® be returned to Phosphagenics. No cash damages were awarded to either party. Phosphagenics' legal costs have now been fully expensed and paid. The ruling was a pleasing outcome for Phosphagenics, with the ownership of these rights representing a valuable opportunity to shareholders. This ruling clears the way for Phosphagenics to progress with the targeted sale of the BioElixia® brand, which had been put on hold while the arbitration was underway.

R&D Tax Incentive

For the period ended 31 December 2016 the Company has recorded R&D tax incentive as Other Income of $1,833,000 (2015: $2,279,000). The Company expects to receive $2,294,000 for the R&D tax incentive for the period July 2015 to June 2016 on 1 March 2017.

Site Consolidation

In January 2017 the Company consolidated its manufacturing site and Company headquarters, and continues manufacturing at its production facilities in Clayton, near Melbourne. The Company changed its registered address and principal place of business to reflect this. This will provide considerable savings for the Company, in the order of $200,000 per year.

Employee Long Term Incentive Scheme

In September 2016 the long term incentive arrangement for its employees and directors was replaced with a three-year Conditional Options Scheme which more appropriately aligns employee performance to the creation of shareholder wealth. For further information see Remuneration Report (d)(iii).

Subsequent events

The Australian Tax Office has confirmed a refund of $2,294,000 for the R&D tax incentive will be paid on 1 March 2017.

Business Strategy and Future Developments

The Company will continue to use its cash resources to invest in research and development activities, licensing activities, and in legal costs to support its contractual rights.

The Company continues to pursue commercialisation of all its development pipeline via licencing agreements appropriate for the stage of each product's development as well as continuing to look at new opportunities to build value for shareholders. The underlying business strategy of developing and commercialising TPM® within the three relevant Business areas (Human Health, Animal Health and Nutrition and Personal Care) remains unchanged from the previous year.

Human Health

The underlying business strategy of developing and commercialising TPM® for dermal and injectable application remains unchanged from the previous year. The Company's key Human Health focus continues to be the development of its two TPM® enhanced opioid patch products, with an expanding focus on TPM®'s application in enhancing injectable formulations. The significant progress made during 2016 in TPM® injectables is expected to lead to candidates with the potential to enter the clinic in 2017/18.

Operating and Financial Review (cont.)

Animal Health and Nutrition

The underlying business strategy of developing and commercialising TPM® as a feed additive for animal livestock remains unchanged from the previous year. The Company's key Animal Health and Nutrition focus continues to be enhanced feed efficiency in poultry and pigs and improved health and fertility in dairy cattle. The initial "feed efficiency" trials were completed and reported in 2016. Animal Health and Nutrition trials will continue through 2017 with dairy cattle data expected in quarter four of 2017.

Production and Personal Care

Phosphagenics continues to produce TPM® products such as TPM® and Vital ET® for commercial sale. The key focus into 2017-18 is improved profit through increased top line revenue predominantly via improved sales volume and improved overall margin via increased efficiencies.

Phosphagenics intends to sell its branded personal care business BioElixia®, following the positive outcome of the ProPhase arbitration.

Legal

The Mylan arbitration will be a considerable focus for the Company in 2017 both in terms of costs, which are estimated at $5,000,000 in total ($3,000,000 in 2017), and management time. Although the evidence in respect of the damages claim is yet to be filed, the Board believes that the claims are well founded and necessary to ensure the Company is properly compensated for the loss and damage it has suffered and continues to suffer. The current estimate of the damages may increase or decrease as fact and expert evidence is lodged. The arbitrator may also fully accept, partially accept or not accept the basis of calculation of the damages. It is also possible that the parties may seek to settle the matter, which may result in the Company considering it a commercial advantage to accept an offer that is different from the amount claimed.

The directors note that there is no guarantee or certainty in respect of the outcome of these arbitration proceedings. Similarly, even if successful there is no certainty in respect of the quantum of damages which may be awarded (and which may be materially less than the current preliminary estimate) or its recoverability.

At the Annual General Meeting to be held in May 2017 shareholder approval will be sought to replace the CEO's current long term incentive scheme with the a scheme that is the same as that of the employees (see Remuneration Report (d)(iii)). Additionally shareholder approval will be sought to issue three-year options to non-executive directors on similar terms to employees apart from the performance hurdles, which are not attached in order to comply with ASX corporate governance recommendations relating to director remuneration.

Material Business Risks

As Phosphagenics is in the biotechnology and pharmaceutical sectors, it undertakes both research and development, which by its nature is high-risk. The Company is subject to normal business risks, including but not limited to government policies, exchange rate fluctuations, labour market conditions and other factors which are outside the control of the Board and management. Material risks specific to the group include, but are not limited to:

- Scientific, technical and clinical – product development requires a high level of scientific investigation, the outcomes of which cannot be known beforehand. Activities are experimental in nature so risk of failure or delay is a real possibility. Key activities, such as product manufacture, preclinical testing and clinical trials, are outsourced to specialist contract organisations, where there are risks in managing performance, costs, timelines and quality outcomes.
- Regulatory – products and their safety data may not be approved by the regulatory agency (e.g., FDA) to proceed to next stage of clinical development or whose approvals are required before the products can be sold in market.
- Financial – the group does not receive sufficient income to cover its operating expenses. Although there are sufficient current cash reserves, there is no certainty that additional funding from raising capital or from other sources will not be required and there is no certainty that this funding will be available.
- Intellectual Property – the Company needs to ensure it operates without infringing other patents and ensure it adequately protects its own existing patents and new experimental outcomes.
- Commercialisation – the Company's strategy is to partner with large and medium sized pharmaceutical, specialty pain companies or global animal health companies to finalise and market its products. There are risks in establishing and maintaining these relationships and in the manner in which the partners execute the agreements.
- Key personnel – the execution of the Company's development plan relies on key personnel of its scientific teams. The ability to attract and retain these personnel is critical.
- R&D Incentives – the Company is eligible for cash rebates of its research and development programs, which are subject to changes in government policy.
- Legal risks – The Company must continue to protect its intellectual property and legal rights as these are core to its success and overall value. These commitments have significant on-going costs but uncertain outcomes.

Operating and Financial Review (cont.)

- Arbitration award risks – a successful arbitral award against Mylan Laboratories Ltd may not be voluntarily paid and may require enforcement in the courts. Despite recent law changes in India this process can be difficult and time consuming, and may result in additional costs and delays in receipt of any damages awarded.

Health and Safety

The Board, CEO and senior management team are committed to creating a positive environment for the health and wellbeing of our employees and anyone affected by our operations, including contractors and visitors. The Company has adopted a Health and Safety Policy and has established a Health and Safety Steering (HSS) committee structure as part of its overall framework. The HSS committee, which includes representatives of management and employees from each operational area, is a forum for management and employees to consult and monitor health and safety matters. The HSS committee meets regularly throughout the year.

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.

The Company is not aware of any material breaches of any environmental regulations.

Directors Meetings

The number of meetings of the Company's Board of Directors and of each committee held during the year and the number of meetings attended by each director were:

	Board	Audit and Risk	Nomin -ation	Remun -eration
P Lankau	14 of 14	1 of 1	2 of 2	2 of 2
N Drona	9 of 9	2 of 2	-	-
G Cauwenbergh	14 of 14	3 of 3	2 of 2	2 of 2
G Collier	13 of 14	3 of 3	2 of 2	2 of 2
R Murdoch	14 of 14	-	2 of 2	-
D Segal	5 of 5	-	-	-

The table above illustrates the number of meetings attended compared with the number of meetings held during the period that the director was in office or was a member of the committee.

Remuneration Report

The remuneration report sets out remuneration information for non-executive directors, executive directors and other key management personnel of the group. The report contains the following sections:

a) Key management personnel disclosed in this report

b) Remuneration governance

c) Use of remuneration consultants

d) Executive remuneration policy and framework

e) Relationship between remuneration and Phosphagenics Limited's performance

f) Performance review and development

g) Non-executive director remuneration policy

h) Voting and comments made at the Company's 2016 Annual General Meeting

i) Details of remuneration

j) Service agreements

k) Details of share-based compensation and bonuses

l) Equity instruments held by key management personnel

a) Key management personnel

Non-executive and executive directors (see pages 1 to 2 for details about each director)	
P Lankau	(from 13 April 2015)
G Cauwenbergh	
G Collier	(from 13 April 2015)
N Drona	(until 18 May 2016)
R Murdoch	(from 14 January 2015)
D Segal	(from 19 May 2016)
L Gozlan	(until 12 May 2015)
H Rosen	(until 8 July 2015)

Other key management personnel	
Name	**Position**
P Gavin	Chief Scientific Officer
A Legg	Chief Financial Officer
J Amon	VP, Product Development (until 28 September 2015)
R Libinaki	General Manager, Animal Health and Nutrition (from 9 April 2015)
G Moses	General Manager, Production and Personal Care (from 9 April 2015)
J Rosen	General Counsel (until 1 January 2016)
A Stojanovic	VP, Business Development and Commercial Operations

Changes since the end of reporting period: None.

b) Remuneration Governance

The Remuneration Committee, currently consisting of three independent non-executive directors, advises the Board on remuneration policies and practices generally, including key management personnel, and makes specific recommendations on remuneration packages and other terms of employment for non-executive directors and executive directors. The objective of the Company's remuneration policies is to attract and retain the highest calibre of employee whilst promoting and rewarding workplace culture and contributions to Company performance. The framework balances employee reward with achievement of strategic objectives and the creation of value for shareholders.

c) Use of remuneration consultants

If remuneration consultants are to be engaged to provide remuneration recommendations as defined in section 9B of the Corporations Act 2001, then they are engaged by, and report directly to, the remuneration committee. No remuneration consultants were engaged to provide remuneration services during the financial year.

d) Executive remuneration policy and framework

In determining executive remuneration, the Board aims to ensure that the remuneration practices are:

- Competitive and reasonable, enabling the Company to attract and retain key talent
- Aligned to the Company's strategic and business objectives and creation of shareholder value
- Transparent and easily understood
- Acceptable to shareholders.

The executive remuneration framework has three components:

- Base pay and benefits
- Short-term incentives (including equity component)
- Long-term incentives through participation in Phosphagenics Employee Conditional Rights Scheme and Equity Incentive Plan.

A combination of these components comprises an executive's total remuneration, with base pay and benefits at an appropriate level to competitive market benchmarks.

(i) Base pay and benefits

Australian based executives receive their base pay and benefits structured as a Total Remuneration Package (TRP) which may be delivered as a combination of cash and prescribed non-financial benefits at the executive's discretion. Superannuation is included in the TRP.

US based executives receive their base pay and health and dental insurance. Phosphagenics has also established a defined contributions pension plan (401(k)) for all its US employees and contributes under Safe Harbour matching contributions to a maximum of 4% or US$8,500 per annum. There are no guaranteed base pay increases in any executives' contracts.

Remuneration Report (cont.)

(ii) Short term incentives

In December 2014, the Board approved the Short Term Incentive Program for all employees to reward for achievement of defined Company and agreed individual performance expectations for 12 months ending 31 December each year.

The Program was modified by the Board in December 2015 to take into account the timing of appointment of the new CEO as well as the significant restructure announced in October 2015. In 2015 and 2016 pro-rata periods were applied with bonuses paid for the period January 2016 to June 2016 in August 2016 and bonuses for the period July 2016 to December 2016 are forecast to be paid in March 2017. For 2017, the bonus period will be set for the entire year.

The available bonus will comprise:

- 33.3% corporate component set by the Board based on organisational targets which align with the Company's overall strategic goals.
- 33.3% individual key performance targets set at beginning of each period, aligning with corporate with organisational targets as well as team and personal targets, the achievement of which will be assessed by the employee's immediate manager.
- 33.3% individual constructive behaviours as assessed by the employee's immediate manager.

The bonus outcomes are discretionary and will be based on performance criteria outlined above, the overall health of the business and other factors which may arise. The Board approves the total bonus pool, the corporate component as well as the total awarded to each executive.

Eligible executives, apart from the CEO, can receive up to 10% of their fixed base salary as a bonus should they meet expected KPIs and up to 20% if KPI targets are exceeded. The CEO is eligible to receive up to 40% of his fixed base salary. The bonus will be paid in March of each year, unless modified, in the form of cash.

US employees are under separate contracts and are entitled to a discretionary annual cash bonus of up to 20% of base pay or other agreed amount based on achieving KPI targets set each year.

(iii) Long term incentives

The long-term incentive remuneration scheme was replaced during 2016 with an Equity Incentive Plan (EIP) under which options (EIP 2016 Option) were issued to employees, apart from the CEO. It was the view of the Board that the milestones set in the previous Phosphagenics' Employee Conditional Rights Scheme (ECRS) could not be achieved and therefore did not provide the requisite incentive. The previous ECRS remains on foot for the CEO but it is intended to put the CEO's proposed grant under the EIP to the shareholders for approval at the AGM in May 2017. Conditional Rights held by employees (ECRS Scheme 1), other than the CEO, were forfeited in October and December 2016.

The Phosphagenics' EIP is designed to reward staff in a manner that aligns remuneration with the creation of shareholder value and to ensure that all staff, including executives, views their relationship with the Group as a long-term one. As such the EIP has been offered to all staff who met the minimum service criteria, with vesting requiring continuation of service.

Equity Incentive Plan 2016 Option (EIP 2016 Option)

The EIP 2016 Option allows eligible employees to acquire Shares at a price of $0.023, which was set at 10% over the 5-day VWAP at the invitation date, subject to certain vesting conditions being achieved. The options will vest and become exercisable in tranches as follows:-

- one-third of the Options will vest on 11 September 2017 (Tranche 1 Vesting Date), subject to the volume weighted average of the prices of Shares traded on ASX in any 5 consecutive trading days (5 Day VWAP) during the period commencing 3-months immediately prior to and extending to 3-months post the Tranche 1 Vesting Date being greater than 50% above the Invitation VWAP ($0.021), calculated to be $0.032;
- one-third of the Options will vest on 10 September 2018 (Tranche 2 Vesting Date), subject to any 5 Day VWAP during the period commencing 3-months immediately prior to and extending to 3-months post the Tranche 2 Vesting Date being greater than 100% above the Invitation VWAP ($0.021), calculated to be $0.042;
- one-third of the Options will vest on 9 September 2019 (Tranche 3 Vesting Date), subject to any 5 Day VWAP during the period commencing 3-months immediately prior to and extending to 3-months post the Tranche 3 Vesting Date being greater than 150% above the Invitation VWAP ($0.021), calculated to be $0.053.

All current and prospective employees, including executive and non-executive directors, 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.

Employee Conditional Rights Scheme approved by Board January 2015 (ECRS Scheme 2)

Under the terms of the ECRS Scheme 2, 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 (VWAP) is not less than $0.25 at any time prior to 31 December 2017, then 100% of the Performance Rights will vest. The VWAP price has not been met and all shares remain unvested.

Alternatively, vesting of the Rights is conditional on Phosphagenics achieving the following conditions:

Remuneration Report (cont.)

Milestone 1 (16.5% of Rights awarded any two of five conditions achieved, or 33% of Rights awarded if any four of five conditions achieved, by 31 December 2015) - Completion of treatment phase of Phase 2a clinical trial of the TPM®/Oxycodone patch, Submission of a US IND for the TPM®/Oxymorphone patch, completion of treatment phase of a clinical trial of the TPM®/Oxymorphone patch, selection of new priority molecule demonstrating transdermal delivery and gross revenues from sales of TPM® products or commercialisation of not less than $6 million. This milestone was not achieved as only one of the five conditions was met and accordingly Rights relating to Milestone 1 remain unvested.

Milestone 2 (34% of Rights awarded if any three of the following achieved by 31 Dec 2016) – Submission of a US IND for any product other than TPM®/Oxymorphone, completion of a Phase 2 clinical trial of the TPM®/Oxycodone patch under a US IND, completion of a Phase 2 clinical trial of the TPM®/Oxymorphone patch under a US IND, completion of a licencing agreement which exceeds $20 million, gross revenues from sales of TPM products of not less than $10 million, and completion of a Phase 1 clinical trial of a product containing TPM® not previously in the development pipeline as at 31 December 2014. Rights relating to Milestone 1 remain unvested.

Milestone 3 (33% of Rights awarded if any one of the following achieved by 31 Dec 2017) - Completion of a Phase 3 clinical trial for TPM®/Oxycodone patch or TPM®/Oxymorphone patch, execution of commercial agreements with minimum upfronts of $10 million and total value of at least $100 million, spin-off of the Company's pain portfolio by way of IPO and gross revenues from sales of TPM® products of not less than $15 million.

All rights issued to employees under this scheme were forfeited in October 2016 and December 2016.

Employee Conditional Rights Scheme approved May 2015 (ECRS Scheme 3)

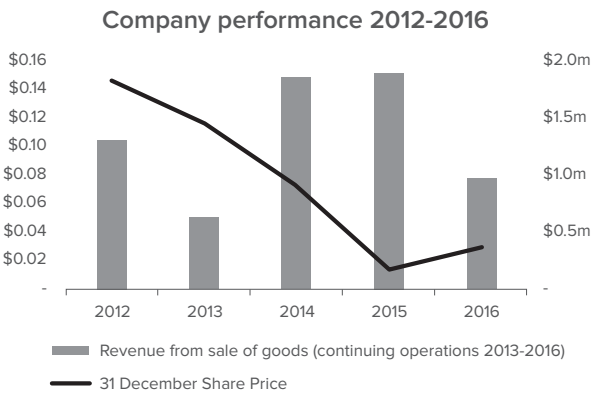
Under the terms of the ECRS Scheme 3, approved by the shareholders at the Annual General Meeting held on 18 May 2015 for the Chief Executive Officer (CEO), the rights will vest if certain non-market or market conditions are fulfilled. One of the key overriding conditions of the Scheme is that if the 10 day Volume Weighted Average Price is not less than $0.25 at any time prior to 31 December 2017, and provided the CEO remains an employee, 33.3% of the Performance Rights will vest on or after 31 December 2015, 33.3% will vest on or after 31 December 2016 and the remainder unvested on or after 31 December 2017. All other vesting conditions are the same as for ECRS Scheme 2.

This scheme remains on foot for the CEO and it is intended to put the CEO's proposed grant under the replacement EIP, with the same vesting conditions as the EIP 2016 Option, to the shareholders for approval at the AGM in May 2017. This will ensure the CEO has an appropriate long-term incentive which aligns with those of the employees.

e) Relationship between remuneration and Phosphagenics Limited's performance

The Company's remuneration policies align executive reward with the interests of shareholders. The main focus is on growth in shareholder value through achievement of share price growth. Typical of companies in this biotech sector, performance goals are not necessarily linked to commercial performance measures. Remuneration is set based on short term key performance indicators (KPIs) as outlined in section (ii) as well as other factors such as benchmarking, overall performance, behaviours and the Company's ability to pay.

The following chart shows the Company's annual revenues (2014 to 2016 from continuing operations) and year end share price over the five-year period from 1 January 2012 to 31 December 2016.



f) Performance review and development

All staff, including executives, participate in a formal bi-annual performance review and development process. Establishment of objectives, setting KPIs and planning relevant staff development are documented and agreed at the beginning of the year. A formal half-year review occurs, the outcome of which contributes to the annual salary review. The full-year review contributes to the award of short-term incentives.

g) Non-executive director remuneration policy

On appointment to the Board, all non-executive directors are given a letter of offer that summarises the proposed remuneration, relevant to the office of director. Non-executive directors receive a Board fee and the chair of the audit and risk committee receives an additional fee for chairing that committee, see table below.

Annual Director's Fees	2015 and 2016 ($)
Chair	110,000
Other non-executive directors	55,000
Audit and risk committee - Chair	10,000

Remuneration Report (cont.)

Non-executive director's fees are reviewed annually by the Board and no change was made to fees in 2016.

Fees and payments are determined within an aggregate non-executive director's pool limit approved by shareholders. The aggregate currently stands at $400,000 and was approved by shareholders at 2014 Annual General Meeting. This amount, or part thereof, is divided among non-executive directors as determined by the Board and reflecting time and responsibility related to the Board and committees. The aggregate paid to non-executive directors was $284,896 (2015 $261,128). Directors fees include statutory superannuation contributions as required under Australian superannuation guarantee legislation.

The non-executive directors do not receive retirement benefits nor do they participate in any short-term incentive programs. Non-executive directors are entitled to participate in the long-term incentive scheme as detailed in the Executive remuneration section.

h) Voting and comments made at the Company's 2016 Annual General Meeting

Of the votes cast on the Company's remuneration report for the 2015 financial year, 77% were in favour of the resolution. The Company did not receive any specific feedback at the Annual General Meeting or throughout the year on its remuneration policies.

i) Details of remuneration

The following tables show details of the remuneration received by the group's key management personnel for the current and previous financial year.

2016	Short-term employee benefits			Post-employment benefits	Long-term benefits	Share based payment		
	Cash salary & fees $	Cash Bonus $	Benefits $	Super-annuation $	Long service leave $	Perform-ance rights $	Options $	Total $
Non executive directors								
P Lankau	110,000	-	-	-	-	-	-	110,000
G Collier	55,860	-	-	5,307	-	-	-	61,167
G Cauwenbergh	55,000	-	-	-	-	-	-	55,000
N Drona [1]	24,812	-	-	-	-	-	-	24,812
D Segal [2]	30,974	-	-	2,943	-	-	-	33,917
Sub-total	276,646	-	-	8,250	-	-	-	284,896
Executive directors								
R Murdoch	371,538	49,000	-	37,905	953	2,286	-	461,682
Other key management personnel								
P Gavin	200,770	16,000	-	20,520	3,333	(200)	3,916	244,339
A Legg	183,021	19,000	-	18,675	4,387	(200)	7,833	232,716
R Libinaki	170,483	13,600	-	17,584	3,513	(200)	3,916	208,896
G Moses	169,704	13,600	-	17,584	4,202	(200)	3,916	208,806
J Rosen [3]	1,905	-	6,456	4,206	-	(200)	-	12,367
A Stojanovic	328,326	26,769	25,613	28,474	-	(200)	3,916	412,898
Total	**1,702,393**	**137,969**	**32,069**	**153,198**	**16,388**	**1,086**	**23,497**	**2,066,600**

[1] Retired 18 May 2016

[2] Elected 19 May 2016

[3] Ceased employment 1 January 2016

Remuneration Report (cont.)

2015	Short-term employee benefits			Post-employment benefits	Long-term benefits	Termination	Share based payment	
	Cash salary & fees $	Cash Bonus $	Benefits $	Superannuation $	Long service leave $	$	Performance rights $	Total $
Non executive directors								
P Lankau [1]	65,509	-	-	-	-	-	-	65,509
L Gozlan [2]	35,888	-	-	3,409	-	-	-	39,297
N Drona	65,886	-	-	-	-	-	-	65,886
G Cauwenbergh	52,971	-	-	-	-	-	-	52,971
G Collier [1]	34,215	-	-	3,250	-	-	-	37,465
Sub-total	254,469	-	-	6,659	-	-	-	261,128
Executive directors								
R Murdoch [3]	353,621	-	104,896	32,142	332	-	1,524	492,515
H Rosen [4]	89,533	-	-	27,768	3,719	292,291	-	413,311
Other key management personnel								
J Amon [5]	149,576	-	-	18,940	-	50,228	-	218,744
P Gavin	200,385	9,570	-	19,909	3,333	-	200	233,397
A Legg	177,520	8,140	-	17,287	1,763	-	200	204,910
R Libinaki [6]	133,239	-	-	11,985	10,008	-	200	155,432
G Moses [6]	130,113	-	-	11,754	3,502	-	200	145,569
J Rosen [7]	330,200	19,395	12,089	5,519	-	150,323	200	517,726
A Stojanovic	322,315	21,381	23,651	12,616	-	-	200	380,163
Total	**2,140,971**	**58,486**	**140,636**	**164,579**	**22,657**	**492,842**	**2,724**	**3,022,895**

[1] Appointed 13 April 2015

[2] Resigned 12 May 2015

[3] Appointed 14 January 2015

[4] Resigned 8 July 2015

[5] Redundant 28 September 2015

[6] Appointed 9 April 2015

[7] Ceased employment 1 January 2016

The relative proportions of remuneration that are linked to performance and those that are fixed are as follows:

	Fixed remuneration		At risk – STI		At risk - LTI	
Name	**2016 %**	**2015 %**	**2016 %**	**2015 %**	**2016 %**	**2015 %**
Executive directors						
R Murdoch	89%	100%	11%	-	-	-
H Rosen	-	100%	-	-	-	-
Other key management personnel						
J Amon	-	100%	-	-	-	-
P Gavin	91%	96%	7%	4%	2%	-
A Legg	89%	96%	8%	4%	3%	-
R Libinaki	91%	100%	7%	-	2%	-
G Moses	91%	100%	7%	-	2%	-
J Rosen	100%	96%	-	4%	-	-
A Stojanovic	93%	94%	6%	6%	1%	-

Remuneration Report (cont.)

j) Service agreements

Remuneration and other terms of employment for the executives are formalised in service agreements which include a position description and sets out duties, rights and responsibilities as well as entitlements on termination. All service agreements include provision that Company can dismiss the employee at any time without notice if the employee is guilty of serious misconduct, becomes unable to pay debts or is found guilty by court of a criminal offence.

The entitlement to participate in Phosphagenics Employee Incentive Schemes is governed by the Scheme document and may not be specifically detailed in the service agreement.

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.

Name	Term of agreement and notice period	Base salary including superannuation #	Termination payments ##
R Murdoch Chief Executive Officer	No fixed term 6 months	$383,250	6 months [1]
P Gavin Chief Scientific Officer	No fixed term 1 month	$219,000	1 month
A Legg Chief Financial Officer	No fixed term 1 month	$208,050	1 month
R Libinaki General Manager, Animal Health and Nutrition	No fixed term 3 months	$189,435	3 months
G Moses General Manager, Production and Personal Care	No fixed term 3 months	$189,435	3 months
A Stojanovic VP, Business Development and Commercial Operations	No fixed term 14 days	US$241,065	30 days [2]

Base salary quoted as at 31 December 2016, reviewed annually by the remuneration committee.

Base salary payable if the Company terminates employee with notice and without cause.

[1] Entitled to severance pay of 6 months base pay where there has been significant or unreasonable diminution of powers or responsibilities, subject to employee giving 30 days notice within 6 months of such change.

[2] Entitled to severance pay of 33.3% of base pay due to sale or other disposition of all or substantially all of Company's asset or business by way of merger, consolidation or spin-off.

k) Details of share-based compensation and bonuses

Options Granted During the Year to Key Management Personnel

In 2016 22,500,000 (2015 nil) options were awarded to key management personnel. The 2016 issued options were valued at weighted average of $0.008 each, are non-quoted, have strike price of $0.023, vesting dates in September 2017, 2018 and 2019 and an expiry date of five years. No options vested during the year.

Performance Rights Granted During the Year to Key Management Personnel

Nil (2015: 26,200,000) ECRS Rights were awarded to key management personnel during the year, of which nil vested.

l) Equity instruments held by key management personnel

The tables below show the number of:

i) options over ordinary shares in the Company;

ii) performance rights holdings granted under the Employee Conditional Rights Scheme;

iii) shares in the Company; and

that were held during the financial year by key management personnel of the group, including their close family members and entities related to them. There were no shares granted during the reporting period as compensation.

Remuneration Report (cont.)

i) Option holdings

2016	Grant date	Strike Price	Balance at start of year No.	Granted No.	Other changes No.	Balance at end of year No.	Vested No.
Non executive directors							
N Drona [1]	23 May 2014	$0.17	1,000,000	-	(1,000,000)	-	1,000,000
G Cauwenbergh	23 May 2014	$0.17	1,000,000	-	-	1,000,000	1,000,000
Other key management personnel							
P Gavin	6 October 2016	$0.023	-	3,750,000	-	3,750,000	-
A Legg	6 October 2016	$0.023	-	7,500,000	-	7,500,000	-
R Libinaki	6 October 2016	$0.023	-	3,750,000	-	3,750,000	-
G Moses	6 October 2016	$0.023	-	3,750,000	-	3,750,000	-
A Stojanovic	6 October 2016	$0.023	-	3,750,000	-	3,750,000	-

[1] Retired 18 May 2016

ii) Performance rights holdings

2016	Grant date	Fair value per option at award date	Balance at start of year No.	Granted No.	Other changes# No.	Balance at end of year No.	Vested No.
R Murdoch	18 May 2015	$0.0004	15,000,000	-	-	15,000,000	-
P Gavin	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-
A Legg	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-
R Libinaki	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-
G Moses	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-
J Rosen	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-
A Stojanovic	28 April 2015	$0.0005	1,600,000	-	(1,600,000)	-	-

Other changes during the year relate to forfeiture or cancellation of rights.

No performance rights vested or were exercised during the year.

1,600,000 performance rights were cancelled during the year in line with scheme terms in which rights are forfeited when personnel cease employment. A further 8,000,000 rights were forfeited in October 2016 as part of the replacement of the long term incentive plan.

iii) Share holdings

2016 Name	Balance at start of year	Received during year on exercise of option	Received vesting of rights to deferred shares	Other changes during the year	Balance at end of year
P Lankau	-	-	-	-	-
G Cauwenbergh	20,000	-	-	-	20,000
G Collier	-	-	-	-	-
N Drona [1]	-	-	-	-	-
R Murdoch	-	-	-	-	-
D Segal [2]	-	-	-	14,931,281	14,931,281
P Gavin	99,000	-	-	-	99,000
A Legg	266,500	-	-	-	266,500
R Libinaki	338,915	-	-	-	338,951
G Moses	-	-	-	-	-
J Rosen [3]	2,000,068	-	-	(2,000,068)	-
A Stojanovic	64,000	-	-	-	64,000

[1] Retired 18 May 2016

[2] Appointed 19 May 2017

[3] Ceased employment 1 January 2016

Share Options

Share options convertible to ordinary shares on issue at the date of this report. All options are unquoted on the Australian Securities Exchange.

Issuing entity	Shares under option No.	Exercise price $	Expiry date
Phosphagenics	3,000,000	$0.17	22 May 2019
Total	**3,000,000**		

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 Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191. The Company is an entity to which this Instrument 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 (the Act). In accordance with section 300(9) of the Act, further details have not been disclosed due to confidentiality provisions contained in the insurance contract.

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 29 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.

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

Peter Lankau
Chairman

28 February 2017
Melbourne

pwc

Auditor's Independence Declaration

As lead auditor for the audit of Phosphagenics Limited for the year ended 31 December 2016, I declare that to the best of my knowledge and belief, there have been:

(a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

(b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Phosphagenics Limited and the entities it controlled during the period.

Anton Linschoten
Partner
PricewaterhouseCoopers

Melbourne
28 February 2017

PricewaterhouseCoopers, ABN 52 780 433 757
2 Riverside Quay, SOUTHBANK VIC 3006, GPO Box 1331, MELBOURNE VIC 3001
T: 61 3 8603 1000, F: 61 3 8603 1999, www.pwc.com.au

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Corporate Governance Statement

This statement summaries the corporate governance policies and procedures adopted by the Phosphagenics' Board of Directors ("Board") and discloses the extent to which the Company has followed the ASX Corporate Governance Council's Corporate Governance Principals and Recommendations (3rd Edition)("ASX Principles") during and since the reporting period. The Board aims to ensure the Company operates with a corporate governance framework and culture that is relevant, practical and cost effective for the current size and stage of development of the business.

Principle 1: Lay solid foundations for management and oversight

1.1 Roles and Responsibilities of Board and Management

The relationship between the Board and senior management is critical to the group's long term success. The Board acts in the best interests of the Company as a whole and is accountable to shareholders for the overall direction, management and corporate governance of the Company and the Group.

Responsibilities of the Board

The responsibilities of the Board include oversight, accountability and approval of:

(a) Strategic Issues
- Approving management's corporate strategy and performance objectives;
- Providing strategic advice to management;
- Monitoring performance and implementation of strategy and ensuring appropriate resources are available.

(b) Shareholding items
- Issuing shares, options or conditional rights;
- Determining the amount of dividend.

(c) Financial items
- Approving and monitoring financial and other reporting;
- Approving and monitoring the progress of major capital expenditure, capital management, acquisitions and divestitures;
- Reporting to shareholders.

(d) Risk and control
- Overseeing groups control and accountability system;
- Reviewing and ratifying systems of risk management, internal compliance and control, and legal compliance to ensure appropriate compliance frameworks are in place.

(e) Board and senior management
- Appointment, performance assessment and, if necessary, removal of CEO;
- Ratifying appointment and, where appropriate, removal of CFO and Company Secretary;
- Ratifying other senior executive appointments, organisational changes and senior management remuneration policies and practices;
- Approving succession plans for management;
- Monitoring performance of the Board both collectively and individually;
- Recommending directors for nomination and removal.

(f) Other Board responsibilities
- Monitoring and ensuring compliance with best practice corporate governance requirements;
- Approving board committee charters.

Further details are outlined in the Board Charter which can be found at
www.phosphagenics.com/investors/corporate-governance

Responsibilities of the CEO

Responsibility for day to day management and administration of the Group is delegated by the Board to the Chief Executive Officer ("CEO"). The CEO manages the Group in accordance with the strategy, plans and policies approved by the Board.

1.2 Director appointment and election

The Board undertakes appropriate checks before appointing any new candidates as directors, which include review by the Nomination Committee against the board skills matrix, interview by all directors and appropriate reference checking. All material information regarding any director proposed for re-election will be included in the Explanatory Information to the relevant Notice of Meeting.

1.3 Written Agreements with Directors and Senior Executives

New directors receive a letter of appointment which outlines the key terms and conditions of their appointment. Senior executives and all employees are required to sign employment agreements which set out the key terms of their employment.

1.4 Responsibilities of the Company Secretary

The Company Secretary is responsible for providing administrative support to the Board and its Committees. The Company Secretary is accountable directly to the Board, through the Chair, on all matters relating to proper functioning of the Board. The specific responsibilities of the Company Secretary are outlined in the Board Charter which is available at www.phosphagenics.com/investors/corporate-governance

1.5 Diversity Policy

The Company recognises the value contributed to the organisation by employing people with varying skills, cultural backgrounds, ethnicity and experience. The Company believes its diverse workforce is the key to continued growth and improved productivity and performance. The Company actively values and embraces diversity of its employees and is committed to creating an inclusive workplace where everyone is treated equally and fairly, and where discrimination, harassment and inequality are not tolerated. While the Company is committed to fostering diversity at all levels, gender diversity continues to be a priority for the group.

In accordance with the Diversity Policy the Nomination Committee established measureable objectives for achieving gender diversity and has conducted an assessment of the progress towards them.

Diversity Objective	Measurement	FY16 Performance
Program activity - training	Senior Executive Leadership development training in culture and leadership.	Completed by July 2016.
Program activity - new policy development	Development and implementation of Performance and Development Planning.	Not completed due to staff restructure.
Program participation in training of policies	Employees undertaking training	100% participation
Program participation in flexible working arrangements	An increase in employees working under flexible working arrangements	Achieved. Employees working under flexible working arrangements increased from 7 to 9.
Program participation in leave purchase requests	An increase in participation	There were no requests for purchased leave in 2016.
Program participation in performance and development planning	Employees having performance plans	100% of employees had performance plans. No development plans were undertaken in 2016.
Program effectiveness reflected in gender diversity by job level	Increase in 2015 rates	See gender diversity table below.
Program effectiveness reflected in gender diversity in recruitment	Increase in 2015 rates	There were no new employees in 2016.
Program effectiveness reflected in gender diversity in turnover	Decrease in 2015 rates	Achieved. Excluding redundancies, 0% of departures were female, compared to 50% in 2015.

It is noted that although Phosphagenics has a high level of gender diversity, due to the low overall number of staff and the significant restructure which occurred, a change of a few employees can have significant impact on the Company's performance in respect of its measurable diversity objectives.

The table below outlines gender diversity within Phosphagenics for 2016 and 2015:

	Whole organisation		Senior Executive		Board	
	2016	2015	2016	2015	2016	2015
Total	18	22	6	7	5	5
Female	10	12	2	2	0	0
% Female	56%	55%	33%	29%	0%	0%

1.6 Board, committee and director performance

The Board and its committees undertake an annual self-assessment of their performance using a questionnaire. Each director is asked to consider matters such as strategies, reporting and control, management, board meetings and the composition and functioning of the Board and its Committees. The questionnaires are collated by the Company Secretary and reviewed by Chairman of the Board. The outcomes and recommendations are discussed by the Board.

The Chairman undertakes a one-on-one assessment with each of the non-executive directors with respect to individual director performance.

The Board, Committees and Chairman undertook performance assessments in February 2017 and they were conducted in accordance with these procedures.

1.7 CEO and senior executive performance

The Company has a performance management program which includes annual assessments of performance in February each year. The program has been modified in 2015 to take into account the timing of appointment of the new CEO as well as the significant corporate restructure announced in October 2015. A pro-rata assessment took place in June 2016 and again in December 2016, before the Company returns to its standard annual assessment program in 2017. For further details on process of evaluation of senior executives please see Remuneration Report pages 21 to 27.

Principle 2: Structure the Board to add value

2.1 Nomination committee

The Board has a nomination committee which is composed of four directors, the majority independent, and is chaired by an independent director. At the date of this report the committee consisted of the following members:

Dr G Cauwenbergh (Chairman)

Mr P Lankau

Dr R Murdoch

Dr G Collier

Details of these directors' attendance at committee meetings are set out in the Directors' Report on page 20.

A charter for the nomination committee can be found at www.phosphagenics.com/investors/corporate-governance

2.2 Board skills

The Board seeks to achieve a mix of skills and diversity that it enables it to most effectively carry out its functions and responsibilities. The following Board skills matrix describes the combined skills of the Board across a range of areas.

Board Skills Matrix	Board Representation
Extensive Board / Director Experience Has extensive director experience in a range of listed companies.	3
Global Executive Management Has been successful in senior executive roles in global companies or equivalent experience in a range of business environments.	4
Strategy Has ability to identify and critically assess strategic opportunities and develop successful strategies.	5
Governance Has commitment to high standards of corporate governance.	5
Financial / Risk Management Has audit / risk management experience at Board or senior executive level in financial accounting and reporting, corporate finance and assessment of financial viability and planning.	4
Pharmaceutical Industry Experience Has senior executive experience in large pharmaceutical or biotech organisation.	5
R&D / Product Development Has experience in research and development or product development within pharmaceutical or biotech organisation.	5
Business Development Has extensive knowledge of licencing and deal structures in US and rest of world.	5
Production Has experience in manufacturing or quality operations of production facilities and global supply	3
Regulatory Has knowledge of regulatory authority pathways in Australia, US and EMEA.	5
Leadership knowledge and abilities Has an understanding of effective leadership principles and systems at organisational level.	5
Ethics and Integrity Has an understanding of the role as director and sets high personal standards for behaviour and values.	5

2.3 Board members

Details of the members of the Board, their experience, qualifications, term of office and independence status are set out in the Directors' Report under the section titled "Information on Directors" on pages 13 to 14.

2.4 Directors' independence

An independent director must be independent of management, be free of any business or other relationship and otherwise meet the criteria for independence set out in the ASX Principles.

Under these criteria the Board has determined that three non-executive directors, which form a majority of the board, were independent and that one non-executive director was not independent, at the date of this report. The Board assesses the independence of directors as and when required.

2.5 Independent Chairman

The current Chairman, Mr Lankau, is an independent non-executive director appointed in April 2015. The CEO, Dr Murdoch, was appointed CEO in January 2015 and as Managing Director in April 2015.

In accordance with current practice, the Board Charter requires the role of Chairman and CEO to be separate.

2.6 Director induction and professional development

The Nomination Committee oversees, reviews and makes recommendations to the Board in relation to induction and development of non-executive directors, to ensure they develop and maintain the skills and knowledge needed to perform their roles as directors effectively.

The Company has a program for the induction of new directors which includes briefings with the CEO, Company Secretary, Senior Management and industry experts, site visits and provision of appropriate Company documentation.

The Board receives regular updates as well as attends a bi-annual workshop provided by the Company's legal advisors to assist with keeping current with relevant legal and industry developments.

Principle 3: Promote ethical and responsible decision making

3.1 Code of Conduct

The directors are committed to making positive economic, social and environmental contributions, while complying with all applicable laws and regulations and acting in a manner that is consistent with the principals of honesty, integrity, fairness and respect. The Company has established a Code of Conduct to establish clear standards against which to guide decision making and hold itself accountable. The Code provides a set of guiding principles covering employment practices, responsibility to shareholders and financial markets, equal opportunity, harassment and bullying, conflicts of interest, use of Company resources and disclosure of confidential information. The Code of Conduct is available on the Company's website at www.phosphagenics.com/investors/corporate-governance

Principle 4: Safeguard integrity in financial reporting

4.1 Audit and Risk Committee

The Board has established an Audit and Risk Committee comprising three independent non-executive directors. The chairman of the committee must be an independent director who is not chairman of the board. At the date of this report the Committee consisted of the following members:

Dr G Collier (Chairman)

Dr G Cauwenbergh

Mr P Lankau

Details of these directors' qualifications and attendance at committee meetings are set out in the Directors' Report on pages 13 to 14 and page 20. The Committee meets at least two times per year and has direct access to the Company's auditors.

The charter of the Committee can be found on the Company's website at www.phosphagenics.com/investors/corporate-governance.

4.2 CEO and CFO Declarations for financial statements

Prior to approval of the Company's financial statements for the half or full year by the Board, the CEO and CFO provide a declaration that, in their opinion, the financial records of the entity have been properly maintained and that the financial statements comply with the appropriate accounting standards and give a true and fair view of the financial position and performance of the entity and that the opinion has been formed on the basis of a sound system of risk management and internal control which is operating effectively.

4.3 External auditors

The external auditor, PricewaterhouseCoopers, attends each AGM and is available to answer questions from shareholders relevant to the audit.

Principle 5: Make timely and balanced disclosure

5.1 Continuous disclosure

The Company has a continuous disclosure policy to ensure compliance with ASX Listing Rules and has a vetting and authorisation process designed to ensure announcements are factual, complete and balanced.

A copy of this policy is available on the Company's website at www.phosphagenics.com/investors/corporate-governance.

Principle 6: Respect the rights of shareholders

6.1 Information on website

The Company provides information about itself and its corporate governance to its shareholders and members of the public on its website at www.phosphagenics.com

6.2 Communication with shareholders

The Board has approved a Shareholder Communication Policy to ensure that shareholders and the wider community are informed of all major developments affecting the Company in a timely and effective manner. Including its disclosure obligations under the ASX Listing Rules, the Company communicates with its shareholders in a number of ways, comprising:

- annual and half-yearly reports;
- quarterly newsletters and shareholder calls to provide updates on operation and developments;
- announcements on the Company's website;
- market briefings; and
- presentations at general meetings.

In addition to ensuring all Company information is available on the Company's website soon after receiving confirmation by the ASX of the receipt of the announcement, the Company will send to each shareholder or member of the public, who has requested, either by post or email, a copy of the release.

6.3 Participation at shareholder meetings

The Company holds its AGM in May each year in Melbourne. The Notice of Meeting and related Explanatory Notes are distributed to shareholders in accordance with the requirements of the Corporations Act, and simultaneously posted to the ASX.

The AGM provides the Company the opportunity to communicate with shareholders through the CEO presentation and the Chairman's address.

Shareholders are given the opportunity at the AGM to ask general questions about the management of the Company, as well as ask questions about particular agenda items. Shareholders who are unable to attend the meeting in person may submit written questions together with their proxy form.

6.4 Electronic communication

Shareholders are encouraged to receive shareholder material electronically, which can be established by registering on the Company website or to certain information via the Company's share registry, Computershare.

Shareholders are also able to contact the Company via the general contact email address info@phosphagenics.com, and where appropriate a response will be provided.

Principle 7: Recognise and manage risk

7.1 Audit and risk committee

The Board has established an Audit and Risk Committee consisting of three independent non-executive directors. Details regarding composition, meetings and charter are set out in section 4.1 of this Corporate Governance Statement.

7.2 Risk management framework

The Board considers risk management fundamental to maintaining efficient and effective operations and generating and protecting shareholder value. The management and oversight of risk is an ongoing process integral to the management and corporate governance of the Company's business.

The Board, through its Audit and Risk Committee, is responsible for ensuring there are adequate policies in relation to risk management, compliance and internal controls. The Company has established a risk management system which aligns with the vision, strategy, processes, technology and governance and provides for:

- appropriate levels of risk taking and acceptance;
- an effective system for management of risk across the Company;
- informed and effective strategy setting, decision making, planning and performance oversight; and
- reliable and efficient execution of operations, programs and projects.

The Company has a Risk Management Policy, a summary of which is available on the Company's website, which sets out the objectives and key principals of risk management, along with responsibilities and authorities of the Board, the Audit and Risk Committee, the CEO, CFO, Executive Management and management. The Company has adopted a risk management

strategy that aims to identify and minimise the potential for loss, while also maximising strategic opportunities for growth and development. The Board sets risk appetite and tolerance levels for the Company and reviews this, and the risk management framework each reporting period in order to satisfy itself that it continues to be sound.

During the reporting period Executive Management has reported to the Audit and Risk Committee as to the effectiveness of the group's management of its material business risks and the effectiveness of the risk management framework.

7.3 Internal audit function

With regard to the Company's size, the Board does not deem it necessary to have an internal audit function. As outlined in section 7.2 the Company has a comprehensive system of risk management and undertakes regular reviews of its effectiveness and where necessary utilises the resources of an external risk consultant.

7.4 Sustainability risks and management

The Company does not have any material exposure to environmental or social sustainability risks. The Company's key economic risks are outlined on pages 19 and 20 of the directors' report under the heading 'Material Business Risks'. In addition to risk management strategies outlined in section 7.1 and 7.2, the Company utilises risk mitigation strategies including employing qualified and specialised consultants, external advisors and holding a comprehensive insurance program.

Principle 8: Remunerate fairly and responsibly

8.1 Remuneration committee

The Board has established a Remuneration Committee consisting of three independent non-executive directors. The chairman of the committee must be an independent director. At the date of this report the Committee consisted of the following members:

Dr G Collier (Chairman)

Mr P Lankau

Dr G Cauwenbergh

Details of these directors' qualifications and attendance at committee meetings are set out in the Directors' Report on pages 13 to 14 and page 20. The Committee meets at least two times per year.

The charter of the Committee can be found on the Company's website at www.phosphagenics.com/investors/corporate-governance

8.2 Executive and non-executive remuneration policies

Non-executive directors are remunerated at market rates for comparable companies for time, commitment, and responsibilities. The Board as a whole determines payments to the non-executive directors and reviews their remuneration annually, based on market practice, duties, and accountability. The maximum aggregate amount of fees that can be paid to non-executive directors is subject to approval by shareholders at the Annual General Meeting.

Each executive has a formal service agreement, which includes a position description and sets out duties, rights and responsibilities as well as entitlement on termination. The Company has policies which apply to base salaries, short-term incentives and long-term incentives. Further information on remuneration is set out in the Remuneration Report on pages 21 to 27.

8.3 Hedging of equity incentive schemes

Phosphagenics prohibits Key Management Personnel from entering into transactions in associated products which operate to limit the economic risk of security holdings in Phosphagenics over unvested entitlements or entitlements which have vested but remain subject to a holding lock. A copy of the Securities Trading Policy can be found on the Company's website at www.phosphagenics.com/investors/corporate-governance.

The Corporate Governance Statement was approved by the Board of directors on 28 February 2017.

Contents

These financial statements are consolidated financial statements for the group consisting of Phosphagenics Limited and its subsidiaries. A list of subsidiaries is included in note 20.

The financial statements are presented in the Australian currency.

Phosphagenics Limited is a Company limited by shares, incorporated and domiciled in Australia. Its registered office and principal place of business is:

Phosphagenics Limited
Unit A8, 2A Westall Road
Clayton Victoria 3168

The financial statements were authorised for issue by the directors on 28 February 2017. The directors have the power to amend and reissue the financial statements.

All press releases, financial reports and other information are available on our website: www.phosphagenics.com.

Consolidated Income Statement

	Notes	2016 $'000	2015 $'000
Revenue from continuing operations			
Total revenue	2	1,588	2,190
Cost of sales		(330)	(667)
Gross profit		1,258	1,523
Income from government grants	2	1,833	2,279
Finance revenue		171	512
Other income		80	7
Recoveries	2	-	160
Employee and directors benefits expenses	3a	(3,428)	(5,852)
Research expenses		(1,752)	(1,956)
Consulting and professional expenses		(1,199)	(1,178)
Legal expenses	3b	(2,678)	(2,051)
Amortisation and depreciation		(2,472)	(3,268)
Impairment losses	10	(7,207)	(7,837)
Other expenses	3c	(1,851)	(1,916)
Loss before income tax		(17,245)	(19,577)
Income tax benefit	4	-	-
Loss from continuing operations		(17,245)	(19,577)
Loss from discontinued operations	18	(69)	(543)
Loss for the period		(17,314)	(20,120)
Earnings per share for loss from continuing operations attributable to the ordinary equity holders of the Company:			
Basic profit / (loss) per share	15	(1.37) cents	(1.55) cents
Diluted profit / (loss) per share	15	(1.37) cents	(1.55) cents
Earnings per share for loss attributable to the ordinary equity holders of the Company:			
Basic profit / (loss) per share	15	(1.37) cents	(1.59) cents
Diluted profit / (loss) per share	15	(1.37) cents	(1.59) cents

The above consolidated income statement should be read in conjunction with the accompanying notes.

Consolidated Statement of Comprehensive Income

	Notes	2016 $'000	2015 $'000
Loss for the period		(17,314)	(20,120)
Other Comprehensive Income			
Items that may be classified to profit or loss			
Exchange differences on translation of foreign operations	14	(3)	16
Income tax/(expense) on items of other comprehensive income		-	-
Other comprehensive income for the period, net of tax	14	(3)	16
Total comprehensive income for the period		(17,317)	(20,104)
Total comprehensive income for the period attributable to:			
Owners of Phosphagenics Ltd arises from:			
Continuing operations		(17,248)	(19,561)
Discontinued operations		(69)	(543)
		(17,317)	(20,104)

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

Consolidated Balance Sheet

	Notes	31 December 2016 $'000	31 December 2015 $'000
ASSETS			
Current Assets			
Cash and cash equivalents	22a	6,092	12,395
Trade and other receivables	7	3,607	4,724
Inventories	8	237	278
Other current assets		247	542
Assets classified as held for sale	18	-	17
Total Current Assets		10,183	17,956
Non-Current Assets			
Plant and equipment	9	385	519
Intangible assets	10	2,786	12,269
Total Non-Current Assets		3,171	12,788
Total Assets		13,354	30,744
LIABILITIES			
Current Liabilities			
Trade and other payables	11	1,318	1,212
Provisions	12	345	569
Total Current Liabilities		1,663	1,781
Non-Current Liabilities			
Provisions	12	44	35
Total Non-Current Liabilities		44	35
Total Liabilities		1,707	1,816
Net Assets		11,647	28,928
EQUITY			
Issued Capital	13	228,100	228,100
Reserves	14	30,224	30,191
Accumulated Losses		(246,677)	(229,363)
Total Equity		11,647	28,928

The above consolidated balance sheet should be read in conjunction with the accompanying notes.

Consolidated Statement of Changes in Equity

	Contributed capital	Reserves	Accumulated losses	Total equity
	$'000	$'000	$'000	$'000
Balance at 31 December 2014	228,100	30,171	(209,243)	49,028
Loss for the year	-	-	(20,120)	(20,120)
Other comprehensive income	-	16	-	16
Total comprehensive income (loss) for the period	-	16	(20,120)	(20,104)
Transactions with owners in their capacity as owners:				
Employee equity settlement benefits	-	4	-	4
Total transactions with owners	-	4	-	4
Balance at 31 December 2015	228,100	30,191	(229,363)	28,928
Loss for the year	-	-	(17,314)	(17,314)
Other comprehensive income	-	(3)	-	(3)
Total comprehensive income (loss) for the period	-	(3)	(17,314)	(17,317)
Transactions with owners in their capacity as owners:				
Employee equity settlement benefits	-	36	-	36
Total transactions with owners	-	36	-	36
Balance at 31 December 2016	228,100	30,224	(246,677)	11,647

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

Consolidated Statement of Cash Flows

	Notes	2016 $'000	2015 $'000
OPERATING ACTIVITIES			
Receipts from customers (inclusive of goods and services tax)		2,140	1,989
Receipt of recoveries		-	160
Receipt of government grants		2,442	2,665
Payments to suppliers and employees (inclusive of goods and services tax)		(10,994)	(13,519)
Net cash used in operating activities	22(b)	(6,412)	(8,705)
INVESTING ACTIVITIES			
Interest received		171	510
Purchase of plant and equipment		(62)	(89)
Net cash from investing activities		109	421
FINANCING ACTIVITIES			
Proceeds from issues of shares	13	-	-
Costs of issue of shares	13	-	-
Net cash from financing activities		-	-
Net (decrease)/ increase in cash and cash equivalents		(6,303)	(8,284)
Cash and cash equivalents at the beginning of period		12,395	20,679
Cash and cash equivalents at the end of period	22(a)	6,092	12,395

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

Notes to the Consolidated Financial Statements

Contents

1. Summary of Significant Accounting Policies

This note provides a list of all significant accounting policies adopted in the preparation of these consolidated financial statements. These policies have been consistently applied to all the years presented, unless otherwise stated. The financial statements are the group consisting of Phosphagenics Ltd and its subsidiaries (the group).

a) Basis of preparation

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and Interpretations issued by the Australian Accounting Standards Board and the Corporations Act 2001. Phosphagenics Ltd is a for-profit entity for the purposes of preparing the financial statements.

i) Compliance with IFRS

The consolidated financial statement of the Phosphagenics Ltd group also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

ii) Historical cost convention

These financial statements have been prepared on a historical cost basis except for certain classes of property, plant and equipment and intangible assets, which have been measured at fair value.

iii) Going concern

For the year ended 31 December 2016, the consolidated entity has incurred losses of $17,314,000 (2015: $20,120,000) and experienced net cash outflows of $6,412,000 from operations (2015: $8,705,000). As at year end the cash position was $6,092,000 (2015: $12,395,000).

During the 2017 financial year, the Company expects decreased operational and R&D expenses, reflecting the restructure effected in September 2015. However whilst the Company is still in development phase there is not sufficient certainty in anticipated licencing revenue to be relied upon in cash flow planning. In addition the directors intend to continue to fund significant legal costs relating to the arbitration against Mylan. As a result of these outflows, the directors propose to raise funds by new equity funding or via other sources to ensure the Company continues to hold adequate levels of available cash resources to meet creditors and other commitments.

The continued viability of the Company and its ability to continue as a going-concern and meet its debts and commitments as they fall due is dependent on the satisfactory completion of raising equity or securing funding from other sources.

Due to uncertainty surrounding the timing, quantum and ability to raise additional funds via the issuance of new equity or reach contractual agreement for other funding, there is material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern and therefore, that it may be unable to realise its assets and discharge its liabilities in the normal course of business. However, the directors have confidence that the Company will be successful in obtaining appropriate funding and accordingly have prepared the financial report on a going concern basis. As such no adjustments have been made to the financial statements relating to the recoverability and classification of the asset carrying amounts or classification of liabilities that might be necessary should the Company not be able to continue as a going concern.

iv) New and amended standards adopted by the group

The group has applied the following standards and amendments for the first time for the annual reporting period commencing 1 January 2016:

- AASB 2014-3 Amendments to Australian Accounting Standards – Accounting for Acquisitions of Interests in Joint Operations
- AASB 2014-4 Amendments to Australian Accounting Standards – Clarification of Acceptable Methods of Depreciation and Amortisation
- AASB 2015-1 Amendments to Australian Accounting Standards – Annual improvements to Australian Accounting Standards 2012 – 2014 cycle, and
- AASB 2015-2 Amendments to Australian Accounting Standards – Disclosure initiative: Amendments to AASB 101.

None of the new and amended standards that are mandatory for the first time for the financial year beginning 1 January 2016 affected any of the amounts recognised in the current period or any prior period and are not likely to affect future periods.

v) New standards and interpretations not yet adopted

The group has elected not to apply any pronouncements before their operative date in the annual reporting period beginning 1 January 2016. The group's assessment of the impact of these new standards and interpretations is set out below.

- AASB 16 Leases was issued in February 2016.
  - Nature of change: Almost all leases will be recognized on the balance sheet, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases.
  - Impact: The standard will affect primarily the accounting for the group's operating leases. As at the reporting date, the group has non-

cancellable operating lease commitments of $262,000, see note 16. However, the group has not yet determined to what extent these commitments will result in the recognition of an asset and a liability for future payments and how this will affect the group's profit and classification of cash flows.

– Date of adoption by group: Mandatory for financial years commencing on or after 1 January 2019. At this stage, the group does not intend to adopt the standard before its effective date.

vi) Critical accounting estimates and judgements

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas of assumptions and estimates are:

(1) R&D Tax Incentives

From 1 July 2011 the Australian Government has provided a tax incentive, in the form of a refundable tax offset of 45%, for eligible research and development expenditure. Management has assessed its research and development activities and expenditure to determine which are likely to be eligible under the scheme. For the period ended 31 December 2016 the Company has recorded an item in other income of $1,833,000 (2015: $2,279,000) to recognise this amount which relates to this period.

(2) 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 and Black Scholes methods 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 within the next annual reporting period but may impact expenses and equity.

(3) Estimated impairment of intangibles

The group tests whether intangible assets have suffered any impairment at each reporting date. The recoverable amount of intangible assets is assessed at its value in use. This calculation requires the use of assumptions. (Refer to Note 10 for details of these assumptions).

b) Principles of consolidation

i) Subsidiaries

Subsidiaries are all entities (including structured entities) over which the group has control. The group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transactions provides evidence of an impairment of the transferred asset. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the group.

ii) Associates

Associates are all entities over which the group has significant influence but not control or joint control. This is generally the case where the group holds between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting (see (iv) below), after initially being recognized at cost.

iii) Joint arrangements

Under AASB 11 Joint Arrangement investments in joint arrangements are classified as either joint operations or joint ventures. The classification depends on the contractual rights and obligations of each investor, rather than the legal structure of the joint arrangements. Phosphagenics Ltd has a joint venture.

Joint venture

Interests in joint venture are accounted for using the equity method (see (iv) below), after initially being measured at cost in the consolidated balance sheet.

iv) Equity method

Under the equity method of accounting, the investments are initially recognised at cost and adjusted thereafter to recognise the group's share of the post-acquisition profits or losses of the investee in profit or loss, and the group's share of movements in other comprehensive income of the investee in other comprehensive income. Dividends received or receivable from associates and joint ventures are recognised as a reduction in the carrying amount of the investment.

When the group's share of losses in an equity-accounted investment equals or exceeds its interest in the entity, including any other unsecured long-term receivables, the group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the other entity.

Unrealised gains on transactions between the group and its associates and joint ventures are eliminated to the extent of the group's interest in these entities. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of equity accounted investees have been changed where necessary to ensure consistency with the policies adopted by the group.

The group treats transactions with non-controlling interests that do not result in a loss of control as transactions with equity owners of the group. A change in ownership interest results in an adjustment between the carrying amounts of the controlling and non-controlling interests to reflect their relative interests in the subsidiary. Any difference between the amount of the adjustment to non-controlling interests and any consideration paid or received is recognised in a separate reserve within equity attributable to owners of Phosphagenics Limited.

v) Changes in ownership interests

When the group ceases to have control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value with the change in carrying amount recognised in profit or loss.

This fair value becomes the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

If the ownership interest in a joint venture or an associate is reduced but joint control or significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to profit or loss where appropriate.

c) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker.

The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer.

d) Foreign currency translation

i) Functional and presentation currency

Items included in the financial statements of each of the group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Australian dollars, which is Phosphagenics Limited's functional and presentation currency.

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year end exchange rates are generally recognised in profit or loss. They are deferred in equity if they relate to qualifying cash flow hedges and qualifying net investment hedges or are attributable to part of the net investment in a foreign operation.

Foreign exchange gains and losses that relate to borrowings are presented in the income statement, within finance costs. All other foreign exchange gains and losses are presented in the income statement on a net basis within other income or other expenses.

Non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Translation differences on assets and liabilities carried at fair value are reported as part of the fair value gain or loss. For example, translation differences on non-monetary assets and liabilities such as equities held at fair value through profit or loss are recognised in profit or loss as part of the fair value gain or loss and translation differences on non-monetary assets such as equities classified as available-for-sale financial assets are recognised in other comprehensive income.

iii) Group companies

The results and financial position of foreign operations (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet
- income and expenses for each income statement and statement of comprehensive income are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions), and
- all resulting exchange differences are recognised in other comprehensive income.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities, and of borrowings and other financial instruments designated as hedges of such investments, are recognised in other comprehensive income. When a foreign operation is sold or any borrowings forming part of the net investment are repaid, the associated exchange differences are reclassified to profit or loss, as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at the closing rate.

e) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are net of returns, trade allowances, rebates and amounts collected on behalf of third parties.

The group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the group's activities as described below. The group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Interest income is recognised using the effective interest method. When a receivable is impaired, the group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

f) Government grants

Grants from the government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the group will comply with all attached conditions. Government grants relating to costs are deferred and recognized in profit or loss over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred income and are credited to the income statement on a straight-line basis over the expected lives of the related assets.

g) Income tax

The income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill. Deferred income tax is also not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax liabilities and assets are not recognised for temporary differences between the carrying amount and tax bases of investments in foreign operations where the Company is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority.

Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Phosphagenics Limited and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation. As a consequence, these entities are taxed as a single entity and the deferred tax assets and liabilities of these entities are set off in the consolidated financial statements.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

h) Investment allowances and similar tax incentives

Companies within the group may be entitled to claim special tax deductions for investments in qualifying assets or in relation to qualifying expenditure (eg the Research and Development Tax Incentive regime in Australia or other investment allowances). The group accounts for such allowances as tax credits, which means that the allowance reduces income tax payable and current tax expense. A deferred tax asset is recognised for unclaimed tax credits that are carried forward as deferred tax assets.

i) Leases

Leases in which a significant portion of the risks and rewards of ownership are not transferred to the group as lessee are classified as operating leases (note 20). Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease.

j) Impairment of assets

Goodwill and 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. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal 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 which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

k) Cash and cash equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the balance sheet.

l) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. See note 7 for further information about the group's accounting for trade receivables and the group's impairment policies.

m) Inventories

Raw materials and stores, work in progress and finished goods are stated at the lower of cost and net realisable value. Cost comprises direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity. Cost includes the reclassification from equity of any gains or losses on qualifying cash flow hedges relating to purchases of raw material but excludes borrowing costs. Costs are assigned to individual items of inventory on the basis of weighted average costs. Costs of purchased inventory are determined after deducting rebates and discounts. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

n) Non-current assets (or disposal groups) held for sale and discontinued operations

Non-current assets (or disposal groups) are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell, except for assets such as deferred tax assets, assets arising from employee benefits, financial assets and investment property that are carried at fair value and contractual rights under insurance contracts, which are specifically exempt from this requirement.

An impairment loss is recognised for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell. A gain is recognised for any subsequent increases in fair value less costs to sell of an asset (or disposal group), but not in excess of any cumulative impairment loss previously recognised. A gain or loss not previously recognised by the date of the sale of the noncurrent asset (or disposal group) is recognised at the date of derecognition.

Non-current assets (including those that are part of a disposal group) are not depreciated or amortised while they are classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale continue to be recognised.

Non-current assets classified as held for sale and the assets of a disposal group classified as held for sale are presented separately from the other assets in the balance sheet. The liabilities of a disposal group classified as held for sale are presented separately from other liabilities in the balance sheet.

A discontinued operation is a component of the entity that has been disposed of or is classified as held for sale and that represents a separate major line of business or geographical area of operations, is part of a single co-ordinated plan to dispose of such a line of business or area of operations, or is a subsidiary acquired exclusively with a view to resale. The results of discontinued operations are presented separately in the income statement.

o) Investments and other financial assets

i) Classification

The group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets. The classification

depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and, in the case of assets classified as held-to-maturity, re-evaluates this designation at the end of each reporting period.

ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except those with maturities greater than 12 months after the reporting date which are classified as non-current assets. Loans and receivables are included in trade and other receivables (note 7) in the balance sheet.

p) Plant and equipment

All property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

The depreciation is calculated using the straight-line method to allocate their cost or revalued amounts, net of the residual values, over their estimated useful lives. The expected net useful lives are 3 to 10 years. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (note 1(i))

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in profit or loss.

q) Intangible assets

i) Intellectual Property

Intellectual property acquired separately or in a business combination are initially measured at cost, which is its fair value as at the date of acquisition. Following initial recognition, intellectual property is carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful life of the intellectual property is referenced to its expiry date. The intellectual property purchased, primarily registered patents, had remaining lives of 15 to 19 years at purchase date. Intellectual property is amortised over its useful life and tested for impairment whenever there is an indication that the intellectual property may be impaired.

Internally generated intellectual property is not capitalised and expenditure is recognised as an expense as incurred.

ii) Trademarks and licences

Trademarks and licences have a finite useful life and are carried at cost less accumulated amortisation and impairment losses.

iii) 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 capitalised is amortised over the period of expected future benefit from the related project on a straight line basis.

r) Trade and other payables

These amounts represent liabilities for goods and services provided to the group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition. Trade and other payables are presented as current liabilities unless payment is not due within 12 months after the reporting period.

s) Provisions

Provisions for legal claims, service warranties and make good obligations are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The discount rate used to determine the present value is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognised as interest expense.

t) Employee benefits

i) Short-term obligations

Liabilities for wages and salaries, including non-monetary benefits and accumulating sick leave that are expected to be settled wholly within 12 months after the end of the period in which the employees render the related service are recognised in respect of employees' services up to the end of the reporting period and are measured at the amounts expected to be paid when the liabilities are settled. The liability for accumulating sick leave is recognised in the provision for employee benefits. All other short-term employee benefit obligations are presented as payables.

ii) Other long-term employee benefit obligations

The liabilities for long service leave and annual leave are not expected to be settled wholly within 12 months after the end of the period in which the employees render the related service. They are therefore recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the end of the reporting period 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 end of the reporting period of government bonds with terms and currencies that match, as closely as possible, the estimated future cash outflows. Remeasurements as a result of experience adjustments and changes in actuarial assumptions are recognised in profit or loss.

The obligations are presented as current liabilities in the balance sheet if the entity does not have an unconditional right to defer settlement for at least twelve months after the reporting period, regardless of when the actual settlement is expected to occur.

iii) Share-based payments

Share-based compensation benefits are provided to employees via the Phosphagenics Employee Option Plan and an employee share scheme. Information relating to these schemes is set out in note 5.

The fair value of options granted under the Phosphagenics Employee Option Plan is recognised as an employee benefits expense with a corresponding increase in equity. The total amount to be expensed is determined by reference to the fair value of the options granted, which includes any market performance conditions and the impact of any non-vesting conditions but excludes the impact of any service and non-market performance vesting conditions.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each period, the entity revises its estimates of the number of options that are expected to vest based on the non-marketing vesting conditions. It recognises the impact of the revision to original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

The fair value of deferred shares granted to employees for nil consideration under the short-term incentive scheme is recognised as an expense over the relevant service period, being the year to which the bonus relates and the vesting period of the shares. The fair value is measured at the grant date of the shares and is recognised in equity in the share-based payment reserve. The number of shares expected to vest is estimated based on the non-market vesting conditions. The estimates are revised at the end of each reporting period and adjustments are recognised in profit or loss and the share-based payment reserve.

iv) Bonus plans

The group recognises a liability and an expense for bonuses and profit-sharing based on a formula that takes into consideration the profit attributable to the Company's shareholders after certain adjustments. The group recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

v) Termination benefits

Termination benefits are payable when employment is terminated by the group before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The group recognises termination benefits at the earlier of the following dates: (a) when the group can no longer withdraw the offer of those benefits; and (b) when the entity recognises costs for a restructuring that is within the scope of AASB 137 and involves the payment of terminations benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

u) Contributed equity

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.

Where any group Company purchases the Company's equity instruments, for example as the result of a share buy-back or a share-based payment plan, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the owners of Phosphagenics

Limited as treasury shares until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the owners of Phosphagenics Limited.

v) Dividends

Provision is made for the amount of any dividend declared, being appropriately authorised and no longer at the discretion of the entity, on or before the end of the reporting period but not distributed at the end of the reporting period.

w) Earnings per share

i) Basic loss per share

Basic loss per share is calculated by dividing:

- the loss attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares
- by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

ii) Diluted loss per share

Diluted loss per share adjusts the figures used in the determination of basic loss per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential
- ordinary shares, and
- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

x) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the taxation authority. In this case it is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables or payables in the balance sheet.

	2016 $'000	2015 $'000

2. Revenue and Other Income

Revenue from continuing operations		
Sale of goods	952	1,880
Royalties and license fees	636	310
Total	**1,588**	**2,190**
Revenue from discontinued operations (note 18)		
Sale of goods	48	30

Income from Government Grants		
R&D tax incentive credit	1,833	2,279
Total	1,833	2,279

Recoveries		
Recoveries received	-	160
Total	-	160

The Company recognises payments received under Deeds of Settlement or from the Bankruptcy Trustee, related to the misappropriations announced in 2014, when they are virtually certain.

3. Expenses

a) Employee and directors benefit expenses

Directors fees	(285)	(261)
Research and development employee expenses[1]	(1,077)	(2,350)
Redundancy costs	(31)	(705)
Recruitment and relocation expenses	-	(196)
ESOP expenses	(36)	(4)
Other employee expenses	(1,999)	(2,336)
Total	**(3,428)**	**(5,852)**

[1] In 2015 Research and development employee expenses of $444,000 were reported within Other employee expenses.

b) Legal expenses

Legal expenses associated with arbitrations	(2,192)	(1,938)
Other legal expenses	(486)	(113)
Total	**(2,678)**	**(2,051)**

c) Other Expenses

Net foreign exchange (loss) / gain	(61)	122
Travel	(466)	(457)
Doubtful debts	(63)	-
Insurance	(157)	(196)
Shareholder and listing expenses	(149)	(151)
Patent portfolio expenses	(448)	(637)
Occupancy expenses	(444)	(553)
Other	(63)	(44)
Total	**(1,851)**	**(1,916)**

4. Income Taxes

	2016 $'000	2015 $'000
Major components of income tax expense are:		
Current income tax	-	-
Deferred income tax	-	-
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	(17,314)	(20,120)
Tax expense calculated at the Australian tax rate of 30% (2015: 30%)	(5,194)	(6,036)
Non-assessable income	(550)	(732)
Non-deductible expenses	3,939	4,340
Unused tax losses and tax offsets not recognised as deferred tax assets	1,805	2,428
Income tax benefit reported in income statement	-	-
Deferred tax liabilities comprise:		
Intellectual property	-	-
Unrecognised deferred tax balances		
The following items have not been brought to account as deferred tax assets:		
Tax losses not recognised (at current tax rate of 30%)	41,351	39,017
Temporary differences not recognised	-	-
Total	**41,351**	**39,017**

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.

(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 Equity Incentive Plan (EIP) and Employee Conditional Rights Scheme (ECRS).

- The EIP 2016 Option Plan was approved by the Board in September 2016 and is designed 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 EIP has been offered to all staff who met the minimum service criteria, with vesting requiring continuation of service as well as achievement of a predefined share price. The vesting share price condition requires that for a period of 3-months before and after the annual vesting date that the 5-day weighted share price increase from the share price on the offer date ($0.021)

by 50% ($0.32) relating to September 2017,100% ($0.042) relating to September 2018 and 150% ($0.053) relating to September 2019. The EIP allows staff to exercise vested options at $0.023

- 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.

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

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	2016 Options No.	2016 WAEP $	2015 Options No.	2015 WAEP $
Outstanding at beginning of the year	3,000,000	$0.17	3,000,000	$0.17
Granted during the year	33,948,150	$0.042	-	-
Forfeited during the year	-	-	-	-
Exercised during the year	-	-	-	-
Expired during the year	-	-	-	-
Outstanding at end of the year	36,948,150	$0.052	3,000,000	$0.17
Exercisable at end of the year	3,000,000	$0.17	3,000,000	$0.17

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

During the year ended 31 December 2016 $nil (2015: nil) was reversed as a result of forfeited unvested options. An amount of $35,454 (2015: nil) was recognised as an expense in the period. The net expense recognised in the period relating to options was $35,454 (2015: nil).

The outstanding balance as at 31 December 2016 is represented by:

Issuing entity	Shares under option (No)	Class of shares	Exercise price ($)	Expiry date
Phosphagenics Ltd	3,000,000	Ordinary	$0.17	22 May 2019
Phosphagenics Ltd	11,316,050	Ordinary	$0.023	11 September 2017
Phosphagenics Ltd	11,316,050	Ordinary	$0.023	10 September 2018
Phosphagenics Ltd	11,316,050	Ordinary	$0.023	9 September 2019
Total	**36,948,150**			

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	2016 Performance Rights No.	2016 WAEP $	2015 Performance Rights No.	2015 WAEP $
Outstanding at beginning of the year	30,960,000	-	13,200,000	-
Granted during the year	-	-	40,010,000	-
Forfeited during the year	(15,960,000)	-	(15,650,000)	-
Exercised during the year	-	-	-	-
Expired during the year	-	-	(6,600,000)	-
Outstanding at end of the year	**15,000,000**	**0.00**	**30,960,000**	**0.00**
Exercisable at end of the year	-	-	-	-

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. There were no cancellations or modifications to the awards in 2016 or 2015.

The outstanding balance as at 31 December 2016 is represented by:

Issuing entity	Performance Rights (No)	Class of shares	Exercise price ($)	Expiry date
Phosphagenics Ltd	15,000,000	Ordinary	$0.00	31 December 2018
Total	**15,000,000**			

During the year ended 31 December 2016 $3,100 (2015: $1,125) was reversed as a result of forfeited unvested performance rights. An amount of $3,704 (2015: $4,641) was recognized as an expense in the period. The net expense recognised in the period relating to performance rights was $604 (2015: $3,516).

Option pricing model

Fair value for performance rights was calculated using a Binomial model. Fair value for the EIP 2016 Option was calculated using a variation of the Black-Scholes mode which took account of the share-price hurdle vesting condition. 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).

Model Inputs	2016 Options	2015 Rights
Dividend yield %	0.0%	0.0%
Expected volatility %	60%	60%
Risk-free interest rate %	1.83%	1.80 -2.07%
Option life (years)	4.93 years	2.6 – 2.7 years
Option Exercise price $	$0.023	$0.00
Weighted Average Share price at measurement date	$0.026	$0.03

The expected life of the rights 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.

6. Remuneration Of Auditors

The auditor of Phosphagenics Ltd (the parent), and the Group for the period ended 31 December 2016 is PricewaterhouseCoopers.

Amounts received or due and receivable by auditor	2016 $	2015 $
PricewaterhouseCoopers		
Audit or review of the financial report	111,724	111,338
Other non-audit services	5,000	-
Total PricewaterhouseCoopers	**116,724**	**111,338**

7. Current Trade And Other Receivables

	2016 $'000	2015 $'000
Trade receivables	337	803
Allowance for impairment losses	(63)	-
	274	803
R&D tax incentive credit receivable	3,014	3,623
Other receivables	319	298
Total	**3,607**	**4,724**

Trade receivables are non-interest bearing and are generally 45 day terms or as specified in contracts or agreements. An amount of $2,294,000 is expected to be received from the R&D tax incentive scheme before end March 2017. A further amount of $720,000 will form part of the R&D tax incentive claimed for the tax year ended 30 June 2017 and is expected to be received before December 2017.

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

	Total	Neither past due or impaired	Past due but not impaired			
			1-30 days	31-60 days	61-90 days	90+ days
	$'000	$'000	$'000	$'000	$'000	$'000
31 December 2016	274	2	76	108	-	88
31 December 2015	803	661	-	92	43	7

Allowance for impairment loss

A provision for impairment is recognised when there is objective evidence 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 uncollectable. Debts totalling $63,135 (2015: $nil) were deemed impaired at 31 December 2016. No debts were written-off during the year (2015: $nil).

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

	2016 $'000	2015 $'000
Raw materials (at cost)	464	522
Finished goods (at cost)	264	245
Less provision for obsolesce	(491)	(489)
Total inventories at the lower of cost and net realisable value	237	278

During 2016 $nil (2015: $16,044) 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 other expenses.

9. Plant And Equipment

Year ended 31 December 2016	**Total $'000**
At 1 January 2016, net of accumulated depreciation and impairment	519
Additions	62
Depreciation charge for the year	(196)
At 31 December 2016, net of accumulated depreciation and impairment	385
At 31 December 2016	
Cost	2,838
Accumulated depreciation and impairment	(2,453)
Net carrying value	385

Year ended 31 December 2015	**Total $'000**
At 1 January 2015, net of accumulated depreciation and impairment	814
Additions	89
Write off of assets for obsolescence	(41)
Depreciation charge for the year	(343)
At 31 December 2015, net of accumulated depreciation and impairment	519
At 31 December 2015	
Cost	2,863
Accumulated depreciation and impairment	(2,344)
Net carrying value	519

10. Intangible Assets

Year ended 31 December 2016	Total Intellectual Property $'000
At 1 January 2016 net of accumulated amortisation and impairment	12,269
Impairment losses	(7,207)
Amortisation	(2,276)
At 31 December 2016, net of accumulated amortisation and impairment	2,786
At 31 December 2016	
Cost (gross carrying amount)	121,362
Accumulated amortisation and impairment	(118,576)
Net carrying amount	2,786

Year ended 31 December 2015	Total Intellectual Property $'000
At 1 January 2015 net of accumulated amortisation and impairment	23,031
Impairment losses	(7,837)
Amortisation	(2,925)
At 31 December 2015, net of accumulated amortisation and impairment	12,269
At 31 December 2015	
Cost (gross carrying amount)	121,362
Accumulated amortisation and impairment	(109,093)
Net carrying amount	12,269

Impairment Testing

Intellectual Property

Intellectual property asset cost represents the fair value of nine patents acquired by the Company at 31 December 2004, less accumulated amortisation and adjusted for any accumulated impairment loss. Intellectual property is amortised over its useful life, being the patent life of between 15 -19 years at acquisition (to between 2020 and 2023), and tested for indicators of impairment at each reporting date. In 2010 one of the purchased patents was abandoned.

At 30 June 2015, due to the Company's net asset value totalling more than its market capitalisation, it was assessed that an impairment trigger had occurred and an independent valuer was engaged to calculate the fair value of the entire acquired patent portfolio. The independent valuer used a discounted cash flow model. For products still in development, probability weightings were applied to clinical trials and regulatory approval. Discount rates of between 13-18% were applied to risk adjusted forecasted cash flows over the remaining economic life of the patents. At 30 June an impairment of $7,837,000 was recognised.

As at 31 December 2015, due to the Company's net asset value totalling more than its market capitalisation, it was assessed that an impairment trigger had also occurred and the independent valuer was re-engaged to calculate the fair value of the acquired patents. Management provided updated assumptions where they had changed from the June 2015 valuation. The independent valuer used the same valuation basis, being a discounted cash flow model, probability weightings were applied to clinical trials and regulatory approval for products still in development and discount rates of between 13-20% were applied to risk adjusted forecasted cash flows over the remaining economic life of the patents. Forecasted cash flows primarily relate to anticipated royalty payments on successful commercialisation of a product or existing revenue streams if commercialised. A range of product launch dates for the initiation of royalty streams was modelled providing a range of valuations of which the Company judged to utillise the low-point of valuations provided by the valuer. As at 31 December 2015, the fair value of the acquired patents was assessed at $12,541,000 which was not materially different to the book value. Accordingly no further impairment was recognised at 31 December.

At 31 December 2016 it was assessed that an impairment event had occurred due to delays to the commercialisation of TPM®/Daptomycin product and to the resulting cash flows assumptions in the valuation model. The independent valuer was re-engaged to calculate the fair value of the acquired patents. Management provided updated assumptions where they had changed from the December 2015 valuation. The independent valuer used the same valuation basis, being a discounted cash flow model, probability weightings were applied to clinical trials and regulatory approval for products still in development and discount rates of between 13-20% were applied to risk adjusted forecasted cash flows over the remaining economic life of the patents. Forecasted cash flows primarily relate to anticipated royalty payments on successful commercialisation of a product or existing revenue streams if commercialised. A range of product launch dates for the initiation of royalty streams was modelled, including an assumption that due to the commercialisation partner for TPM®/Daptomycin not having advised a launch date that an inference can be drawn that this partner does not have the intention to launch the product. The valuer has provided a range of valuations of which the Company judged to utillise the low-point of valuations provided. As at 31 December 2016, the fair value of the acquired patents was assessed at $3,218,000. Where the valuer provided a higher patent value than the existing net carrying amount, the lower of the two values was taken. Accordingly the Company has recognised an impairment of $7,207,000.

The remaining fair value of the acquired patents is dependent on the continued sales of Vital ET® and the commercialisation of TPM®/Oxycodone prior to the expiry of the patents. Revenue assumptions related to this have been assessed for delays in revenue receipts, with delays of one year not materially impacting the value of the assets.

11. Current Trade and Other Payables

	2016 $'000	2015 $'000
Trade payables	571	409
Accrued expenses	526	691
Other payables	221	112
Total	**1,318**	**1,212**

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.

12. Provisions

	2016 $'000	2015 $'000
Current		
Annual leave benefits	197	276
Redundancy	-	149
Long service leave benefits	148	144
Total Current	**345**	**569**
Non-Current		
Long service leave benefits	44	35
Total Non-Current	**44**	**35**
Total	**389**	**604**

a) Movement in provisions

2016	Annual leave $'000	Redundancy $'000	Long service leave $'000	Total $'000
Carrying amount at start of year	**276**	**149**	**179**	**604**
Charged to profit or loss				
Additional provisions recognised	112	-	13	125
Amounts used during the year	(191)	(149)	-	(340)
Carrying amount at end of year	**197**	**-**	**192**	**389**

b) Amounts not expected to be settled in the next 12 months

The provision for annual leave represents the employee's statutory entitlements and the entire amount of $197,000 (2015: $276,000) is presented as current since the group does not have the right to defer such settlements.
The provision for long service leave shown in current includes all unconditional entitlements where employees have completed the required period of service. The amount of $148,000 (2015: $144,000) is presented as current as the group does not have the unconditional right to defer settlement.

However, based on past experience, the group does not expect all employees to take the full amount of accrued leave or require payment in the next 12 months. The following amounts reflect leave that is not expected to be taken or paid in the next 12 months.

	2016 $'000	2015 $'000
Annual leave obligations expected to be settled after 12 months	56	42
Long service leave obligations expected to be settled after 12 months	148	101
Total	**204**	**143**

13. Issued Capital

Fully paid ordinary shares	2016 No. '000's	2016 $'000	2015 No. '000's	2015 $'000
Balance at beginning of year	1,261,965	228,100	1,261,965	228,100
Issue of shares	-	-	-	-
Exercise of options	-	-	-	-
Balance at end of year	1,261,965	228,100	1,261,965	228,100

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 2016 there were a total of 36,948,150 unexercised unquoted options issued as share based payments, of which 3,000,000 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 2016 there were a total of 15,000,000 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.

14. Reserves

	2016 $'000	2015 $'000
Reserves		
Business combination	27,812	27,812
Employee equity-settled benefits	2,096	2,060
Other equity-settled benefits	306	306
Foreign Currency Translation Reserve	10	13
	30,224	30,191
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	2,060	2,056
Share based payment expense	36	4
Balance at end of year	2,096	2,060

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.

Other equity-settled benefits reserve		
Balance at beginning of year	306	306
Balance at end of year	306	306

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

Foreign Currency Translation Reserve		
Balance at beginning of year	13	(3)
Foreign Currency Translation	(3)	16
Balance at end of year	10	13

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

15. Earnings Per Share

a) 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.

	2016 cents	2015 cents
From continuing operations attributable to the ordinary equity holders of the Company	(1.37)	(1.55)
From discontinued operations	(0.00)	(0.04)
Total basic earnings per share attributable to the ordinary equity holders of the Company	(1.37)	(1.59)

b) 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).

From continuing operations attributable to the ordinary equity holders of the Company	(1.37)	(1.55)
From discontinued operations	(0.00)	(0.04)
Total diluted earnings per share attributable to the ordinary equity holders of the Company	(1.37)	(1.59)

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.

c) Reconciliation of earnings used in calculating earnings per share

	2016 $'000	2015 $'000
Net Loss attributable to ordinary equity holders for the calculation of basic and diluted earnings per share		
From continuing operations	(17,245)	(19,577)
From discontinued operations	(69)	(543)
	(17,314)	(20,120)

d) Weighted average number of shares used as the denominator

	2016 No. '000's	2015 No. '000's
Weighted average number of ordinary shares for the purposes of basic earnings per share	1,261,966	1,261,966
Effect of dilution:		
Share options	10,977	3,000
Performance rights	26,090	34,308
Weighted average number of ordinary shares adjusted for the effect of dilution	1,299,033	1,299,274

Share options and performance rights are anti-dilutive and are not included in earnings per share dilutive calculation.

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.

16. Commitments and Contingencies

a) Lease Commitments

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

Non-cancellable operating lease payments	2016 $'000	2015 $'000
Within 1 year	81	80
After 1 year but not more than 5 years	181	3
After more than 5 years	-	-
Total minimum lease payments	262	83

b) Cash Commitments

The Company holds term deposits totalling $155,515 (2015: $151,543) as security for the corporate credit card facility and lease at its principal place of business.

17. Segment Information

a) Description of segments

The group has identified its operating segments based on the internal reports that are reviewed and used by the Chief Executive Officer 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.

Production and Personal Care

Production and Personal Care manufactures and sells TPM® and Vital ET® for the use in drug delivery and cosmetic formulations.

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. TPM® is also able to increase the penetration of molecules formulated in the same cream.

Human Health

Phosphagenics' Human Health portfolio covers delivery of drugs through gels, injectables and patches.

The division continues to prioritise development work on the two existing patch assets: TPM®/Oxymorphone and TPM®/Oxycodone.

The division intends to continue to assess commercial opportunities for TPM® enhanced products in gels and injectables.

Revenue is derived from royalty streams and contract research.

All other segments

The BioElixia® division, which previously formed part of the Production and Personal Care segment, was put up for sale at the end of 2014. Information about this discontinued division is provided in note 18.

Sales to the Animal Health and Nutrition segment did not meet materiality levels and is included in the unallocated segment.

b) Segment results

The segment information provided to the chief executive officer for the reportable segments for the year ended 31 December 2016 is as follows:

2016	Production and Personal Care $'000	Human Health $'000	Total all Segments $'000	Unallocated $'000	Total Group $'000
Sales and Royalties	1,293	238	1,531	57	1,588
Total segment revenue	**1,293**	**238**	**1,531**	**57**	**1,588**
Other income	-	76	76	4	80
Interest revenue	-	-	-	171	171
Income from government grants	-	-	-	1,833	1,833
Depreciation and amortisation	(11)	-	(11)	(2,461)	(2,472)
Impairment losses on intangible assets	-	-	-	(7,207)	(7,207)
Employee and directors benefit expense	(447)	(853)	(1,300)	(2,128)	(3,428)
Other operating expenses from continuing operations	(366)	(1,366)	(1,732)	(6,078)	(7,810)
Net operating profit/(loss) after tax	**469**	**(1,905)**	**(1,436)**	**(15,809)**	**(17,245)**
Segment assets	**634**	**162**	**796**	**12,558**	**13,354**

2015	Production and Personal Care $'000	Human Health $'000	Total all Segments $'000	Unallocated $'000	Total Group $'000
Sales and Royalties	2,057	42	2,099	91	2,190
Total segment revenue	**2,057**	**42**	**2,099**	**91**	**2,190**
Other income	-	6	6	1	7
Interest revenue	-	-	-	512	512
Income from government grants	-	-	-	2,279	2,279
Recoveries	-	-	-	160	160
Depreciation and amortisation	(137)	-	(137)	(3,131)	(3,268)
Impairment losses on intangible assets	-	-	-	(7,837)	(7,837)
Employee and directors benefit expense	-	-	-	(5,852)	(5,852)
Other operating expenses from continuing operations	(811)	(2,244)	(3,055)	(4,713)	(7,768)
Net operating profit/(loss) after tax	**1,109**	**(2,196)**	**(1,087)**	**(18,490)**	**(19,577)**
Segment assets	**1,310**	**194**	**1,504**	**29,240**	**30,744**

c) Understanding segment results

i) Segment revenue

Revenues from external customers comes from the sale of TPM® products on a wholesale basis as well as royalties. Revenues of approximately $818,000 (2015: $1,669,000) are derived from a single external customer group. These revenues are attributed to the Bulk and Personal Care segment.

The entity is domiciled in Australia. The amount of its revenue from external customers broken down by location of customers is shown below.

	2016 $'000	2015 $'000
Australia	6	3
Switzerland	809	1,389
United States	397	544
India	193	163
Japan	123	-
Other	3	-
Total revenue	1,531	2,099
Segment revenue reconciles to total revenue from continuing operations as follows:		
Total segment revenue	1,531	2,099
Other revenue	57	91
Total revenue from continuing operations (note 2)	1,588	2,190

ii) Segment assets

Segment assets are measured in the same way as the financial statements. These assets are allocated based on the operations of the segments and physical location of the asset.

The total of non-current assets broken down by location of assets is as follows:

Australia	3,170	12,785
United States	1	3
Total assets	3,171	12,788

Reportable segments' assets are reconciled to total assets as follows:

Segment operating assets	796	1,504
Discontinued operation (BioElixia® - see note 18)	-	17
Unallocated		
• Intangibles	2,786	12,269
• Cash & cash equivalents	6,092	12,395
• All other operating assets from continuing activities	3,680	4,559
Total assets per the balance sheet	13,354	30,744

iii) Segment liabilities

Segment liabilities are measured in the same way as the financial statements. These liabilities are allocated based on the operations of the segment.

Reportable segments' liabilities are reconciled to total liabilities as follows:

Segment operating liabilities	-	-
Unallocated:		
• Deferred tax liabilities	-	-
• Other operating liabilities from continuing activities	1,707	1,816
Total liabilities per the balance sheet	1,707	1,816

18. Discontinued Operation

a) Description

In December 2014, the Company made the strategic decision to sell its branded cosmetics division, BioElixia®. The sale was put on hold pending the outcome of the Prophase arbitration. Accordingly, this division has been treated as a discontinued operation for the periods ended 31 December 2015 and 2016.

b) Financial performance and cash flow information

The financial performance and cash flow information presented is for the years ended 31 December 2016 and 2015.

	2016 $'000	2015 $'000
Total sales	48	144
Less retailer discounts applied	-	(114)
Revenue (note 2)	48	30
Cost of sales	(43)	(110)
Stock obsolescence expense	(2)	(236)
Marketing	-	(50)
Other expenses	(72)	(177)
Loss before income tax	(69)	(543)
Income tax expense	-	-
Loss from discontinued operation	(69)	(543)

c) Assets and liabilities of disposal group classified as held for sale

The following assets and liabilities were reclassified as held for sale in relation to the discontinued operation as at 31 December 2016.

Assets classified as held for sale		
Inventories	-	17
Total assets of group held for sale	-	17

19. Related Party Transactions

a) Subsidiaries

Interests in subsidiaries are set out in note 20(a)

b) Key management personnel compensation

Short-term employee benefits	1,872,431	2,340,093
Post-employment benefits	153,198	164,579
Long-term benefits	16,388	22,657
Termination benefits	-	492,842
Share-based payments	24,583	2,724
	2,066,600	3,022,895

Detailed remuneration disclosures are provided in the remuneration report on pages 21 to 27.

c) Transactions with other related parties

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.

20. Interest in Other Entities

a) Subsidiaries

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

Entity	Country of Incorporation	2016 Equity Interest	2015 Equity Interest	2016 Investment $'000	2015 Investment $'000
Vital Health Sciences Pty Ltd	Australia	100%	100%	4,300	13,300
Preform Technologies Pty Ltd[1]	Australia	100%	100%	-	-
Adoil Pty Ltd[1]	Australia	100%	100%	-	-
Phosphagenics Inc.	USA	100%	100%	-	-

[1] Non-operating subsidiaries

b) Interests in associates and joint ventures

Entity	Country of Incorporation	2016 Equity Interest	2015 Equity Interest	2016 Investment $'000	2015 Investment $'000
Phusion Laboratories LLC	USA	50%	50%	-	-

Phusion Laboratories was a jointly controlled entity formed in March 2010 with ProPhase Labs Inc. Under the Operating Agreement Phosphagenics was not required to contribute to funding. Phusion had accumulated losses which management had assessed that Phosphagenics did not have an obligation to make good. Accordingly Phosphagenics' share of losses has historically not been recorded in the Consolidated Income Statement or Balance Sheet.

Phosphagenics and ProPhase were in arbitration relating to the jointly controlled entity from October 2014 until the ruling was handed down by the American Arbitration Association in November 2016. The ruling included an order for the jointly controlled entity to be wound up. This process has initiated but has not yet completed.

21. Events After Balance Sheet Date

The Australian Tax Office has confirmed a refund of $2,294,000 for the R&D tax incentive will be paid on 1 March 2017.

22. 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:

	2016 $'000	2015 $'000
Cash at Bank	5,887	4,471
Short Term Deposits	205	7,924
	6,092	12,395

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

Net Loss after tax	(17,314)	(20,120)
Adjustments for:		
Depreciation and amortisation and impairments	2,472	3,268
Impairment of intangible assets	7,207	7,837
Write down of fixed assets for obsolescence	-	41
Share based payment expense	36	4
Foreign currency translation reserve	(3)	16
Interest received	(171)	(510)
Changes in assets and liabilities:		
Decrease in trade receivables and other receivables	1,117	489
Decrease/ (increase) in inventories	41	(58)
Decrease in other current assets	295	20
Decrease in assets classified as held for sale	17	365
Decrease in trade payables and other payables	106	186
(Decrease) in provisions	(215)	(243)
Net cash (used in) operating activities	(6,412)	(8,705)

23. Financial Risk Management

This note explains the group's exposure to financial risks and how these risks could affect the group's future financial performance. Current year profit and loss information has been included where relevant to add further context.

Risk	Exposure arising from	Measurement	Management
Market risk – interest rate	Cash deposits at variable rates	Sensitivity analysis	
Market risk – foreign exchange	Future commercial transactions Recognised financial assets and liabilities not denominated in AUD	Cash flow forecasting Sensitivity analysis	Foreign currency hedges
Credit risk	Cash and cash equivalents, trade receivables	Aging analysis	Credit limits
Liquidity risk	Other liabilities	Rolling cash flow forecast	Availability of cash

The group's overall risk management program recognises the unpredictability of financial markets and seeks to minimise material adverse effects on the financial performance of the group. The Chief Executive Officer, Chief Financial Officer and Executive Management team are responsible to the Board through the audit and risk committee for the risk management program.

a) Market risk

i) Interest rate risk

The group holds interest bearing assets and therefore the income and operating cash flows are exposed to market interest rates. At the end of the reporting period, the group had the following term and at call deposits. Refer to note 22 for additional information.

	2016 $'000	2015 $'000
Financial Assets		
Cash and cash equivalents	6,092	12,395

Sensitivity

Profit or loss is sensitive to higher/lower interest income from cash and cash equivalents as a result of changes in interest rates. Equity does not change as a result of increase/decrease in interest rates as the group does not hold financial assets or liabilities designated as cash flow hedges.

	Impact on post tax profit		Impact on other components of equity	
	2016 $'000	2015 $'000	2016 $'000	2015 $'000
Judgements of reasonably possible movements:				
+1% (100 basis points)	61	123	-	-
-0.5% (50 basis points)	(30)	(62)	-	-

ii) Foreign Currency Risk

Foreign exchange risk arises when future commercial transactions and recognised assets and liabilities are denominated in a currency that is not the group's functional currency. The group operates in the United States as well as sells TPM® products and buys raw materials for their production which are denominated in US dollars. The Company still has outstanding commitments related to the reformulation of the TPM®/Oxymorphone patch which are denominated in Euros. The group is exposed to foreign exchange risk arising from currency exposures of transactions in US dollars and Euros.

The Chief Executive Officer and Chief Financial Officer regularly monitor the potential impact of movements in foreign exchange exposure and from time to time may take out short-term foreign exchange hedges for committed expenditures.

Approximately 84% of sales and royalties (2015: 75%) are denominated in currencies other than the presentation currency of the Group (Australian dollars), whilst approximately 68% (2015: 71%) of costs are denominated in the Groups presentation currency.

At 31 December 2016 the Group had the following exposure to US dollar foreign currency not designated in cash flow hedges:

	2016 $'000	2015 $'000
Financial Assets		
Cash and cash equivalents	671	22
Trade and other receivables	185	731
	856	753
Financial Liabilities		
Trade and other payables	(115)	(565)
Net Exposure	741	188

Sensitivity

The group is primarily exposed to changes in US/AUD exchange rates. The sensitivity of profit or loss to changes in the US/AUD exchange rate arises mainly from US-denominated financial assets and liabilities.

	Impact on post tax profit		Impact on other components of equity	
	2016 $'000	2015 $'000	2016 $'000	2015 $'000
Judgements of reasonably possible movements:				
Consolidated				
AUD/USD +10%	(67)	(17)	-	-
AUD/USD -10%	82	21	-	-

b) Credit risk

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 setting appropriate credit limits, as a means of mitigating the risk of financial loss from defaults.

Group exposure to 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 2016	≤ 6 Months $'000	6-12 Months $'000	1-5 Years $'000	>5 Years $'000	Total $'000
Financial Assets					
Cash and cash equivalents	6,092	-	-	-	6,092
Trade and other receivables	2,887	720	-	-	3,607
	8,979	720	-	-	9,699
Financial Liabilities					
Trade and other payables	(1,318)	-	-	-	(1,318)
	(1,318)	-	-	-	(1,318)
Net Exposure	**7,661**	**720**	**-**	**-**	**8,381**

c) Liquidity risk

Prudent liquidity risk management implies maintain sufficient cash balances. The directors regularly monitor the cash positon of the group, giving consideration to the level of expenditure and future project commitments.

d) Fair value

Due to the short term nature of the financial instruments, their carrying value is assumed to approximate their fair value.

24. Parent Entity Financial Information

	2016 $'000	2015 $'000
Balance Sheet		
Current assets	9,274	17,093
Total assets	38,279	55,440
Current liabilities	1,539	1,518
Total liabilities	1,595	1,574
Shareholders' equity		
Issued capital	228,100	228,100
Reserves		
Employee equity benefits reserve	2,096	2,060
Foreign Currency Translation Reserve	348	336
Other equity-settled benefits reserve	306	306
Accumulated losses	(194,166)	(176,936)
	36,684	53,866
Loss of the parent entity	(17,230)	(24,052)
Total comprehensive loss of the parent entity	(17,230)	(24,052)
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.	-	-

Directors' Declaration

In the directors' opinion:

(a) the financial statements and notes of Phosphagenics Limited for the financial year ended 31 December 2016 are in accordance with the Corporations Act 2001, including:

  (i) complying with Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001 and other mandatory professional reporting requirements; and

  (ii) giving a true and fair view of the consolidated entity's financial position as at 31 December 2016 and of its performance for the year ended on that date; and

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

Note 1(a) confirms that the financial statements and notes also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A of the Corporations Act 2001.

This declaration is made in accordance with a resolution of the directors.

Peter Lankau
Chairman

28 February 2017
Melbourne

Independent auditor's report

To the shareholders of Phosphagenics Limited

Report on the audit of the financial report

Our opinion

In our opinion:

The accompanying financial report of Phosphagenics Limited (the Company) and its controlled entities (together, the Group) is in accordance with the *Corporations Act 2001*, including:

a) giving a true and fair view of the Group's financial position as at 31 December 2016 and of its financial performance for the year then ended

b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

What we have audited

The Group's financial report comprises:

- the consolidated balance sheet as at 31 December 2016
- the consolidated statement of comprehensive income for the year then ended
- the consolidated income statement for the year then ended
- the consolidated statement of changes in equity for the year then ended
- the consolidated statement of cash flows for the year then ended
- the notes to the consolidated financial statements, which include a summary of significant accounting policies
- the directors' declaration

Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial report* section of our report.

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

Independence

We are independent of the Group in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

Material uncertainty related to going concern

We draw attention to Note 1 in the financial report, which indicates that the Group incurred a net loss of $17,314,000 during the year ended 31 December 2016 and a net cash outflow from operating activities of $6,412,000. The Group's ability to continue as a going concern is dependent upon the Group being successful in raising funds via the issuance of new equity or reaching contractual agreement for other funding within the next twelve months. These conditions, along with other matters set forth in Note 1, indicate that a material uncertainty exists that may cast significant doubt about the Group's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Our audit approach

An audit is designed to provide reasonable assurance about whether the financial report is free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial report as a whole, taking into account the geographic and management structure of the Group, its accounting processes and controls and the industry in which it operates.

The Group operates in the biotechnology industry, undertaking development and optimisation of proprietary drug delivery methodology for pharmaceutical, consumer products and animal health sectors. The Group owns a portfolio of proprietary technology with applications in different stages between development and commercialisation. Operations are primarily based in Australia.

Materiality	*Audit scope*	*Key audit matters*
• For the purpose of our audit we used overall Group materiality of $526,750, which represents approximately 5% of the Group's loss before impairment losses and tax. • We applied this threshold, together with qualitative considerations, to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements on the financial report as a whole. • We chose loss before impairment loses and tax as the benchmark because, in our view, it is the metric against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark. • We selected 5% based on our professional judgement which is within the range of commonly acceptable benchmarks.	• Our audit focused on where the directors made subjective judgements; for example, significant accounting estimates involving assumptions and inherently uncertain future events. • The accounting processes are structured around a Group finance function at the head office in Melbourne. Our audit procedures included attendances at the Group head office.	• Amongst other relevant topics, we communicated the following key audit matters to the Audit and Risk Committee: – Carrying value of intangible assets – Research and development tax incentive • These are further described in the *Key audit matters* section of our report, except for the matter which is described in the *Material uncertainty related to going concern* section.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial report for the current period. In addition to the matter described in the *Material uncertainty related to going concern* section, we have determined the matters described below to be the key audit matters to be communicated in our report.

The key audit matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. Further, any commentary on the outcomes of a particular audit procedure is made in that context.

Key audit matter	How our audit addressed the key audit matter
Carrying value of intangible assets *(Refer to Note 10 Intangible Assets)* The Group holds intangible assets which relate to patents that were purchased by the Group at 31 December 2004. Other intellectual property developed by the Group is not capitalised on the Balance Sheet. Management consider annually if there are any indicators that the intangible assets are impaired. The main two indicators that management consider are: • market capitalisation • the ongoing viability of the capitalised patent portfolio As indicators of possible impairment were noted at 31 December 2015, management engaged an expert to value the patents in line with Australian Accounting Standards. At 31 December 2015 this resulted in an impairment of $7.8 million being recognised. At 31 December 2016 management noted further impairment indicators for two projects and obtained a third party valuation of the affected patents and their related products. This resulted in an impairment of $7.2m being recognised with on project being written down to $0. The value of this project previously related to the expected royalties from a 3rd party drug launch is no longer expected be commercialised by the 3rd party. For the other project where indicators of impairment were noted, a valuation was performed which concluded that this project was not impaired. The value of the remaining intangible assets on the balance sheet is $2.8m. We focused on the carrying values of the intangible assets due to their financial significance and the inherent judgement	We considered the appropriateness of the methodology applied by management in performing the impairment review. We inspected management's paper which considered the indicators of impairment at 31 December 2016 and discussed this with the Audit and Risk Committee. For the project that was fully impaired, we discussed the rationale for the impairment with management and inspected supporting legal documents. For the project where an impairment indicator was noted but no impairment was recognised, we inspected management's 3rd party valuation and obtained support for the key assumptions. We evaluated the adequacy of disclosures made in the financial report in this respect.

Key audit matter	How our audit addressed the key audit matter
involved in assessing indicators of impairment.	
Research and development tax incentive (Refer to Note 1(vi) Critical accounting estimates and judgements) Under the research and development (R&D) Tax Incentive scheme, the Group receives a 45% (43.5% for FY2017) refundable tax offset of eligible expenditure if its turnover is less than $20 million per annum provided, it is not controlled by income tax exempt entities. An R&D plan is filed with AusIndustry in the following financial year, and based on this filing, the Group receives the incentive in cash. Management performed a detailed review of the Group's total research and development expenditure to determine the potential claim under the R&D tax incentive legislation. The receivable at year end for the incentive was $3.0m. This includes: • A lodged claim of $2.3m for the period 1 July 2015 to 30 June 2016. • An estimated claim of $0.7m for the period 1 July 2016 to 31 December 2016. We focused on the R&D tax incentive due to the size of the accrual and because there is a degree of judgement and interpretation of the R&D tax legislation required by management to assess the eligibility of the R&D expenditure under the scheme.	We considered management's R&D tax estimate to assess the amount accrued as at 31 December 2016. As part of our procedures we: • Compared the estimates made in previous years to the amount of cash actually received after lodgement of the R&D tax claim. • Compared the nature of the R&D expenditure included in the current year estimate to the prior year estimate. • Considered the nature of the expenses against the eligibility criteria of the R&D tax incentive scheme to form a view about whether the expenses included in the estimate were likely to meet the eligibility criteria. • Assessed the eligible expenditure used to calculate the estimate to the expenditure recorded in the general ledger. • Inspected copies of relevant correspondence with AusIndustry and the ATO related to the claims. Recent correspondence from the ATO indicated a refund of $2.3m will be paid to the Group on 1 March 2017 in respect of the lodged claim.

Other information

The directors are responsible for the other information. The other information comprises the Chairman's letter to shareholders, operating and financial review, director's report, corporate governance statement, statement of shareholdings, shareholder information and corporate directory in the Group's annual report for the year ended 31 December 2016, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors 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 control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: http://www.auasb.gov.au/auditors_files/ar2.pdf. This description forms part of our auditor's report.

Report on the remuneration report

Our opinion on the remuneration report

We have audited the remuneration report included in pages 21 to 27 of the directors' report for the year ended 31 December 2016.

In our opinion, the remuneration report of Phosphagenics Limited for the year ended 31 December 2016 complies with section 300A of the *Corporations Act 2001*.

Responsibilities

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.

PricewaterhouseCoopers

Anton Linschoten
Partner

28 February 2017

Additional Shareholder Information

The shareholder information set out below was applicable as at 16 March 2017.

Supplementary information as required by ASX listing requirements.

A. Distribution of Equity Shareholders

Range of Shareholders			
Range	**Holders**	**Units**	**%**
1 - 1,000	463	115,606	0.01
1,001 - 5,000	964	2,986,912	0.24
5,001 - 10,000	751	5,970,223	0.47
10,001 - 100,000	2,334	90,588,802	7.18
100,001 - 9,999,999,999	1,113	1,162,304,414	92.10
	5,625	**1,261,965,957**	**100.00**

There were 3,264 holders of less than a marketable parcel of ordinary shares.

B. Equity Security Holders

The names of the twenty largest holders of quoted equity securities are listed below:

	Name	Number held	% of issued shares
1	Citicorp Nominees Pty Limited	118,656,200	9.40
2	Merrill Lynch (Australia) Nominees Pty Limited	68,639,378	5.44
3	HSBC Custody Nominees (Australia) Limited	59,918,341	4.75
4	Paroha Nominees Pty Ltd	45,367,143	3.59
5	J P Morgan Nominees Australia Limited	33,346,523	2.64
6	Rosscope Pty Ltd <Ross Copeland Family A/C>	26,846,548	2.13
7	Jogra Nominees Pty Ltd	26,000,000	2.06
8	BNP Paribas Noms Pty Ltd <DRP>	25,815,253	2.05
9	Mr Ross Copeland + Mrs Gina Copeland	15,992,642	1.27
10	Holdrey Pty Ltd <Don Mathieson Family A/C>	15,000,000	1.19
11	Dr Maurice Arthur Trewhella + Mrs Elizabeth Trewhella <Simpetejen Super Fund A/C>	14,500,000	1.15
12	Berkeley Consultants Pty Ltd	13,546,738	1.07
13	Mr Brandon Armon Batagol	12,672,263	1.00
14	BHL Pension Pty Ltd <BHL Pension Fund A/C>	12,000,000	0.95
15	Mr Ross Graham Copeland + Mrs Gina Copeland <Publicity Press S/F A/C>	11,094,836	0.88
16	Mr David Segal	9,000,000	0.71
17	ABN Amro Clearing Sydney Nominees Pty Ltd <Custodian A/C>	8,816,547	0.70
18	Mrs Susan Margaret Chudleigh + Mr John West Chudleigh	8,600,000	0.68
19	Helping Hand Sweet Co Pty Ltd	7,462,403	0.59
20	Mr Jeffrey Markoff <Markoff Super St5 A/C>	7,365,575	0.58
	Sub-Total – Top 20 Holders	**540,640,390**	**42.84**
	– Other Holders	721,325,567	57.16
	TOTAL ISSUED SHARES	**1,261,965,957**	**100.00**

Unquoted equity securities over ordinary shares	Number on issues	Number of holders.
Employee performance rights	15,000,000	1
Employee options	33,948,000	16
Options expiring 22 May 2019	3,000,000	3

Holders of options	Number on issues	% of options.
Dr G Cauwenberg	1,000,000	33.3
Mr N Drona	1,000,000	33.3
Montoya Pty Ltd (ATF Buttercup Trust)	1,000,000	33.3

C. Substantial Holders

Substantial shareholders with a shareholding greater than 5% as shown in substantial shareholder notices received by the Company as at 16 March 2017:

Holder of relevant interest	Entitlement to No. securities	Date of SSH Notice	Form No.
Allan Gray Australia Pty Ltd	94,853,127	04.01.2016	604

D. Voting Rights

The voting rights attached to each class of equity securities are set out below:

(a)	Ordinary shares	On a show of hands every member present at a meeting in person or by proxy shall have one vote and on a poll each share shall have one vote.
(b)	Employee performance rights	No voting rights
(c)	Options	No voting rights

E. Buy-Back

The Company has not undertaken any share buy-backs during or since the year ended 31 December 2016.

Corporate Directory

Phosphagenics Limited
(ABN 32 056 482 403)

Board of Directors

Mr Peter Lankau (Chairman)
Dr Ross Murdoch (Chief Executive Officer)
Dr Geert Cauwenbergh
Dr Greg Collier
Mr David Segal

Company Secretary

Ms Anna Legg

Registered Office

Unit A8, 2A Westall Road
Clayton VIC 3168
Australia

Principal Business Office

Unit A8, 2A Westall Road
Clayton VIC 3168
Australia

Telephone: +61 (0)3 9002 5000

Email: info@phosphagenics.com

Web: www.phosphagenics.com
www.bioelixia.com

Share Registry

Computershare Investor Services Pty Ltd
Yarra Falls
452 Johnston Street
Abbotsford VIC 3067
Australia

Auditors

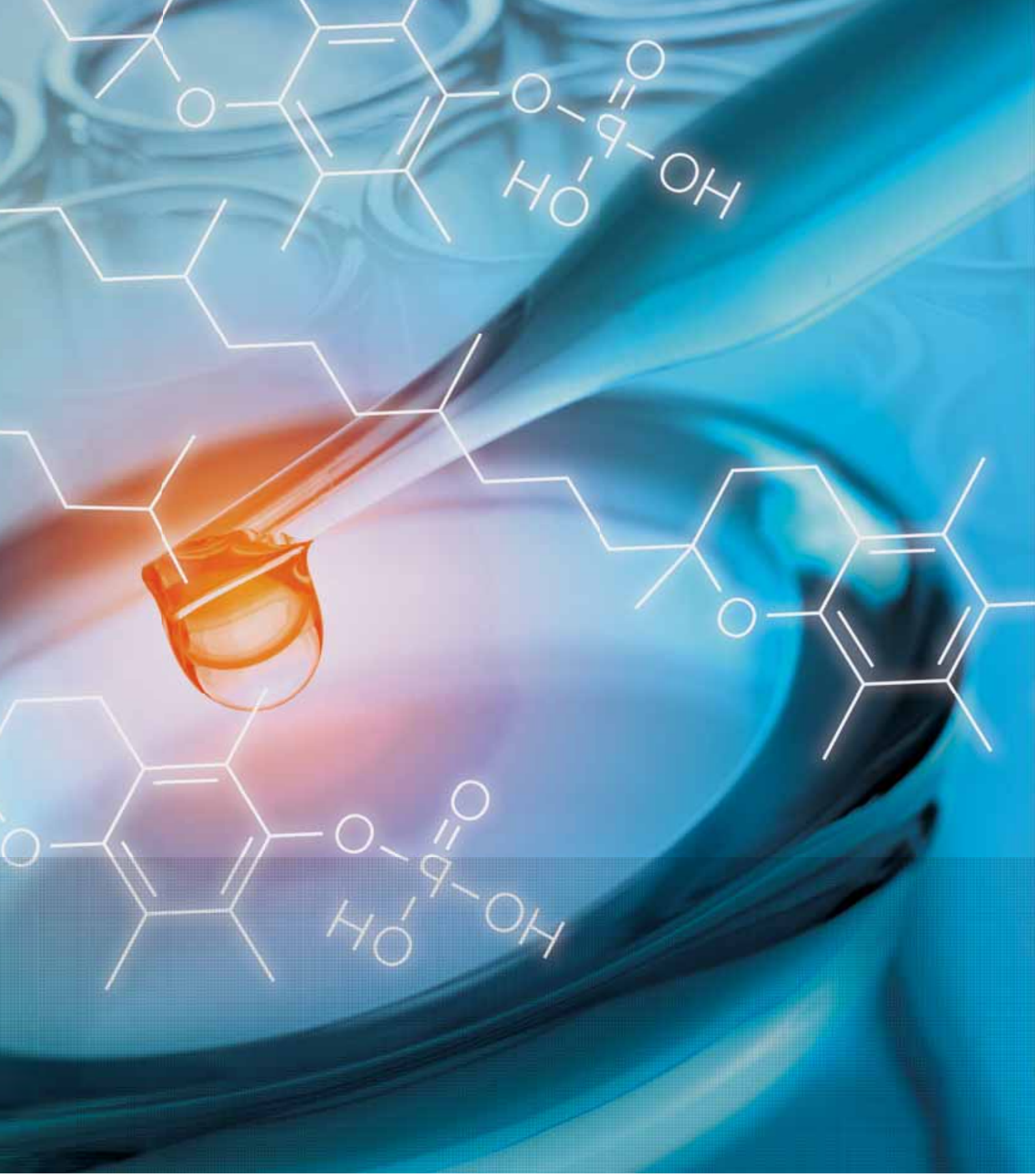
PricewaterhouseCoopers
2 Riverside Quay
Southbank VIC 3006
Australia

Australian Securities Exchange Limited

The Company's securities are quoted on the official lists of the Australian Securities Exchange Limited (ASX). The Company's ASX Code is POH and the home exchange is in Melbourne.

American Depository Receipt

In July 2007 the Company upgraded its level 1 American Depository Receipt (ADR) on the US over-the-counter (OTC) securities market to the international OTCQX, a new premium market tier in the US for international exchange-listed companies, operated by OTC Markets Group, Inc. The Company's ADR ticker symbol is PPGNY.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