PALLA PHARMA

# Palla Pharma Limited

ABN 26 107 872 453

# Annual report for the year ended 31 December 2019

# Appendix 4E

The following information is presented in accordance with ASX listing rule 4.3A.

**1. Details of the reporting period and previous corresponding period**

| | |
|---|---|
| Reporting period: | year ended 31 December 2019 |
| Previous corresponding period: | year ended 31 December 2018 |

**2. Results for announcement to the market**

| | | Consolidated entity | | |
|---|---|---|---|---|
| | | **31 December 2019 $** | 31 December 2018 $ | Change % |
| 2.1 | Revenue from ordinary activities | **54,843,483** | 46,563,381 | +17.8% |
| 2.2 | Loss from ordinary activities after tax attributable to members | **(7,639,443)** | (5,788,408) | +32.0% |
| 2.3 | Net loss for the period attributable to members | **(7,639,443)** | (5,788,408) | +32.0% |

2.4 There were no dividends paid, recommended or declared during the current or previous reporting period.

2.5 The record date for determining entitlements to dividends – not applicable.

2.6 Supplementary commentary on figures presented in 2.1 to 2.4 above – please refer to the Annual Report for the year ended 31 December 2019 attached and Results Presentation issued 27 February 2020.

**3. Consolidated statement of profit or loss and other comprehensive income**

Please refer to the Annual Report for the year ended 31 December 2019 attached.

**4. Consolidated statement of financial position**

Please refer to the Annual Report for the year ended 31 December 2019 attached.

**5. Consolidated statement of cash flows**

Please refer to the Annual Report for the year ended 31 December 2019 attached.

**6. Consolidated statement of changes in equity**

Please refer to the Annual Report for the year ended 31 December 2019 attached.

**7. Dividend payments**

Not applicable.

**8. Dividend reinvestment plans**

Not applicable.

**9. Net tangible assets per security**

| | Consolidated entity | | |
|---|---|---|---|
| | **31 December 2019** | 31 December 2018 | Change |
| | **$** | $ | % |
| Net tangible assets per security | 0.43 | 0.43 | nil |

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

Not applicable.

**11. Associate or joint venture entities**

Not applicable.

**12. Other significant information**

Please refer to the Annual Report for the year ended 31 December 2019 attached.

**13. Foreign entities**

Not applicable.

**14. Results commentary for period**

14.1 Earnings per security and the nature of any dilution - please refer to note 30 of the Annual Report for the year ended 31 December 2019 attached.

14.2 Returns to shareholders including distributions and buy-backs - not applicable.

14.3 Significant features of operating performance - please refer to the Annual Report for the year ended 31 December 2019 attached and Results Presentation issued 27 February 2020.

14.4 The results of segments that are significant to an understanding of the business as a whole - please refer to note 5 of the Annual Report for the year ended 31 December 2019 attached.

14.5 A discussion of trends in performance - please refer to the Annual Report for the year ended 31 December 2019 attached and Results Presentation issued 27 February 2020

14.6 Any other factors which have affected the results in the period or which are likely to affect the results in the future, including those where the effect could not be quantified - please refer to the Annual Report for the year ended 31 December 2019 attached and Results Presentation issued 27 February 2020.

**15. Independent audit of financial statements**

The financial information contained in this report has been extracted from the financial statements in the attached audited Annual Report for the year ended 31 December 2019.

# Palla Pharma Limited

ACN 107 872 453

# Annual report
# for the year ended 31 December 2019

# Palla Pharma Limited ACN 107 872 453
# Annual report - 31 December 2019

## Contents

| | |
|---|---|
| **Directors** | Mr. Simon Moore (Independent Non-Executive Chairman)<br>Mr. Jarrod Ritchie (Managing Director and CEO)<br>Mr. Todd Barlow (Non-Executive Director)<br>Mr. Stuart Black (Independent Non-Executive Director)<br>Ms. Sue MacLeman (Independent Non-Executive Director) |
| **Secretary** | Mr. Jaime Pinto |
| **Principal registered office in Australia** | c/- Link Market Services Limited<br>Tower 4<br>727 Collins Street<br>Docklands VIC 3008<br><br>Tel: +61 3 9301 0800<br>Fax: +61 3 9301 0899 |
| **Share registry** | Link Market Services Limited<br>Tower 4<br>727 Collins Street<br>Docklands VIC 3008 |
| **Auditor** | KPMG<br>Tower 2<br>727 Collins Street<br>Docklands VIC 3008 |
| **Australian company number** | 107 872 453 |
| **Mailing address** | PO Box 2139<br>Melbourne VIC 3001 |
| **Stock exchange listing** | Australian Securities Exchange<br>(ASX Code: PAL) |
| **Website** | www.pallapharma.com |

## Directors' report

The directors present their report on the consolidated entity (referred to hereafter as the Group) consisting of Palla Pharma Limited ("the Company") and the entities it controlled at the end of, or during, the year ended 31 December 2019.

### Change of company name

On 19 June 2019 the company name was changed from TPI Enterprises Limited to Palla Pharma Limited.

### Directors

The following persons were directors of Palla Pharma Limited during the whole of the financial year and up to the date of this report:

Mr. Simon Moore (Independent Non-Executive Chairman)
Mr. Jarrod Ritchie (Managing Director and CEO)
Mr. Todd Barlow (Non-Executive Director)
Mr. Stuart Black (Independent Non-Executive Director)
Ms. Sue MacLeman (Independent Non-Executive Director)

### Principal activities

During the year the principal continuing activities of the Group were the production and distribution of Narcotic Raw Material ("NRM"), Active Pharmaceutical Ingredients ("API") and Finished Dosage Formulations ("FDF") for supply to international pharmaceutical markets, and the production and distribution of poppy seed for supply to international culinary markets.

### Review of operations

*Financial Results Summary*

| | **Consolidated entity** | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Sales of Narcotic Raw Material ("NRM"), Active Pharmaceutical Ingredients ("API"), Finished Dosage Formulations ("FDF") and Poppy Seed | **54,685,394** | 46,170,998 |
| Statutory Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) | **(2,174,672)** | (2,567,893) |
| Statutory Earnings Before Interest and Tax (EBIT) | **(4,688,558)** | (5,119,188) |
| Statutory (Loss) for the year after Interest and Tax | **(7,639,443)** | (5,788,409) |
| Net cash (outflow) from operating activities | **(9,469,268)** | (14,645,705) |
| Operating EBITDA | **(311,751)** | (2,431,650) |

A near breakeven Operating EBITDA for 2019 supports the Group's strategy to pivot from a pure NRM supplier to a downstream API and FDF producer.

Operating EBITDA, a non-GAAP financial measure, is used internally within the Group to manage performance and is determined by adding back significant non-recurring items (litigation settlement and acquisition expenses), and deducting other income and gains on non-core asset disposals of $1.9 million (2018: $0.1 million). A $2.1 million improvement in the reported Operating EBITDA loss from $2.4 million for the 2018 full-year to an Operating EBITDA loss of $0.3 million for the 2019 full-year reflects the increased operating leverage associated with increased production volumes, improved sales mix and minimal change in Indirect overhead costs.

A 77% increase in margin accretive API sales, early termination of a non-opiate contract manufacturing supply agreement and increasing opiate FDF sales were highlights of the year. Offsetting these positives, was a deferral of UK and French sales in the 4th quarter, along with significant non-recurring legal and quality costs, which negatively impacted resulting in both Revenue and Operating EBITDA below expectation.

**Review of operations (continued)**

Despite these short-term setbacks, the business continues to strengthen its foundation for the future with an increased focus on downstream, margin accretive FDF sales, through both contract manufacturing and marketing authorisation based supply agreements.

To support the strategy of increasing downstream margin accretive sales, the Group acquired six opiate based marketing authorisations subsequent to 31 December 2019 and expanded its API production capacity to 70 tonne per annum. The Group continues to focus on increased poppy straw supply diversification and alkaloid yields for its NRM operations, via its Australian and northern hemisphere supply chains.

The Group reported a statutory loss after income tax for the year ended 31 December 2019 of $7.6 million (2018: $5.8 million) and a statutory Earnings Before Interest, Tax, Depreciation and Amortisation ("EBITDA") loss of $2.2 million (2018: $2.6 million).

Sales revenue increased to $54.7 million representing an 18.4% increase over the corresponding full year period. The increase was primarily driven by the growth of API, opiate based FDF and Poppy Seed sales. Reported Gross Profit for the Group increased to $17.3 million, a 15.3% increase from 2018, due to the continued benefit of sales volume growth and greater plant utilisation. Indirect overhead costs of $17.6 million for the 2019 full-year period (2018: $17.5 million) increased marginally, despite additional investment in new product development and one-off costs associated with improvements in the Norway quality processes.

Net finance expenses increased for 2019 to $3.1 million (2018: $1.7 million) due to higher utilisation of the working capital debt facilities, driven by increased net working capital employed in inventories as a result of the high codeine patent litigation and inability to process harvested high codeine poppy straw until the dispute was resolved in June 2019.

In November 2019 the Group completed an equity capital raise through a placement and entitlement offering to raise net proceeds of $29.5 million. Capital raised was used to repay borrowings and meet the Group's near term NRM and API growth capital expenditure needs. By reducing its borrowing levels, the Group was able to consider other debt financing options which enabled it to renegotiate its working capital debt facility offering with Washington H. Soul Pattinson and Company Limited on more favourable terms, which included a reduced interest rate and extension of maturity date to August 2021.

*Raw Material Straw Supply and Poppy Seed*

A positive 2018/19 growing season in Australia saw the Group harvest record poppy straw volumes at the lowest growing cost achieved for a domestic harvest for the Group. Northern Hemisphere straw supply improved further during 2019, with the securing of additional aggregator supply agreements and a continued focus on improving local expertise with increased farmer and aggregator engagement through the Group's on-the-ground agricultural expertise in Europe. The diversity of poppy straw supply sources continues to be of benefit in negating any impacts on domestic supply through climatic risks that adversely impacted mainland growers in Australia for the 2019/20 growing season.

Poppy seed sales prices held at record levels during the first half of 2019 at over €4 per kilogram for premium grade product, and the Group took advantage of this strong pricing by realising most of its seed inventory during this period.

*NRM production in Australia*

NRM production productivity continued to improve with a more reliable straw supply, seeing daily extraction rates in 2019 increasing further compared to 2018.

The majority of the Group's NRM production is transferred to Norway for conversion to both Codeine Phosphate and Pholcodine API's. However, as the capacity of NRM production for the Group is currently greater than that of API production, external NRM sales will continue to be an important revenue contributor in the short to medium term.

**Review of operations (continued)**

The Group continues to invest in research and development of its core NRM production process to further optimise the extraction process and increase production efficiencies. The unique water-based extraction process used is delivering a competitive cost advantage for the Group and when combined with a more reliable straw supply, has enabled increased sales volumes and long-term supply agreements to be secured throughout the supply chain.

*API production in Norway*

During 2019 the Group experienced significant growth in API production and sales volumes and further volume growth is expected throughout 2020, with a major enhancement in production capacity achieved in the latter part of 2019. Further market share gains and customer diversification have continued to be realised in both Codeine Phosphate and Pholcodine API markets, along with sales into new regions not previously supplied, including first sales into developing markets in south-east Asia and North Africa.

While pricing across the industry is at cyclical lows, the Group continues to attract new API volumes and grow market share at commercially attractive margins, demonstrating the Group's competitive cost advantage in API production. This was further underpinned by the securing of several multi-year supply agreements through 2019 for opiate based API and FDF products.

*FDF production in Norway*

FDF production provides contract manufacturing ("CMO") services for third parties under long term manufacture and supply agreements. These services include granulating, tableting, packaging and warehousing, all of which requires high levels of labour, working capital and generates lower margins than the core businesses of the Group; NRM production and downstream conversion of NRM into API.

During 2019 further improvement in both tableting and packaging production uptime was achieved. However, non-opiate based production remained a challenge due to the bespoke nature of the legacy non-opiate based contract and range of products needing to be produced. This requires short production runs resulting in significant production downtime for product changeover and line cleaning. In late 2019 the Group successfully negotiated an early exit from its legacy non-opiate based CMO contract from February 2020. This which will free up significant tableting capacity to direct towards higher-margin opiate-based products, while reducing operational costs and inventory holdings that were required to be contractually maintained as a safety buffer.

*Reconciliation of Operating EBITDA to Statutory EBITDA and Loss After Tax*

The consolidated financial statements comply with International Financial Reporting Standards (IFRS's) adopted by the International Accounting Standards Board (IASB). In the presentation of its financial results the Group uses a non-GAAP financial measure which is not prepared in accordance with IFRS being:

- Operating EBITDA: calculated by adding back (or deducting) finance expense / (income), income tax expense/(benefit), depreciation, amortisation, litigation settlement expenses, acquisition related expenses, transaction integration services, agricultural area trialling expenses, inventory impairments, losses from discontinued operations, gains/losses on disposal of non-core plant and equipment, and deducting other income and depreciation expense from discontinued operations, to net profit / (loss) after tax.

The Group uses this measure internally and believes that this non-GAAP financial measure provides useful information to readers to assist in the understanding of the Group's financial performance, financial position and returns, as it is the predominant measure of financial performance used by management. It represents the best measure of performance as a result of initiatives and activities directly controlled by management. Non-GAAP financial measures should not be viewed in isolation, nor considered as a substitute for measures reported in accordance with IFRS. Non-GAAP financial measures may not be comparable to similarly titled amounts reported by other companies.

**Review of operations (continued)**

The table below reconciles the Operating EBITDA to Statutory EBITDA and Loss After Tax:

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| **Statutory (Loss) after income tax** | **(7,639,443)** | (5,788,409) |
| Less: Profit from discontinued operation | **-** | (1,119,003) |
| Add/(Less): Income tax expense/(benefit) | **(138,193)** | 134,893 |
| Add: Net finance expenses | **3,089,078** | 1,653,331 |
| **Statutory Earnings Before Interest and Tax (EBIT)** | **(4,688,558)** | (5,119,188) |
| Add: Depreciation and amortisation expense | **2,513,886** | 2,551,295 |
| **Statutory Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA)** | **(2,174,672)** | (2,567,893) |
| Add: | | |
| Acquisition related expenses - legal and other expenses | **122,001** | 295,851 |
| (Gain)/loss on disposal of property, plant and equipment | **(14,400)** | 232,775 |
| Litigation settlement expenses | **1,913,409** | - |
| Deduct: | | |
| Other income | **(158,089)** | (392,383) |
| **Operating EBITDA** | **(311,751)** | (2,431,650) |

*Summary of key business risks*

The business, assets and operations of the Group are subject to certain risk factors that have the potential to influence the Group's operating and financial performance in the future. The Directors aim to manage these risks by carefully planning the Group's activities and implementing mitigating risk control measures. Specific risks to which the Group is exposed to include:

- failure to obtain or renew all necessary licences and permits across all jurisdictions in which the Group operates;
- inability to source sufficient raw material, including as a result of climate-induced variations such as extreme adverse weather events or plant diseases;
- changes in international, national or state laws, regulations or conventions relating to the growing, manufacture, export or sale of NRM;
- loss of key staff and inability to replace them with appropriately qualified personnel;
- claims arising from the consequences of inappropriate use or excessive exposure to NRM;
- diversion or illicit use of NRM during manufacture, storage or freight;
- introduction or growth of competing pain relief products, including non-narcotic opiate products;
- increasing poppy prices, including due to the reduction or withdrawal of government subsidies;
- failure to maintain its trade secrets, including in relation to its water based, solvent free extraction process;
- changes to scheduling or availability of pain relief medication or restrictions on import quotas for NRM;
- fluctuations in foreign exchange rates against the Group's functional currency (Australian dollars);
- changes in the supply of, and/or demand for, poppy seed and changes in pricing of poppy seed;
- changes to the cost of purifying poppy seed;
- customer and supplier performance risks;
- failure to comply with applicable standards and the risk of product recalls; and
- restrictions on sales in some countries of API's which have not been manufactured in that country or region.

**Significant changes in the state of affairs**

Contributed equity increased by $29,514,931 (from $181,482,260 to $210,997,191) as a result of a placement and entitlement offer completed in November 2019. Details of the changes in contributed equity are disclosed in note 23 of the financial statements. The net cash received from the increase in contributed equity was used to repay borrowings and to meet the Group's near term NRM and API growth capital expenditure needs.

There have been no other significant changes in the state of affairs of the Group during the year.

**Events since the end of the financial year**

On 10 February 2020 the Group announced that it had entered into an option agreement to acquire the shares of its largest customer in the United Kingdom, a manufacturer of codeine phosphate finished dosage products. Simultaneously, the Group also acquired four Market Authorisations from the customer for supply of codeine phosphate based products into the United Kingdom, and on 18 February 2020 the Group acquired a further two codeine phosphate based Market Authorisations from the same customer.

No other matter or circumstance has arisen since 31 December 2019 that has significantly affected the Group's operations, results or state of affairs, or may do so in future years.

**Likely developments and expected results of operations**

Information about likely developments in the operations of the Group and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Group.

**Dividends**

No dividends have been paid during the financial year. The directors do not recommend that a dividend be paid in respect of the financial year (2018: $nil).

**Environmental regulation**

The Group’s operations are not subject to any particular or significant environmental regulation under a law of the Commonwealth of Australia or of a State or Territory.

**Indemnification and insurance of officers and auditors**

During the financial year, the Company paid a premium in respect of a contract insuring the Directors and Company Secretary (as named above), and all executive officers of the Group against a liability incurred when acting in their capacity as a Director, Company Secretary or executive officer to the extent permitted by the *Corporations Act 2001.* Further disclosure required under section 300(9) of the *Corporations Act 2001* is prohibited under the terms of the insurance contract.

Other than to the extent permitted by law, the Company has not otherwise, during or since the end of the financial year, indemnified or agreed to indemnify an officer or auditor of the Company or any other related body corporate against a liability incurred as such by an officer or auditor.

**Meetings of directors**

The numbers of meetings of the Company's board of directors and of each board committee held during the year ended 31 December 2019, and the numbers of meetings attended by each director were:

| | Board of Directors | | Human Capital Committee | | Audit & Risk Committee | |
|---|---|---|---|---|---|---|
| | **Held and Eligible to Attend** | **Attended** | **Held and Eligible to Attend** | **Attended** | **Held and Eligible to Attend** | **Attended** |
| Mr. Simon Moore (Independent Non-Executive Chairman) | 20# | 20 | 2 | 2 | 3* | 3* |
| Mr. Jarrod Ritchie (Managing Director and CEO) | 20# | 19 | - | - | 3* | 3* |
| Mr. Todd Barlow (Non-Executive Director) | 19 | 19 | 2 | 2 | 3 | 2 |
| Mr. Stuart Black (Independent Non-Executive Director) | 20# | 19 | 2 | 2 | 3 | 3 |
| Ms. Sue MacLeman (Independent Non-Executive Director) | 19 | 18 | 2 | 2 | 3 | 3 |

* Attended by invitation
\# Includes special purpose board sub-committee meetings

**Proceedings on behalf of the Company**

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Company, or to intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Company with leave of the Court under section 237 of the *Corporations Act 2001.*

**Information on directors**

The following information is current as at the date of this report.

**Mr. Simon Moore, B.Com/LLB (Hons), Independent Non-Executive Chairman**

***Qualifications and Experience***

Simon Moore is currently Deputy Chairman of ASX Listed AMA Group Limited.

Simon is a Senior Partner of Colinton Capital Partners, a mid-market Australasian private equity investment manager. He was formerly a Managing Director and Partner of global alternative asset manager, The Carlyle Group. Prior to joining Carlyle, Simon was a Managing Director and Investment Committee Member of Investcorp International, Inc. based in New York. Prior to that he worked in private equity investments and investment banking at J.P. Morgan & Co. in New York, Hong Kong and Melbourne. Simon's personal investments include significant pastoral holdings and investments in a number of agricultural enterprises.

Former listed company directorships within past three years:
• Non-Executive Director of Megaport Limited (appointed 2015, resigned 2019)
• Non-Executive Director of First Wave Cloud Technology Limited (appointed 2017, resigned 2019)

Director of Palla Pharma Limited since 1 June 2016 and Chairman since 1 May 2018. Simon is a member of the Human Capital Committee.

**Mr. Jarrod Ritchie, BSc (Hons), Managing Director and Chief Executive Officer**

***Qualifications and Experience***

Jarrod Ritchie has over 20 years' experience in the opiates industry. He has led Palla Pharma Limited from its inception as a start-up to its current position as Australia's third licensed poppy processor with a strong international reputation.

Jarrod has led new research in the opiates industry including Palla Pharma Limited's unique, environmentally-sustainable, solvent-free manufacturing process. He has also led the successful trialling of a new thebaine-rich variety of poppy; the introduction of commercial crops to Victoria and New South Wales; the trialling of poppy crops in the Northern Territory; and the expansion of Palla Pharma Limited's global operations.

Director of Palla Pharma Limited since 5 February 2004.

**Mr. Todd Barlow, B.Bus/LLB (Hons), Non-Executive Director**

***Qualifications and Experience***

Todd Barlow is the Managing Director and CEO of Washington H. Soul Pattinson and Company Limited and a Non-Executive Director of New Hope Corporation Limited. Before joining Washington H. Soul Pattinson and Company Limited, he was Managing Director of Pitt Capital Partners Limited, a Sydney based corporate advisory firm. He continues to serve as a Non-Executive Director of Pitt Capital Partners Limited as well as a number of unlisted entities.

Between 2005 and 2008 Todd was based in Hong Kong, and provided advice on cross-border transactions between Asia and Australia. He previously practiced as a lawyer, specialising in corporate law and mergers and acquisitions.

Former listed company directorships within past three years:
• Non-Executive Director of PM Capital Asian Opportunities Fund Limited (appointed 2014, resigned 2017)

Director of Palla Pharma Limited since 18 June 2015. Todd is a member of the Human Capital Committee and the Audit & Risk Committee.

**Information on directors (continued)**

**Mr. Stuart Black AM, FCA, FAICD, BA (Accounting), Independent Non-Executive Director**

***Qualifications and Experience***

Stuart Black is a Chartered Accountant with extensive experience in agribusiness. He retired in 2013 as managing partner of a practice specialising in agribusiness. Stuart is a current Non-Executive Director of ASX listed Australian Agricultural Company Limited, and a Past President of the Institute of Chartered Accountants of Australia. He was the inaugural Chair and a past board member of the Accounting Professional and Ethical Standards Board and served as the Australian representative on the International Federation of Accountants SMP Committee. Stuart is Chair of the Chartered Accountants Benevolent Fund Limited and a former Director of the Country Education Foundation of Australia Limited.

In 2012 Stuart was appointed a Member of the Order of Australia for services to the profession of accounting, to ethical standards, as a contributor to professional organisations and to the community.

Former listed company directorships within past three years:
• Non-Executive Director of NetComm Wireless Limited (appointed 2013, resigned 2019)

Director of Palla Pharma Limited since 7 June 2016. Stuart is Chair of the Audit & Risk Committee, and a member of the Human Capital Committee.

**Ms. Sue MacLeman, BPharm, LLM, MMkt, FAICD, FATSE, FACPP, Independent Non-Executive Director**

***Qualifications and Experience***

Sue MacLeman has more than 30 years' experience as a pharmaceutical, biotechnology and medical technology executive having held senior roles in corporate, medical, commercial and business development. Sue has also served as CEO and Board member of several ASX and NASDAQ listed companies in the pharmaceutical sector and is currently Chair of Anatara Lifesciences Limited, Chair of Tali Digital Limited, Chair and Non-Executive Director of MTPConnect, Non-Executive Director of Oventus Medical Limited and Non-Executive Director of veski.

Former listed company directorships within past three years:
• Non-Executive Director of RHS Limited (appointed 2014, resigned 2018)

Director of Palla Pharma Limited since 27 November 2018. Sue is Chair of the Human Capital Committee and a member of the Audit & Risk Committee.

**Information on secretary**

The following information is current as at the date of this report.

**Mr. Jaime Pinto, BComm, CA, Company Secretary**

***Qualifications and Experience***

Mr. Pinto is a Chartered Accountant with extensive experience in both professional practice and in senior commercial roles across a broad range of industries. Jaime is currently Company Secretary of Quickstep Holdings Limited, BKI Investment Company Limited, and is Company Secretary and CFO of a number of unlisted investment and industrial companies.

Company Secretary of Palla Pharma Limited since 28 October 2016.

**Remuneration report - Audited**

The directors present the Palla Pharma Limited 2019 remuneration report, outlining key aspects of our remuneration policy and framework, and remuneration awarded this year.

The report is structured as follows:

(a) Key management personnel (KMP) disclosed in this report
(b) Remuneration governance
(c) Principals used to determine the nature and amount of remuneration
(d) Details of remuneration
(e) Service agreements
(f) Equity instruments granted
(g) Movement in shares held
(h) Loans given to key management personnel
(i) Other transactions with key management personnel

*(a) Key management personnel disclosed in this report*

**Non-executive and executive directors**

(i) Non-Executive Chairman

Mr. Simon Moore

(ii) Managing Director and Chief Executive Officer

Mr. Jarrod Ritchie

(iii) Non-Executive Directors

Mr. Todd Barlow
Mr. Stuart Black
Ms. Sue MacLeman

**Other key management personnel**

(i) Chief Financial Officer

Mr. Brendan Middleton

*(b) Remuneration governance*

The Board is responsible for determining and reviewing compensation arrangements for the Non-Executive Directors, the Non-Executive Chairman and the Executive Management team. The Board has established a Human Capital Committee, which is currently comprised of three Non-Executive Directors and the Chair. This Committee is primarily responsible for making recommendations to the board on:

- the over-arching executive remuneration framework;
- the operation of incentive plans, including key performance indicators and performance hurdles;
- remuneration levels of executive directors and other key management personnel; and
- non-executive director fees.

The objective of the Committee is to ensure that remuneration policies and structures are fair and competitive and aligned with the long-term interests of the Company. The Corporate Governance Statement provides further information on the role of this committee.

**Remuneration report - Audited (continued)**

*(c) Principles used to determine the nature and amount of remuneration*

The Company's goal is to engage and promote excellence at Board level, in staff members and partner organisations. The Company looks to engage the services of individuals and organisations with the experience necessary to assist the Company in meeting its strategic objectives.

The Board seeks to ensure that executive reward complies with good reward governance practices:

- Competitiveness and reasonableness;
- Acceptability to shareholders;
- Performance linkage;
- Transparency; and
- Capital management.

The Company has an executive remuneration framework that is market competitive and complementary to the reward strategy of the organisation. The Company's remuneration framework seeks alignment with shareholders' interests and is aligned to the rapid commercialisation of the Company's intellectual property and in achieving its milestones in a highly ethical and professional manner. The executive remuneration framework provides a mix of fixed and variable pay and performance incentive rewards, including a Short Term Incentive (STI) and Long Term Incentive (LTI) scheme.

The STI scheme is designed to focus the organisation on key shorter-term objectives that drive long-term shareholder value, and the Board sets annual key performance indicators (KPIs) for the CEO and executives which also serve as the Company's objectives.

The LTI scheme assists in the motivation, retention and reward of executives and employees and aligns the interests of employees with the interests of shareholders. Full time or part time employees, and Executive Directors of PAL or any of its subsidiaries will be eligible to participate in the LTI scheme. The Executive Directors of PAL will require approval from PAL's shareholders prior to being permitted to participate in the LTI scheme. There is no intention of Non-Executive Directors participating at this time.

**Non-Executive Directors' fees**

Non-Executive Directors' fees are determined by reference to industry standards, and were last reviewed effective 21 July 2015. Directors' fees are paid in cash. A Non-Executive Directors' Fee Pool of $700,000 has been approved by shareholders.

Directors' fees are currently set at $120,000 for the Non-Executive Chairman and $70,000 per Non-Executive Director plus statutory superannuation, with an additional $10,000 plus statutory superannuation for the Chairman of the Audit & Risk Committee. These fees reflect the demands which are made on and the responsibilities of the Directors.

**Executive pay**

The executive pay and reward framework has three components:

- Base pay and benefits;
- Short term performance incentives; and
- Long term incentives.

The combination of these comprises the executive's total remuneration.

**Remuneration report - Audited (continued)**

*(c) Principles used to determine the nature and amount of remuneration (continued)*

(i) Base pay and benefits

A total employment cost package may include a combination of cash and prescribed non-financial benefits at the executive's discretion.

Executives are offered a competitive base pay that comprises the fixed component of pay and rewards. The base pay for executives is reviewed annually to ensure the executive's pay is competitive with the market. An executive's pay is also reviewed on promotion.

There are no ongoing guaranteed base pay increases included in any executive contracts.

(ii) Short term incentives (STI's)

STI's payable to executives are based upon the attainment of agreed corporate and individual milestones and are reviewed and approved by the Board of Directors. STI's are payable in cash.

(iii) Long term incentives (LTI's)

At the discretion of the Board of Directors, executives are issued with Share Appreciation Rights under the Company's Share Appreciation Rights Plan as LTI's in a manner that aligns this element of remuneration with the creation of shareholder wealth. Each Share Appreciation Right is an equity security that confers on the participant a right to be issued a specified number of the Group's shares, calculated by reference to the increase in market price of the Company's shares over a three-year period, but subject to satisfaction of the vesting condition that the participant must be an employee of the Company on the third anniversary of the grant date. Share Appreciation Rights are granted under the plan for no consideration and carry no dividend or voting rights. Share Appreciation Rights grants are made to executives who are able to influence the generation of shareholder wealth and thus have a direct impact on the creation of shareholder wealth.

(iv) Relationship between remuneration policy and company performance

LTI's and STI's may be issued to new and existing employees, subject to performance review and based on performance of the individual and/or the Company in absolute terms. The STI component of remuneration provides a short term monetary reward for past performance and the equity component of the LTI aligns employees future remuneration potential to growth in shareholder value in the future.

The Company's remuneration policy seeks to reward staff members for their contribution to achieving significant operational, strategic, financial and regulatory milestones. Achievement of milestones selected will build sustainable and long term shareholder value.

*Statutory performance indicators*

The Company aims to align executive remuneration to strategic and business objectives and the creation of shareholder wealth. The table following shows measures of the Company's financial performance over the last five years as required by the Corporations Act 2001. However, these measures are not necessarily consistent with the measures used in determining the variable amounts of remuneration to be awarded to executives and consequently, there may not always be a direct correlation between the statutory key performance measures and the variable remuneration awarded.

**Remuneration report - Audited (continued)**

*(c) Principles used to determine the nature and amount of remuneration (continued)*

| | 2019 | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|---|
| Revenue | 54,843,483 | 46,563,381 | 22,263,174 | 10,556,449 | 3,679,063 |
| Net profit/(loss) after tax | (7,639,443) | (5,788,409) | (16,692,689) | (14,020,835) | (25,899,838) |
| Closing share price | $1.06 | $1.15 | $2.20 | $2.91 | $3.90 |
| Price increase/(decrease) $ | ($0.09) | ($1.05) | ($0.71) | ($0.99) | N/A |
| Price increase/(decrease) % | (7.8%) | (47.7%) | (24.4%) | (25.4%) | N/A |
| Earnings per share (cents) | (8.66) | (8.52) | (23.38) | (26.96) | (52.07) |

*(d) Details of remuneration*

The following table shows details of the remuneration expense recognised for the Group's executive key management personnel for the current and previous financial year measured in accordance with the requirements of the accounting standards.

| 2019 | Short-term employee benefits | | | Post-employment benefits | | Equity-based payments | | |
|---|---|---|---|---|---|---|---|---|
| Name | Cash salary and fees<br>$ | STI<br>$ | Non-monetary benefits<br>$ | Super-annuation<br>$ | Other long term benefits<br>$ | Share Appreciation Rights<br>$ | Total<br>$ | Proportion of remuneration performance related<br>% |
| Non-executive directors | | | | | | | | |
| Todd Barlow | 70,000 | - | - | 6,650 | - | - | 76,650 | - |
| Simon Moore | 120,000 | - | - | 11,400 | - | - | 131,400 | - |
| Stuart Black | 80,000 | - | - | 7,600 | - | - | 87,600 | - |
| Sue MacLeman | 70,000 | - | - | 6,650 | - | - | 76,650 | - |
| **Sub-total non-executive directors** | **340,000** | **-** | **-** | **32,300** | **-** | **-** | **372,300** | **-** |
| Executive directors | | | | | | | | |
| Jarrod Ritchie | 775,000 | 2,996 | 31,097 | 26,127 | 12,466 | 121,997 | 969,683 | 0.3 |
| **Sub-total executive directors** | **775,000** | **2,996** | **31,097** | **26,127** | **12,466** | **121,997** | **969,683** | **0.3** |
| Other key management personnel | | | | | | | | |
| Brendan Middleton | 275,000 | 25,958 | - | 26,118 | 10,329 | 45,984 | 383,389 | 6.9 |
| **Sub-total other key management personnel** | **275,000** | **25,958** | **-** | **26,118** | **10,329** | **45,984** | **383,389** | **6.9** |
| **Total key management personnel compensation** | **1,390,000** | **28,954** | **31,097** | **84,545** | **22,795** | **167,981** | **1,725,372** | **1.7** |

**Remuneration report - Audited (continued)**

*(d) Details of remuneration (continued)*

| **2018** | Short-term employee benefits | | | Post-employment benefits | | Equity-based payments | | |
|---|---|---|---|---|---|---|---|---|
| Name | Cash salary and fees $ | STI $ | Non-monetary benefits $ | Super-annuation $ | Other long term benefits $ | Share Appreciation Rights $ | Total $ | Proportion of remuneration performance related % |
| Non-executive directors | | | | | | | | |
| Peter Robinson * | 43,231 | - | - | 4,107 | - | - | 47,338 | - |
| Todd Barlow | 70,000 | - | - | 6,650 | - | - | 76,650 | - |
| Simon Moore | 101,410 | - | - | 9,634 | - | - | 111,044 | - |
| Stuart Black | 80,000 | - | - | 7,600 | - | - | 87,600 | - |
| Sue MacLeman ** | 4,846 | - | - | 460 | - | - | 5,306 | - |
| **Sub-total non-executive directors** | **299,487** | **-** | **-** | **28,451** | **-** | **-** | **327,938** | **-** |
| Executive directors | | | | | | | | |
| Jarrod Ritchie | 775,417 | - | - | 24,583 | 11,142 | 93,333 | 904,475 | - |
| **Sub-total executive directors** | **775,417** | **-** | **-** | **24,583** | **11,142** | **93,333** | **904,475** | **-** |
| Other key management personnel | | | | | | | | |
| Brendan Middleton | 275,000 | - | - | 25,000 | 14,122 | 35,158 | 349,280 | - |
| **Sub-total other key management personnel** | **275,000** | **-** | **-** | **25,000** | **14,122** | **35,158** | **349,280** | **-** |
| **Total key management personnel compensation** | **1,349,904** | **-** | **-** | **78,034** | **25,264** | **128,491** | **1,581,693** | **-** |

* Non-Executive Director until 1 May 2018
** Non-Executive Director from 27 November 2018

*(e) Service agreements*

Remuneration and other terms of employment for the Non-Executive Chairman, Managing Director and Chief Executive Officer, Non-Executive Directors and other key management personnel are formalised in service agreements. The agreements, other than for Non-Executive Directors, may provide for the provision of performance related cash bonuses and the award of equity in the Company.

Other major provisions of the agreements relating to remuneration are set out below:

*Simon Moore, Independent Non-Executive Chairman*
• Term of Agreement - Commencing from 1 May 2018
• Director’s fee - $120,000 plus statutory superannuation per annum to be reviewed independently and annually by the Board of Directors
• Termination - No terms have been agreed
• Bonus - Nil
• Equity - Nil

**Remuneration report - Audited (continued)**

*(e) Service agreements (continued)*

*Jarrod Ritchie, Managing Director and Chief Executive Officer*
• Term of Agreement - Commencing from 21 July 2015 and ongoing unless terminated in accordance with its terms
• Base Remuneration - $800,000 inclusive of statutory superannuation per annum, subject to increases at the discretion of the Board of Directors
• Termination - By twelve months' notice from either side
• Bonus - At the discretion of the Board of Directors
• Equity - The Director shall be entitled to participate in the LTI scheme of the Company

*Todd Barlow, Non-Executive Director*
• Term of Agreement - Commencing from 18 June 2015
• Director's Fees - $70,000 plus statutory superannuation per annum to be reviewed independently and annually by the Board of Directors
• Termination - No terms have been agreed
• Bonus - Nil
• Equity - Nil

*Stuart Black, Independent Non-Executive Director*
• Term of Agreement - Commencing from 7 June 2016
• Director's Fees - $80,000 plus statutory superannuation per annum to be reviewed independently and annually by the Board of Directors
• Termination - No terms have been agreed
• Bonus - Nil
• Equity - Nil

*Sue MacLeman, Independent Non-Executive Director*
• Term of Agreement - Commencing from 27 November 2018
• Director's Fees - $70,000 plus statutory superannuation per annum to be reviewed independently and annually by the Board of Directors
• Termination - No terms have been agreed
• Bonus - Nil
• Equity - Nil

*Brendan Middleton, Chief Financial Officer*
• Term of Agreement - Commencing from 5 June 2017
• Base Remuneration - $300,000 inclusive of statutory superannuation per annum, subject to increases at the discretion of the Board of Directors
• Termination - By three months' notice from either side
• Bonus - At the discretion of the Board of Directors
• Equity - The Executive shall be entitled to participate in the LTI scheme of the Company

**Remuneration report - Audited (continued)**

*(f) Equity instruments granted*

Details of equity instruments granted as remuneration to each KMP is set out below.

| | Number of equity instruments issued | Grant Opening Price | Fair value of equity instruments per share | Total value of equity instruments issued | Start of performance period | End of performance period | Included in 2019 remuneration |
|---|---|---|---|---|---|---|---|
| *Jarrod Ritchie, Managing Director and Chief Executive Officer* | | | | | | | |
| 2019 Share Appreciation Rights - Tranche 1 | 451,613 | $1.05 | $0.250 | $112,903 | 28 March 2019 | 28 March 2022 | 28,664 |
| 2019 Share Appreciation Rights - Tranche 2 | 668,387 | $4.75 | $0.001 | $668 | 28 March 2019 | 28 March 2022 | - |
| 2017 Share Appreciation Rights | 451,613 | $2.62 | $0.620 | $280,000 | 27 March 2017 | 27 March 2020 | 93,333 |
| *Brendan Middleton, Chief Financial Officer* | | | | | | | |
| 2019 Share Appreciation Rights - Tranche 1 | 120,968 | $1.05 | $0.250 | $30,242 | 28 March 2019 | 28 March 2022 | 7,678 |
| 2019 Share Appreciation Rights - Tranche 2 | 179,032 | $4.75 | $0.001 | $179 | 28 March 2019 | 28 March 2022 | - |
| 2018 Share Appreciation Rights | 120,968 | $1.39 | $0.330 | $39,919 | 28 March 2018 | 28 March 2021 | 13,306 |
| 2017 Share Appreciation Rights | 120,968 | $2.62 | $0.620 | $75,000 | 5 June 2017 | 27 March 2020 | 25,000 |

Total share appreciation rights issued are disclosed in note 31.

**Remuneration report - Audited (continued)**

*(g) Movement in shares held*

The movement during the year in the number of ordinary shares of the Company, held directly, indirectly or beneficially, by each KMP is as follows:

| Name | Held at 1 January 2019 | Purchased | Sold | Other changes during the year | Held at 31 December 2019 |
|---|---|---|---|---|---|
| *Non-executive directors* | | | | | |
| Todd Barlow | - | - | - | - | - |
| Simon Moore | 2,154,067 | 871,884 | - | - | 3,025,951 |
| Stuart Black | 15,000 | 8,772 | - | - | 23,772 |
| Sue MacLeman | - | - | - | - | - |
| *Executive directors* | | | | | |
| Jarrod Ritchie | 1,533,805 | 603,981 | - | - | 2,137,786 |
| *Other key management personnel* | | | | | |
| Brendan Middleton | - | - | - | - | - |

*(h) Loans given to key management personnel*

Details of loans made to directors of Palla Pharma Limited and other key management personnel of the Group, including their close family members and entities related to them, are set out below.

**Consolidated entity**

| Name | Balance at the start of the year | Interest paid and payable for the year | Interest not charged | Balance at the end of the year | Highest indebtedness during the year |
|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ |
| Jarrod Ritchie | - | 2,490 | - | 425,277 | 425,277 |

Loans to key management personnel outstanding at the end of the current year include a secured loan to a director of Palla Pharma Limited of $422,787 which was made for a period of 25 years and is repayable on a quarterly amortising reducing balance basis, maturing on 31 December 2044. Interest is payable on this loan at a rate of 5% per annum, payable quarterly. This loan enabled the director to fully participate in the pro-rata Entitlement Offer completed by the Group in November 2019 and is secured against the new shares subscribed to under the offer.

The amounts shown for interest not charged in the table above represents the difference between the amount paid and payable for the year and the amount of interest that would have been charged on an arm's-length basis.

No write-downs or allowances for doubtful receivables have been recognised in relation to any loans made to key management personnel.

**Remuneration report - Audited (continued)**

*(i) Other transactions with key management personnel*

A number of key management personnel (KMP), or their related parties, hold positions in other entities that result in them having control, or joint control, over the financial or operating policies of those entities.

During 2019 company secretarial services and financial reporting services amounting to $4,500 (2018: $9,096) were provided by Corporate and Administrative Services Pty Ltd, a subsidiary of Washington H. Soul Pattinson and Company Limited. Interest and finance expenses during the year attributable to Washington H. Soul Pattinson and Company Limited amounted to $2,741,896 (2018: $917,174).

**End of the Remuneration Report (Audited)**

**Non-audit services**

During the year KPMG, the Group's auditor, has performed certain other services in addition to the audit and review of the financial statements.

The board has considered the non-audit services provided during the year by the auditor and in accordance with written advice provided by resolution of the audit committee, is satisfied that the provision of those non-audit services during the year by the auditor is compatible with, and did not compromise, the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services were subject to the corporate governance procedures adopted by the Group and have been reviewed by the audit committee to ensure they do not impact the integrity and objectivity of the auditor; and
- the non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision-making capacity for the Group, acting as an advocate for the Group or jointly sharing risks and rewards.

Details of the amounts paid to the auditor of the Group, KPMG, and its network firms for audit and non-audit services provided during the year are set out below:

| | **Consolidated entity** | |
|---|---|---|
| | **2019** | 2018 |
| | **$** | $ |
| *(i) Audit and review services* | | |
| Audit and review of financial statements - Group | **167,214** | 173,756 |
| Audit and review of financial statements - controlled entities | **12,156** | 14,127 |
| Total remuneration for audit and review services | **179,370** | 187,883 |
| *(ii) Assurance services* | | |
| Due diligence services | **28,463** | - |
| Total remuneration for assurance services * | **28,463** | - |
| *(iii) Other services* | | |
| Taxation advice and tax compliance services | **12,156** | 12,156 |
| Technical assistance for subsidiary financial statements | **4,052** | 5,673 |
| Total remuneration for other services | **16,208** | 17,829 |
| Total remuneration of KPMG | **224,041** | 205,712 |

* There were no regulatory assurance services provided during the year.

No officers were previously partners of the audit firm KPMG.

The comparatives include amounts billed in the current period relating to the prior year.

**Auditor's independence declaration**

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 21.

**Auditor**

KPMG continues in office in accordance with section 327 of the *Corporations Act 2001*.

This report is made in accordance with a resolution of directors.

Simon Moore

Mr. Simon Moore
Director

Melbourne
27 February 2020

# Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

## To the Directors of Palla Pharma Limited

I declare that, to the best of my knowledge and belief, in relation to the audit of Palla Pharma Limited for the financial year ended 31 December 2019 there have been:

i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and

ii. no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

KPMG

Tony Batsakis
*Partner*
Melbourne

27 February 2020

## Corporate governance statement

The Board of Directors of Palla Pharma Limited (Board) is responsible for the corporate governance of the Company. The Board guides and monitors the business and affairs of the Company on behalf of the shareholders by whom they are elected and to whom they are accountable.

The Board supports the core corporate governance principles published by the ASX Corporate Governance Council (Council). The Company’s corporate governance framework is designed to comply with the Council's principles whilst being relevant, efficient and cost effective for the current stage of the Company’s development.

The Corporate Governance Statement contains certain specific information and discloses the extent to which the Company has followed the Council’s principles during the 2019 financial year.

The Company's Corporate Governance Statement and Appendix 4G is structured with reference to the ASX Corporate Governance Principles and Recommendations and can be found on the "Corporate Governance" section of the Company's website at: http://pallapharma.com/investors.

The Board will continue its ongoing review process to ensure that the model is relevant, efficient and cost effective to the Company and its shareholders.

# Palla Pharma Limited ACN 107 872 453
# Financial statements - 31 December 2019

## Contents



These financial statements are the consolidated financial statements of the consolidated entity consisting of Palla Pharma Limited and its subsidiaries. A list of subsidiaries is included in note 27. These financial statements are presented in Australian dollars ($), which is the Group's functional currency.

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

Palla Pharma Limited
c/- Link Market Services Limited
Tower 4
727 Collins Street
Docklands VIC 3008

A description of the nature of the consolidated entity's operations and its principal activities is included in the directors' report on page 2, which is not part of these financial statements.

The financial statements were authorised for issue by the directors on 27 February 2020. The directors have the power to amend and reissue the financial statements.

| | Notes | Consolidated entity 31 December 2019 $ | 31 December 2018 $ |
|---|---|---|---|
| **Revenue** | | | |
| Sales from contracts with customers | | **54,685,394** | 46,170,998 |
| Other income | | **158,089** | 392,383 |
| | 6 | **54,843,483** | 46,563,381 |
| **Expenses** | | | |
| Raw materials, consumables and other production expenses | | **(29,169,271)** | (24,213,450) |
| Employee benefits (production) expenses | 7 | **(8,214,073)** | (6,909,702) |
| Employee benefits (non-production) expenses | 7 | **(11,076,501)** | (11,610,865) |
| Legal and listing compliance expenses | | **(874,225)** | (703,312) |
| Market development expenses | | **(1,033,829)** | (1,018,036) |
| Occupancy expenses | | **(1,585,590)** | (1,520,126) |
| Contract research expenses | | **(129,555)** | (268,863) |
| Acquisition related expenses - legal and other expenses | | **(122,001)** | (295,851) |
| Profit/(loss) on disposal of property, plant and equipment | | **14,400** | (232,775) |
| Litigation settlement expenses | | **(1,913,409)** | - |
| Consulting expenses | | **(487,120)** | (287,271) |
| Outsourced quality consulting expenses | | **(461,740)** | (62,136) |
| Other expenses | | **(1,965,241)** | (2,008,887) |
| **Total expenses** | | **(57,018,155)** | (49,131,274) |
| **Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA)** | | **(2,174,672)** | (2,567,893) |
| Depreciation and amortisation expense | 7 | **(2,513,886)** | (2,551,295) |
| **Earnings Before Interest and Tax (EBIT)** | | **(4,688,558)** | (5,119,188) |
| Finance income | | **23,028** | 21,418 |
| Finance expenses | | **(3,112,106)** | (1,674,749) |
| **Net finance expenses** | 7 | **(3,089,078)** | (1,653,331) |
| **(Loss) before income tax** | | **(7,777,636)** | (6,772,519) |
| Income tax benefit/(expense) | 8 | **138,193** | (134,893) |
| **(Loss) from continuing operations** | | **(7,639,443)** | (6,907,412) |
| Profit from discontinued operation, net of tax | | **-** | 1,119,003 |
| **(Loss) for the year** | | **(7,639,443)** | (5,788,409) |
| **Other comprehensive income/(loss)** | | | |
| *Item that may be reclassified to profit or loss* | | | |
| Exchange differences on translation of foreign operations | | **(111,877)** | 1,179,901 |
| **Total comprehensive (loss) for the year** | | **(7,751,320)** | (4,608,508) |

*The above consolidated statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.*

| | Notes | **Consolidated entity** **31 December 2019 $** | 31 December 2018 $ |
|---|---|---|---|
| (Loss) is attributable to: | | | |
| Owners of Palla Pharma Limited | | **(7,639,443)** | (5,788,409) |
| Total comprehensive (loss) for the year is attributable to: | | | |
| Owners of Palla Pharma Limited | | **(7,751,320)** | (4,608,508) |
| | | **Cents** | Cents |
| **Earnings per share for the (loss) from continuing operations attributable to the ordinary equity holders of the Company:** | | | |
| Basic (loss) per share | 30 | **(8.66)** | (8.52) |
| Diluted (loss) per share | 30 | **(8.66)** | (8.52) |
| **Earnings per share for the profit from discontinued operations attributable to the ordinary equity holders of the Company:** | | | |
| Basic profit per share | | **0.00** | 1.38 |
| Diluted profit per share | | **0.00** | 1.38 |

*The above consolidated statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.*

| | Notes | Consolidated entity<br>**31 December 2019 $** | <br>31 December 2018 $ |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 9 | **2,019,087** | 1,904,583 |
| Trade and other receivables | 10 | **11,507,068** | 11,932,039 |
| Inventories | 11 | **22,149,374** | 19,166,364 |
| Contract assets | 6 | **5,995,039** | 3,527,827 |
| Prepayments | | **1,481,425** | 2,723,041 |
| **Total current assets** | | **43,151,993** | 39,253,854 |
| | | | |
| **Non-current assets** | | | |
| Other receivables | 12 | **405,875** | - |
| Investments | 14 | **103,272** | 103,549 |
| Property, plant and equipment | 15 | **26,693,955** | 27,762,272 |
| Intangible assets | 16 | **16,967,608** | 14,816,227 |
| Inventories | 13 | **2,250,585** | 1,821,873 |
| **Total non-current assets** | | **46,421,295** | 44,503,921 |
| | | | |
| **Total assets** | | **89,573,288** | 83,757,775 |
| | | | |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 17 | **8,907,120** | 9,426,538 |
| Borrowings | 18 | **467,424** | 166,074 |
| Current tax liabilities | | **-** | 134,893 |
| Provisions | 19 | **1,847,235** | 1,710,002 |
| **Total current liabilities** | | **11,221,779** | 11,437,507 |
| | | | |
| **Non-current liabilities** | | | |
| Trade and other payables | 20 | **1,563,462** | - |
| Borrowings | 21 | **5,000,000** | 22,702,960 |
| Provisions | 22 | **378,044** | 314,549 |
| **Total non-current liabilities** | | **6,941,506** | 23,017,509 |
| | | | |
| **Total liabilities** | | **18,163,285** | 34,455,016 |
| | | | |
| **Net assets** | | **71,410,003** | 49,302,759 |
| | | | |
| **EQUITY** | | | |
| Share capital | 23 | **210,997,191** | 181,482,260 |
| Reserves | 24 | **3,595,223** | 3,363,467 |
| (Accumulated losses) | | **(143,182,411)** | (135,542,968) |
| | | | |
| **Total equity** | | **71,410,003** | 49,302,759 |

*The above consolidated statement of financial position should be read in conjunction with the accompanying notes.*

| | | Attributable to owners of Palla Pharma Limited | | | | |
|---|---|---|---|---|---|---|
| **Consolidated entity** | Notes | **Contributed equity $** | **Foreign currency translation reserve $** | **Other reserves $** | **(Accumulated losses) $** | **Total equity $** |
| **Balance at 1 January 2018** | | 181,482,260 | (264,593) | 2,120,662 | (129,754,559) | 53,583,770 |
| (Loss) for the year | | - | - | - | (5,788,409) | (5,788,409) |
| Other comprehensive income | | - | 1,179,901 | - | - | 1,179,901 |
| **Total comprehensive income/(loss) for the year** | | **-** | **1,179,901** | **-** | **(5,788,409)** | **(4,608,508)** |
| **Transactions with owners in their capacity as owners:** | | | | | | |
| Share-based payments | 31 | - | - | 327,497 | - | 327,497 |
| **Total transactions with owners in their capacity as owners** | | - | - | 327,497 | - | 327,497 |
| **Balance at 31 December 2018** | | **181,482,260** | **915,308** | **2,448,159** | **(135,542,968)** | **49,302,759** |
| **Balance at 1 January 2019** | | 181,482,260 | 915,308 | 2,448,159 | (135,542,968) | 49,302,759 |
| (Loss) for the year | | - | - | - | (7,639,443) | (7,639,443) |
| Other comprehensive (loss) | | - | (111,877) | - | - | (111,877) |
| **Total comprehensive income/(loss) for the year** | | **-** | **(111,877)** | **-** | **(7,639,443)** | **(7,751,320)** |
| **Transactions with owners in their capacity as owners:** | | | | | | |
| Contributions of equity, net of transaction costs and tax | 23 | 29,514,931 | - | - | - | 29,514,931 |
| Share-based payments | 31 | - | - | 343,633 | - | 343,633 |
| **Total transactions with owners in their capacity as owners** | | 29,514,931 | - | 343,633 | - | 29,858,564 |
| **Balance at 31 December 2019** | | **210,997,191** | **803,431** | **2,791,792** | **(143,182,411)** | **71,410,003** |

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

| | Notes | **Consolidated entity** **31 December 2019 $** | 31 December 2018 $ |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Receipts from customers (inclusive of VAT) | | **58,308,188** | 40,767,047 |
| Payments to suppliers and employees (inclusive of GST and VAT) | | **(64,688,378)** | (54,016,366) |
| | | **(6,380,190)** | (13,249,319) |
| Other cash receipts | | **-** | 256,945 |
| Interest received | | **23,028** | 21,418 |
| Interest and finance costs paid | | **(3,112,106)** | (1,674,749) |
| **Net cash (outflow) from operating activities** | 28 | **(9,469,268)** | (14,645,705) |
| | | | |
| **Cash flows from investing activities** | | | |
| Proceeds/(payments) for acquisition of subsidiary, net of cash acquired | | **-** | 761,935 |
| Payments for property, plant and equipment | 15 | **(1,879,368)** | (2,781,687) |
| Payments for capitalised development costs and patents | 16 | **(611,339)** | (454,541) |
| Proceeds from sale of non-current assets | | **14,400** | 979,799 |
| Proceeds from sale of held-for-sale assets | | **-** | 4,291,522 |
| **Net cash (outflow) inflow from investing activities** | | **(2,476,307)** | 2,797,028 |
| | | | |
| **Cash flows from financing activities** | | | |
| Proceeds from issues of shares | 23 | **30,980,882** | - |
| Share issuance transaction costs | 23 | **(1,888,738)** | - |
| Proceeds from borrowings | 21 | **9,147,040** | 25,669,130 |
| Repayment of borrowings | 21 | **(26,548,650)** | (16,026,934) |
| **Net cash inflow from financing activities** | | **11,690,534** | 9,642,196 |
| | | | |
| **Net (decrease) in cash and cash equivalents** | | **(255,041)** | (2,206,481) |
| Cash and cash equivalents at the beginning of the financial year | | **1,904,583** | 3,644,547 |
| Effects of exchange rate changes on the balance of assets held in foreign currencies | | **369,545** | 466,517 |
| Cash and cash equivalents at end of year | 9 | **2,019,087** | 1,904,583 |

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

## Contents of the notes to the consolidated financial statements

## 1 Reporting entity

Palla Pharma Limited (the 'Company') is domiciled in Australia. The Company's registered office is at c/- Link Market Services Limited, Tower 4, 727 Collins Street, Docklands VIC 3008. These consolidated financial statements comprise the Company and the entities it controlled at the end of or during the financial year (together referred to as the 'Group'). These financial statements were approved on 27 February 2020.

The Group is a for-profit entity and is primarily involved in the production and distribution of Narcotic Raw Material, Active Pharmaceutical Ingredients and Finished Dosage Formulations for supply to global pharmaceutical markets, and the production and distribution of poppy seed for supply to global culinary markets.

## 2 Summary of significant accounting policies

This note provides a list of significant accounting policies adopted in the preparation of these consolidated financial statements. These policies have been consistently applied to the years presented, unless otherwise stated. The financial statements are for the Group consisting of Palla Pharma Limited and its subsidiaries.

### (a) Basis of preparation

*(i) Compliance with IFRS*

The consolidated financial statements are general purpose financial statements which have been prepared in accordance with Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board (AASB) and the *Corporations Act 2001*. The consolidated financial statements comply with International Financial Reporting Standards (IFRSs) adopted by the International Accounting Standards Board (IASB).

*(ii) Historical cost convention*

The consolidated financial statements have been prepared on the historical cost basis unless stated otherwise.

*(iii) Changes in significant accounting policies*

This is the first set of the Group's financial statements where AASB16 *Leases* has been applied. There has been no material impact on the Group's financial statements on adoption of AASB16.

A number of other new standards are also effective from 1 January 2019 but they do not have a material effect on the Group's financial statements.

*(iv) New accounting standards for application in future periods*

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2019 reporting periods and have not been early adopted by the Group. These standards are not expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

## 2 Summary of significant accounting policies (continued)

### (b) Principles of consolidation

*Business combinations*

The Group accounts for business combinations using the acquisition method when control is transferred to the Group. The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase is recognised in profit or loss immediately. Transaction costs are expensed as incurred, except if related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, other contingent consideration is remeasured at fair value at each reporting date and subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

If share-based payment awards (replacement awards) are required to be exchanged for awards held by the acquiree's employees (acquiree's awards), then all or a portion of the amount of the acquirer's replacement awards is included in measuring the consideration transferred in the business combination. This determination is based on the market-based measure of the replacement awards compared with the market-based measure of the acquiree's awards and the extent to which the replacement awards relate to pre-combination service.

*Subsidiaries*

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Palla Pharma Limited as at 31 December 2019 and the results of all subsidiaries for the year then ended.

Subsidiaries are all those companies over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date control eases.

Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred. Accounting policies of subsidiaries are consistent with the policies adopted by the Group.

### (c) Segment reporting

Operating segments are presented using the 'management approach', where the information presented is on the same basis as the internal reports provided to the Chief Operating Decision Makers ('CODM'). The CODM is responsible for the allocation of resources to operating segments and assessing their performance.

## 2 Summary of significant accounting policies (continued)

### (d) Foreign currency translation

*(i) Functional and presentation currency*

These consolidated financial statements are presented in Australian dollars, which is the Group's functional currency.

*(ii) Transactions and balances*

Transactions in foreign currencies are translated to the functional currency of the Group at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the year.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured in terms of historical cost are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising on retranslation are recognised in the consolidated statement of profit or loss and other comprehensive income as either finance income or finance expenses see note 2(p).

*(iii) Foreign operations*

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into the functional currency at the exchange rates at the reporting date. The income and expenses of foreign operations are translated into the functional currency at the exchange rates at the dates of the transactions.

Foreign currency differences are recognised in the consolidated statement of profit or loss and other comprehensive income and accumulated in the translation reserve, except to the extent that the translation difference is allocated to non-controlling interests.

### (e) Going concern

The consolidated financial statements have been prepared on a going concern basis, which assumes that the Group will be able to continue trading, realise its assets and discharge its liabilities in the ordinary course of business for a period of at least 12 months from the date that these financial statements are approved.

The Directors note the following events and conditions which have been considered in assessing the appropriateness of the going concern assumption:

- For the year ended 31 December 2019 the Group generated a loss after income tax of $7,639,443 (2018: $5,788,409) and had cash outflows from operations of $10,010,864 (2018: $14,645,705).

- As at 31 December 2019 the Group's current assets exceeded its current liabilities by $31,930,214 (31 December 2018: $27,816,347), with cash and cash equivalents of $2,019,087 (31 December 2018: $1,904,583).

- The Group has a standby debt facility in place with Washington H. Soul Pattinson and Company Limited to meet the Group's short-term working capital requirements. As at the date of this report the facility has a limit of $16,000,000 and at 31 December 2019 the Group had drawn down $5,000,000 of the Facility. The remaining facility available for utilisation of $11,000,000 combined with cash and cash equivalents of $2,019,087 provides adequate funding to meet the Group's immediate needs.

## 2 Summary of significant accounting policies (continued)

### (e) Going concern (continued)

- The standby debt facility in place with Washington H. Soul Pattinson expires on 31 August 2021. The Directors acknowledge that prima facie a refinancing risk exists at 31 August 2021 if the facility is not renewed in line with past practice, repaid out of funds secured from an alternative source of debt or raised from the issue of additional equity.

- In November 2019 the Group raised $31.4m in new equity from a placement and entitlement offer. The Directors have confidence that the recent equity capital raised and availability of debt facilities can meet the Group's immediate funding needs.

- The Directors have confidence in the continuing support from existing shareholders and ability to attract new investors and debt providers to fund the Group's future financing requirements, if required, as demonstrated by previous capital and debt raisings.

- The Directors have confidence in the basis of preparation and achievability of the business plans, cash flow and profit and loss forecasts prepared by management which project positive EBITDA and positive operating cash flows.

After considering the above factors, the Directors have concluded that the use of the going concern basis of preparation is appropriate.

### (f) Financial instruments

*Non-derivative financial assets*

*Financial instruments*

The Group initially recognises trade receivables on the date that they are originated. All other financial assets (including assets designated at fair value through profit or loss) are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability. Financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

*Classification and subsequent measurement*

On initial recognition, a financial asset is classified as measured at: amortised cost; or FVTPL.

Financial assets are not reclassified subsequent to their initial recognition unless the Group changes its business model for managing financial assets, in which case all affected financial assets are reclassified on the first day of the first reporting period following the change in the business model.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

## 2 Summary of significant accounting policies (continued)

### (f) Financial instruments (continued)

*Financial assets at amortised cost*

These assets are subsequently measured at amortised cost using the effective interest method. The amortised cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognised in profit or loss (see note 2(j)). Any gain or loss on derecognition is recognised in profit or loss.

*Financial assets at fair value through profit or loss*

A financial asset is classified as at fair value through profit or loss if it is classified as held-for-trading or is designated as such on initial recognition. Directly attributable transaction costs are recognised in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value and changes therein, including any interest or dividend income, are recognised in profit or loss.

*Cash and cash equivalents*

Cash and cash equivalents comprise cash balances and call deposits with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments.

*Non-derivative financial liabilities*

The Group initially recognises debt securities issued and subordinated liabilities on the date that they are originated. All other financial liabilities (including liabilities designated at fair value through profit or loss) are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire. The Group also derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different, in which case a new financial liability based on the modified terms is recognised at fair value.

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortised cost using the effective interest rate method.

Other financial liabilities comprise loans and borrowings and trade and other payables.

*Share capital - Ordinary shares*

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

*Impact on the financial statements*

The Group has applied AASB 9 cumulatively, the comparative figures are therefore not restated. The effect of initially applying the standard is the reclassification of trade receivables from the category of 'loans and receivables' to 'Amortised cost'. The adoption of an Expected Credit Loss ('ECL') model did not result in any material adjustments.

## 2 Summary of significant accounting policies (continued)

### (g) Revenue recognition

*(i) Sale of goods*

Under AASB 15, revenue is recognised when a customer obtains control of the goods or services. Determining the timing of the transfer of control - at a point in time or over time - requires judgement.

*Sale of goods - contract manufacturing revenue recognised over time*

The Group has determined that for certain goods that are manufactured and supplied under contract manufacturing and supply arrangements, the customer controls the goods once the goods are duly finished, approved for distribution and packaged in accordance with the relevant agreement. This is because under those agreements, goods are manufactured to a customer's specification, packaged with the customer's branding, and if a firm order that is placed by the customer in accordance with the agreement is terminated, the Group is entitled to reimbursement of the costs incurred in manufacturing the goods, including a reasonable margin. Therefore, revenue from these agreements and the associated costs are recognised over time - i.e. before the goods are delivered to the customer's premises. Invoices are issued according to contractual terms and amounts not yet invoiced are presented as contract assets in the consolidated statement of financial position.

*Sale of goods - other revenue recognised at a point in time*

Revenue from the sale of goods that are not subject to contract manufacturing arrangements is measured at the fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognised when a customer obtains control of the promised goods and the Group has satisfied its performance obligation in relation to the promised goods. In determining when control of promised goods passes to the customer, the Group considers the transfer of significant risks and rewards of ownership of the goods to the customer to indicate that the customer has obtained the ability to direct the use of and obtain substantially all of the remaining benefits from the goods. The timing of the transfer of risks and rewards to the customer for the sale of goods occurs either:

- When the goods are despatched or delivered in line with the International Chamber of Commerce's International Commercial Terms (Incoterms®) as detailed in the relevant contract of sale or purchase order for the goods;
- When they are made available to the customer and ownership transfers prior to despatch as detailed in the relevant contract of sale or purchase order for the goods; or
- On notification that the product has been used when the goods are consignment products located at customers' premises.

Where cash consideration has been received but the revenue recognition criteria has not been met, such amounts have been recorded on the consolidated statement of financial position as a contract liability.

*(ii) Government grants*

Government grants are recognised initially as deferred income at fair value and when there is reasonable assurance that they will be received and that the Group will comply with the conditions associated with the grant, they are then recognised in profit or loss as other income on a systematic basis over the useful life of the asset. Grants that compensate the Group for expenses incurred are recognised in profit or loss or other income on a systematic basis in the same periods in which the expenses are recognised. Grants that compensate the Group for expenditure capitalised are recognised as a reduction in the carrying value of the asset and grants that compensate the Group for expenditure recognised in profit or loss is recognised as government grant income.

### (h) Income tax

Tax expense comprises current and deferred tax. Current and deferred taxes are recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

## 2 Summary of significant accounting policies (continued)

### (h) Income tax (continued)

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Current tax payable also includes any tax liability arising from the declaration of dividends.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss,
- temporary differences related to investments in subsidiaries and associates and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future, and
- taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date.

In determining the amount of current and deferred tax, the Group takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. The Group believes that its accruals for tax liabilities are adequate for all open tax years based on its assessment of many factors, including interpretations of tax law and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the Group to change its judgement regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact tax expense in the period that such a determination is made.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income tax expenses that arise from the distribution of cash dividends are recognised at the same time that the liability to pay the related dividend is recognised. The Group does not distribute non-cash assets as dividends to its shareholders.

### (i) Leases

<u>Policy applicable before 1 January 2019</u>

For contracts entered into before 1 January 2019, the Group determined whether the arrangement was or contained a lease based on the assessment of whether:

- fulfilment of the arrangement was dependent on the use of a specific asset or assets; and
- the arrangement had conveyed a right to use the asset. An arrangement conveyed the right to use the asset if one of the following was met:
  - the purchaser had the ability or right to operate the asset while obtaining or controlling more than an insignificant amount of the output;
  - the purchaser had the ability or right to control physical access to the asset while obtaining or controlling more than an insignificant amount of the output; or
  - facts and circumstances indicated that it was remote that other parties would take more than an insignificant amount of the output, and the price per unit was neither fixed per unit of output nor equal to the current market price per unit of output.

## 2 Summary of significant accounting policies (continued)

### (i) Leases (continued)

*Leased assets*

Leases that transfer to the Group substantially all of the risks and rewards of ownership are classified as finance leases. Assets acquired under finance leases are initially measured at an amount equal to the lower of their fair value and the present value of the minimum lease payments. Subsequent to initial recognition, these leased assets are accounted for in accordance with the accounting policy applicable to each asset.

Other leases are classified as operating leases, and the underlying assets are not recognised in the Group's consolidated statement of financial position.

*Lease payments*

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

*Determining whether an arrangement contains a lease*

At inception of an arrangement, the Group determines whether the arrangement is or contains a lease. A specific asset is the subject of a lease if fulfilment of the arrangement is dependent on the use of that specified asset. An arrangement conveys the right to use the asset if the arrangement conveys to the Group the right to control the use of the underlying asset.

At inception and on reassessment of an arrangement that contains a lease, the Group separates payments and other consideration required by the arrangement into those for the lease and those for other elements on the basis of their relative fair values. If an arrangement contains a finance lease and the Group concludes that it is impracticable to separate the payments reliably, then an asset and a liability are recognised at an amount equal to the fair value of the underlying asset. The liability is subsequently reduced as payments are made, and an imputed finance cost on the liability is recognised using the Group's incremental borrowing rate.

<u>Policy applicable from 1 January 2019</u>

At inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Group uses the definition of a lease in IFRS 16.

This policy is applied to contracts entered into, on or after 1 January 2019.

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of its relative stand-alone prices. However, for the leases of property the Group has elected not to separate non-lease components and account for the lease and non-lease components as a single lease component.

## 2 Summary of significant accounting policies (continued)

### (i) Leases (continued)

The Group recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Group by the end of the lease term or the cost of the right-of-use asset reflects that the Group will exercise a purchase option. In that case the right-of-use asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate.

The Group determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease and type of the asset leased.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Group is reasonably certain to exercise, lease payments in an optional renewal period if the Group is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee, if the Group changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The Group presents right-of-use assets that do not meet the definition of investment property in 'property, plant and equipment' and lease liabilities in 'loans and borrowings' in the consolidated statement of financial position.

*Short-term leases and leases of low-value assets*

The Group has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases, including IT equipment. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

## 2 Summary of significant accounting policies (continued)

### (j) Impairment

*Non-derivative financial assets*

Financial instruments and contract assets

The Group recognises loss allowances for Expected Credit Losses on:

- financial assets measured at amortised cost; and
- contract assets.

Loss allowances for trade receivables and contract assets are always measured at an amount equal to lifetime Expected Credit Losses.

When determining whether the credit risk of a financial asset has increased significantly since initial recognition and when estimating Expected Credit Losses, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and informed credit assessment and including forward-looking information.

The Group assumes that the credit risk on a financial asset has increased significantly if it is more than 30 days past due.

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held); or
- the financial asset is more than 90 days past due

Measurement of Expected Credit Losses

Expected Credit Losses are a probability-weighted estimate of credit losses. The Group uses an allowance matrix to measure the expected credit losses of trade receivables from individual customers.

Loss rates are calculated using a 'roll rate' method based on the probability of a receivable progressing through successive stages of delinquency to write-off. Roll rates are calculated separately for exposures in different segments based on the following common credit risk characteristics - geographic region, age of customer relationship and type of product purchased.

Expected Credit Losses are discounted at the effective interest rate of the financial asset.

Presentation of allowance for Expected Credit Loss in the statement of financial position

Loss allowances for financial assets measured at amortised cost are deducted from the gross carrying amount of the assets.

Write-off

The gross carrying amount of a financial asset is written off when the Group has no reasonable expectations of recovering a financial asset in its entirety or a portion thereof. For individual customers, the Group has a policy of writing off the gross carrying amount when the financial asset is 180 days past due based on historical experience of recoveries of similar assets. For corporate customers, the Group individually makes an assessment with respect to the timing and amount of write-off based on whether there is a reasonable expectation of recovery. The Group expects no significant recovery from the amount written off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

## 2 Summary of significant accounting policies (continued)

### (j) Impairment (continued)

*Non-financial assets*

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Indefinite life intangible assets are tested annually for impairment. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less cost of disposal. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax or post-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. Subject to an operating segment ceiling test, CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU (or group of CGUs), and then to reduce the carrying amounts of the other assets in the CGU (or group of CGUs) on a pro rata basis.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

*Goodwill*

Goodwill is tested annually for impairment.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGUs. Goodwill arising from a business combination is allocated to CGUs or groups of CGUs that are expected to benefit from the synergies of the combination.

### (k) Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first-in first-out principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs, and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

### (l) Assets held for sale

Non-current assets, or disposal groups comprising assets and liabilities, are classified as held-for-sale if it is highly probable that they will be recovered primarily through sale rather than through continuing use.

Such assets, or disposals group, are generally measured at lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group is allocated first to goodwill and then the remaining assets and liabilities on a pro rata basis, except that no loss is allocated to inventories, financial assets, employee benefit assets or investment property, which continue to be measured in accordance with the Group's other accounting policies. Impairment losses on initial classification as held-for-sale or held-for- distribution and subsequent gains and losses on re-measurement are recognised in profit or loss.

Once classified as held-for-sale, intangible assets and property, plant and equipment are no longer amortised or depreciated, and any equity-accounted investee is no longer equity accounted.

## 2 Summary of significant accounting policies (continued)

### (m) Property, plant and equipment

*Recognition and measurement*

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the following:

- the cost of materials and direct labour,
- any other costs directly attributable to bringing the assets to a working condition for their intended use,
- when the Group has an obligation to remove the assets or restore the site, an estimate of the costs of dismantling and removing the items and restoring the site on which they are located, and
- capitalised borrowing costs.

Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment. Any gains and losses on disposal of an item of property, plant and equipment (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in profit or loss.

*Subsequent costs*

Subsequent expenditure is capitalised only when it is probable that the future economic benefits associated with the expenditure will flow to the Group. Ongoing repairs and maintenance is expensed as incurred.

*Depreciation*

Items of property, plant and equipment are depreciated on a straight-line basis in profit or loss over the estimated useful lives of each component. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

Items of property, plant and equipment are depreciated from the date that they are installed and are ready for use, or in respect of internally constructed assets, from the date that the asset is completed and ready for use.

The estimated useful lives for the current and comparative years of significant items of property, plant and equipment are as follows:

| | |
|---|---|
| • Buildings | 40 years |
| • Contract plant and equipment | 5 - 20 years |
| • Manufacturing plant and equipment | 3 - 25 years |
| • Motor vehicles | 8 years |
| • Office equipment | 2 - 7 years |

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

### (n) Investments

Details of shares in controlled entities are disclosed at note 27(a). Controlled entities are accounted for in the consolidated accounts as set out in the note 2(b).

## 2 Summary of significant accounting policies (continued)

### (o) Intangible assets

*(i) Research and development*

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in profit or loss as incurred.

Development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is capitalised only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Group intends to and has sufficient resources to complete development and to use or sell the asset. The expenditure capitalised includes the cost of materials, direct labour, overhead costs and external costs that are directly attributable to preparing the asset for its intended use, and capitalised borrowing costs. Other development expenditure is recognised in profit or loss as incurred. Capitalised development expenditure is measured at cost less accumulated amortisation and accumulated impairment losses.

*(ii) Patents and trademarks*

Other intangible assets that are acquired by the Group and have finite useful lives are measured at cost less accumulated amortisation and accumulated impairment losses.

*(iii) Goodwill*

Goodwill arising on the acquisition of subsidiaries is measured at cost less accumulated impairment losses.

*(iv) Subsequent expenditure*

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in profit or loss as incurred.

*(v) Amortisation*

Identifiable intangible assets are amortised on a straight-line basis in profit or loss over their estimated useful lives, from the date that they are available for use. Goodwill is not amortised.

The estimated useful lives for the current and comparative years are as follows:

- Patents and trademarks 3 - 5 years
- Capitalised development costs 2 - 5 years

Amortisation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

### (p) Finance income and finance expenses

Finance income comprises interest income on funds invested. Interest income is recognised as it accrues in profit or loss, using the effective interest method.

Finance expenses comprise interest expense on borrowings. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance expense depending on whether foreign currency movements are in a net gain or net loss position.

## 2 Summary of significant accounting policies (continued)

### (q) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as a finance cost.

### (r) Employee benefits

*(i) Short-term obligations*

Short-term employee benefit obligations including salaries and wages, annual leave and long service leave expected to be settled within 12 months of the reporting date are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

*(ii) Other long-term employee benefit obligations*

The Group's obligation in respect of long service leave is the amount of future benefit that employees have earned in return for their service in the current and prior periods. That liability is measured as the present value of expected future payments to be made in respect of the services provided by employees up to the end of the reporting period. 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 on corporate bonds with terms to maturity that match, as closely as possible, the estimated future cash outflows.

The obligations are presented as a current liability in the consolidated statement of financial position if the Group does not have an unconditional right to defer settlement for at least twelve months after the reporting date, regardless of when the actual settlement is expected to occur.

*(iii) Share-based payment arrangements*

The grant-date fair value of equity-settled share-based payment arrangements granted to employees is generally recognised as an expense, with a corresponding increase in equity, over the vesting period of the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market performance conditions are expected to be met, such that the amount ultimately recognised is based on the number of awards that meet the related service and non-market performance conditions at the vesting date. For share-based payment awards with non-vesting conditions, the grant-date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

### (s) Earnings per share

*(i) Basic earnings per share*

Basic earnings per share is calculated by dividing the profit/(loss) attributable to equity holders 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. Refer to note 30 for further details.

*(ii) Diluted earnings per share*

Diluted earnings per share adjusts the figures used in the determination of basic earnings 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. Refer to note 30 for further details.

## 2 Summary of significant accounting policies (continued)

### (t) Goods and Services Tax (GST) and Value Added Tax (VAT)

Revenues, expenses and assets are recognised net of the amount of associated GST or VAT, unless the GST or VAT 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 or VAT receivable or payable. The net amount of GST or VAT recoverable from, or payable to, the taxation authority is included with other receivables or payables in the consolidated statement of financial position.

Cash flows are presented on a gross basis. The GST or VAT components of cash flows arising from investing or financing activities which are recoverable from, or payable to the taxation authority, are presented as operating cash flows.

### (u) Parent entity financial information

The financial information for the parent entity, Palla Pharma Limited, disclosed in note 32, has been prepared on the same basis as the consolidated financial statements, except for investments in subsidiaries. Investments in subsidiaries are accounted for at cost in the financial statements of Palla Pharma Limited.

## 3 Financial risk management

*Overview*

The Group's activities expose it to the following risks arising from their use of financial instruments:
- credit risk;
- liquidity risk; and
- market risk (including currency and interest rate risk).

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk and the Group's management of capital.

*Risk management framework*

The Directors have overall responsibility for the establishment and oversight of the risk management framework.

The Board of Directors seek to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position. Capital requirements have been principally funded by equity in the form of share capital from investors and debt in the form of shareholder loans. It is anticipated any further expansion will be funded predominantly through debt in the form of bank loans, and equity in the form of placements and rights issues.

### (a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date for recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets.

*Exposure to credit risk*

The Group limits its exposure to credit risk from trade receivables by establishing a maximum payment period three months for corporate customers.

The carrying amount of the Group's financial assets represents the maximum credit exposure. The maximum exposure to credit risk at reporting date was:

| | | **Consolidated entity** | |
|---|---|---|---|
| | Notes | **31 December 2019 $** | 31 December 2018 $ |
| Trade receivables | 10 | **11,269,118** | 10,171,554 |
| Other receivables and loans - current | 10 | **237,950** | 1,760,485 |
| Cash and cash equivalents | 9 | **2,019,087** | 1,904,583 |
| Contract assets | | **5,995,039** | 3,527,827 |
| Other receivables and loans - non-current | 12 | **405,875** | - |
| | | **19,927,069** | 17,364,449 |

## 3 Financial risk management (continued)

### (a) Credit risk (continued)

The maximum exposure to credit risk for receivables at the reporting date by geographic region was:

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Europe | **11,052,052** | 6,994,216 |
| Other regions | **217,066** | 3,177,338 |
| | **11,269,118** | 10,171,554 |

The maximum exposure to credit risk for trade receivables at the reporting date by type of counter party was:

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| End-user customers | **11,269,118** | 10,171,554 |

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. In monitoring customer credit risk, customers are grouped by their ageing profile. Monitoring of receivable balances on an ongoing basis minimises the exposure of bad debts. A provision for impairment is recognised when there is objective evidence that an individual trade receivable in impaired.

The aging of the Group's trade receivables at the reporting date was:

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Not past due | **7,642,862** | 7,279,522 |
| 1 - 30 days | **1,098,684** | 2,410,254 |
| 31 - 60 days | **-** | 225,179 |
| 61 - 90 days | **282,053** | 256,599 |
| 90 days and over | **2,245,519** | - |
| | **11,269,118** | 10,171,554 |

The trade receivable balances are reviewed monthly and an allowance is raised where an indication of impairment exists such as customer insolvency or slow payment record without due cause. Where the Group considers that recovery of the amount owing is not possible, the amounts considered irrecoverable are written off against the financial asset directly. As at 31 December 2019, there was no provision for impairment in relation to trade receivable balances (2018: nil).

The credit risk of contract assets amounting to $5,995,039 and other receivables and loans of $218,548 were primarily in respect of the European geographic region, owing from end-user customers and aging that was not past due at 31 December 2019 and $425,277 owing from key management personnel. Other receivables of $1,760,485 in the 2018 financial period were predominately owing from statutory authorities.

## 3 Financial risk management (continued)

### (a) Credit risk (continued)

*Expected credit loss assessment for individual customers*

The following table provides information about the exposure to credit risk and expected credit losses for trade receivables and contract assets from individual customers as at 31 December 2019.

| **31 December 2019** | **Weighted-average loss rate %** | **Gross carrying amount $** | **Loss allowance** | **Credit impaired** |
|---|---|---|---|---|
| Current (not past due) | 0.00% | 7,642,862 | - | No |
| 1 - 30 days past due | 0.00% | 1,098,684 | - | No |
| 31 - 60 days past due | 0.00% | - | - | No |
| 61 - 90 days past due | 0.00% | 282,053 | - | No |
| 90 days and over | 0.00% | 2,245,519 | - | No |
| | | 11,269,118 | - | |

Loss rates are based on actual credit loss experience over a period of 48 months. These rates are multiplied by scalar factors to reflect differences between economic conditions during the period over which the historical data has been collected, current conditions and the Group's view of economic conditions over the expected lives of the receivables.

As at 31 December 2019, the credit risk assessment of a customer ($3,672,860) has been assessed based on the net-off value of certain assets acquired from that customer; refer to note 29. Whilst the debtor is not past due, based on ongoing credit monitoring and assessment, it has been assessed that there is a higher risk associated with its collectability.

*Cash and cash equivalents*

The Group held cash and cash equivalents, including other assets, of $2,019,087 at 31 December 2019 (2018: $1,904,583), which represents its maximum credit exposure on these assets. The cash and cash equivalents are held with bank and financial institution counterparts, which are rated AA-, based on S&P ratings.

## 3 Financial risk management (continued)

**(b) Liquidity risk**

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The Group monitors the level of expected cash outflows on trade and other payables. In addition, details of lines of credit maintained by the Group are set out in note 21.

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements:

| **Contractual maturities of financial liabilities** | **Less than 6 months** | **6 - 12 months** | **Between 1 and 2 years** | **Between 2 and 5 years** | **Over 5 years** | **Total contractual cash flows** | **Carrying amount of liabilities** |
|---|---|---|---|---|---|---|---|
| **At 31 December 2019** | **$** | **$** | **$** | **$** | **$** | **$** | **$** |
| **Non-derivatives** | | | | | | | |
| Shareholder loan facility | **-** | **-** | **(5,962,500)** | **-** | **-** | **(5,962,500)** | **5,000,000** |
| Trade and other payables | **(8,349,055)** | **(558,065)** | **-** | **(1,563,462)** | **-** | **(10,470,582)** | **10,470,582** |
| Insurance premium funding | **(194,035)** | **(281,646)** | **-** | **-** | **-** | **(475,681)** | **455,256** |
| Other | **(12,168)** | **-** | **-** | **-** | **-** | **(12,168)** | **12,168** |
| **Total non-derivatives** | **(8,555,258)** | **(839,711)** | **(5,962,500)** | **(1,563,462)** | **-** | **(16,920,931)** | **15,938,006** |
| At 31 December 2018 | | | | | | | |
| **Non-derivatives** | | | | | | | |
| Shareholder loan facility | - | - | (26,659,402) | - | - | (26,659,402) | 22,702,960 |
| Trade and other payables | (9,426,538) | - | - | - | - | (9,426,538) | 9,426,538 |
| Insurance premium funding | (184,148) | - | - | - | - | (184,148) | 174,647 |
| Other | 8,573 | - | - | - | - | 8,573 | (8,573) |
| **Total non-derivatives** | (9,602,113) | - | (26,659,402) | - | - | (36,261,515) | 32,295,572 |

## 3 Financial risk management (continued)

### (c) Market risk

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

*(i) Currency risk*

The Group undertakes certain transactions denominated in foreign currencies, hence exposures to exchange rate fluctuation arise. Exchange rate exposures are managed within approved policy parameters. The Group manages the currency risk by monitoring the trend of the US dollar, Euro, Norwegian Krone, Swedish Krona, Danish Krone, British Pound and Swiss Franc. The Group maintains US dollar, Euro and Norwegian Krone bank accounts to cover a portion of its anticipated expenditures in the respective foreign currencies.

The Group’s foreign currency risk denominated financial assets and financial liabilities at the reporting date are as follows:

| **Consolidated entity** | **31 December 2019** | | | | | | |
|---|---|---|---|---|---|---|---|
| | **USD** | **EUR** | **NOK** | **SEK** | **DKK** | **GBP** | **CHF** |
| Financial assets | | | | | | | |
| Cash and cash equivalents | **291,271** | **439,180** | **2,707,954** | **-** | **-** | **-** | **-** |
| Trade and other receivables | **1,180,804** | **1,588,833** | **19,611,341** | **-** | **-** | **1,917,500** | **-** |
| Financial liabilities | | | | | | | |
| Trade and other payables | **(2,951,297)** | **(200,080)** | **(11,147,183)** | **(1,525,534)** | **-** | **(5,377)** | **(1,963)** |
| Net exposure | **(1,479,222)** | **1,827,933** | **11,172,112** | **(1,525,534)** | **-** | **1,912,123** | **(1,963)** |

| **Consolidated entity** | 31 December 2018 | | | | | | |
|---|---|---|---|---|---|---|---|
| | USD | EUR | NOK | SEK | DKK | GBP | CHF |
| Financial assets | | | | | | | |
| Cash and cash equivalents | 11,955 | 243,408 | 7,676,105 | - | - | - | - |
| Trade and other receivables | 4,387,777 | 893,640 | 11,247,740 | - | - | - | - |
| Financial liabilities | | | | | | | |
| Trade and other payables | (108,970) | (254,565) | (10,198,010) | (3,399,938) | (19,430) | - | - |
| Net exposure | 4,290,762 | 882,483 | 8,725,835 | (3,399,938) | (19,430) | - | - |

# 3 Financial risk management (continued)

## (c) Market risk (continued)

*Sensitivity*

The following sensitivity analysis is based on the foreign currency risk exposures in existence at the statement of financial position date. A 10 percent increase or decrease in the foreign exchange rate is used and represents management's assessment of the possible change in foreign exchange rates and historically is within a range of rate movements. A positive number indicates an increase in profit and equity. A negative number indicates a decrease in profit and equity. At 31 December 2019, if foreign exchange rates had moved, as illustrated in the table below, with all other variables held constant, pre-tax profit and equity would have been affected as follows:

| | **-10% in AUD** | | **+10% in AUD** | |
|---|---|---|---|---|
| **31 December 2019** | | | | |
| **Consolidated entity** | **Profit $** | **Equity $** | **Profit $** | **Equity $** |
| *Financial assets* | | | | |
| Cash and cash equivalents | **172,956** | **172,956** | **(141,510)** | **(141,510)** |
| Trade and other receivables | **1,221,479** | **1,221,479** | **(999,392)** | **(999,392)** |
| *Financial liabilities* | | | | |
| Trade and other payables | **(814,856)** | **(814,856)** | **666,701** | **666,701** |
| | **579,579** | **579,579** | **(474,201)** | **(474,201)** |

| | **-10% in AUD** | | **+10% in AUD** | |
|---|---|---|---|---|
| **31 December 2018** | | | | |
| **Consolidated entity** | **Profit** $ | **Equity** $ | **Profit** $ | **Equity** $ |
| *Financial assets* | | | | |
| Cash and cash equivalents | 184,521 | 184,521 | (152,839) | (152,839) |
| Trade and other receivables | 1,056,448 | 1,056,448 | (864,367) | (864,367) |
| *Financial liabilities* | | | | |
| Trade and other payables | (546,063) | (546,063) | 446,780 | 446,780 |
| | 694,906 | 694,906 | (570,426) | (570,426) |

*(ii) Interest rate risk*

The Group is exposed to interest rate risk arising from changes in market interest rate on its variable rate investments. The Group's policy is to manage its finance costs using a mix of fixed and variable rate debt. Management periodically reviews its interest rate exposure and consideration is given to potential renewals of existing positions, alternative financing and the mix of fixed and variable interest rates.

## 3 Financial risk management (continued)

### (c) Market risk (continued)

*Profile*

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was as follows:

| | Carrying amounts | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| *Fixed rate instruments* | | |
| Financial assets | **425,277** | - |
| Financial liabilities | **5,455,256** | 22,877,607 |
| *Variable rate instruments* | | |
| Financial assets | **457,573** | 221,892 |
| Financial liabilities | **-** | - |

*Fair value sensitivity analysis for fixed rate instruments*

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit and loss. Therefore a change in interest rate at the reporting date would not affect the profit and loss or equity.

*Cash flow sensitivity analysis for variable rate instruments*

A change of 100 basis points in interest rates would have increased or decreased the Group's equity by $4,576 (2018: $2,219). This analysis assumes that all other variables, in particular foreign currency rates remain constant.

### (d) Capital management

The Board's policy is to maintain a strong capital base to ensure the Group continues as a going concern, and to sustain future development of the business while maximising returns to stakeholders.

The Board seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position. With the Group still in its early stages, capital requirements have been principally funded by equity in the form of share capital from investors, shareholder loans and surplus operating cash flows. As the Group consolidates its operating position, it is anticipated that further expansion will be funded predominantly through debt in the form of bank loans and equity in the form of placements and right issues.

### (e) Fair values

None of the Group's financial assets or financial liabilities are readily traded on an organised market in standardised form, and all are classified as Level 3 in the fair value hierarchy. As such, the Group uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique for each asset or liability is listed below, and where relevant incorporate all of the factors that market participants would take into account in pricing a transaction.

| ***Financial instrument*** | ***Valuation technique*** |
|---|---|
| Unlisted investments | Group's share in the net asset value of the investee at balance date |
| All other financial assets and liabilities | Fair value approximates their carrying value |

## 3 Financial risk management (continued)

### (e) Fair values (continued)

*Accounting classifications and fair values*

The following table shows the carrying amounts and fair values of financial assets and financial liabilities. It does not include fair value information for financial assets and financial liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value.

| | Carrying amounts | | | |
|---|---|---|---|---|
| **31 December 2019** | **Fair value through profit and loss $** | **Financial assets at amortised cost $** | **Other financial liabilities $** | **Total $** |
| *Financial assets measured at fair value* | | | | |
| Unlisted investments | **103,272** | **-** | **-** | **103,272** |
| *Financial assets not measured at fair value* | | | | |
| Cash and cash equivalents | **-** | **2,019,087** | **-** | **2,019,087** |
| Trade, other receivables and loans | **-** | **11,912,943** | **-** | **11,912,943** |
| | **103,272** | **13,932,030** | **-** | **14,035,302** |
| *Financial liabilities not measured at fair value* | | | | |
| Shareholder loan facility | **-** | **-** | **5,000,000** | **5,000,000** |
| Insurance premium funding | **-** | **-** | **455,256** | **455,256** |
| Other borrowings | **-** | **-** | **12,168** | **12,168** |
| Trade and other payables | **-** | **-** | **10,470,582** | **10,470,582** |
| | **-** | **-** | **15,938,006** | **15,938,006** |
| **31 December 2018** | **$** | **$** | **$** | **$** |
| *Financial assets measured at fair value* | | | | |
| Unlisted investments | 103,549 | - | - | 103,549 |
| *Financial assets not measured at fair value* | | | | |
| Cash and cash equivalents | - | 1,904,583 | - | 1,904,583 |
| Trade, other receivables and loans | - | 11,932,039 | - | 11,932,039 |
| | 103,549 | 13,836,622 | - | 13,940,171 |
| *Financial liabilities not measured at fair value* | | | | |
| Shareholder loan facility | - | - | 22,702,960 | 22,702,960 |
| Insurance premium funding | - | - | 174,647 | 174,647 |
| Other borrowings | - | - | (8,573) | (8,573) |
| Trade and other payables | - | - | 9,426,538 | 9,426,538 |
| | - | - | 32,295,572 | 32,295,572 |

Unlisted investments represents the Group’s interest in the Macquarie River Pipeline Partnership and its fair value categorised as level 3 in the fair value hierarchy based on inputs that are not based on observable market data.

## 4 Use of estimates and judgements

The preparation of consolidated financial statements in conformity with AASBs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

*Assumptions and estimation uncertainties*
Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ending 31 December 2019 is included in the following notes:

Notes 15 and 16 - impairment test: key assumptions underlying recoverable amounts of property, plant and equipment and intangible assets.

*Measurement of fair values*
A number of the Group's accounting policies and disclosures require the measurement of fair values for both financial and non-financial assets and liabilities.

When measuring the fair value of an asset or a liability, the Group uses observable market data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- *Level 1*: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- *Level 2*: inputs other than quoted prices in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- *Level 3*: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability fall into different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

## 5 Segment information

Operating segments are presented using the 'management approach', where the information presented is on the same basis as the internal reports provided to the Chief Operating Decision Maker ('CODM') of the Group. The CODM is responsible for the allocation of resources to operating segments and assessing their performance. The CODM has been identified as the CEO. Segment information is presented to the CEO comprising two segments: Australia and Norway.

*Australia*
Segment activities: Narcotic Raw Material and Poppy Seed production and distribution.

*Norway*
Segment activities: Active Pharmaceutical Ingredient and Finished Dosage Formulation production and distribution.

| | Australia | | Norway | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|
| **Consolidated entity** | **31 December 2019 $** | **31 December 2018 $** | **31 December 2019 $** | **31 December 2018 $** | **31 December 2019 $** | **31 December 2018 $** | **31 December 2019 $** | **31 December 2018 $** |
| External revenue | **8,043,325** | **8,792,653** | **46,642,069** | **37,378,345** | **-** | **-** | **54,685,394** | **46,170,998** |
| Inter-segment revenue | **21,226,183** | **10,500,690** | **-** | **-** | **(21,226,183)** | **(10,500,690)** | **-** | **-** |
| Total segment revenue | **29,269,508** | **19,293,343** | **46,642,069** | **37,378,345** | **(21,226,183)** | **(10,500,690)** | **54,685,394** | **46,170,998** |
| Reportable segment profit/(loss) after tax | **(2,304,283)** | **(6,218,549)** | **(2,089,880)** | **678,511** | **(156,202)** | **285,957** | **(4,550,365)** | **(5,254,081)** |
| *Unallocated amounts* | | | | | | | | |
| Net financing costs | **-** | **-** | **-** | **-** | **-** | **-** | **(3,089,078)** | **(1,653,331)** |
| Profit from discontinued operation | **-** | **-** | **-** | **-** | **-** | **-** | **-** | **1,119,003** |
| **(Loss) for the year** | **-** | **-** | **-** | **-** | **-** | **-** | **(7,639,443)** | **(5,788,409)** |

## 5 Segment information (continued)

| | Australia | | Norway | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|
| | 31 December 2019 | 31 December 2018 | 31 December 2019 | 31 December 2018 | 31 December 2019 | 31 December 2018 | 31 December 2019 | 31 December 2018 |
| **Consolidated entity** | $ | $ | $ | $ | $ | $ | $ | $ |
| Timing of External revenue recognition: | | | | | | | | |
| At a point in time | 8,043,325 | 8,792,653 | 18,860,079 | 10,684,300 | - | - | 26,903,404 | 19,476,953 |
| Over time | - | - | 27,781,990 | 26,694,045 | - | - | 27,781,990 | 26,694,045 |
| | 8,043,325 | 8,792,653 | 46,642,069 | 37,378,345 | - | - | 54,685,394 | 46,170,998 |

## 5 Segment information (continued)

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| **Non-current assets** | | |
| Australia | **29,706,630** | 27,366,538 |
| Europe | **16,714,665** | 17,137,383 |
| | **46,421,295** | 44,503,921 |

## 6 Revenue

### (a) Revenue streams

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| **From continuing operations** | | |
| *Sale of goods* | | |
| Sales from contracts with customers | **54,685,394** | 46,170,998 |
| *Other income* | | |
| Rental income | **158,366** | 101,446 |
| Macquarie Pipeline Partnership | **(277)** | 1,783 |
| Other items | **-** | 289,154 |
| | **158,089** | 392,383 |
| | **54,843,483** | 46,563,381 |

### (b) Contract balances

The following table provides information about receivables and contract assets from contracts with customers.

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Receivables, which are included in 'trade and other receivables' | **11,269,118** | 10,171,554 |
| Contract assets - refer to note 2(g)(i) | **5,995,039** | 3,527,827 |
| | **17,264,157** | 13,699,381 |

## 7 Expenses

| | Notes | Consolidated entity 31 December 2019 $ | 31 December 2018 $ |
|---|---|---|---|
| **(Loss) before income tax includes the following specific expenses:** | | | |
| *Employee benefits expenses* | | | |
| Salaries and wages | | **16,613,290** | 15,581,094 |
| Other associated personnel expenses | | **1,565,539** | 1,660,743 |
| Defined contribution superannuation expenses | | **567,384** | 460,366 |
| Increase/(decrease) in liability for long service leave | | **63,495** | (17) |
| Increase in liability for annual leave | | **137,233** | 490,884 |
| Share-based payments | 31 | **343,633** | 327,497 |
| Total employee benefits expenses | | **19,290,574** | 18,520,567 |
| *Depreciation* | | | |
| Buildings | | **429,713** | 419,564 |
| Contract equipment | | **171,866** | 185,654 |
| Manufacturing plant and equipment | | **1,624,393** | 1,722,681 |
| Office equipment | | **226,230** | 162,204 |
| Motor vehicles | | **18,277** | 28,961 |
| Total depreciation | | **2,470,479** | 2,519,064 |
| *Amortisation* | | | |
| Patents | | **43,407** | 32,231 |
| Total depreciation and amortisation | | **2,513,886** | 2,551,295 |
| *Finance income* | | | |
| Interest income | | **(23,028)** | (21,418) |
| | | **(23,028)** | (21,418) |
| *Finance costs* | | | |
| Interest and finance expenses on financial liabilities measured at amortised cost | | **2,801,015** | 1,657,773 |
| Net exchange losses on foreign currency | | **311,091** | 16,976 |
| | | **3,112,106** | 1,674,749 |
| Net finance expenses recognised in profit or loss | | **3,089,078** | 1,653,331 |

## 8 Income tax expense

### (a) Numerical reconciliation of income tax expense to prima facie tax payable

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| (Loss) from continuing operations before income tax expense | **(7,777,636)** | (6,772,519) |
| Tax at the Australian tax rate of 30.0% (2018 - 30.0%) | **(2,333,291)** | (2,031,756) |
| Tax effect of amounts which are not deductible (taxable) in calculating taxable income: | | |
| Effect of different tax rates of subsidiaries operating in other jurisdictions | **99,534** | (41,054) |
| Deferred tax assets not brought into account | **2,095,564** | 2,207,703 |
| Income tax (benefit)/expense | **(138,193)** | 134,893 |

### (b) Unrecognised deferred tax assets

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| The following deferred tax assets have not been brought to account as assets: | | |
| Deductible temporary differences | **3,319,155** | 3,284,749 |
| Tax losses – revenue | **35,130,520** | 33,069,362 |
| | **38,449,675** | 36,354,111 |

These deductible temporary differences and tax losses can be carried forward indefinitely, and the tax losses are subject to the company loss recoupment rules under current tax legislation in Australia. Deferred tax assets have not been recognised in respect of these items because, given the stage of business, the Group cannot currently satisfy the necessary standard of probability that future taxable profits will be available against which the Group can utilise the benefits therefrom.

## 9 Current assets - Cash and cash equivalents

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Cash at bank | **2,019,087** | 1,904,583 |

## 10 Current assets - Trade and other receivables

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Trade receivables | **11,269,118** | 10,171,554 |
| Other receivables | **218,548** | 1,760,485 |
| Loan to key management personnel | **19,402** | - |
| | **11,507,068** | 11,932,039 |

The balance of trade and other receivables of $11,507,068 (2018: $11,932,038) are not considered impaired. Refer to note 3 for details of the credit risk exposure analysis.

## 11 Current assets - Inventories

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Raw materials and consumables | **6,607,925** | 5,830,836 |
| Work in progress | **15,194,810** | 12,751,135 |
| Finished goods | **346,639** | 584,393 |
| | **22,149,374** | 19,166,364 |

## 12 Non-current assets - Other receivables

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Loan to key management personnel | **405,875** | - |

## 13 Non-current assets - Inventories

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Raw materials and consumables | **1,977,493** | 1,200,529 |
| Work in progress | **250,901** | 599,095 |
| Finished goods | **22,191** | 22,249 |
| | **2,250,585** | 1,821,873 |

## 14 Non-current assets - Investments

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Macquarie River Pipeline Partnership - at fair value | **103,272** | 103,549 |

The unlisted interest in the Macquarie River Pipeline Partnership has been designated at fair value through profit or loss because it is managed on a fair value basis (refer note 4). The Group recognised its share of profits generated by the Partnership during the year.

## 15 Non-current assets - Property, plant and equipment

| Consolidated entity | Land and buildings $ | Manufacturing plant and equipment $ | Office equipment $ | Motor vehicles $ | Contract plant and equipment $ | Total $ |
|---|---|---|---|---|---|---|
| **At 1 January 2018** | | | | | | |
| Cost | 17,383,499 | 26,036,796 | 1,148,017 | 660,324 | 2,345,907 | 47,574,543 |
| Accumulated depreciation | (7,389,126) | (11,093,642) | (439,316) | (526,130) | (739,289) | (20,187,503) |
| Net book amount | 9,994,373 | 14,943,154 | 708,701 | 134,194 | 1,606,618 | 27,387,040 |
| **Year ended 31 December 2018** | | | | | | |
| Opening net book amount | 9,994,373 | 14,943,154 | 708,701 | 134,194 | 1,606,618 | 27,387,040 |
| Exchange differences | 23,802 | 68,523 | 1,735 | 290 | - | 94,350 |
| Additions | 585,300 | 1,507,030 | 655,478 | 21,818 | 12,061 | 2,781,687 |
| Disposals | - | - | (415) | (41,550) | (70,610) | (112,575) |
| Transfers | - | - | 130,834 | - | - | 130,834 |
| Depreciation charge | (419,564) | (1,722,681) | (162,204) | (28,961) | (185,654) | (2,519,064) |
| Closing net book amount | 10,183,911 | 14,796,026 | 1,334,129 | 85,791 | 1,362,415 | 27,762,272 |
| **At 31 December 2018** | | | | | | |
| Cost | 17,994,157 | 27,616,556 | 1,931,659 | 252,975 | 2,233,071 | 50,028,418 |
| Accumulated depreciation | (7,810,246) | (12,820,530) | (597,530) | (167,184) | (870,656) | (22,266,146) |
| Net book amount | 10,183,911 | 14,796,026 | 1,334,129 | 85,791 | 1,362,415 | 27,762,272 |

## 15 Non-current assets - Property, plant and equipment (continued)

| Consolidated entity | Land and buildings $ | Manufacturing plant and equipment $ | Office equipment $ | Motor vehicles $ | Contract plant and equipment $ | Total $ |
|---|---|---|---|---|---|---|
| **Year ended 31 December 2019** | | | | | | |
| Opening net book amount | 10,183,911 | 14,796,026 | 1,334,129 | 85,791 | 1,362,415 | 27,762,272 |
| Exchange differences | (4,983) | (391,278) | (80,923) | (22) | - | (477,206) |
| Additions | 65,410 | 1,545,431 | 267,906 | - | 621 | 1,879,368 |
| Depreciation charge | (429,713) | (1,624,393) | (226,230) | (18,277) | (171,866) | (2,470,479) |
| Closing net book amount | 9,814,625 | 14,325,786 | 1,294,882 | 67,492 | 1,191,170 | 26,693,955 |
| **At 31 December 2019** | | | | | | |
| Cost | 18,192,282 | 29,124,070 | 2,149,354 | 258,748 | 2,233,692 | 51,958,146 |
| Accumulated depreciation | (8,377,657) | (14,798,284) | (854,472) | (191,256) | (1,042,522) | (25,264,191) |
| Net book amount | 9,814,625 | 14,325,786 | 1,294,882 | 67,492 | 1,191,170 | 26,693,955 |

### Impairment testing

During the year ended 31 December 2019, the Group continued to record operating losses and accordingly has performed impairment testing to assess whether the recoverable amount of its property, plant and equipment and intangible assets is in excess of carrying value.

For the purpose of impairment testing the Group has defined two Cash Generating Units (CGU) the Australia CGU and the Norway CGU.

The recoverable amount for the CGU's was determined based on value-in-use calculations which require the use of assumptions.

Value in use as at 31 December 2019 was determined for the CGU's, based on the following key assumptions:

- Cash flows were forecast based on the Group’s five-year business plan with the terminal value based on the fifth-year cash flow and a long-term growth rate of 2.5%, which is consistent with the long-term inflation and growth targets of between 2% and 3%.
- Forecast sales volumes are based on past performance and management’s expectations of market development.
- Forecast foreign currency rates are set based on a range of external market commentator forecasts.
- Sales prices are based on current industry trends for each sales territory and contracted pricing where applicable.
- Forecast gross margins are based on past performance and management’s expectations for the future.
- Other operating costs of the CGU, which do not vary significantly with sales volumes or prices, have been forecast by management based on the current structure of the business, but not reflecting any future restructurings or cost saving measures.

## 15 Non-current assets - Property, plant and equipment (continued)

- Poppy straw harvesting yields were considered based on historical yield performance, climate-induced variations such as severe weather events, past plant losses and new growing areas coming into production.

- Annual capital expenditure is based on the historical experience of management. No incremental cost savings are assumed in the value-in-use model as a result of this expenditure.

- An after-tax discount rate of 8.5% and 10% for the Australia and Norway CGU's respectively was applied in determining the recoverable amount of the CGU's based on an industry average weighted-average cost of capital and applying a premium to the industry average due to the Group's size and stage of lifecycle.

The recoverable amount of the Australia CGU which was most sensitive to changes in key assumptions was determined to be higher than its carrying amount, indicating that no impairment is evident. In addition, reasonably possible changes in key assumptions were considered, such as changes in the forecast sales volumes, foreign exchange rates and the discount rate; sufficient headroom exists and no impairment was noted.

| | **Change required for carrying amount to equal recoverable amount** | |
|---|---|---|
| *In percent* | **2019** | **2018** |
| Discount rate | 3.1 | 0.5 |

In addition, a reasonably possible change in the USD/AUD foreign exchange rate would increase/(decrease) the headroom between the recoverable amount based on the value in use calculations and the carrying amount of the Australian CGU as follows:

| ***In cents*** | **Change to headroom (increase/(decrease))** | |
|---|---|---|
| ***USD/AUD exchange rate – 1 cent movement*** | **2019** | **2018** |
| Increase by 1 cent | $7.8m | $6.1m |
| Decrease by 1 cent | ($7.6m) | ($5.9m) |

## 16 Non-current assets - Intangible assets

| Consolidated entity | Goodwill $ | Patents, trademarks and other rights $ | Capitalised development costs $ | Irrigation rights $ | Total $ |
|---|---|---|---|---|---|
| **At 1 January 2018** | | | | | |
| Cost | 13,795,140 | 607,450 | 1,070,646 | 1,100,000 | 16,573,236 |
| Accumulated amortisation and impairment | - | (360,729) | (760,891) | - | (1,121,620) |
| Net book amount | 13,795,140 | 246,721 | 309,755 | 1,100,000 | 15,451,616 |
| **Year ended 31 December 2018** | | | | | |
| Opening net book amount | 13,795,140 | 246,721 | 309,755 | 1,100,000 | 15,451,616 |
| Exchange differences | 160,363 | 12,772 | - | - | 173,135 |
| Additions | - | - | 454,541 | - | 454,541 |
| Disposals | - | - | - | (1,100,000) | (1,100,000) |
| Transfers between assets classes | - | (130,834) | - | - | (130,834) |
| Amortisation charge | - | (32,231) | - | - | (32,231) |
| Closing net book amount | 13,955,503 | 96,428 | 764,296 | - | 14,816,227 |
| **At 31 December 2018** | | | | | |
| Cost | 13,955,503 | 128,571 | 764,296 | - | 14,848,370 |
| Accumulated amortisation and impairment | - | (32,143) | - | - | (32,143) |
| Net book amount | 13,955,503 | 96,428 | 764,296 | - | 14,816,227 |

| Consolidated entity | Goodwill $ | Patents, trademarks and other rights $ | Capitalised development costs $ | Irrigation rights $ | Total $ |
|---|---|---|---|---|---|
| **Year ended 31 December 2019** | | | | | |
| Opening net book amount | 13,955,503 | 96,428 | 764,296 | - | 14,816,227 |
| Exchange differences | - | (917) | - | - | (917) |
| Additions | - | 2,160,520 | 35,185 | - | 2,195,705 |
| Amortisation charge | - | (43,407) | - | - | (43,407) |
| Closing net book amount | 13,955,503 | 2,212,624 | 799,481 | - | 16,967,608 |
| **At 31 December 2019** | | | | | |
| Cost | 13,955,503 | 2,287,492 | 799,481 | - | 17,042,476 |
| Accumulated amortisation and impairment | - | (74,868) | - | - | (74,868) |
| Net book amount | 13,955,503 | 2,212,624 | 799,481 | - | 16,967,608 |

**Impairment testing**

The Group reviewed the carrying value of development costs at 31 December 2019 and determined that no impairments were required in respect of these assets.

The goodwill, intangible assets, development costs were tested as part of the CGU testing performed.

Refer to note 15 for further details of the Group's impairment testing for the year ended 31 December 2019.

## 17 Current liabilities - Trade and other payables

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Trade payables | **7,039,444** | 8,053,892 |
| GST and VAT | **976,780** | 455,896 |
| Other payables | **890,896** | 916,750 |
| | **8,907,120** | 9,426,538 |

## 18 Current liabilities - Borrowings

This note provides information about the Group's current interest-bearing loans and borrowings, which are measured at amortised cost.

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Other loans | **467,424** | 166,074 |
| Total current borrowings | **467,424** | 166,074 |

Refer to note 21 for movements during the year, and the contractual terms of the Group's current borrowings.

Refer to note 21 for reconciliation of movements of liabilities to cash flows arising from financing activities.

## 19 Current liabilities - Provisions

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Employee benefits - annual leave | **1,847,235** | 1,710,002 |

## 20 Non-current liabilities - Trade and other payables

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Trade payables | **1,563,462** | - |

## 21 Non-current liabilities - Borrowings

This note provides information about the Group's non-current interest-bearing loans and borrowings, which are measured at amortised cost.

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Shareholder loan facility | **5,000,000** | 22,702,960 |
| Total non-current borrowings | **5,000,000** | 22,702,960 |

Washington H. Soul Pattinson and Company Limited, a substantial shareholder has provided the Group with a standby debt facility with a limit of up to $16,000,000 (2018: $25,000,000) to meet the Group's short term working capital needs. At 31 December 2019 the Group had drawn down $5,000,000 of the facility (2018: $22,702,960). The maturity date of this facility is August 2021. This facility is secured by a mortgage over the property located in Australia, which has a book value of $8,313,469 at 31 December 2019.

### (a) Movements during the year

| | Currency | Nominal interest rate | Year of maturity | Movement | Carrying amount ($) |
|---|---|---|---|---|---|
| **At 1 January 2019** | | | | | **22,869,034** |
| *(Repayments)/drawings* | | | | | |
| Shareholder loan facility - Tranche A | AUD | 11.00% | 2020 | (16,400,000) | - |
| Shareholder loan facility - Tranche B | AUD | 9.00% | 2020 | (6,302,960) | - |
| Shareholder loan facility - Tranche C | AUD | 8.25% | 2021 | 5,000,000 | 5,000,000 |
| Insurance premium funding | AUD | 5.57% | 2020 | 95,151 | 183,797 |
| Insurance premium funding | AUD | 3.75% | 2020 | 185,458 | 271,459 |
| Other | AUD | | 2019 | 20,741 | 12,168 |
| **Carrying amount at 31 December 2019** | | | | (17,401,610) | **5,467,424** |

### (b) Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

| | | | | 31 December 2019 | | 31 December 2018 | |
|---|---|---|---|---|---|---|---|
| | Currency | Nominal interest rate | Year of maturity | Face value ($) | Carrying amount ($) | Face value ($) | Carrying amount ($) |
| Shareholder loan facility - Tranche A | AUD | 11.00% | 2020 | - | - | 16,400,000 | 16,400,000 |
| Shareholder loan facility - Tranche B | AUD | 9.00% | 2020 | - | - | 6,302,960 | 6,302,960 |
| Shareholder loan facility - Tranche C | AUD | 8.25% | 2021 | 5,000,000 | 5,000,000 | - | - |
| Insurance premium funding | AUD | 5.57% | 2020 | 183,797 | 183,797 | 88,646 | 88,646 |
| Insurance premium funding | AUD | 3.75% | 2020 | 271,459 | 271,459 | 86,001 | 86,001 |
| Other | AUD | | 2019 | 12,168 | 12,168 | (8,573) | (8,573) |
| **Total interest bearing liabilities** | | | | **5,467,424** | **5,467,424** | **22,869,034** | **22,869,034** |

## 21 Non-current liabilities - Borrowings (continued)

### (c) Reconciliation of movements of liabilities to cash flows arising from financing activities

| | Liabilities | | Equity | |
|---|---|---|---|---|
| | Loans<br>$ | Finance lease liabilities<br>$ | Share capital<br>$ | Total<br>$ |
| Balance 1 January 2019 | 22,869,034 | - | 181,482,260 | 204,351,294 |
| **Changes from financing cash flows** | | | | |
| Proceeds from issue of share capital | - | - | 29,514,931 | 29,514,931 |
| Proceeds from loans and borrowings | 9,147,040 | - | - | 9,147,040 |
| Repayment of borrowings | (26,548,650) | - | - | (26,548,650) |
| Total changes from financing cash flows | (17,401,610) | - | 29,514,931 | 12,113,321 |
| Balance at 31 December 2019 | 5,467,424 | - | 210,997,191 | 216,464,615 |
| **Liability - related** | | | | |
| Interest expense | (2,801,015) | - | - | (2,801,015) |
| Interest paid | 2,801,015 | - | - | 2,801,015 |
| Total liability-related other changes | - | - | - | - |

| | Liabilities | | Equity | |
|---|---|---|---|---|
| **Consolidated entity** | Loans<br>$ | Finance lease liabilities<br>$ | Share capital<br>$ | Total<br>$ |
| Balance 1 January 2018 | 5,076,838 | 8,150,000 | 181,482,260 | 194,709,098 |
| **Changes from financing cash flows** | | | | |
| Proceeds from loans and borrowings | 25,669,130 | - | - | 25,669,130 |
| Repayment of borrowings | (7,876,934) | - | - | (7,876,934) |
| Payment of finance lease liabilities | - | (8,150,000) | - | (8,150,000) |
| Total changes from financing cash flows | 17,792,196 | (8,150,000) | - | 9,642,196 |
| Balance at 31 December 2018 | 22,869,034 | - | 181,482,260 | 204,351,294 |
| **Liability - related** | | | | |
| Interest expense | (935,575) | (722,198) | - | (1,657,773) |
| Interest paid | 935,575 | 722,198 | - | 1,657,773 |
| Total liability-related other changes | - | - | - | - |

## 22 Non-current liabilities - Provisions

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Employee benefits - long service leave | **378,044** | 314,549 |

## 23 Contributed equity

### (a) Share capital

| | **31 December 2019 Shares** | 31 December 2018 Shares | **31 December 2019 $** | 31 December 2018 $ |
|---|---|---|---|---|
| Ordinary shares | | | | |
| Fully paid | **125,947,977** | 81,085,594 | **210,997,191** | 181,482,260 |

### (b) Movements in ordinary shares:

| **Details** | **Number of shares** | **Total $** |
|---|---|---|
| Opening balance 1 January 2018 | 81,085,594 | 181,482,260 |
| Balance 31 December 2018 | 81,085,594 | 181,482,260 |
| | | |
| Opening balance 1 January 2019 | 81,085,594 | 181,482,260 |
| Shares issued for cash | 44,258,402 | 30,980,882 |
| Shares issued for secured directors loan | 603,981 | 422,787 |
| Less: Transaction costs arising on share issues | - | (1,888,738) |
| Balance 31 December 2019 | 125,947,977 | 210,997,191 |

### (c) Ordinary shares

The Company does not have authorised capital or par values in respect of its issued shares. All issued shares are fully paid. All shares rank equally.

Ordinary shares participate in dividends and the proceeds on winding up of the Company in equal proportion to the number of shares held. At shareholder meetings each ordinary share is entitled to one vote when a poll is called, otherwise each shareholder has one vote on a show of hands. In respect of the Company's shares that are held by the Company, all rights are suspended until those shares are reissued.

The holders of ordinary shares are entitled to receive dividends as declared from time to time, and are entitled to one vote per share at meetings of the Company.

## 24 Reserves

**Foreign currency translation reserve**

Exchange differences relating to translation from functional currencies of the Group’s foreign controlled entities into Australian Dollars are brought to account by entries made directly to the foreign currency translation reserve.

**Other reserves**

Other reserves comprise a share-based payment reserve.

## 25 Remuneration of auditors

During the year the following fees were paid or payable for services provided by the auditor of the parent entity, its related practices and non-related audit firms:

**KPMG**

*(i) Audit and review services*

| | Consolidated entity | |
|---|---|---|
| | **2019** | 2018 |
| | **$** | $ |
| Audit and review of financial statements - Group | **167,214** | 173,756 |
| Audit and review of financial statements - controlled entities | **12,156** | 14,127 |
| Total remuneration for audit and review services | **179,370** | 187,883 |

*(ii) Assurance services*

| | | |
|---|---|---|
| Due diligence services | **28,463** | - |
| Total remuneration for assurance services * | **28,463** | - |

*(iii) Other services*

| | | |
|---|---|---|
| Taxation advice and tax compliance services | **12,156** | 12,156 |
| Technical assistance for subsidiary financial statements | **4,052** | 5,673 |
| Total remuneration for other services | **16,208** | 17,829 |
| | | |
| Total remuneration of KPMG | **224,041** | 205,712 |

* There were no regulatory assurance services provided during the year.

The comparatives include amounts billed in the current period relating to the prior year.

## 26 Commitments

**Capital commitments**

As at 31 December 2019 the Group had capital commitments for equipment of $nil (2018: $nil).

## 27 Related party transactions

### (a) Controlled subsidiary entities

| | Country of incorporation | Class of shares | Equity holding **2019** % | 2018 % |
|---|---|---|---|---|
| *Parent Entity:* | | | | |
| Palla Pharma Limited | Australia | | | |
| *Controlled Entities:* | | | | |
| Purplebay Pty Limited | Australia | Ordinary | **100** | 100 |
| TPI Norway Holding AS | Norway | Ordinary | **100** | 100 |
| TPI Norway AS | Norway | Ordinary | **100** | 100 |

The consolidated financial statements incorporate the assets, liabilities and results of these subsidiaries in accordance with the accounting policy described in note 2(b).

### (b) Key management personnel compensation

The aggregate compensation made to Directors and other members of key management personnel of the Company is set out below:

| | Consolidated entity **31 December 2019** $ | 31 December 2018 $ |
|---|---|---|
| Short-term employee benefits | **1,450,051** | 1,349,904 |
| Post-employment benefits | **84,545** | 78,034 |
| Other long term benefits | **22,795** | 25,264 |
| Share-based payments | **167,981** | 128,491 |
| | **1,725,372** | 1,581,693 |

Further disclosures regarding key management personnel compensation are contained within the Remuneration Report.

### (c) Amounts owing to related parties

Refer to note 21 for details of loans from shareholders.

### (d) Other related party transactions

During 2019 company secretarial and financial reporting services amounting to $4,500 (2018: $9,096) were provided by Corporate and Administrative Services Pty Ltd, a subsidiary of Washington H. Soul Pattinson and Company Limited. Interest and finance expenses during the year attributable to Washington H. Soul Pattinson and Company Limited amounted to $2,741,896 (2018: $917,174).

The following balances were outstanding at the end of the reporting period in relation to these transactions:

| | Consolidated entity **31 December 2019** $ | 31 December 2018 $ |
|---|---|---|
| Corporate and Administrative Services Pty Ltd | **825** | - |

## 27 Related party transactions (continued)

### (e) Loans to related parties

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| *Loans to key management personnel* | | |
| Beginning of the year | **-** | - |
| Loans advanced | **422,787** | - |
| Interest charged | **2,490** | - |
| End of year | **425,277** | - |

### (f) Terms and conditions

Other related party transactions were made on normal commerical terms and conditions and at market rates.

Loans to key management personnel outstanding at the end of the current year include a secured loan to a director of Palla Pharma Limited of $422,787 which was made for a period of 25 years and is repayable on a quarterly amortising reducing balance basis, maturing on 31 December 2044. Interest is payable on this loan at a rate of 5% per annum, payable quarterly. This loan enabled the director to fully participate in the pro-rata Entitlement Offer completed by the Group in November 2019 and is secured against the new shares subscribed to under the offer.

Outstanding balances other than loans to key management personnel are unsecured and are repayable in cash.

## 28 Cash flow information

### (a) Reconciliation of (loss) after income tax to net cash (outflow) from operating activities

| | Consolidated entity | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| (Loss) for the period | **(7,639,443)** | (5,788,409) |
| Adjustment for | | |
| Depreciation expense | **2,470,479** | 2,519,064 |
| Amortisation expense | **43,407** | 32,231 |
| Partnership distribution | **277** | - |
| Net (gain)/loss on sale of non-current assets | **(14,400)** | 232,775 |
| Litigation settlement expense | **1,161,365** | (1,783) |
| Gain on sale of discontinued operation, net of income tax | **-** | (1,119,003) |
| Income tax (benefit)/expense | **(138,193)** | 134,893 |
| Equity-settled share-based payment transactions | **343,633** | 327,497 |
| Change in operating assets and liabilities: | | |
| (Increase) in trade, other receivables and contract assets | **(2,025,329)** | (5,537,606) |
| (Increase) in inventories | **(3,411,722)** | (4,488,767) |
| Decrease/(increase) in prepayments | **1,241,615** | (1,520,753) |
| (Decrease)/increase in trade and other payables | **(1,701,685)** | 73,289 |
| Increase in other provisions | **200,728** | 490,867 |
| Net cash (outflow) from operating activities | **(9,469,268)** | (14,645,705) |

## 28 Cash flow information (continued)

### (b) Non-cash investing activities

During the year, the Group acquired license intangibles of a $1,918,067 with the corresponding entry recorded as a non current payable of $1,563,462 (note 20) and the residual being paid by 31 December 2019.

## 29 Events occurring after the reporting period

On 10 February 2020 the Group announced that it had entered into an option agreement to acquire the shares of its largest customer in the United Kingdom, a manufacturer of codeine phosphate finished dosage products. Simultaneously, the Group also acquired four Market Authorisations from the customer for supply of codeine phosphate based products into the United Kingdom, and on 18 February 2020 the Group acquired a further two codeine phosphate based Market Authorisations from the same customer.

No other matters or circumstances have occurred subsequent to year end that has significantly affected, or may significantly affect, the operations of the Group, the results of those operations or the state of affairs of the Group or economic entity in subsequent financial years.

## 30 Earnings per share

### (a) Reconciliation of earnings used in calculating earnings per share

| | **Consolidated entity** | |
|---|---|---|
| | **31 December 2019 $** | 31 December 2018 $ |
| Net loss used in calculating basic earnings per share: | **7,639,443** | 6,907,412 |
| Net loss used in calculating diluted earnings per share: | **7,639,443** | 6,907,412 |

### (b) Weighted average number of shares used as the denominator

| | **Consolidated entity** | |
|---|---|---|
| | **2019 Number** | 2018 Number |
| Weighted average number of ordinary shares used in calculating basic earnings per share | **88,214,983** | 81,085,594 |
| Weighted average number of ordinary and potential ordinary shares used as the denominator in calculating diluted earnings per share | **88,214,983** | 81,085,594 |

### (c) Information concerning the classification of securities

Fully paid ordinary shares carry the right to participate in dividends and the proceeds on winding up of the Company in equal proportion to the number of shares held. At shareholder meetings each ordinary share is entitled to one vote when a poll is called, otherwise each shareholder has one vote on a show of hands. Fully paid ordinary shares are included as ordinary shares in the determination of basic earnings per share.

No other securities are currently on issue.

## 31 Share-based payments

At 31 December 2019, the Group had the following share-based payment arrangement:

**Share appreciation rights (equity settled)**

The establishment of the Group's Share Appreciation Rights Plan was approved by shareholders at the 2017 annual general meeting.

Each Share Appreciation Right ("SAR") is an equity security that confers on the participant a right to be issued a specified number of the Company's shares, calculated by reference to the increase in market price of the Company's shares over a three year period, but subject to satisfaction of the vesting condition that the participant must be an employee of the Group on the third anniversary of the grant date at the Boards discretion. Share Appreciation Rights are granted under the plan for no consideration and carry no dividend or voting rights. Tranche 1 Share Appreciation Rights are based on employment and Tranche 2 Share Appreciation Rights are based on market prices or the Company's shares.

The fair value of the Share Appreciation Rights at grant date is determined using the Black-Scholes model.

*Measurement of grant date fair values*

The following inputs were used in the measurement of the fair values at grant date of the Share Appreciation Rights granted:

| | SAR's Granted | | | |
|---|---|---|---|---|
| | **2019** | **2019** | **2018** | **2017** |
| | **Tranche 2** | **Tranche 1** | **Tranche 1** | **Tranche 1** |
| Number of SAR's granted | 1,890,697 | 1,160,136 | 800,000 | 1,259,597 |
| Fair value at grant date | $0.001 | $0.250 | $0.330 | $0.620 |
| Grant date | 28 March 2019 | 28 March 2019 | 28 March 2018 | 27 March 2017 |
| Expiry and vesting date | 28 March 2022 | 28 March 2022 | 28 March 2021 | 27 March 2020 |
| Share price at grant date | $1.05 | $1.05 | $1.39 | $2.62 |
| Expected volatility | 30% | 30% | 30% | 30% |
| Risk-free interest rate | 2.5% | 2.5% | 2.5% | 2.5% |
| Expected dividends | nil | nil | nil | nil |

None of the Share Appreciation Rights had vested at 31 December 2019. Total expenses arising from share-based payment transactions recognised during the period as part of employee benefit expenses was $343,633 (2018: $327,497).

Total number of Share Appreciation Rights granted as at 31 December 2019 are 5,110,430.

Expected volatility has been based on an evaluation of the historical volatility of the Company's share price, particularly over the historical period commensurate with the expected term. The expected term of the instruments has been based on historical experience and general option holder behaviour.

## 32 Parent entity financial information

### (a) Summary financial information

The individual financial statements for the parent entity show the following aggregate amounts:

| | **31 December 2019 $** | 31 December 2018 $ |
|---|---|---|
| Balance sheet | | |
| Current assets | **54,608,209** | 46,649,205 |
| Total assets | **87,185,292** | 77,751,744 |
| Current liabilities | **11,727,407** | 27,936,760 |
| Total liabilities | **12,105,451** | 28,251,309 |
| *Shareholders' equity* | | |
| Issued capital | **210,997,191** | 181,482,260 |
| Reserves | **3,711,447** | 3,771,092 |
| (Accumulated losses) | **(139,628,797)** | (135,752,917) |
| Total shareholders' equity | **75,079,841** | 49,500,435 |
| **(Loss) for the year of the parent entity** | **(3,875,880)** | (6,189,898) |
| **Total comprehensive (loss) of the parent entity** | **(3,875,880)** | (6,189,898) |

### (b) Guarantees entered into by the parent entity

The parent entity did not enter any guarantees in relation to the debts of its subsidiaries as at 31 December 2019 or 31 December 2018.

### (c) Contractual commitments for the acquisition of property, plant or equipment

Refer to note 26.

In the directors' opinion:

(a) the consolidated financial statements and notes set out on pages 23 to 73 are in accordance with the *Corporations Act 2001*, including:

(i) complying with Australian Accounting Standards, 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 2019 and of its performance for the financial 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 2(a) confirms that the financial statements 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* for the financial year ended 31 December 2019.

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

Simon Moore

Mr. Simon Moore
Director

Melbourne
27 February 2020

# Independent Auditor's Report

## To the shareholders of Palla Pharma Limited

## Report on the audit of the Financial Report

### Opinion

We have audited the ***Financial Report*** of Palla Pharma Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Group's financial position as at 31 December 2019 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The ***Financial Report*** comprises:

- *Consolidated statement of financial position* as at 31 December 2019
- *Consolidated statement of profit or loss and other comprehensive income, Consolidated statement of changes in equity, and Consolidated statement of cash flows* for the year then ended
- Notes including a summary of significant accounting policies
- *Directors' Declaration.*

The ***Group*** consists of Palla Pharma Limited (the Company) and the entities it controlled at the year end or from time to time during the financial year.

### Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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 are independent of the Group in accordance with *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 fulfilled our other ethical responsibilities in accordance with the Code.

### 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 of the current period.

This matter was 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 this matter.

| **Recoverable amount of plant and equipment and intangibles** | |
|---|---|
| Refer to property, plant and equipment ($26,693,955 Note 15) and intangible assets ($16,967,608 Note 16) to the Financial Report | |
| **The key audit matter** | **How the matter was addressed in our audit** |
| A key audit matter for us was the Group's testing of intangible assets and property, plant and equipment for impairment. The Group has incurred a loss during the year and has a history of operating losses, which increased the judgement applied by us when evaluating the evidence available. The value of these assets is significant at balance date (being 49% of total assets).<br><br>Given the operating losses, this has increased the possibility of intangible assets and property, plant and equipment being impaired, plus the risk of inaccurate forecasts or a wider range of possible outcomes for us to consider.<br><br>Our audit attention focused on assessing the significant judgements the Group applied in their value in use model for the Australian CGU. This model uses forward looking estimations, which can be inherently difficult to determine with precision, and to audit. Key judgements and estimates included the:<br><br>• discount rate applied to the forecast cash flows;<br><br>• forecast cash outflows, in particular, cost of purchases which is influenced by supplier volumes, poppy straw harvesting yields, and other climate-induced volumes;<br><br>• forecast cash inflows which is influenced by forecast customer demand, expected production volumes, sales prices and foreign exchange rates; and,<br><br>• forecast growth rates applied in the Group's value in use model.<br><br>We involved valuation specialists to supplement our senior audit team members in assessing this key audit matter. | Our procedures included:<br><br>• We considered the appropriateness of the value in use method applied by the Group to perform the test of intangible assets and property, plant and equipment for impairment against the requirements of the accounting standards.<br><br>• We assessed the integrity of the value in use models used, including the accuracy of the underlying calculation formulas.<br><br>• We considered the sensitivity of the Group's model by varying key assumptions, such as the foreign exchange rates and the discount rate, within a reasonably possible range. We did this to identify those CGUs at higher risk of impairment and to focus our further procedures.<br><br>• We compared the forecast cash flows contained in the value in use model to Board approved forecasts.<br><br>• We assessed the accuracy of previous Group forecasts to inform our evaluation of forecasts incorporated in the model.<br><br>• We checked the key judgements and estimates for evidence of detailed review and approval by the Directors.<br><br>• We challenged the significant forecast cash flows and growth assumptions given the operating losses. We compared key events to the Board approved plan and strategy. We compared forecast growth rates to published studies of industry trends and expectations, and considered differences for the Group's operations. We used our knowledge of the Group, their past performance, business and customers, and our industry experience. In addition:<br><br>- We compared the forecast cash inflows, which is influenced by expected production volumes to the Group's production plans and forecast customer demand. We compared the sales |

| | |
|---|---|
| | prices to historically achieved prices as per underlying accounting records.<br>- Working with our valuation specialists we compared the forecast foreign exchange rates to published views of market commentators on future trends.<br>- We compared the forecast cash outflows to the previous year’s achieved poppy straw harvesting yields, supplier and other climate-induced volumes.<br>• Working with our valuation specialists, we independently developed an acceptable range of discount rates based on market data for comparable entities, adjusted by risk factors specific to the Group.<br>• We assessed the disclosures in the financial report using our understanding obtained from our testing and against the requirements of the accounting standards. |

## Other Information

Other Information is financial and non-financial information in Palla Pharma Limited’s annual reporting which is provided in addition to the Financial Report and the Auditor’s Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we 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.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor’s Report we have nothing to report.

## Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error
- assessing the Group and Company's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters

related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Group and Company or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- 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 *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They 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_responsibilities/ar1.pdf. This description forms part of our Auditor's Report.

## Report on the Remuneration Report

### Opinion

In our opinion, the Remuneration Report of Palla Pharma Limited for the year ended 31 December 2019, complies with *Section 300A of the Corporations Act 2001*.

### Directors' 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 responsibilities

We have audited the Remuneration Report included in *pages 10 to 18* of the Directors' report for the year ended 31 December 2019.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with *Australian Auditing Standards*.

KPMG

KPMG

Tony Batsakis
*Partner*
Melbourne

27 February 2020

The shareholder information set out below was applicable as at 14 February 2020.

### A. Distribution of equity securities

Analysis of numbers of equity security holders by size of holding:

| Holding | Class of equity security Ordinary shares |
|---|---|
| 1 - 1000 | 334 |
| 1,001 - 5,000 | 537 |
| 5,001 - 10,000 | 241 |
| 10,001 - 100,000 | 489 |
| 100,001 and over | 91 |
| | 1,692 |

There were 166 holders of less than a marketable parcel of ordinary shares.

### B. Equity security holders

*Twenty largest quoted equity security holders*

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

| Name | Ordinary shares | |
|---|---|---|
| | Number held | Percentage of issued shares |
| Washington H. Soul Pattinson and Company Limited | 25,040,465 | 19.9 |
| UBS Nominees Pty Ltd | 23,489,809 | 18.7 |
| Sandhurst Trustees Ltd | 10,664,711 | 8.5 |
| National Nominees Limited | 10,005,876 | 7.9 |
| JP Morgan Nominees Australia Limited | 3,969,361 | 3.2 |
| Colinton Investments Pty Ltd | 2,963,895 | 2.4 |
| Skylights Pty Ltd | 2,906,714 | 2.3 |
| Sico Holdings Pty Ltd | 2,740,741 | 2.2 |
| Sky Lights Pty Ltd | 2,173,024 | 1.7 |
| HSBC Custody Nominees (Australia) Limited | 1,908,772 | 1.5 |
| Gaspard Boot | 1,498,000 | 1.2 |
| Jarrod Ritchie & Catrina Ritchie | 1,381,177 | 1.1 |
| Bond Street Custodians Limited | 1,298,729 | 1.0 |
| Gowing Bros Limited | 1,064,914 | 0.8 |
| Ian Lindeman Pty Ltd | 850,001 | 0.7 |
| Langburgh Pty Ltd | 723,173 | 0.6 |
| Mr Jarrod David Ritchie | 703,587 | 0.6 |
| Radiata Investments Pty Ltd | 701,060 | 0.6 |
| Citicorp Nominees Pty Limited | 582,525 | 0.5 |
| Australian Philanthropic Services Foundation Pty Ltd | 500,000 | 0.4 |
| | 95,166,534 | 75.8 |

### C. Substantial shareholders

The Company's Holders of Relevant Interests as notified by ASX Substantial Shareholders and the number of shares in which they have an interest as disclosed by notices received under Part 6.7 of the *Corporations Act 2001* as at 14 February 2020 are listed below:

| Name | Ordinary Shares | Percentage |
|---|---|---|
| Washington H. Soul Pattinson and Company Limited & Brickworks Limited | 25,040,465 | 19.9% |
| Thorney Opportunities Limited & TIGA Trading Pty Limited | 23,489,809 | 18.7% |
| Wentworth Williamson Management Pty Ltd | 10,664,711 | 8.5% |
| Sico Holdings Pty Ltd ATF Oranje Trust and associates | 8,361,889 | 6.6% |
| National Nominees Ltd ACF Australian Ethical Investment Limited | 7,987,076 | 6.3% |

### D. Voting rights

The voting rights attaching 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 upon a poll each share shall have one vote.