

Virtus Health Pty Limited

ACN 129 643 492

**Annual report
for the year ended 30 June 2012**

Virtus Health Pty Limited ACN 129 643 492
Annual Financial Report – 30 June 2012

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Directors	Marcus Darville <i>Chair</i> Simon Pither Susan Channon John McBain Andrew Othen John Esler Frank Quinn John Moller
Secretary	Glenn Powers
Alternate Directors	Michael Chapman Keith Harrison Manuela Toledo
Principal registered office in Australia	Level 3, 176 Pacific Highway Greenwich, NSW 2065
Auditor	PricewaterhouseCoopers Darling Park Tower 2 201 Sussex Street Sydney, NSW 2000
Solicitors	Minter Ellison Aurora Place 88 Phillip Street, Sydney, NSW 2000
Bankers	Australia and New Zealand Banking Group Limited Level 15, 20 Martin Place Sydney, NSW 2000 Australian Super Pty Limited as Trustee of Australian Super c/o Fidante Partners Limited as investment manager for Australian Super Level 15, 255 Pitt Street Sydney NSW 2000 Westpac Banking Corporation Level 3, 275 Kent Street Sydney, NSW 2000 Challenger Life Company Limited Level 15, 255 Pitt Street Sydney NSW 2000 GE Capital Finance Pty Limited (as Trustee of the Real Estate Financing & Services (Australia) Unit Trust) Level 13, 255 George Street Sydney NSW 2000 Massachusetts Mutual Life Insurance Company c/o Babson Capital Australia Level 22, Grosvenor Place, 255 George Street Sydney NSW 2000 Siemens Financial Services Inc 170 Wood Avenue, South Iselin New Jersey 08830, New Jersey 08830 Morgan Stanley Australia 2 Chifley Square Sydney NSW 2000 Victoria Funds Management Corporation (VFMC) Level 13, 101 Collins Street MELBOURNE VIC 3000

Directors' Report

Your directors present their report on the consolidated entity (referred to hereafter as the Group) consisting of Virtus Health Pty Limited and the entities it controlled at the end of, or during, the year ended 30 June 2012.

Directors

The following persons were directors of Virtus Health Pty Limited during the whole of the financial year and up to the date of this report:

Marcus Darville
Susan Channon
Frank Quinn
Simon Pither
John McBain
John Moller
John Esler
Andrew Othen

Michael Chapman, Manuela Toledo and Keith Harrison were reappointed as alternate directors and continue in office at the date of this report.

Principal activities

During the year the principal continuing activities of the Group were the provision of fertility services, medical day procedure services and medical diagnostic services. There were no significant changes in the nature of these activities during the period.

Dividends – Virtus Health Pty Limited

Since the end of the financial year, the directors have paid an ordinary dividend of \$45,833,685 (82 cents per ordinary share). The dividend was paid on 17 August 2012 out of retained earnings at 30 June 2012. Furthermore, a capital return of \$55,335,791 (99 cents per ordinary share) was paid on 7 September 2012.

Review of operations

The Group continued to engage in its principal activities, the results of which are disclosed in the attached financial statements.

Significant changes in the state of affairs

Significant changes in the state of affairs of the group during the financial year were as follows:

Acquisition of Queensland Fertility Group Gold Coast

On 29 July 2011 Virtus Health Pty Limited, through its wholly owned subsidiary Queensland Fertility Group Pty Limited, acquired 100% of the issued share capital Fertility Gold Coast Pty Limited for a consideration of \$5.063 million paid in cash and the issue of ordinary shares in Virtus Health Pty Limited. The cash element of the acquisition was funded by a drawdown from the Group capital expenditure facility.

Acquisition of Mackay Day Surgery

On 31 January 2012, Virtus Health Pty Limited, through its wholly owned subsidiary Queensland Fertility Group Pty Limited, acquired the business, assets and liabilities of Mackay Day Surgery Pty Limited. The net assets acquired consisted of \$374,000 of plant and equipment, liabilities totalling \$19,000 and \$155,000 of goodwill.

Matters subsequent to the end of the financial year

Acquisition of Maroubra Day Surgery

On 7 August 2012, Virtus Health Pty Limited, through its wholly owned subsidiary IVF Australia Pty Limited, acquired the remaining 50% of the issued share of Maroubra Day Surgery Pty Limited for a cash consideration of \$7.100 million. The acquisition was funded by a drawdown from the Group capital expenditure facility and existing cash.

Refinancing of the borrowing facility

On 16 August 2012, IVF Finance Pty Limited, a subsidiary of Virtus Health Pty Limited successfully renegotiated the external borrowing facility for a total of \$225,000,000, with an initial expiry date of 17 August 2013. The funds were used to pay an ordinary dividend of \$45,833,685 (82 cents per ordinary share) on 17 August 2012. A capital return of \$55,335,791 (99 cents per ordinary share) was paid on 7 September 2012.

The financial effects of these transactions have not been brought to account as at 30 June 2012. The operating results, assets and liabilities of the Maroubra Day Surgery will be consolidated from 7 August 2012.

Except for the matters discussed above, no other matter or circumstance has arisen since 30 June 2012 that has significantly affected, or may significantly affect:

- (a) the group's operations in future financial years, or
- (b) the results of those operations in future financial years, or
- (c) the group's state of affairs in future financial years.

Likely developments and expected results of operations

Further information on likely developments in the operations of the Group and the expected results of operations have not been included in this annual report because the directors believe it would be likely to result in unreasonable prejudice to the Group.

Shares under option

Unissued ordinary shares of Virtus Health Pty Limited under option at the date of this report are as follows:

Date options granted	Expiry date	Option exercise price	Number under option
10 April 2008*	16 February 2015	\$1.64	60,976
10 April 2008*	1 January 2016	\$3.15	183,496
10 April 2008*	14 February 2017	\$3.15	216,075
10 April 2008*	1 January 2018	\$3.26	228,100
10 April 2008	10 April 2018	\$2.98	9,000
10 April 2008	10 April 2018	\$2.53	1,550,000
10 April 2008	10 April 2018	\$0.01	403,536
12 November 2008	12 November 2018	\$4.12	312,527
20 November 2008	20 November 2018	\$0.00	272,470
25 February 2009	25 February 2019	\$4.12	41,000
01 July 2009	01 July 2019	\$3.11	450,000
01 October 2009	01 October 2019	\$3.11	241,491
01 July 2010	01 July 2020	\$4.71	200,000
01 September 2010	01 September 2020	\$4.71	233,546
01 July 2011	01 July 2021	\$5.17	258,027
			<u>4,660,244</u>

*These options were issued to replace options previously held in IVF Australia Pty Limited following the acquisition of IVF Sub-Holdings Pty Limited by Virtus Health Pty Limited.

No option holder has any right under the options to participate in any other share issue of the company or any other entity.

Insurance of officers

During the financial year, Virtus Health Pty Limited paid a premium of \$25,000 to insure the directors and secretaries of the Company and its Australian-based controlled entities, and the managing directors of each of the divisions of the Group.

The liabilities insured are legal costs that may be incurred in defending civil or criminal proceedings that may be brought against the officers in their capacity as officers of entities in the Group, and any other payments arising from liabilities incurred by the officers in connection with such proceedings. This does not include such liabilities that arise from conduct involving a wilful breach of duty by the officers or the improper use by the officers of their position or of information to gain advantage for themselves or someone else or to cause detriment to the company. It is not possible to apportion the premium between amounts relating to the insurance against legal costs and those relating to other liabilities.

Proceedings on behalf of the company

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

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

Environmental regulation

The group is not subject to significant environmental regulation.

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 6.

Rounding of amounts

The Company is of a kind referred to in Class Order 98/100, issued by the Australian Securities and Investments Commission, relating to the "rounding off" of amounts in the directors' report. Amounts in the directors' report have been rounded off in accordance with that Class Order to the nearest thousand dollars, or in certain cases, to the nearest dollar.

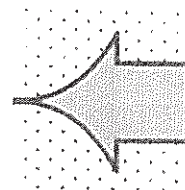
Auditor

PwC continues in office in accordance with section 325 of the *Corporations Act 2001*.

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



Marcus Darville
Director
Sydney
31 October 2012





Auditor's Independence Declaration

As lead auditor for the audit of Virtus Health Pty Limited for the year ended 30 June 2012, I declare that to the best of my knowledge and belief, there have been:

- a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
- b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Virtus Health Pty Limited and the entities it controlled during the period.

A handwritten signature in dark ink, appearing to read 'Eddie Wilkie'.

Eddie Wilkie
Partner
PricewaterhouseCoopers

Sydney
31 October 2012

PricewaterhouseCoopers, ABN 52 780 433 757
Darling Park Tower 2, 201 Sussex Street, GPO BOX 2650, SYDNEY NSW 1171
DX 77 Sydney, Australia
T +61 2 8266 0000, F +61 2 8286 9999, www.pwc.com.au

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These financial statements are the consolidated financial statements of the consolidated entity consisting of Virtus Health Pty Limited and its subsidiaries. The financial statements are presented in the Australian currency.

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

Virtus Health Pty Limited
Level 3
176 Pacific Highway
Greenwich NSW 2065

A description of the nature of the consolidated entity's operations and its principal activities is included in the review of operations in the directors' report on pages 3 to 5, which is not part of these financial statements.

The financial statements were authorised for issue by the directors on 31 October 2012. The directors have the power to amend and reissue the financial statements.

Virtus Health Pty Limited
Consolidated statement of comprehensive income
For the year ended 30 June 2012

	Notes	2012 \$'000	2011 \$'000
Revenue from continuing operations	4	165,119	131,897
Other income	5	369	817
Surgeon, consumables and associated costs		(44,674)	(34,101)
Occupancy expenses		(8,813)	(7,213)
Employee benefits expense		(47,805)	(39,756)
Advertising & marketing		(2,700)	(1,803)
Practice equipment expenses		(1,274)	(817)
Depreciation and amortisation expense	6	(8,972)	(8,277)
Finance costs	6	(13,796)	(12,611)
Professional and consulting fees		(3,017)	(2,680)
Other expenses		(9,500)	(6,900)
Share of net profit of associates accounted for using the equity method		1,436	1,066
Profit before income tax		26,373	19,622
Income tax expense	7	(6,713)	(4,285)
Profit for the year		19,660	15,337
Other comprehensive income		-	-
Total comprehensive Income is attributable to: equity holders of Virtus Health Pty Limited		19,660	15,337

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

Virtus Health Pty Limited
Consolidated balance sheet
As at 30 June 2012

	Notes	2012 \$'000	2011 \$'000
ASSETS			
Current assets			
Cash and cash equivalents	8	9,439	6,963
Trade and other receivables	9	9,613	8,191
Inventories	10	-	120
Total current assets		<u>19,052</u>	<u>15,274</u>
Non-current assets			
Investments accounted for using the equity method	11	3,913	3,822
Other financial assets	12	241	208
Derivative financial instruments	13	-	138
Property, plant and equipment	14	22,596	20,159
Deferred tax assets	15	3,329	1,426
Intangible assets	16	312,529	309,816
Total non-current assets		<u>342,608</u>	<u>335,569</u>
Total assets		<u>361,660</u>	<u>350,843</u>
LIABILITIES			
Current liabilities			
Trade and other payables	17	15,450	13,299
Deferred revenue		3,973	3,338
Borrowings	18	14,240	18,383
Provisions	21	1,561	1,090
Current tax liabilities		<u>5,320</u>	<u>6,922</u>
Total current liabilities		<u>40,544</u>	<u>43,032</u>
Non-current liabilities			
Borrowings	19	89,267	99,204
Derivative financial liabilities	13	3,217	2,387
Provisions	21	3,641	2,911
Total non-current liabilities		<u>96,125</u>	<u>104,502</u>
Total liabilities		<u>136,669</u>	<u>147,534</u>
Net assets		<u>224,991</u>	<u>203,309</u>
EQUITY			
Contributed equity	22	184,815	183,309
Reserves	23(a)	3,259	2,743
Retained earnings	23(b)	36,917	17,257
Total equity		<u>224,991</u>	<u>203,309</u>

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

Virtus Health Pty Limited
Consolidated statement of changes in equity
For the year ended 30 June 2012

		Attributable to owners of the parent			
		Share Based		Retained earnings \$'000	Total equity \$'000
Notes		Contributed equity \$'000	Payments Reserve \$'000		
		170,360	2,287	1,920	174,567
Balance at 1 July 2010		-	-	15,337	15,337
Profit for the year		-	-	-	-
Other comprehensive income		-	-	15,337	15,337
Total comprehensive income		-	-	-	-
Transactions with owners in their capacity as owners:					
Equity issued for acquisition consideration	22,29	12,458	-	-	12,458
Subscription for new shares	22	459	-	-	459
Issued to employees	22,23	32	(169)	-	(137)
Employee share options - value of employee services	6,34	-	625	-	625
		12,949	456	-	13,405
Balance at 30 June 2011		183,309	2,743	17,257	203,309
		-	-	19,660	19,660
Profit for the year		-	-	-	-
Other comprehensive income		-	-	19,660	19,660
Total comprehensive income		-	-	-	-
Transactions with owners in their capacity as owners:					
Equity issued for acquisition consideration	22,29	1,506	-	-	1,506
Employee share options - value of employee services	6,34	-	516	-	516
		1,506	516	-	2,022
Balance at 30 June 2012		184,815	3,259	36,917	224,991

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

Virtus Health Pty Limited
Consolidated statement of cash flows
For the year ended 30 June 2012

Notes	2012 \$'000	2011 \$'000
Cash flows from operating activities		
Receipts from customers (inclusive of goods and services tax)	164,125	119,509
Payments to suppliers and employees (inclusive of goods and services tax)	(112,370)	(84,204)
Other revenue	369	242
Finance costs paid	(12,813)	(12,611)
Income taxes paid	(10,200)	(167)
Net cash inflow from operating activities	33 <u>29,111</u>	<u>22,769</u>
Cash flows from investing activities		
Payment for acquisition of subsidiary and businesses, net of cash acquired	(4,035)	(14,406)
Payments for property, plant, equipment and intangibles	(8,521)	(8,165)
Payments for acquisition of associates	(91)	(1,397)
Associate distributions received	642	900
Proceeds on sale of property, plant & equipment	-	510
Interest received	433	466
Net cash outflow from investing activities	<u>(11,572)</u>	<u>(22,092)</u>
Cash flows from financing activities		
Proceeds from issues of shares and other equity securities	-	201
Payment for shares bought back	-	(169)
Proceeds from borrowings	-	18,807
Repayment of borrowings	(14,481)	(20,606)
Payment for finance lease facility	(582)	(728)
Net cash outflow from financing activities	<u>(15,063)</u>	<u>(2,495)</u>
Net increase / (decrease) in cash and cash equivalents	2,476	(1,818)
Cash and cash equivalents at the beginning of the financial year	<u>6,963</u>	<u>8,781</u>
Cash and cash equivalents at end of year	8 <u>9,439</u>	<u>6,963</u>

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

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1 Summary of significant accounting policies

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below. Unless otherwise stated, the accounting policies adopted are consistent with those of the previous year. Comparative information is reclassified where appropriate to enhance comparability. The financial statements are for the consolidated entity consisting of Virtus Health Pty Limited and its subsidiaries.

(a) Basis of preparation

These general purpose financial statements have been prepared in accordance with Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board and the *Corporations Act 2001*. Virtus Health Pty Limited is a for-profit entity for the purpose of preparing financial statements.

(i) Compliance with IFRS

The consolidated financial statements of the Virtus Health Pty Limited group also comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

(ii) New and amended standards adopted by the Group

None of the new standards and amendments to standards that are mandatory for the first time for the financial year beginning 1 July 2011 affected any of the amounts recognised in the current period or any prior period and are not likely to affect future periods.

(iii) Historical cost convention

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, financial assets and liabilities (including derivative instruments) at fair value through profit or loss, certain classes of property, plant and equipment and investment property.

(iv) Critical accounting estimates

The preparation of financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 3.

(v) Going Concern

At 30 June 2012 the consolidated entity had a current net asset deficiency of \$21.492 million (2011: \$27.758 million) arising primarily from its deferred revenue receipts of \$3.973 million (2011: \$3.338 million) and short term borrowings of \$14.240 million (2011: \$18.383 million). These deficiencies are a normal feature of the consolidated entity's activities and the deferred revenue is normally recognised within six weeks of receipt.

Having reviewed and considered the expected cash flows and the working capital, capital expenditure and loan facilities available to the consolidated entity which were renegotiated and increased in August 2012 (see note 19 and 32), the directors and management have formed the view that the consolidated entity will continue as a going concern for a period of at least 12 months from the date of this report and consequently will realise its assets and extinguish its liabilities in the normal course of business and at the amounts stated in the financial report.

The financial report for the Consolidated Entity has therefore been prepared on a going concern basis.

(b) Principles of consolidation

(i) Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of Virtus Health Pty Limited ("company" or "parent entity") as at 30 June 2012 and the results of all subsidiaries for the year then ended. Virtus Health Pty Limited and its subsidiaries together are referred to in these financial statements as the group or the consolidated entity.

Subsidiaries are all entities (including special purpose entities) over which the group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the group controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are de-consolidated from the date that control ceases.

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

(ii) Associates

The interest in an associate is accounted for in the consolidated financial statements using the equity method. Under the equity method, the share of the profits or losses of the associate is recognised in the statement of comprehensive income, and the share of movements in reserves is recognised in reserves in the balance sheet. Details relating to the associates are set out in note 31.

Profits or losses on transactions establishing the associates and transactions with the associates are eliminated to the extent of the Group's ownership interest until such time as they are realised by the associates on consumption or sale, unless they relate to an unrealised loss that provides evidence of the impairment of an asset transferred.

(c) Revenue recognition

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

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

Revenue is recognised for the major business activities as follows:

(i) Rendering of services

Revenue from the rendering of services is recognised upon the delivery of the service to a patient or customer. Revenue is recognised on completion of a medical procedure, on supply of drugs, or on completion of an analytical test. If payments received from patients exceed the revenue recognised the difference is disclosed as deferred revenue.

(ii) Lease income

Lease income from property sub-leases is recognised as income on a straight-line basis over the lease term.

(iii) Interest income

Interest income is recognised on a time apportioned basis using the effective interest method.

(iv) Deferred revenue

Fees for fertility treatment cycles paid in advance are recognised as deferred revenue until the service has been provided whereupon the fees are recognised as revenue

(d) Sponsorship

Sponsorship grants relating to costs are deferred and recognised in the statement of comprehensive income over the period necessary to match them with the costs that they are intended to compensate.

(e) Income tax

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

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

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

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

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

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

(f) Leases

Leases of property, plant and equipment where the group, as lessee, has substantially all the risks and rewards of ownership are classified as finance leases (note 27). Finance leases are capitalised at the lease's inception at the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding rental obligations, net of finance charges, are included in other short-term and long-term payables. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to the profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases is depreciated over the asset's useful life or over the shorter of the asset's useful life and the lease term if there is no reasonable certainty that the group will obtain ownership at the end of the lease term.

Leases in which a significant portion of the risks and rewards of ownership are not transferred to the group as lessee are classified as operating leases (note 27). Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease.

(g) Business combinations

The purchase price method of accounting is used to account for all business combinations, except for business combinations involving entities or businesses under common control, regardless of whether equity instruments or other assets are acquired. Cost is measured as the fair value of the assets given, equity instruments issued or liabilities incurred or assumed at the date of exchange. Costs directly attributable to the acquisition are expensed. Where equity instruments are issued in an acquisition, the fair value of the instruments is their published market price are expensed as at the date of exchange unless, in rare circumstances, it can be demonstrated that the published price at the date of exchange is an unreliable indicator of fair value and that other evidence and valuation methods provide a more reliable measure of fair value. Transaction costs arising on the issue of equity instruments are recognised as a deduction, net of tax, from the proceeds.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill (refer to note 1(o)). If the cost of acquisition is less than the Group's share of the fair value of the identifiable net assets of the subsidiary acquired, the difference is recognised directly in the statement of comprehensive income, but only after a reassessment of the identification and measurement of the net assets acquired.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

(h) Impairment of assets

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units).

Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

(i) Cash and cash equivalents

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

(j) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Trade receivables are generally due for settlement within 30 days. They are presented as current assets unless collection is not expected for more than 12 months after the reporting date.

Collectability of trade receivables is reviewed on an ongoing basis. Debts which are known to be uncollectible are written off by reducing the carrying amount directly. An allowance account (provision for impairment of trade receivables) is used when there is objective evidence that the group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired. The amount of the impairment allowance is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. Cash flows relating to short-term receivables are not discounted if the effect of discounting is immaterial.

The amount of the impairment loss is recognised in profit or loss within other expenses. When a trade receivable for which an impairment allowance had been recognised becomes uncollectible in a subsequent period, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against other expenses in profit or loss.

(k) Inventories

Inventory comprises medical supplies used in the fertility procedures performed in the Group's fertility clinics. Inventories are valued at the lower of cost and net realisable value.

(l) Investments and other financial assets

Classification

The group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and, in the case of assets classified as held-to-maturity, re-evaluates this designation at the end of each reporting period.

Recognition and derecognition

Purchases and sales of financial assets are recognised on trade-date - the date on which the group commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the group has transferred substantially all the risks and rewards of ownership.

When securities classified as available-for-sale are sold, the accumulated fair value adjustments recognised in other comprehensive income are reclassified to profit or loss as gains and losses from investment securities.

Impairment

The Group assesses at each balance date whether there is objective evidence that a financial asset or group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of a security below its cost is considered as an indicator that the securities are impaired.

If any such evidence exists for available-for-sale financial assets, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss - is removed from equity and recognised in the statement of comprehensive income. Impairment losses recognised in the statement of comprehensive income on equity instruments classified as available-for-sale are not reversed through the statement of comprehensive income.

(m) Derivatives and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The group designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges)
- hedges of the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges).

The Group has decided not to adopt hedge accounting. Changes in the fair value of any fair value financial instrument are recognised immediately in the statement of comprehensive income and are included in finance costs.

(n) Property, plant and equipment

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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

Depreciation on assets is calculated using the straight line method to allocate their cost amounts, net of their residual values, over their estimated useful lives, as follows:

- Leasehold improvements	Over the life of the lease or useful life if shorter
- Medical equipment	2 to 10 years
- Office equipment	2 to 5 years
- Furniture, fittings	2 to 5 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

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

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

(o) Intangible assets

(i) Goodwill

Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of associates is included in investments in associates. Goodwill is not amortised but it is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. Each of those cash-generating units represents the Group's investment in each primary reporting segment.

(ii) IT development and software

Costs incurred in developing products or systems and costs incurred in acquiring software and licenses that will contribute to future period financial benefits through revenue generation and/or cost reduction are capitalised to software and systems. Costs capitalised include external direct costs of materials and service, direct payroll and payroll related costs of employees' time spent on the project. Amortisation is calculated on a straight-line basis over periods generally ranging from 1 to 5 years.

IT development costs include only those costs directly attributable to the development phases and are only recognised following completion of technical feasibility and where the Group has an intention and ability to use the asset.

(p) Trade and other payables

These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid. The amounts are unsecured and are usually paid within agreed credit terms.

(q) Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method. Fees paid on the establishment of loan facilities, which are not an incremental cost relating to the actual draw-down of the facility, are recognised as prepayments and amortised on a straight-line basis over the term of the facility.

Borrowings are removed from the balance sheet when the obligation specified in the contract is discharged, cancelled or expired. The difference between the carrying amount of a financial liability that has been extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in other income or other expenses. Any unamortised transaction costs relating to the extinguished obligation are taken to the statement of comprehensive income upon extinguishment of the obligation.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

(r) Provisions

Provisions for legal claims and make good obligations are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

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

(s) Employee benefits

(i) Short-term obligations

Liabilities for wages and salaries, including non-monetary benefits, annual leave and accumulating sick leave expected to be settled within 12 months after the end of each reporting period in which the employees render the related service are recognised in respect of employees' services up to the end of the reporting period and are measured at the amounts expected to be paid when the liabilities are settled.

(ii) Other long-term employee benefit obligations

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

(iii) Share-based payments

Share-based compensation benefits are provided to employees via the Virtus Health Pty Limited Share Option Plan and other closed share option schemes. Information relating to these schemes is set out in note 34.

The fair value of options granted under the plans is recognised as an employee benefit expense with a corresponding increase in equity. The fair value is measured at grant date and recognised over the period during which the employees become unconditionally entitled to the options.

The fair value at grant date is independently determined using a Binomial option pricing model that takes into account the exercise price, the term of the option, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk free interest rate for the term of the option.

The fair value of the options granted excludes the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each reporting date, the entity revises its estimate of the number of options that are expected to become exercisable. The employee benefit expense recognised each period takes into account the most recent estimate. The impact of the revision to original estimates, if any, is recognised in the statement of comprehensive income with a corresponding adjustment to equity.

(iv) Profit-sharing and bonus plans

The group recognises a liability and an expense for bonuses and profit-sharing based on a formula that takes into consideration the profit attributable to the company's shareholders after certain adjustments. The group recognises a

provision where contractually obliged or where there is a past practice that has created a constructive obligation.

(v) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The group recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal or to providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

(t) Contributed equity

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds. Incremental costs directly attributable to the issue of new shares or options for the acquisition of a business are not included in the cost of the acquisition as part of the purchase consideration.

If the entity reacquires its own equity instruments, for example as the result of a share buy-back, those instruments are deducted from equity and the associated shares are cancelled. No gain or loss is recognised in the profit or loss and the consideration paid including any directly attributable incremental costs (net of income taxes) is recognised directly in equity.

(u) Dividends

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

(v) Goods and Services Tax (GST)

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

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

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

(w) Tax consolidation legislation

Virtus Health Pty Limited and its wholly-owned subsidiaries have formed a tax consolidated group and are therefore taxed as a single entity. The head entity within the tax consolidated group is Virtus Health Pty Limited.

The head entity, Virtus Health Pty Limited, and the controlled entities in the tax consolidated group account for their own current and deferred tax amounts. These tax amounts are measured as if each entity in the tax consolidated group continues to be a stand-alone taxpayer in its own right. In addition to its own current and deferred tax amounts, Virtus Health Pty Limited also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group.

The wholly owned entities fully compensate Virtus Health Pty Limited for any current tax payable assumed and are compensated by Virtus Health Pty Limited for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to Virtus Health Pty Limited under the tax consolidation legislation. These amounts are determined by reference to the amounts recognised in the wholly owned entities' financial statements.

The tax amounts receivable/payable are due upon request from the head entity, which is issued as soon as practicable after the end of each financial year. The head entity may also require payment of interim funding amounts to assist with its obligations to pay tax instalments.

Assets or liabilities arising with tax consolidated entities are recognised as current amounts receivable from or payable to other entities in the group. Any difference between the amounts assumed and amounts receivable or payable are recognised as a contribution to (or distribution from) wholly owned tax consolidated entities.

(x) Rounding of amounts

The company is of a kind referred to in Class Order 98/100, issued by the Australian Securities and Investments Commission, relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded off in accordance with that Class Order to the nearest thousand dollars, or in certain cases, the nearest dollar.

(y) **New accounting standards and interpretations**

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2012 reporting periods. The group's assessment of the impact of these new standards and interpretations is set out below.

- (i) *AASB 9 Financial Instruments, AASB 2009-11 Amendments to Australian Accounting Standards arising from AASB 9 and AASB 2010-7 Amendments to Australian Accounting Standards arising from AASB 9 (December 2010)* (effective from 1 January 2013)

AASB 9 *Financial Instruments* addresses the classification, measurement and derecognition of financial assets and is likely to affect the group's accounting for its financial assets and financial liabilities. The standard is not applicable until 1 January 2013 but is available for early adoption. When adopted, the standard will affect in particular the group's accounting for its available-for-sale financial assets, since AASB 9 only permits the recognition of fair value gains and losses in other comprehensive income if they relate to equity investments that are not held for trading. Fair value gains and losses on available-for-sale debt investments, for example, will therefore have to be recognised directly in profit or loss.

There will be no impact on the group's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the group does not have any such liabilities. The derecognition rules have been transferred from AASB 139 *Financial Instruments: Recognition and Measurement* and have not been changed. The group will adopt AASB 9 in financial year ending 30 June 2014.

- (ii) *AASB 10 Consolidated Financial Statements, AASB 11 Joint Arrangements, AASB 12 Disclosure of Interests in Other Entities, revised AASB 127 Separate Financial Statements and AASB 128 Investments in Associates and Joint Ventures and AASB 2011-7 Amendments to Australian Accounting Standards arising from the Consolidation and Joint Arrangements Standards* (effective 1 January 2013)

In August 2011, the AASB issued a suite of five new and amended standards which address the accounting for joint arrangements, consolidated financial statements and associated disclosures.

AASB 10 replaces all of the guidance on control and consolidation in AASB 127 *Consolidated and Separate Financial Statements*, and Interpretation 12 *Consolidation – Special Purpose Entities*. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single economic entity remains unchanged, as do the mechanics of consolidation. However the standard introduces a single definition of control that applies to all entities. It focuses on the need to have both power and rights or exposure to variable returns before control is present. Power is the current ability to direct the activities that significantly influence returns. Returns must vary and can be positive, negative or both. There is also new guidance on participating and protective rights and on agent/principal relationships. While the group does not expect the new standard to have a significant impact on its composition, it has yet to perform a detailed analysis of the new guidance in the context of its various investees that may or may not be controlled under the new rules.

AASB 12 sets out the required disclosures for entities reporting under the two new standards, AASB 10 and AASB 11, and replaces the disclosure requirements currently found in AASB 128. Application of this standard by the group will not affect any of the amounts recognised in the financial statements, but will impact the type of information disclosed in relation to the group's investments.

AASB 127 is renamed *Separate Financial Statements* and is now a standard dealing solely with separate financial statements. Application of this standard by the group and parent entity will not affect any of the amounts recognised in the financial statements, but may impact the type of information disclosed in relation to the parent's investments in the separate parent entity financial statements.

The group does not expect to adopt the new standards before their operative date. They would therefore be first applied in the financial statements for the annual reporting period ending 30 June 2014.

- (iii) *AASB 13 Fair Value Measurement and AASB 2011-8 Amendments to Australian Accounting Standards arising from AASB 13* (effective 1 January 2013)

AASB 13 was released in September 2011. It explains how to measure fair value and aims to enhance fair value disclosures. The group does not use fair value measurements extensively. It is therefore unlikely that the new rules will have a significant impact on any of the amounts recognised in the financial statements. However, application of the new standard will impact the type of information disclosed in the notes to the financial statements. The group does not intend to adopt the new standard before its operative date, which means that it would be first applied in the annual reporting period ending 30 June 2014.

- (iv) *AASB 2011-9 Amendments to Australian Accounting Standards – Presentation of Items of Other Comprehensive Income* (effective 1 July 2012)

In September 2011, the AASB made an amendment to AASB 101 *Presentation of Financial Statements* which requires entities to separate items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future. This will not affect the measurement of any of the items recognised in the balance sheet or the profit or loss in the current period. The group intends to adopt the new standard from 1 July 2012.

(v) AASB 2012-3 *Amendments to Australian Accounting Standard - Offsetting Financial Assets and Financial Liabilities* and AASB 2012-2 *Disclosures - Offsetting Financial Assets and Financial Liabilities* (effective 1 January 2014 and 1 January 2013 respectively)

In June 2012, the AASB approved amendments to the application guidance in AASB 132 *Financial Instruments: Presentation*, to clarify some of the requirements for offsetting financial assets and financial liabilities in the balance sheet. These amendments are effective from 1 January 2014. They are unlikely to affect the accounting for any of the entity's current offsetting arrangements. However, the AASB has also introduced more extensive disclosure requirements into AASB 7 which will apply from 1 January 2013. When they become applicable, the group will have to provide a number of additional disclosures in relation to its offsetting arrangements. The group intends to apply the new rules for the first time in the financial year commencing 1 July 2013

(z) Parent entity financial information

The financial information for the parent entity, Virtus Health Pty Limited, disclosed in note 35 has been prepared on the same basis as the consolidated financial statements, except as set out below.

(i) Investments in subsidiaries, associates and joint venture entities

Investments in subsidiaries, associates and joint venture entities are accounted for at cost in the financial statements of Virtus Health Pty Limited. Dividends received from associates are recognised in the parent entity's profit or loss, rather than being deducted from the carrying amount of these investments.

(ii) Tax consolidation legislation

Virtus Health Pty Limited and its wholly owned Australian controlled entities have implemented the tax consolidation legislation.

The head entity, Virtus Health Pty Limited, and the controlled entities in the tax consolidated group account for their own current and deferred tax amounts. These tax amounts are measured as if each entity in the tax consolidated group continues to be a stand-alone taxpayer in its own right.

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

The wholly owned entities fully compensate Virtus Health Pty Limited for any current tax payable assumed and are compensated by Virtus Health Pty Limited for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to Virtus Health Pty Limited under the tax consolidation legislation. These amounts are determined by reference to the amounts recognised in the wholly owned entities' financial statements.

The tax amounts receivable/payable are due upon request from the head entity, which is issued as soon as practicable after the end of each financial year. The head entity may also require payment of interim funding amounts to assist with its obligations to pay tax instalments.

Assets or liabilities arising with tax consolidated entities are recognised as current amounts receivable from or payable to other entities in the group.

Any difference between the amounts assumed and amounts receivable or payable are recognised as a contribution to (or distribution from) wholly owned tax consolidated entities.

(iii) Financial guarantees

Where the parent entity has provided financial guarantees in relation to loans and payables of subsidiaries for no compensation, the fair values of these guarantees are accounted for as contributions and recognised as part of the cost of the investment.

(iv) Share-based payments

The grant by the company of options over its equity instruments to the employees of subsidiary undertakings in the group is treated as a capital contribution to that subsidiary undertaking. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the vesting period as an increase to investment in subsidiary undertakings, with a corresponding credit to equity.

2 Financial risk management

The group's activities expose it to a variety of financial risks: market risk (including currency risk, interest rate risk and price risk), credit risk and liquidity risk. The group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the group. The group uses derivative financial instruments such as interest rate swaps to hedge certain risk exposures. Derivatives are exclusively used for hedging purposes, i.e. not as trading or other speculative instruments. The group uses different methods to measure different types of risk to which it is exposed. These methods include sensitivity analysis in the case of interest rate, foreign exchange and other price risks, aging analysis for credit risk.

The group's management of financial risk is aimed at ensuring net cash flows are sufficient to:

- Meet all its financial commitments as and when they fall due; and
- Maintain the capacity to fund acquisitions and technological upgrades

The group holds the following financial instruments:

	2012 \$'000	2011 \$'000
Financial assets		
Cash and cash equivalents	9,439	6,963
Trade and other receivables	8,475	7,230
Other financial assets	241	208
Derivative financial instruments	-	138
Investments	3,913	3,822
Total financial assets	<u>22,068</u>	<u>18,361</u>
Financial liabilities		
Trade and other payable	15,450	13,299
Deferred revenue	3,973	3,338
Borrowings/Interest bearing liabilities	103,507	117,587
Derivative financial instruments	3,217	2,387
Total financial liabilities	<u>126,147</u>	<u>136,611</u>

(a) Market risk

(i) Cash flow and fair value interest rate risk

The group's main interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the group to cash flow interest rate risk. Borrowings issued at fixed rates expose the group to fair value interest rate risk if the borrowings are carried at fair value. Group policy is to maintain approximately 75% of its borrowings at fixed rate using interest rate swaps to achieve this when necessary.

As at the end of each reporting period, the group had the following variable rate borrowings and interest rate swap contracts outstanding:

	30 June 2012		30 June 2011	
	Weighted average interest rate %	Balance \$'000	Weighted average interest rate %	Balance \$'000
Bank overdrafts and bank loans	8.10 %	102,943	8.14 %	116,574
Interest rate cap	7.86 %	(6,435)	7.86 %	(31,098)
Interest rate swaps (notional principal amount)	6.36 %	(60,183)	6.31 %	(62,153)
Net exposure to cash flow interest rate risk		<u>36,325</u>		<u>23,323</u>

The group manages its cash flow interest rate risk by using floating-to-fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates. Generally, the group raises long-term borrowings at floating rates and swaps them into fixed rates that are lower than those available if the group borrowed at fixed rates directly. Under the interest rate swaps, the group agrees with other parties to exchange, at specified intervals (mainly quarterly), the difference between fixed contract rates and floating rate interest amounts calculated by reference to the agreed notional principal amounts. The interest rate caps limit the maximum interest rate on a nominated amount of the facility.

Group Sensitivity

At 30 June 2012, if interest rates had changed by +/- 100 basis points from the year end rates with all other variables held constant, post-tax profit for the year would have been \$236,000 higher/lower (2011 – change of 100 bps: \$81,600 higher/lower), mainly as a result of lower/higher interest expense on bank loans.

(b) Credit risk

Credit risk is managed on a group basis. Credit risk arises from cash and cash equivalents, favourable derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to customers, including outstanding receivables and committed transactions. The group does not have any material exposure to any individual customer or counterparty, other than Medicare (Government body) and private health funds. There are no significant concentrations of credit risk within the group.

Receivable balances and ageing analysis are monitored on an ongoing basis. In order to minimise the group's exposure to bad debts, rigorously enforced processes are in place to send reminder notices, demands for repayment and ultimately to refer to debt collection agencies.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities and the availability of funding through an adequate amount of committed credit facilities to meet obligations when due and close out market positions. The group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

Financing arrangements

The group had access to the following undrawn borrowing facilities at the end of each reporting period:

	2012 \$'000	2011 \$'000
Floating rate		
- Expiring beyond one year (bank loans)	<u>5,461</u>	<u>8,444</u>
	<u>5,461</u>	<u>8,444</u>

The Group has total facilities of \$25 million in the form of a capital expenditure facility of \$20 million and a working capital facility of \$5 million. As at 30 June 2012, the drawdown on the capital expenditure facilities is \$18,031,514. Drawdowns of \$2,503,952 in the form of financial guarantees have been made against the working capital facility. Subject to the continued compliance with debt covenants, the bank facilities may be drawn at any time and have an average maturity of 2 years (2011: 3 years)

Maturities of financial liabilities

The tables below analyse the Group's financial liabilities, net and gross settled derivative financial instruments into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

For interest rate swaps the cash flows have been estimated using forward interest rates applicable at the end of each reporting period.

Virtus Health Pty Limited
Notes to the consolidated financial statements
30 June 2012
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Contractual maturities of financial liabilities	Less than 6 months	6 - 12 months	Between 1 and 2 years	Between 2 and 5 years	Over 5 years	Total contractual cash flows	Carrying Amount (assets)/ liabilities
At 30 June 2012	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Trade and other payables	15,450	-	-	-	-	15,450	15,450
Deferred revenue	3,973	-	-	-	-	3,973	3,973
Bank loans	11,250	11,070	104,354	-	-	126,674	102,943
Lease liabilities	142	115	166	216	-	639	564
Derivative financial instruments	-	-	3,217	-	-	3,217	3,217
Financial liabilities	30,815	11,185	107,737	216	-	149,953	126,147
At 30 June 2011							
Trade and other payables	13,299	-	-	-	-	13,299	13,299
Deferred revenue	3,338	-	-	-	-	3,338	3,338
Bank loans	11,541	11,256	21,657	104,411	-	148,865	116,574
Lease liabilities	319	197	285	350	4	1,156	1,013
Derivative financial instruments	-	-	-	2,387	-	2,387	2,387
Financial liabilities	28,497	11,453	21,942	107,148	4	169,045	136,611

(d) Fair value estimation

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes. Derivative contracts classified as held for trading are fair valued by comparing the contracted rate to the current market rate for a contract with the same remaining period to maturity.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives and investments in unlisted subsidiaries) is determined using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance date. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values due to their short term nature. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

As of 1 July 2010, Virtus Health Pty Limited adopted the amendment to AASB 7 Financial Instruments: This requires disclosure of fair value measurements by level of the following fair value measurement hierarchy:

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

The following tables present the group's assets and liabilities measured and recognised at fair value at 30 June 2012 and 30 June 2011.

At 30 June 2012	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Assets				
Derivatives financial instruments	-	-	-	-
Total assets	-	-	-	-
Liabilities				
Derivatives financial liabilities	-	3,217	-	3,217
Total liabilities	-	3,217	-	3,217

At 30 June 2011	Level 1	Level 2	Level 3	Total
	\$'000	\$'000	\$'000	\$'000
Assets				
Derivatives financial instruments	-	138	-	138
	-	138	-	138
Total assets				
Liabilities				
Other financial liability	-	-	-	-
Derivatives financial liabilities	-	2,387	-	2,387
Total liabilities	-	2,387	-	2,387

The fair value of financial instruments traded in active markets (such as publicly traded derivatives, and trading and available-for-sale securities) is based on quoted market prices at the end of the reporting period. These instruments are included in level 1.

The fair value of financial instruments that are not traded in an active market (for example over-the-counter derivatives) is determined using valuation techniques. The group uses a variety of methods and makes assumptions that are based on market conditions existing at the end of each reporting period. Quoted market prices or dealer quotes for similar instruments are used to estimate fair value for long term debt for disclosure purposes. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward exchange contracts is determined using forward exchange market rates at the end of the reporting period. These instruments are included in level 2 and comprise debt instruments and derivative financial instruments. In the circumstances where a valuation technique for these instruments is based on significant unobservable inputs, such instruments are included in level 3.

3 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.

(a) Critical accounting estimates and assumptions

The group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom 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) Impairment of goodwill

The group tests annually whether goodwill has suffered any impairment, in accordance with the accounting policy stated in note 1(h). The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of assumptions. Refer to note 16 for details of these assumptions and the potential impact of changes to the assumptions.

(ii) Share based payment transactions

The group measures the cost of equity settled transactions with employees by reference to the fair value of equity instruments at the date they were granted. The fair value is determined by an external valuer using a binominal pricing model, taking into account the terms and conditions upon which the options were granted, as discussed in Note 34.

(iii) Provisional accounting of business combinations

The group provisionally accounts for certain business combinations where it is in the process of ascertaining the fair value of identifiable assets, liabilities and contingent liabilities acquired. In doing so, the group relied on the best estimate of the identifiable assets, liabilities and contingent liabilities, as disclosed in Note 29, until the quantification and treatment of items under review is complete.

4 Revenue

	2012 \$'000	2011 \$'000
From continuing operations		
Rendering of services	163,476	130,845
Rents and sub-lease rentals	1,210	586
Interest	433	466
	<u>165,119</u>	<u>131,897</u>

5 Other income

	2012 \$'000	2011 \$'000
Trial grants	187	125
Other revenue	182	692
	<u>369</u>	<u>817</u>

6 Expenses

	2012 \$'000	2011 \$'000
Profit before income tax includes the following specific expenses:		
<i>Depreciation</i>	2,983	2,319
Leasehold improvements	346	617
Plant and equipment under finance leases	1,627	1,103
Medical equipment	503	393
Office equipment	167	63
Furniture and fittings	<u>5,626</u>	<u>4,495</u>
Total depreciation		
<i>Amortisation</i>	910	878
Brand names	2,436	2,904
IT Development and software	<u>3,346</u>	<u>3,782</u>
Total amortisation	<u>8,972</u>	<u>8,277</u>
Total depreciation and amortisation expense		
<i>Finance expenses</i>	11,845	12,621
Interest expenses	968	(870)
Revaluation of interest rate swaps (net)	850	694
Amortisation of bank facility fees	133	166
Finance charge payable under finance leases	<u>13,796</u>	<u>12,611</u>
Total Finance costs		
<i>Total rental expense relating to operating leases</i>	6,841	5,555
<i>Share based payment expense</i>	516	625
<i>Inventory expense</i>	2,052	1,796
<i>Superannuation contributions</i>	3,159	2,594
<i>Research and development</i>	2,806	3,118

7 Income tax expense

	2012 \$'000	2011 \$'000
(a) Income tax expense:		
Current tax	9,318	6,514
Deferred tax	(1,430)	(656)
Adjustments to current tax in relation to prior periods	(1,175)	(1,573)
	<u>6,713</u>	<u>4,285</u>
Deferred income tax (revenue) expense included in income tax expense comprises:		
Decrease (increase) in deferred tax assets (note 15)	(1,657)	(361)
(Decrease) increase in deferred tax liabilities (note 20)	227	(295)
	<u>(1,430)</u>	<u>(656)</u>
(b) Numerical reconciliation of income tax expense to prima facie tax payable		
Profit from continuing operations before income tax expense	<u>26,373</u>	<u>19,622</u>
Tax at the Australian tax rate of 30% (2011 – 30%)	7,912	5,887
Tax effect of amounts which are not deductible (taxable) in calculating taxable income:		
Entertainment	11	22
Share-based payments	134	188
Research and development	(169)	(239)
	<u>7,888</u>	<u>5,858</u>
Adjustments for current tax of prior years	(1,175)	(1,573)
Income tax expense	<u>6,713</u>	<u>4,285</u>

8 Current assets - Cash and cash equivalents

	2012 \$'000	2011 \$'000
Cash at bank and in hand	<u>9,439</u>	<u>6,963</u>
	<u>9,439</u>	<u>6,963</u>

(a) Reconciliation to cash at the end of the year

The above figures are reconciled to cash at the end of the financial year as shown in the consolidated statement of cash flows as follows:

	2012 \$'000	2011 \$'000
Balances as above	9,439	6,963
Balances per consolidated statement of cash flows	<u>9,439</u>	<u>6,963</u>

(a) Risk exposure

The group's exposure to interest rate risk is discussed in note 2. The maximum exposure to credit risk at the end of each reporting period is the carrying amount of each class of cash and cash equivalents mentioned above.

9 Current assets - Trade and other receivables

	2012 \$'000	2011 \$'000
Trade receivables	6,798	5,715
Provision for impairment of receivables (a)	<u>(752)</u>	<u>(771)</u>
	6,046	4,944
Other receivables	2,429	2,286
Prepayments	<u>1,138</u>	<u>961</u>
	9,613	8,191

(a) Impaired trade receivables

As at 30 June 2012 current trade receivables of the group with a nominal value of \$900,000 (30 June 2011 - \$1,112,000) were impaired. The amount of the provision was \$752,000 (30 June 2011 - \$771,000).

The ageing of these receivables is as follows:

	2012 \$'000	2011 \$'000
1 to 3 months	-	40
3 to 6 months	504	897
Over 6 months	<u>396</u>	<u>175</u>
	900	1,112

Movements in the provision for impairment of receivables are as follows:

	2012 \$'000	2011 \$'000
At 1 July	771	339
Provision for impairment recognised during the year	445	735
Receivables written off during the year as uncollectible	<u>(464)</u>	<u>(303)</u>
	752	771

The creation and release of the provision for impaired receivables has been included in 'other expenses' in profit or loss. Amounts charged to the allowance account are generally written off when there is no expectation of recovering additional cash.

(b) Past due but not impaired

Receivables that are past due but not impaired are as follows:

	2012 \$'000	2011 \$'000
1 to 3 months	<u>2,411</u>	<u>814</u>
	2,411	814

10 Current assets - Inventories

	2012 \$'000	2011 \$'000
Finished goods – at cost	-	120
	-	<u>120</u>

11 Non-current assets – investments accounted for using the equity method

	2012 \$'000	2011 \$'000
Interest in associates (note 31)	<u>3,913</u>	<u>3,822</u>
	<u>3,913</u>	<u>3,822</u>

12 Non-current assets – other financial assets

	2012 \$'000	2011 \$'000
Security deposits	<u>241</u>	<u>208</u>
	<u>241</u>	<u>208</u>

13 Derivative financial instruments

	2012 \$'000	2011 \$'000
Non-current assets		
Interest rate swap contracts - cash flow hedges ((a)(i))	<u>-</u>	<u>138</u>
Total non-current derivative financial instrument assets	<u>-</u>	<u>138</u>
Non-Current liabilities		
Interest rate swap and cap contracts – cash flow hedges ((a)(i))	<u>(3,217)</u>	<u>(2,387)</u>
Total non-current derivative financial instrument liabilities	<u>(3,217)</u>	<u>(2,387)</u>

(a) Instruments used by the group

The group is party to derivative financial instruments in the normal course of business in order to hedge exposure to fluctuations in interest and foreign exchange rates in accordance with the group's financial risk management policies (refer to note 2).

(i) Interest rate swap contracts - cash flow hedges

Bank loans of the group currently bear an average variable interest rate of 8.10% (2011: 8.14%). It is policy to protect part of the loans from exposure to increasing interest rates. Accordingly, the Group has entered into interest rate swap contracts under which it is obliged to receive interest at variable rates and to pay interest at fixed rates and an interest rate cap which limits the maximum interest rate payable on a loan to a pre-determined interest rate.

Interest rate swaps and the interest rate cap currently in place cover at least 75% (2011: 75%) of the loan principal outstanding and are timed to expire as each loan repayment falls due. The fixed interest rates range between 4.74% and 7.86% (2011: 4.74% - 7.86%) and the variable rates are set at the 90 day bank bill swap rate updated quarterly which at balance date was 3.49% (2011: 4.89%).

The contracts require settlement of net interest receivable or payable each 90 days. The settlement dates coincide with the dates on which interest is payable on the underlying debt. The contracts are settled on a net basis.

The gain or loss from remeasuring the hedging instruments is recognised in the statement of comprehensive income. In the year ended 30 June 2012 a net loss of \$967,778 was recognised in finance costs (2011: net profit of \$869,668).

(b) Risk exposures and fair value measurements

Information about the group's exposure to credit risk, foreign exchange and interest rate risk and about the methods and assumptions used in determining fair values is provided in note 2. The maximum exposure to credit risk at the end of each reporting period is the carrying amount of each class of derivative financial assets mentioned above.

14 Non-current assets - Property, plant and equipment

	Leasehold Improvements \$'000	Plant and Equipment \$'000	Medical equipment \$'000	Office Equipment \$'000	Furniture and Fittings \$'000	Total \$'000
At 30 June 2011						
Cost or fair value	19,387	1,990	7,949	1,662	401	31,389
Accumulated depreciation	(5,391)	(1,644)	(3,074)	(919)	(202)	(11,230)
Net book amount	<u>13,996</u>	<u>346</u>	<u>4,875</u>	<u>743</u>	<u>199</u>	<u>20,159</u>
Year ended 30 June 2011						
Opening net book amount	12,559	963	3,284	797	153	17,756
Acquisition of subsidiary	-	-	282	44	31	357
Additions	4,274	-	2,427	315	89	7,105
Disposals	(518)	-	(15)	(20)	(11)	(564)
Depreciation charge	(2,319)	(617)	(1,103)	(393)	(63)	(4,495)
Closing net book amount	<u>13,996</u>	<u>346</u>	<u>4,875</u>	<u>743</u>	<u>199</u>	<u>20,159</u>
At 30 June 2012						
Cost or fair value	21,621	1,990	12,295	2,373	1,173	39,452
Accumulated depreciation	(8,374)	(1,990)	(4,701)	(1,422)	(369)	(16,856)
Net book amount	<u>13,247</u>	<u>-</u>	<u>7,594</u>	<u>951</u>	<u>804</u>	<u>22,596</u>
Year ended 30 June 2012						
Opening net book amount	13,996	346	4,875	743	199	20,159
Acquisition of subsidiaries/ businesses	38	-	498	8	-	544
Additions	2,196	-	3,856	799	772	7,623
Disposals	-	-	(8)	(96)	-	(104)
Depreciation charge	(2,983)	(346)	(1,627)	(503)	(167)	(5,626)
Closing net book amount	<u>13,247</u>	<u>-</u>	<u>7,594</u>	<u>951</u>	<u>804</u>	<u>22,596</u>

15 Non-current assets - Deferred tax assets

	2012 \$'000	2011 \$'000
The balance comprises temporary differences attributable to:		
Employee benefits	1,837	1,457
Other	226	231
Doubtful debts	703	564
Make good provision	591	418
Accruals	965	675
Financial derivatives	1,517	818
Other	5,839	4,163
Total deferred tax assets	<u>13,247</u>	<u>13,247</u>
Set-off of deferred tax liabilities pursuant to set-off provisions (Note 20)	<u>(2,510)</u>	<u>(2,737)</u>
Net deferred tax assets	<u>10,737</u>	<u>10,510</u>
Deferred tax assets expected to be recovered within 12 months	817	648
Deferred tax assets expected to be recovered after more than 12 months	<u>5,022</u>	<u>3,515</u>
	<u>5,839</u>	<u>4,163</u>

Movements	Employee benefits \$'000	Other \$'000	Total \$'000
At 30 June 2010	1,197	2,571	3,768
Credited to the statement of comprehensive income	242	119	361
Acquisition of subsidiary	18	16	34
At 30 June 2011	1,457	2,706	4,163
Credited to the statement of comprehensive income	365	1,292	1,657
Acquisition of subsidiary	15	4	19
At 30 June 2012	1,837	4,002	5,839

16 Non-current assets - Intangible assets

	Brand Names \$'000	Goodwill \$'000	Software \$'000	Total \$'000
At 30 June 2011				
Cost	9,095	299,196	9,074	317,365
Accumulated amortisation and impairment	(2,226)	-	(5,323)	(7,549)
Net book amount	6,869	299,196	3,751	309,816
Year ended 30 June 2011				
Opening net book amount	7,257	289,445	5,373	302,075
Acquisition of subsidiary	490	9,751	-	10,241
Additions	-	-	1,282	1,282
Disposals	-	-	-	-
Amortisation charge	(878)	-	(2,904)	(3,782)
Closing net book amount	6,869	299,196	3,751	309,816
At 30 June 2012				
Cost	9,095	304,357	9,972	323,424
Accumulated amortisation and impairment	(3,136)	-	(7,759)	(10,895)
Net book amount	5,959	304,357	2,213	312,529
Year ended 30 June 2012				
Opening net book amount	6,869	299,196	3,751	309,816
Acquisition of subsidiaries/ businesses	-	5,161	-	5,161
Additions	-	-	898	898
Disposals	-	-	-	-
Amortisation charge	(910)	-	(2,436)	(3,346)
Closing net book amount	5,959	304,357	2,213	312,529

(a) Impairment tests for goodwill

Goodwill is allocated to the group's cash-generating units (CGUs) identified according to operating segment.

A segment-level summary of the goodwill allocation is presented below.

2012	New South Wales \$'000	Victoria \$'000	Queensland \$'000	Total \$'000
Goodwill	100,209	124,904	79,244	304,357
	100,209	124,904	79,244	304,357
2011	New South Wales \$'000	Victoria \$'000	Queensland \$'000	Total \$'000
Goodwill	100,209	124,904	74,083	299,196
	100,209	124,904	74,083	299,196

The recoverable amount of a CGU is determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated using the estimated growth rates stated below. The growth rate does not exceed the long-term average growth rate for the business.

(b) Key assumptions used for value-in-use calculations

CGU	Long Term Growth rate		Pre Tax Discount rate	
	2012 %	2011 %	2012 %	2011 %
New South Wales	3%	3%	16.0%	16.0%
Victoria	3%	3%	16.0%	14.9%
Queensland	3%	3%	16.0%	15.8%

These assumptions have been used for the analysis of each CGU within the business segment. The equity rates of return and therefore discount rates reflect specific risks relating to the relevant segments. In performing the value-in-use calculations for each CGU, the Group has applied post tax discount rates to discount the forecast future attributable post-tax cash flows. The equivalent pre-tax discount rates are disclosed above.

(c) Impact of possible changes in key assumptions

In considering the robustness of the valuation of goodwill, the long term growth rate was reduced to 2.5% and the recoverable amounts of the CGU's recalculated. In each CGU the recoverable amount of the goodwill exceeded the carrying value by material amounts. Management does not consider an adverse change in any of the other key assumptions to be reasonably possible.

17 Current liabilities - Trade and other payables

	2012 \$'000	2011 \$'000
Trade payables	5,765	4,499
Other payables	9,685	8,800
	<u>15,450</u>	<u>13,299</u>

18 Current liabilities - Borrowings

	2012 \$'000	2011 \$'000
Bank loans (note 19)	14,000	17,947
Lease liabilities (note 27)	240	436
Total current borrowings	<u>14,240</u>	<u>18,383</u>

(a) Security and fair value disclosures

Information about the security relating to each of the secured liabilities and the fair value of each of the borrowings is provided in note 19.

(b) Risk exposures

Details of the group's exposure to risks arising from current and non-current borrowings are set out in note 2.

19 Non-current liabilities - Borrowings

	2012 \$'000	2011 \$'000
Secured		
Bank loans	88,943	98,627
Lease liabilities (note 27)	<u>324</u>	<u>577</u>
Total secured non-current borrowings	<u>89,267</u>	<u>99,204</u>
 Secured liabilities and assets pledged as security		
The total secured liabilities (current and non-current) are as follows:		
Bank loans	102,943	116,574
Lease liabilities	<u>564</u>	<u>1,013</u>
Total secured liabilities	<u>103,507</u>	<u>117,587</u>

The bank loans are secured by guarantees by all group companies and fixed and floating charges over the Group's assets.

Lease liabilities are effectively secured as the rights to the leased assets recognised in the financial statements revert to the lessor in the event of default. The carrying amounts of assets pledged as security are:

	2012 \$'000	2011 \$'000
Current		
<i>Floating charge</i>		
Cash and cash equivalents	9,439	6,963
Receivables	9,613	8,191
Inventories	-	120
Other financial assets	<u>-</u>	<u>-</u>
Total assets pledged as security	<u>19,052</u>	<u>15,274</u>
 Non-current		
<i>Finance lease</i>		
Plant and equipment	<u>-</u>	<u>346</u>
<i>Floating charge</i>		
Investments	3,913	3,822
Other financial assets	241	208
Derivative financial instruments	-	138
Plant and equipment	22,596	19,813
Deferred tax assets	3,329	1,426
Intangible assets	<u>312,529</u>	<u>309,816</u>
Total non-current assets pledged as security	<u>342,608</u>	<u>335,569</u>
 Total assets pledged as security	<u>361,660</u>	<u>350,843</u>

The assets of Maroubra Day Surgery Pty Limited, City West Day Surgery Pty Limited and Obstetrics & Gynaecological Imaging Pty Limited are excluded from the assets pledged as security. However the shares representing the 50% interest are included in the charges over the Group.

Risk exposures

Information about the Group's exposure to interest rate changes is provided in note 2.

20 Non-current liabilities - Deferred tax liabilities

	2012 \$'000	2011 \$'000
The balance comprises temporary differences attributable to:		
Property, plant and equipment	722	675
Other		
	<u>1,788</u>	<u>2,062</u>
Intangible assets	<u>2,510</u>	<u>2,737</u>
Total deferred tax liabilities		
	<u>(2,510)</u>	<u>(2,737)</u>
Set-off of deferred tax liabilities pursuant to set-off provisions (note 15)	<u>-</u>	<u>-</u>
Net deferred tax liabilities		
	<u>(2,510)</u>	<u>(2,737)</u>
Deferred tax liabilities expected to be settled within 12 months	<u>(2,510)</u>	<u>(2,737)</u>
Deferred tax liabilities expected to be settled after more than 12 months	<u>(2,510)</u>	<u>(2,737)</u>

Movements

	Property, plant and equipment \$'000	Intangible Assets \$'000	Other \$'000	Total \$'000
At 30 June 2010	648	2,177	59	2,884
Charged/(credited)	27	(263)	(59)	(295)
Acquisition of subsidiary	<u>-</u>	<u>148</u>	<u>-</u>	<u>148</u>
At 30 June 2011	<u>675</u>	<u>2,062</u>	<u>-</u>	<u>2,737</u>
	<u>47</u>	<u>(274)</u>	<u>-</u>	<u>(227)</u>
Charged/(credited)	<u>722</u>	<u>1,788</u>	<u>-</u>	<u>2,510</u>
At 30 June 2012				

21 Liabilities - Provisions

	2012 \$'000	2011 \$'000
Current	<u>1,561</u>	<u>1,090</u>
Employee benefits - long service leave – (a) below		

(a) Amounts not expected to be settled within the next 12 months

The current provision for long service leave includes all unconditional entitlements where employees have completed the required period of service and also those where employees are entitled to pro-rata payments in certain circumstances. The entire amount is presented as current, since the Group does not have an unconditional right to defer settlement. However, based on past experience, the Group does not expect all employees to take the full amount of accrued long service leave or require payment within the next 12 months. The following amounts reflect leave that is not expected to be taken or paid within the next 12 months.

	2012	2011
	\$'000	\$'000
Leave obligations expected to be settled after 12 months	<u>1,117</u>	<u>780</u>

	2012	2011
	\$'000	\$'000
Non-current		
Employee benefits - long service leave	1,296	1,031
Make good provision	<u>2,345</u>	<u>1,880</u>
	<u>3,641</u>	<u>2,911</u>

Make good provision

The group has an obligation under property lease agreements to perform certain make good activities on the premises at the end of the respective leases which expire between 2013 and 2020. A provision has been recognised for the present value of the estimated expenditure required to remove certain leasehold improvements. The provision will be utilised at the end of the leases if they are not renewed. The estimated future cash outflow required to settle the obligation is discounted at 3.04% (2011: 5.16%) per annum. These costs have been capitalised as part of the cost of leasehold improvements and are amortised over the shorter of the term of the lease or the useful life of the assets.

Movements in provisions

Movements in each class of provision during the financial year, other than employee benefits, are set out below:

	Make good provision
	\$'000
Carrying amount at start of year	1,880
Additional provision recognised	170
Charged/(credited) to the profit or loss	<u>295</u>
Carrying amount at end of year	<u>2,345</u>

22 Contributed equity

	2012 Shares	2011 Shares	2012 \$'000	2011 \$'000
(a) Share capital				
Ordinary shares				
Fully paid	<u>53,644,738</u>	<u>53,324,938</u>	<u>184,815</u>	<u>183,309</u>
	<u>53,644,738</u>	<u>53,324,938</u>	<u>184,815</u>	<u>183,309</u>

(b) Movements in ordinary share capital

Date	Details	Number of shares	Issue price	\$'000
1 July 2010	Opening balance	48,613,257		170,360
1 July 2010	QFG contingent consideration	3,878,579	\$2.41	9,328
1 July 2010	Subscription for new shares	150,558	\$3.11	459
1 October 2010	Exercise 2008 options	35,816	\$4.71	169
1 October 2010	Share buy back	(35,816)	\$4.71	(169)
1 March 2011	Shares issued – acquisition consideration	664,544	\$4.71	3,130
1 March 2011	Exercise 2008 options	18,000	\$1.75	32
30 June 2011	Balance	53,324,938		183,309
28 July 2011	Shares issued – acquisition consideration	212,315	\$4.71	1,000
23 May 2012	Shares issued – acquisition consideration	107,485	\$4.71	506
30 June 2012	Balance	53,644,738		184,815

(c) Ordinary shares

Ordinary shares entitle the holder to participate in dividends and the proceeds on winding up of the company in proportion to the number of and amounts paid on the shares held.

On a show of hands every holder of ordinary shares present at a meeting in person or by proxy, is entitled to one vote, and upon a poll each share is entitled to one vote.

Ordinary shares have no par value and the company does not have a limited amount of authorised capital.

(d) Options

Information relating to the Group's share option plans, including details of options issued, exercised and lapsed during the financial year and options outstanding at the end of the reporting period, is set out in note 34.

(e) Capital risk management

The group's objectives when managing capital are to safeguard their ability to continue as a going concern, so that they can continue to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure in accordance with the group's financial facility agreements.

In order to maintain or adjust the capital structure, the Group may issue new shares, sell assets to reduce debt or remit excess cash to its debt providers. The capital structure and gearing ratios are as follows:

	2012 \$'000	2011 \$'000
Total borrowings	103,507	117,587
Less: cash and cash equivalents	<u>(9,439)</u>	<u>(6,963)</u>
Net debt	94,068	110,624
Total equity	<u>224,991</u>	<u>203,309</u>
Total capital	<u>319,059</u>	<u>313,933</u>
Gearing ratio	29%	35%

23 Reserves and retained earnings

	2012 \$'000	2011 \$'000
(a) Reserves		
Share-based payments	<u>3,259</u>	<u>2,743</u>
	<u>3,259</u>	<u>2,743</u>
Movements:		
<i>Share-based payments reserve</i>		
Balance at 1 July	2,743	2,287
Option expense	516	625
Issue of shares upon exercise of options	-	(169)
Balance 30 June	<u>3,259</u>	<u>2,743</u>

(b) Retained earnings

Movements in retained earnings were as follows:

	2012 \$'000	2011 \$'000
Balance at 1 July	17,257	1,920
Net profit for the year	<u>19,660</u>	<u>15,337</u>
Balance at 30 June	<u>36,917</u>	<u>17,257</u>

(c) Nature and purpose of reserves

Share-based payments reserve

The share-based payments reserve is used to recognise the fair value of options issued to employees and third parties but not exercised.

24 Key management personnel disclosures

(a) Directors

The following persons were directors of Virtus Health Pty Limited during the financial year:

(i) Chairman - non-executive

Marcus Darville

(ii) Executive directors

Susan Channon, Chief Executive Officer, Virtus Health Pty Limited

Andrew Othen, Managing Director, Melbourne IVF Pty Limited

John Moller, Managing Director, IVF Australia Pty Limited and Queensland Fertility Group Pty Limited

(iii) Non-executive directors

Simon Pither

John McBain

Manuela Toledo (Alternate Director)

Michael Chapman (Alternate Director)

Frank Quinn

John Esler

Keith Harrison (Alternate Director)

(b) Other key management personnel

The following persons also had authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, during the financial year:

Name	Position
Glenn Powers	Chief Financial Officer and Secretary, Virtus Health Pty Limited
Peter Illingworth	Medical Director, IVF Australia Pty Limited
Lyndon Hale	Medical Director, Melbourne IVF Pty Limited
David Molloy	Medical Director, Queensland Fertility Group Pty Limited

All of the above persons were also key management persons during the year ended 30 June 2011.

(c) Key management personnel compensation

	2012 \$	2011 \$
Short-term employee benefits*	1,965,102	2,197,793
Post-employment benefits	134,051	127,646
Long-term benefits	94,209	140,478
Share-based payments	188,900	220,198
	<u>2,382,262</u>	<u>2,686,115</u>

*Short-term employee benefits includes fees paid to contractors in respect of services provided in their capacity as a Medical Director.

(d) Equity instrument disclosures relating to key management personnel

(i) Options provided as remuneration

Details of options provided as remuneration and shares issued on the exercise of such options, together with terms and conditions of the options, can be found in Note 34.

(ii) Option holdings

The numbers of options over ordinary shares in the company held during the financial year by each director of Virtus Health Pty Limited and other key management personnel of the Group, including their personally related parties, are set out below.

2012

Name	Balance at start of the year	Granted as compensation	Exercised	Other changes	Balance at end of the year	Vested and exercisable	Unvested
Directors of Virtus Health Pty Limited							
Susan Channon	202,133	-	-	-	202,133	95,976	106,157
Michael Chapman	87,500	-	-	-	87,500	87,500	-
Frank Quinn	357,500	-	-	-	357,500	107,500	250,000
John Moller	241,491	-	-	-	241,491	160,994	80,497
Andrew Othen	127,389	-	-	-	127,389	-	127,389
Other key management personnel of the group							
Peter Illingworth	457,150	-	-	-	457,150	83,888	373,262
Glenn Powers	312,527	-	-	-	312,527	208,351	104,176

2011

Name	Balance at start of the year	Granted as compensation	Exercised	Other changes	Balance at end of the year	Vested and exercisable	Unvested
Directors of Virtus Health Pty Limited							
Susan Channon	95,976	106,157	-	-	202,133	90,976	111,157
Michael Chapman	87,500	-	-	-	87,500	77,500	10,000
Frank Quinn	357,500	-	-	-	357,500	97,500	260,000
John Moller	241,491	-	-	-	241,491	80,497	160,994
Andrew Othen	-	127,389	-	-	127,389	-	127,389
Other key management personnel of the group							
Peter Illingworth	457,150	-	-	-	457,150	55,394	401,756
Glenn Powers	312,527	-	-	-	312,527	104,175	208,352

(iii) *Share holdings*

The numbers of ordinary shares in the company held during the financial year by each director of Virtus Health Pty Limited and other key management personnel of the Group, including their personally related parties, are set out below. There were no shares granted during the reporting period as compensation.

2012

Name	Balance at the start of the year	Received during the year on the exercise of options	Other changes during the year	Balance at the end of the year
Directors of Virtus Health Pty Limited				
Sue Channon	529,146	-	-	529,146
Michael Chapman	915,436	-	-	915,436
Frank Quinn	1,127,702	-	-	1,127,702
John McBain	1,632,231	-	-	1,632,231
Manuela Toledo	778,620	-	-	778,620
John Moller	219,984	-	-	219,984
John Esler	509,830	-	-	509,830
Keith Harrison	415,983	-	-	415,983
Other key management personnel of the group				
Peter Illingworth	287,847	-	-	287,847
Lyndon Hale	1,224,173	-	-	1,224,173
David Molloy	667,900	-	-	667,900

2011

Name	Balance at the start of the year	Received during the year on the exercise of options	Other changes during the year	Balance at the end of the year
Directors of Virtus Health Pty Limited				
Sue Channon	509,644	-	19,502	529,146
Michael Chapman	881,698	-	33,738	915,436
Frank Quinn	1,086,141	-	41,561	1,127,702
John McBain	1,566,684	-	65,547	1,632,231
Manuela Toledo	737,294	-	41,326	778,620
John Moller	160,994	-	58,990	219,984
John Esler	373,116	-	136,714	509,830
Keith Harrison	304,435	-	111,548	415,983
Other key management personnel of the group				
Peter Illingworth	277,238	-	10,609	287,847
Lyndon Hale	1,175,013	-	49,160	1,224,173
David Molloy	488,799	-	179,101	667,900

(e) Other trading transactions with key management personnel

A director, Mr Michael Chapman, is a director and shareholder of Bridgemyth Pty Limited. IVF Australia Pty Limited entered into a contract with Bridgemyth Pty Limited to rent property at St George Private Hospital, Kogarah commencing 1 July 2005. The contract expired on 30 June 2009. IVF Australia Pty Limited continued to use the property and make rental payments to Bridgemyth Pty Limited from 1 July 2009 to 30 June 2010. The new contract was renegotiated and signed on 15 September 2010, which commences from 1 July 2010. The contract is based on normal commercial terms and conditions.

A director, Mr John Esler, is a director and shareholder of Dendeen Pty Limited. Queensland Fertility Group Pty Limited entered into a contract with Dendeen Pty Limited to rent property at 9 Scott Street, Toowoomba commencing 1 August 2007. The contract is based on normal commercial terms and conditions.

A director, Mr Keith Harrison is a director and shareholder of Keith Harrison Pty Limited. Queensland Fertility Group Pty Limited entered into a contract with Keith Harrison Pty Limited to rent property at 225 Wickham Terrace, Brisbane commencing 1 September 2008. The contract is based on normal commercial terms and conditions.

Aggregate amounts of each of the above types of other transactions with key management personnel of Virtus Health Pty Limited:

	2012 \$	2011 \$
Amounts recognised as revenue		
Rental income for use of Virtus Health Pty Limited facilities	<u>148,075</u>	<u>119,464</u>
Amounts recognised as expense		
Fees for provision of medical services and procedures	6,748,296	6,346,600
Rental expense in respect of property at St George Private Hospital, Kogarah	171,434	164,840
Rental expense in respect of property at 9 Scott Street, Toowoomba	59,124	56,851
Rental expense in respect of property at 225 Wickham Terrace, Brisbane	<u>26,640</u>	<u>49,861</u>
	<u>7,005,494</u>	<u>6,618,152</u>

At balance sheet date \$186,796 was payable to key management personnel of the Group (2011: \$626,132).

(f) Capital transactions with key management personnel

Marcus Darville, a Director of the Company, has a beneficial interest in Quadrant, a company which beneficially owns 46.7% of the issued ordinary shares of Virtus Health Pty Limited at 30 June 2012.

25 Remuneration of auditors

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

	2012 \$	2011 \$
PwC Australia		
(i) <i>Audit and other assurance services</i>		
Audit and review of financial statements	485,000	307,500
Total remuneration for audit and other assurance services	<u>485,000</u>	<u>307,500</u>
(ii) <i>Taxation services</i>		
Tax compliance services	82,250	45,000
Other tax services	-	34,700
Total remuneration for taxation services	<u>82,250</u>	<u>79,700</u>
(iii) <i>Other services</i>		
Accounting and other services	-	50,917

It is Group policy to utilise appropriate accounting and consulting resource for other services which may include tax advice and due diligence reporting on acquisitions, and it is Group policy to seek competitive tenders for such assignments as appropriate.

26 Contingencies

(a) Contingent liabilities

The Group had contingent liabilities at 30 June 2012 in respect of:

(i) Claims

Group companies are currently involved in litigations which may result in future liabilities and legal fees up to an insurance excess of \$50,000. The company has disclaimed liability and is defending the actions. It is not practical to estimate the potential effect of these claims but advice indicates that any liability that may arise in the unlikely event that the claims are successful will not be significant and will be covered by the Group's insurance policies.

(ii) Guarantees

In addition to the secured loans, the Group has additional facilities in the form of a Working Capital facility of \$25 million and a Capital Expenditure facility of \$20.0 million. As at the date of signing this report the drawdown on the capital expenditure facility is \$18,031,514. Drawdowns of \$2,503,952 in the form of financial guarantees have been made against the working capital facility. Subject to the continued compliance with debt covenants, the bank facilities may be drawn at any time and have an average maturity of 2 years (2011: 3 years).

(iii) Associates

For contingent liabilities relating to associates refer to note 31.

27 Commitments

(a) Capital commitments

Capital expenditure contracted for at the end of each reporting period but not recognised as liabilities is as follows:

	2012 \$'000	2011 \$'000
<i>Property, plant and equipment</i>		
Payable:		
Within one year	<u>236</u>	<u>473</u>
	<u>236</u>	<u>473</u>

(b) Lease commitments: group as lessee

(i) Non-cancellable operating leases

The group leases various offices and medical centres under non-cancellable operating leases expiring within two to eight years. The leases have varying terms, escalation clauses and renewal rights. On renewal, the terms of the leases are renegotiated. Excess office space is sub-let to third parties also under non-cancellable operating leases.

	2012 \$'000	2011 \$'000
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:		
Within one year	5,559	5,833
Later than one year but not later than five years	12,761	16,043
Later than five years	1,600	3,877
	<u>19,920</u>	<u>25,753</u>
	2012 \$'000	2011 \$'000

Sub-lease payments

Future minimum lease payments expected to be received in relation to non-cancellable sub-leases of operating leases

<u>61</u>	<u>122</u>
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(ii) Finance leases

	2012 \$'000	2011 \$'000
Commitments in relation to finance leases are payable as follows:		
Within one year	285	516
Later than one year but not later than five years	354	640
Later than five years	-	-
Minimum lease payments	639	1,156
Future finance charges	(75)	(143)
Recognised as a liability	<u>564</u>	<u>1,013</u>
Representing lease liabilities:		
Current (note 18)	240	436
Non-current (note 19)	<u>324</u>	<u>577</u>
	<u>564</u>	<u>1,013</u>

28 Related party transactions

(a) Parent entity

The parent entity within the Group is Virtus Health Pty Limited.

(b) Subsidiaries

Interests in subsidiaries are set out in note 30.

(c) Key management personnel

Disclosures relating to key management personnel are set out in note 24.

(d) Transactions with other related parties

The following transactions occurred with related parties:

Virtus Health Pty Limited
Notes to the consolidated financial statements
30 June 2012
(continued)

	2012 \$	2011 \$
<i>Share of profits (losses) of associates</i>		
Maroubra Day Surgery Pty Limited	855,041	919,901
Obstetrics & Gynaecological Imaging Pty Limited	6,433	(43,088)
City West Day Surgery Pty Limited	574,298	188,763

Other transactions

Fees paid to related party for services to the Board of the ultimate Australian parent entity	50,000	50,000
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(e) Outstanding balances arising from sales/purchases of goods and services

The following balances are outstanding at the end of each reporting period in relation to transactions with related parties:

	2012 \$	2011 \$
<i>Current receivables (sales of goods and services)</i>		
Associates	580,731	188,763
<i>Current payables (purchase of goods)</i>		
Associates	(26,640)	(43,088)
<i>Distributions received in advance</i>		
Associates	(81,726)	(243,075)

No provisions for doubtful debts have been raised in relation to any outstanding balances, and no expense has been recognised in respect of bad or doubtful debts due from related parties.

(f) Transactions within the group

Virtus Health Pty Limited is responsible for group strategy and raising equity capital. IVF Finance Pty Limited is responsible for debt finance and making acquisitions on behalf of the group. IVF Australia Pty Limited, The Heptarchy Trust, Queensland Fertility Group Pty Limited and North Shore Specialist Day Surgery Pty Limited employ the medical and other staff including certain directors. The proceeds of any issue of shares by Virtus Health Pty Limited are passed to IVF Finance Pty Limited as an interest free loan. IVF Finance Pty Limited uses the funds for acquisitions.

g) Guarantees

The group is party to bank facility cross guarantees.

(h) Terms and conditions

All other transactions were made on normal commercial terms and conditions and at market rates, except that there are no fixed terms for the repayment of loans between subsidiaries and the loans are interest free. Outstanding balances are unsecured and are repayable in cash.

29 Business combination

(a) Summary of acquisitions

1. Acquisition of Gold Coast IVF

On 29 July 2011 Virtus Health Pty Limited, through its wholly owned subsidiary Queensland Fertility Group Pty Limited, acquired 100% of the issued share capital Fertility Gold Coast Pty Limited.

Details of the purchase consideration, the net assets acquired and goodwill are as follows:

	\$'000
Purchase consideration	3,557
Cash paid	1,000
Fair value of equity instruments issued	506
Fair value of equity instruments issued	5,063
Total purchase consideration	111
Fair value of net identifiable assets acquired (refer to (b) below)	4,952
Goodwill on acquisition	

The acquired business contributed revenues and other income of \$2,880,386 and net profit before tax of \$756,184 (excluding the cost of financing the transaction) to the Group for the period from 29 July 2011 to 30 June 2012. If the acquisition had occurred on 1 July 2011, consolidated revenue and other income and consolidated net profit before tax for the year ended 30 June 2012 would have been \$3,142,239 and \$824,928 respectively excluding any additional financing or brand amortisation costs. These amounts have been calculated using the Group's accounting policies and by adjusting the results of the subsidiary to reflect the additional depreciation and amortisation that would have been charged assuming the fair value adjustments to property, plant and equipment and intangible assets had applied from 1 July 2011, together with the consequential tax effects.

2. Acquisition of Mackay Day Surgery

On 31 January 2012, Virtus Health Pty Limited, through its wholly owned subsidiary Queensland Fertility Group Pty Limited, acquired the business, assets and liabilities of Mackay Day Surgery Pty Limited. The net assets acquired consisted of \$374,000 of plant and equipment, liabilities totalling \$19,000 and \$209,000 of goodwill.

The accounting for this acquisition is on a provisional basis.

3. Acquisition of Hunter IVF

On 1 March 2011 Virtus Health Pty Limited, through its wholly owned subsidiary IVF Australia Pty Limited, acquired 100% of the issued share capital and units of Hunter IVF Group Pty Limited.

Details of the purchase consideration, the net assets acquired and goodwill are as follows:

	\$'000
Purchase consideration	
Cash paid	7,320
Fair value of equity instruments issued	3,130
Total purchase consideration	<u>10,450</u>
Fair value of net identifiable assets acquired (refer to (b) below)	699
Goodwill on acquisition	<u>9,751</u>

The acquired business contributed revenues and other income of \$1,260,436 and net profit before tax of \$565,567 (excluding the cost of financing the transaction) to the Group for the period from 1 March 2011 to 30 June 2011. If the acquisition had occurred on 1 July 2010, consolidated revenue and other income and consolidated net profit before tax for the year ended 30 June 2011 would have been \$4,176,694 and \$1,449,852 respectively excluding any additional financing or brand amortisation costs. These amounts have been calculated using the Group's accounting policies and by adjusting the results of the subsidiary to reflect the additional depreciation and amortisation that would have been charged assuming the fair value adjustments to property, plant and equipment and intangible assets had applied from 1 July 2010, together with the consequential tax effects.

Included in the purchase consideration are 664,544 ordinary shares of Virtus Health Pty Limited valued at \$4.71 per share. The share price of \$4.71 was based on a negotiated valuation of the business between the vendors of New South Wales IVF Group Pty Limited and Virtus Health Pty Limited.

(b) Assets and liabilities acquired

1. Acquisition of Gold Coast IVF

	Fair value \$'000
Cash	86
Trade receivables	100
Plant, equipment and software	170
Deferred tax assets	19
Trade and other payables	(104)
Deferred revenue	(57)
Other provisions	(54)
Provision for employee benefits	(49)
Net assets	<u>111</u>

The goodwill is attributable to the reputation of Gold Coast IVF in Queensland. The fair value of assets and liabilities acquired are based on discounted cash flow models. No acquisition provisions were created.

2. Acquisition of Hunter IVF

	Fair Value \$'000
Cash	414
Trade and other receivables	173
Other current assets	15
Plant and equipment	357
Other non-current assets	-
Intangible assets: brand names	490
Deferred tax assets	34
Trade and other payables	(193)
Deferred revenue	(106)
Deferred tax liability	(148)
Other provisions	(259)
Provision for employee benefits	(78)
Net assets	<u>699</u>

The goodwill is attributable to the reputation of Hunter IVF Pty Limited in New South Wales. The fair value of assets and liabilities acquired are based on discounted cash flow models. No acquisition provisions were created.

30 Subsidiaries and transactions with non-controlling interests

(a) Significant investments in subsidiaries

The consolidated financial statements incorporate the assets, liabilities and results of the following subsidiaries in accordance with the accounting policy described in note 1(b).

Name of entity	Country of incorporation	Class of shares	Beneficial Interest	
			2012 %	2011 %
IVF Finance Pty Limited	Australia	Ordinary	100	100
IVFA Sub-Holdings Pty Limited	Australia	Ordinary	100	100
IVF Australia Pty Limited	Australia	Ordinary	100	100
Melbourne IVF Holdings Pty Limited	Australia	Ordinary	100	100
Melbourne IVF Pty Limited	Australia	Ordinary	100	100
The Heptarchy Trust	Australia	Units	100	100
North Shore Specialist Day Surgery Pty Limited	Australia	Ordinary	100	100
Queensland Fertility Group Pty Limited	Australia	Ordinary	100	100
IVF Australia Plan Management Pty Limited	Australia	Ordinary	100	100
North Shore ART Pty Limited	Australia	Ordinary	100	100
IVF Australia Participants Pty Limited	Australia	Ordinary	100	100
IVF South Pty Limited	Australia	Ordinary	100	100
City West IVF Pty Limited	Australia	Ordinary	100	100
Spring Hill Specialist Day Hospital Pty Limited	Australia	Ordinary	100	100
The QFG Day Theatres Unit Trust	Australia	Units	100	100
Hunter IVF Pty Limited	Australia	Ordinary	100	100
Hunter Fertility Unit Trust	Australia	Units	100	100
Queensland Fertility Group Gold Coast Pty Limited	Australia	Ordinary	100	-
Gold Coast Obstetrics & Gynaecology Specialist Services Pty Limited	Australia	Ordinary	100	-
Mackay Specialist Day Hospital Pty Limited	Australia	Ordinary	100	-

The proportion of ownership interest is equal to the proportion of voting power held.

31 Interests in associates

(a) Investments in associates

Interests are held in the following associates:

Unlisted	Country of Residence	Principal Activities	Ownership Interest		Carrying Amount of Investment	
			2012	2011	2012 \$'000	2011 \$'000
Maroubra Day Surgery Pty Limited	Australia	Provision of medical services	50%	50%	2,400	2,400
Obstetrics & Gynaecological Imaging Australia Pty Limited	Australia	Provision of medical services	50%	50%	25	25
City West Day Surgery Pty Limited	Australia	Provision of medical services	50%	50%	1,488	1,397
					<u>3,913</u>	<u>3,822</u>
					2012 \$'000	2011 \$'000
Current assets					2,562	1,116
Non-current assets					<u>2,543</u>	<u>3,479</u>
Total assets					<u>5,105</u>	<u>4,595</u>
Current liabilities					(1,192)	(773)
Non-current liabilities					-	-
Total liabilities					<u>(1,192)</u>	<u>(773)</u>
Share of assets employed in associates					<u>3,913</u>	<u>3,822</u>

Share of associates' revenue, expenses and results

	2012 \$'000	2011 \$'000
Revenue	6,335	5,932
Expenses	<u>(4,899)</u>	<u>(4,866)</u>
Profit before income tax	1,436	1,066
Income tax expense	-	-
Profit after income tax	<u>1,436</u>	<u>1,066</u>

32 Events occurring after the reporting period

(a) Acquisition of Maroubra Day Surgery

On 7 August 2012, IVF Australia, a subsidiary of Virtus Health Pty Limited, acquired the remaining 50% share capital and units of Maroubra Day Surgery Pty Limited for a cash consideration of \$7,074,317, and was funded by a drawdown from the Group capital expenditure facility and existing cash.

The financial effects of this transaction have not been brought to account at 30 June 2012. The operating results and assets and liabilities of the company will be consolidated from 7 August 2012.

(b) Refinancing of the borrowing facility

On 16 August 2012, IVF Finance Pty Limited, a subsidiary of Virtus Health Pty Limited successfully renegotiated the external borrowing facility for a total of \$225,000,000, with an expiry date of 17 August 2013. The funds were used to pay an ordinary dividend of \$45,833,685 (82 cents per ordinary share) on 17 August 2012. A capital return of \$55,335,791 (99 cents per ordinary share) was paid on the 7 September 2012.

33 Reconciliation of profit after income tax to net cash inflow from operating activities

	2012 \$'000	2011 \$'000
Profit for the year	19,660	15,337
Depreciation and amortisation	8,972	8,277
Net loss on disposal of assets	104	53
Amortisation of bank facility fees	850	694
Interest on finance lease facilities	133	122
Share based payments expense	516	625
Share of net profits of associates	(1,436)	(1,066)
Dividend and interest income	(433)	(466)
(Gain)/loss on revaluation of hedging instruments	968	(870)
Unwinding of discount on deferred consideration on acquisition of subsidiary	-	166
Doubtful debts expense	-	144
Other non-cash items	(34)	(3)
Change in operating assets and liabilities		
(Increase)/decrease in trade debtors	(1,322)	(3,650)
(Increase)/decrease in inventories	120	4
(Increase)/decrease in deferred tax assets	(1,885)	(543)
(Decrease)/increase in trade creditors	2,841	2,282
(Decrease)/increase in deferred revenue	580	(2,999)
Increase/(decrease) in provision for income taxes payable	(1,602)	4,776
(Decrease)/increase in other provisions	1,079	(114)
Net cash inflow from operating activities	<u>29,111</u>	<u>22,769</u>

During the year, the company issued \$1,506,000 of new equity as part of the payment for Queensland Fertility Group Gold Coast Pty Limited.

34 Share-based payments

(a) Employee Option Plan

Virtus Health Share Option Plan

The Virtus Health Share Option plan was adopted by the Board on 12 November 2008. The plan was established to reward, retain and motivate doctors and senior employees through recognition of their abilities, performance and contributions. Participation in the plan is at the Board's discretion and no individual has a contractual right to participate in the plan or to receive any guaranteed benefits. Key features of the plan are as follows:

Options are vested in equal instalments over a two to four year period, subject to performance conditions.

Once issued, options remain exercisable for a period of ten years. Options are granted under the plan at an exercise price equal to market value at the time of grant. Options granted under the plan carry no dividend or voting rights. No option holder has any right under the options to participate in any other share issue of the company or any other entity.

When exercisable, each option is convertible into one ordinary share.

IVF Australia Restructuring Plan

The IVF Australia Restructuring Share Option plan was adopted by the Board on 10 April 2008. The plan was established to reward, retain and motivate doctors and senior employees through recognition of their abilities, efforts and contributions. The plan is now closed for further option grants. Participation in the plan is at the Board's discretion and no individual has a contractual right to participate in the plan or to receive any guaranteed benefits. Key features of the plan are as follows:

Options are vested in equal instalments over a two to four year period, subject to performance conditions.

Once issued, options remain exercisable for a period of ten years. Options are granted under the plan at a various exercise prices as set out below. Options granted under the plan carry no dividend or voting rights. No option holder has any right under the options to participate in any other share issue of the company or any other entity.

When exercisable, each option is convertible into one ordinary share.

Melbourne IVF Restructuring Share Option Plan

The Melbourne IVF Restructuring Share Option plan was adopted by the Board on 13 November 2008. The plan was established to reward, retain and motivate doctors and senior employees of Melbourne IVF Pty Limited through recognition of their abilities, efforts and contributions. The plan is now closed for further option grants. Under the plan, participants are granted options under time based and performance based vesting conditions. Participation in the plan is at the Board's discretion and no individual has a contractual right to participate in the plan or to receive any guaranteed benefits. Key features of the plan are as follows:

Options are vested in equal instalments over a 3 year period, subject to performance conditions.

Once issued, options remain exercisable for a period of ten years. Options are granted under the plan for no consideration. Options granted under the plan carry no dividend or voting rights. No option holder has any right under the options to participate in any other share issue of the company or any other entity.

When exercisable, each option is convertible into one ordinary share.

Set out below are summaries of options granted under the plans:

Grant Date	Expiry date	Exercise price	Balance at start of the year Number	Granted during the year Number	Exercise d during the year Number	Forfeited during the year Number	Balance at end of the year Number	Vested and exercisable at end of the year Number
Consolidated 2012								
Virtus Health Plan								
12-Nov-08	12-Nov-18	\$4.12	312,527	-	-	-	312,527	208,351
25-Feb-09	25-Feb-19	\$4.12	44,000	-	-	-	44,000	27,333
1-Jul-09	1-Jul-19	\$3.11	450,000	-	-	-	450,000	152,667
1-Oct-09	1-Oct-19	\$3.11	241,491	-	-	-	241,491	160,993
1-Jul-10	1-Jul-20	\$4.71	327,389	-	-	-	327,389	-
1-Sep-10	1-Sep-20	\$4.71	106,157	-	-	-	106,157	-
1-Jul-11	1-Jul-14	\$5.17	-	258,027	-	-	258,027	-
IVF Australia Restructuring Plan								
10-Apr-08	16-Feb-15	\$1.64	60,976	-	-	-	60,976	60,976
10-Apr-08	1-Jan-16	\$3.15	183,496	-	-	-	183,496	183,496
10-Apr-08	14-Feb-17	\$3.15	216,075	-	-	-	216,075	216,075
10-Apr-08	1-Jan-18	\$3.26	228,100	-	-	-	228,100	228,100
10-Apr-08	10-Apr-18	\$2.98	9,000	-	-	-	9,000	6,660
10-Apr-08	10-Apr-18	\$2.53	1,550,000	-	-	-	1,550,000	-
10-Apr-08	10-Apr-18	\$0.01	403,536	-	-	-	403,536	-
Melbourne IVF Restructuring Share Option Plan								
20-Nov-08	20-Nov-18	\$0.00	272,470	-	-	-	272,470	272,470
Total			4,405,217	258,027	-	-	4,663,244	1,517,121
Weighted average exercise price			\$2.66	\$5.17	-	-	\$2.80	\$3.27
Consolidated 2011								
Virtus Health Plan								
12-Nov-08	12-Nov-18	\$4.12	312,527	-	-	-	312,527	104,175
25-Feb-09	25-Feb-19	\$4.12	44,000	-	-	-	44,000	13,666
1-Jul-09	1-Jul-19	\$3.11	450,000	-	-	-	450,000	-
1-Oct-09	1-Oct-19	\$3.11	241,491	-	-	-	241,491	80,497
1-Jul-10	1-Jul-20	\$4.71	-	327,389	-	-	327,389	-
1-Sep-10	1-Sep-20	\$4.71	-	106,157	-	-	106,157	-
IVF Australia Restructuring Plan								
10-Apr-08	16-Feb-15	\$1.64	60,976	-	-	-	60,976	60,976
10-Apr-08	1-Jan-16	\$3.15	193,496	-	(6,000)	(4,000)	183,496	183,496
10-Apr-08	14-Feb-17	\$3.15	216,075	-	-	-	216,075	154,042
10-Apr-08	1-Jan-18	\$3.26	238,100	-	(10,000)	-	228,100	146,802
10-Apr-08	10-Apr-18	\$2.98	11,000	-	(2,000)	-	9,000	6,660
10-Apr-08	10-Apr-18	\$2.53	1,550,000	-	-	-	1,550,000	-
10-Apr-08	10-Apr-18	\$0.01	403,536	-	-	-	403,536	-
Melbourne IVF Restructuring Share Option Plan								
20-Nov-08	20-Nov-18	\$0.00	328,287	-	(35,816)	(20,001)	272,470	272,470
Total			4,049,488	433,546	(53,816)	(24,001)	4,405,217	1,022,784
Weighted average exercise price			\$2.41	\$4.71	\$1.07	\$0.52	\$2.66	\$2.39

No options expired during the periods covered by the above tables.

The weighted average remaining contractual life of share options outstanding at the end of the period was 6.25 years (2011 – 7.07 years).

Fair value of options granted

The assessed fair value at grant date of options granted during the year ended 30 June 2012 is set out as follows:

	Virtus Health Share Option Plan
Grant date	1 July 2011
Fair value per option at grant date	\$0.77 - \$0.78

The fair value at grant date is independently determined using a Binomial Option Valuation Model.

The assessed fair value at grant date of options granted during the year ended 30 June 2011 is set out below:

	Virtus Health Share Option Plan 1 July 2010	Virtus Health Share Options Plan 1 September 2010
Grant date		
Fair value per option at grant date	\$0.42 - \$0.43	\$0.40- \$0.41

The fair value at grant date is independently determined using a Binomial Option Valuation Model.

(b) Expenses arising from share-based payment transactions

Total expenses arising from share-based payment transactions recognised during the period as part of employee benefit expense were as follows:

	2012 \$'000	2011 \$'000
Options issued under employee option plan	<u>516</u>	<u>625</u>

35 Parent entity financial information

(a) Summary financial information

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

	2012 \$'000	2011 \$'000
Balance sheet		
Current assets	824	908
Total assets	192,618	201,500
Current liabilities	13,256	21,363
Total liabilities	<u>13,256</u>	<u>21,363</u>
	<u>179,362</u>	<u>180,137</u>
Shareholders' equity		
Contributed equity	184,815	183,309
Reserves	2,891	2,595
Share-based payments	<u>(8,344)</u>	<u>(5,767)</u>
Accumulated losses	<u>179,362</u>	<u>180,137</u>
Profit (loss) for the year	<u>(2,577)</u>	<u>1,115</u>
Total comprehensive income (loss)	<u>(2,577)</u>	<u>1,115</u>

(b) Guarantees entered into by the parent entity

Carrying amount included in current liabilities (refer to note 26 for the details of guarantees).

(c) Contingent liabilities of the parent entity

The parent entity did not have any contingent liabilities as at 30 June 2012 or 30 June 2011. For information about guarantees given by the parent entity, please see above.

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

As at 30 June 2012 and 30 June 2011, the parent entity had no contractual commitments.

36 Franking Credits

	2012 \$'000	2011 \$'000
Franking credits available for subsequent financial years based on a tax rate of 30% (2011: 30%)	<u>32,079</u>	<u>23,065</u>
	<u>32,079</u>	<u>23,065</u>

The above amounts represent the balance of the franking account as at the reporting date, adjusted for franking credits that will arise from the payment of the amount of the provision for income tax.

**Virtus Health Pty Limited
Directors' declaration**

For the year ended 30 June 2012

In the directors' opinion:

- (a) the financial statements and notes set out on pages 7 to 50 are in accordance with the *Corporations Act 2001*, including:
 - (i) complying with Accounting Standards, the *Corporations Regulations 2001* and other mandatory professional reporting requirements, and
 - (ii) giving a true and fair view of the consolidated entity's financial position as at 30 June 2012 and of its performance for the financial year ended on that date, and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable, and

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

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

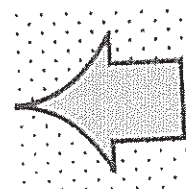


Marcus Darville

Director

Sydney

31 October 2012





Independent auditor's report to the members of Virtus Health Pty Limited

Report on the financial report

We have audited the accompanying financial report of Virtus Health Pty Limited (the company), which comprises the balance sheet as at 30 June 2012, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration for the Virtus Health Pty Limited Group (the consolidated entity). The consolidated entity comprises the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1(a)(i), the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with *International Financial Reporting Standards*.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. 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.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report.

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

Independence

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

PricewaterhouseCoopers, ABN 52 780 433 757
Darling Park Tower 2, 201 Sussex Street, GPO BOX 2650, SYDNEY NSW 1171
T: +61 2 8266 0000, F: +61 2 8266 9999, www.pwc.com.au



Auditor's opinion

In our opinion:

- (a) the financial report of Virtus Health Pty Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the consolidated entity's financial position as at 30 June 2012 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*; and
- (b) the financial report and notes also comply with International Financial Reporting Standards as disclosed in Note 1(a)(i)

PricewaterhouseCoopers

PricewaterhouseCoopers

Eddie Wilkie

Eddie Wilkie
Partner

Sydney
31 October 2012