

PhotonGroup 

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Following the recent completion of the recapitalisation proposal Photon has an improved capital structure which will allow it to better serve its clients and meet its strategic objectives, which include completing the operational restructure, continuing to support new business opportunities and exploring organic expansion of key international brands.



Chairman's Report

2010 proved to be a challenging year for Photon Group, however the activities of the last few months have established a solid platform for the coming year and beyond.

Trading Performance

Photon experienced a disappointing financial result in FY2010 driven by one-off costs, losses associated with discontinued businesses and a non-cash impairment of intangible assets. FY2010 EBITDA and FY2010 NPAT were approximately \$46.7 million and \$(87.4) million respectively after one-off costs, losses associated with discontinued businesses and non-cash impairment charges relating primarily to the search marketing segment (which together aggregated to a negative impact of \$108.4 million after tax). Excluding the impact of the one-off costs normalised EBITDA was approximately \$75 million and normalised NPAT was \$21 million.

The underperformance of the internet & e-commerce division was primarily attributable to losses in the Geekdom and Geekversity businesses which have now been closed and sold respectively. The aggregate normalised FY2010 EBITDA of the other four operating divisions was positive on the prior year on a common currency basis.

Recapitalisation Proposal

In addition there was a material increase in the deferred consideration liabilities. As a result of this, Photon conducted a strategic review which considered a broad range of options to reduce existing drawn debt and manage deferred consideration liabilities. This review resulted in the recapitalisation proposal which included a restructure of deferred consideration liabilities, a refinance of Photon's debt facilities for three years and completing an equity raising of \$102.5 million through an underwritten placement and shareholder offer.

The recapitalisation proposal was approved by shareholders at a general meeting on 17 September 2010 and completed on 29 September 2010. The effect of the restructure proposal is that it enabled Photon to pay deferred consideration payments due in September 2010 and to be in compliance with its debt facilities.

Strategic Objectives

The Board believes the recapitalisation proposal has provided Photon with an improved capital structure to allow Photon to better serve its clients and meet its strategic objectives. Photon has many projects currently underway to meet its strategic objectives of completing the operational restructure, continuing to support new business opportunities and exploring organic expansion of key international brands. Growth via acquisition will not be the focus of Photon.

Corporate Governance

During the year, we proactively looked at ways to enhance corporate governance. Jeremy Philips was appointed CEO from June 2010. Tim Hughes resigned from the Board on 11 August 2010 and Paul Gregory will not be standing for re-election at this year's AGM. Photon intends to appoint three new independent, non-executive Directors to the Board. One of the new independent non-executive Directors will become the non-executive Chairman. In line with ASX guidelines, following these appointments we will maintain a majority of independent directors. We are working to finalise this process as quickly as possible.

Through this challenging time, our people have played a major role in ensuring Photon's future success. I would like to take this opportunity to personally thank our employees, clients and shareholders for their continued support. The quality of our underlying businesses, together with the commitment and determination of our employees, will position us well for the future. I look forward to bringing you further updates on the Company's progress as the coming year unfolds.



Brian Bickmore / Chairman

2010 proved to be a challenging year for Photon Group, however the activities of the last few months have established a solid platform for the coming year and beyond.

Chief Executive Officer's Report

Since joining Photon in June 2010, a large amount of my time has been spent working on our recapitalisation. The approval of the recapitalisation proposal by shareholders on 17 September 2010 marked the close of a difficult stage for all Photon stakeholders. I greatly regret the loss suffered by shareholders and appreciate the patience and support of our employees, shareholders, clients and other stakeholders. This support has been essential to completing this process while continuing to deliver high quality work for our clients.

FY2010 Performance Summary

Photon's businesses include leading creative agencies, field marketing services, specialised communications firms and search advertising. The majority of our business is in Australia, with our international businesses accounting for about 28% of our revenues.

Photon's businesses are exposed to a broad spectrum of marketing spend including traditional above-the-line advertising, below-the-line advertising and sales force outsourcing. Photon has a diverse client base with our top 10 clients representing 25% of net revenue in FY2010. Our clients operate in a broad range of industries with a majority of net revenues coming from industries such as FMCG, beverages, telecommunications and consumer banking. In FY2010, 28% of net revenues were generated outside Australia.

Since joining Photon in June 2010, a large amount of my time has been spent working on our recapitalisation. The approval of the recapitalisation proposal by shareholders on 17 September 2010 marked the close of a difficult stage for all Photon stakeholders.

Strategic Intelligence: Normalised EBITDA was up 4% in FY2010 on the prior period on a constant currency basis; continued declines in the market research sector and a weaker performance in the 2H2010 by Naked Communications were offset by margin improvements across the division.

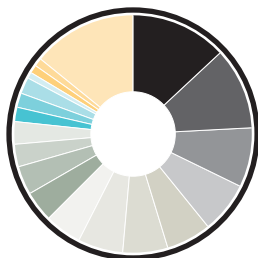
Integrated Communications and Digital: Normalised EBITDA growth of 14% in FY2010 over the prior period was a result of continuing strong growth in our two large Australian integrated agencies, BWM and BMF.

Field Marketing: Normalised EBITDA was down 9% in FY2010 on a common currency basis off a strong prior period result due substantially to budget constraints from certain international clients and margin pressure in the demonstrations market.

Internet and E-Commerce: Normalised EBITDA was down 47% in FY2010 as a result of the impact of the material losses made by the Geekdom and Geekversity businesses which were closed and sold respectively during the 12 month period to 30 June 2010, and the abnormal impairment of working capital within the division. The balance of the underperformance was largely driven by the declines in earnings performance of the search engine marketing businesses.

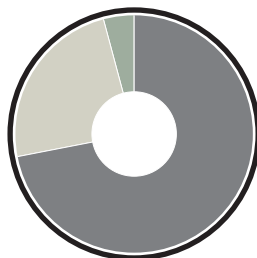
Specialised Communications: Normalised EBITDA was up 8% in FY2010 on the prior period on a common currency basis, with strong earnings performance from the European public relations agencies, Hotwire and Frank PR; margin improvements due to operational efficiency; and some recovery in the corporate communications and experiential agencies.

Net revenue by industry



FMCG – Food	13%
Telecommunications	11%
FMCG – General	8%
FMCG – Beverages	7%
Banking Finance Insurance	6%
Retail – Consumer Goods	6%
Electronics and IT	6%
Alcohol and Tobacco	5%
Media and Entertainment	4%
Retail – Groceries/Mass Merchants	4%
Internet	3%
Government, Education, Health, Non-Profit Org	3%
Professional Services	2%
Manufacturing, Industrial and Automotive	2%
Pharmaceuticals	2%
Property and Construction	1%
Travel, Tourism and Transport	1%
Energy, Oil and Mining	1%
Unallocated	15%

Net revenue by geography



Australia, New Zealand and Asia	72%
United Kingdom and Europe	24%
North America	4%

Operational Restructure

The operational restructure announced in June 2010 is well underway. The aim is to reduce complexity and better exploit the strengths of the businesses across the group. It will drive greater collaboration, better leverage management expertise and improve operational efficiencies.

Since July 2010 a number of key businesses have been being brought together to form bigger, stronger businesses. The BellamyHayden team has joined Naked Australia to form a highly awarded strategic and creative agency. UK-based Likemind and Corporate Edge have merged to form a corporate brand and communications consultancy operating under the Corporate Edge banner. The Adpartners business has joined leading integrated agency, BWM. When I joined on 1 June 2010 we had approximately 45 stand-alone business units. We will reduce that by at least 25% by the end of December 2010.

These changes will create a stronger foundation for the future. In the immediate term we are working to minimise the disruption. We are working hard to make it easier for all members of the Photon group to work together to deliver better results to our clients and best take advantage of the deep pool of talent we have within the company. We look forward to keeping shareholders updated on our progress throughout the year.

Jeremy Phillips / Chief Executive Officer

Board of Directors



Brian Bickmore
Independent Chairman

Brian was appointed as a Non-Executive Director of the Company with effect from 25 March 2004 and was appointed Chairman on 1 July 2010. In 1980, Brian was a founding executive of Austereo and served as a Director of that company for almost 25 years until 2004. Brian was initially Austereo's Finance Director and, from 1997, was the Group General Manager. He is also a Director of oOH! Media Group Limited. Brian was previously a director of RG Capital Radio Limited. Brian is the Chairman of both the Audit Committee and the Remuneration Committee.



Susan McIntosh
Non-executive Director

Susan was appointed as a Director with effect from 2 June 2000. A Chartered Accountant, Susan has more than 25 years business experience in media (radio and television production and distribution) and asset management. She is also the Managing Director of RG Capital Holdings (Australia) Pty Ltd. Susan is a member of the Audit Committee.



Paul Gregory
Independent Non-executive Director

Paul was appointed as a Director of the Company with effect from 25 March 2004. He has led a diverse range of medium-sized private retail companies, including Australian Geographic Pty Ltd and Red Earth Australia Pty Ltd, and has overseen the expansion of both companies in Australia and overseas. Currently, Paul is a business consultant providing management and strategic advice to several Australian and international retail groups. He is a member of the Audit Committee.

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Corporate Governance Statement

This statement outlines the corporate governance policies and practices of Photon, in the context of the Corporate Governance Principles and Recommendations that have been set by the ASX Corporate Governance Council (**ASX Guidelines**). Since the listing of Photon on 30 April 2004, the Board has continually considered and reviewed the corporate governance practices and policies of Photon.

The table below sets down each of the recommendations made in the ASX Guidelines and indicates where the relevant disclosure can be found in this report. Photon considers that its governance practices are consistent with all but three of the Recommendations contained in the ASX Guidelines. The Chair of Photon is not an independent Director (Recommendation 2.2) and a majority of the Board members are not independent Directors (Recommendation 2.1). Photon also has not established a formal Nomination Committee at this time (Recommendation 2.4). An explanation for the departure from these ASX Recommendations is provided in the Corporate Governance Statement.

A copy of the ASX Guidelines can be obtained from the ASX website www.asx.com.au

Recommendation		Section
Recommendation 1.1	Functions of the Board and Senior Executives	1.1
Recommendation 1.2	Evaluation of Senior Executives	1.2 and Remuneration Report
Recommendation 1.3	Reporting on Principle 1	1.1, 1.2 and Remuneration Report
Recommendation 2.1	Independent Directors	2.1 and Director's Report
Recommendation 2.2	Independent Chair	2.2
Recommendation 2.3	Role of the Chair and CEO	2.3
Recommendation 2.4	Establishment of Nomination Committee	2.4
Recommendation 2.5	Performance evaluation of the Board, Committees and Directors	2.5 and Remuneration Report
Recommendation 2.6	Reporting on Principle 2	2.1, 2.2, 2.3, 2.4, 2.5, Director's Report and Remuneration Report
Recommendation 3.1	Company Code of Conduct	3.1
Recommendation 3.2	Company Security Trading Policy	3.2
Recommendation 3.3	Reporting on Principle 3	3.1, 3.2
Recommendation 4.1	Establishment of Audit Committee	4.1
Recommendation 4.2	Structure of Audit Committee	4.2, Director's Report and Director Profiles
Recommendation 4.3	Audit Committee Charter	4.3
Recommendation 4.4	Reporting on Principle 4	4.1, 4.2, 4.3, Director's Report and Director Profiles
Recommendation 5.1	Policy for compliance with continuous disclosure	5.1
Recommendation 5.2	Reporting on Principle 5	5.1
Recommendation 6.1	Communications strategy	6.1
Recommendation 6.2	Reporting on Principle 6	6.1
Recommendation 7.1	Policies on risk oversight and management	7.1
Recommendation 7.2	Risk management roles and responsibilities	7.1 and 7.2
Recommendation 7.3	Statement of CEO and CFO in relation to systems	7.3
Recommendation 7.4	Reporting on Principle 7	7.1, 7.2 and 7.3
Recommendation 8.1	Establishment of remuneration committee	8.1 and Director Profiles
Recommendation 8.2	Executive and Non-Executive Director remuneration	8.2, Director's Report and Financial Statements
Recommendation 8.3	Reporting on Principle 8	8.1, 8.2, Director Profiles, Director's Report and Financial Statements

Principle 1: Lay solid foundations for management and oversight

1.1 Functions of the Board and management

1.1.1 Role of the Board and management

The Board has approved a formal Board Charter, which details the Board's role, powers, duties and functions. A copy of the Board Charter is available on the Photon website.

In general, the Board is responsible for, and has the authority to determine, all matters relating to the policies, practices, management and operations of the Consolidated Entity. It is required to do all things that may be necessary to be done, in order to carry out the objectives of the Consolidated Entity.

Without intending to limit this general role of the Board, the principal functions and responsibilities of the Board include the following.

1. Leadership of the Organisation: overseeing the Consolidated Entity and establishing codes that reflect the values of the Company and guide the conduct of the Board, management and employees.
2. Strategy Formulation: working with senior management to set and review the overall strategy and goals for the Company.
3. Overseeing Planning Activities: overseeing the development of the Consolidated Entity's strategic plan and approving that plan as well as the annual and long-term budgets.
4. Shareholder Liaison: ensuring effective communications with shareholders through an appropriate communications policy and promoting participation at general meetings of the Company.
5. Monitoring, Compliance and Risk Management: overseeing the Company's management of material business risks, compliance, control and accountability systems and monitoring and directing the financial and operational performance of the Company.
6. Company Finances: approving expenses in excess of those approved in the annual budget and approving and monitoring acquisitions, divestitures and financial and other reporting.
7. Human Resources: appointing, and, where appropriate, removing the Chief Executive Officer (CEO) and Executives as well as reviewing the performance of the CEO and monitoring the performance of senior Executives in their implementation of the Company's strategy.
8. Ensuring the Health, Safety and Wellbeing of Employees: in conjunction with the senior management team, developing, overseeing and reviewing the effectiveness of the Company's occupational health and safety systems to ensure the wellbeing of all employees.
9. Delegation of Authority: other than as specifically reserved to the Board in the Board Charter,

responsibility for the management of Photon's business activities is delegated to the CEO who is accountable to the Board. The Board has also delegated specific authorities to various Board Committees.

1.1.2 Conflicts of interest

Directors must:

- disclose to the Board actual or potential conflicts of interest that may or might reasonably be thought to exist between the interests of the Director and the interests of any other parties in carrying out the activities of the Consolidated Entity; and
- if requested by the Board, within seven days or such further period as may be permitted, take such necessary and reasonable steps to remove any conflict of interest.

If a Director cannot or is unwilling to remove a conflict of interest, then the Director must, as per the *Corporations Act*, absent himself or herself from the room when discussion and/or voting occurs on matters about which the conflict relates.

1.1.3 Related party transactions

Related party transactions include any financial transaction between a Director and the Consolidated Entity and will be reported in writing to each Board meeting. Unless there is an exemption under the *Corporations Act* from the requirement to obtain shareholder approval for the related party transaction, the Board cannot approve the transaction.

1.2 Evaluation of senior Executives

1.2.1 Induction of senior Executives

New Executives undertake an induction program upon joining Photon, including comprehensive briefings on the Company's businesses, and its policies and procedures. The program includes meetings with people in key internal and external roles in order to start developing the relationships necessary to meet the requirements of their role.

As discussed further below and in the Remuneration Report, key performance indicators are agreed with each Executive to ensure goals and performance measures are fully understood and disclosed.

1.2.2 Performance evaluation of senior Executives

The performance evaluation of key Executives is undertaken by the Board, in conjunction with the CEO on both a formal regular and informal ongoing basis. Each senior Executive's performance is reviewed at least annually. Performance evaluation of senior Executives has taken place during the reporting period in accordance with the process disclosed.

Corporate Governance Statement

The process for evaluating the performance of senior Executives and the remuneration policy for senior Executives is further discussed in the Remuneration Report.

Principle 2: Structure the Board to add value

2.1 Independent Directors

The constitution of the Company provides that the number of Directors must not be less than three and not more than 13. The names of the Directors of the Company in office at the date of this report are set out in the Directors' Report on page 15 of this report, including the period of office held by each Director as at the date of this report. There are currently three Directors each of whose skills, experience and expertise is described in their Director profiles on page 15. There are no Executive Directors and three Non-Executive Directors (Susan McIntosh, Brian Bickmore and Paul Gregory).

The Board meets the ASX Corporate Governance Council's recommendation that a majority of the Board should be independent. Two members of the Board, Brian Bickmore and Paul Gregory, are independent according to the definition in the ASX Guidelines. Susan McIntosh is not considered independent because she is an officer of the RG Capital group of companies, which have a substantial holding in Photon. The Board believes that its current composition has the required skills and independence of thought and judgement to ensure that decisions are made by the Board in the best interests of the Company.

The Board regularly assesses whether each Non-Executive Director is independent, based on the criteria specified in the Board Charter (which is consistent with the criteria set out in Recommendation 2.1 of the ASX Guidelines).

The Board does not have a formal procedure for Directors to take professional advice at the expense of the Company, however the Directors have the ability to do so.

2.2 Independent Chair

The Chair of Photon, Brian Bickmore, is a Non-Executive Director and an independent Director. This meets with the ASX Recommendation that the Chairman should be an independent Director. Brian Bickmore assumed the role of Chair on 1 July 2010 on the resignation of Tim Hughes. Brian Bickmore was also Chairman of the Audit Committee during the year. The Board considered that Brian Bickmore was the best Director to discharge the requirements of these roles given the size and composition of the Board.

2.3 Role of the Chair and CEO

The roles of Chair and CEO are not exercised by the same individual and the division of responsibilities between the Chair and the CEO have been agreed by the Board.

2.4 Establishment of Nomination Committee

The Board has determined that due to the relative size of Photon it is not necessary or appropriate for a Nomination Committee to be established at this time. The Board will continue to revisit this question on an ongoing basis as the Company continues to grow. In addition, a number of the responsibilities identified by the ASX Guidelines as being within the ambit of a Nomination Committee have been delegated to the Remuneration Committee.

2.5 Performance evaluation of the Board, Committees and Directors

2.5.1 Induction and education

New Directors undergo an induction process in which they are given a full briefing on the Consolidated Entity. This includes meetings with key Executives, tours of the premises, an induction package and presentations. Information conveyed to new Directors include:

- formal policies on Director appointments as well as conduct and contribution expectations;
- details of all relevant legal requirements;
- a copy of the Board Charter;
- guidelines on how the Board processes function;
- details of past, recent and likely future developments relating to the Board, including anticipated regulatory changes;
- background information on and contact information for key people in the organisation, including an outline of their roles and capabilities;
- an analysis of the Consolidated Entity;
- a synopsis of the current strategic direction of the Company including a copy of the current strategic plan and annual budget; and
- a copy of the Constitution of the Company.

2.5.2 Performance review

The Chair is responsible, in the first instance, for monitoring the contribution of individual Directors, and providing guidance on any areas of improvement.

The Board undertakes an annual self assessment of both its collective performance and that of individual Directors and seeks specific feedback from the senior management team on particular aspects of its performance. The Remuneration Committee establishes procedures and oversees this annual performance assessment program.

In addition, each Board Committee undertakes an annual self assessment on the performance of the committee and achievement of committee objectives. The performance of the CEO is reviewed annually by the Remuneration Committee and the Board. The performance of the CEO is reviewed annually against set performance goals and competencies. Performance evaluation of the Board, its committees and Directors has taken place during the reporting period in accordance with the process disclosed.

2.6 Retirement and re-election

As required under Photon's Constitution and the ASX Listing Rules, and excluding any managing Director or Director newly appointed during the relevant year, at each Annual General Meeting one-third of the Directors must retire from office. Retiring Directors are eligible for re-election by shareholders.

No Director (other than the Managing Director) may hold office for more than three years without standing for re-election and any Director appointed by the Board since the previous Annual General Meeting must stand for election by no later than the next Annual General Meeting.

2.7 Appointment of new Directors

When a vacancy exists for a Board position, through whatever cause, or where the Board considers that it would benefit from the services of a new member with particular skills, the Board will consider candidates having regard to:

- what may be appropriate for the Company;
- the skills, expertise and experience of the candidates;
- the desirability of those skills, expertise and experience when combined with those of the existing Directors; and
- the perceived compatibility of the candidates with the Company and with the existing Directors.

Potential candidates to be appointed as Directors will be considered by the Board. The Board will appoint the most suitable candidates who (assuming that they consent to act as Directors) continue in office only until the next annual general meeting and are then eligible for election.

The terms and conditions of the appointment of all new members of the Board must be specified in a letter of appointment to be signed by the Chair with the authority of the Board.

Principle 3: Promote ethical and responsible decision making

3.1 Company Code of Conduct

To assist the Board in carrying out its functions, Photon has developed a Code of Conduct to guide the Directors, the CEO and other key Executives in the performance of their roles. The Company Code of Conduct was adopted by resolution of the Board on 27 May 2004. This Code includes the following:

Responsibilities to shareholders and the financial community generally

The Company complies with the spirit, as well as the letter of all laws and regulations that govern shareholders' rights. The Company has processes in place designed to ensure the truthful and factual presentation of the Company's financial position and prepares and maintains its accounts fairly and accurately in accordance with the generally accepted accounting and financial reporting standards.

Responsibilities to clients, customers and consumers

Each employee has an obligation to use their best efforts to deal in a fair and responsible manner with each of the Company's suppliers and customers.

Employment practices

The Company endeavours to ensure that its employees maintain the highest standard of conduct at all times and to provide an environment in which there is equal opportunity for all employees at all levels of the Company. The Company does not tolerate the offering or acceptance of bribes or the misuse of Company assets or resources.

Obligations relative to fair trading and dealing

The Company aims to conduct its business fairly and to compete ethically and in accordance with relevant laws. The Company strives to deal fairly with the Company's customers, suppliers, competitors and other employees and encourages its employees to strive to do the same.

Conflicts of interest

Employees and Directors must avoid conflicts as well as the appearance of conflicts between personal interests and the interests of the Company.

Compliance with legislation affecting its operations

Directors, officers and senior Executives of the Company and all operating entities are responsible for setting up and maintaining a system of internal controls, financial and otherwise, in order to provide reasonable assurance of effective and efficient operations, reliable financial information and reporting, and compliance with laws and regulations.

How the Company monitors and ensures compliance with its Code

The Board, management and all employees of the Company are committed to implementing this Code of Conduct and each individual is accountable for such compliance. Disciplinary measures may be imposed for violating the Code.

A copy of the Code is available on the Photon website.

3.2 Company Securities Trading Policy

Photon has a Securities Trading Policy under which Directors, senior Executives and other employees likely to be in possession of unpublished price-sensitive information and their associates may not trade in Photon securities during the following "blackout periods" commencing:

- 31 December each year until the release by Photon of its half-yearly results to the ASX in February; and
- 30 June each year until the release by Photon of its annual results to the ASX in August.

In addition, consistent with the law, designated officers are prohibited from trading in Photon's securities while in the possession of unpublished price-sensitive information concerning the Consolidated Entity. Unpublished price-sensitive information is information regarding the Consolidated Entity, of which the market is not aware, that a reasonable person would expect to have a material effect on the price or value of Photon's securities.

Notice of an intention to trade must be given to the Company Secretary prior to trading in the Company's securities. The completion of any such trade by a Director must also be notified to the Company Secretary who in turn advises the ASX.

Corporate Governance Statement

A copy of the Securities Trading Policy is available on the Photon website.

Principle 4: Safeguard integrity in financial reporting

4.1 Establishment of Audit Committee

The Audit Committee monitors and reviews the effectiveness of the Consolidated Entity's controls in the areas of operational and balance sheet risk, legal, compliance and financial reporting. The committee discharges these responsibilities by:

- overseeing the adequacy of the controls established by senior management to identify and manage areas of potential risk and to safeguard the assets of Photon;
- overseeing Photon's relationship with the external auditor and the external audit function generally; and
- evaluating the processes in place to ensure that accounting records are properly maintained in accordance with statutory requirements, and financial information provided to investors and the Board is accurate and reliable.

The Audit Committee has also adopted a policy on the provision of non-audit services, and complies with the statutory requirements regarding the rotation of external audit personnel. All non-audit services were subject to the corporate governance procedures adopted by the company and have been reviewed by the audit committee to ensure they do not impact the integrity and objectivity of the auditor. 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 Company, acting as an advocate for the Company or jointly sharing risks and rewards.

Members of management and the external auditors attend meetings of the committee by invitation. The committee may also have access to financial and legal advisors, in accordance with the Board's general policy.

4.2 Structure of Audit Committee

The Audit Committee consists only of Non-Executive Directors, including a majority of independent Directors. The current members of the Audit Committee are Mr Brian Bickmore, Ms Susan McIntosh and Mr Paul Gregory. Brian Bickmore is the independent Chair of this committee. All members can read and understand financial statements and are otherwise financially literate. The details of the member's qualifications can be found in their Director profiles on page 15.

Details of the number of meetings of the Audit Committee and the names of attendees can be found in the Directors' Report on page 16. The Audit Committee meets with an external auditor at least twice a year.

4.3 Audit Committee Charter

The Audit Committee Charter sets out the Committee's role and responsibilities, structure, membership requirements and procedures. The committee meets at least four times each year and reports to the Board on all matters within its role and responsibilities.

The Audit Committee reviews the audited annual and half yearly financial statements and other reports which accompany published financial statement before submission to the Board and recommends their approval.

The Audit Committee also recommends to the Board the appointment of the external auditor each year, reviews the appointment of the external auditor, their independence, the audit fee, and any question of resignation or dismissal.

The Audit Committee is also responsible for establishing policies on risk oversight and management.

A copy of the Charter is available on the Photon website.

Principle 5: Make timely and balanced disclosure

5.1 Policy for compliance with continuous disclosure

Photon has established a Continuous Disclosure Plan to ensure compliance with the ASX Listing Rule disclosure requirements.

The Board has designated the Company Secretary as the person responsible for overseeing and coordinating disclosure of information to the ASX as well as communicating with the ASX. In accordance with the ASX Listing Rules, the Company immediately notifies the ASX of information:

- concerning the Company that a reasonable person would expect to have a material effect on the price or value of the Company's securities; and
- that would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose of the Company's securities.

A copy of the Company's Continuous Disclosure Plan is available on the Photon website.

Principle 6: Respect the rights of shareholders

6.1 Communications strategy

To facilitate the effective exercise of the rights of shareholders, the Company is committed to ensuring that all external communications with shareholders will:

- be factual;
- not omit material information; and
- be timely and expressed in a clear and concise manner.

Where practicable, Photon uses the latest widely available electronic technology to communicate openly with shareholders and the market in general. Announcements to the ASX and notices of meetings are posted on the Company's website and retained there for at least three years.

The Company encourages shareholders to participate in general meetings of the Consolidated Entity. The Company seeks to choose a date, venue and time for the Annual General Meeting that is convenient to the greatest number of its shareholders, and takes reasonable measures to ensure the attendance of the external auditor to answer questions from shareholders about the conduct of the audit and the preparation and content of the auditor's report.

The Company also makes available a telephone number and email address for shareholders to make enquiries of the Consolidated Entity.

Principle 7: Recognise and manage risk

7.1 Policies on risk oversight and management

Photon recognises that identification and effective management of risk is viewed as an essential part of good corporate governance and the Company's approach to creating long-term shareholder value.

Photon has therefore established and implemented the Risk Management Policy designed to identify and respond to risks in a way that creates value for Photon shareholders and to allow the Company to meet its long-term growth objectives. The Risk Management Policy includes specific risk management activities in core areas of risk for the Consolidated Entity, including: operational, financial reporting and compliance risks.

The Risk Management Policy, adopted by the Company includes:

- process for identification of the material business risks faced by the Company;
- prioritisation of material business risks;
- where the level of risk is greater than the risk tolerance, identification of controls to manage the risk; and
- ongoing reporting and discussion of material business risks throughout the year.

Risk management is a key element of Photon's strategic planning and decision-making. Photon strives to balance the risks and rewards in conducting business to optimise returns, in accordance with its goals of delivering shareholder value and its commitments to stakeholders, customers and the broader community.

7.2 Risk management roles and responsibilities

Management, through the CEO, is responsible for designing, implementing and reporting on the adequacy of the Company's risk management and internal control system. Management reports to the Audit Committee on the Company's key risks and the extent to which it believes these risks are being managed. This is performed on an annual basis or more frequently as required by the Board.

The Board is responsible for satisfying itself annually, or more frequently as required, that management has developed and implemented a sound risk management and internal control system. Detailed work on this task is delegated to the Audit Committee and reviewed by the Board. The Audit Committee also oversees the adequacy of the Company's risk reporting from management.

Strategic and operational risks are reviewed at least annually by all operating divisions as part of the annual strategic planning and budgeting process. Division risk profiles are also reviewed quarterly as part of the regular reporting to the Board. The CEOs of the Company's subsidiaries and managing Directors of the Company's divisions are required to report to the Board each month on operational risks. These are then reviewed by the CEO, CFO and General Counsel each month and external auditors as part of the half-yearly reporting to the market.

The General Counsel monitors the Company's compliance with its legal and regulatory obligations. Senior management meet regularly to deal with specific areas of risk, such as treasury risk, exposure to interest rates and

foreign exchange rates, and provides reporting to the Board on these areas at least annually.

The Company will provide updates to any changes in its circumstances in press releases on the investor section of the Company's website.

7.3 Statement of CEO and CFO in relation to systems

The Board has received assurance from the CEO and the CFO that the declaration provided by them in accordance with section 295A of the *Corporations Act* is founded on a sound system of risk management and internal control and that, in their opinion, the Company's Risk Management System is operating effectively in all material respects in relation to financial reporting risks.

The Board notes that due to its nature, internal control assurance from the CEO and CFO can only be reasonable rather than absolute. This is due to such factors as the need for judgement and because much of the evidence available is persuasive, rather than conclusive, and therefore is not and cannot be designed to detect all weaknesses in control procedures.

Principle 8: Remunerate fairly and responsibly

8.1 Establishment of Remuneration Committee

The Remuneration Committee was formed by resolution of the Board on 25 March 2004. The Remuneration Committee has established a Charter, a copy of which is available on the Company's website.

8.1.1 Role

The Remuneration Committee reviews and makes recommendations to the Board on remuneration packages and policies including but not limited to succession planning, recruitment and the appointment of the CEO, senior Executives and Directors themselves and overseeing succession planning, selection and appointment practices and remuneration packages for management and employees of Photon.

The objectives of the Committee include to:

- review, assess and make recommendations to the Board on the desirable competencies of the Board;
- assess the performance of the members of the Board;
- oversee the selection and appointment practices for Non-Executive Directors and senior management of Photon;
- develop succession plans for the Board and oversee the development of succession planning in relation to senior Executives; and
- assist the Board in determining appropriate remuneration policies.

Corporate Governance Statement

8.1.2 Composition

Brian Bickmore and Susan McIntosh are the current members of the Remuneration Committee, who are both independent Directors. Brian Bickmore, the Chair of the Remuneration Committee, is an Independent Director. Tim Hughes was a member of the Remuneration Committee up until his resignation as Executive Chairman on 1 July 2010. Paul Gregory was a member of the Remuneration Committee during the year and resigned as a member on 25 June 2010.

Details of the number of meetings of the Remuneration Committee and the names of the attendees can be found in the Directors' Report on page 16.

8.1.3 Responsibilities

The responsibilities of the Remuneration Committee include setting policies for senior officers' remuneration, setting the terms and conditions of employment for the CEO, reviewing and making recommendations to the Board on the Company's incentive schemes and superannuation arrangements, making recommendations to the Board on any proposed changes to the Board and undertaking an annual review of the CEO's performance, including, setting with the CEO, goals for the coming year and reviewing progress in achieving these goals.

8.2 Executive and Non-Executive Director's remuneration

The Senior Executive Remuneration Policy was approved by resolution of the Board in September 2004 and the Non-Executive Director Remuneration Policy was approved by resolution of the Board on 25 March 2004.

8.2.1 Senior Executive Remuneration Policy

The Consolidated Entity is committed to remunerating its senior Executives in a manner that is market-competitive and consistent with best practice, as well as supporting the interests of shareholders. Consequently, under the Senior Executive Remuneration Policy the remuneration of senior Executives may be comprised of the following:

- fixed salary that is determined from a review of the market and reflects core performance requirements and expectations;
- a performance bonus designed to reward actual achievement by the individual of performance objectives and for materially improved Company performance;
- participation in the equity based incentive scheme with thresholds approved by shareholders; and
- statutory superannuation.

By remunerating senior Executives through performance and long-term incentive plans, in addition to their fixed remuneration, the Company aims to align the interests of senior Executives with those of shareholders, and increase Company performance.

Details of the amount of remuneration, including both monetary and non-monetary components, for each of the five highest paid (non-Director) Executives during the year (discounting accumulated entitlements) is detailed in the Director's Report and Note 21 of the notes to the financial statements.

8.2.2 Non-Executive Director Remuneration Policy

The Constitution provides that the Non-Executive Directors are each entitled to be paid such remuneration from the Company as the Directors decide for their services as a Director, but the total amount paid to all Non-Executive Directors for their services must not exceed in aggregate in any financial year the amount fixed by the Company in a general meeting. This amount is currently fixed at \$750,000. The remuneration of Non-Executive Directors must not include a commission on, or a percentage of, profits or operating revenue. Directors may also be reimbursed for travelling and other expenses incurred in attending to the Company's affairs. Directors may be paid such additional or special remuneration as the Directors decide is appropriate where a Director performs extra services or makes exertions for the benefit of the Company.

Non-Executive Directors are entitled to statutory superannuation, but do not otherwise receive retirement benefits.

Details of the amount of remuneration, including both monetary and non-monetary components, for each of the Directors paid during the year (discounting accumulated entitlements) is detailed in the Director's Report and Note 20 to the notes to the financial statements.

Directors' Report

The Directors present their report together with the financial statements of Photon Group Limited ("the Company") and of the Consolidated Entity, being the Company and its controlled entities and the Company's interest in associates, for the year ended 30 June 2010 and the auditor's report thereon.

Directors

The Directors of the Company at any time during or since the end of the financial year are:

Brian Bickmore – Independent non-Executive Chairman

Brian was appointed as a Non-Executive Director of the Company on 25 March 2004 and appointed Non-Executive Chairman on 1 July 2010. In 1980, Brian was a founding Executive of Austereo and served as a Director of the Company for almost 25 years until 2004. Brian was initially Austereo's Finance Director and from 1997, was the Group General Manager. Brian is a Director of oOH! Media Group Limited and was previously a Director of RG Capital Radio Limited. Brian is the Chairman of both the Audit Committee and the Remuneration Committee.

Susan McIntosh – Non-Executive Director

Susan was appointed as a Non-Executive Director of the Company on 2 June 2000. A Chartered Accountant, Susan has more than 25 years' business experience in media (radio and television production and distribution) and asset management, and is also the Managing Director of RG Capital Holdings (Australia) Pty Ltd. Susan is a member of the Audit Committee and was appointed to the Remuneration Committee on 25 June 2010.

Paul Gregory – Independent Non-Executive Director

Paul was appointed as a Director of the Company on 25 March 2004. Paul has led a diverse range of medium-sized private retail companies, including Australian Geographic Pty Ltd, and Red Earth Australia Pty Ltd, and has overseen the expansion of both companies in Australia and overseas. Currently, Paul is a business consultant providing management and strategic advice to several Australian and international retail groups. Paul is a member of the Audit Committee and resigned from the Remuneration Committee on 25 June 2010.

Tim Hughes – Non-Executive Director

Tim was appointed a Director of the Company on 2 June 2000 and was Executive Chairman from 2 June 2000 to 1 July 2010. Tim resigned as a Director on 11 August 2010.

Matthew Bailey – Chief Executive Officer/Executive Director

Matthew was appointed Chief Executive Officer and Director of the Company on 25 March 2004. Matthew ceased to be Chief Executive Officer on 31 March 2010 and resigned as a Director on 24 May 2010.

Company secretary

Eleni North was appointed Company Secretary on 11 February 2009. She is also the General Counsel of the Consolidated Entity. Prior to joining Photon, Eleni was Vice President, Legal at Travelport. Eleni has a Bachelor of Economics and a Bachelor of Laws (Hon) from the Australian National University. She is admitted to practice as a lawyer in Australia and the United Kingdom.

Principal activities

The principal activities of the Consolidated Entity during the course of the financial year was specialist integrated marketing services, specialising in retail marketing and merchandising, advertising, public relations, graphic design, digital printing, production of sales promotion material and Point of Sale (POS), Point of Production (POP), communications planning, email marketing, events management, direct marketing, market research services and online marketing.

There were no significant changes in the nature of the activities of the Consolidated Entity during the year.

Review and result of operations

The consolidated earnings before interest, tax, depreciation, amortisation and impairment charges (EBITDA) reduced 48% to \$46,681,680 (2009: \$89,303,865). The consolidated net loss from ordinary activities after income tax attributable to the members of the parent entity amounted to \$87,566,342 (2009: profit of \$21,407,728).

The results for the year included an impairment charge of \$88,929,375 (2009: \$4,214,854) and the following significant costs:

Redundancy charges	\$2,869,916
Closed business costs	\$13,000,469
Incidental acquisition costs	\$1,266,884
Restructuring provision	\$6,226,816
Impairment of working capital	\$4,277,126
Other	\$732,851
Total significant costs	\$28,374,062

Acquisitions

On 7 December 2009, the Company acquired a controlling interest in Dark Blue Sea Limited, as a result of acceptances under the takeover offer which was announced on 1 October 2009. After gaining acceptance in excess of 90% of the share capital, the Company compulsorily acquired the remaining share capital in Dark Blue Sea Limited and therefore owns 100% of the share capital post the compulsory acquisition period.

During the year ended 30 June 2009, there were no individually material or significant acquisitions.

Further detail in relation to the above is provided in note 28 of the notes to the consolidated financial statements.

Issue of shares and share options

On 21 August 2009, the Company issued 14,439,268 ordinary shares pursuant to a placement announced on 17 August 2009. These shares rank equally with existing shareholders, including participation in the final dividend for the year ending 30 June 2009.

On 18 September 2009, the Company issued 58,639,842 ordinary shares following the completion of the rights issue announced on 17 August 2009. These shares rank equally with existing shareholders.

Directors' Report

On 30 September 2009, the Company issued 2,471,608 ordinary shares. These shares were issued to satisfy deferred consideration from acquisition agreements which allow deferred consideration to be paid by the issue of Photon Group Limited shares. These shares were subject to voluntary escrow restrictions that ceased six months from issue date. These shares rank equally with other shareholders.

On 27 October 2009, the Company issued 940,000 options to employees under the Company's Employee Share Option Scheme (ESOS), which was approved by shareholders at the Company's Annual General Meeting in 2004. The exercise price of these options is \$1.85, being the VWAP for the 30 days prior to 22 October 2009.

On 29 October 2009, the Company issued 25,495 ordinary shares for no consideration to certain Executives of Photon and its subsidiaries pursuant to an incentive-based bonus scheme. These shares rank equally with existing shareholders.

On 8 December 2009, the Company issued 400,000 options to senior Executives under the Company's Employee Share Option Scheme (ESOS), which was approved by shareholders at the Company's Annual General Meeting in 2004. These options vested immediately and have an exercise price of \$1.80.

On 12 February 2010, the Company issued 200,000 options to senior Executives under the Company's Employee Share Option Scheme (ESOS), which was approved by shareholders at the Company's Annual General Meeting in 2004. The exercise price of these options is \$1.80.

On 5 March 2010, the Company issued 100,000 options to senior Executives under the Company's Employee Share Option Scheme (ESOS), which was approved by shareholders at the Company's Annual General Meeting in 2004. The exercise price of these options is \$1.80.

On 22 April 2010, the Company issued 24,017 ordinary shares for no consideration to certain Executives of Photon and its subsidiaries pursuant to an incentive-based bonus scheme. These shares rank equally with existing shareholders.

On 22 April 2010, the Company issued 9,000,000 ordinary shares to the Chief Executive Officer, Jeremy Philips, under a long-term incentive plan. The funding for the Chief Executive Officer's subscription of shares was facilitated by the Consolidated Entity providing a limited recourse loan.

Dividends

Dividends paid or declared by the Company to members since the end of the previous financial year were:

Type	Cents per share	Total amount \$'000	Date of payment	Franked/unfranked
<i>Declared and paid during the year</i>				
Final 2009 – Ordinary shares	6.5c	7,623	11 September 2009	Franked
Interim 2010 – Ordinary shares	3.0c	5,353	30 March 2010	Franked
Note				
Dealt with in the financial statements as:				
– Dividends	23			

State of affairs

There were no significant changes in the state of affairs of the Consolidated Entity during the financial year

Directors' meetings

The number of Directors' meetings (including meetings of committees of Directors) and number of meetings attended by each of the Directors of the Company during the financial year are:

Director	Board meetings		Audit Committee meetings		Remuneration Committee meetings	
	A	B	A	B	A	B
Tim Hughes	14	14	–	–	3	3
Matthew Bailey	9	10	–	–	–	–
Susan McIntosh	13	14	3	3	1	1
Brian Bickmore	14	14	3	3	3	3
Paul Gregory	11	14	2	3	2	3

A – Number of meetings attended.

B – Number of meetings held during the time the Director held office during the year.

Directors' interests

The relevant interest of each Director in the shares or options issued by the Consolidated Entity, as notified by the Directors to the Australian Stock Exchange in accordance with S205G(1) of the *Corporations Act 2001*, at the date of this report is as follows:

Director	Ordinary shares	Options over ordinary shares
Susan McIntosh	2,200,006	Nil
Brian Bickmore	643,582	Nil
Paul Gregory	200,000	Nil
Total	3,043,588	Nil

Share Options

Unissued shares under option

At the date of this report unissued shares of the Company under option are:

Expiry date	Number of options	Exercise price
30 August 2011	872,000	\$4.56
28 November 2011 ⁽ⁱ⁾	250,000	\$4.56
26 August 2012	100,000	\$5.90
10 October 2012	909,500	\$5.59
10 October 2012 ⁽ⁱⁱ⁾	250,000	\$5.59
31 March 2012 ⁽ⁱⁱ⁾	3,400,000	\$6.00
28 February 2013	250,000	\$5.23
31 March 2013	55,000	\$3.86
1 April 2013 ⁽ⁱⁱ⁾	400,000	\$6.00
30 September 2013 ⁽ⁱⁱ⁾	250,000	\$3.01
30 September 2013	1,302,000	\$2.58
11 February 2014	250,000	\$1.65
30 June 2014	400,000	\$1.36
26 October 2014	837,500	\$1.85
8 December 2014	400,000	\$1.80
12 February 2015	200,000	\$1.80
4 March 2015	100,000	\$1.80
Total unissued shares under options granted	10,226,000	
SEOP options ⁽ⁱⁱ⁾	(3,800,000)	
Total unissued shares under option⁽ⁱⁱⁱ⁾	6,426,000	

(i) Represents options held by former Executive.

(ii) Represents options granted under the SEOP as at 30 June 2010 but subject to vesting conditions which have not been met at 30 June 2010. SEOP options are not issued as at 30 June 2010.

(iii) 73,946,415 shares issued to the CEO under a limited recourse loan are treated as in-substance options however are not included in the above table.

These options in the table above do not entitle the holder to participate in any share issue of the Company.

Shares issued on exercise of options

During or since the end of the financial year, no ordinary shares were issued by the Company as a result of the exercise of options.

Events subsequent to balance date

Recapitalisation proposal

Since 7 June 2010, Photon Group Limited conducted a strategic review of its capital structure. On 17 August 2010, the Company announced a recapitalisation proposal which included the following elements:

- raising a minimum of \$102,500,000 through an underwritten entitlement issue and placement;
- a restructure of the deferred consideration payments; and
- refinancing the Company's debt facilities.

Please refer to Note 32 Subsequent events for further details on the recapitalisation proposal which was completed on 29 September 2010.

The financial effects of the above transactions have not been brought to account in the financial statements for the year ended 30 June 2010.

Other than the matters discussed above, there has not arisen, in the interval between the end of the financial year and the date of this report, any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors of the Company, to affect significantly the operations of the Consolidated Entity, the results of those operations, or the state of affairs of the Consolidated Entity in future financial years.

Likely Developments

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

Indemnification and insurance of officers and auditors

Indemnification

The Company has agreed to indemnify the following current Directors of the Company, Susan McIntosh, Brian Bickmore, Paul Gregory, the secretary Eleni North, Chief Executive Officer Jeremy Philips and Chief Financial Officer Clare Battellino against liabilities to another person (other than the Company or a related body corporate) that may arise from their positions as Directors or secretaries of the Company and its controlled entities, except where the liability arises out of conduct involving a lack of good faith. The agreement stipulates that the Company will meet the full amount of any liabilities, including costs and expenses.

The Company has also agreed to indemnify the current Directors and secretaries of its controlled entities for all liabilities to another person (other than the Company or a related body corporate) that may arise from their position, except where the liability arises out of conduct involving a lack of good faith. The agreements stipulate that the Company will meet the full amount of any such liabilities, including costs and expenses.

Directors' Report

Insurance premiums

During the financial year the Company has paid insurance premiums in respect of Directors' and officers' liabilities, for current Directors and officers covering the following:

- costs and expense incurred by the relevant officers in defending proceedings, whether civil or criminal; and
- other liabilities that may arise from their position, with the exception of conduct involving a wilful breach of duty or improper use of information or position to gain a personal advantage.

The Directors have not included details of the amount of the premium paid in respect of the Directors' and officers' liability and legal expenses insurance contracts, as such disclosure is prohibited under the terms of the contract.

Non Audit Services

During the year KPMG, the Company's auditor, has performed certain other services in addition to their statutory duties.

The Board has considered the non-audit services provided during the year by the auditor and in accordance with 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 Company 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 principals 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 Company, acting as an advocate for the Company or jointly sharing risks and rewards.

A copy of the Auditor's Independence Declaration as required under section 307C of the *Corporations Act 2001* is on page 90 of this annual report.

Details of the amounts paid to the auditor of the Company, KPMG, and its related practices for non-audit services provided during the year are set out below. In addition, amounts paid to other auditors for the statutory audit have been disclosed in Note 5 to the financial statements.

	2010 \$	Consolidated 2009 \$
<i>Services other than statutory audit</i>		
Auditors of the Company		
<i>Other services:</i>		
<i>Migration services work:</i>		
KPMG Australia	10,100	17,150
<i>Taxation compliance services:</i>		
KPMG Australia	28,000	47,500
Overseas KPMG firms	249,494	265,662
<i>Transaction and due diligence services:</i>		
KPMG Australia	949,489	535,600
Overseas KPMG firms	2,684	179,281
Total services other than statutory audit	1,239,767	1,045,193

Rounding off

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial statements and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Remuneration report – Audited

1 Principles of remuneration

Compensation is referred to as remuneration throughout this report.

(a) Remuneration policies

Key management personnel have authority and responsibility for planning, directing and controlling the activities of the Consolidated Entity, comprise the Directors of the Company and Executives of the Company and the Consolidated Entity, including the five most highly remunerated Company and Consolidated Entity Executives.

The remuneration levels for key management personnel of the Consolidated Entity are competitively set to attract and retain appropriately qualified and experienced Directors and senior Executives.

The compensation structures explained below are designed for suitably qualified candidates, reward the achievement of strategic objectives and achieve the broader outcome of creation of value for shareholders. The compensation structures take into account:

- the capability and experience of key management personnel;
- the key management personnel's ability to control the relevant Company's performance;
- the Consolidated Entity's performance including:
 - the Consolidated Entity's earnings;
 - the growth in share price and delivering constant returns on shareholder wealth; and
 - the level of incentives within each key management person's compensation.

Remuneration packages contain a mix of fixed and variable remuneration, short-term and long-term performance-based incentives and equity-based remuneration.

The Remuneration Committee reviews and makes recommendations to the Board on remuneration packages and policies including but not limited to succession planning, recruitment and the appointment of the Chief Executive Officer, senior Executives and Directors themselves and overseeing succession planning, selection and appointment practices and remuneration packages for management and employees of Photon.

(b) Fixed remuneration

Fixed remuneration consists of base remuneration (which is calculated on a total cost-to-Company basis and includes FBT charges related to employee benefits including motor vehicles), as well as employer contributions to superannuation/pension funds.

Remuneration levels are reviewed annually by the Remuneration Committee through a process that considers individual, division and overall performance of the Consolidated Entity. A senior Executive's remuneration is also reviewed on promotion.

(c) Performance-linked remuneration

Performance linked remuneration includes both short-term and long-term incentives and is designed to reward key management personnel for meeting or exceeding their financial and personal objectives. The short-term incentives (STI) are "at risk" bonuses provided in the form of cash and shares while the long-term incentives (LTI) are provided as options over ordinary shares in the Company under the rules of the Executive Share Option Scheme (ESOS) (see note 20), the Senior Executive Option Plan (SEOP) (see note 20), the Executive Committee Option Scheme (ECOS) (see note 20), or under the terms of the contracts with Matthew Bailey and Tim Hughes (see note 20) or the subscription of ordinary shares in the Company funded by a limited recourse loan for the CEO (CEO LTIP) (see note 20).

Short-term incentives

There are a number of short-term incentive plans available to employees, senior Executives, Division Managing Directors and the CEO.

The short-term incentives for individual Company Chief Executive Officers and senior employees are linked to the financial performance of their individual Company, relative to Company budgets or the prior financial year. The incentives are typically payable in cash, with incentives over a certain threshold payable 50% in cash and 50% in shares. Any share component of the STI is issued over two years from the end of the financial year to which the STI relates.

Short-term incentives for Division Managing Directors in the current financial year are based on the financial performance of their respective division (typically 1–2% of Division EBITDA or EBIT) and paid in cash, in accordance with the terms of their individual service agreements.

The short-term incentive for the CEO is based on financial performance of the Consolidated Entity, being 5% of net profit after tax and before amortisation of acquired intangibles in each financial year above \$20 million plus a discretionary bonus based on strategic non financial measures capped at individual service agreement levels.

Long-term incentives

Long-term incentives are designed to link Executive remuneration with long-term shareholder wealth and the performance of the business.

CEO Long-term Incentive Plan (CEO LTIP)

In April 2010, the Company granted Jeremy Philips a limited recourse loan to subscribe for 9,000,000 ordinary shares in the Company. The ordinary shares were issued at \$1.13, with the limited recourse loan being provided for the issue price. The ordinary shares issued under the CEO LTIP are subject to vesting and escrow conditions.

In accordance with the terms of the CEO's service agreement, in circumstances where the Company issues shares within twelve months of the grant date, the Company must offer the CEO the right to acquire additional shares as will, following the issue of shares, maintain his proportionate holding relative to the total number of shares on issue and to provide an additional limited recourse loan to fund the additional shares subscribed for (on the same terms as the original limited recourse loan). In connection with the equity raising announced on 17 August 2010 (see Note 32 Subsequent events for further details), Jeremy Philips subscribed for a further 64,946,415 shares funded by limited recourse loan provided by the Company. The additional ordinary shares under the CEO LTIP were issued at 10 cents, with the further limited recourse loan being provided for the issue price.

The CEO is not able to deal with any ordinary shares issued under the CEO LTIP until they vest as follows:

- 16,432,537 at 30 June 2012
- 24,648,805 at 30 June 2013
- 32,865,073 at 30 June 2014

Any dividends received from the ordinary shares will be offset against interest payable on the limited recourse loan. Repayment of the loan will be made on the earlier of the sale of the relevant shares or 12 months after vesting. The CEO may elect to forfeit the shares to which any loan repayment relates, in lieu of making a repayment which is due.

If the CEO resigns the CEO LTIP continues to vest (subject to compliance with post employment restrictions) during the contractual notice period and the period of the post employment restrictions. If the CEO is terminated without cause the CEO LTIP vests in accordance with the above vesting profile. The CEO forfeits the CEO LTIP if terminated for serious misconduct.

Executive share option scheme (ESOS)

The Company has an Executive share option scheme (ESOS).

The plan allows for the Board to determine who is entitled to participate in the ESOS and may grant options accordingly. Photon's Remuneration Committee may determine whether or not the grant or exercise of options is conditional on the achievement of performance hurdles, and if so, the nature of such performance hurdles. The exercise of an option will entitle the option holder to subscribe for one share. All options will be granted at an exercise price being the average of the daily volume

Directors' Report

weighted average sale price (VWAP) of the Company shares on each of the 30 business days prior to the issue date. All options expire on the earlier of their expiry date or termination of the individual's employment. The options issued on or after 1 April 2004, under the ESOS, are exercisable by the option holder as follows:

- After two years from issue date – 33 ⅓%
- After three years from issue date – 66 ⅔%
- After four years from issue date the option holder is entitled to exercise all options until expiry date (being 5 years after the issue date)

As at 30 June 2010, 6,522,368 options over unissued shares are outstanding which have been issued under the ESOS.

In prior periods, options were issued to Tim Hughes and Matthew Bailey under the ESOS with specific and individual terms. These options have reached their respective vesting conditions and have been previously issued. As both Tim Hughes and Matthew Bailey have resigned as Directors of the Company and will not be considered key management personnel, these options no longer provide any long-term incentives for key management personnel.

Senior Executive Option Plan (SEOP)

In July 2007, the Company introduced a Senior Executive Option Plan (SEOP), designed to incentivise the Company's Executive Directors, Division Managing Directors and other senior management. The plan allows for the Board to determine who is entitled to participate in the SEOP and may grant options accordingly. The exercise of the options will entitle the option holder to subscribe for one share. The options were granted at the date of the shareholder approval, being the Company's AGM on 20 November 2007, or, if later, when the employee commenced employment, with an exercise price of \$6.00. The granted options have both a service condition and a market performance hurdle. Options are only issued if fully vested such that both the performance hurdle, requiring an 18% year on year increase in Photon Group's share price, and service condition is satisfied. The options issued under the SEOP are exercisable by the option holder as follows:

- At 1 July 2010 (tranche 1) – 33 ⅓ %, and which expire on 31 March 2011
- At 1 July 2011 (tranche 3) – 33 ⅓ %, and which expire on 31 March 2012
- At 1 July 2011 (tranche 2) – 33 ⅓ %, and which expire on 31 March 2012

As at 30 June 2010 no SEOP options had been issued as none of the performance hurdles required to be achieved had been met.

Executive Committee Option Scheme (ECOS)

In October 2008, the Company introduced an Executive Committee Option Scheme (ECOS), designed to incentivise the Company's Executive Directors, Division Managing Directors and other senior management.

The plan allows the Board to determine who is entitled to participate in the ECOS and may grant options accordingly. Each grant of options has both a service condition and a non-market performance hurdle (determined at the Board's discretion). Options are only issued if both performance hurdles and service conditions are satisfied. The exercise of the options will entitle the option holder to subscribe for one share. This scheme was approved at the Company's 2008 AGM on 28 October 2008.

As at 30 June 2010, the performance hurdles required for the ECOS to vest have not been satisfied and therefore no ECOS options have been issued.

Refer Director's Report section 2(d) for further information regarding the ESOS, SEOP and ECOS.

The board has requested Directors disclose any interests in shares or other share-based payments that allow borrowing against share interests or limit exposures to the losses that would result from share price decreases.

(d) Service contracts

It is the Consolidated Entity's policy that service contracts for key management personnel are in force for a fixed period, with an extension period negotiable after completion of the initial term or on a rolling basis. The agreements are capable of termination, acknowledging appropriate notice periods, and the Consolidated Entity retains the right to terminate the contract immediately for contractual breach by the Executive or by making payment in lieu of notice.

The service agreements outline the components of remuneration paid to the key management personnel and prescribe that the remuneration levels are modified based on inflation or performance criteria individually agreed. Remuneration levels are reviewed annually by the Remuneration Committee.

Refer to the table on page 21 for a summary of terms for current service agreements for key management personnel.

(e) Non-executive Directors

The Company's Constitution provides that the Non-executive Directors are each entitled to be paid such remuneration from the Company as the Directors decide for their services as Director, but the total amount provided to all Non-executive Directors for their services must not exceed in aggregate in any financial year the amount fixed by the Company in a general meeting. This amount has been fixed by the Company at \$750,000 for the financial year ended 30 June 2010.

The remuneration of Non-executive Directors must not include a commission on, or percentage of, profits or operating revenue. Directors may also be reimbursed for travelling and other expenses incurred in attending to the Company's affairs. Directors may be paid such additional or special remuneration as the Directors decide is appropriate where a Director performs extra services or makes special exertions for the benefit of the Company.

Summary terms for current service agreements for key management personnel:

Key management personnel	Duration of contract	Notice period on termination by Consolidated Entity	Notice period on resignation by key management personnel	Termination payment on termination by Consolidated Entity (i) (ii) (iii)	Termination payment on resignation by key management personnel (i) (ii)
CEO ^(iv)	Rolling	12 months	6 months	12 months average base salary calculated in accordance with the Corporations Act 2001.	12 months average base salary calculated in accordance with the Corporations Act 2001
Division Managing Directors	2–4 years	6–12 months	6 months	Maximum 6–12 months average base salary calculated in accordance with the Corporations Act 2001	Maximum 6–12 months average base salary calculated in accordance with the Corporations Act 2001.

(i) In addition to termination payments, key management personnel are also entitled to receive, on termination of their employment, their statutory entitlements of accrued annual and long service leave, together with any superannuation benefits.

(ii) Includes any payment in lieu of notice.

(iii) No termination payment is due if termination is for serious misconduct.

(iv) CEO is entitled to a pro rata STI payment on termination except for termination for serious misconduct.

(f) Consequences of performance on shareholder wealth

In considering the Consolidated Entity's performance and benefits of shareholder wealth, the Remuneration Committee has regard to the performance of the Consolidated Entity. The achievement of division budgets and individual Company budgets are considered as the financial performance target in setting the short-term incentives. Profitability, growth in EPS, dividends, changes in share price and return of capital are factors the Remuneration Committee takes into account in assessing the long-term incentives.

The Remuneration Committee have reviewed the current financial year and the previous four financial year's performance including the impact of significant costs in the current financial year. The Remuneration Committee considers that STI and LTI for key management personnel remuneration should take into account performance, including the profits of the Consolidated Entity over a number of years. Prior to the year ended 30 June 2010 the Consolidated Entity achieved profits and returned profits to shareholders.

2(a) Directors' and Executive officers' cash and post employment and other long-term remuneration

Details of the nature and amount of each major element of the remuneration of each Director of the Company and each of the five named relevant Company and Consolidated Entity Executives, who are all key management personnel and receive the highest remuneration.

		Salary and fees \$	Cash bonus ⁽ⁱ⁾ \$	Non-cash benefits \$	Post-employment Super/ Pension contributions \$	Other long-term \$	Other compensation Termination benefits \$	Total Cash and other compensation excluding equity-based remuneration \$
Directors								
Non-Executive								
Susan McIntosh	2010	125,000	—	—	11,250	—	—	136,250
	2009	125,000	—	—	11,250	—	—	136,250
Brian Bickmore	2010	125,000	—	—	11,250	—	—	136,250
	2009	125,000	—	—	11,250	—	—	136,250
Paul Gregory	2010	125,000	—	—	—	—	—	125,000
	2009	125,000	—	—	—	—	—	125,000
Executive								
Tim Hughes ^(viii)	2010	1,120,000	—	7,532	14,461	201,154	1,120,000	2,463,147
	2009	1,065,000	—	—	13,745	—	—	1,078,745
Matthew Bailey ^(ix)	2010	744,141	4,095	—	14,461	—	895,000	1,657,697
	2009	822,259	224,060	—	50,616	13,872	—	1,110,807

Refer to page 23 for footnote details.

Directors' Report

Details of the nature and amount of each major element of the remuneration of each Director of the Company and each of the five named relevant Company and Consolidated Entity Executives, who are all key management personnel and receive the highest remuneration.

		Salary and fees \$	Cash bonus(i) \$	Non-cash benefits \$	Post- employment Super/ Pension contributions \$	Other long-term compensation \$	Other Termination benefits \$	TOTAL Cash and other compensation excluding equity-based remuneration \$
Relevant Consolidated Entity Executives								
Jeremy Philips, Chief Executive Officer ^(vii)	2010	147,909	—	1,751	25,000	93	—	174,753
	2009	—	—	—	—	—	—	—
Nigel Long, Managing Director, Strategic Intelligence Division	2010	475,935	159,222	2,496	110,603	—	—	748,256
	2009	498,342	78,451	—	65,366	—	—	642,159
Jon Wilkins, Managing Director, Integrated Communications & Digital Division ^(iv)	2010	476,416	115,000	19,359	58,689	—	—	669,464
	2009	—	—	—	—	—	—	—
Stewart Bailey, Managing Director, Field Marketing Division	2010	644,334	51,933	—	26,132	14,999	—	737,398
	2009	362,504	366,959	—	50,000	2,733	—	782,196
Mark Dagleish, Managing Director, Internet Marketing & E-Commerce Division ^{(iii) (xi)}	2010	256,773	—	—	14,450	—	—	271,223
	2009	—	—	—	—	—	—	—
Adam Kilgour, Managing Director, Specialised Communications Division ^(xi)	2010	324,295	3,760	—	14,461	11,189	—	353,705
	2009	327,279	122,000	—	13,745	6,773	—	469,797

Refer page 23 for footnote details.

2(b) Directors' and Executive officers' equity-based remuneration

Details of the nature and amount of each major element of the remuneration of each Director of the Company and each of the five named relevant Company and Consolidated Entity Executives, who are all key management personnel and receive the highest remuneration.

Share-based payments – Accounting value at Grant Date									
		Value of options under CEO LTIP ^(x)	Value of options under ESOS ⁽ⁱⁱ⁾	Value of options under SEOP ^{(i) (v)}	Value of options under ECOS ⁽ⁱ⁾	Value of shares	Total Equity-based remuneration	Proportion of total remuneration performance related ^(vi)	Value of options proportion of total remuneration ^(vi)
		\$	\$	\$	\$	\$	\$	%	%
Directors									
Non-Executive									
Susan McIntosh	2010	—	—	—	—	—	—	—	—
	2009	—	—	—	—	—	—	—	—
Brian Bickmore	2010	—	—	—	—	—	—	—	—
	2009	—	—	—	—	—	—	—	—
Paul Gregory	2010	—	—	—	—	—	—	—	—
	2009	—	—	—	—	—	—	—	—
Executive									
Tim Hughes ^(viii)	2010	—	610,000	1,127,500	—	—	1,737,500	41.36	41.36
	2009	—	614,429	1,127,500	—	—	1,741,929	61.76	61.76
Matthew Bailey ^(ix)	2010	—	95,361	—	—	—	95,361	5.67	5.44
	2009	—	244,570	338,250	—	—	582,820	47.64	34.41

Refer page 23 for footnote details.

Details of the nature and amount of each major element of the remuneration of each Director of the Company and each of the five named relevant Company and Consolidated Entity Executives, who are all key management personnel and receive the highest remuneration.

Share-based payments – Accounting value at Grant Date									
		Value of options under CEO LTIP ^(x)	Value of options under ESOS ⁽ⁱⁱ⁾	Value of options under SEOP ^{(ii)(v)}	Value of options under ECOS ⁽ⁱⁱ⁾	Value of shares	Equity-based remuneration	Proportion of total remuneration performance related ^(vi)	Value of options proportion of total remuneration ^(vi)
		\$	\$	\$	\$	\$	\$	%	%
Relevant Consolidated Entity Executives									
Jeremy Philips, Chief Executive Officer ^(vii)	2010	152,710	–	–	–	–	152,710	46.63	46.63
	2009	–	–	–	–	–	–	–	–
Nigel Long, Managing Director, Strategic Intelligence Division	2010	–	36,749	11,367	–	–	48,116	26.04	6.06
	2009	–	38,046	11,367	89	–	49,502	18.50	7.16
Jon Wilkins, Managing Director, Integrated Communications & Digital Division ^(iv)	2010	–	15,224	–	16,310	–	31,534	20.90	4.50
	2009	–	–	–	–	–	–	–	–
Stewart Bailey, Managing Director, Field Marketing Division	2010	–	139,568	131,000	–	–	270,568	32.00	26.84
	2009	–	80,436	131,000	89	–	211,525	58.21	21.29
Mark Dagleish, Managing Director, Internet Marketing & E-Commerce Division ^{(iii)(xi)}	2010	–	15,224	–	–	–	15,224	5.31	5.31
	2009	–	–	–	–	–	–	–	–
Adam Kilgour, Managing Director, Specialised Communications Division ^(xi)	2010	–	144,317	131,000	–	–	275,317	44.37	43.77
	2009	–	95,391	131,000	89	–	226,480	50.05	32.53

Refer page 23 for footnote details.

- (i) The short-term, incentive bonus is for performance during the 30 June 2010 financial year using the criteria set out on page 19.
- (ii) The fair value of the ESOS options are calculated at the date of grant using either the Black Scholes model or Binomial option pricing model. The fair value of the SEOP options are calculated at the date of grant using a Monte Carlo Simulation Model. The fair value of the ECOS options are calculated at the date of the grant using either the Black Scholes model or the Binomial option pricing model. The fair value is allocated to each reporting period on a straight-line basis over the period from grant date to vesting date. The value disclosed above is the portion of the fair value of the options allocated to this reporting period. In valuing options, market conditions have been taken into account. The factors and assumptions used in determining the fair value of options on grant date are discussed in Note 20 Employee benefits.
- (iii) Appointed Managing Director of Internet Marketing & E-Commerce Division in July 2009.
- (iv) Appointed Managing Director of Integrated Communications & Digital Division in July 2009.
- (v) Options granted under SEOP have minimal fair value to the option holders at 30 June 2010 due to the significant decline in the share price since the options were granted. The SEOP options granted have a strike price of \$6.00 and require year on year share price growth of 18% to vest in full. The options have been accounted for in accordance with AASB 2 *Share-Based Payments* and valued based on share price of the date of approval by shareholders at the Company's AGM, being 20 November 2007 or the date agreed between the Company and the respective employee. There is no allowance made in the grant value for the movement of the share price before vesting conditions are met because SEOP options are based on market conditions (share price growth between 8–18% year-on-year for the three years ending 30 June 2010). In accordance with AASB 2, the probability of vesting has been taken into account in determining the fair value of the granted option and no adjustment is made in the event of those market conditions not being met. These SEOP options are ultimately expensed in the profit and loss of the Consolidated Entity over the vesting period irrespective of market conditions being met. The expense is adjusted if the service condition is not met. The subsequent significant fall in the share price of the Company results in the disclosed total remuneration value SEOP being significantly greater than the current underlying value of the granted options, which are "out of the money" options as at 30 June 2010. This analysis is deemed relevant to understanding the remuneration of Directors and Key Management Personnel relative to changes in shareholder wealth.
- (vi) Percentages are based on total remuneration including equity, cash, post employment and other long-term remuneration.
- (vii) Appointed Chief Executive Officer on 1 June 2010. Salary and fees includes relocation expenses.
- (viii) Resigned as Executive Chairman on 1 July 2010 and resigned as a Director on 11 August 2010. The payment terms of Tim Hughes's termination payment is 50% on or about 30 September 2010 and the remaining 50% will be subject to terms substantially the same as the restructured deferred consideration. Please refer to Note 32 Subsequent events for details on the restructured deferred consideration terms.
- (ix) Resigned as Chief Executive Officer on 31 March 2010 and resigned as a Director on 24 May 2010.
- (x) The ordinary shares under the CEO LTIP funded through a limited recourse loan are accounted for as an in-substance option under AASB 2 *Share-Based Payments*. The fair value of the ordinary shares issued are calculated at the date of the grant, being 20 April 2010. The fair value is allocated to each reporting period on a straight-line basis over the period from grant date to vesting date.
- (xi) Adam Kilgour and Mark Dagleish are no longer key management personnel, effective 30 July 2010 and 28 June 2010 respectively.

Directors' Report

2(b) Details of performance related remuneration

Details of the Company's policy in relation to the proportion of remuneration that is performance based is discussed on page 19.

2(c) Analysis of bonuses included in remuneration

Details of the vesting profile of the short-term incentive cash bonuses awarded as remuneration to each Director of the Company of the five named Company Executives and relevant Consolidated Entity Executives, who are key management personnel, are detailed below.

	Included in remuneration \$	Short-term incentive bonus ⁽ⁱ⁾ % vested in year
Company Executive		
Matthew Bailey	4,095	100
Relevant Company and Consolidated Entity Executives		
Nigel Long	157,451	100
Jon Wilkins	115,000	100
Stewart Bailey	28,158	100
Adam Kilgour	3,760	100

Other key management personnel did not receive an STI.

- (i) Amounts included in remuneration for the financial year represent the amount that vested in the financial year based on achievement of satisfaction of specified performance criteria as discussed in principles of remuneration note 1(c) short-term incentives.

2(d) Directors' and senior Executives' remuneration

The following factors and assumptions were used in determining the fair value of the options on the grant date:

Grant date	Expiry date	Value per option	Exercise price ⁽ⁱ⁾	Price of shares on grant date	Expected volatility	Risk free interest rate	Dividend yield	Expected life (years)
22 Oct 2009 ⁽ⁱⁱ⁾	31 Aug 2013	\$0.448	\$1.51	\$1.89	35%	5.53%	6.5%	1–4
27 Oct 2009	27 Oct 2014	\$0.381 – \$0.435	\$1.85	\$1.92	35%	5.54%	6.5%	2–5
8 Dec 2009	8 Dec 2014	\$0.381	\$1.80	\$1.67	35%	5.54%	6.5%	1–5
12 Feb 2010	12 Feb 2015	\$0.178 – \$0.305	\$1.80	\$1.20	35%	6.00%	6.5%	2–5
5 Mar 2010	5 Mar 2015	\$0.139 – \$0.253	\$1.80	\$1.11	35%	6.00%	6.5%	2–5
20 Apr 2010 ⁽ⁱⁱⁱ⁾	30 Jun 2015	\$0.27 – \$0.31	\$1.13	\$1.17	40%	5.42%	6.0%	2–5
17 Sep 2010 ^(iv)	30 Jun 2015	\$0.03 – \$0.04	\$0.10	\$0.10	40%	4.72%	0.0%	2–5

- (i) As set out in the Company's ESOS, the exercise price of options granted after 25 March 2004 is calculated with reference to the volume weighted average price (VWAP) of the Company's ordinary shares for 30 business days prior to the issue date.
- (ii) Options granted under ECOS have not been issued as at 30 June 2010, and will not be issued as performance hurdles have not been met.
- (iii) Grant is in relation to a CEO LTIP provided to CEO for the sole purpose of subscribing for 9,000,000 ordinary shares in the Company. Dividends paid by the Company will be applied against interest on the loan. The issue price is the 30 business day VWAP prior to the grant date.
- (iv) Grant is in relation to a CEO LTIP provided to CEO for the sole purpose of subscribing for 64,946,415 ordinary shares in the Company. Dividends paid by the Company will be applied against interest on the loan. The grant date is 17 September 2010, being the date of shareholder approval at a general meeting. The valuation factors and assumptions are an estimate as the valuation has not been finalised as at the date of this report.

2(e) Options granted during 2010 as remuneration to Directors' and senior Executives

Employee Share Option Scheme (ESOS)

The following options were granted under the terms of the ESOS for no consideration. The exercise price of the options is calculated on the VWAP for the 30 days prior to the date when the options were granted.

Executive	Number of options granted	Grant date	2010 Exercise price
Adam Kilgour	200,000	8 Dec 2009	\$ 1.80
Stewart Bailey	200,000	8 Dec 2009	\$ 1.80

The above granted options have no vesting conditions and therefore vested immediately.

Executive Committee Option Scheme (ECOS)

On 22 October 2009, the Company granted Tim Hughes 400,000 options and Matthew Bailey 400,000 options under ECOS, which was approved by shareholders at the Company's AGM on 22 October 2009. The exercise price of the options is \$1.51, being the VWAP for the 30 days prior to the AGM grant date. The options vest with the holders (and the holders may exercise the options) if the increase in Photon's EPS for the year ending 30 June 2010 compared to Photon's EPS for the year ending 30 June 2009 is greater than 10%.

As the EPS vesting condition attached to this grant of ECOS options has not been satisfied, these ECOS options will not vest and therefore no share-based payments expense will be accounted for in the profit and loss of the Consolidated Entity. Additionally, no remuneration will be attributable to each of Tim Hughes and Matthew Bailey in respect of this grant (see table page 22).

CEO Long-term Incentive Plan (CEO LTIP)

Directors' Report

Details of the vesting profile of the options granted as remuneration to each Director of the Company and each of the five named relevant Consolidated Entity Executives, who are all key management personnel, are detailed below:

Company and Consolidated Entity	Number of options granted	Type of option granted	Grant date	% vested in year	% forfeited in year	% vesting condition not met ^(vi)	% remaining to vest	Vesting date ⁽ⁱⁱ⁾
Executives								
Stewart Bailey	20,000	ESOS	29 Jul 2005	33⅓	—	—	—	29 Jul 2007
								29 Jul 2008
								29 Jul 2009
	80,000	ESOS	30 Aug 2006	33⅓	—	—	33⅓	30 Aug 2008
								30 Aug 2009
								30 Aug 2010
	100,000	ESOS	1 Jul 2007	33⅓	—	—	66⅔	1 Jul 2009
								1 Jul 2010
								1 Jul 2011
	600,000	SEOP	20 Nov 2007	—	—	—	100	1 Jul 2010
Adam Kilgour	100,000	ESOS	1 Oct 2008	—	—	—	100	1 Jul 2011
								1 Oct 2010
								1 Oct 2011
								1 Oct 2012
	100,000	ESOS	30 Jun 2009	—	—	—	100	30 Jun 2011
								30 Jun 2012
								30 Jun 2013
	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	200,000	ESOS	8 Dec 2009	100	—	—	—	8 Dec 2009
	5,000	ESOS	29 Jul 2005	33⅓	—	—	—	29 Jul 2007
								29 Jul 2008
								29 Jul 2009
	100,000	ESOS	30 Aug 2006	33⅓	—	—	33⅓	30 Aug 2008
								30 Aug 2009
								30 Aug 2010
	100,000	ESOS	1 Jul 2007	33⅓	—	—	66⅔	1 Jul 2009
								1 Jul 2010
								1 Jul 2011
	600,000	SEOP	20 Nov 2007	—	—	—	100	1 Jul 2010
								1 Jul 2011
	200,000	ESOS	1 Oct 2008	—	—	—	100	1 Oct 2010
								1 Oct 2011
								1 Oct 2012
	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	200,000	ESOS	8 Dec 2009	100	—	—	—	8 Dec 2009

Details of the vesting profile of the options granted as remuneration to each Director of the Company and each of the five named relevant Consolidated Entity Executives, who are all key management personnel, are detailed below:

Company and Consolidated Entity	Number of options granted	Type of option granted	Grant date	% vested in year	% forfeited in year	% vesting condition not met ⁽ⁱ⁾	% remaining to vest	Vesting date ⁽ⁱⁱ⁾
Executives								
Nigel Long	55,000	ESOS	1 Apr 2008	33⅓	—	—	66⅔	1 Apr 2010 1 Apr 2011 1 Apr 2012
	95,000	ESOS	5 Feb 2008	33⅓	—	—	66⅔	28 Feb 2010 28 Feb 2011 28 Feb 2012
	450,000	SEOP	1 Apr 2008	—	—	—	100	1 Jul 2010 1 Jul 2011
	100,000	ESOS	1 Oct 2008	—	—	—	100	1 Oct 2010 1 Oct 2011 1 Oct 2012
Jon Wilkins	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	150,000	ESOS	30 Jun 2009	—	—	—	100	30 Jun 2011 30 Jun 2012 30 Jun 2013
	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	150,000	ESOS	30 Jun 2009	—	—	—	100	30 Jun 2011 30 Jun 2012 30 Jun 2013
Mark Dalglish	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	150,000	ESOS	30 Jun 2009	—	—	—	100	30 Jun 2011 30 Jun 2012 30 Jun 2013
	180,000	ECOS	30 Jun 2009	—	—	100	—	31 Aug 2010
	9,000,000	CEO LTIP	20 Apr 2010	—	—	—	100	30 Jun 2012 30 Jun 2013 30 Jun 2014
Jeremy Philips ^(vii)	64,946,415	CEO LTIP	17 Sep 2010	—	—	—	100	30 Jun 2012 30 Jun 2013 30 Jun 2014

(i) ECOS options granted on 28 October 2008 and 22 October 2009 did not meet performance hurdles for the year ended 30 June 2009 and 30 June 2010 respectively and were therefore not issued.

(ii) The options granted vest over various periods, based on the terms of the option agreements. The date reflected in the table above represents all of the vesting dates for each tranche of options.

(iii) Tim Hughes resigned as a Director on 11 August 2010 (after the year end reporting date) and therefore 2,000,000 options granted under SEOP will be forfeited as the service condition will not be met.

(iv) Matthew Bailey's options granted on 17 October 2006 vest over various periods, based on the terms of the option agreement. The options are to be issued in four tranches of 250,000 options. The first tranche vested on 17 October 2008, the second tranche on 30 September 2009 and the third tranche on 30 September 2010. The fourth tranche did not meet the required vesting conditions and has therefore not been issued. The date reflected above represents the final vesting date for the third tranche of options. Matthew Bailey resigned as a Director on 24 May 2010.

(v) Matthew Bailey resigned during the year and therefore 900,000 options granted under SEOP were forfeited as the service condition was not met.

(vi) ECOS options granted on 30 June 2009 are based on specific performance conditions described in the Remuneration report 1(c) Performance Linked Remuneration Long-Term Incentives. These options did not meet performance hurdles for 30 June 2010 and were therefore not issued.

(vii) Grant is in relation to a CEO LTIP provided to CEO for the sole purposed of subscribing for ordinary shares in the Company. The grant date is 17 September 2010, being the date of shareholder approval at a general meeting.

Directors' Report

3(d) Analysis of movements in options

The movement during the reporting period by value, of options over ordinary shares in the Company held by each Company Director and each of the named relevant Company and Consolidated Entity Executives, who are all key management personnel, is detailed below.

	Granted in year \$ ⁽ⁱ⁾	Type of option granted in year	Value of Options	
			Exercised in year \$	Forfeited in year \$ ⁽ⁱⁱ⁾
Directors				
Tim Hughes ⁽ⁱ⁾	—	ECOS	—	—
Matthew Bailey ⁽ⁱ⁾	—	ECOS	—	—
Consolidated Entity Executives				
Jeremy Philips	2,560,000	CEO LTIP	—	—
Jeremy Philips ^(iv)	2,237,043	CEO LTIP	—	—
Stewart Bailey	76,120	ESOS	—	—
Adam Kilgour	76,120	ESOS	—	—

- (i) Tim Hughes and Matthew Bailey were granted ECOS options during the year (see page 25), however as these will not meet vesting conditions, no share-based payment expense will be recognised for such options and therefore no value exists for options granted in current year.
- (ii) The value of options granted in the year is the fair value of the options calculated at grant date using a range of valuation models including the Black Scholes, Binomial and Monte Carlo Simulation. For further details on the valuation methodologies of these valuations see Note 20 Employee Benefits. The total value of the options granted is included in the table above. This amount is allocated to remuneration over the vesting period (i.e. on a straight-line basis).
- (iii) All of the options forfeited during the year have a nil value due to the fact that all of these options are out of the money.
- (iv) The value of options granted under the CEO LTIP is an estimate as the valuation has not been finalised as at the date of this report.

3(e) Modification of terms of equity-settled share-based payment transactions

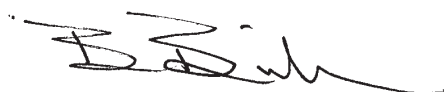
No terms of equity-settled share-based payment transactions (including options and rights granted as compensation to a key management person) have been altered or modified by the issuing entity during the reporting period or the prior period.

Lead Auditor's Independence Declaration

The lead auditor's independence declaration is set out on page 90, and forms part of the Directors' Report for the year ended 30 June 2010.

This report is made in accordance with a resolution of the Directors.

Dated at Sydney this 30th day of September 2010.



Brian Bickmore

Director

Consolidated income statement for the year ended 30 June 2010

In thousands of AUD	Note	2010	Consolidated 2009
Gross revenue	3	587,259	653,455
Directly attributable costs of sales	3	(208,652)	(212,816)
Net revenue	3	378,607	440,639
Other income	3	792	1,233
Total revenue	2	379,399	441,872
Employee expenses		(260,267)	(281,110)
Occupancy costs		(20,178)	(19,133)
Depreciation and amortisation expense		(21,096)	(20,556)
Insurance expense		(1,186)	(1,384)
Consultancy fees		(13,542)	(15,210)
Equipment hire charges		(990)	(1,062)
Travel expenses		(5,266)	(8,964)
Communication expenses		(6,516)	(7,874)
Other operating expenses		(23,389)	(17,975)
Net finance expenses	4	(24,125)	(26,551)
Acquisition transaction cost		(1,266)	—
Share of profit/(loss) of associates	13	(117)	145
Fair value adjustment to deferred consideration liability		(52)	—
Impairment of intangible assets		(86,871)	—
Impairment of investment in equity accounted investee		(2,059)	(4,215)
Profit/(Loss) before tax		(87,521)	37,983
Income tax expense	6	(586)	(15,582)
Profit/(loss) for the period		(88,107)	22,401
Attributable to:			
Equity holders of the parent		(87,566)	21,408
Non controlling interest		(541)	993
		(88,107)	22,401
Basic earnings per share (AUD cents)	7	(26.83)	10.00
Diluted earnings per share (AUD cents)	7	(26.83)	10.00

The notes on pages 34 to 86 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income for the year ended 30 June 2010

In thousands of AUD	Note	2010	Consolidated 2009
Profit/(loss) for the period		(88,107)	22,401
Other comprehensive income			
Cash flow hedge gain/(loss)		1,402	(5,049)
Foreign currency translation differences for foreign operations		(12,752)	3,497
Net loss on hedge of net investment in foreign operations		(2,281)	—
Income tax on items of other comprehensive income	6	885	—
Other comprehensive income for the period net of tax		(12,746)	(1,552)
Total comprehensive income for the period		(100,853)	20,849
Attributable to:			
Equity holders of the parent		(100,223)	19,683
Non controlling interest		(630)	1,166
		(100,853)	20,849

The notes on pages 34 to 86 are an integral part of these consolidated financial statements.

Consolidated statement of changes of equity as at 30 June 2010

In thousands of AUD	Note	Share capital	Retained earnings	Option reserve	Cash flow hedge reserve	Foreign currency translation reserve	Total	Non controlling interest	Total equity
Opening balance at 1 July 2008		180,371	10,850	5,914	697	(9,997)	187,835	1,815	189,650
Profit for the period		–	21,408	–	–	–	21,408	993	22,401
Other comprehensive income for the period		–	–	–	(5,049)	3,324	(1,725)	173	(1,552)
Total comprehensive income for the period		–	21,408	–	(5,049)	3,324	19,683	1,166	20,849
Transactions with owners recorded directly in equity:									
Shares issued	23	77,042	–	–	–	–	77,042	–	77,042
Shares issued as part of business combinations	23	1,371	–	–	–	–	1,371	–	1,371
Tax effect of transaction costs	23	862	–	–	–	–	862	–	862
Share issue costs	23	(4,146)	–	–	–	–	(4,146)	–	(4,146)
Non controlling interests acquired		–	–	–	–	–	–	10	10
Dividends paid to equity holders	23	–	(23,563)	–	–	–	(23,563)	(998)	(24,561)
Share option expense		–	–	3,628	–	–	3,628	–	3,628
Closing balance at 30 June 2009		255,500	8,695	9,542	(4,352)	(6,673)	262,712	1,993	264,705
Opening balance at 1 July 2009		255,500	8,695	9,542	(4,352)	(6,673)	262,712	1,993	264,705
Profit/(Loss) for the period		–	(87,566)	–	–	–	(87,566)	(541)	(88,107)
Other comprehensive income for the period net of tax		–	–	–	2,287	(14,944)	(12,657)	(89)	(12,746)
Total comprehensive income for the period		–	(87,566)	–	2,287	(14,944)	(100,223)	(630)	(100,853)
Transactions with owners recorded directly in equity:									
Shares issued	23	114,749	–	–	–	–	114,749	–	114,749
Shares issued as part of business combinations	23	3,732	–	–	–	–	3,732	–	3,732
Tax effect of share issue costs	23	1,015	–	–	–	–	1,015	–	1,015
Share issue costs	23	(5,728)	–	–	–	–	(5,728)	–	(5,728)
Dividends paid to equity holders	23	–	(12,976)	–	–	–	(12,976)	(718)	(13,694)
Share option expense		–	–	2,267	–	–	2,267	–	2,267
Closing balance at 30 June 2010		369,268	(91,847)	11,809	(2,065)	(21,617)	265,548	645	266,193

The notes on pages 34 to 86 are an integral part of these consolidated financial statements.

Consolidated statement of financial position as at 30 June 2010

In thousands of AUD	Note	2010	Consolidated 2009
Assets			
Cash and cash equivalents	8	22,762	23,559
Trade and other receivables	9	92,901	110,025
Other assets	10	12,139	18,707
Income tax receivable	12	9,263	—
Total current assets		137,065	152,291
Receivables	9	570	991
Other financial assets	11	565	223
Investments in equity accounted investees	13	—	10,132
Deferred tax assets	14	13,464	9,117
Plant and equipment	15	18,002	20,691
Other assets	10	1,151	2,337
Intangible assets	16	662,551	580,781
Total non-current assets		696,303	624,272
Total assets	2	833,368	776,563
Liabilities			
Trade and other payables	17	76,098	81,901
Deferred consideration payables	18	78,848	66,708
Interest-bearing loans and borrowings	19	45,540	35,927
Employee benefits	20	8,681	8,286
Income tax payable	12	2,952	6,907
Provisions	22	7,876	2,265
Total current liabilities		219,995	201,994
Trade and other payables	17	26	23
Deferred consideration payables	18	90,690	44,724
Interest-bearing loans and borrowings	19	241,490	248,392
Deferred tax liabilities	14	10,592	11,851
Employee benefits	20	1,666	1,710
Provisions	22	2,716	3,164
Total non-current liabilities		347,180	309,864
Total liabilities	2	567,175	511,858
Net assets		266,193	264,705
Equity			
Issued capital	23	369,268	255,500
Reserves		(11,873)	(1,483)
Retained earnings		(91,847)	8,695
Total equity attributable to equity holders of the parent		265,548	262,712
Non controlling interest		645	1,993
Total equity		266,193	264,705

The notes on pages 34 to 86 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows for the year ended 30 June 2010

In thousands of AUD	Note	2010	Consolidated 2009
Cash flows from operating activities			
Cash receipts from customers		663,171	721,070
Cash paid to suppliers and employees		(591,542)	(645,532)
Cash generated from operations		71,629	75,538
Interest received		426	724
Income taxes paid		(17,247)	(17,353)
Interest paid		(19,076)	(21,687)
Dividends received		—	102
Net cash from operating activities	29	35,732	37,324
Cash flows from investing activities			
Proceeds from disposal of non current assets		718	523
Payments of deferred consideration		(108,621)	(34,174)
Payments for equity accounted investments	13	(423)	(399)
Acquisition of controlled entities, net of cash acquired	28	(16,848)	(5,443)
Acquisition of plant and equipment		(4,284)	(6,126)
Acquisition of intangibles	16	(5,747)	—
Development expenditure	16	(4,876)	(6,155)
Net cash used in investing activities		(140,081)	(51,774)
Cash flows from financing activities			
Proceeds from the issue of share capital	23	114,673	76,589
Proceeds from the exercise of options	23	—	338
Transaction costs for the issue of share capital	23	(5,728)	(4,146)
Proceeds from borrowings		126,703	46,549
Repayment of borrowings		(115,349)	(90,041)
Finance lease payments		(2,343)	(2,550)
Dividends paid to shareholders of Photon Group Limited		(12,976)	(23,564)
Dividends paid to non controlling interest in controlled entities		(718)	(1,243)
Net cash from financing activities		104,262	1,932
Net increase in cash and cash equivalents		(87)	(12,518)
Effect of exchange rate fluctuations on cash held		(710)	1,032
Cash and cash equivalents at 1 July		23,559	35,045
Cash and cash equivalents at 30 June	8	22,762	23,559

The notes on pages 34 to 86 are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements for the year ended 30 June 2010

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1. Significant accounting policies

Photon Group Limited (the "Company") is a Company domiciled in Australia. The address of the Company's registered office is Level 9, 155 George St Sydney, NSW 2000. The consolidated financial statements of the Company as at and for the year ended 30 June 2010 comprises the Company and its subsidiaries (together referred to as the "Consolidated Entity") and the Consolidated Entity's interest in associates.

The financial statements for the year ended 30 June 2010 were authorised for issue in accordance with a resolution of the Directors on 30 September 2010.

(a) Statement of compliance

The consolidated financial statements are a general purpose financial report which has been prepared in accordance with Australian Accounting Standards ("AASBs") (including Australian Interpretations) adopted by the Australian Accounting Standards Board ("AASB") and the *Corporations Act 2001*. The consolidated financial statements comply with International Financial Reporting Standards (IFRS) and interpretations adopted by the International Accounting Standards Board (IASB).

(b) Basis of preparation

(i) Basis of measurement

The financial statements are prepared on the historical cost basis except for the items as described in Note 1(y).

Notwithstanding the net current liabilities and the after tax loss during the year, the consolidated financial statements have been prepared on a going concern basis which assumes the Consolidated Entity will continue its operations and be able to meet its obligations as and when they become due and payable. This assumption is based on the successful completion of the recapitalisation proposal as described in Note 32 Subsequent events, which took place on 29 September 2010 after being approved by shareholders on 17 September 2010 at a general meeting. The recapitalisation proposal includes:

- raising a minimum of \$102,500,000 through an underwritten entitlement offer and placement;
- a restructure of the deferred consideration payments, including capping substantially all of the future expected payments and restructuring the timing and form of the payments; and
- refinancing the Consolidated Entity's debt facilities, including extending the debt facilities term to expire in September 2013 and establishing a bank guarantee facility to provide support to a portion of the deferred consideration payments.

The effect of the recapitalisation proposal is that it will enable the Consolidated Entity to make deferred consideration payments due by 30 September 2010 and avoid being in breach of financial covenants under the debt facilities at that date. The completion of the recapitalisation proposal will also provide funding capacity, along with operating cash flow to meet future deferred consideration payments.

(ii) Functional and presentation currency

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

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the consolidated financial statements and Directors' Report have been rounded off to the nearest thousand dollars, unless otherwise stated.

(iii) Use of estimates and judgements

The preparation of financial statements in conformity with AASBs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. Refer to accounting policy 1(y) for further details on critical accounting estimates and judgements.

(iv) Changes in accounting policies

Starting as of 1 July 2009, the Consolidated Entity has changed its accounting policies in the following areas:

- Accounting for business combinations
- Accounting for acquisitions of non controlling interests
- Presentation of financial statements

Other than the above, the accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements.

Certain comparative amounts have been re-classified to conform with the current year's presentation.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

(c) Basis of consolidation

(i) Business combinations

Change in accounting policy

The Consolidated Entity has adopted revised AASB 3 *Business Combinations* (2008) and amended AASB 127 *Consolidated and Separate Financial Statements* (2008) for business combinations occurring in the financial year starting 1 July 2009. All business combinations occurring on or after 1 July 2009 are accounted for by applying the acquisition method. The change in accounting policy is applied prospectively and had no material impact on earnings per share.

The Consolidated Entity has applied the acquisition method for the business combinations disclosed in Note 28 Acquisitions of subsidiaries and non controlling interests.

For every business combination, the Consolidated Entity identifies the acquirer, which is the combining entity that obtains control of other combining entities or businesses. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Consolidated Entity takes into consideration potential voting rights that currently are exercisable. The acquisition date is the date on which control is transferred to the acquirer. Judgement is applied in determining the acquisition date and determining whether control is transferred from one party to another.

Measuring goodwill

The Consolidated Entity measures goodwill at fair value of the consideration transferred including the recognised amount of any non controlling interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as of the acquisition date.

Consideration transferred includes the fair values of the assets transferred, liabilities incurred by the Consolidated Entity to the previous owners of the acquiree, and equity interests issued by the Consolidated Entity. Consideration transferred also includes the fair value of any contingent consideration and share-based payment awards of the acquiree that are replaced mandatorily in the business combination.

Contingent liabilities

A contingent liability of the acquiree assumed in a business combination only if such a liability represents a present obligation and arises from a past event, and its fair value can be measured reliably.

Non controlling interest

The Consolidated Entity measures any non controlling interest at its proportionate interest in the identifiable net assets of the acquiree.

Transaction costs

Transaction costs that the Consolidated Entity incurs in connection with a business combination, such as finders' fees, legal fees, due diligence fees, and other professional and consulting fees, are expensed as incurred.

(ii) Accounting for acquisitions of non controlling interests

Change in accounting policy

The Consolidated Entity has adopted revised AASB 3 *Business Combinations* (2008) and amended AASB 127 *Consolidated and Separate Financial Statements* (2008) for acquisitions of non controlling interests occurring in the financial year starting 1 July 2009. Under the new accounting policy, acquisitions of non controlling interests are accounted for as transactions with equity holders in their capacity as equity holders and therefore no goodwill is recognised as a result of such transactions. Previously, goodwill was recognised arising on the acquisition of non controlling interest in a subsidiary; and that represented the excess of the cost of the additional investment over the carrying amount of the interest in the net assets acquired at the date of exchange. The change in accounting policy was applied prospectively and had no material impact on earnings per share.

(iii) Subsidiaries

Subsidiaries are entities controlled by the Consolidated Entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies of the Consolidated Entity.

(iv) Investments in associates (equity accounted investees)

Associates are those entities in which the Consolidated Entity has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Consolidated Entity holds between 20 and 50 per-cent of the voting power of another entity.

Investments in associates are accounted for using the equity method (equity accounted investees) and are initially recognised at cost. The Consolidated Entity's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The consolidated financial statements include the Consolidated Entity's share of the total recognised gains and losses of associates on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases. The Consolidated Entity's share of movements in reserves is recognised directly in consolidated reserves. When the Consolidated Entity's share of losses exceeds its interest in an associate, the Consolidated Entity's carrying amount is reduced to nil and recognition of further losses is discontinued, except to the extent that the Consolidated Entity has incurred legal or constructive obligations or made payments on behalf of an associate.

(v) Transactions eliminated on consolidation

Intra-group balances, and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with associates are eliminated to the extent of the Consolidated Entity's interest in the entity with adjustments made to the "Investment in associates" and "Share of associate's net profit" accounts. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Gains and losses are recognised as the contributed assets are consumed or sold by the associate or, if not consumed or sold by the associate, when the Consolidated Entity's interest in such entities is disposed of.

(d) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Consolidated Entities at the foreign exchange rate ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the respective functional currencies of the Consolidated entities at the foreign exchange rate ruling at that date. Foreign exchange differences arising on re-translation are recognised in the income statement, except for differences arising on the retranslation of available-for-sale equity instruments and a financial liability designated as a hedge of the net investment in a foreign operation, which are recognised directly in equity (see (iii) below). Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

(ii) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to Australian dollars at foreign exchange rates prevailing at the reporting date. The income and expenses of foreign operations are translated to Australian dollars at rates approximating the foreign exchange rates ruling at the dates of the transactions.

Foreign currency differences are recognised in other comprehensive income. Since 1 July 2004, the date of transition to AASBs, such differences have been recognised in the foreign currency translation reserve (FCTR). When a foreign operation is disposed of, in part or in full, the relevant amount in the FCTR is transferred to profit or loss as part of the profit or loss on disposal.

Foreign exchange gains and losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely in the foreseeable future, are considered to form part of a net investment in a foreign operation and are recognised in other comprehensive income, and are presented within equity in the FCTR.

(iii) Hedge of net investment in foreign operations

Foreign currency differences arising from the retranslation of a financial liability designated as a hedge of the net investment in foreign operations are recognised in other comprehensive income to the extent that the hedge is effective, and are presented within equity in the FCTR. To the extent that the hedge is ineffective, such differences are recognised in profit or loss. When the hedged net investment is disposed of, the relevant amount in the FCTR is transferred to profit or loss as an adjustment to the profit or loss on disposal.

(e) Financial instruments

Non derivative financial assets

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

The Consolidated Entity derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive 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 Consolidated Entity is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the 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.

The Consolidated Entity has the following non-derivative financial assets: loans and receivables, work in progress and cash and cash equivalents.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value, plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables comprise trade and other receivables. Trade and other receivables are stated at their cost less impairment losses (see accounting policy (h)). The collectability of debts is assessed at reporting date, and specific provision is made for any doubtful accounts. Bad debts are written off as incurred.

Work in progress represents accrued revenue recognised in accordance with accounting policy (l) together with rechargeable disbursements.

Cash and cash equivalents comprise cash balances and call deposits with original maturities of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Consolidated Entity's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Non derivative financial liabilities

The Consolidated Entity initially recognises debt securities issued and subordinated liabilities on the date 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 Consolidated Entity becomes a party to the contractual provisions of the instrument. The Consolidated Entity derecognises a financial liability when its contractual obligations are discharged or cancelled or expire. Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Consolidated Entity 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.

The Consolidated Entity has the following non derivative financial liabilities: loans and borrowings, bank overdrafts and trade and other payables.

Such financial liabilities are recognised initially at fair value, plus any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortised cost using the effective interest rate method.

Derivative financial instruments including hedging accounting

The Consolidated Entity uses derivative financial instruments to hedge its exposure to interest rate risks and foreign currency exposure arising from operational, financing and investment activities. In accordance with its treasury policy, the Consolidated Entity does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

On initial designation of the hedge, the Consolidated Entity formally documents the relationship between the hedging instrument(s) and hedged item(s), including the risk management and strategy in undertaking the hedge transaction, together with the methods that will be used to assess the effectiveness of the hedging relationship. The Consolidated Entity makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, whether the hedging instruments are expected to be "highly effective" in offsetting the changes in fair value or cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80–125 per-cent. For a cash flow hedge of a forecast transaction, the transaction should be highly probable to occur and should present an exposure to variations in cash flows that could ultimately affect reported net income.

Derivatives are recognised initially at fair value and attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, derivatives are measured at fair value and changes therein are described below.

Cash flow hedges

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised in other comprehensive income to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in profit or loss.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in other comprehensive income is transferred to the carrying amount of the asset when it is recognised. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is recognised immediately in profit and loss. In other cases the amount recognised in other comprehensive income is transferred to profit or loss in the same period that the hedged item affects profit or loss.

(f) Plant and equipment

(i) Recognition and measurement

Items of plant and equipment are stated at cost or deemed cost less accumulated depreciation (see below) and impairment losses (see accounting policy (h)). The cost of plant and equipment at 1 July 2004, the date of transition to AASBs, was measured on the basis of deemed cost and was determined by reference to its fair value at that date.

Cost includes expenditure that is directly attributable to the acquisition of the asset. Purchased software, that is integral to the functionality of the related equipment, is capitalised as part of that equipment.

Where parts of an item of plant and equipment have different useful lives, they are accounted for as separate items of plant and equipment.

Gains and losses on disposal of an item of plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of plant and equipment and are recognised net within "other income" in profit or loss.

(ii) Leased assets

Leases in terms of which the Consolidated Entity assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases; the leased assets are not recognised on the Consolidated Entity's statement of financial position.

The Consolidated Entity recognises in the carrying amount of an item of property, plant and equipment, the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied within the item will flow to the Consolidated Entity and the cost of the item can be measured reliably. The carrying amount of the replaced part is de-recognised. All other costs are recognised in the income statement as an expense as incurred.

(iv) Depreciation

Depreciation is charged to the income statement on both a straight-line and diminishing value basis, as indicated below, over the estimated useful lives of each part of an item of property, plant and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Consolidated Entity will obtain ownership by the end of the lease term. Land is not depreciated. The estimated useful lives in the current and comparative periods are as follows:

	2010		2009	
	Straight line	Diminishing Value	Straight line	Diminishing Value
Computer equipment	25%–40%	20%–40%	25%–40%	20%–40%
Office furniture and equipment	5%–25%	5%–40%	5%–25%	5%–40%
Plant and equipment	10%–25%	–	10%–25%	–
Leasehold improvements	Life of lease	Life of lease	Life of lease	Life of lease
Plant and equipment under finance lease	Life of lease	Life of lease	Life of lease	Life of lease

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

(g) Intangible assets

(i) Goodwill

Goodwill arises on the acquisition of subsidiaries and associates.

Change in accounting policy

As from 1 July 2009, the Consolidated Entity has adopted the revised AASB 3 *Business Combinations* (2008) and amended AASB 127 *Consolidated and Separate Financial Statements* (2008). Revised AASB 3 and AASB 127 have been applied prospectively for business combinations with an acquisition date on or after 1 July 2009.

For details on the initial recognition and measurement of goodwill related to business combinations that occurred during the financial year ended 30 June 2010, see note 28.

Acquisitions of non controlling interests

Acquisitions of non controlling interests are accounted for as transactions with equity holders in their capacity as equity holders and therefore no goodwill is recognised as a result of such transactions.

Subsequent measurement

Goodwill is measured at cost, less accumulated impairment losses. In respect of equity accounted investees, the carrying amount of the investment, and an impairment loss on such an investment is not allocated to any assets, including goodwill, that forms part of the carrying amount of equity accounted investee.

Deferred consideration on acquisitions is provided based on management's best estimate of the liability at the reporting date. The liability is discounted using a market interest rate for the liability and a present value interest charge is included in the income statement as the discount unwinds. Fair value adjustments through profit and loss are made in relation to changes to estimates of the fair value of amounts payable of the deferred consideration.

Business combinations between 1 July 2004 and 30 June 2009

All business combinations between 1 July 2004 and 30 June 2009 are accounted for by applying the purchase method. The cost of acquisition is measured at the aggregate of the fair values, at the time of exchange, of assets given, liabilities incurred or assumed and equity instruments issued in exchange for control of the acquiree, plus any costs attributable to the business combination. Goodwill represents the difference between the cost of the acquisition and the fair value of net assets, liabilities and contingent liabilities acquired.

Deferred consideration on acquisitions is provided based on management's best estimate of the liability at the reporting date. The liability is discounted using a market interest rate for the liability and a present value interest charge is included in the income statement as the discount unwinds. Changes to estimates of amounts payable are made by adjusting deferred consideration using the original interest rate, together with goodwill.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

Business combinations prior to 1 July 2004

As part of the transition to AASBs, the classification and accounting treatment of business combinations that occurred prior to 1 July 2004 has been recognised under the Consolidated Entity's previous accounting framework, Australian GAAP.

Goodwill allocation to cash generating units

Goodwill is allocated to cash generating units expected to benefit from synergies created by the business combination and is tested for impairment annually or more frequently if events or changes in circumstances indicate the carrying value may be impaired.

Negative goodwill arising on an acquisition is recognised immediately in profit or loss.

(ii) Research and development

Expenditure on research activities, undertaken with the prospect of gaining new technical knowledge and understanding, is recognised in the income statement as an expense as incurred.

Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes (including internally developed software), is capitalised only if development costs can be reliably measured, the product or process is technically and commercially feasible, future economic benefits are probable and the Consolidated Entity 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 and an appropriate proportion of overhead costs that are directly attributable to preparing the asset for its intended use. Other development expenditure is recognised in the income statement as an expense as incurred. Capitalised development expenditure is measured at cost, less accumulated amortisation (see below) and impairment losses (see accounting policy (h)).

(iii) Other intangible assets

Other intangible assets that are acquired by the Consolidated Entity are stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy (h)). For each business combination, a review is completed to identify any intangible assets and a valuation of fair value is performed for all intangible assets identified.

Expenditure on internally generated goodwill and brands is recognised in the income statement as an expense as incurred.

(iv) Subsequent expenditure

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

(v) Amortisation

Amortisation is calculated over the cost of the asset, or another amount substituted for cost, less its residual value.

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Goodwill is systematically tested for impairment each year at the same time. Other intangible assets are amortised from the date they are available for use. The estimated useful lives in the current and comparative periods are as follows:

- IT related intellectual property – 2 to 8 years
- Customer contracts – 3 to 4 years
- Customer relationships – 2 to 8 years
- Brand names – 6 years
- Internally generated intangibles – 2 to 5 years

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

(h) Impairment

(i) Financial assets (including receivables)

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Consolidated Entity on terms that the Consolidated Entity would not consider otherwise, indications that a debtor or issuer will enter bankruptcy, the disappearance of an active market for a security.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. Losses are recognised in profit and loss and reflected in an allowance account against receivables. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit and loss.

The Consolidated Entity considers evidence of impairment for receivables at a specific asset level. In assessing impairment the Consolidated Entity uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred/ adjusted for management's judgement. The remaining financial assets are assessed collectively, which share similar credit risk characteristics.

(ii) Non financial assets

The carrying amounts of the Consolidated Entity's non-financial assets, other than 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. For goodwill and intangible assets that are not yet available for use, the recoverable amount is estimated each year at the same time.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value, less costs to sell. In assessing value in use, the estimated future post tax cash flows are discounted to their present value using a post tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purposes 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 groups of assets (the "cash generating unit"). Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, cash generating units (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. Goodwill acquired in a business combination is allocated to the CGU that are expected to benefit from the synergies of the combination.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit (CGU) exceeds its recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGU are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. 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.

(i) Share capital

(i) Ordinary shares

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

(ii) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(iii) Transaction costs

Transaction costs of an equity transaction are accounted for as a deduction from equity, net of any related income tax benefit.

(j) Employee Benefits

(i) Long-term employee benefits

The Consolidated Entity's net obligation in respect of long-term service benefits, other than pension plans, is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using expected future increases in wage and salary rates including related on-costs and

expected settlement dates, and is discounted using the rates attached to the Commonwealth Government bonds at the reporting date which have maturity dates approximating to the terms of the Consolidated Entity's obligations.

(ii) Wages, salaries, annual leave, and non-monetary benefits

Liabilities for employee benefits for wages, salaries, and annual leave that are due to be settled within 12 months of the reporting date, represent present obligations resulting from employees' services provided to reporting date, and are calculated at undiscounted amounts based on remuneration wage and salary rates that the Consolidated Entity expects to pay as at reporting date including related on-costs, such as workers compensation insurance, statutory superannuation and payroll tax.

A provision is recognised for the amount expected to be paid under short-term cash bonus or profit sharing plans if the Consolidated Entity has a present legal or constructive obligation to pay this amount as a result of past services provided by the employee and the obligation can be reliably estimated.

(iii) Termination benefits

Termination benefits are recognised as an expense when the Consolidated Entity is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the Consolidated Entity has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

(iv) Share-based payment transactions

The grant date fair value of share-based payment awards granted to employees is recognised and an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that meet the related services 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.

(k) Provisions

A provision is recognised in the statement of financial position when the Consolidated Entity has a present legal or constructive obligation as a result of a past event, 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, where appropriate, the risks specific to the liability. The unwinding of the discount is recognised as finance costs.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

(i) Make good provision

The Consolidated Entity has made provision for make good on all operating leases for premises which require make good expenditure at completion of the lease. The amount of the provision for make good is capitalised and then amortised over the remaining term of the individual leases. The provision is the best estimate of the expenditure required to settle the make good obligation. Future make good costs are reviewed annually and any changes are reflected in the provision at the end of the reporting period.

(ii) Lease incentive provision

The Consolidated Entity has made provision for lease incentives received. Lease incentives received are recognised in the income statement as an integral part of the total lease expense spread over the lease term.

(iii) Restructuring

A provision for restructuring is recognised when the Consolidated Entity has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

(iv) Onerous contracts

A provision for onerous contracts is recognised when the expected benefits to be derived by the Consolidated Entity from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Consolidated Entity recognises any impairment loss on the assets associated with that contract.

(l) Revenue

All operating revenue from services rendered is recognised in the income statement in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is determined by reference to outputs and deliverables in connection to the completion of the service. No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the costs incurred or to be incurred cannot be measured reliably.

Gross revenue represents billings to clients, inclusive of costs of sales, relating to Consolidated Entity subsidiaries where a principal relationship exists between the entity and its client. Where the Consolidated Entity subsidiaries act as an agent, the amount included as revenue is recognised net of amounts collected/paid on behalf of clients.

Net revenue is the amount that flows to the Consolidated Entity net of directly attributable cost of sales. Directly attributable cost of sales includes any project related costs.

(i) Advertising, media and production revenue

Advertising, media and production revenues are recognised net of directly attributable cost of sales.

(ii) Retainer fees and commissions

Retainer fees which arise as part of a contract to provide services to a client are recognised over the term of the contract on a straight-line basis, unless there is some other method that better represents the stage of completion.

Commissions-based client revenue is recognised as the service is performed.

(iii) Licences and other intangible rights

The Consolidated Entity allocates revenue to each element in software or other intangible right arrangements involving multiple elements, based on the estimated relative fair value of each element. The typical elements in the multiple element arrangement are licence and maintenance fees. The Company's determination of fair value is based on the price charged when the same element is sold separately or cost plus a reasonable margin in other cases.

Revenue from the sales of licences, where the licence period is for the major part of the economic life of the software or other intangible right, is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer.

In other cases, revenue from licences is recognised ratably over the term of the agreement.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due, the costs incurred, or to be incurred, cannot be measured reliably, there is a risk of return of goods or there is continuing management involvement to the degree usually associated with ownership or effective control of the goods.

(iv) Interest

Interest income is recognised in the income statement as it accrues, using the effective interest method.

(m) Lease payments

(i) Operating lease payments

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

(ii) Finance lease payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge 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.

The interest expense component of finance lease payments is recognised in the income statement using the effective interest method.

(iii) Determining whether an arrangement contains a lease

At inception of an arrangement, the Consolidated Entity determines whether such an 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 specific asset. An arrangement conveys the right to use the asset if the arrangement conveys to the Consolidated Entity the right to control the use of the underlying asset. At inception or upon reassessment of the arrangement, the

Consolidated Entity separates payments and other consideration required by such an arrangement into those for the lease and those for other elements on the basis of their relative fair values. If the Consolidated Entity concludes for a finance lease, that it is impracticable to separate the payments reliably, an asset and a liability are recognised at an amount equal to the fair value of the underlying asset. Subsequently the liability is reduced as payments are made and an imputed finance charge on the liability is recognised using the Consolidated Entity's incremental borrowing rate.

(n) Finance Income and Expenses

Finance income comprises interest income on funds invested, dividend income and gains on hedging instruments that are recognised in profit or loss. Interest income is recognised as it accrues, using the effective interest method. Dividend income is recognised on the date that the Consolidated Entity's right to receive payment is established, which in the case of quoted securities is the ex-dividend date.

Finance expenses comprise interest expense on borrowings, present value interest charges with respect to the deferred consideration of acquisitions, unwinding of the discount on provisions and losses on hedging instruments that are recognised in profit or loss. All borrowing costs are recognised in profit or loss using the effective interest method.

(o) Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Current and deferred tax is recognised in the income statement except, to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of, temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date. 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 only to the extent that it is probable that future taxable profits will be available, against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

(p) Segment reporting

The Consolidated Entity early adopted AASB 8 *Operating Segments* in the year ended 30 June 2009, in which the Consolidated Entity determines and presents segments based on the information that is provided internally to the CEO, who is the Consolidated Entity's chief operating decision maker.

An operating segment is a component of the Consolidated Entity that engages business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Consolidated Entity's other components. All operating segment's operating results are regularly reviewed by the Consolidated Entity's CEO to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the CEO include items directly attributable to a segment, as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly of costs associated with the centralised management and governance of the Consolidated Entity, such as interest bearing loans, costs of borrowings and related expenses, and corporate head office assets and expenses.

Segment capital expenditure, development expenditure and acquisition of intangibles are the total cost incurred during the period to acquire plant and equipment, and intangible assets other than goodwill.

(q) Goods and services tax

Revenue, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the Australian Taxation Office (ATO) is included as a current asset or liability in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

(r) Earnings per share

The Consolidated Entity presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit and loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible share options granted to employees.

(s) Presentation of financial statements

The Consolidated Entity applies revised AASB 101 *Presentation of Financial Statements* (2007) which became effective as of 1 January 2009. As a result the Consolidated Entity presents in the consolidated statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the consolidated statement of comprehensive income.

Comparative information has been re-presented so that it is in conformity with the revised standard. Since the change in accounting policy only impacts presentation aspects, there is no impact on earnings per share.

(t) New standards and interpretations not yet adopted

The following standards, amendments to standards and interpretations have been identified as those which may impact the entity in the period of initial application. They are available for early adoption at 30 June 2010, but have not been applied in preparing the financial statements.

- AASB 9 *Financial Instruments* includes requirements for the classification and measurement of financial assets resulting from the first part of Phase 1 of the project to replace AASB 139 *Financial Instruments: Recognition and Measurement*. AASB 9 will become mandatory for the Consolidated Entity's 30 June 2014 financial statements. Retrospective application is generally required, although there are exceptions, particularly if the entity adopts the standard for the year ended 30 June 2012 or earlier. The Consolidated Entity has not yet determined the potential effect of the standard.
- AASB 124 *Related Party Disclosures* (revised December 2009) simplifies and clarifies the intended meaning of the definition of a related party and provides a partial exemption from the disclosure requirements of a government related entity. The amendments, which will become mandatory for the Consolidated Entity's 30 June 2012 financial statements, are not expected to have any impact on the financial statements.

- AASB 2009 - 5 *Further amendments to Australian Accounting Standards arising from the Annual Improvements process* affect various AASBs resulting in minor changes for presentation, disclosure, recognition and measurement purposes. The amendments, which become mandatory for the Consolidated Entity's 30 June 2011 financial statements, are not expected to have a significant impact on the financial statements.
- AASB 2009 – 8 *Amendments to Australian Accounting Standards – Group Cash-settled Share-Based Payment Transactions* resolves diversity in practice regarding the attribution of cash-settled share-based payments between different entities within a group. As a result of the amendments AI 8 Scope of AASB 2 and AI 11 AASB 2 – *Group and Treasury Share Transactions* will be withdrawn from the application date. The amendments, which become mandatory for the Group's 30 June 2011 financial statements, are not expected to have a significant impact on the financial statements.

(u) Determination of fair values

A number of the Consolidated Entity's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(i) Intangible assets

The fair value of other intangible assets acquired is based on valuation techniques generally using the excess earnings method.

(ii) Trade and other receivables

The fair value of other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. The fair value is determined for disclosure purposes only.

(iii) Derivatives

The fair value of interest rate swaps is based on market valuation, which includes estimated future cash flows based on the terms and maturity of each contract. The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate.

(iv) Share-based payment transactions

The fair value of employee share options is measured using the Black Scholes, Binomial Model or Monte Carlo Sampling. Measurement inputs include share price on measurement date, exercise price of the instruments, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk free interest rate (based on government bonds). Service and non market performance conditions attached to the transactions are not taken into account in determining fair value.

(v) Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. For finance leases the market rate of interest is determined by reference to similar lease arrangements.

(v) Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that may have a financial impact on the entity and that are believed to be reasonable under the circumstances.

The Consolidated Entity makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, not always equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(i) Estimated impairment of goodwill

The Consolidated Entity tests annually whether there is any impairment of goodwill. The recoverable amounts of cash-generating units have been determined by applying a 'value in use' method using assumptions of future profit margins and cash flows. Refer to Note 16 for the details of these assumptions and the potential impact of changes to the assumptions.

(ii) Intangible assets and business combinations

AASB 3 *Business Combinations* and AASB 138 *Intangible Assets*, the Australian standards on business combinations and intangibles respectively, require the acquirer to separately identify the acquiree's identifiable assets and liabilities, including other intangibles arising on acquisition. This means that the acquirer must recognise other intangible assets, separately from goodwill, where the definition of an intangible asset is met and the fair value of the intangible asset can be measured reliably.

Where significant business acquisitions are undertaken, the Directors commission an independent expert, having satisfied themselves that the expert was appropriately qualified to form a view and to assist them in determining the valuation of intangible assets separately identified and recognised as part of the business combination.

For further details, refer to Note 16 Intangible assets and Note 28 Acquisitions of subsidiaries and non controlling interests.

(iii) Share-based payments

The grant date fair value of share-based payment arrangements is determined by an appropriately qualified independent expert commissioned by the Directors. Inputs to the determination of fair value are subjective and include the market value of the instrument on the grant date, expected volatility of the Company's share price, the risk free interest rate, the dividend yield, the expected life of the instrument and the exercise price. Certain of these inputs are estimates.

The Directors review the methodologies used by the expert and make enquiries with management to assure themselves that the factual information used by the expert is correct prior to relying on the expert's opinion. Refer to Note 20 for further details.

(iv) Deferred consideration liability

Certain acquisitions of subsidiaries made by the Consolidated Entity contain arrangements for further consideration to be paid to vendors subject to certain targets being met. At each reporting date an estimate is made of whether such targets will be achieved and the Consolidated Entity's liability, based on the achievement of such targets. The estimate is based on budgets and forecasts prepared by management of the subsidiary, subject to potential additional consideration. The nature of the arrangements means that at the reporting date there is uncertainty around the amount and timing of the liability to be paid in the future under such deferred consideration arrangements.

The uncertainty around such liabilities increasing was reduced subsequent to the reporting date, as substantially all the arrangements which include deferred consideration liabilities were renegotiated such that liabilities were capped at approximately the amount of the estimated liability at 30 June 2010. This maximum capped amount was based on the best estimate of expected payments using management budgets and forecasts for future years of individual subsidiaries and the Consolidated Entity as a whole. There is still uncertainty around the actual payments that will be made as the budgeted and forecast targets must still be met by the subsidiaries for the vendors to receive the maximum capped amount determined to be the outstanding liability subsequent to the reporting date. Actual future payments may be below the capped amounts. Refer to Notes 18 and 32 for further details on the restructure of the deferred consideration liability after the reporting date.

Notes to the consolidated financial statements for the year ended 30 June 2010

1. Significant accounting policies (continued)

(v) Impairment of receivables

The Consolidated Entity carries trade receivables at amortised cost less impairment. The impairment of these receivables is an estimate based on whether there is evidence suggesting that an event has occurred leading to a negative effect on the estimated future cash inflow. Events subsequent to the reporting date but prior to the signing of the financial statements which indicate a negative effect are taken into effect in the calculation of impairment. Future events may occur which change these estimates of the future cash inflows related to impaired trade receivables.

2. Operating segments

The Consolidated Entity has realigned its organisational structure and now focuses on four business divisions which are the entity's operating segments based on regularly reviewed internal reporting and management by the Chief Executive Officer and the management team (the chief operating decision makers). The divisions are the basis for assessing performance and determining allocation of resources.

The operating segments are defined by management, based on the manner in which the services are provided and the geographies which each segment operates in, and report to the Chief Executive Officer and the management team on a monthly basis. Each operating segment is a reportable segment, and these are the sources of the Consolidated Entity's major risks and returns.

The Consolidated Entity considers it now operates in four segments:

- International Agencies – International specialised marketing services weighted towards public relations, communications strategy and research and data analytics.
- Australian Agencies – Focused on providing a broad spectrum of marketing services to Australian clients including above the line advertising, direct marketing, promotional campaigns, consumer research, public relations, corporate communications and digital agency services.
- Australian Field Marketing – Outsourced sales forces and point of sale marketing.
- International Internet – primarily US facing search marketing group.

Inter-segment pricing is determined on an arm's length basis.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly of costs associated with the centralised management and governance of Photon Group Limited, such as interest bearing loans, costs of borrowings and related expenses, and corporate head office assets and expenses.

Segment capital expenditure and development expenditure is the total cost incurred during the period to acquire assets that are expected to be used for more than one period.

The measure of reporting to the chief operating decision maker is on a normalised EBITDA basis, which excludes significant items which are separately presented because of their nature, size and expected infrequent occurrence.

In relation to segment reporting the following definitions apply to operating segments:

Normalised EBITDA – earnings before one off items, interest, taxes, depreciation, amortisation and impairment charges.

EBITDA – earnings before interest, taxes, depreciation, amortisation and impairment charges.

EBIT – earnings before interest, taxes and impairment charges.

The 30 June 2009 comparative amounts have been restated to reflect the current business segment presentation.

2010 In thousands of AUD	International Agencies	Australian Agencies	Field Marketing	International Internet	Unallocated	Eliminations	Consolidated
Gross revenue	143,661	286,205	125,783	38,317	–	(6,707)	587,259
Directly attributable cost of sales	(43,607)	(137,191)	(7,317)	(27,244)	–	6,707	(208,652)
Net revenue	100,054	149,014	118,466	11,073	–	–	378,607
Other operating income	280	306	41	165	–	–	792
Total revenue	100,334	149,320	118,507	11,238	–	–	379,399
Operating expenses	(76,007)	(121,197)	(99,200)	(17,711)	(18,485)	–	(332,600)
Significant costs	862	3,908	1,196	12,962	9,446	–	28,374
Normalised EBITDA	25,189	32,031	20,503	6,489	(9,039)	–	75,173
Reconciliation to EBITDA							
Significant costs	(862)	(3,908)	(1,196)	(12,962)	(9,446)	–	(28,374)
EBITDA	24,327	28,123	19,307	(6,473)	(18,485)	–	46,799
Depreciation & amortisation expenses							(21,096)
EBIT							25,703
Share of loss of equity accounted investee				(117)			(117)
Impairment of investment in equity accounted investee				(2,059)			(2,059)
Impairment of intangibles				(86,871)			(86,871)
Fair value adjustment							(52)
Net finance expenses							(24,125)
Income tax expense							(586)
Profit for the period							(88,107)
Goodwill	200,261	247,375	137,870	49,950	–	–	635,456
Other intangibles	5,550	9,466	3,945	8,134	–	–	27,095
Assets excluding intangibles	59,136	64,383	37,751	1,679	137,236	(129,368)	170,817
Total assets	264,947	321,224	179,566	59,763	137,236	(129,368)	833,368
Liabilities	27,607	39,246	16,406	8,703	604,581	(129,368)	567,175
Total liabilities	27,607	39,246	16,406	8,703	604,581	(129,368)	567,175
Amortisation of Intangibles	2,513	4,804	1,833	4,004	–	–	13,154
Depreciation	1,845	3,616	1,077	600	804	–	7,942
Capital expenditure	979	1,757	928	402	218	–	4,284
Development expenditure	1,091	1,115	151	2,519	–	–	4,876
Acquisition of intangibles	–	–	–	5,747	–	–	5,747

*All segments are continuing operations.

Notes to the consolidated financial statements for the year ended 30 June 2010

2. Operating segments (continued)

2009 In thousands of AUD	International Agencies	Australian Agencies	Field Marketing	International Internet	Unallocated	Eliminations	Consolidated
Gross revenue	162,006	294,875	137,951	67,373	–	(8,750)	653,455
Directly attributable cost of sales	(47,472)	(132,974)	(4,494)	(36,626)	–	8,750	(212,816)
Net revenue	114,534	161,901	133,457	30,747	–	–	440,639
Other operating income	451	713	69	–	–	–	1,233
Total revenue	114,985	162,614	133,526	30,747	–	–	441,872
Operating expenses	(90,396)	(133,673)	(108,555)	(11,235)	(8,853)	–	(352,712)
One off costs	965	2,326	116	47	216	–	3,670
Normalised EBITDA	25,554	31,267	25,087	19,559	(8,637)	–	92,830
Reconciliation to EBITDA							
One off costs	(965)	(2,326)	(116)	(47)	(216)	–	(3,670)
EBITDA	24,589	28,941	24,971	19,512	(8,853)	–	89,160
Depreciation & amortisation expenses							(20,556)
EBIT							68,604
Share of profit of equity accounted investee				145			145
Impairment of investment in equity accounted investee				(4,215)			(4,215)
Net finance expenses							(26,551)
Income tax expense							(15,582)
Profit for the period							22,401
Goodwill	153,245	191,362	113,011	89,584	–	–	547,202
Other intangibles	8,590	13,250	5,808	5,931	–	–	33,579
Investment in equity accounted investee	–	–	–	10,132	–	–	10,132
Assets excluding intangibles	50,557	67,605	29,846	15,089	150,936	(128,383)	185,650
Total assets	212,392	272,217	148,665	120,736	150,936	(128,383)	776,563
Liabilities	24,900	43,243	17,328	11,627	543,143	(128,383)	511,858
Total liabilities	24,900	43,243	17,328	11,627	543,143	(128,383)	511,858
Amortisation of Intangibles	2,914	5,063	2,194	1,277	–	–	11,448
Depreciation	2,062	4,270	1,247	716	813	–	9,108
Capital expenditure	1,949	2,301	893	906	77	–	6,126
Development expenditure	1,339	1,701	306	2,809	–	–	6,155
Acquisition of intangibles	–	–	–	–	–	–	–

*All segments are continuing operations

Geographical segments

The operating segments are managed on a worldwide basis, however there are three geographic areas of operation.

Geographical information

In thousands of AUD	2010		2009	
	Net revenues	Non-current assets	Net revenues	Non-current assets
Australasia	265,429	466,677	290,632	425,134
UK & Europe	96,257	201,967	120,077	154,647
USA	16,921	27,659	29,930	44,491
Total	378,607	696,303	440,639	624,272

3. Revenue and other income

In thousands of AUD	2010	Consolidated 2009
Gross revenue from the rendering of services	586,509	642,098
Gross revenue from licences and other intangible rights	750	11,357
Gross revenue	587,259	653,455
Directly attributable cost of sales	(208,652)	(212,816)
Net revenue	378,607	440,639
Trade discounts	29	472
Other	763	761
Other income	792	1,233
Total revenue and other income	379,399	441,872

4. Finance income and expense

In thousands of AUD	2010	Consolidated 2009
Finance income		
Interest income	426	724
Total interest income	426	724
Finance expenses		
Present value interest charges on deferred consideration for business combinations	(5,480)	(5,588)
Interest on external loans	(18,616)	(21,217)
Finance lease interest	(455)	(470)
Total interest expense	(24,551)	(27,275)
Net finance expense	(24,125)	(26,551)

Foreign exchange losses of \$238,927 (2009: gains of \$1,943,649) have been recognised in the consolidated income statement and have been included in other operating expenses in the income statement.

5. Auditors' remuneration

In AUD	2010	Consolidated 2009
Audit services – auditors of the Company		
KPMG Australia	659,000	553,000
Overseas KPMG firm	253,296	330,443
	912,296	883,443
Other services – auditors of the Company		
Migration services work:		
KPMG Australia	10,100	17,150
Taxation compliance services:		
KPMG Australia	28,000	47,500
Overseas KPMG firm	249,494	265,662
Transaction and due diligence service:		
KPMG Australia	949,489	535,600
Overseas KPMG firm	2,684	179,281
	1,239,767	1,045,193

Notes to the consolidated financial statements for the year ended 30 June 2010

6. Income tax expense

Recognised in the income statement

In thousands of AUD	2010	Consolidated 2009
Current tax expense		
Current year	9,177	17,578
Adjustments for prior years	(1,820)	(801)
Adjustments for prior years due to tax legislation changes	(2,819)	—
	4,538	16,777
Deferred tax expense		
Origination and reversal of temporary differences	(3,917)	(947)
Benefit of tax losses recognised	(35)	(248)
	(3,952)	(1,195)
Total income tax expense in income statement	586	15,582
Numerical reconciliation between tax expense and pre-tax accounting profit/(loss)		
In thousands of AUD	2010	Consolidated 2009
Profit/(loss) before income tax	(87,521)	37,983
Income tax expense using the Company's domestic tax rate of 30% (2009: 30%)	(26,256)	11,395
Increase in income tax expense due to:		
Present value interest charges	1,597	1,659
Other non-deductible/(subtraction) terms	2,380	52
Effect of higher tax rate on overseas incomes	420	990
Accounting amortisation of identifiable intangible assets	2,581	2,766
Imputation gross up on dividends received	281	213
Share option expense	680	1,088
Impairment charge	25,719	1,264
Decrease in income tax expense due to:		
Tax amortisation of identifiable intangible assets	(387)	(346)
Share of associates net loss	35	44
Effect of losses previously not booked	(559)	—
Franking credits on dividends received	(937)	(709)
Under/(over) provision for tax in previous years	(1,820)	(801)
Under/(over) provision for tax in previous years due to tax legislation changes	(2,819)	—
Unwinding of deferred tax liability established in business combinations	(2,133)	(2,365)
Tax losses not brought to account	1,804	332
Income tax expense on pre-tax net profit	586	15,582
Deferred tax asset recognised directly in equity		
Share issue costs	1,015	862
	1,015	862
Income tax recognised in other comprehensive income		
Cash flow hedges	885	—
	885	—

7. Earnings per share

In thousands of AUD	2010	Consolidated 2009
Net (loss)/profit for the year	(88,107)	22,401
Non controlling interest	541	(993)
Net (loss)/profit for the year attributable to shareholders	(87,566)	21,408
In thousands of shares		
Weighted average number of ordinary shares – basic ⁽ⁱ⁾	326,353	214,178
Shares issuable under equity-based compensation plans ⁽ⁱⁱ⁾	-	35
Weighted average number of ordinary shares – diluted	326,353	214,213
Earnings per share – basic (AUD cents)	(26.83)	10.00
Earnings per share – diluted (AUD cents)	(26.83)	10.00

- (i) The weighted average number of shares outstanding includes an adjustment for the equity raising announced after year end reporting date which was completed on 29 September 2010 after receiving shareholder approval at a general meeting on 17 September 2010. Also earnings per share for the year ended 30 June 2009 has been restated to take into effect the equity raising on 29 September 2010 as well as actual equity raisings in the form of a placement which was completed in August 2009 and a rights issue which was completed in September 2009.
- (ii) The weighted average shares outstanding includes the incremental shares that would be issued upon the assumed exercise of stock options if the effect is dilutive. Because the Company has a loss from continuing operations in 2010, no potentially dilutive shares were included in the denominator computing diluted earnings per shares since the impact on earnings per share would be anti-dilutive. For fiscal year ended 30 June 2010, 42,090 shares were excluded from the calculation of diluted earnings per share because their inclusion would be anti-dilutive.

8. Cash and cash equivalents

In thousands of AUD	Note	2010	Consolidated 2009
Cash at bank and on hand		22,607	23,531
Bank short-term deposits		155	28
Cash and cash equivalents in statement of financial position and statement of cash flows	28	22,762	23,559

The Consolidated Entity's exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities are disclosed in Note 24 Financial risk management/financial instruments.

9. Trade and other receivables

In thousands of AUD	Note	2010	Consolidated 2009
Current			
Trade receivables		92,615	107,057
Less: provision for impairment loss	24	(3,257)	(1,213)
		89,358	105,844
Other debtors		3,543	4,181
		92,901	110,025
Non-current			
Other non-current receivables		570	991
		570	991
Total trade and other receivables		93,471	111,016

No interest is charged on trade debtors. The consolidated entities exposure to credit and currency risk and impairment losses related to trade and other receivables are disclosed in note 24.

Notes to the consolidated financial statements for the year ended 30 June 2010

10. Other assets

In thousands of AUD	2010	Consolidated 2009
Current		
Work in progress	4,394	10,864
Prepayments	5,662	4,584
Other current assets	2,083	3,259
	12,139	18,707
Non-current		
Deposits	587	523
Other non-current assets	564	1,814
	1,151	2,337

11. Other financial assets

In thousands of AUD	Note	2010	Consolidated 2009
Non-current investments			
Deposits – interest bearing		565	223
		565	223
Investments in associated entities	13	–	10,132

Deposit – interest bearing

Interest bearing deposits are amounts paid to secure leasing facilities. These amounts are held in bank term deposit accounts and pay at an average weighted interest rate of 5.82% at 30 June 2010 (30 June 2009: 2.95%).

12. Current tax assets and liabilities

The Consolidated Entity has a net current tax receivable of \$6,311,398 (2009: current tax liability \$6,906,690). The net current receivable is comprised of current tax receivables of \$9,263,298 and current tax payables of \$2,951,900. As the balances relate to different tax jurisdictions and therefore no legal right of set off exists, the amounts have been disclosed separately.

13. Investments accounted for using the equity method

Investments in associates

The Consolidated Entity accounts for investments in Dark Blue Sea Limited using the equity method.

The Consolidated Entity had the following investments in associates during the period:

	Principal activities	Country	Reporting Date	Ownership 2010	2009
Dark Blue Sea Limited	Internet Property Development	Australia	30 June 2010	100%	28.25%

In thousands of AUD	Revenues (100%)	Profit/(loss) (100%)	Share of associates net profit/(loss) recognised	Total Assets (100%)	Total Liabilities (100%)	Net assets as reported by associates (100%)	Share of associate net assets equity accounted
2010							
Dark Blue Sea Limited	2,248	(393)	(117)	–	–	–	–
	2,248	(393)	(117)	–	–	–	–
2009							
Dark Blue Sea Limited	8,405	615	145	9,890	3,127	6,763	1,911
	8,405	615	145	9,890	3,127	6,763	1,911

	2010	Consolidated 2009
Movements in carrying amount of associated entities		
Carrying amount at the beginning of the year	10,132	13,904
Acquisition of interest in associated entity	423	399
Share of associate entity (loss)/profit	(117)	145
Dividends received from associates	–	(101)
Impairment loss	(2,059)	(4,215)
Reclassification to controlled entity	(8,379)	–
Carrying amount at the end of the year	–	10,132

On 7 December 2009, the Company acquired a controlling interest in Dark Blue Sea Limited, as a result of acceptances under the takeover offer which commenced on 1 October 2009. After gaining acceptances in excess of 90% of the share capital, the Company compulsorily acquired the remaining share capital in Dark Blue Sea Limited and therefore owns 100% of the share capital post the compulsory acquisition period. Prior to the takeover bid, the Company had a 29.79% interest in Dark Blue Sea Limited.

From 7 December 2009, as a result of acquiring a controlling interest, the equity accounting method no longer applies and Dark Blue Sea forms part of the consolidated financial statements of the Consolidated Entity.

In accordance with Australian Accounting Standard AASB 3 *Business Combinations* the Company has remeasured its previously held equity interest in Dark Blue Sea at fair value on 7 December 2009 and recognised the resulting impairment loss of \$2,058,698 in the income statement. The fair value of the equity interest has been deemed at 35 cents per share, being the final price under the takeover offer.

Notes to the consolidated financial statements for the year ended 30 June 2010

14. Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

In thousands of AUD	2010	Consolidated 2009
Deferred tax asset		
Tax losses carried forward	37	1,661
Employee benefits	3,002	3,142
Impairment of doubtful debts	970	293
Accruals and income in advance	3,776	1,055
Leased assets	159	193
Lease make good	486	419
Lease incentive	280	308
Deductible share issue costs	2,241	1,226
Fixed assets	633	555
Identifiable intangibles	528	—
Hedge reserve on interest rate swaps	885	—
Other	467	265
	13,464	9,117
Deferred tax liabilities		
Identifiable intangibles	7,397	7,062
Lease make good asset	106	143
Work in progress	2,876	3,771
Other	213	875
	10,592	11,851
Deferred tax assets/liabilities not taken into account		
Deferred tax assets have not been recognised in respect of the following items because it is not probable that future taxable profit will be available against which the Consolidated Entity can utilise the benefits from:		
Revenue losses	8,765	497
Capital losses	-	4,170
Gross tax losses carried forward	8,765	4,667

15. Plant and equipment

In thousands of AUD	2010	Consolidated 2009
Computer equipment		
At cost	21,355	21,795
Accumulated depreciation	(15,556)	(15,548)
	5,799	6,247
Office furniture & equipment		
At cost	12,259	14,093
Accumulated depreciation	(8,767)	(9,384)
	3,492	4,709
Plant and equipment		
At cost	7,255	7,088
Accumulated depreciation	(4,908)	(4,175)
	2,347	2,913
Leasehold Improvements		
At cost	9,443	11,409
Accumulated depreciation	(5,854)	(7,919)
	3,589	3,490

In thousands of AUD	2010	Consolidated 2009
Plant & equipment under finance lease		
At cost	7,481	7,147
Accumulated amortisation	(4,706)	(3,815)
	2,775	3,332
Total plant and equipment, net written-down value	18,002	20,691
Reconciliations		
<i>Reconciliations of the carrying amounts of each class of property, plant and equipment are set out below:</i>		
Computer equipment		
Carrying amount at the beginning of the year	6,247	6,413
Acquisitions through business combinations	188	47
Additions	3,079	3,683
Depreciation	(3,227)	(3,909)
Effect of movements in exchange rates	(266)	114
Disposals	(222)	(101)
Carrying amount at the end of the year	5,799	6,247
Office furniture & equipment		
Carrying amount at the beginning of the year	4,709	4,948
Acquisitions through business combinations	68	31
Additions	224	1,493
Depreciation	(1,278)	(1,675)
Effect of movements in exchange rates	(204)	(4)
Disposals	(27)	(84)
Carrying amount at the end of the year	3,492	4,709
Plant & equipment		
Carrying amount at the beginning of the year	2,913	3,366
Acquisitions through business combinations	—	1
Additions	648	800
Depreciation	(1,073)	(975)
Effect of movements in exchange rates	(25)	6
Disposals	(116)	(285)
Carrying amount at the end of the year	2,347	2,913
Leasehold improvements		
Carrying amount at the beginning of the year	3,490	3,942
Acquisitions through business combinations	—	59
Additions	1,455	849
Amortisation	(1,276)	(1,355)
Effect of movements in exchange rates	(78)	16
Disposals	(2)	(21)
Carrying amount at the end of the year	3,589	3,490
Leased plant and equipment		
Carrying amount at the beginning of the year	3,332	3,768
Additions	557	968
Amortisation	(1,088)	(1,293)
Effect of movements in exchange rates	(12)	2
Disposals	(14)	(113)
Carrying amount at the end of the year	2,775	3,332

Notes to the consolidated financial statements for the year ended 30 June 2010

16. Intangible assets		
In thousands of AUD	2010	Consolidated 2009
Goodwill		
At cost	710,750	547,202
Impairment	(75,294)	–
	635,456	547,202
IT related intellectual property		
At cost	18,611	7,378
Accumulated amortisation	(7,378)	(5,533)
Impairment	(5,836)	–
	5,397	1,845
Contracts and customer relationships		
At cost	40,160	40,434
Accumulated amortisation	(25,975)	(19,339)
Impairment	(46)	–
	14,139	21,095
Brand names		
At cost	751	751
Accumulated amortisation	(588)	(463)
	163	288
Internally generated intangible assets		
At cost	20,908	13,650
Accumulated amortisation	(7,817)	(3,299)
Impairment	(5,695)	–
	7,396	10,351
Total intangible assets, net carrying value	662,551	580,781
Reconciliations		
Reconciliations of the carrying amounts of intangibles are set out below:		
Goodwill		
Carrying amount at the beginning of the year	547,202	462,632
Acquisitions through business combinations	19,017	8,958
Adjustments through deferred consideration	169,302	67,963
Impairment	(75,294)	–
Effect of movement in exchange rate	(24,771)	7,649
Carrying amount at the end of the year	635,456	547,202
IT related intellectual property		
Carrying amount at the beginning of the year	1,845	3,137
Acquisitions through business combinations	5,561	224
Additions	5,747	–
Impairment	(5,836)	–
Amortisation	(1,844)	(1,564)
Effect of movement in exchange rate	(76)	48
Carrying amount at the end of the year	5,397	1,845
Contracts and customer relationships		
Carrying amount at the beginning of the year	21,095	30,066
Acquisitions through business combinations	1,502	170
Impairment	(46)	–
Amortisation	(6,672)	(7,662)
Effect of movement in exchange rate	(1,740)	(1,479)
Carrying amount at the end of the year	14,139	21,095

In thousands of AUD	2010	Consolidated 2009
Brand name		
Carrying amount at the beginning of the year	288	414
Amortisation	(125)	(126)
	163	288
Internally generated intangible assets		
Carrying amount at the beginning of the year	10,351	6,008
Acquisitions through business combinations	2,632	218
Additions	4,876	6,155
Impairment	(5,695)	—
Amortisation	(4,513)	(2,097)
Effect of movement in exchange rate	(255)	67
Carrying amount at the end of the year	7,396	10,351

Amortisation charge

The amortisation charge of \$13,154,000 (2009: \$11,449,000) is recognised in the depreciation and amortisation expense in the income statement.

Impairment charge

An impairment charge on intangible assets of \$86,871,000 (2009: Nil) was recognised in the income statement.

During the year ended 30 June 2010 the International Internet cash generating unit (CGU) group, which is a segment specialising in search marketing, experienced a significant decline in trading due to general weakness in the online global advertising spend market, a reliance on US online advertising spend, weakness in the domain name sales market and exposure to a weaker US dollar. During the year this CGU group also closed or divested the Geekversity, Future House, iMega and Crystal Storm businesses.

Specific assets impaired:

The Consolidated Entity closed various development projects within the International Internet CGU group including developed software and technology products and domain names which were assessed to have no individual recoverable amounts and therefore an impairment charge of \$11,531,000 was recognised. Customer relationships recognised for the closed businesses were also impaired in the amount of \$46,000.

Specific goodwill impaired:

The Consolidated Entity closed businesses identified above and therefore these businesses were excluded from the International Internet CGU group as they were no longer obtaining synergies from the CGU group. These businesses were assessed to have no recoverable amounts and therefore an impairment charge of \$41,264,000 was recognised.

International Internet CGU group impaired:

The recoverable amount of the CGU group was estimated based on its value in use excluding the closed or divested businesses and reflecting the best estimate of future cash flows for that CGU group. An impairment charge of \$34,030,000 was recognised relating to goodwill for the CGU group.

The estimate of the value in use for the International Internet CGU group impairment testing was determined using:

- A post tax discount rate of 12.78% (2009: 9.23%);
- Growth rate of 7.5% for 4 years from the best estimate of the CGU group future cash flows (2009: 7.5%); and
- Long-term growth rate of 3% into perpetuity (2009: 3%).

Impairment tests for cash generating unit groups containing goodwill

Goodwill is tested for impairment on a division or business unit basis, reflecting the synergies obtained by the division or business unit. During the year the Consolidated Entity announced an organisational restructure. In doing so, the aggregation of assets for identifying CGU groups was adjusted to reflect the lowest level of management of the groups of assets and the synergies of the business groupings. The aggregation of assets in CGU groups continues to be determined using both a service offering and geographical approach. The CGU groups are consistent with the new operating segments of the Consolidated Entity.

Notes to the consolidated financial statements for the year ended 30 June 2010

16. Intangible assets (continued)

Goodwill CGU group allocation

In thousands of AUD	2010	Consolidated 2009
<i>The Consolidated Entity's carrying amount of goodwill for each of the CGU groups identified:</i>		
International Agencies	200,261	153,245
Australian Agencies	221,246	164,556
Australian Communication	26,129	26,807
Field marketing	137,870	113,011
International Internet	49,950	89,583
	635,456	547,202

Impairment tests for cash generating units containing goodwill

The recoverable amount of a CGU group is assessed using calculation methodologies based on value-in-use calculation.

Key assumptions used in the approach to test for impairment relate to the discount rate and the medium-term and long-term growth rates applied to projected cash flows.

Projected cash flows:

The projected cash flows are derived from budgets to be approved by the Directors for the next financial year which reflect the best estimate of the CGU group's cash flows at the time. The budgets are derived from a combination of historical trading performance and expectations of the CGU group based on market and life cycle factors. Projected cash flows can differ from future actual results of operations and cash flows.

Discount rates:

The discount rate is based on the Consolidated Entity's pre-tax weighted average cost of capital (WACC) adjusted if necessary to reflect the specific characteristics of each CGU group and to obtain a post tax discount rate.

Growth rates:

A growth rate of 7.5% on the cash flows for next financial year is used to determine cash flows for the next four years. The five years of cash flows are discounted to present value. The growth rate is sourced from historical trading performance and organic growth expectations.

Long-term growth rate into perpetuity:

Long-term growth rates of 3% are used into perpetuity, based on expected long-range growth rates for the industry.

	2010 Inputs		2009 Inputs	
	Discount rate	Growth rate	Discount rate	Growth rate
Impairment testing assumptions for CGU groups				
<i>The following inputs are attributable to each CGU group for impairment testing:</i>				
International Agencies	9.83%	7.5%	9.23%	7.5%
Australian Agencies	9.83%	7.5%	9.23%	7.5%
Australian Communication	9.83%	7.5%	9.23%	7.5%
Field Marketing	9.83%	7.5%	9.23%	7.5%
International Internet	12.78%	7.5%	9.23%	7.5%

The higher discount rate applied to the cash flows of the International Internet CGU group reflects the risks and returns associated with that group of assets. If this discount rate above had been applied in the prior reporting period, it would not have resulted in any impairment charge.

Sensitivity range assumptions for impairment testing assumptions

The following sensitivity ranges are attributable to each CGU group for impairment testing excluding International Internet CGU group for which the impairment loss was calculated on the assumptions above:

	2010 Sensitivity range		2009 Sensitivity range	
	Discount rate	Growth rate	Discount rate	Growth rate
International Agencies	8.48% – 11.18%	5–10%	7.98% – 10.94%	5–10%
Australian Agencies	8.48% – 11.18%	5–10%	7.98% – 10.94%	5–10%
Australian Communication	8.48% – 11.18%	5–10%	7.98% – 10.94%	5–10%
Field Marketing	8.48% – 11.18%	5–10%	7.98% – 10.94%	5–10%

No CGU group, excluding the International Internet CGU group, would be impaired at any of the sensitivity ranges tested.

17. Trade and other payables

In thousands of AUD	2010	Consolidated 2009
Current liabilities		
Trade payables	27,094	29,735
Other trade payables and accrued expenses	32,580	38,038
Unearned income	16,424	14,128
	76,098	81,901
Non-current liabilities		
Other payables	26	23
	26	23

The Consolidated Entity's exposure to currency and liquidity risk related to trade and other payables is disclosed in Note 24 Financial risk management/Financial Instruments.

18. Deferred consideration payables

In thousands of AUD	2010	Consolidated 2009
Current liabilities		
Deferred consideration payable	78,848	66,708
	78,848	66,708
Non-current liabilities		
Deferred consideration payable	90,690	44,724
	90,690	44,724
Total deferred consideration payable current and non current	169,538	111,432

Deferred consideration liabilities at year end reporting date are the present value of expected future payments.

As disclosed in Note 32 Subsequent events, the Consolidated Entity has entered into agreements to restructure its deferred consideration liabilities after the reporting date such that substantially all of the deferred consideration liabilities have been capped. On the assumption that all other variables remain the same in relation to critical assumptions and judgements made at 30 June 2010, the Consolidated Entity expects the present value liability of the restructured deferred consideration liability to be approximately \$161,700,000 at the date the agreements are signed. The Consolidated Entity's exposure to currency and liquidity risk in relation to deferred consideration is described in Note 24 Financial risk management/financial instruments.

19. Loans and borrowings

This note provides information about the contractual terms of the Consolidated Entity's interest-bearing loans and borrowings. For more information about the Consolidated Entity's exposure to interest rate, liquidity risk and foreign currency risk, see Note 24 Financial risk management/Financial instruments.

In thousands of AUD	2010	Consolidated 2009
Current liabilities		
Secured bank loans	38,801	33,558
Finance lease liabilities	803	908
Hire purchase lease liabilities	1,560	1,280
Loan notes payable	3,892	-
Derivative financial liability	484	181
	45,540	35,927
Non-current liabilities		
Secured bank loans	235,065	239,548
Other non-current loans	703	516
Finance lease liabilities	1,413	1,928
Hire purchase lease liabilities	1,843	2,228
Derivative financial liability	2,466	4,172
	241,490	248,392

Notes to the consolidated financial statements for the year ended 30 June 2010

19. Loans and borrowings (continued)

Terms and debt repayment schedule

Terms and conditions of outstanding loans were as follows:

In thousands of AUD

Currency	Date of maturity	Face value	30 June 2010	Face value	Consolidated 30 June 2009
			Carrying amount		Carrying amount
AUD	30 Apr 2010	—	—	33,558	33,558
AUD	31 Oct 2010	—	—	59,805	59,805
GBP	31 Oct 2010	—	—	57,735	57,735
AUD	31 Mar 2011	22,973	22,973	46,000	46,000
GBP	31 Mar 2011	15,828	15,828	—	—
USD	31 Oct 2011	31,103	31,103	20,509	20,509
GBP	31 Oct 2011	17,604	17,604	20,552	20,552
AUD	31 Oct 2011	28,150	28,150	34,947	34,947
AUD	30 Apr 2012	38,000	38,000	—	—
AUD	31 Oct 2012	70,581	70,581	—	—
GBP	31 Oct 2012	49,627	49,627	—	—
Total secured bank loans		273,866	273,866	273,106	273,106

Financing facilities

In thousands of AUD	2010	Consolidated 2009
The Consolidated Entity has access to the following lines of credit:		
<i>Total facilities available:</i>		
Bank overdrafts	4,284	4,771
Cash advance facility	280,000	330,000
Interest rate swap facility	11,400	11,400
Lease finance facility	6,874	5,500
Indemnity guarantee facility	3,500	3,500
ANZ Online facility	7,000	7,000
Credit card facility	2,300	3,100
Invoice discounting facility	879	879
	316,237	366,150
<i>Facilities used at reporting date:</i>		
Bank overdrafts	—	—
Cash advance facility ⁽ⁱ⁾	274,284	273,106
Interest rate swap facility	—	—
Lease finance facility	5,071	4,990
Indemnity guarantee facility	3,460	3,473
ANZ Online facility	—	—
Credit card facility	386	659
Invoice discounting facility	—	—
	283,201	282,228
<i>Facilities not utilised at reporting date:</i>		
Bank overdrafts	4,284	4,771
Cash advance facility	5,716	56,894
Interest rate swap facility	11,400	11,400
Lease finance facility	1,802	510
Indemnity guarantee facility	40	27
ANZ Online facility	7,000	7,000
Credit card facility	1,914	2,441
Invoice discounting facility	879	879
	33,035	83,922

(i) As at 30 June 2010 the fixed/variable rate cash advance facility used at reporting date includes a financial guarantee drawn against the facility in the amount of \$417,622. No amount existed at 30 June 2009.

Financing arrangements

All finance facilities, with the exception of the bank overdraft, are negotiated by the Company on behalf of the Consolidated Entity. The carrying amount of amounts drawn down on facilities as at the reporting date equate to face value.

Bank overdrafts

The bank overdraft of Photon Group Limited is included in the security arrangements associated with the Fixed/Variable Rate Cash Advance Facility. The bank overdraft is payable on demand and subject to annual review. Interest on the bank overdraft is charged at prevailing market rates.

The bank overdraft of Belgiovane Williams Mackay Pty Limited is secured by a debenture over the assets and undertakings of Belgiovane Williams Mackay Pty Limited. The bank overdraft is payable on demand and subject to annual review. Interest on the bank overdraft is charged at prevailing market rates.

The bank overdraft of Corporate Edge Group Limited and Lorica Group Limited is secured by a debenture over the assets and undertakings of Corporate Edge Group Limited and Lorica Group Limited. The bank overdraft is payable on demand and subject to annual review. Interest on the bank overdraft is charged at prevailing market rates.

The bank overdraft of Naked Communications BV is secured by a debenture over the assets and undertakings of Naked Communications BV. The bank overdraft is payable on demand and subject to annual review. Interest on the bank overdraft is charged at prevailing market rates.

The bank overdraft of Naked Communications Limited, Hyper Happen Limited and Lunch Communications Limited is secured by a debenture over the assets and undertakings of Naked Communications Limited, Hyper Happen Limited and Lunch Communications Limited. The bank overdraft is payable on demand and subject to annual review. Interest on the bank overdraft is charged at prevailing market rates.

Cash Advance Facility

Amounts drawn on the Cash Advance Facility are denominated in AUD, GBP and USD and bear interest, based on the following:

- \$280,000,000 (2009: \$330,000,000) general corporate finance facility: the bank bill swap reference rate – average bid for 30 days plus a fixed margin.

Some exposure to the bank bill swap rate is fixed through the use of interest rate swap arrangements (as detailed below).

The Cash Advance Facility is secured by:

- A First Registered Company Charge (Mortgage Debenture) over all the assets and undertakings of Photon Group Limited and certain of its wholly owned subsidiaries.
- Cross Guarantee and Indemnity between Photon Group Limited and certain of its wholly owned subsidiaries, and

- Standard Shares and Securities Mortgage over all shares held by Photon Group Limited and certain of its wholly owned subsidiaries in their controlled and associated entities.

Interest rate swap facility

The interest rate swap facility is in place to assist with hedging in interest rate exposures.

As at 30 June 2010 interest rate swap transactions swapping floating for fixed interest rates were in place under the following arrangements:

- Fixed rate of 5.93% for a notional amount of GBP 15,000,000 for the period 25 July 2008 to 31 October 2010.
- Fixed rate of 5.92% for a notional amount of GBP 10,000,000 for the period 25 July 2008 to 31 October 2011.
- Fixed rate of 3.98% for a notional amount of USD 10,000,000 for the period 25 July 2008 to 31 October 2011.
- Fixed rate of 2.72% for a notional amount of GBP 10,000,000 for the period 24 December 2009 to 31 October 2012.
- Fixed rate of 1.40% for a notional amount of USD 10,000,000 for the period 24 December 2009 to 31 October 2012.

As at 30 June 2009 interest rate swap transactions, swapping floating for fixed interest rates, were in place under the following arrangements:

- Fixed rate of 5.93% for a notional amount of GBP 15,000,000 for the period 25 July 2008 to 31 October 2010.
- Fixed rate of 5.92% for a notional amount of GBP 10,000,000 for the period 25 July 2008 to 31 October 2011.
- Fixed rate of 3.98% for a notional amount of USD 10,000,000 for the period 25 July 2008 to 31 October 2011.

Lease finance facility

The lease finance facility is subject to annual review and is in place to assist with capital expenditure requirements.

Indemnity guarantee facility

The indemnity guarantee facility is in place to support financial guarantees outstanding at any one time. Specific guarantee amounts are \$3,459,765 (2009: \$3,472,599) supporting property rental and other obligations.

ANZ Online facility

The ANZ Online facility of \$7,000,000 (2009: \$7,000,000) is subject to annual review and is in place to assist with distribution of payroll and payments to creditors.

Credit card facility

The credit card facility is subject to annual review and is subject to application approval and the Bank's standard terms and conditions.

Notes to the consolidated financial statements for the year ended 30 June 2010

19. Loans and borrowings (continued)

In thousands of AUD	2010	Consolidated 2009
Finance lease and hire purchase payable commitments		
<i>Finance lease commitments are payable:</i>		
Within one year	2,550	2,517
One year or later and no later than five years	3,600	4,661
	6,150	7,178
Less: Future lease finance charges	(531)	(834)
	5,619	6,344
Finance lease and hire purchase liabilities provided for in the financial statements		
Current	2,363	2,188
Non-current	3,256	4,156
<i>Finance lease commitments are payable</i>	5,619	6,344

The Consolidated Entity leases plant and equipment under finance leases expiring from 1 to 5 years (2009: 1 to 5 years). At the end of the lease term, the Consolidated Entity has the option to purchase the equipment at a substantial discount to market value. The terms of the leases require that additional debt and further leases are not undertaken without prior approval of the lessor.

20. Employee benefits

In thousands of AUD	2010	Consolidated 2009
Aggregate liability for employee benefits, including on-costs		
Current		
Employee benefits provision	8,681	8,286
Non-current		
Employee benefits provision	1,666	1,710

	2010	Consolidated 2009
<i>The present values of employee entitlements not expected to be settled within twelve months of reporting date have been calculated using the following weighted averages:</i>		
Assumed rate increase in salary and wage rates	0–5%	0–5%
Discount rate	5.42%	5.55%
Settlement term (years)	7–10	7–10

Equity-based plans

Executive share option scheme (ESOS)

The Company has an ESOS which was approved by shareholders at the Company's Annual General Meeting in 2004.

The plan allows for the Board to determine who is entitled to participate in the ESOS and may grant options accordingly. Photon's remuneration committee may determine whether or not the grant or exercise of options is conditional on the achievement of performance hurdles, and if so, the nature of such performance hurdles.

The exercise of an option will entitle the option holder to subscribe for one share.

The fair value options issued under the ESOS is measured using the Black Scholes formula or the Binomial model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historical volatility), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

On 27 October 2009, the Company issued 940,000 options to employees under the Company's ESOS. The exercise price of these options is \$1.85, being the VWAP for the 30 days prior to 27 October 2009.

On 8 December 2009, the Company issued 400,000 options to senior Executives under the Company's ESOS. These options vest immediately and have an exercise price of \$1.80.

On 12 February 2010, the Company issued 200,000 options to senior Executives under the Company's ESOS. The exercise price of these options is \$1.80.

On 5 March 2010, the Company issued 100,000 options to senior Executives under the Company's ESOS. The exercise price of these options is \$1.80.

Senior Executive Option Plan (SEOP)

In July 2007, the Company introduced the SEOP, designed to incentivise the Company's Executive Directors, Division Managing Directors and other senior management. The plan allows for the Board to determine who is entitled to participate in the SEOP and may grant options accordingly. The exercise of the options will entitle the option holder to subscribe for one share. The options are granted at the date of the agreement between the Company and the employee, or for Directors, the date of shareholder approval, being the Company's 2007 AGM on 20 November 2007 at an exercise price of \$6.00. The granted options have both a service condition, being continued employment, and a performance hurdle requiring an 18% year-on-year increase in the Photon share price to fully vest. As at 30 June 2010, no SEOP options had been issued.

The fair value of options issued under SEOP is measured using the Monte Carlo simulation method. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historical volatility), weighted average

expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

The Monte Carlo Simulation Method requires the use of many individual simulations, each simulation entails the following steps:

- Simulate the share price of the Company, and the companies in the peer group, as at a performance test date. The share prices are simulated such that they are consistent with the assumed distribution of, and correlation between, share price outcomes.
- Determine whether any awards vest at the current test date, based on simulated share prices.
- For any vesting awards, calculate the value using the simulated share price. This valuation uses either an analytic or Binomial tree methodology.
- Calculate the present value of the award as at the valuation date.

The results of many simulations are aggregated to determine the total fair value of the award.

Executive Committee Option Scheme (ECOS)

In October 2008, the Company introduced the ECOS, designed to incentivise the Company's Executive Directors, division Managing Directors and other senior Executives. The plan allows for the Board to determine who is entitled to participate in the ECOS and may grant options accordingly. The exercise of the options will entitle the option holder to subscribe for one share. This scheme was approved in Company's 2008 AGM on 28 October 2008.

The fair value of options issued under ECOS is measured using the Black Scholes formula of the Binomial model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historical volatility), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

On 22 October 2009, the Company granted Tim Hughes 400,000 options and Matthew Bailey 400,000 options under ECOS with an exercise price of \$1.51 per option. The options granted have both a service condition being continued employment and a performance hurdle requiring greater than 10% growth in Photon's Earning Per Share (EPS) for the year ending 30 June 2010 compared to Photon's EPS for the year ending 30 June 2009.

As at 30 June 2010, no ECOS options have been issued.

Notes to the consolidated financial statements for the year ended 30 June 2010

20. Employee benefits (continued)

Matthew Bailey options

On 17 October 2006, one million options were approved to be issued to Matthew Bailey in four tranches of 250,000 options. The fair value of Tranche 1 was measured using the Binomial Tree method and Tranches 2 to 4 were measured using the Monte Carlo simulation method (refer above). Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historical volatility), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

The following tranches have been issued and vested at 30 June 2010:

- Tranche 1: 250,000 options on 17 October 2006. The exercise price of the options was \$4.56, being the Volume Weighted Average Share Price (VWAP) for the 30 days prior to 30 June 2006, the date on which the Company's Remuneration Committee approved the issue of options (subject to shareholder approval).
- Tranche 2: 250,000 options on 28 November 2007. The exercise price of the options was \$5.59, being the Volume Weighted Average Share Price (VWAP) for the 30 days prior to 30 June 2007, the date on which the Company's Remuneration Committee approved the issue of options (subject to shareholder approval). This issue was subject to EPS hurdles.
- Tranche 3: 250,000 options on 1 October 2008. The exercise price of the options was \$3.01, being the Volume Weighted Average Share Price (VWAP) for the 30 days prior to 30 June 2008, the date on which the Company's Remuneration Committee approved the issue of options (subject to shareholder approval). This issue was subject to EPS hurdles.

As the EPS vesting condition attached to the grant of 250,000 Tranche 4 options has not been satisfied, these options will not vest.

Tim Hughes options

On 20 December 2007, one million options were issued to Tim Hughes. The fair value of options was measured using the Binomial Tree method. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historical volatility), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value. The exercise price of the options was \$6.00.

CEO Long-term Incentive Plan (CEO LTIP)

In April 2010, the Company granted Jeremy Philips a limited recourse loan to subscribe for 9,000,000 ordinary shares in the Company. The ordinary shares were issued at \$1.13, with the limited recourse loan being provided for the issue price. The ordinary shares issued under the CEO LTIP are subject to vesting and escrow conditions.

In accordance with the terms of the CEO's service agreement, in circumstances where the Company issues shares within twelve months of the grant date, the Company must offer the CEO the right to acquire additional shares as will, following the issue of shares, maintain his proportionate holding relative to the total number of shares on issue and to provide an additional limited recourse loan to fund the additional shares subscribed for (on the same terms as the original limited recourse loan). In connection with the equity raising announced on 17 August 2010 (see Note 32 Subsequent events for further details), Jeremy Philips subscribed for a further 64,946,415 shares funded by limited recourse loan provided by the Company. The additional ordinary shares under the CEO LTIP were issued at 10 cents, with the further limited recourse loan being provided for the issue price.

The CEO is not able to deal with any ordinary shares issued under the CEO LTIP until they vest as follows:

- 16,432,537 at 30 June 2012
- 24,648,805 at 30 June 2013
- 32,865,073 at 30 June 2014

Any dividends received from the ordinary shares will be offset against interest payable on the limited recourse loan. Repayment of the loan will be made on the earlier of the sale of the relevant shares or 12 months after vesting. The CEO may elect to forfeit the shares to which any loan repayment relates in lieu of making a repayment which is due.

If the CEO resigns the CEO LTIP continues to vest (subject to compliance with post employment restrictions) during the contractual notice period and the period of the post employment restrictions. If the CEO is terminated without cause the CEO LTIP vests in accordance with the above vesting profile. The CEO forfeits the CEO LTIP if terminated for serious misconduct.

Share options granted prior to November 2002 are not required to be recognised and measured in accordance with AASB 2 *Share-Based Payments*. Details of options over unissued ordinary shares held by Executives of the Consolidated Entity are set out in the Remuneration Report.

Employee Share Option Scheme (ESOS), Executive Committee Option Scheme (ECOS), Senior Executive Option Plan (SEOP) and CEO Long-Term Incentive Plan (CEO LTIP)

Summary of options over unissued ordinary shares

Grant date	Expiry date	Weighted average Exercise Price	Numbers of options outstanding at beginning of year	Options granted during year	Options exercised during year	Options expired during year	Options forfeited during year	Number of options at year end		Proceeds received	Date issued	No. of shares issued	Expected life (years)
								Outstanding	Vested				
2010													
31 May 2005	31 May 2010	\$2.52	666,667	—	—	666,667	—	—	—	—	—	—	5
29 Jul 2005	29 Jul 2010	\$2.64	1,380,868	—	—	—	—	1,380,868	1,380,868	—	—	—	2–5
30 Aug 2006	30 Aug 2010	\$4.56	997,000	—	—	—	105,000	892,000	594,667	—	—	—	2–5
17 Oct 2006	30 Sep 2011– 30 Sep 2012	\$4.39	1,000,000	—	—	—	250,000	750,000	500,000	—	—	—	3.5–6.5
1 Jul 2007	1 Jul 2012	\$5.59	1,141,500	—	—	—	17,000	1,124,500	374,833	—	—	—	3.5–4.5
27 Aug 2007	26 Aug 2012	\$5.90	100,000	—	—	—	—	100,000	33,333	—	—	—	3.5–4.5
20 Nov 2007	20 Dec 2012	\$5.65	1,000,000	—	—	—	—	1,000,000	—	—	—	—	3–4
20 Nov 2007 ^(iv)	31 Mar 2011– 31 Mar 2012	\$6.00	6,522,950	—	—	—	1,422,950	5,100,000	—	—	—	—	2.8–3.8
5 Feb 2008	28 Feb 2013	\$5.23	250,000	—	—	—	—	250,000	83,333	—	—	—	2–5
1 Apr 2008	31 Mar 2013	\$3.86	55,000	—	—	—	—	55,000	18,333	—	—	—	2.4–3.4
1 Apr 2008 ^(iv)	31 Mar 2011– 31 Mar 2012	\$6.00	450,000	—	—	—	—	450,000	—	—	—	—	2.4–3.4
2 Jun 2008	31 May 2013	\$3.13	100,000	—	—	—	100,000	—	—	—	—	—	4–5
2 Jun 2008 ^(iv)	31 Mar 2011– 31 Mar 2012	\$6.00	400,000	—	—	—	400,000	—	—	—	—	—	2.2–3.2
1 Oct 2008	30 Sep 2013	\$2.58	1,650,000	—	—	—	255,000	1,395,000	—	—	—	—	2–5
28 Oct 2008	31 Aug 2012	\$2.24	800,000	—	—	—	800,000	—	—	—	—	—	1–4
17 Nov 2008	16 Nov 2013	\$1.65	50,000	—	—	—	—	50,000	—	—	—	—	2–5
11 Feb 2009	31 Jan 2014	\$1.65	255,000	—	—	—	—	255,000	—	—	—	—	2–5
30 Jun 2009	30 Jun 2014	\$1.36	400,000	—	—	—	—	400,000	—	—	—	—	2–5
30 Jun 2009	31 Aug 2013	\$1.36	1,180,000	—	—	—	1,180,000	—	—	—	—	—	1–4
22 Oct 2009 ⁽ⁱ⁾	31 Aug 2013	\$1.51	—	800,000	—	—	800,000	—	—	—	—	—	1–4
26 Oct 2009	26 Oct 2014	\$1.85	—	940,000	—	—	20,000	920,000	—	—	—	—	2–5
8 Dec 2009	8 Dec 2014	\$1.80	—	400,000	—	—	—	400,000	400,000	—	—	—	1–5
12 Feb 2010	12 Feb 2015	\$1.80	—	200,000	—	—	—	200,000	—	—	—	—	2–5
5 Mar 2010	5 Mar 2015	\$1.80	—	100,000	—	—	—	100,000	—	—	—	—	2–5
20 Apr 2010 ⁽ⁱⁱ⁾	30 Jun 2015	\$1.13	—	9,000,000	—	—	—	9,000,000	—	—	—	—	2–5
17 Sep 2010 ⁽ⁱⁱⁱ⁾	30 Jun 2015	\$0.10	—	64,946,415	—	—	—	64,946,415	—	—	—	—	2–5
			18,398,985	76,386,415	—	666,667	5,349,950	88,768,783	3,385,367	—		—	

(i) ECOS options were granted during the year ended 30 June 2010 however were cancelled as vesting conditions were not met.

(ii) Relates to subscription to ordinary shares through a CEO LTIP which are accounted for as in-substance options.

(iii) Relates to subscription to ordinary shares through a CEO LTIP which are accounted for as in-substance options. The grant date is 17 September 2010, being the date of shareholder approval at a general meeting.

(iv) SEOP options were granted but are not issued until vesting conditions are met.

Notes to the consolidated financial statements for the year ended 30 June 2010

20. Employee benefits (continued)

Employee Share Option Scheme (ESOS), Executive Committee Option Scheme (ECOS) and Senior Executive Option Plan (SEOP)

Summary of options over unissued ordinary shares

Grant date	Expiry date	Weighted average Exercise Price	Numbers of options outstanding at beginning of year	Options granted during year	Options exercised during year	Options expired during the year	Options forfeited during year	Number of options at year end		Proceeds received	Date issued	No. of shares issued	Expected life (years)
								Outstanding	Vested				
2009													
1 Apr 2004	1 Apr 2009	\$1.60	346,667	—	211,000	135,667	—	—	—	337,600	29 Sep 2008	211,000	5
31 May 2005	31 May 2010	\$2.52	666,667	—	—	—	—	666,667	666,667	—		—	—
29 Jul 2005	29 Jul 2010	\$2.79	1,437,288	—	—	—	56,420	1,380,868	1,221,175	—	—	—	2–5
30 Aug 2006	30 Aug 2010	\$4.71	1,213,000	—	—	—	216,000	997,000	332,333	—	—	—	2–5
17 Oct 2006	30 Sep 2011– 30 Sep 2012	\$5.74	1,000,000	—	—	—	—	1,000,000	250,000	—	—	—	3.5–6.5
1 Jul 2007	1 Jul 2012	\$5.74	1,365,500	—	—	—	224,000	1,141,500	—	—	—	—	3.5–4.5
27 Aug 2007	26 Aug 2012	\$6.05	100,000	—	—	—	—	100,000	—	—	—	—	3.5–4.5
20 Nov 2007 ⁽ⁱⁱ⁾	30 Mar 2011– 30 Mar 2012	\$6.00	6,522,950	—	—	—	—	6,522,950	—	—	—	—	2.8–3.8
20 Nov 2007	20 Dec 2012	\$5.80	1,000,000	—	—	—	—	1,000,000	—	—	—	—	3–4
5 Feb 2008	28 Feb 2013	\$5.38	300,000	—	—	—	50,000	250,000	—	—	—	—	2–5
1 Apr 2008	31 Mar 2013	\$4.01	55,000	—	—	—	—	55,000	—	—	—	—	2.4–3.4
1 Apr 2008 ⁽ⁱⁱⁱ⁾	30 Mar 2011– 30 Mar 2012	\$6.00	450,000	—	—	—	—	450,000	—	—	—	—	2.4–3.4
2 Jun 2008	31 May 2013	\$3.28	100,000	—	—	—	—	100,000	—	—	—	—	4–5
2 Jun 2008 ⁽ⁱⁱⁱ⁾	30 Mar 2011– 30 Mar 2012	\$6.00	400,000	—	—	—	—	400,000	—	—	—	—	2.2–3.2
1 Oct 2008	30 Sep 2013	\$2.73	—	1,730,000	—	—	80,000	1,650,000	—	—	—	—	2–5
28 Oct 2008 ⁽ⁱ⁾	31 Aug 2012	\$2.24	—	800,000	—	—	—	800,000	—	—	—	—	1–4
17 Nov 2008	16 Nov 2013	\$1.80	—	50,000	—	—	—	50,000	—	—	—	—	2–5
11 Feb 2009	31 Jan 2014	\$1.80	—	255,000	—	—	—	255,000	—	—	—	—	2–5
30 Jun 2009 ⁽ⁱ⁾	30 Jun 2014	\$1.51	—	400,000	—	—	—	400,000	—	—	—	—	2–5
30 Jun 2009 ⁽ⁱ⁾	31 Aug 2013	\$1.51	—	1,180,000	—	—	—	1,180,000	—	—	—	—	1–4
			14,957,072	4,415,000	211,000	135,667	626,420	18,398,985	2,470,175	337,600	211,000		

(i) ECOS options were granted during the year ended 30 June 2009 but were not issued.

(ii) SEOP options were granted but are not issued until vesting conditions are met.

The number and weighted average exercise price of share options is as follows:

	Weighted average exercise price 2010	Number of options 2010	Weighted average exercise price 2009	Number of options 2009
Outstanding at 1 July (excludes former employees)	\$4.50	18,398,985	\$5.14	14,957,072
Forfeited during the period	\$3.37	(5,349,950)	\$3.15	(626,420)
Expired during the period	\$2.52	(666,667)	\$1.60	(135,667)
Exercised during the period	—	—	\$1.60	(211,000)
Granted during the period	\$0.27	76,386,415	\$2.14	4,415,000
Outstanding at 30 June (excludes former employees)	\$0.93	88,768,783	\$4.50	18,398,985
Exercisable at 30 June	\$3.67	3,385,367	\$3.21	2,470,175

- The options outstanding at 30 June 2010 have an exercise price in the range of \$0.10 to \$6.00 and a weighted average contractual life of 4.54 years.
- There were no options exercised during the year (2009: the weighted average share price at the date of exercise for share options exercised during the year ended 30 June 2009 was \$2.68).
- The fair value of services received in return from share options granted is based on the fair value of share options granted, measured using:
 - The Black Scholes model: options under ESOS and ECOS;
 - The Binomial model: options under ESOS and ECOS, options issued to Tim Hughes, Tranche 1 options issued to Matthew Bailey and CEO LTIP; and
 - Monte Carlo Simulation Method: Tranches 2–4 of options issued to Matthew Bailey.

The fair value of share options and associated assumptions are disclosed in the Remuneration Report within the Directors' Report. The total expense recognised in the Consolidated Entity for the financial year 30 June 2010 for share-based payment transactions was \$2,267,090 (2009: \$3,591,671).

2010 – Inputs for measurement of grant date fair value

The following factors and assumptions were used in determining the fair value of the options on the grant date:

Grant date	Expiry date	Value per option	Exercise price	Price of shares on grant date	Expected volatility	Risk free interest rate	Dividend yield	Expected life (years)
22 Oct 2009 ⁽ⁱ⁾⁽ⁱⁱⁱ⁾	31 Aug 2013	\$0.448	\$1.51	\$1.89	35%	5.53%	6.5%	1–4
27 Oct 2009 ⁽ⁱ⁾	27 Oct 2014	\$0.381– \$0.435	\$1.85	\$1.92	35%	5.54%	6.5%	2–5
8 Dec 2009 ⁽ⁱ⁾	8 Dec 2014	\$0.381	\$1.80	\$1.67	35%	5.54%	6.5%	1–5
12 Feb 2010 ⁽ⁱ⁾	12 Feb 2015	\$0.178– \$0.305	\$1.80	\$1.20	35%	6.00%	6.5%	2–5
5 Mar 2010 ⁽ⁱ⁾	5 Mar 2015	\$0.139– \$0.253	\$1.80	\$1.11	35%	6.00%	6.5%	2–5
20 Apr 2010 ^(iv)	30 Jun 2015	\$0.27–\$0.31	\$1.13	\$1.17	40%	5.42%	6.0%	2–5
17 Sep 2010 ^(v)	30 Jun 2015	\$0.03 – \$0.04	\$0.10	\$0.10	40%	4.72%	0.0%	2–5

(i) As set out in the Company's ESOS, the exercise price of options granted after 25 March 2004 is calculated with reference to the volume weighted average price (VWAP) of the Company's ordinary shares for 30 business days prior to the issue date.

(ii) As set out in the Company's ECOS, the exercise price of options is calculated with reference to either the volume weighted average price (VWAP) of the Company's ordinary shares for the previous financial year's AGM or the VWAP for 30 business days prior to the issue date.

(i) Options granted under ECOS have not been issued as at 30 June 2010, are not issued until certain performance hurdles are met.

(iv) Relates to subscription for ordinary shares through a limited recourse loan which are accounted for as in-substance options. The exercise price is calculated with reference to the 30 business day VWAP prior to the grant date.

(v) Relates to subscription to ordinary shares through a CEO LTIP which are accounted for as in-substance options. The grant date is 17 September 2010, being the date of shareholder approval at a general meeting. The valuation factors and assumptions are an estimate as the valuation has not been finalised as at the date of this report.

Notes to the consolidated financial statements for the year ended 30 June 2010

20. Employee benefits (continued)

2009 – Inputs for measurement of grant date fair value

The following factors and assumptions were used in determining the fair value of the options on the grant date:

Grant date	Expiry date	Value per option	Exercise price (i)	Price of shares on grant date	Expected volatility	Risk free interest rate	Dividend yield	Expected life (years)
1 Oct 2008 ⁽ⁱ⁾	30 Sep 2013	\$0.378– \$0.423	\$2.73	\$2.59	25%–30%	5.7%	7.2%	2–5
28 Oct 2008 ⁽ⁱⁱ⁾ (iii)	31 Aug 2012	\$0.0558	\$2.24	\$1.50	30%	4.76%	7.2%	1–4
17 Nov 2008 ⁽ⁱ⁾	16 Nov 2013	\$0.140– \$0.280	\$1.80	\$1.38	25%–30%	4.76%	7.2%	2–5
11 Feb 2009 ⁽ⁱ⁾	31 Jan 2014	\$0.100– \$0.220	\$1.80	\$1.28	25%–30%	4.76%	7.2%	2–5
30 Jun 2009 ⁽ⁱ⁾	30 Jun 2014	\$0.268– \$0.299	\$ 1.51	\$ 1.64	35%	5.23%	8%	2–5
30 Jun 2009 ⁽ⁱⁱ⁾ (iii)	31 Aug 2013	\$0.212	\$ 1.51	\$ 1.64	35%	5.23%	8%	1–4

(i) As set out in the Company's ESOS, the exercise price of options granted after 25 March 2004 is calculated with reference to the volume weighted average price (VWAP) of the Company's ordinary shares for 30 business days prior to the issue date.

(ii) As set out in the Company's ECOS, the exercise price of options is calculated with reference to either the volume weighted average price (VWAP) of the Company's ordinary shares for the previous financial year's AGM or the VWAP for 30 business days prior to the issue date.

(iii) Options granted under ECOS have not been issued as at 30 June 2009, are not issued until certain performance hurdles are met.

21. Key management personnel disclosures

In addition to Executive and Non-Executive Directors, the following were key management personnel of the Consolidated Entity at any time during the reporting period.

Name	Position
Jeremy Philips	Chief Executive Officer
Stewart Bailey	Managing Director Field Marketing Division
Nigel Long	Managing Director Strategic Intelligence Division
Jon Wilkins	Managing Director Integrated Communications & Digital Division
Mark Dalglish	Managing Director Internet & E-Commerce Division
Adam Kilgour	Managing Director Specialised Communications Division

Loans with key management personnel

No loans were outstanding at the reporting date to key management personnel and their related parties except for the limited recourse loan granted to Jeremy Philips as described in section 2(e) of the remuneration report.

Other transactions with the Company or its controlled entities

A number of the key management personnel, or their related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities.

A number of these entities transacted with the Company or its subsidiaries in the reporting period. The terms and conditions of those transactions were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to unrelated entities on an arm's length basis. The aggregate amounts recognised during the year relating to key management personnel, and their related entities, total revenues of \$179,232 and total expenses of \$237,710. Details of the transactions are as follows:

Key management personnel	Transaction	Note	Consolidated 2010 Revenue/(Expense) \$'000	Consolidated 2009 Revenue/(Expense) \$'000
S McIntosh	Project management and production	(i)	179	768
M Bailey	Rental of subsidiary premises	(ii)	(237)	(226)

(i) Project management, production services and public relations services provided to RG Capital Pty Ltd by Australian Business Theatre Pty Limited and Mark Communications Pty Limited. S McIntosh is Director of RG Capital Pty Ltd.

(ii) The Bailey Superannuation Fund provided rental property services to The Bailey Group Pty Limited.

The key management personnel compensation (including all Directors) is as follows:

In AUD	2010	Consolidated 2009
Short-term employee benefits	4,929,951	4,887,364
Other long-term benefits	227,435	24,535
Post-employee benefits	300,757	241,172
Termination benefits	2,015,000	—
Share-based payments – CEO LTIP	152,710	—
Share-based payments – Options granted under ESOS	1,056,444	1,108,860
Share-based payments – Options granted under ECOS	16,310	267
Share-based payments – Options granted under SEOP	1,400,867	1,933,286
Total	10,099,474	8,195,484

Stewart Bailey, Adam Kilgour, Mark Dalgleish, Jon Wilkins and Nigel Long receive no compensation in relation to the management of the Company. The compensation disclosed above represents an allocation of the key management personnel's estimated compensation from the Consolidated Entity in relation to their services rendered to the Company.

The prior year comparative totals include key management personnel in 2009 who were not key management personnel in 2010 and have therefore not been disclosed in the remuneration report while being included in the total above in accordance with AASB 124 *Related Party Disclosures*.

Options and rights over equity instruments granted as remuneration

The movement during the reporting period in the number of options over ordinary shares in Photon Group Limited held, directly, indirectly or beneficially, by each key management personnel, including their related entities is as follows:

	Granted held at 1 July 2009	Granted as remuneration in year	Cancelled	Exercised	Granted held at 30 June 2010	Vested during the year	Vested and exercisable at 30 June 2010
Directors							
Tim Hughes ^(v)	5,500,000	400,000	—	—	5,900,000	—	1,000,000
Matthew Bailey ^{(ii)(iv)}	2,200,000	400,000	(1,850,000)	—	750,000	250,000	500,000
Executives							
Jeremy Philips	—	9,000,000	—	—	9,000,000	—	—
Stewart Bailey ⁽ⁱⁱ⁾	1,180,000	200,000	—	—	1,380,000	266,667	306,667
Adam Kilgour	1,183,334	200,000	—	—	1,383,334	268,333	303,333
Nigel Long	880,000	—	—	—	880,000	—	—
Mark Dalgleish ⁽ⁱⁱⁱ⁾	330,000	—	—	—	330,000	—	—
Jon Wilkins ⁽ⁱⁱⁱ⁾	330,000	—	—	—	330,000	—	—

	Granted held at 1 July 2008	Granted as remuneration in year	Cancelled	Exercised	Granted held at 30 June 2009	Vested during the year	Vested and exercisable at 30 June 2009
Directors							
Tim Hughes	5,100,000	500,000	—	(100,000)	5,500,000	—	1,000,000
Matthew Bailey ⁽ⁱⁱ⁾	1,900,000	300,000	—	—	2,200,000	250,000	250,000
Executives							
Stewart Bailey ⁽ⁱⁱ⁾	800,000	380,000	—	—	1,180,000	33,334	40,000
Adam Kilgour	803,334	380,000	—	—	1,183,334	35,000	35,000
Nigel Long	600,000	280,000	—	—	880,000	—	—
Andrew Davie ⁽ⁱ⁾	500,000	—	—	—	500,000	—	—
Caitlin Millar – Jack ⁽ⁱ⁾	522,950	150,000	—	—	672,950	—	—

(i) Ceased to be key management personnel with effect from 1 July 2009.

(ii) Matthew Bailey and Stewart Bailey are related parties.

(iii) Opening balances represent options granted prior to becoming key management personnel.

(iv) Matthew Bailey resigned as a Director of the Company on 24 May 2010. The above balance represents the options granted and exercisable at time of resignation.

(v) Tim Hughes resigned as a Director after the year end reporting date on 11 August 2010.

No options held by key management personnel are vested but not exercisable at 30 June 2010.

Notes to the consolidated financial statements for the year ended 30 June 2010

21. Key management personnel disclosures (continued)

No options were held by key management personnel related parties.

Movements in shares

The movement during the reporting period in the number of ordinary shares in Photon Group Limited held directly, indirectly or beneficially, by each key management person, including their related parties, is as follows:

	Held at 1 July 2009	Purchases	Issued as remuneration	Received on exercise of option	Sales	Held at 30 June 2010
Directors						
Tim Hughes	4,565,216	2,440,139	—	—	—	7,005,355
Matthew Bailey ⁽ⁱ⁾⁽ⁱⁱ⁾	11,907,269	5,953,634	8,237	—	(10,037,009)	7,832,131
Susan McIntosh	325,926	162,964	—	—	—	488,890
Brian Bickmore	208,234	24,117	—	—	(89,333)	143,018
Paul Gregory	160,000	40,000	—	—	—	200,000
Executives						
Adam Kilgour	1,771,455	120,000	—	—	—	1,891,455
Stewart Bailey ⁽ⁱ⁾	11,907,269	5,953,634	8,237	—	(10,037,009)	7,832,131
Mark Dagleish	127,155	—	—	—	(127,155)	—

	Held at 1 July 2008	Purchases	Issued as remuneration	Received on exercise of option	Sales	Held at 30 June 2009
Directors						
Tim Hughes	3,130,505	1,334,711	—	100,000	—	4,565,216
Matthew Bailey ⁽ⁱ⁾	8,930,450	2,976,819	—	—	—	11,907,269
Susan McIntosh	244,444	81,482	—	—	—	325,926
Brian Bickmore	158,234	50,000	—	—	—	208,234
Paul Gregory	160,000	—	—	—	—	160,000
Executives						
Adam Kilgour	1,249,841	521,614	—	—	—	1,771,455
Stewart Bailey ⁽ⁱ⁾	8,930,450	2,976,819	—	—	—	11,907,269

(i) Matthew Bailey's and Stewart Bailey's shareholdings are inclusive of their related party shareholdings.

(ii) Matthew Bailey resigned as a Director on 24 May 2010. The above balance represents shares held at the time of resignation.

22. Provisions

In thousands of AUD	2010	Consolidated 2009
Current		
Lease make good	771	752
Lease incentive	756	832
Rent increase	122	681
Restructure provision	6,227	—
	7,876	2,265
Non-current		
Lease make good	1,471	1,559
Lease incentive	456	907
Rent increase	789	698
	2,716	3,164
Total provisions current and non-current	10,592	5,429
Reconciliations		
Reconciliations of the carrying amounts of each class of provision, except for employee benefits, are set out below:		
<i>Lease make good</i>		
Carrying amount at beginning of year	2,311	2,450
Increase due to new provision	189	74
Increase through business combination	60	39
Effect of movement in exchange rates	(113)	4
Provision used during the year	(205)	(256)
Carrying amount at end of year	2,242	2,311
<i>Lease incentive</i>		
Carrying amount at beginning of year	1,739	2,266
Increase due to new incentive	280	35
Effect of movement in exchange rates	(41)	3
Used during the year	(766)	(565)
Carrying amount at end of year	1,212	1,739
<i>Rent increase</i>		
Carrying amount at beginning of year	1,379	888
Net rental expense/(benefit) recognised in period	(471)	490
Increase due to new provision	3	—
Increase through business combination	—	1
Carrying amount at end of year	911	1,379
<i>Restructure provision</i>		
Carrying amount at beginning of year	—	—
Increase due to new provision	6,227	—
Carrying amount at end of year	6,227	—
Total provisions current and non-current	10,592	5,429

Notes to the consolidated financial statements for the year ended 30 June 2010

23. Capital and reserves

In thousands of AUD	2010	Consolidated 2009
Share capital		
187,440,645 (2009: 102,840,415) ordinary shares, fully paid	369,268	255,500

Ordinary shares

Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholder meetings.

Ordinary shares

Movements during the year

Balance at beginning of year 102,840,415 (2009: 76,589,369) shares	255,500	180,371
2010 shares issued:		
- 14,439,268 shares issued pursuant to placement for \$1.85 per share	26,713	—
- 58,639,842 shares issued pursuant to the rights issue for \$1.50 per share	87,960	—
- 2,471,608 shares issued pursuant to acquisition of Found for \$1.51 per share	3,732	—
- 49,512 shares issued pursuant to equity settled employee bonuses	76	—
- 9,000,000 ordinary shares issued in connection with CEO LTIP	—	—
2009 shares issued:		
- 434,650 shares issued pursuant to acquisition of Found for \$3.16 per share	—	1,371
- 211,000 shares issued pursuant to exercise of options under the terms of the ESOS	—	338
- 25,529,790 shares issued pursuant to the rights issue for \$3.00 per share	—	76,589
- 75,606 shares issued pursuant to equity settled employee bonuses	—	115
Share issue costs:		
Share issue costs	(5,728)	(4,146)
Tax effect of share issue costs	1,015	862
Balance at end of year	369,268	255,500

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations as well as from the translation of liabilities that hedge the Company's net investment in a foreign subsidiary.

Options reserve

The options reserve comprises the cumulative expense relating to the fair value of options on issue to key management personnel and employees.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

Dividends	Cents per share	Total amount \$'000	Date of payment	Franked/unfranked
2010				
Final 2009 – Ordinary shares	6.5c	7,622	11 September 2009	Franked
Interim 2010 – Ordinary shares	3.0c	5,354	30 March 2010	Franked
		12,976		
2009				
Final 2008 – Ordinary shares	17.0c	17,396	7 October 2008	Franked
Interim 2009 – Ordinary shares	6.0c	6,167	7 April 2009	Franked
		23,563		

Franked dividends declared or paid during the year were franked at the tax rate of 30%.

Dividend franking account	Company	
In thousands of AUD	2010	2009
30% franking credits available to shareholders of Photon Group Limited for subsequent financial years	27,644	24,811

The above amounts represent the balance of the franking account at year end adjusted for:

- franking credits that will arise from the payment of the current tax liability
- franking debits that will arise from the payment of dividends recognised as a liability at year end
- franking credits that will arise from the receipt of dividends recognised as receivables at year end
- franking credits that may be prevented from being distributed in subsequent years

The ability to utilise the franking credits is dependent upon there being sufficient available profits to declare dividends and any restrictions to paying dividends in connection with the recapitalisation proposal discussed in Note 32 Subsequent events.

There is no impact on the dividend franking account as no dividends have been proposed after the reporting date (2009: \$2,864,840).

24. Financial risk management/financial instruments

The Consolidated Entity has exposure to the followings risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

The Consolidated Entity's principal financial instruments comprise cash, receivables, payables, interest bearing liabilities, other financial liabilities and derivative financial instruments.

The Consolidated Entity manages its exposure to key financial risks in accordance with the Consolidated Entity's treasury risk management policy. The policy has been established to manage the key financial risks, such as interest rate, foreign exchange, counterparty credit and liquidity.

The Consolidated Entity's treasury risk management policies seek to identify and analyse the risks faced by the Consolidated Entity, to set appropriate risk limits and controls to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Consolidated Entity's activities.

The Consolidated Entity uses different methods to measure and manage different types of risks to which it is exposed. These include monitoring levels of exposure to interest rates, foreign exchange, liquidity and credit risk. The Consolidated Entity enters into derivative financial instruments, principally interest rate swaps and forward rate agreements to manage interest rate and foreign currency risks. The Consolidated Entity seeks to deal only with creditworthy counterparties and these assessments are regularly reviewed. Liquidity risk is monitored through the use of future rolling cash flow forecasts.

Credit risk

Exposure to credit risk

Credit risk is the risk of financial loss to the Consolidated Entity if a customer or counterparty to a financial instrument fails to meet its contractual obligation, and arises principally from a Consolidated Entity's receivables from customers. Each subsidiary is responsible for its analysis of the creditworthiness of new customers and for determining whether the subsidiary's standard payment terms and conditions are offered. The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date to recognised financial assets, is the carrying amount, net of any provisions for impairment of those assets, as disclosed in the Statement of financial position and Notes to the financial statements.

During the year ended 30 June 2010, the Consolidated Entity entered into transactions with more than 2,000 unique customers. The ten largest customers accounted for 25% of net revenue for the year ended 30 June 2010 with no one customer accounting for more than 7.6% of net revenue. There are no material credit exposures relating to single or groups of receivables.

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

In thousands of AUD	Note	Carrying amount	
		2010	2009
Trade and other receivables	9	93,471	111,016
Cash and cash equivalents	8	22,762	23,559
Deposits	10	587	523
Deposits – interest bearing	11	565	223
		117,385	135,321

The Consolidated Entity's maximum exposure to trade receivables credit risk at the reporting date was:

In thousands of AUD	Note	Carrying amount	
		2010	2009
Trade and other receivables	9	89,358	105,844

The Consolidated Entity's credit risk exposure is consistent across the geographic and business segments in which the Consolidated Entity operates.

Notes to the consolidated financial statements for the year ended 30 June 2010

24. Financial risk management/financial instruments (continued)

Impairment losses

The ageing of the Consolidated Entity's trade receivables at the reporting date was:

In thousands of AUD	Gross 2010	Impairment 2010	Gross 2009	Impairment 2009
Not past due	65,884	—	72,739	—
Past due and less than 90 days	19,237	—	23,810	—
Past due and more than 90 days	4,237	—	9,295	—
Past due, more than 90 days and impaired	3,257	3,257	1,213	1,213
	92,615	3,257	107,057	1,213

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

In thousands of AUD	2010	2009
Balance at 1 July	1,213	799
Impairment loss recognised in income statement	6,945	1,838
Provision used during year	(4,901)	(1,424)
Balance at 30 June	3,257	1,213

Based on historic trading terms, the Consolidated Entity believes that no impairment allowance is necessary in respect of trade receivables not past due or past due by up to 90 days; which represents 91.9% (2009: 90.2%) of the trade receivables balance. For trade receivables which are past due and over 90 days, the Consolidated Entity individually assesses each trade receivable and determines its recoverability. For those trade receivables which are assessed as non recoverable, an impairment allowance is made, which represents 3.5% (2009: 1.1%) of the total trade receivables balance.

The allowance accounts in respect of trade receivables are used to record impairment losses unless the Consolidated Entity is satisfied that no recovery of the amount owing is possible; at that point the amount is considered irrecoverable and is written off against the financial asset directly.

Market risk

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

The Consolidated Entity enters into derivatives in the ordinary course of business, and also incurs financial liabilities, in order to manage market risks. All such transactions are carried out within the guidelines set by the

Consolidated Entity's treasury risk management policy.

Liquidity risk

Liquidity risk is the risk that the Consolidated Entity will not be able to meet its financial obligations as they become due. The Consolidated Entity'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.

The Consolidated Entity manages liquidity risk by monitoring forecast operating cash flows, committed unutilised borrowing facilities, and re-estimating the value of deferred consideration liabilities semi-annually. At 30 June 2010 the Consolidated Entity had \$5,716,000 (2009: \$56,894,000) of committed unutilised borrowing capacity under its cash advance facilities. The Consolidated Entity also has \$4,284,000 (2009: \$4,771,000) of overdraft facilities available to it which was undrawn at 30 June 2010.

During the year the Consolidated Entity completed a capital raising of \$114,673,000 through a placement and rights issue. The raising was used to pay down debt and meet deferred consideration liabilities throughout the financial year ended 30 June 2010.

In order to meet its future contractual cash flow obligations the Consolidated Entity has announced, after the year end reporting date on 17 August 2010, a recapitalisation proposal including:

- a capital raising for a minimum of \$102,500,000 through an underwritten entitlement issue and placement;
- a restructure of its deferred consideration liabilities; and
- refinancing its existing debt facilities.

Please refer to Note 32 Subsequent events for further details on the recapitalisation proposal which was completed on 29 September 2010.

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

Consolidated 30 June 2010 In thousands of AUD	Carrying amount	Contractual cash flows	Less than 1 year	1–5 years	Over 5 years
Non-derivative financial liabilities					
Finance lease/hire purchase liabilities	5,619	6,150	2,550	3,600	–
Secured bank loans	273,866	303,624	54,619	249,005	–
Trade and other payables (excluding unearned revenue)	59,700	59,700	59,674	26	–
Deferred consideration	169,538	183,769	81,156	102,613	–
Loan notes payable	3,892	3,892	3,892	–	–
Other loans payable	703	703	–	703	–
Derivative financial instruments					
Interest rate swaps used for hedging	2,950	2,950	484	2,466	–
	516,268	560,788	202,375	358,413	–

Consolidated 30 June 2009 In thousands of AUD	Carrying amount	Contractual cash flows	Less than 1 year	1–5 years	Over 5 years
Non-derivative financial liabilities					
Finance lease/hire purchase liabilities	6,344	7,178	2,517	4,661	–
Secured bank loans	273,106	293,965	46,155	247,810	–
Trade and other payables (excluding unearned revenue)	67,796	67,796	67,773	23	–
Deferred consideration	111,432	119,279	69,300	49,979	–
Other loans payable	516	516	–	516	–
Derivative financial instruments					
Interest rate swaps used for hedging	4,353	4,353	181	4,172	–
	463,547	493,087	185,926	307,161	–

The periods in which the cash flows associated with derivatives that are cash flow hedges are expected to occur and expected to impact the profit or loss are consistent with the contractual maturities disclosed in the above table.

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier; or at significantly different amounts, except for deferred consideration and secured bank loans which have been restructured and refinanced after the year end reporting date.

Liquidity risk in relation to deferred consideration liabilities: There are critical accounting estimates and judgements in relation to deferred consideration liabilities as noted in significant accounting policies Note 1(y)(iii). The estimates and judgements impact the amount of deferred consideration payable such that the final amount payable under acquisition agreements can be different to the estimated contractual cash flow amounts payable at the year end reporting date. In connection with the recapitalisation proposal announced and completed after the year end reporting date, the Consolidated Entity has restructured its future deferred consideration liabilities. Please refer to Note 32 Subsequent events for further details.

The significance of the restructure of deferred consideration to liquidity risk of the Consolidated Entity is that:

- the total amount payable for substantially all deferred consideration liabilities has been capped at a comparable amount to the estimated liability at 30 June 2010;

- the payments of deferred consideration can not be made earlier than the contractual payment dates in the original acquisition agreements as set out in the contractual maturities disclosed in the tables above;
- a reduction in the total cash element of deferred consideration payables through satisfying elements of deferred consideration through the issue of Photon Group Limited shares; and
- approximately 50% of the aggregate estimated payments are now subject to the Consolidated Entity meeting certain hurdles in relation to financial performance and leverage ratio levels ensuring sufficient liquidity before deferred consideration payments are made.

Liquidity risk in relation to secured bank loans:

In connection with the recapitalisation proposal announced after the year end reporting date, the Consolidated Entity has refinanced its existing debt facilities. This will result in all the disclosed contractual liabilities for secured bank loans at year end 30 June 2010 having maturity dates expiring on 30 September 2013. Further, the recapitalisation proposal includes an equity raising of a minimum of \$102,500,000 through an underwritten entitlement issue and placement. The proceeds from this equity raising will be used to pay down debt, meet deferred consideration liabilities and pay transaction costs associated with the recapitalisation proposal. The refinanced facilities will be reduced to \$230,000,000 as a mandatory \$50,000,000 of the equity raising will be applied to a permanent reduction in the overall facilities of the Consolidated Entity.

Notes to the consolidated financial statements for the year ended 30 June 2010

24. Financial risk management/financial instruments (continued)

There are no other significant uncertainties in the timing or amount of contractual liabilities.

Interest rate risk

Interest rate risk refers to the risk that the fair value of the future cash flows of financial instruments will fluctuate because of changes in market interest rates.

The Consolidated Entity has no significant interest-bearing assets. The Consolidated Entity's interest-rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the Consolidated Entity to cash flow interest rate risk. Borrowings issued at fixed rates expose the Consolidated Entity to fair value interest rate risk. The Consolidated Entity's policy is to ensure between 25% and 50% of its exposure to changes in interest rates on borrowings is on a fixed rate basis. This is achieved by entering into interest rate swaps.

Such interest rate swaps have the economic effect of converting borrowings from floating to fixed rates, lower than those available if the Consolidated Entity borrowed at fixed rates directly. Under the interest rate swaps, the Consolidated Entity agrees with other parties to exchange, at specified intervals, the difference between fixed contract rates and floating rate interest amounts calculated by reference to the agreed notional principal amounts. Refer to Note 19 for details on the interest rate swap facility.

The impact of a change in interest rates by $\pm 1\%$ from the year end rates applicable to the loans and borrowings is set out below:

Fair values

Fair values versus carrying amounts

The fair values of financial assets and liabilities, together with the carrying amounts shown in the statement of financial position, are as follows:

Consolidated In thousands of AUD	30 June 2010		30 June 2009	
	Carrying amount	Fair value	Carrying amount	Fair value
Cash and cash equivalents	22,607	22,607	23,531	23,531
Bank short-term deposit	155	155	28	28
Trade receivables	89,358	89,358	105,844	105,844
Derivative financial liabilities	(2,950)	(2,950)	(4,353)	(4,353)
Interest-bearing deposits	565	565	223	223
Trade and other payables	(59,700)	(59,700)	(67,796)	(67,796)
Secured bank loan	(273,866)	(273,866)	(273,106)	(273,106)
Finance lease liabilities	(2,216)	(2,216)	(2,836)	(2,836)
Hire purchase lease liabilities	(3,403)	(3,403)	(3,508)	(3,508)
Loan notes payable	(3,892)	(3,892)	-	-
Other loans payable	(703)	(703)	(516)	(516)
	(234,045)	(234,045)	(222,489)	(222,489)

The basis for determining the fair value is disclosed in Note 1(u).

Profile

At the reporting date the interest rate profile of the Company's and the Consolidated Entity's interest-bearing financial instruments with interest rate risk was:

In thousands of AUD	Consolidated Carrying amount	
	2010	2009
Variable rate instruments		
Secured bank loans	273,866	273,106
Cash and cash equivalents	22,607	23,531
Deposits	155	28

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2009.

Consolidated Effect in thousands of AUD	Profit or loss		Equity	
	+100bp	-100bp	+100bp	-100bp
30 June 2010				
Variable rate instruments	(2,642)	2,642	-	-
Interest rate swap	702	(702)	(2,248)	(3,652)
Cash flow sensitivity (net)	(1,940)	1,940	(2,248)	(3,652)
30 June 2009				
Variable rate instruments	(2,675)	2,675	-	-
Interest rate swap	719	(719)	(3,454)	(4,891)
Cash flow sensitivity (net)	(1,956)	1,956	(3,454)	(4,891)

Currency risk

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The source and nature of this risk arises from operations and translation risks.

The Consolidated Entity generated approximately 28% of its net revenue in FY2010 from outside Australia. The Consolidated Entity's reporting currency is Australian dollars, however the international operations give rise to an exposure to changes in foreign exchange rates, as the majority of its revenues from outside Australia are denominated in currencies other than Australian dollars, most significantly pound sterling and US dollars. In addition, the Consolidated Entity has significant portion of its long-term borrowings and deferred consideration liabilities denominated in pound sterling and US dollars. Therefore changes in exchange rates impact the Consolidated Entity's financial indebtedness, quantum of deferred consideration liabilities and earnings as reported in Australian dollars.

The Consolidated Entity partially hedges the exposure to foreign currency assets on the balance sheet through obtaining borrowings in foreign currencies to minimise the exposure for the Consolidated Entity. Interest on these borrowings is denominated in currencies that match the cash flows generated by the underlying operations of the consolidated entities, primarily US dollars and pound sterling. This provides an economic hedge. The Consolidated Entity will from time to time enter into forward rate agreements to hedge its net investment in foreign operations. Such forward rate agreements have the economic effect of fixing the Australian dollar value of foreign operations.

The Consolidated Entity has minimal exposure to profit and loss translation risk as the majority of transactions denominated in foreign currency are transacted by entities within the group with the same functional currency of the relevant transaction.

Fair value hierarchy

The table below analyses financial instruments carried at fair value, by valuation method.

The different levels have been defined as follows:

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

In thousands of AUD	Level 1	Level 2	Level 3	Total
30 June 2010				
Derivative financial liabilities	–	(2,950)	–	(2,950)
	–	(2,950)	–	(2,950)
30 June 2009				
Derivative financial liabilities	–	(4,353)	–	(4,353)
	–	(4,353)	–	(4,353)

Capital Management

The Consolidated Entity's key sources of capital are available committed facilities under the Cash Advance Facility and share capital. The Board seeks to maintain a balance between higher returns that might be possible with higher levels of gearing and the advantages afforded by a prudent capital position.

Under the terms of its Cash Advance Facility, the Consolidated Entity is required to maintain certain maximum capitalisation (book), maximum leverage and minimum interest cover ratios. At 30 June 2010 the Consolidated Entity received waivers from its lender in relation to a number of these requirements and is in compliance with these amended requirements.

The Consolidated Entity is also now subject to restrictions on the payment of future dividends under its refinance of debt facilities and deferred consideration restructure (see Note 32 Subsequent events for further details), such that no dividends can be paid until after 30 September 2012, and then, paid only if certain leverage and deferred consideration payments have been met.

Notes to the consolidated financial statements for the year ended 30 June 2010

25. Commitments

Operating leases

Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

In thousands of AUD	2010	Consolidated 2009
Less than one year	13,948	13,380
Between one and five years	20,525	23,144
More than five years	891	404
	35,364	36,928

The Consolidated Entity leases property under non-cancellable operating leases generally expiring from two to ten years. Leases generally provide the Consolidated Entity with a right of renewal at which time terms are renegotiated. Some lease payments comprise a base amount plus an incremental contingent rental. Contingent rentals are based on movements in the consumer price index.

Generally operating leases are subject to standard two to five year renewal terms with no purchase option or escalation clauses included.

During the year ended 30 June 2010, \$16,578,015 was recognised as an expense in the income statement in respect of operating leases (2009: \$15,640,465).

Other expenditure commitments

The Consolidated Entity has entered into contracts with various advisors in relation to the equity raising announced after the year end reporting date. See Note 32 Subsequent events for further details on the equity raising. These expenditure commitments are expected to be settled within twelve months and as they are in relation to transaction costs for share capital they will be accounted for as a deduction from equity.

26. Contingencies

Contingent liabilities

Indemnities

Indemnities have been provided to Directors and certain Executive Officers of the Company in respect to third parties arising from their positions, except where the liability arises out of conduct involving lack of good faith. No monetary limit has been applied to these agreements and there are no known obligations outstanding at 30 June 2010.

The Consolidated Entity has agreed to provide Jeremy Philips with an indemnity in respect of Australian income tax, including related interest, fines, penalties, charges and other costs referable to that Australian income tax (collectively "tax") payable by him in respect of the CEO LTIP shares. The indemnity will only apply where the CEO LTIP shares are issued at a discount, that is where the market value of a Photon share on the date of the issue under the recapitalisation proposal (see Note 32 Subsequent events for further details) is greater than the issue price (10 cents) and the discount is treated as taxable for income tax purposes. If the indemnity applies, then Photon's liability under the indemnity will not exceed an amount equal to 46.5% of the discount multiplied by the total number of CEO LTIP shares. If the issue of the CEO LTIP shares at a discount gives rise to a taxing event which is covered by the indemnity, Jeremy Philips may obtain a benefit in the form of reduced tax payable upon disposal of his CEO LTIP shares because of a taxing event. Where Photon is required to make a payment under the indemnity, Jeremy Philips is obliged to pass the benefit of the resulting tax savings in respect of any CEO LTIP shares which he ceases to own back to Photon. The effect of this is to partially reimburse Photon for payments previously made by Photon under the indemnity.

27. Controlled entities

Particulars in relation to controlled entities:

Name	Consolidated Entity interest	
	2010 %	2009 %
Parent entity		
Photon Group Limited		
Controlled entities		
AdPartners Group Pty Limited	100	100
Ad Partners Group (Media) Pty Limited	100	100
SC Division Pty Ltd	100	100
— Australian Business Theatre Pty Limited	100	100
— ABT Limited ⁽ⁱⁱ⁾	100	100
— ABT Creative ^(xiv)	100	100
Brass Tacks Pty Limited	100	100
— Kaleidoscope Marketing Communications Pty Limited	100	100
CPR Communications and Public Relations Pty Limited	100	100
Australian Research Group Pty Limited	100	100
Capital Policies and Trade Pty Limited	100	94
The Precinct Group Pty Limited	100	100
— Vox Holdings Pty Limited	100	100
— Ross Barr & Associates Pty Ltd	100	100
ImageBox Group Pty Limited	51	51
Love Pty Limited	100	100
IDEAssociates Pty Limited	100	100
Returnity Pty Limited	100	100
The Bailey Group NZ Ltd ⁽ⁱ⁾	100	100
Photon Group NZ Ltd ⁽ⁱ⁾	100	100
Barimos Pty Limited	100	100
— The Bailey Group Pty Limited	100	100
— Powerforce Total Merchandising Pty Limited	100	100
— Retail*Facts Pty Limited	100	100
— REL Field Marketing Australia Pty Limited	100	100
— The Leading Edge Market Research Consultants Pty Limited	100	100
— The Leading Edge Market Research Consultants Limited ⁽ⁱⁱⁱ⁾	100	100
— The Leading Edge Market Research Consultants Pte Limited ^(vi)	100	100
ONAT Holdings Pty Limited	100	100
— Orchard National Pty Limited	100	100
— Brand Impact Pty Limited	100	100
— Retail Insight Australia Pty Limited	100	100
Be Interactive Holdings Pty Limited	100	100
— MessageNet Pty Limited	100	100
— Be Retail Pty Ltd	100	100
— Blue Sky Frog Pty Limited	100	100
— Legion Interactive(NZ) Pty Limited ⁽ⁱ⁾	100	100
— Media Zoo Pty Limited	99.1	99.1
— Be Interactive Pty Ltd	100	100
Kinetics Pty Limited	100	100
Counterpoint Marketing & Sales Pty Limited	100	100
Belong Pty Limited	100	100
— SEE Life Differently Holdings Pty Limited	100	100
SEE Life Differently Pty Limited	100	100
Creo Limited ⁽ⁱ⁾	100	100
Demonstration Plus Pty Limited	100	100
— 4Exposure Pty Limited	100	100

Notes to the consolidated financial statements for the year ended 30 June 2010

27. Controlled entities (continued)

Name	Consolidated Entity interest	
	2010 %	2009 %
Demonstration Plus(NZ) Pty Limited ⁽ⁱ⁾	100	100
iMega Pty Ltd	100	100
— USA Online Pty Limited	100	100
— iMarketing Pty Limited	100	100
— Web Agency Pty Limited	100	100
— Freegroove Pty Limited	100	100
— Zearch Pty Limited	100	100
— ICM Division Pty Ltd	100	100
Ausrep Pty Ltd	100	100
Jigsaw Strategic Research Pty Limited	100	100
Belgiovane Williams Mackay Pty Ltd ^(xvii)	100	100
— Paterson Partners Adcafe Pty Limited	100	100
— Cox Inall Communications Pty Limited	100	100
— Pixel Dust Pty Limited	100	100
— I-Group BWM Pty Limited	100	100
DVL Smith Group Pty Ltd	100	100
— DVL Smith Group Limited ⁽ⁱⁱⁱ⁾	100	100
— DVL Smith Consulting Limited ^(iv)	100	100
— DVL Smith Training Limited ^(v)	100	100
C4 Communications Pty Limited	100	100
City Public Relations Pty Limited	100	100
The Artel Group Pty Limited	100	100
— SI Division Pty Ltd	100	100
— FM Division Pty Ltd	100	100
— ICD Division Pty Ltd	100	100
Found Agency Pty Limited	100	100
— Yield Media Pty Limited	100	100
Wardell R C Advertising Pty Ltd	100	100
Eastern Media Marketing Pty Ltd	100	100
Element Media Marketing Pty Ltd	100	100
Bellamy Hayden Pty Limited	100	100
— Bellamy Hayden SE Asia Pty Limited	100	100
Auspoll Pty Limited	100	100
Domain Active Holdco Pty Limited	100	100
— Domain Active Pty Limited	100	28.25
Club Food Brokerage Pty Limited	100	100
Club Sales & Merchandising Pty Limited	100	100
Future House Pty Limited	100	100
— Geeksville Pty Limited	100	100
Crystal Storm Pty Limited	51	51
Mark Communications Pty Limited	100	100
ISS Marketing Pty Limited	100	100
— ISS Marketing NZ Limited ⁽ⁱ⁾	100	100
BMF Holdco Pty Limited	100	100
BMF Advertising Pty Limited	100	100
The Population Pty Limited	100	100
Frank PR Australia Pty Limited	100	100
Photon (Hong Kong) Limited ⁽ⁱⁱ⁾	100	100
Naked Communications Australia Pty Limited	100	100
— Naked Breakfast Pty Limited	100	100
— Naked NZ Limited ⁽ⁱ⁾	100	100
Dark Blue Sea Limited	100	28.25
— Dark Blue Sea Enterprises Pty Limited	100	28.25
— Fabulous Parking Pty Limited	100	28.25
— DarkBlue.com Pty Limited	100	28.25
— DBS Administration Pty Limited	100	28.25
— Fabulous.com Pty Limited	100	28.25

Name	Consolidated Entity interest	
	2010 %	2009 %
— Pageseeker.com Pty Limited	100	28.25
— Protopixel Pty Limited	100	28.25
— Roar.com Pty Limited	100	28.25
— Fabulous.com.au Pty Limited	100	28.25
— Yexa Pty Limited	100	28.25
— Whois Privacy Pty Limited	100	28.25
— Domain Active Europe Limited ⁽ⁱⁱⁱ⁾	100	28.25
Resource Experience Limited ⁽ⁱⁱⁱ⁾	100	100
— RELSC Franco Limited ⁽ⁱⁱⁱ⁾	51	51
— REL Sales Consulting Limited ⁽ⁱⁱⁱ⁾	100	100
Lorica Group Limited ⁽ⁱⁱⁱ⁾	100	100
— Corporate Edge Group Limited ⁽ⁱⁱⁱ⁾	100	100
— Likemind Limited ⁽ⁱⁱⁱ⁾	100	100
— CLK MPL Limited ^(iv)	100	100
— Lorica Group Trustees Limited ^(v)	100	100
North By Northwest Group Limited ⁽ⁱⁱⁱ⁾	100	100
Hotwire Public Relations GmbH ^(vii)	100	100
— Hotwire Public Relations SARL ^(viii)	100	100
— Hotwire Public Relations SL ^(ix)	100	100
— Hotwire Public Relations SRL ^(x)	100	100
— Hotwire Public Relations Limited ⁽ⁱⁱⁱ⁾	100	100
— Skywrite Communications Limited ⁽ⁱⁱⁱ⁾	100	100
— 33 Digital Limited ⁽ⁱⁱⁱ⁾	100	100
Naked Communications Limited ⁽ⁱⁱⁱ⁾	100	100
— Naked Ventures Limited ⁽ⁱⁱⁱ⁾	100	100
— Hyper Happen Limited ⁽ⁱⁱⁱ⁾	100	100
— Lunch Communications Limited ⁽ⁱⁱⁱ⁾	100	100
— Ne Kid SAS ^(viii)	100	100
— Naked Communications BV ^(xi)	100	100
— Naked Communications AS ^(xii)	100	100
— Naked Communications Sweden AB ^(xv)	65	65
— Naked Communications ApS ^(xvi)	92.5	92.5
— Naked Communications Holdings Inc ^(iv)	100	100
— Naked New York LLC ^(iv)	100	100
— Naked Communications Inc ^(xiii)	100	100
Photon Group UK Holdings Pty Limited	100	100
Photon Group UK Limited ⁽ⁱⁱⁱ⁾	100	100
Sledge Limited ⁽ⁱⁱⁱ⁾	100	100
Frank PR Limited ⁽ⁱⁱⁱ⁾	100	100
The Bailey Group UK Limited ⁽ⁱⁱⁱ⁾	100	100
Retail Insight Limited ⁽ⁱⁱⁱ⁾	100	100
Photon Group (US) Pty Limited	100	100
Photon Group (US) Inc ^(iv)	100	100
OB Media LLC ^(iv)	51	51
Precinct LLC ^(iv)	100	100
Findology Interactive Media Inc ^(iv)	100	100

(i) Companies incorporated and carrying on a business in New Zealand.

(ii) Companies incorporated and carrying on a business in Hong Kong.

(iii) Companies incorporated and carrying on a business in the United Kingdom.

(iv) Companies incorporated and carrying on a business in the United States of America.

(v) Companies incorporated in the United Kingdom and dormant.

(vi) The Leading Edge Market Research Consultants Pte Limited was incorporated and carries on a business in Singapore.

(vii) Hotwire Public Relations GmbH was incorporated and carries on a business in Germany.

(viii) Companies incorporated and carrying on a business in France.

(ix) Hotwire Public Relations SL was incorporated and carries on a business in Spain.

(x) Hotwire Public Relations SRL was incorporated and carries on a business in Italy.

Notes to the consolidated financial statements for the year ended 30 June 2010

27. Controlled entities (continued)

- (xi) Naked Communications BV was incorporated and carries on a business in the Netherlands.
- (xii) Naked Communications AS was incorporated and carries on a business in Norway.
- (xiii) Naked Communications Inc. was incorporated and carries on a business in Japan.
- (xiv) ABT Creative Limited was incorporated and carries on a business in China.
- (xv) Naked Communications Sweden AB was incorporated and carries on a business in Sweden.
- (xvi) Naked Communications ApS was incorporated and carries on a business in Denmark.
- (xvii) Although only 51% of the issued capital was acquired by the Company, the option tied to the remaining 49% non controlling interest requires 100% of the earnings and statement of financial position to be included in the Consolidated Entity's statement of financial position and income statement.

28. Acquisitions of subsidiaries and non controlling interests

The Consolidated Entity has adopted revised AASB 3 *Business Combinations* (2008) and amended AASB 127 *Consolidated and Separate Financial Statements* (2008) for business combinations occurring in the financial year commencing 1 July 2009.

In the current period, the following entities were acquired:

On 7 December 2009, the Company acquired a controlling interest in Dark Blue Sea Limited, as a result of acceptances under the takeover offer which commenced on 1 October 2009. After gaining acceptances in excess of 90% of the share capital, the Company compulsorily acquired the remaining share capital in Dark Blue Sea Limited and therefore owns 100% of the share capital post the compulsory acquisition period. Prior to the takeover bid, the Company had a 29.79% interest in Dark Blue Sea Limited. The purchase price for the remaining 70.21% interest in Dark Blue Sea acquired during the year ended 30 June 2010 was \$19,826,000.

From 7 December 2009, as a result of acquiring a controlling interest, the equity accounting method no longer applies and Dark Blue Sea forms part of the consolidated financial statements of the Consolidated Entity.

The purchase price for the other acquisition during the period, which is not individually significant, is contingent upon future earnings of the business acquired.

In the prior period, there were no individually material significant acquisitions.

Effect of acquisitions for the year ended 30 June 2010

The acquisitions had the following effect on the Consolidated Entity's assets and liabilities.

Acquiree's identifiable assets and liabilities assumed at the acquisition date

In thousands of AUD	Recognised values	Fair value adjustments	Carrying amounts
Plant and equipment	256		256
Intangible assets	2,632	6,580	9,212
Trade and other receivables	1,173		1,173
Cash and cash equivalents	2,978		2,978
Deferred tax asset	195		195
Other assets	1,702		1,702
Trade and other payables	(1,942)		(1,942)
Deferred tax liability	—	(306)	(306)
Provisions	(577)		(577)
Tax asset	11		11
Other liabilities	(1,706)		(1,706)
	4,722	6,274	10,996

Consideration transferred

Cash	19,826	Total consideration transferred	29,665
Transfer from equity accounted investee	8,379	Incidentals on prior acquisitions	348
Contingent consideration	1,460	Less fair value on identifiable net assets	(10,996)
	29,665		19,017

The above acquisitions cumulatively contributed \$3,067,629 of net revenues to the total net revenue and \$3,373,884 of net losses to the total loss after tax and of the Consolidated Entity.

The full year net revenue effect, if the above acquisitions were acquired on 1 July 2009, would have been to increase net revenue by \$4,511,132.

The full year net loss after tax effect, if the above acquisitions were acquired on 1 July 2009, would have been to reduce the loss after tax by \$468,356.

Goodwill has arisen on the acquisition of entities during the year as some intangibles such as key management and technical employee relationships and certain customer relationships did not meet the criteria for recognition as an intangible asset at the date of acquisition. Considering the characteristics of marketing and communication services companies, acquisitions do not usually have significant amounts of tangible assets as the principal asset typically acquired is creative talent and know-how of people. As a result, a substantial proportion of the purchase price is allocated to goodwill. Assets and liabilities of the acquired entities have been included in the financial statements based on fair values.

Fair value adjustments represent identifiable intangible assets, net of deferred tax liabilities, acquired in connection with the business combination.

Contingent/deferred consideration:

Contingent/deferred consideration is based on the achievement of specific earnings hurdles and the fair value of the deferred consideration at acquisition was calculated by estimating future earnings and an estimate of whether such targets will be achieved.

Any changes to the contingent/deferred consideration during the year are recognised in the income statement as a fair value adjustment to deferred consideration.

Effect of acquisitions for the year ended 30 June 2009

The acquisitions had the following effect on the Consolidated Entity's assets and liabilities.

Acquiree's identifiable assets and liabilities assumed at the acquisition date

In thousands of AUD	Recognised Values	Fair value adjustments	Carrying amounts
Plant and equipment	137	—	137
Intangible assets	218	394	612
Trade and other receivables	385	—	385
Cash and cash equivalents	972	—	972
Deferred tax asset	1	—	1
Other assets	86	—	86
Trade and other payables	(213)	—	(213)
Interest bearing liabilities	(70)	—	(70)
Deferred tax liability	—	(118)	(118)
Provisions	(21)	—	(21)
Tax liabilities	(72)	—	(72)
Other liabilities	(1,089)	—	(1,089)
Net identifiable assets	334	276	610

Consideration transferred

Cash	6,415
Contingent consideration	1,063
	7,478

Goodwill

Total consideration transferred	7,478
Incidentals on prior acquisitions	2,090
Less fair value on identifiable net assets	(610)
	8,958

The above acquisitions cumulatively contributed \$13,557,933 of net revenues to the total net revenue and \$5,505,138 of net profit to the total profit after tax of the Consolidated Entity.

The full year net revenue effect, if the above acquisitions were acquired on 1 July 2008, would have been to increase net revenue by \$448,328.

The full year net profit after tax effect, if the above acquisitions were acquired on 1 July 2008, would have been to decrease the profit after tax by \$610,524.

Notes to the consolidated financial statements for the year ended 30 June 2010

29. Reconciliation of cash flows from operating activities

In thousands of AUD	Note	2010	Consolidated 2009
(i) Reconciliation of cash			
For the purpose of the statements of cash flows, cash includes cash on hand and at bank and short-term deposits at call, net of outstanding bank overdrafts. Cash at the end of the financial year as shown in the statements of cash flows is reconciled to the related items in the statement of financial position as follows:			
Cash assets	8	22,762	23,559
(ii) Reconciliation of profit/(loss) after income tax to net cash provided by operating activities			
Profit/(Loss) after income tax		(88,107)	21,401
(Profit)/loss on sale of non-current assets		(337)	84
Share-based payments expense		2,267	3,628
Add/(less) non-cash items:			
Depreciation and amortisation		7,942	9,267
Occupancy costs – release of provision		(995)	(36)
Lease make good amortisation		331	343
Release of lease make good provision		(205)	(257)
Equity settled bonus		76	115
Share of (profits)/losses of associated entities		117	(145)
Present value interest charges on deferred consideration of acquisitions		5,480	5,588
Amortisation of identifiable intangibles		13,154	11,289
Impairment loss		88,930	4,215
Fair value adjustment on deferred consideration liability		52	–
Increase/(decrease) in income taxes payable		(13,208)	(616)
Increase/(decrease) in deferred tax liabilities		(1,709)	(311)
(Increase)/decrease in deferred tax assets		(2,252)	(736)
Net cash provided by operating activities before change in assets and liabilities		11,536	54,829
Changes in assets and liabilities adjusted for the effects of purchase and disposal of controlled entities during the financial year:			
(Increase)/decrease in receivables		18,297	(737)
(Increase)/decrease in work in progress		6,470	(425)
(Increase)/decrease in prepayments		625	4,117
(Increase)/decrease in other assets		2,205	(73)
Increase/(decrease) in payables		(11,757)	(21,034)
Increase/(decrease) in deferred income		2,296	1,147
Increase/(decrease) in provisions		6,060	(500)
Net cash from operating activities		35,732	37,324

30. Parent entity disclosures

As at, and throughout, the financial year ending 30 June 2010 the parent Company of the Consolidated Entity was Photon Group Limited.

In thousands of AUD	The Company	
	2010	2009
Result of the parent entity		
Profit/(loss) for the period	(5,752)	25,404
Other comprehensive income	6	(5,049)
Total comprehensive income for the period	(5,746)	20,355
Financial position of the parent entity at year end		
Current assets	18,770	4,029
Total assets	647,098	537,251
Current liabilities	79,075	83,681
Total liabilities	273,490	262,350
Total equity of the parent entity comprising of:		
Share capital	369,268	255,500
Option reserve	11,809	9,542
Hedging reserve	(2,950)	(4,352)
Retained earnings	(4,519)	14,211
Total Equity	373,608	274,901

Parent entity guarantees in respect of debts of its subsidiaries

The parent entity has entered into a Deed of Cross Guarantee with the effect that the Company guarantees debts in respect of its subsidiaries.

Further details of the Deed of Cross Guarantee and the subsidiaries subject to the deed, are disclosed in Note 31.

Contingent liabilities

Indemnities

Indemnities have been provided to Directors and certain Executive Officers of the Company in respect to third parties arising from their positions, except where the liability arises out of conduct involving lack of good faith. No monetary limit applied to these agreements and there are no known obligations outstanding at 30 June 2010.

31. Deed of Cross Guarantee

Pursuant to ASIC Class Order 98/1418 (as amended) dated 13 August 1998, the wholly-owned subsidiaries listed below are relieved from the *Corporations Act 2001* requirements for preparation, audit and lodgement of financial statements, and Directors' Report.

It is a condition of the Class Order that the Company and each of the subsidiaries enter into a Deed of Cross Guarantee. The effect of the Deed is that the Company guarantees to each creditor payment in full of any debt in the event of winding up of any of the subsidiaries under certain provisions of the *Corporations Act 2001*. If a winding up occurs under other provisions of the Act, the Company will only be liable in the event that after six months any creditor has not been paid in full. The subsidiaries have also given similar guarantees in the event that the Company is wound up.

The Leading Edge Market Research Consultants Pty Limited, The Bailey Group Pty Ltd, Barimos Pty Ltd, BMF Holdco Pty Limited, Belong Pty Limited became party to the Deed on 25 June 2008. Counterpoint Marketing and Sales Pty Ltd and Demonstration Plus Pty Limited became party to the Deed on 29 June 2010.

A consolidated income statement and consolidated statement of financial position, comprising the Company and controlled entities which are party to the Deed, after eliminating all transactions between parties to the Deed of Cross Guarantee, at 30 June 2010 is set out as follows:

Summarised income statement and retained profits

In AUD	Consolidated 2010
Profit/(Loss) before tax	(2,098,546)
Income tax benefit	3,356,803
Profit after tax	1,258,257
Retained profits at beginning of year	11,876,630
Dividends recognised during the year	(12,975,680)
Retained profits at end of year	159,207
Attributable to:	
Equity holders of the Company	159,207
Profit for the period	159,207

Statement of financial position

In AUD	Consolidated 2010
Assets	
Cash and cash equivalents	4,297,534
Trade and other receivables	27,319,609
Income tax receivable	8,875,509
Other assets	611,290
Total current assets	41,103,942
Receivables	107,352,038
Other financial assets	333,623,500
Deferred tax assets	5,908,803
Plant and equipment	5,062,966
Other assets	30,989
Intangible assets	177,931,115
Total non-current assets	629,909,411
Total assets	671,013,353
Liabilities	
Trade and other payables	17,945,656
Loans and borrowings	13,588,385
Employee benefits	3,430,465
Provision	847,762
Deferred consideration	56,639,647
Unearned revenue	1,714,097
Other financial liabilities	483,986
Total current liabilities	94,649,998
Loans and borrowings	138,706,012
Deferred tax liabilities	940,183
Employee benefits	1,042,231
Provisions	1,169,738
Deferred consideration	53,752,489
Other financial liabilities	2,466,263
Total non-current liabilities	198,076,916

Notes to the consolidated financial statements for the year ended 30 June 2010

31. Deed of cross guarantee (continued)

In AUD	Consolidated 2010
Total liabilities	292,726,914
Net assets	378,286,439
Equity	
Issued capital	369,268,473
Reserves	8,858,758
Retained profits	159,207
Total equity	378,286,438

32. Subsequent events

Recapitalisation Proposal

Since 7 June 2010, Photon conducted a strategic review of its capital structure. On 17 August 2010, the Company announced a recapitalisation proposal which included the following elements:

- raising a minimum of \$102,500,000 through an underwritten entitlement issue and placement;
- a restructure of the deferred consideration payments; and
- refinancing the Company's debt facilities.

For full details of the recapitalization proposal please refer to the prospectus dated 17 August 2010.

Equity raising

The Company announced an equity raising of \$102,500,000 on 17 August 2010. The equity raising includes an underwritten entitlement issue of \$62,500,000 and an underwritten placement of \$40,000,000. The two components of the underwritten equity raising were approved by shareholders at a general meeting on 17 September 2010. The equity raising was completed on 29 September 2010. The proceeds from the equity raising (net of fees) will be used to pay down existing debt and to satisfy current deferred consideration liabilities due on or around 30 September 2010.

Deferred consideration restructure

In August 2010 the Consolidated Entity entered into agreements with substantially all of the vendors of operating entities expected to receive future deferred consideration payments to restructure the terms of the

deferred consideration payments. The effect of the restructured arrangements is to:

- provide an aggregate cap for substantially all of the estimated future deferred consideration payments of approximately \$176,000,000;
- reduce the total estimated deferred consideration to be paid in cash to \$149,000,000 with approximately 15% of the aggregate final capped payments being paid in Photon shares (subject to shareholder approval); and
- approximately 50% of the aggregate estimated payments (\$83,000,000) only being made if the Consolidated Entity reaches certain hurdles in relation to financial performance and leverage ratio levels.

Refinance of debt facilities

The Company has agreed with its lender to refinance its existing debt facilities with \$230,000,000 cash advance facilities and a \$45,000,000 bank guarantee facility. The cash advance facilities in combination with the operating cash flow of the Consolidated Entity are anticipated to provide capacity to make future deferred consideration payments which are to be settled as cash. The bank guarantee facility is drawn to provide bank guarantees to the beneficiaries for the cash portion of the deferred consideration payments due after 30 September 2010. The new facilities will have a term of three years, expiring in September 2013 and will have financial covenants and margins substantially in line with the existing facilities.

The financial effects of the above transactions have not been brought to account in the financial statements for the year ended 30 June 2010.

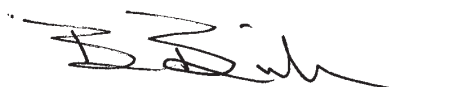
Other than the matters discussed above, there has not arisen, in the interval between the end of the financial year and the date of this report, any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors of the Company, to affect significantly the operations of the Consolidated Entity, the results of those operations, or the state of affairs of the Consolidated Entity, in future financial years.

Directors' Declaration

1. In the opinion of the Directors of Photon Group Limited ("the Company"):
 - (a) the consolidated financial statements and notes, set out on pages 29 to 86 and the Remuneration report in the Directors' Report, set out on pages 15 to 28, are in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the Consolidated Entity's financial position as at 30 June 2010 and of its performance, for the financial year ended on that date;
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001; and
 - (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.
2. There are reasonable grounds to believe the Company and entities identified in note 31 will be able to meet any obligations or liabilities to which they are or may become subject by virtue of the Deed of Cross Guarantee between the Company and those entities pursuant to ASIC Class Order 98/1418.
3. The Directors have been given the declarations by the Chief Executive Officer and Chief Financial Officer for the financial year ended 30 June 2010 pursuant to Section 295A of the *Corporations Act 2001*.
4. The Directors draw attention to Note 1(a) to the consolidated financial statements, which includes a statement of compliance with International Financial Reporting Standards.

Dated at Sydney this 30th day of September 2010.

Signed in accordance with a resolution of the Directors:



Brian Bickmore

Director

Independent Auditor's report to the members of Photon Group Limited



Independent auditor's report to the members of Photon Group Limited

Report on the financial report

We have audited the accompanying financial report of the Group comprising Photon Group Limited (the Company) and the entities it controlled at the year's end or from time to time during the financial year, which comprises the consolidated statement of financial position as at 30 June 2010, and consolidated income statement and consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year ended on that date, a summary of significant accounting policies and other explanatory notes 1 to 32 and the directors' declaration.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal control relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In note 1, the directors also state, in accordance with Australian Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

Auditor's responsibility

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

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

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001* and Australian Accounting Standards (including the Australian Accounting Interpretations), a view which is consistent with our understanding of the Group's financial position and of its performance.

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



Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

Auditor's opinion

In our opinion:

(a) the financial report of the Group is in accordance with the *Corporations Act 2001*, including:

- (i) giving a true and fair view of the Group's financial position as at 30 June 2010 and of its performance for the year ended on that date; and
- (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001.

(b) the financial report also complies with International Financial Reporting Standards as disclosed in note 1.

Report on the remuneration report

We have audited the Remuneration Report included in of the directors' report for the year ended 30 June 2010. The directors of the company are responsible for the preparation and presentation of the remuneration report in accordance with Section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with auditing standards.

Auditor's opinion

In our opinion, the remuneration report of Photon Group Limited for the year ended 30 June 2010, complies with Section 300A of the *Corporations Act 2001*.

A handwritten signature in black ink, appearing to read 'J Wigglesworth'.

KPMG

A handwritten signature in black ink, appearing to read 'John Wigglesworth'.

John Wigglesworth
Partner

Sydney

30 September 2010

Lead Auditor's independence declaration under Section 307 of The Corporations Act 2001



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

To: the directors of Photon Group Limited

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2010 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.

A handwritten signature in black ink, appearing to read 'John Wigglesworth'.

KPMG

A handwritten signature in black ink, appearing to read 'John Wigglesworth'.

John Wigglesworth
Partner

Sydney

30 September 2010

ASX Additional Information

Additional information required by the Australian Securities Exchange Limited Listing Rules and not disclosed elsewhere in this report is set out below. The shareholder information set out below was applicable at 20 September 2010.

Substantial shareholders

The number of ordinary shares held by substantial shareholders and their associates is set out below:

Shareholder	Number
RG Capital Multimedia Pty Limited	44,573,821

Unquoted equity securities

As at 20 September 2010 there were 8,806,868 options granted over unissued ordinary shares in the Company. Details of holders of 20% or more of those options are set out in the Directors' Report.

Voting rights

Ordinary shares – refer to Note 23.

Options – refer to Note 20 and the Remuneration Report included in the Directors' Report.

Distribution of equity security holders

Range	Number of equity security holders	
	Ordinary shares	Options
1 – 1,000	481	2
1,001 – 5,000	1,126	57
5,001 – 10,000	519	50
10,001 – 100,000	806	59
100,001 and over	187	15

The number of shareholders holding less than a marketable parcel of ordinary shares is 1,608.

Twenty largest shareholders

Rank	Name	Units	% of issued capital
1	RG Capital Multimedia Pty Limited	18,047,778	9.63
2	Merrill Lynch (Australia) Nominees Pty Limited <Berndale A/C>	17,462,262	9.32
3	Mr Jeremy Philips	9,000,000	4.80
4	UBS Nominees Pty Limited	7,000,000	3.73
5	National Nominees Limited	5,124,893	2.73
6	Wyllie Group Pty Limited	4,946,262	2.64
7	Merrill Lynch (Australia) Nominees Limited	3,897,385	2.08
8	Equitas Nominees Pty Limited <821471 A/C>	3,651,112	1.95
9	Carinya Media Management Pty Limited	3,390,435	1.81
10	J P Morgan Nominees Australia Pty Limited	3,345,077	1.78
11	Citicorp Nominees Pty Limited	3,126,069	1.67
12	Irish Global Equity Limited	2,530,517	1.35
13	RG Capital Multimedia Limited	2,400,000	1.28
14	Mr Matthew William Bailey + Mrs Frances Loraine Bailey <Matthew Bailey A/C>	2,335,235	1.25
15	Wyllie Group Pty Limited	2,320,001	1.24
16	Bond St Custodians Limited <Officium Special Situat A/C>	2,054,412	1.10
17	Franma Pty Limited <Frangipani Super Fund A/C>	2,016,063	1.08
18	Hudson Conway Investments Pty Limited	1,894,455	1.01
19	Mr Adam Mckenzie Kilgour	1,891,455	1.01
20	Asia Union Investments Pty Limited	1,800,000	0.96
Total		98,233,748	52.41

Equity securities in escrow

Date escrow period ends	Number of equity securities in escrow
30 June 2012	2,000,000
30 June 2013	3,000,000
30 June 2014	4,000,000
	9,000,000

All equity securities in escrow are ordinary shares

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Corporate Directory

Company Secretary

Eleni North

Principal Registered Office

Photon Group Limited
Level 9, 155 George Street
Sydney NSW 2000
Telephone: + 61 2 8213 8000
Facsimile: + 61 2 8213 3030

Location of Share Registry

Computershare Investor
Services Pty Limited
Level 3, 60 Carrington Street
Sydney NSW 2000
Telephone: 1300 855 080
Outside Australia: + 61 3 9415 4000
Facsimile: + 61 2 8234 5050

Securities Exchange

The Company is listed on the
Australian Securities Exchange (PGA).
The home exchange is Sydney.

Other information

Photon Group Limited,
incorporated and domiciled
in Australia, is a publicly listed
company limited by shares.

Solicitors

Gilbert + Tobin
2 Park Street
Sydney NSW 2000 Australia

Auditors

KPMG
10 Shelley Street
Sydney NSW 2000 Australia

