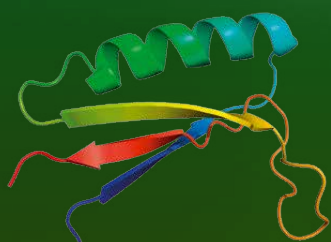




annual report

PHYLOGICA LIMITED



PHYLOGICA



14

www.phylogica.com

PHYLOGICA LTD World-class drug discovery platform harnessing the rich biodiversity of nature to discover novel peptide therapeutics. Phylomer libraries have been optimised by natural evolutionary selection for peptides with stable drug-like structures. Strategy to accelerate cash sustainability by focusing on fee-for-service drug discovery partnerships. Unique qualities of Phylomer libraries validated by partnerships with Roche Group, MedImmune, Pfizer and Janssen. Capitalising on the growing trend for large pharmaceutical companies to outsource drug discovery to small specialised players. Rapid growth in peptide therapeutic market is attracting increasing interest from the pharmaceutical industry. Preparing to enter new markets by offering target discovery and validation services to big Pharma.

Corporate Information

Phylogica Limited

ACN 098 391 961

Directors

Dr Doug Wilson
Non-Executive Chairman

Mr Bruce McHarrie
Non-Executive Director

Mr Jeremy Curnock Cook
Non-Executive Director

Dr Bernard Hockings
Non-Executive Director

Dr Richard Hopkins
Executive Director

Company Secretary

Mr Graeme Boden
Telephone: +61 8 9286 1219
Facsimile: +61 8 9284 3801
Email: gboden@bigpond.net.au

Share Registry

Security Transfer Registrars Pty Ltd
PO Box 535
Applecross
Western Australia 6953
770 Canning Highway
Applecross
Western Australia 6153
Telephone: +61 8 9315 2333
Facsimile: +61 8 9315 2233
Email: registrar@securitytransfer.com.au

Bankers

Australia and New Zealand Banking Group
Subiaco Branch
464 Hay Street
Subiaco
Western Australia 6008

Auditors

HLB Mann Judd
Level 4
130 Stirling Street
Perth
Western Australia 6000

Registered Office

15 Lovegrove Close
Mount Claremont
Western Australia 6010
Telephone: +61 8 9286 1219
Facsimile: +61 8 9284 3801

Postal Address

PO Box 8207
Subiaco East
Western Australia 6008

Principal Place of Business

Telethon Kids Institute
100 Roberts Road
Subiaco
Western Australia 6008
Telephone: +61 8 9489 7777
Facsimile: +61 8 9489 7700

Website

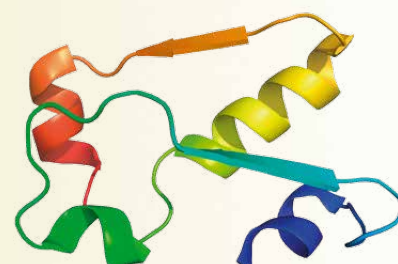
www.phylogica.com

Incorporated in Western Australia, October 2001

Listed on:
Australian Securities Exchange (ASX)
Home Exchange: Perth

Code: PYC ordinary shares

Frankfurt Exchange
Code: PH7 ordinary shares



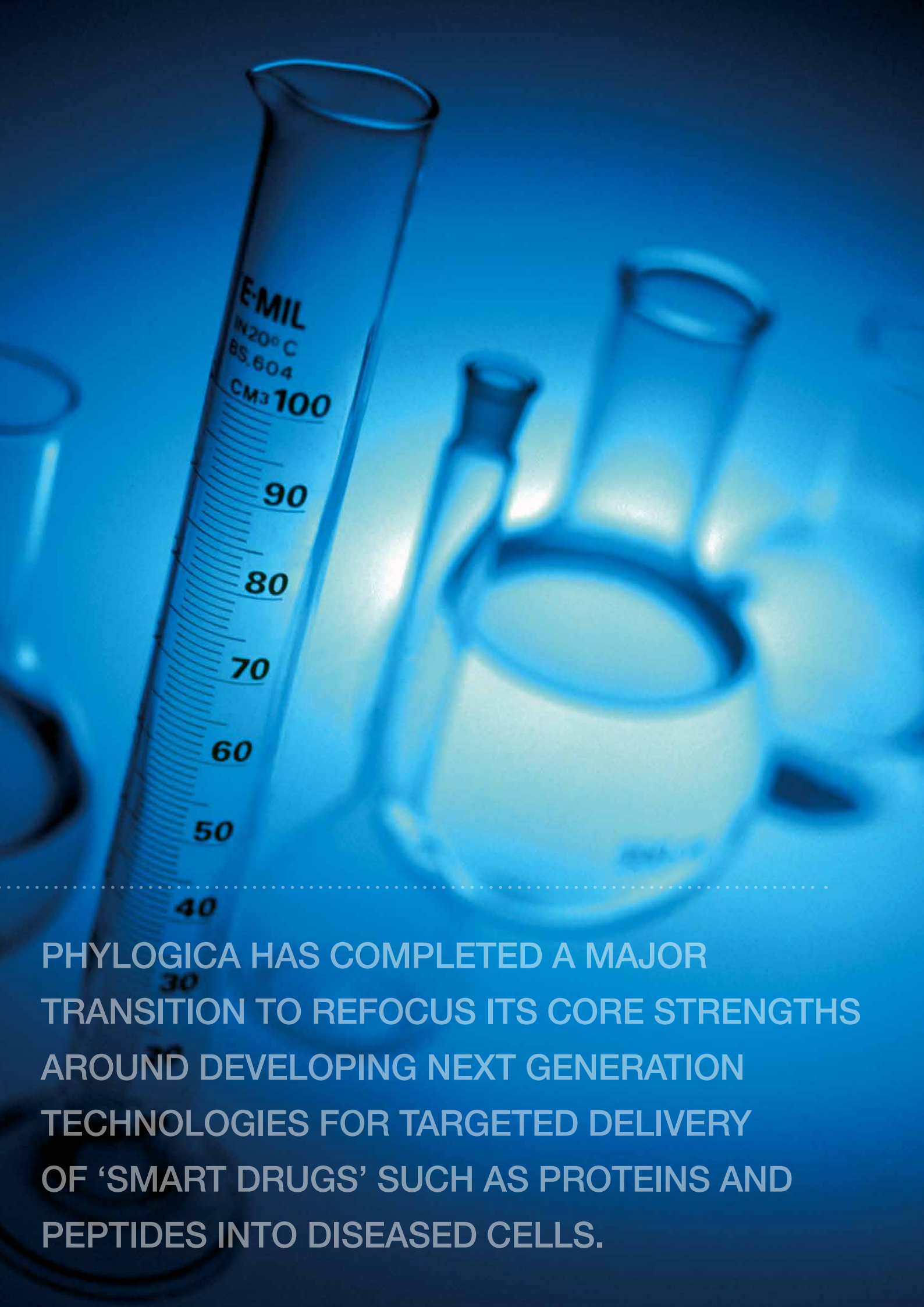


PHYLOGICA LIMITED

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PHYLOGICA HAS COMPLETED A MAJOR
TRANSITION TO REFOCUS ITS CORE STRENGTHS
AROUND DEVELOPING NEXT GENERATION
TECHNOLOGIES FOR TARGETED DELIVERY
OF 'SMART DRUGS' SUCH AS PROTEINS AND
PEPTIDES INTO DISEASED CELLS.

Executive Report

DEAR SHAREHOLDER

Key Highlights

- Raised \$6.1 Million via a non-renounceable rights offer that was strongly supported by existing shareholders.
- Validated our proprietary drug delivery technology, referred to as the Endosomal Escape Trap, for the Janssen collaboration.
- Identified a panel of cell penetrating peptides that improved drug delivery by 25-50 fold - confirmed as being 'best-in-class' for delivering biologics drugs inside cells.
- Announced a new research agreement with Genentech – a major subsidiary of Roche and a pioneer in the biotechnology industry
- Initiated an in-house drug discovery oncology programme aimed at developing novel Phylomer-based drugs for treatment of breast cancer.
- New patent grants further strengthen Phylogica's formidable intellectual property estate.
- Awarded highly competitive government grants in collaboration with prestigious academic groups at the University of Western Australian and the University of Queensland.

Overview

The past year has seen the company achieve a number of important and exciting milestones. During this time, Phylogica completed a major transition to refocus its core strengths around developing next generation technologies for targeted delivery of 'smart drugs' such as proteins and peptides into diseased cells. This led to the successful validation of a proprietary drug delivery platform that is now considered 'best-in-class' for delivering peptide-linked drugs inside cells. The company also completed a restructure to significantly reduce corporate overheads and accelerate platform development. Key research activities were further supported by leveraging non-dilutive grant funding and through expanded eligibility for the R&D tax concession (see following pages). The emphasis of the company on its differentiated intracellular expertise is already yielding results, with the recent announcement of an exciting new alliance with a member of the Roche group, Genentech. In another very important development, Phylogica formally announced it had initiated an in-house programme to discover Phylomer-based drugs against breast cancer. This marks an exciting transition for Phylogica as it seeks to become a fully integrated drug discovery company.

PHYLOGICA SIGNS DEAL WITH MAJOR US BIOTECH OWNED BY ROCHE

In September, Phylogica was delighted to announce its latest research collaboration with Genentech, the US-based biotechnology company regarded as one of the most influential leaders in the development of new cancer treatments.

Genentech pioneered the use of recombinant DNA technology in the 1970s to produce the synthetic human insulin that became the world's first ever genetically engineered therapeutic agent. Today, the company is still regarded as one of the world's biotech success stories, developing and manufacturing an array of bestselling drugs for diseases ranging from breast, lung and colorectal cancer to stroke, asthma, arthritis and cystic fibrosis.

The company's collaboration with Phylogica will focus on novel applications of a proprietary screening system, devised to identify peptides with the capacity to penetrate cells and deliver their biologically active cargoes via the cells' endosomes.

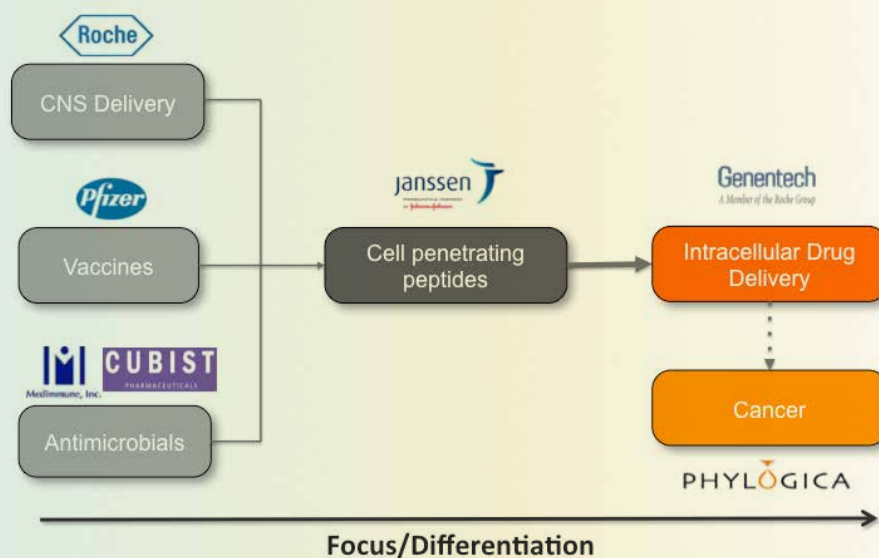
The Genentech agreement validates the industry's growing interest in Phylogica's biologics delivery technology. The company believes that the agreement may lead to an expanded partnership with the Roche group as Phylogica continue to explore the novel and largely unexploited potential of its peptides to deliver therapeutic drug cargoes to cells infected with cancer and other deadly diseases.

PHYLOGICA: SPECIALISING IN INTRACELLULAR DRUG DELIVERY

The Genentech agreement represents Phylogica's fifth collaboration in less than five years with a major pharmaceutical company – an unprecedented number for an Australian biotech company. This milestone further supports Phylogica's strategy to specialise in intracellular drug delivery – a decision that has already yielded the following results:

- A \$2.4 million investment by Janssen, which facilitated the successful validation of Phylogica's novel Endosomal Escape Trap (EET) technology.
- Significant outcomes from the EET intracellular delivery approach, including a growing panel of novel best-in-class cell penetrating peptides.
- Exclusive ownership of key intellectual property around next generation intracellular delivery, including two patents filed covering the development and use of the EET.
- New commercialisation opportunities around the EET technology, as evident from the recent partnership with Genentech.

Partnerships: focus on intracellular delivery of biologics



DIFFERENTIATED EXPERTISE IN INTRACELLULAR DELIVERY: BREAKTHROUGH PEPTIDE THERAPEUTICS

In working with pharmaceutical company Janssen, Phylogica was able to validate its proprietary delivery technology, the Endosomal Escape Trap (EET), to discover novel cell penetrating peptides which could deliver their scaffold into cells. The EET is a unique approach that enables Phylogica to screen billions of Phylomers for extremely rare peptides that can escape from endosomes to deliver their cargo more efficiently into cells. This is a critical step required for identifying peptides that can efficiently deliver drugs against intracellular targets. The ability of the Phylogica's delivery technology to break through the cell penetration barrier with large molecules, is reflected in the company's new tagline: 'Breakthrough Peptide Therapeutics'.

In February 2014, Phylogica highlighted several key milestones achieved with the Endosomal Escape Trap. These included:

- Identification of Phylomers that improved delivery of a protein cargo inside cells by 25-50 times.
- Establishing that the EET yielded an unprecedented hit-rate for functionally active peptides.
- Observed high sequence and structural diversity in the pool of validated hits, suggesting a range of cell-uptake mechanisms.
- Phylomers shown to deliver a range of therapeutic cargoes, including protein toxins and the Janssen cargo, into a variety of particular cell types.
- Information collected across populations of novel cell penetrating peptides provides Phylogica with unique insight and hence intellectual property into the requirements for efficient cell penetration.

These exciting data firmly establish Phylogica as a leader in the field of intracellular drug delivery. Having validated its novel platform for discovery of functionally active delivery reagents, the company is actively pursuing expressions of interest from multiple prospective partners interested in accessing this breakthrough technology.

Due to changed strategic priorities, Janssen announced in June that it would not extend its collaboration, despite Phylogica achieving the technical milestones required for the project. However, the Johnson and Johnson company has indicated continuing interest in Phylogica's intracellular delivery technology and in its new Oncology Program in particular. Phylogica is maintaining discussions with a range of pharmaceutical companies that have expressed interest in accessing intracellular oncology targets. It is expected that further validation of the oncology programme will facilitate new opportunities for commercialisation.

PHYLOGICA INITIATES AN INTERNAL DISCOVERY PROGRAM IN BREAST CANCER

Based on the successful technical outcome with the Endosomal Escape Trap, Phylogica has taken the strategic decision to combine the company's drug delivery platform with an internal discovery program to investigate the efficacy of peptide-based drugs against high-value cancer targets. While this initiative will initially focus on breast cancer, the targets chosen are also relevant to other common malignancies, including colon, lung and pancreatic cancers.

Benefits of this strategy include:

- Ability to address a major challenge in developing drugs against compelling intracellular targets (eg transcription factors) that have proven intractable to small molecules.
- Deployment of well-validated Phylomer technologies to accelerate the path to drug discovery.
- Rapid access to high-value commercial inflexion points, resulting in significantly larger deal economics.
- Provides the company with alternative revenues streams that complement the Discovery Alliance Model.

Phylogica's Proprietary Oncology Programme

Program	Indication	Differentiation	Discovery	Functional Validation	Preclinical
Stat3/5	Breast Cancer	• Relevant for cancer stem cells (CD34+/24-) with triple -ve tumours • > specificity than JAK inhibitors			
cMyc/N-Myc	Breast Cancer	• Master regulators of many cancers • Relevant to triple -ve breast cancer • > specific than BET-bromodomain inhibitors			

A close-up photograph of a person in a blue lab coat using a pipette. The pipette has a yellow and black handle with the word 'PHYLOGICA' on it. The person is holding a small vial with a pink cap. The background is a blurred laboratory setting with various equipment and containers.

NEW PATENT GRANTS FURTHER
STRENGTHEN PHYLOGICA
FORMIDABLE INTELLECTUAL
PROPERTY ESTATE.

THE ABILITY OF THE PHYLOGICA'S DELIVERY
TECHNOLOGY TO BREAKTHROUGH THE CELL
PENETRATION BARRIER WITH LARGE MOLECULES,
IS REFLECTED IN THE COMPANY'S NEW TAGLINE:
'BREAKTHROUGH PEPTIDE THERAPEUTICS'.

The initial stages of Phylogica's oncology program will investigate the capacity of peptides in the company's Phylomer libraries to inhibit the activity of transcription factors – the critical proteins that bind DNA and regulate how genes express themselves in cells to switch biological processes on and off.

While transcription factors are among the most validated targets in cancer, they have generally proven intractable to small molecule drugs. However, mounting evidence suggests that larger biologics – including peptides – can be more effective at inhibiting transcription factors. Phylomer technology has already proven well suited to addressing transcription factor targets, generating impressive hit rates and biological activities in a range of biological assays, including animal models. The proven success of Phylogica in both hitting this target class and delivering Phylomers into cells significantly lowers the risk of this approach.

Several Pharma companies have already expressed an interest in partnering with Phylogica to establish the feasibility of using peptide drugs to modulate high-value transcription factor targets. The ultimate goal of the oncology program will be to fully validate the integration of the company's drug delivery and drug discovery platforms. This integration provides rich opportunities to develop our Phylomer libraries in conjunction with a dedicated internal or partnered discovery programs.

STRENGTHENED FINANCIAL POSITION

In January Phylogica was delighted with the successful non-renounceable rights offer that raised \$6.1 million. The offer was fully underwritten by Dr Bernard Hockings, our largest shareholder, and Patersons Securities. In a show of strong support, 87% of the entitlement offer was taken-up by existing shareholders. The capital provided Phylogica with a cash runway of about two years, in order to commercialise its unique drug discovery platform.

The cash position of the Company at 30 June 2014 was A\$3.8 million, with an R&D rebate of a further A\$1.8 million expected by October 2014.

GRANTS TO SUBSIDISE EXPANSION OF PHYLOGICA'S RESEARCH CAPABILITIES

Phylogica was awarded three non-dilutive grants worth over \$650,000 to fund specific drug delivery and drug discovery projects. They include:

- ARC Linkage Grant to Develop Drugs Targeting a Novel Cancer Target: In collaboration with the University of Queensland, Phylogica was awarded a prestigious ARC linkage grant of \$546,420 to develop drugs against a novel cancer target. This project will focus on another transcription factor called SOX18, which acts as a master regulator controlling the spread of cancer throughout the body.
- Two Research in Business Grants: Phylogica has been awarded two grants totalling \$110,000 from the Research in Business scheme – an initiative of Enterprise Connect and the Australian Government. The grants will be used to fund novel applications of the Endosomal Escape Trap, including: discovery of cell-penetrating antimicrobial peptides; discovery of cell-penetrating peptides that can modulate intracellular functions of an important class of target proteins called G-coupled protein receptors (GPCRs). This grant is in collaboration with Professor Kevin Pflieger, of the Harry Perkins Research Institute of the University of Western Australia.

CONTINUING TO STRENGTHEN PHYLOGICA'S INTELLECTUAL PROPERTY PROTECTION

The company continued to develop and expand its intellectual property with the following major patent milestones:

- Completed the filing of a patent application for a method for determining the extent to which cell penetrating peptides such as Phylomers, are able to efficiently deliver their protein cargoes to the cytoplasm of cells. This technology represents one of the first functional assays to be developed for measuring endosomal escape.
- Completed the international PCT (Patent Cooperation Treaty) filing for Phylogica's novel 'Endosomal Escape Trap' technology, which facilitates the isolation of Phylomer peptides capable of escaping from endosomes into the cytoplasm of cells. This technology underpinned the Janssen collaboration and has also attracted considerable interest from other potential Pharma partners.
- Granted a core patent in Australia, Japan and the US covering synthetic Phylomer libraries as 'composition-of-matter' *per se*, regardless of how such libraries are constructed or screened. This patent has priority until 2027, significantly increasing core patent life of Phylomers.



PHYLOGICA RECENTLY ANNOUNCED IT
HAD INITIATED AN IN-HOUSE PROGRAMME
TO DISCOVER PHYLOMER-BASED DRUGS
AGAINST BREAST CANCER.

- Granted two new US patents covering lead Phylomer peptides, for the treatment of acute lung inflammation and in chronic inflammatory diseases such as rheumatoid arthritis and inflammatory bowel disease
- The allowance in September 2014 of a new US patent covering topical applications of Phylomer for the treatment of wounds such as burns. This patent is highly relevant to the applications of Phylomers to burns, such as cosmeceuticals for treatment of sunburn (see below).

OPPORTUNITIES TO OUT-LICENSE GLYCINAMIDE FOR COSMETIC APPLICATIONS

In April 2014, Phylogica received notice that Le Metier Tribeca, the parent company of Le Métier De Beauté, had filed for bankruptcy. In September 2012 Phylogica entered a non exclusive licence with Le Métier Tribeca to formulate and market Glycinamide into a cosmetic product for sunburn. Phylogica is pursuing alternative opportunities for this product and has engaged the licensing specialist consultancy Bio-Link for this purpose. This partnering outreach programme is well-advanced and Phylogica has been very encouraged by the level of interest expressed in the Glycinamide product by several of the leading cosmetics and cosmeceutical companies. This interest has resulted in the multiple follow up meetings, including recent face-to-face discussions with two of the major companies based in Switzerland, which are active in the cosmetics arena.

PHYLOGICA BUILDS ITS INTERNATIONAL PROFILE AT INDUSTRY-FOCUSSED MEETINGS

The recent international biotech conference season saw significant interest from several 'big pharma' and biotech companies – in the potential of Phylogica's technology to open up the intracellular landscape to new drug classes.

CEO Dr Richard Hopkins and Chief Scientific Officer Dr Paul Watt presented to more than 30 companies as part of the industry-leading One-on-One Partnering forum at the 2014 BIO International Convention in San Diego in June.

The meetings also provided an opportunity to promote Phylogica's new oncology program and to obtain valuable feedback regarding the critical end-points required to crystallise big pharma partnering opportunities.

Phylogica was also invited to present at 9 other international conferences focused on novel ways of delivering smart drugs and molecular therapies into target cells – confirming the increasing interest in this space among both the scientific and investment communities.

The events outlined above provide a compelling indication of the broad market interest in Phylogica's technologies, which are clearly competitive with approaches from our peers in the peptide discovery field such as Bicycle Therapeutics, Peptidream and Ra Pharma. This exposure provides an opportunity to further establish the company as a leader among its peers, particularly in intracellular peptide discovery.

FUTURE GUIDANCE

- Genentech: This project is on-track to deliver on the major milestone by the end of 2014. Phylogica remains optimistic that successful delivery on project milestones will lead to an expanded relationship in early 2015.
- The company will continue to accelerate its internal oncology discovery programme, aimed at developing drugs against high-value cancer targets. The company expects to deliver key functional data from its early-stage cell-based screens by Q1 2015, which will then be used to select lead candidates for assessment in relevant animal models of cancer during 2015.
- The unique capabilities of the Endosomal escape trap, the oncology programme and the Phylomer platform in general have attracted considerable interest from potential partners. Phylogica is engaged in discussions with multiple interested parties and remains confident that at least some of these will convert to formal collaborations that will generate additional revenues in the 2015 financial year.
- Progress collaborations with Cambridge University in the UK and the University of Queensland to develop and commercialise a Phylomer-based phenotypic screening platform.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

The directors present their report on the consolidated group, comprising Phylogica Limited (referred to in these financial statements as "the Group" or "Phylogica") and its wholly owned subsidiary, together with the financial report for the year ended 30 June 2014 and the audit report thereon.

1. DIRECTORS

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

NON-EXECUTIVE

Dr Doug Wilson 77



MB, ChB, FRACP, FRCPA
Non-Executive Chairman

Appointed as a Director on 10 December 2007. Transitioned from Executive Chairman to Non-Executive Chairman on 1 November 2012. Current term ends November 2014.

Dr Wilson is a New Zealand medical graduate with post graduate experience in London at St Thomas Hospital Medical School, and at Walter and Eliza Hall Institute Melbourne.

Dr Wilson joined the international pharmaceutical industry and became Senior Vice president for Boehringer Ingelheim for Medicine and Regulatory Affairs in the USA, responsible for all dealings with FDA. He moved to Ingelheim and had the same responsibilities world-wide. Dr Wilson headed the company's International Labelling Committee, deputy head of the International Medical Committee which oversaw all drugs in clinical development globally. During his tenure he saw ten drugs approved in the USA.

Dr Wilson is now a consultant and is on the board of a number of other companies and consults widely on biotech and pharmaceutical issues.

Mr Bruce McHarrie 56



BCom FCA GAICD
Non-Executive Director

Appointed as a Director on 9 August 2002. Current term ends November 2015.

Mr McHarrie has been associated with the biotechnology industry for almost 20 years. He is currently the Director of Strategic Projects at the Telethon Kids Institute (formerly Telethon Institute for Child Health Research) (the Institute). Mr McHarrie joined the Institute in 1999 initially as the Chief Financial Officer after returning to Perth from the United Kingdom. The role evolved to become Director of Operations, which reflected the broader operational responsibilities that the position encompassed. In response to a number of very significant projects in progress at the Institute, Mr McHarrie took on the strategic projects portfolio at the beginning of 2014.

In the United Kingdom Mr McHarrie was Assistant Director in the Bioscience Unit at Rothschild Asset Management. The Bioscience Unit focused on investing in biotechnology and healthcare companies from the early start-up stage through to the publicly listed stage. In this capacity Mr McHarrie was invited to join the board of a number of United Kingdom based biotechnology companies.

Prior to joining Rothschild Asset Management, Mr McHarrie was with Coopers and Lybrand in London servicing a client base primarily in the financial services industry. He holds a Bachelor of Commerce Degree from the University of Western Australia, qualified as a Chartered Accountant with Deloitte and is a graduate of the Australian Institute for Company Directors.

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



Mr Jeremy Curnock Cook 64



MA
Non-Executive Director

Appointed as a Director on 29 February 2012. Current term ends November 2014.

Mr Curnock Cook is an experienced entrepreneur, fund manager, executive and non-executive director in the life science sector. Mr Curnock Cook is currently Executive Chairman of International Bioscience Managers Limited.

He was formerly the head of the life science private equity team at Rothschild Asset Management in the UK and an active investor in the Australian life science sector. At Rothschild, Mr Curnock Cook was responsible for the launch of the first dedicated biotechnology fund for the Australian market.

Over his 40-year career, Mr Curnock Cook has specialised in creating value in emerging biotech enterprises, through active participation with management. He has served on over 40 Boards in various roles, including Chairman, of private and public biotechnology companies listed on NASDAQ, LSE, TSX and ASX.

Mr Curnock Cook serves as a non-executive director on the board of Australian ASX listed company, Avita Medical Ltd.

Mr Curnock Cook received his MA in Natural Sciences from Trinity College in Dublin, Ireland.

Dr Bernard Hockings 66



R.F.D., MD (WA),
M.B.B.S (WA),
F.R.A.C.P., F.C.S.A.N.Z
Non-Executive Director

Appointed as a Director on 23 January 2014. Current term ends November 2014.

Dr Hockings is an Interventional Cardiologist in Private Practice in Western Australia and is a Clinical Associate Professor in Medicine at the University of Western Australia. Previously he was Director of the Coronary Care Unit at Royal Perth Hospital, Chairman of the Medical Advisory Committee at the Mount Hospital and Director of Health Reserves (WA) for the Royal Australian Air Force.

Dr Hockings has a lifelong interest in medical research. His Doctoral Thesis involved Vasodilator Therapy in the treatment of Heart Failure. He has been closely involved with clinical teaching throughout his career. Dr Hockings is now a major shareholder in Phylogica.

EXECUTIVE

Dr Richard Hopkins 47



BSc (Hons), PhD
Chief Executive Officer
(from 19 July 2013)
Chief Operating Officer
(to 19 July 2013)

Appointed as a Director on 19 July 2013. Current terms ends November 2016.

Dr Hopkins was a founder of Phylogica. His most recent research is focussed on engineering peptide leads for drug development. He has published over 20 peer reviewed papers and is a co-inventor on over 10 patent applications, several of which have been issued in the US and Europe.

Previously, Dr Hopkins carried out postdoctoral research in yeast genetics at the Telethon Institute for Child Health Research, Perth, Western Australia. His research focussed on the development of a novel class of peptides, trademarked by Phylogica as Phylomers® and the methods to integrate them into various high throughput screening platforms such as yeast- two-hybrid and phage display.

Dr Hopkins has a BSc (Hons) and completed a PhD in Molecular Parasitology.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

Dr Paul Watt 49



BSc(Hons) D Phil
Chief Scientific Officer
(from 19 July 2013)
Chief Executive Officer
(to 19 July 2013)

Appointed a Director on 9 August 2002. Resigned as a Director on 19 July 2013.

Dr Watt is a leading graduate from The University of Western Australia. He completed his doctorate in Molecular Biology at Oxford University before taking up postdoctoral appointments in yeast genetics at Harvard and Oxford Universities. Working in genomic instability and cancer research, Dr Watt discovered three novel genes, including the yeast homologue of the human Bloom's and Werner's syndrome genes involved in cancer susceptibility. A member of faculty at the Telethon Kids Institute, Dr Watt was appointed adjunct Professor at the School of Paediatrics and Child Health of the University of Western Australia. Dr Watt has published more than 50 peer reviewed scientific papers, is an inventor on 23 patents and currently acts as the Chief Scientific Officer for Phylogica, of which he was a cofounder.

Mr Nick Woolf 46



MA (Oxon) FCCA
Chief Financial Officer
(to 19 July 2013).

Appointed as a Non-Executive Director on 22 April 2010 and transitioned to Executive Director on 8 October 2010. Resigned as a Director and CFO 19 July 2013.

Unless otherwise indicated, all Directors held their position as a Director throughout the entire year and up to the date of this report, and held no directorships in the past three years in other ASX listed entities.

2. COMPANY SECRETARY

Mr Graeme Boden 65



BEC(Hons) FAICD
Company Secretary
Chief Financial Officer
(from 19 July 2013)

Mr Boden is an experienced business executive with more than 35 years in senior corporate or financial roles, particularly in the planning and evaluation function of the resources industry and in the finance and administration function of a range of industries, including resources, biotechnology, medical devices and pharmaceuticals. He has more than 25 years experience as a Director or Secretary of ASX listed companies.

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



3. DIRECTORS' MEETINGS

The number of directors' meetings (including meeting of committees of directors) and the number of meetings attended by each of the directors of the company during the financial year are:

	Directors' Meetings		Audit Committee		Nomination Committee		Remuneration Committee	
	A	B	A	B	A	B	A	B
D Wilson	15	15	2	2	1	1	4	4
B McHarrie	15	14	2	2	1	1	4	4
J Curnock Cook	15	12	2	1	1	1	4	3
B Hockings	6	6	-	-	1	1	-	-
R Hopkins	14	14	-	-	1	1	-	-
P Watt	1	1	-	-	-	-	-	-
N Woolf	1	1	-	-	-	-	-	-

A = Number of meetings held while in office

B = Meetings attended

4. PRINCIPAL ACTIVITIES

The principal activity of the Company during the financial year was the provision of drug discovery services to the international pharmaceutical industry utilising the Company's Phylomer_ peptide libraries and proprietary screening capabilities.

5. OPERATING RESULTS

The consolidated operating loss after tax for the financial year ended on 30 June 2014 was \$3,257,695 (2013 loss: \$3,439,624).

The accounting standards do not permit the capitalisation of development expenditure in circumstances where the company cannot demonstrate sustainable revenue generation derived from the results of the expenditure. Research expenditure must be expensed under Australian Accounting Standards. The expenditure incurred in relation to obtaining and maintaining patent protection is allowed to be capitalised under the Standards but the Company has adopted a policy of expensing such expenditure as it is incurred.

Since incorporation, Phylogica has raised \$42.2 million in capital, reduced to \$39.7 million after netting capital raising fees. From this amount the following expenditures have been undertaken (all amounts \$ million):

Research & Development:	Prior to 2012	2013	2014	Total
Contract Research	12.99	2.43	2.67	18.09
Personnel (allocation)	5.36	0.78	0.56	6.70
Laboratory Consumables	3.43	0.55	0.58	4.56
	21.78	3.76	3.81	29.35
IP Maintenance	2.51	0.28	0.37	3.16
	24.29	4.04	4.18	32.51



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

6. OPERATING AND FINANCIAL REVIEW

6.1 BUSINESS STRATEGY

Phylogica is a specialist drug discovery company offering peptide discovery services to the pharmaceutical industry in exchange for upfront licence fees, milestone payments and a share in revenue arising from any drugs discovered as a result of the Company's research.

The Company also aims to add enterprise value through internal discovery programmes and enhancements to its intellectual property portfolio, which increases potential for further licensing deals and may also make the Company an attractive merger or acquisition candidate.

6.2 OPERATIONS

During the 2014 financial year the Company pursued its business strategy through the following activities:

In conjunction with Janssen, Phylogica made significant progress towards validation of one of its proprietary technologies – the Endosomal Escape Trap (EET), to discover novel cell penetrating peptides. The EET is a unique technology that enables Phylogica to screen billions of Phylomers for the relatively rare peptide that can escape from endosomes to deliver its cargo more efficiently into cells. This is a critical first step towards identifying peptides that can deliver drugs against intracellular targets.

In February 2014, Phylogica highlighted several key milestones achieved with the Endosomal Escape Trap. These included;

- Identifying Phylomers that improved delivery of a protein cargo inside cells by 25-50 times.
- Establishing that the EET yielded an unprecedented hit-rate for functionally active peptides.
- Observing high sequence and structural diversity in the pool of validated hits suggesting a range of cell- uptake mechanisms.
- Showing Phylomers delivering a range of therapeutic cargoes inside cells including toxins and the Janssen cargo.
- Collecting information across populations of novel cell penetrating peptides provides Phylogica with unique insight and hence intellectual property into the requirements for cell penetration.

These exciting data firmly established Phylogica as a global leader in the field of intracellular drug delivery. Having validated its novel platform for discovery of functionally active delivery reagents the company is actively pursuing expressions of interest from multiple potential partners.

In June 2014, Phylogica announced that Janssen Biotech would not extend its collaboration despite Phylogica achieving the technical milestones required for the project. However, Janssen has indicated continuing interest in Phylogica's technology and in its new Oncology Program in particular. Phylogica is maintaining discussions with Janssen in the expectation that its emerging oncology research will reengage the collaboration.

Based on the successful technical outcome with the Endosomal Escape Trap, Phylogica has taken the strategic decision to combine the company's drug delivery platform with a broader program to investigate the efficacy of peptide-based drugs against high-value cancer targets. While the initiative will initially focus on breast cancer, the targets chosen are also relevant to other common malignancies, including colon, lung and pancreatic cancers.

The initial stages of Phylogica's Oncology Program will investigate the capacity of peptides in the company's Phylomer libraries to inhibit the activity of transcription factors – the critical proteins that bind DNA and regulate how genes express themselves in cells.

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



Patents:

The company continued to develop and expand its intellectual property with the following patents:

- Completed the filing of a patent application for a method for determining the extent to which cell penetrating peptides such as Phylomers are able to efficiently deliver their protein cargoes to the cytoplasm of cells. This technology represents one of the first functional assays to be developed for measuring endosomal escape.
- Completed the PCT filing for Phylogica's novel 'Endosomal Escape Trap' technology, which facilitates the isolation of Phylomer peptides capable of escaping from endosomes into the cytoplasm of cells. This technology underpins the Janssen collaboration and has also attracted considerable interest from other potential Pharma partners.
- Granted a core patent in Australia, Japan and the US covering synthetic Phylomer libraries as 'composition- of-matter' *per se*, regardless of how such libraries are constructed or screened. This patent has priority until 2027, significantly increasing core patent life of Phylomers.
- Granted two new US patents covering lead Phylomer peptides, for the treatment of acute lung inflammation and in chronic inflammatory diseases such as such as rheumatoid arthritis and inflammatory bowel disease.

In April 2014, Phylogica received notice that Le Metier Tribeca, the parent company of Le Métier De Beauté, had filed for bankruptcy. In September 2012 Phylogica entered a non-exclusive licence with Le Métier Tribeca to formulate and market Glycinamide into a cosmetic product for sunburn. Phylogica is pursuing alternative opportunities for this product and has engaged Bio-Link for this purpose. This outreach programme is well- advanced and Phylogica has been very encouraged by the level of interest expressed in the Glycinamide product.

Phylogica was awarded three non-dilutive grants worth approximately \$650,000 to fund specific drug delivery and drug discovery projects. They include:

- ARC Linkage Grant to Develop Drugs Targeting a Novel Cancer Target: The University of Queensland, with Phylogica as a commercial collaborator, was awarded a prestigious ARC linkage grant of \$546,420 to develop drugs against a novel cancer target. This project will focus on another transcription factor called SOX18, which acts as a master regulator controlling the spread of cancer throughout the body.
- Research in Business Grant: Phylogica is benefiting from two grants totalling \$100,000 from the Research in Business scheme – an initiative of Enterprise Connect and the Australian Government. The first grant was awarded directly to Telethon Institute for Kids in conjunction with Phylogica and will be used to explore novel applications of the Endosomal Escape Trap to discover antimicrobial peptides. The second grant was awarded to the University of Western Australia in conjunction with Phylogica. This grant subsidises the cost of Phylogica contracting the UWA-based scientist who will work on a project aimed at discovering cell- penetrating peptides that can modulate a class of intracellular proteins called G-coupled protein receptors (GPCRs); and new approaches to modulating GPCRs via their intracellular components.

Phylogica staff were invited to present at several key international biotechnology conferences in the USA and Europe.

6.3 FINANCIAL POSITION

In January Phylogica was delighted with the successful non-renounceable rights offer that raised \$6.1 million. The offer was fully underwritten by Bernard Hockings, our largest shareholder. In a show of strong support 87% of the entitlement offer was taken-up by new and existing shareholders. The capital provided is being applied to the further development of its unique drug discovery platform.

The cash position of the Company at 30 June 2014 was A\$4.0 million, with an R&D rebate of a further A\$1.7 million expected by October 2014.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

6.4 FUTURE PROSPECTS

Phylogica has made significant progress with its novel drug delivery platform and is now well poised to take on the challenge of opening up the intracellular landscape to new drug classes. Phylogica's technology is well regarded by the pharmaceutical industry and its peers in the peptide drug discovery space.

Upcoming milestones/achievements include:

- In August, Phylogica was delighted to announce it had entered into a collaboration with Genentech, a subsidiary of the Roche group of companies. Phylogica looks forward to delivering on the current project objectives, which could lead an expanded relationship with Genentech.
- The Company will continue to progress and validate its unique 'Endosomal Escape Trap' platform for discovery of novel cell penetrating peptides that can deliver therapeutic cargoes inside cells. In addition, the company looks forward to progressing its early-stage Oncology programme, aimed at developing drugs against high-value cancer targets. Successful delivery on this programme promises to unlock substantial value in the Phylomer platform is successful.
- The unique capabilities of the Endosomal escape trap, the Oncology programme and the Phylomer platform in general have attracted considerable interest from potential partners. Phylogica is engaged in discussions with a number of interested parties and remains optimistic that at least some of these will convert to formal collaborations that will generate additional revenues in the 2015 financial year.
- Work continues to optimise the quality of the Phylomer libraries by incorporating new features such as the ability to generate Macrocyclic libraries that should further improve the drug-like properties of the peptides. Phylogica expects that these capabilities will unlock further value in the platform.
- Phylogica will initiate self-funded screens against high value commercial targets.
- Collaborations will be progressed with Cambridge University in the UK and University of Queensland to develop and commercialise a Phylomer-based phenotypic screening platform.

In common with a range of companies engaged in research and development or resources exploration, Phylogica arrives at each balance date with a cash balance which is less than required to meet its forecast requirement for the coming year. As alluded to previously, the Company expects to be able to fund its continuing operations by a combination of increased revenue, a corporate transaction, equity raising or expenditure reduction as required.

7. SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS

The Company completed the conversion of 16,000 converting notes by the issue of 140,350,876 ordinary shares and 93,567,252 PYCOA listed options with an exercise price of \$0.09 per share and an expiry date of 30 June 2016. Subsequent to the conversion of the notes the total issued capital of the Company became 601,241,620 ordinary shares. For further details on this conversion see note 17.

The Company issued 400,827,747 shares upon the completion of a fully underwritten entitlement issue at a price of \$0.015 per share to raise \$6,012,417.

The Company cancelled a total of 6,000,000 loan funded shares upon the cessation of employment of an executive director.

8. DIVIDENDS

No dividends have been paid or declared by the Company since the end of the previous financial year.

9. EVENTS SUBSEQUENT TO REPORTING DATE

There are no matters or circumstances that have arisen since the end of the financial year that have significantly affected or may significantly affect the operations of the Consolidated Entity, the results of those operations or the state of affairs of the Consolidated Entity, in future financial years.

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



10. DIRECTORS' INTERESTS

The relevant interest of each director in the shares and options over shares issued by Phylogica as notified by the directors to the Australian Securities Exchange in accordance with Section 205G(1) of the Corporations Act 2001, at the date of this report is as follows:

Director	Ordinary Shares	Options
D Wilson	1,711,989	584,795
B McHarrie	3,304,576	-
J Curnock Cook	-	-
B Hockings	225,406,101	77,844,256
R Hopkins	16,487,611	504,262

11. INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

11.1 DIRECTORS' AND OFFICERS' INDEMNITY

The Group has agreed to indemnify each Director and the Company Secretary (Officers) against all liabilities or loss (other than the Group or a related body corporate) that may arise from their position as Officers of the Group and its controlled entities, except where the liability arises out of conduct involving a lack of good faith, or indemnification is otherwise not permitted under the Corporations Act. The indemnity stipulates that the Group will meet the full amount of any such liabilities, including costs and expenses, and covers a period of seven years after ceasing to be an Officer of the Group.

The Group has also indemnified the current directors and certain members of its senior management for all liabilities and loss (other than the Group or a related body corporate) that may arise from their position, except where the liability arises out of conduct involving lack of good faith or indemnification is otherwise not permitted under the Corporations Act.

The Group has executed deeds of indemnity, access and insurance in favour of each Officer of the Group.

11.2 DIRECTORS' AND OFFICERS' INSURANCE

The Group has paid insurance premiums for one of year cover in respect of directors' and officers' liability insurance contracts, for Officers of the Group. The insurance cover is on standard industry terms and provides cover for loss and liability for wrongful acts in relation to the relevant person's role as an Officer, except that cover is not provided for loss in relation to Officers gaining any profit or advantage to which they were not legally entitled, or Officers committing any criminal, dishonest, fraudulent or malicious act or omission, or any knowing or wilful violation of any statute or regulation. Cover is also only provided for fines and penalties in limited circumstances and up to a small financial limit.

The insurance does not provide cover for the independent auditors of the Group or of a related body corporate of the Group.

In accordance with usual commercial practice, the insurance contract prohibits disclosure of details of the nature of the liabilities covered by the insurance, the limit of indemnity and the amount of the premium paid under the contract.

12. NON-AUDIT SERVICES

During the year, HLB Mann Judd, the Group's auditor, did not perform other services in addition to its statutory duties.

Details of the amounts paid or payable to HLB Mann Judd and its related entities for audit services provided during the year are set out below.

	\$
Audit and review of financial reports	31,495



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

13. INTERESTS IN CONTRACTS OR PROPOSED CONTRACTS WITH THE COMPANY

There are no contracts or proposed contracts with the Company in which any director has an interest, other than a contract of executive employment for Dr R Hopkins.

Details of this contract are outlined in section 20.8 of this report.

14. OPTIONS AND UNISSUED SHARES UNDER CONVERTIBLE SECURITIES

At the date of this report, ordinary shares of the Company under option totalled 172,782,280 exercisable at various dates on or before 31 March 2016 (2013: 79,215,028 options exercisable at various dates on or before 31 March 2016).

Number of options	Exercisable at \$0.035	Exercisable at \$0.09	Total
Issued	8,125,000	164,657,280	172,782,280
Vested	8,125,000	164,657,280	172,782,280

These converting securities do not entitle the holder to participate in any share issue of the Company or any other body corporate.

15. ENVIRONMENTAL REGULATION AND PERFORMANCE

The Company does not hold any permits in relation to environmental discharge and does not handle or store hazardous materials.

16. NOMINATION COMMITTEE

The full Board carries out the function of the nomination committee. During the reporting period, the Board met once to consider matters as the Nomination Committee. The committee members' attendance record is disclosed in the table of directors' meetings on page 15.

17. AUDIT COMMITTEE

The audit committee during the year was comprised of:

Mr B McHarrie	Non-Executive (Chairman)
Dr D Wilson	Non-Executive
Mr J Curnock Cook	Non-Executive

The audit committee met twice during the reporting period. The committee members' attendance record is disclosed in the table of directors' meetings on page 15.

The members of the audit committee possess financial expertise by virtue of their academic qualifications or career history in executive roles. Details of their qualifications and experience are set out earlier in the Directors' report.

18. REMUNERATION COMMITTEE

The remuneration committee reviews and makes recommendations to the board on remuneration arrangements and policies applicable to the executive officers of the company and directors themselves. Its responsibility includes employee share option plan administration and entitlements and incentive performance arrangements.

Details of remuneration, including the Company's policy on remuneration, are contained in the "Remuneration Report" which forms of part of the Directors' report.

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



The members of the remuneration committee during the year were:

Mr B McHarrie	Non-Executive (Chairman)
Dr D Wilson	Non-Executive
Mr J Curnock Cook	Non-Executive

The remuneration committee met four times during the year. The committee members' attendance record is disclosed in the table of directors' meetings on page 15.

The remuneration committee charter is available on the company's website.

19. OTHER

19.1 SKILLS, EXPERIENCE, EXPERTISE AND TERM OF OFFICE OF EACH DIRECTOR

A profile of each director containing the skills, experience, expertise and term of office of each director is set out earlier in the Directors' report.

19.2 IDENTIFICATION OF INDEPENDENT DIRECTORS

In considering independence of directors, the Board refers to the criteria for independence as recommended by ASX. To the extent that it is necessary for the Board to consider issues of materiality, the Board refers to the thresholds for qualitative and quantitative materiality as adopted by the Board and contained in the Statement of Board and Management Functions, which is disclosed in full on the Company's website.

Applying the independence criteria, Mr Curnock Cook is the only one of the present directors who is classified as independent.

19.3 STATEMENT CONCERNING AVAILABILITY OF INDEPENDENT PROFESSIONAL ADVICE

If a director considers it necessary to obtain independent professional advice to properly discharge the responsibility of his office as a director, then, provided the director first obtains approval for incurring such expense from the chairperson, the Company will pay the reasonable expenses associated with obtaining such advice.

19.4 CONFIRMATION WHETHER PERFORMANCE EVALUATION OF THE BOARD AND ITS MEMBERS HAVE TAKEN PLACE AND HOW CONDUCTED

An evaluation of the performance of the board and its members was last carried out during the 2012 reporting period. The evaluation process was an internal self- assessment based on questions and analysis of answers with round table discussions. All members of the Board participated in the assessment.

19.5 EXISTENCE AND TERMS OF ANY SCHEMES FOR RETIREMENT BENEFITS FOR NON-EXECUTIVE DIRECTORS

There are no terminations or retirement benefits for non-executive directors, other than the statutory superannuation contribution paid, where applicable, in relation to directors' fees.

20. REMUNERATION REPORT - AUDITED

Remuneration is referred to as compensation throughout this report.

20.1 PRINCIPLES OF COMPENSATION

Key management personnel have authority and responsibility for planning, directing and controlling the activities of the Company, including directors of the Company and other executives. Key management personnel includes all directors, the company secretary and specific executives of the Company.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

Compensation levels for key management personnel of the Company are set competitively to attract and retain appropriately qualified and experienced directors and senior executives. The remuneration committee has researched information from companies of similar size or stage of development in the technology sector to assess the level of compensation which would be competitive, receiving this information by way of a report from independent remuneration consultants.

The compensation structures for executives are designed to attract suitably qualified candidates, reward the achievement of strategic objectives and achieve the broader outcome of the creation of value for shareholders. The compensation structures take into account the executives' capability and experience, level of responsibility and ability to contribute to the Company's performance, including, in particular, the establishment of revenue streams and growth in the Company's share price.

Compensation packages include a mix of fixed and variable compensation and short-and long-term performance based incentives.

20.2 FIXED REMUNERATION

Fixed compensation consists of a base salary (calculated on a total cost basis, including any fringe benefits tax related to employee benefits) as well as employer contributions to superannuation funds.

Compensation levels are reviewed annually by the remuneration committee through a process that considers individual and company achievement.

20.3 PERFORMANCE LINKED REMUNERATION

Performance linked compensation includes short term incentives (STI), in the form of cash bonuses paid upon the achievement of predetermined Key Performance Indicators (KPI), and long term incentives (LTI) provided as shares under a Loan Funded Share Plan. In the case of Executive Directors, the number and conditions of the options or loan funded shares are approved by the shareholders in general meeting.

20.4 SHORT TERM INCENTIVE BONUS (STI)

The remuneration committee has set KPIs in conjunction with each of the Executive Directors and senior management.

Each of the Company's employees is set KPIs and a bonus is payable on achievement of these KPIs. This is either an amount equal to between 0% and 25% of the base salary or a fixed sum per KPI determined at the beginning of the financial year. The objectives include such targets as successful negotiation of commercial deals; delivering on the research objectives specified by a pharmaceutical customer; achieving project milestones for internal programmes; publications of significance in scientific journals; and successful fund raising.

At the end of the year, the remuneration committee assesses the extent to which KPIs have been achieved and the aggregate achievement of all set KPIs for the individual to determine the bonus to be paid.

No bonuses were paid in relation to the 2013 and the 2014 financial years.

20.5 LONG TERM INCENTIVES (LTI)

The Employee Share Option Plan (ESOP) was established during the 2006 financial year and is open to all employees and contractors. The ESOP was renewed at the annual general meeting held 30 November 2010. Options are granted for no consideration and have a three year term. One half of those options allocated will vest immediately and, unless agreed by the Directors, one half will vest on the subsequent anniversary of issue. During the year, no options were granted under the ESOP (2013: 8,125,000).

During June 2011 the Board resolved to implement a Loan Funded Share Plan ("Plan") for Key Management Personnel. The Loan Funded Share Plan was approved by shareholders at the annual general meeting of held on 24 November 2011. Participants of the plan acquire ordinary shares at market value and the purchase price of the shares will be 100% funded by a loan provided by the Company. Repayment of the loan will be made from sale of the shares and the recourse for repayment will be limited to the shares. The shares will be subject to vesting conditions which will, in turn,

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



be subject to continuing employment with the Company. If the vesting conditions are not met, the Plan shares will be reacquired by the Company and the loan offset against the share value so the participants receive no benefit from the Plan for unvested shares.

20.6 SHORT-TERM AND LONG-TERM INCENTIVE STRUCTURE

The Company has not established a causal relationship between compensation structure and shareholder returns. The remuneration committee and the directors consider that the Company's progress to date and external remuneration levels provide support for the premise that the compensation structure is appropriate, given the objectives set out earlier in this report.

20.7 CONSEQUENCES OF PERFORMANCE ON SHAREHOLDERS' WEALTH

The Board has regard to a broad range of factors in considering the Company's performance and how best to generate shareholder value. These include financial factors, securing new drug discovery partnerships and others that relate to meeting the objectives of existing discovery alliances, scientific progress of the Company's in-house projects, grants awarded, staff development etc. The Board has some, but not absolute regard to the Company's result and cash consumption during the year. It does not utilise earnings per share as a performance measure nor does it contemplate consideration of any dividends in the short to medium term, given that efforts are being expended to build the business and generate self-sustaining revenue streams. The Company is of the view that any adverse movement in the Company's share price should not be taken into account in assessing the performance of employees, unless such a measure is agreed with the executive as a KPI.

20.8 SERVICE AGREEMENTS

At 30 June 2014, the senior executives of the Company who are full time employees, had conditions of employment as set out below. Either party may terminate their agreement without cause by giving written notice of three months. There is no termination fee payable other than during the term of notice.

Name	Dr Richard Hopkins	Dr Paul Watt
Position	Chief Executive Officer	Chief Scientific Officer
Term Expiring	30 June 2014	30 June 2014
Package	\$250,000 pa	\$220,500 pa
Shares ¹	6,000,000	9,000,000

¹ Loan Funded Shares issued 3 April 2012 after approval at the annual general meeting held on 24 November 2011 (see note 16).

Set out below are the details of the draft executive contract extensions to be finalised.

Name	Dr Richard Hopkins	Dr Paul Watt
Position	Chief Executive Officer	Chief Scientific Officer
Term Expiring	2018	2018
Implementation Date	1 July 2014	1 July 2014
Package	\$250,000 pa	\$220,500 pa
Shares ¹	6,000,000	9,000,000

Dr Doug Wilson, is a contractor and transitioned from Executive Chairman to Non-Executive Chairman on 1 November 2012, with a fixed fee set at \$70,000 per annum.

The Company Secretary is a contractor with no financial commitment by the Company other than a monthly fee, payable in arrears at hourly rates, for services rendered by himself and other employees of the service company.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

20.9 NON-EXECUTIVE DIRECTORS

The aggregate remuneration of all non-executive directors was set at \$200,000 per annum at the annual general meeting held on 26 November 2004. The base fee for a non-executive director has been \$40,000 per annum since 1 July 2011. The Company makes contributions at the statutory minimum rate to superannuation funds nominated by directors, in addition to the base fee.

Directors' fees cover all main board activities and committee memberships.

20.10 EQUITY INSTRUMENTS

20.10.1 OPTIONS

All options refer to options over ordinary shares of Phylogica Limited which are exercisable on a one-for-one basis.

(a) Options and rights over equity instruments granted as compensation

During the reporting period no options over ordinary shares in the Company were granted as compensation to key management personnel (2013: 5,250,000).

No options vested during the reporting period ending 30 June 2014. Details of options in relation to the previous reporting period are as follows:

	Number of options outstanding at 30 June 2013	Grant date	Fair value per option at grant date (\$)	Exercise price per option (\$)	Expiry date	Number of options vested during 2013
Directors						
Dr P Watt	2,250,000 ⁽¹⁾	22 November 2012	\$0.022	-	2 December 2013	-
Mr N Woolf	1,500,000 ⁽¹⁾	22 November 2012	\$0.022	-	2 December 2013	-
Executives						
Dr R Hopkins	1,500,000 ⁽¹⁾	22 November 2012	\$0.022	-	2 December 2013	-

(1) Zero priced Incentive Options were approved at the 2012 annual general meeting and expired 2 December 2013 without meeting the vesting conditions.

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

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

(c) Exercise of options granted as compensation

During the reporting period, no options previously granted as compensation were exercised (2013: Nil).

(d) Analysis of options and rights over equity instruments granted as compensation

Details of vesting profiles of the options granted as remuneration to executive directors of the Company and the named Company executive are detailed as follows:

	Options Granted		Vested in year (%)	Forfeited in year (%)	Financial years in which grant vests	Value yet to vest	
	Number	Date				Minimum (\$)	Maximum (\$)
Directors							
Dr R Hopkins	1,500,000	22 November 2012	-	100	1 July 2012	-	-
Mr N Woolf	1,500,000	22 November 2012	-	100	1 July 2012	-	-
Executives							
Dr P Watt	2,250,000	22 November 2012	-	100	1 July 2012	-	-

Directors' Report

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(e) Analysis of Movements in options

The only movements during the reporting period of options over ordinary shares in the Company held by Company director's and other Key Management Personnel were the expiry of options which were unexercised at the expiry date. These options did not meet the exercise conditions required prior to the expiry date.

Number of Options	Exercise Price	Expiry Date
5,250,000	Nil	2 December 2013

20.10.2 LOAN FUNDED SHARE PLAN

During June 2011 the Board resolved to implement a Share Funded Loan Plan ("Plan") for Key Management Personnel. Offers of allocations under the plan were made to three key management personnel on 3 June 2011 and acceptances were received from all key management personnel. The plan and the allocations to directors, P Watt and N Woolf, were approved at the general meeting of shareholders; the allocation to the third key management person did not require shareholder approval.

The offers accepted were as follows:

- (a) Term of the loan: 7 years (3 June 2018) or cessation of employment, whichever is earlier.
- (b) Purchase price of shares funded by loan is 6.4 cents.
- (c) 33% of the shares vested on 3 June 2014, 33% on 3 June 2015 and 34% on 3 June 2016.
- (d) Allocations have been made to:

Dr P Watt:	9,000,000 shares, \$576,000 loan
Mr N Woolf:	6,000,000 shares, \$384,000 loan
Dr R Hopkins	6,000,000 shares, \$384,000 loan

A valuation of these shares at the date of shareholder approval, using the Black & Scholes option pricing model totalled \$831,600, which is being allocated over the vesting period as a share based payment. The charges as remuneration of these executives in previous financial years, amounted to \$291,666. The charge incurred for the 2013-14 financial year was \$170,691.

Mr N Woolf ceased employment with the Company on 31 July 2013. Consequently under the terms of the loan funded share plan the 6,000,000 shares awarded to him were cancelled.

20.11 PAYMENTS TO PERSONS BEFORE TAKING OFFICE

During the reporting period no payment was made to a person before the person took office as part of the consideration for the person agreeing to hold office.

20.12 DIRECTORS' AND EXECUTIVE OFFICERS' REMUNERATION

Details of the nature and amount of each major element of remuneration of each director and each of the executives of the Company (Key Management Personnel) are as set out on the following page.



Directors' Report

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DIRECTORS' AND EXECUTIVE OFFICERS' REMUNERATION

Directors	Year	Short Term Benefits		Long Term Benefits	Post-Employment Benefits	Share-Based Payments	Total	Proportion of remuneration performance related	Value of Options/ Loan Shares as proportion of Remuneration
		Salary & Fees	Cash Bonus						
		\$	\$	\$	\$	\$	\$	%	%
Non-Executive									
Mr B McHarrie	2014	40,000	-	40,000	-	3,700	-	43,700	-
	2013	40,000	-	40,000	-	3,600	-	43,600	-
Mr J Curnock Cook	2014	43,700	-	43,700	-	-	-	43,700	-
	2013	43,600	-	43,600	-	-	-	43,600	-
Dr Bernard Hockings (Appointed 23 Jan 2014)	2014	19,266	-	19,266	-	-	-	19,266	-
	2013	-	-	-	-	-	-	-	-
Dr D Wilson - Chairman (Transitioned from Executive Chairman 31 Oct 2013)	2014	70,000	-	70,000	-	-	-	70,000	-
	2013	82,000	-	82,000	-	-	-	82,000	-
Executive									
Dr R Hopkins - Chief Executive Officer (Appointed 19 July 2014)	2014	248,652	-	248,652	4,865	17,790	68,276	339,583	20.1
	2013	-	-	-	-	-	-	-	-
Dr P Watt - Chief Executive Officer (Resigned 19 July 2013)	2014	-	-	-	-	-	-	-	-
	2013	315,000	-	315,000	8,231	16,470	110,526	450,227	24.5
Mr N Woolf - Chief Financial Officer (Resigned 19 July 2013)	2014	82,887	-	82,887	-	1,482	-	84,369	-
	2013	220,500	-	220,500	2,166	16,470	73,684	312,820	23.6
Management									
Dr P Watt - Chief Scientific Officer (Appointed 19 July 2013)	2014	248,444	-	248,444	8,619	17,790	102,415	377,268	27.15
	2013	-	-	-	-	-	-	-	-
Dr R Hopkins - Chief Scientific Officer (Transitioned to CEO 19 July 2014)	2014	-	-	-	-	-	-	-	-
	2013	220,500	-	220,500	8,676	16,470	73,684	319,330	23.1
Total Key Management Personnel	2014	752,949	-	752,949	13,484	40,762	170,691	977,886	-
	2013	921,600	-	921,600	19,073	53,010	257,894	1,251,577	20.6
Secretary									
Mr G Boden (3)	2014	145,626	-	145,626	-	-	-	145,626	-
	2013	101,601	-	101,601	-	-	-	101,601	-

Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014



Notes in relation to the table of directors' and executive officers' remuneration

- (1) The fair values of the options and loan funded shares are calculated at the date of grant using a Black-Scholes pricing model and allocated to each reporting period in accordance with the vesting profile of the options/ loan funded shares. The value recognised is the portion of the fair value of the options or loan funded shares allocated to the reporting period. In valuing the options and loan funded shares, market conditions have been taken into account.
- (2) The Company pays an insurance premium for company reimbursement and directors' and officers' liability insurance as a combined amount. The portion of the premium which relates to directors and officers has not been included as part of remuneration.
- (3) Payments made to Boden Corporate Services Pty Ltd (BCS) include time spent on Company activities, including accounting and administration by G Boden and other employees of BCS.

20.13 ANALYSIS OF BONUSES INCLUDED IN REMUNERATION

No bonuses were awarded in relation to the 2014 financial year as the key performance criterion of financial sustainability was not met.

20.14 MOVEMENTS IN SHARE AND OPTIONS HOLDINGS

Movements in Key Management Personnel equity holdings during the period are now redefined to be disclosed in the remuneration report.

20.14.1 OPTIONS OVER EQUITY INSTRUMENTS

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

	Balance 1 July 2013	Granted As Compensation	Exercised	Other Changes	Balance 1 July 2014	Vested During The Year	Vested & Exercisable 30 June 2014
Directors							
Dr D Wilson	-	-	-	584,795	584,795	584,795	584,795
Dr R Hopkins ⁽¹⁾	211,864	-	-	292,398	504,262	504,262	504,262
Dr B Hockings ⁽²⁾	n/a	-	-	-	77,844,256	77,844,256	77,844,256
Mr N Woolf ⁽³⁾	423,728	n/a	n/a	n/a	n/a	n/a	n/a
Executives							
Dr P Watt ⁽⁴⁾	169,466	-	-	292,398	461,864	292,398	461,864

	Balance 1 July 2012	Granted As Compensation	Exercised	Other Changes	Balance 30 June 2012	Vested During The Year	Vested & Exercisable 30 June 2013
Directors							
Dr D Wilson	500,000	-	-	(500,000)	-	-	-
Dr P Watt ⁽⁵⁾	1,669,466	2,250,000	-	(1,500,000)	2,419,466	2,250,000	169,466
Mr N Woolf	1,823,728	1,500,000	-	(1,400,000)	1,923,728	1,500,000	423,728
Executives							
Dr R Hopkins	1,211,864	1,500,000	-	(1,000,000)	1,711,864	1,500,000	211,864

- (1) Dr Richard Hopkins was appointed as a director on 19 July 2013.
- (2) Dr Bernard Hockings was appointed as a director on 23 January 2014.
- (3) Mr Nick Woolf resigned as a director on 19 July 2013.
- (4) Dr Paul Watt ceased to be a director on 19 July 2013. He remained an executive of the company.
- (5) Options held by key management personnel related parties.



Directors' Report

FOR THE YEAR ENDED 30 JUNE 2014

20.14.2 EQUITY HOLDINGS AND TRANSACTIONS

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

	Balance 1 July 2013	Purchases	Other Changes	Granted As Compensation	Sales	Balance 30 June 2014
Directors						
Dr D Wilson	250,000	584,796	877,193	-	-	1,711,989
Mr B McHarrie	2,304,576	1,000,000	-	-	-	3,304,576
Dr B Hockings ⁽¹⁾	n/a	-	-	-	-	225,406,101
Dr R Hopkins ⁽²⁾	9,623,461	6,425,554	438,596	-	-	16,487,611
Mr N Woolf ⁽³⁾	8,471,956	n/a	n/a	n/a	n/a	n/a
Executives						
Dr P Watt ⁽⁴⁾	16,758,730	4,283,334	438,596	-	-	21,480,660
Mr G Boden	422,917	2,077,083	-	-	-	2,500,000

	Balance 1 July 2012	Purchases	Other Changes	Granted As Compensation	Sales	Balance 30 June 2013
Directors						
Dr D Wilson	250,000	-	-	-	-	250,000
Mr B McHarrie	2,304,576	-	-	-	-	2,304,576
Dr P Watt	16,253,730	505,000	-	-	-	16,758,730
Mr N Woolf	8,471,956	-	-	-	-	8,471,956
Executives						
Dr R Hopkins	9,233,461	390,000	-	-	-	9,623,461
Mr G Boden	422,917	-	-	-	-	422,917

(1) Dr Bernard Hockings was appointed as a director on 23 January 2014.

(2) Dr Richard Hopkins was appointed as a director on 19 July 2013.

(3) Mr Nick Woolf resigned as a director on 19 July 2013.

(4) Dr Paul Watt ceased to be a director on 19 July 2013. He remained an executive of the company.

21. PROCEEDINGS ON BEHALF OF THE COMPANY

No person has applied for leave of court to bring proceedings on behalf of the Company or 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 any part of those proceedings.

22. AUDITOR'S INDEPENDENCE DECLARATION

The auditor's independence declaration is set out on page 29 and forms part of the Directors' report for the year ended 30 June 2014.

Signed in accordance with a resolution of the directors:

Bruce McHarrie

Director

Perth

28 August 2014



Accountants | Business and Financial Advisers

AUDITOR'S INDEPENDENCE DECLARATION

As lead auditor for the audit of the consolidated financial report of Phylogica Limited for the year ended 30 June 2014, I declare that to the best of my knowledge and belief, there have been no contraventions of:

- a) the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- b) any applicable code of professional conduct in relation to the audit.

A handwritten signature in black ink, appearing to read 'M R W Ohm'.

Perth, Western Australia
28 August 2014

M R W Ohm
Partner



Statement of Comprehensive Income

FOR THE YEAR ENDED 30 JUNE 2014

		Consolidated	
		2014	2013
	Note	\$	\$
Continuing Operations			
Commercial income	5(ii)	692,150	600,335
Government grant income	5(i)	6,500	111,556
Net interest income		86,478	73,777
Other income		40,741	-
Contract research costs		(2,670,032)	(2,433,031)
Personnel expenses	7	(1,111,135)	(1,526,435)
Depreciation	8	(214,256)	(274,165)
Professional services		(433,957)	(534,127)
Travel and accommodation		(241,959)	(255,852)
Intellectual property maintenance		(372,946)	(284,543)
Laboratory consumables		(576,475)	(549,162)
Occupancy costs		(14,888)	(23,596)
Other operating expenses		(239,881)	(223,619)
Loss before income tax expense		(5,049,660)	(5,318,862)
Income tax benefit	9	1,791,965	1,879,238
Net loss for the period		(3,257,695)	(3,439,624)
Other comprehensive income for the period, net of tax		-	-
Total comprehensive loss for the period		(3,257,695)	(3,439,624)
Total comprehensive loss for the period attributable to the members of Phylogica Limited	17(iii)	(3,257,695)	(3,439,624)
		Cents	Cents
Basic loss per share	18	(0.44)	(0.74)
Diluted loss per share	18	(0.44)	(0.74)

This statement of comprehensive income is to be read in conjunction with the notes to the financial statements set out on pages 34 to 53.

Statement of Financial Position

FOR THE YEAR ENDED 30 JUNE 2014



		Consolidated	
	Note	2014 \$	2013 \$
Current assets			
Cash and cash equivalents		4,021,588	1,806,905
Trade and other receivables	10	172,345	118,698
Total current assets		4,193,933	1,925,603
Non-current assets			
Plant and equipment	11	330,202	336,858
Total non-current assets		330,202	336,858
Total assets		4,524,135	2,262,461
Current liabilities			
Trade and other payables	12	504,815	778,434
Employee benefits	16	295,156	270,656
Total current liabilities		799,971	1,049,090
Non-current liabilities			
Employee benefits	16	5,505	18,498
Total non-current liabilities		5,505	18,498
Total liabilities		805,476	1,067,588
Net assets		3,718,659	1,194,873
Equity			
Issued capital	17(i)	39,666,296	34,055,506
Reserves	17(ii)	545,102	1,514,209
Accumulated losses	17(iii)	(36,492,739)	(34,374,842)
Total equity		3,718,659	1,194,873

This statement of financial position is to be read in conjunction with the notes to the financial statements set out on pages 34 to 53.



Statement of Cashflows

FOR THE YEAR ENDED 30 JUNE 2014

		Consolidated	
		2014	2013
	Note	\$	\$
Cash flows from operating activities			
Commercial income received		692,150	743,840
Government grants received		6,500	111,556
Other income		40,741	-
Cash paid to suppliers and employees		(5,806,258)	(5,124,758)
Cash used in operations		(5,066,867)	(4,269,362)
R&D tax rebate		1,791,965	1,879,238
Interest received		74,611	74,921
Net cash used in operating activities	19	(3,200,291)	(2,315,203)
Cash flows from investing activities			
Acquisition of property, plant and equipment		(195,816)	(256,982)
Net cash used in investing activities		(195,816)	(256,982)
Cash flows from financing activities			
Proceeds from the issue of share capital	17(i)	6,012,417	1,600,000
Payment of transaction costs	17(i)	(401,627)	-
Net cash from financing activities		5,610,790	1,600,000
Net increase/(decrease) in cash and cash equivalents		2,214,683	(972,185)
Cash and cash equivalents at 1 July		1,806,905	2,779,090
Cash and cash equivalents at 30 June		4,021,588	1,806,905

This statement of cash flows is to be read in conjunction with the notes to the financial statements set out on pages 34 to 53.

Statement of Changes in Equity

FOR THE YEAR ENDED 30 JUNE 2014



		Consolidated			
		Issued Capital \$	Accumulated Losses \$	Reserves \$	Total \$
	Note				
Balance at 1 July 2012		32,455,506	(30,935,218)	1,173,570	2,693,858
Loss attributable to members of the consolidated entity		-	(3,439,624)	-	(3,439,624)
Other comprehensive income		-	-	-	-
Total comprehensive income/(loss)		-	(3,439,624)		(3,459,624)
Shares issued during the year	17(i)	1,600,000	-	-	1,600,000
Share capital transaction costs	17(i)	-	-	-	-
Share-based payments	17(ii)	-	-	340,639	340,639
Balance at 30 June 2013		34,055,506	(34,374,842)	1,514,209	1,194,873
Balance at 1 July 2013		34,055,506	(34,374,842)	1,514,209	1,194,873
Loss attributable to members of the consolidated entity		-	(3,257,695)	-	(3,257,695)
Other comprehensive income		-	-	-	-
Total comprehensive income/(loss)		-	(3,257,695)	-	(3,257,695)
Shares issued during the year	17(i)	6,012,417	-	-	6,012,417
Share capital transaction costs	17(i)	(401,627)	-	-	(401,627)
Transfer from option reserve		-	1,139,798	(1,139,798)	-
Share-based payments	17(ii)	-	-	170,691	170,691
Balance at 30 June 2014		39,666,296	(36,492,739)	545,102	3,718,659

This statement of changes in equity is to be read in conjunction with the notes to the financial statements set out on pages 34 to 53.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

1. REPORTING ENTITY

Phylogica is listed public company incorporated and operating in Australia. The financial report of the Consolidated Entity comprising the Company and its wholly owned subsidiary for the financial year ended 30 June 2014 was authorised for issue by the directors on 28 August 2014. The Company is primarily involved in the provision of peptide drug discovery services to the pharmaceutical industry.

2. BASIS OF PREPARATION

(a) Statement of Compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AAS's) which includes Australian equivalents to International Financial Reporting Standards (AIFRS) adopted by the Australian Accounting Standards Board (AASB), and the Corporations Act 2001. Compliance with AIFRS ensures that the financial report, comprising the financial statements and notes thereto, complies with International Financial Reporting Standards (IFRS's).

(b) Basis of measurement

The financial statements have been prepared on a historical cost basis and are presented in Australian dollars.

(c) Use of estimates and judgements

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

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The areas of estimation and uncertainty where judgement is used in applying accounting principles and where there may be an impact in the accounting revenue or expense are described in the following notes:

- Note 17(ii) – share based payments amount expensed for 2014 is \$170,691 (2013: \$340,639).
- Note 16 – employee benefits, where the rate of pay may change between balance date and payment and where long service leave utilisation may change.

(d) Going Concern

The financial report has been prepared on a going concern basis which assumes the settlement of liabilities and the realisation of assets in the normal course of business. For the year ended 30 June 2014 the Company has incurred a loss of \$3,257,695 (2013: loss of \$3,439,624) and at year end the Company had working capital of \$3,393,962 (2013: \$876,513) including a cash and cash equivalents balance of \$4,021,588 (2013: \$1,806,905). Cash used in operating activities in 2014 was \$3,200,291 (2013: \$2,315,203).

The Directors believe that it is appropriate to prepare the financial report on a going concern basis because:

- There is capacity for the Company to significantly reduce its cash burn rate via reduction of overheads and selective variable cost reductions.
- The Company expects to receive an R&D rebate of approximately \$1,700,000 during the first half of the 2015 financial year.
- To the extent that further funding is required the Directors are confident that a sufficient capital raising can be completed, as has previously been demonstrated via the successful entitlement issue during the period.

The following accounting policies have been applied consistently to all periods presented in these financial statements.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



2. BASIS OF PREPARATION (CONT.)

(e) Basis of consolidation

The consolidated financial statements incorporate the assets and liabilities of the subsidiary of Phylogica Limited ('company' or 'parent entity') as at 30 June 2014 and the results of its subsidiary for the year then ended. Phylogica Limited and its subsidiary are referred to in this financial report as the Group or the consolidated entity.

The financial statements of the subsidiary are prepared for the same reporting period as the parent entity, using consistent accounting policies. The subsidiary was dormant during the 2014 financial year.

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

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. Control exists where the company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing when the Group controls another entity.

Unrealised gains or transactions between the Group and its associates are eliminated to the extent of the Group's interests in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

When the Group ceases to have control, joint control or significant influence, any retained interest in the entity is remeasured to its fair value with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint controlled entity or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES

(a) Foreign currency

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction.

(b) Property, plant and equipment

(i) Recognition and measurement

The Group holds no property. Items of plant and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses - see note 3(f). Cost includes expenditures that are directly attributable to the acquisition of the asset.

(ii) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. The Company has no finance leases. Leases other than finance leases are classified as operating leases and are accounted for as described in note 3(p).

(iii) Depreciation

Depreciation is charged to the statement of comprehensive income on a straight-line basis over the estimated useful lives of each part of an item of plant and equipment. The estimated useful lives in the current and comparative periods are as follows:

Office and research equipment 2-13 years

The residual value, depreciation method and useful lives if significant, are reassessed annually.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(c) Research and development

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the statement of comprehensive income as an expense as incurred. The Company does not currently undertake development activities as defined in AASB 138 *Intangible Assets* and therefore has not capitalised development expenditure.

(d) Trade and other receivables

Trade and other receivables are initially measured at fair value and are subsequently measured at their amortised cost less any impairment losses (see note 3(f)). Trade receivables are due for settlement in no more than 30 days and the nominal amount is deemed to reflect fair value.

(e) and cash equivalents

Cash and cash equivalents comprise cash balances and short term deposits with an original maturity of three months or less.

(f) Impairment

(i) Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost, the reversal is recognised in profit or loss.

(ii) Non- Financial Assets

The carrying amounts of the Company's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to cash-generating units that are expected to benefit from the synergies of the combination.

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

(iii) Calculation of recoverable amount

The recoverable amount of non-financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(iv) Reversals of impairment

An impairment loss in respect of a receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. In respect of other assets, an impairment loss is reversed if there has been a change in estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the asset's carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(g) Earnings per share

Basic earnings per share (EPS) is calculated by dividing the income or loss attributable to the members of the Company for reporting period, after exclusion of any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the half year, adjusted for any bonus elements.

Diluted EPS adjusts the figures used in the determination of basic EPS to take into account the after tax effect of interest recognised associated with the dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration in relation to dilutive potential ordinary shares adjusted for any bonus elements.

(h) Transaction costs

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

(i) Employee benefits

(i) Long-term service benefits

The Company's net obligation in respect of long-term service benefits is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using expected future increases in wage and salary rates including related on-costs and expected settlement dates, and is discounted using the rates attached to the Commonwealth Government bonds at the reporting date which have maturity dates approximating to the terms of the Company's obligations.

(ii) Share based payment transactions

The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest.

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

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

No provision is made for non-vesting sick leave as the anticipated pattern of future sick leave taken indicates that accumulated non-vesting sick leave will never be paid.

(iv) Defined contribution superannuation funds

Obligations for contributions to defined contribution superannuation funds are recognised as an expense in the statement of comprehensive income as incurred.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(j) Provisions

A provision is recognised in the statement of financial position when the Group has a present legal or constructive obligation as a result of a past event that can be measured reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, when appropriate, the risks specific to the liability.

(k) Trade and other payables

Trade and other payables are initially recognised at fair value and are subsequently measured at their amortised cost. These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial year which are unpaid. The amounts are unsecured and normally settled within 30 days of recognition.

(l) Revenue

Goods sold and services rendered

Revenues are recognised at fair value of the consideration received net of the amount of Goods and Services Tax (GST) payable to the taxation authority.

(m) Commercial income

Commercial income is recognised in the statement of financial position initially as deferred income when there is reasonable assurance that it will be received and that the Group will comply with the conditions attaching to it. Commercial income which compensates the Group for expenses incurred is recognised as revenue in the statement of comprehensive income on a systematic basis in the same periods in which the related expenses are incurred.

(n) Finance income and expense

Finance income comprises interest income on funds invested. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group's right to receive payment is established, which in the case of quoted securities is the ex-dividend date. Finance expenses comprise interest expense on borrowings.

(o) Government Grants

Government grant income is recognised in the statement of financial position initially as deferred income when there is reasonable assurance that it will be received and that the Group will comply with the conditions attaching to it. Grants that compensate the Group for expenses incurred are recognised as revenue in the statement of comprehensive income on a systematic basis in the same periods in which the related expenses are incurred.

(p) Expenses

Operating lease payments

Payments made under operating leases are recognised in the statement of comprehensive income on a straight-line basis over the term of the lease.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(q) Financial instruments

(i) Non-derivative financial instruments

Non-derivative financial instruments comprise trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables. Non-derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Regular way purchases and sales of financial assets are accounted for at trade date, i.e., the date that the Group commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

Cash and cash equivalents comprise cash balances and call deposits.

Accounting for finance income and expense is discussed in note 3(n).

Other non-derivative financial instruments are subsequently measured at amortised cost using the effective interest method, less any impairment losses.

(ii) Share capital

Ordinary shares

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

(r) Income tax

Income tax in the statement of comprehensive income for the periods presented comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

The following temporary differences are not provided for: initial recognition of goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(s) Segment reporting

The Group comprises a single business segment comprising discovery and development of novel therapeutics and a single geographical location being Australia. The segment details are therefore fully reflected in the results and balances reported in the statement of comprehensive income and statement of financial position.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(t) Goods and services tax

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

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the taxation authority is included as a current asset or liability in the statement of financial position.

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

(u) New standards and interpretations not yet adopted

In the year ended 30 June 2014, the Directors have reviewed all of the new and revised Standards and Interpretations issued by the AASB that are relevant to the Groups operations and effective for the current annual reporting period.

It has been determined by the Directors that there is no impact, material or otherwise, of the new and revised Standards and Interpretations on the Groups business and, therefore, no change is necessary to Group accounting policies.

The Directors have also reviewed all new Standards and Interpretations that have been issued but are not yet effective for the year ended 30 June 2014. As a result of this review the Directors have determined that there is no impact, material or otherwise, of the new and revised Standards and Interpretations on the Groups business and therefore, no change necessary to Group accounting policies.

4. FINANCIAL RISK MANAGEMENT

Overview

The Company has exposure to the following risks from their use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Company's exposure to each of the above risks, their objectives, policies and processes for measuring and managing risk, and the management of capital. Further quantitative disclosures are included throughout this financial report. The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. The Board has delegated to the Audit Committee, the responsibility for developing and monitoring risk management policies.

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

The Company, through their training and management standards and procedures, aim to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Audit Committee oversees how management monitors compliance with the Company's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Company.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company receivables and cash investments.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



4. FINANCIAL RISK MANAGEMENT (CONT.)

Trade and other receivables

The Group had no material credit risk at 30 June 2014 or 2013.

Cash investments

The Group limits its exposure to credit risk by banking only with Australia and New Zealand Banking Group. Given that bank's credit rating, management does not expect it to fail to meet its obligations.

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return. The Group does not presently use financial derivatives as a risk management tool.

Currency risk

The Group is exposed to currency risk on some purchases that are denominated in a currency other than the functional currency of the Group, the Australian dollar (AUD). As the exposure is immaterial in value and of short term duration, the Group does not employ any hedging strategies for foreign currency risk management.

Interest rate risk

The Group does not have any borrowings. The Group invests temporarily idle funds at call at variable interest rates.

Capital management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board's target is for employees and directors of the Group to hold between five and ten percent of the Group's ordinary shares as performance incentives. At present employees hold approximately 2% of fully diluted issued capital, assuming that all outstanding share options and loan funded shares vest and / or are exercised.

There were no changes in the Group's approach to capital management during the year. The Group is not subject to externally imposed capital requirements.

5. INCOME

(i) Government grant income

The Group had been awarded a government grant which was recognised as revenue in the statement of comprehensive income in the same period as which the related expenses are incurred. The amount of \$6,500 (2013: \$13,500) was recognised in the year ended 30 June 2014.

Additionally, a rebate of \$98,056 was achieved through the Export Market Development Grant Scheme during the year ended 30 June 2013. The rebate relates to expenditure which was incurred in the financial year ending 30 June 2011 which was the final EMDG grant for which the company was eligible at that time.

(ii) Commercial income

Commercial income is derived from contracts to fund research and is based upon a mixture of funding full time equivalent research salaries and milestone payments. A total of \$692,150 was received from contract payments during the year (2013: \$600,335).



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

6. RESEARCH AND DEVELOPMENT EXPENDITURE

The accounting standards do not permit the capitalisation of development expenditure in circumstances where the company cannot demonstrate sustainable revenue generation derived from the results of the expenditure. Research expenditure must be expensed under accounting standards. The expenditure incurred in relation to obtaining and maintaining patent protection is allowed to be capitalised under the standards but the Company has adopted a policy of expensing such expenditure as it is incurred.

Since incorporation, Phylogica has raised \$42.2 million in capital, reduced to \$39.7 million after netting capital raising fees. From this amount the following expenditures have been undertaken (all amounts \$ million):

Research & Development:	Prior to 2012	2013	2014	Total
Contract Research	12.99	2.43	2.67	18.09
Personnel (allocation)	5.36	0.78	0.56	6.70
Laboratory Consumables	3.43	0.55	0.58	4.56
	21.78	3.76	3.81	29.35
IP Maintenance	2.51	0.28	0.37	3.16
	24.29	4.04	4.18	32.51

7. PERSONNEL EXPENSES

	Consolidated	
	2014	2013
	\$	\$
Wages and salaries	880,303	1,034,980
Other associated staff costs	4,010	47,023
Contributions to defined contribution superannuation funds	51,690	71,898
Increase in annual leave accrual	4,441	31,895
Share based compensation - note 17	170,691	340,639
	1,111,135	1,526,435

8. DEPRECIATION

Depreciation of equipment	214,256	274,165
	214,256	274,165

9. INCOME TAX

(i) Income tax benefit

The prima facie tax on the operating loss is reconciled to the income tax provided in the accounts as follows:

Prima facie tax benefit on operating loss before income tax at 30%	1,514,898	1,595,659
Tax effect of permanent differences	16,017	(48,524)
Current period tax losses and temporary differences not brought to account	(1,530,915)	(1,547,135)
R&D income tax incentive received relating to prior year	1,791,965	1,879,238
Income tax benefit	1,791,965	1,879,238

(ii) Unrecognised deferred tax asset

Deferred tax assets have not been recognised in respect of the following items:

Deductible/(Assessable) temporary differences	(215)	(14,001)
Tax losses	10,967,265	10,643,427
	10,967,050	10,629,426

Tax losses do not expire under current tax legislation. Deferred tax assets have not been recognised in respect of these items because it cannot yet be considered probable that future taxable profit will be available against which the Company can utilise the benefits therefrom.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



10. TRADE AND OTHER RECEIVABLES

	Consolidated	
	2014	2013
	\$	\$
GST receivable	96,627	80,961
Accrued Interest	12,483	616
Other receivables	63,235	37,121
	172,345	118,698

11. PLANT AND EQUIPMENT

Office and research equipment at cost	1,370,457	1,180,655
Accumulated depreciation	(1,040,255)	(843,797)
	330,202	336,858

Reconciliation:

Carrying amount at the beginning of the year	336,858	478,715
Acquisitions	208,950	132,308
Disposals	(19,148)	-
Depreciation	(196,458)	(274,165)
	330,202	336,858

12. TRADE AND OTHER PAYABLES

Trade payables ⁽¹⁾	411,398	717,815
Accrued expenses	74,974	37,535
Other	18,443	23,084
	504,815	778,434

(1) Trade payables are non-interest bearing and are normally settled on 30 day terms.

13. SEGMENT INFORMATION

The Company comprises a single business segment being the provision of drug discovery services to the international pharmaceutical industry utilising the Company's Phylomer® peptide libraries and proprietary screening capabilities; and a single geographical location being Australia. The segment details are therefore fully reflected in the results and balances reported in the statement of comprehensive income and statement of financial position.

14. EVENTS SUBSEQUENT TO BALANCE DATE

There are no matters or circumstances that have arisen since the end of the financial year that have significantly affected or may significantly affect the operations of the Consolidated Entity, the results of those operations or the state of affairs of the Consolidated Entity, in future financial years.

15. CONTINGENT LIABILITIES

Phylogica has a research services contract with the Telethon Kids Institute. If this contract were to be terminated Phylogica would be responsible to reimburse the Telethon Kids Institute for the payout of severance and annual leave for the staff terminated as a consequence of the terminated contract.

At 30 June 2014 it was estimated this cost would be \$350,000 for 20 employees.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

16. EMPLOYEE BENEFIT

	Consolidated	
	2014	2013
	\$	\$
Current:		
Liability for annual leave	193,765	189,324
Superannuation payable	-	900
Liability for Long Service Leave	101,391	80,432
	295,156	270,656
Non-Current:		
Liability for Long Service Leave	5,505	18,498
	5,505	18,498
Remuneration for all employees other than non-executive directors includes an at risk performance component.		
Consolidated:		
Balance as 1 July 2013	98,930	189,324
Payments made	-	(56,252)
Charges raised or written back	7,966	60,693
Balance as 30 June 2014	106,896	193,765

(i) Share-based payments

(a) ESOP

In 2005 the Group established an employee share option programme (ESOP) that entitles key management personnel and senior employees to purchase shares in the Group. The ESOP was renewed at the Annual General Meeting in November 2010.

No options were granted under the ESOP during the year ended 30 June 2014.

During the year ended 30 June 2013, 8,125,000 options were granted under the ESOP, of which 7,500,000 vested immediately upon grant, with the remaining 625,000 vesting six months later. These options were granted with an exercise price of \$0.035 per option and an expiry date of 15 August 2015.

(b) Loan Funded Shares

A scheme under which shares may be issued by the Group to directors or employees for no cash consideration was approved by shareholders at the Annual General Meeting held on 24 November 2011.

Participants of the Plan are determined by the Board and can be directors or employees of the Company or a subsidiary. The Board considers length of service, seniority, responsibilities, potential contribution and any other relevant matters in determining eligibility of potential participants.

The issue price for the shares issued under the Plan is the share price on the day of the offer to the participant. A participant who is invited to subscribe for shares under the Plan will be invited to apply for a loan up to the amount payable in respect of the shares accepted by the participant.

These loans are to be made on the following terms:

- Interest free;
- Applied directly against the issue price of the shares to be acquired under the Plan;
- For a term to be determined by the Board;
- Repayable to the extent of the lesser of the issue price of the relevant shares issued, less any cash dividends applied against the outstanding principal; and the last market sale price of the shares on the date of repayment of the loan;

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



16. EMPLOYEE BENEFITS (CONT.)

- The loan must be repaid in full prior to expiry of the loan;
- The Company will have a lien over the shares in respect of which a loan is outstanding;
- Shares issued under the Plan are not transferable while a loan amount in respect of those shares remains payable; and
- Shares issued under the Plan will not be quoted on a publicly traded stock market while a loan amount in respect of those shares remains payable.

During the year ended 30 June 2012 a total of 21 million shares were issued under the Plan to key management personnel. The offers, which were accepted, were as follows:

- Term of the loan: 7 years (3 June 2018) or cessation of employment, whichever is earlier.
- Purchase price of shares funded by loan is 6.4 cents.
- 33% of the shares will vest on 3 June 2014, 33% on 3 June 2015 and 34% on 3 June 2016.
- Allocations have been made to:

Dr P Watt	9,000,000 shares
Mr N Woolf	6,000,000 shares
Dr R Hopkins	6,000,000 shares

Mr N Woolf ceased employment with the Company on 31 July 2013. Consequently the 6,000,000 shares awarded to him were cancelled in accordance with the terms of the Plan.

No loan funded shares were issued under the Plan during the year ended 30 June 2013 or 30 June 2014.

(c) Zero Exercise Price Options (ZEPOs)

During the year ended 30 June 2013 6,000,000 ZEPOs were issued. The ZEPOs had a nil exercise price and expired on 2 December 2013 unexercised as they did not meet the exercise conditions.

(ii) Fair value and assumptions

(a) Options

All options refer to options over ordinary shares of Phylogica Ltd which are exercisable on a one for one basis.

In 2014 no options were granted under the ESOP. In 2013 8,125,000 options were granted under the ESOP.

The fair value of the options is calculated at grant date using a Black-Scholes pricing model and allocated to each reporting period in accordance with the vesting profile of the options.

The value recognised is the portion of the fair value of the options allocated to the reporting period. The factors and assumptions used in determining the fair value on grant date of options issued during the financial year as follows:

Granted during 2013:

Number of Options	Grant Date	Expiry Date	Fair Value per Option	Exercise Price	Share Price on Grant Date	Risk Free Interest Rate (%)	Estimated Volatility (%)	Number Vested at 30 June 2013
8,125,000	22/08/2013	15/08/2015	\$0.013	\$0.035	\$0.024	2.8	100	8,125,000

In the table above, the following vesting profiles have been adopted:

- 7,500,000 options vested immediately upon grant and 625,000 vested on 30 April 2013.

The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options), adjusted for any expected changes to future volatility due to publicly available information. No dividends have been assumed to be paid during the life of the options. No employee options were exercised during the year.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

16. EMPLOYEE BENEFITS (CONT.)

(b) Loan Funded Shares

All shares issued under the Plan with limited recourse loans are valued in a similar way to options and the fair value of shares issued under the Plan is determined as detailed below.

Fair value of shares issued under the plan during 2014 was Nil (2013: Nil).

The assessed fair value at grant date of shares issued under the plan during the year ended 30 June 2012 was 3.96 cents per share. The fair value at grant date is determined using a Black-Scholes pricing model that takes into account the exercise price, the term of the loan, 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 loan giving a total value of \$831,600. The fair value of the LFS on issue has been reduced to \$594,000 due to the cancellation of 6,000,000 loan funded shares during the year ended 30 June 2014. In accordance with accounting standards, the allocations amortised over the vesting periods would lead to the following expense and corresponding increase in the Share Based Payment Reserve:

	\$
2012 financial year	150,438
2013 financial year	257,894
2014 financial year cancelled 6,000,000 LFS	(116,666)
2014 financial year	170,692
Two years 2015 to 2016	131,642
	594,000

Granted during 2012 and outstanding at 30 June 2014:

Number of Loan Funded Shares	Grant Date	Expiry Date	Fair Value per Loan Funded Share	Exercise Price	Share Price on Grant Date	Risk Free Interest Rate (%)	Estimated Volatility (%)	Number Vested at 30 June 2012
15,000,000	24/11/2011	03/06/2018	\$0.049	\$0.064	\$0.06	5.2	100	Nil

(c) Zero Exercise Price Options (ZEPOs)

The fair value of the options is calculated at grant date using a Black-Scholes pricing model and allocated to each reporting period in accordance with the vesting profile of the options. No expense was allocated for the ZEPOs as the vesting conditions made exercise highly unlikely.

The value recognised is the portion of the fair value of the options allocated to the reporting period. The factors and assumptions used in determining the fair value on grant date of zero exercise price options issued during the previous financial year as follows (granted during 2014: Nil):

Granted during 2013:

Number of ZEPOs	Grant Date	Expiry Date	Fair Value per ZEPO	Exercise Price	Share Price on Grant Date	Risk Free Interest Rate (%)	Estimated Volatility (%)	Number Vested at 30 June 2013
6,000,000	22/11/12	02/12/13	\$0.0	Nil	\$0.022	2.8	100	Nil

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



17. CAPITAL AND ACCUMULATED LOSSES

	Consolidated	
	2014 \$	2013 \$
(i) Issued, unissued and paid up capital		
1,002,069,367 (2013: 466,890,744) ordinary shares fully paid.	39,666,296	32,455,506
Shares to be issued on conversion of converting notes	-	1,600,000
	39,666,296	34,055,506

Movements in capital during the year:

	Consolidated		Consolidated	
	2014 Shares	2014 \$	2013 Shares	2013 \$
Ordinary Shares				
Opening balance	466,890,744	34,055,506	466,890,744	32,455,506
Shares issued during the year:				
- Issued at \$0.015	400,827,747	6,012,417	-	-
- Share issue costs	-	(401,627)	-	-
- Shares to be issued on conversion of converting notes ⁽¹⁾	-	-	-	1,600,000
- Shares issued on conversion of converting notes ⁽¹⁾	140,350,876	-	-	-
- Shares cancelled ⁽²⁾	(6,000,000)	-	-	-
Closing balance	1,002,069,367	39,666,296	466,890,744	34,055,506

(1) 16,000 converting notes were converted for 140,350,876 ordinary shares and 93,567,252 PYCOA. See note 17(vii).

(2) 6,000,000 loan funded shares previously issued to an executive, were cancelled upon the cessation of his employment. See note 17(v).

Terms and Conditions:

Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings. In the event of winding up of the Group, ordinary shareholders rank after all other shareholders and creditors and are fully entitled to any proceeds of liquidation.

The shares have no par value.

	Consolidated	
	2014 \$	2013 \$
(ii) Reserves		
Opening balance	1,514,209	1,173,570
Share based payments for the period	170,691	340,639
Transfer to accumulated losses	(1,139,798)	-
Balance at the end of the year	545,102	1,514,209

Nature and purpose of reserves:

Share based payments reserve

This reserve is used to record the value of equity benefits provided to employees and directors as part of their remuneration. Refer to Note 16 and the Remuneration Report for further details of these plans.

	Consolidated	
	2014 \$	2013 \$
(iii) Accumulated losses		
Opening balance	(34,374,842)	(30,935,218)
Loss for the period	(3,257,695)	(3,439,624)
Transfer from option reserve	1,139,798	-
Balance at the end of the year	(36,492,739)	(34,374,842)



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

17. CAPITAL AND ACCUMULATED LOSSES (CONT.)

(iv) Options

Options on issue at end of the year:	Weighted Av. Exercise Price 2014	Number of Options 2014	Weighted Av. Exercise Price 2013	Number of Options 2013
(a) Options exercisable at \$0.09 on or before 30 June 2016:				
Balance at beginning of year	\$0.09	71,090,028	\$0.09	71,090,028
Issued during the year	\$0.09	93,567,252	-	-
Lapsed	-	-	-	-
Balance at end of year	\$0.09	164,657,280	\$0.09	71,090,028
(b) Options exercisable at \$0.035 on or before 15 August 2015:				
Balance at beginning of year	\$0.035	8,125,000	-	-
Issued during the year	-	-	\$0.035	8,125,000
Lapsed	-	-	-	-
Balance at end of year	\$0.035	8,125,000	\$0.035	8,125,000

(c) Fair value:

The options outstanding at 30 June 2014 have exercise prices of \$0.035 or \$0.09. No options were exercised during the year ended 30 June 2014.

The fair value of services received in return for share options granted is based on the fair value of share options granted, measured using the Black – Scholes option pricing formula. 93,567,252 share options were granted on conversion of 16,000 converting notes during the year ended 30 June 2014.

Fair value of share options and assumptions	Employees 2013
Grant date	22 August 2012
Fair value at grant date	\$0.013
Share price	\$0.024
Exercise price	\$0.035
Expected volatility (weighted average)	100%
Option life (expected weighted average)	2.75 years
Expected dividends	-
Risk free interest rate (based on government bonds)	2.78%

(v) Loan Funded Shares

Loan funded shares on issue at the end of the year:	Weighted Av. Exercise Price 2014	Number of Shares 2014	Weighted Av. Exercise Price 2013	Number of Shares 2013
(a) LFS exercisable at \$0.064 on or before 3 June 2018:				
Balance at beginning of year	\$0.064	21,000,000	\$0.064	21,000,000
Issued during the year	-	-	-	-
Lapsed	-	-	-	-
Cancelled ⁽¹⁾	\$0.064	(6,000,000)	-	-
Balance at end of year	\$0.064	15,000,000	\$0.064	21,000,000

(1) 6,000,000 LFS held by Mr Woolf (ceased employment 31 July 2013) were cancelled.

Fair value of loan funded shares and assumptions:	Key Management Personnel 2012
Grant date	24 November 2011
Fair value at grant date	\$0.049
Share price	\$0.060
Exercise price	\$0.064
Expected volatility (weighted average)	100%
Option life (expected weighted average)	6.53 years
Expected dividends	-
Risk free interest rate (based on government bonds)	5.15%

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



17. CAPITAL AND ACCUMULATED LOSSES (CONT.)

(vi) Zero Exercise Price Options (ZEPOs)

<i>Zero exercise price options on issue at the end of the year:</i>	Weighted Av. Exercise Price 2014	Number of Options 2014	Weighted Av. Exercise Price 2013	Number of Options 2013
(a) ZEPOs on or before 2 December 2013:				
Balance at beginning of year	-	6,000,000	-	-
Issued during the year	-	-	-	6,000,000
Lapsed	-	(6,000,000)	-	-
Balance at end of year	-	-	-	6,000,000

Key Management Personnel

	2013
(b) Fair value of zero exercise price options and assumptions:	22 November 2012
Grant date	
Fair value at grant date	\$0.022
Share price	\$0.022
Exercise price	-
Option life (expected weighted average)	1.03 years
Expected dividends	-
Risk free interest rate (based on government bonds)	2.79%

5,250,000 ZEPOs were issued to Directors during the year to 30 June 2013.

The 6,000,000 ZEPOs expired unexercised on 2 December 2013 as they did not meet the vesting conditions.

(iii) Converting Notes

	2014	2013
(d) Converting notes on issue at the end of the year:		
Balance at beginning of year	16,000	-
Issued during the year	-	16,000
Converted	(16,000)	-
Balance at end of year	-	16,000

(b) Terms

In accordance with the conditions of the Converting Notes, holders were issued 140,350,876 shares and 93,567,252 PYCOA options upon conversion during the year ended 30 June 2014.

	Consolidated 2014 \$	2013 \$
(v) Employee Expense		
Equity – settled share-based payments issued		
In 2013	-	82,745
In 2012	170,691	257,894
Total recognised as employee expense	170,691	340,639

18. EARNINGS PER SHARE

(i) Loss attributable to ordinary shareholders

Loss for the period:		
Basic earnings	(3,257,695)	(3,439,624)
Diluted earnings*	(3,257,695)	(3,439,624)

(ii) Weighted average number of ordinary shares

	Number	Number
Weighted average number of shares used for basic earnings per share	740,016,387	466,890,744

*As the Group incurred a loss for the year ended 30 June 2014, the options on issue have an antidilutive effect, therefore the diluted earnings per share is equal to the basic earnings per share.



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

19. NOTE TO THE STATEMENT OF CASH FLOWS

	Consolidated	
	2014 \$	2013 \$
Reconciliation of loss for the year to net cash used in operating activities:		
Loss for the year	(3,257,695)	(3,439,624)
Depreciation, amortisation & impairment	214,256	274,165
Share based payment expense	170,691	340,639
Increase/(decrease) in provisions for employee benefits	11,507	47,601
Increase/(decrease) in payables and deferred income	(285,403)	315,169
(Increase)/decrease in receivables & prepayments	(53,647)	146,847
Net cash used in operating activities	(3,200,291)	(2,315,203)

20. COMMITMENTS

Payable within one year	179,875	-
Payable after one year but not more than five years	65,000	-
	244,875	-

Research Collaboration Commitment:

Phylogica is collaborating on a project with the University of Queensland.

Phylogica has a cash contribution payable to the University of Queensland over three years.

Research Contract:

Phylogica has contracted a research from the University of Western Australia for a term of 11 months. Phylogica has a commitment to pay placement fees as well as the salary expenses of the researcher to the University of Western Australia. This commitment is payable within one year.

21. FINANCIAL INSTRUMENTS

(i) Interest rate risk profile:

At reporting date the interest rate profile of the Group's interest bearing financial instrument was:

Variable rate instruments:

- Financial assets	4,021,588	1,806,905
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Fair value sensitivity analysis for fixed rate instruments:

The Group does not account for any fixed rate financial assets and liabilities at fair value through the profit and loss.

Cash flow sensitivity analysis for variable rate instruments:

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables remain constant. The analysis is performed on the same basis for 2013.

	Consolidated			
	2014		2013	
	100 bp increase	100 bp decrease	100 bp increase	100 bp decrease
Variable rate instruments	40,216	(40,216)	18,069	(18,069)

(ii) Fair value

The financial assets and financial liabilities of the Group are all current so that fair value is equal to carrying value. Consequently the Group does not make any adjustments through the statement of comprehensive income or on the statement of financial position to restate the carrying value of the financial assets and liabilities.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



21. FINANCIAL INSTRUMENTS (CONT.)

(iii) Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. The Group undertakes due diligence prior to entering into any collaboration, co-development or licensing agreement with a counterparty that exposes the Group to credit risk.

No receivables are past due or considered impaired in 2014 or 2013.

(iv) Foreign exchange risk

The Group is exposed to foreign currency risk on purchases that are denominated in a currency other than the AUD. Management does not consider the value of transactions is sufficient to warrant entering into forward currency contracts.

(v) Capital management

The operations of the Group are not presently cash positive and the Group is reliant upon developing additional revenue and raising further capital. The Group's policy on capital management is set out in note 4.

(vi) Liquidity risk

The following are the contractual maturities of the Group's financial liabilities.

	Carrying Amount	Contractual Cash Flows	6 months or less
	\$	\$	\$
Trade and other payables:			
at 30 June 2014	504,815	(504,815)	(504,815)
at 30 June 2013	778,434	(778,434)	(778,434)

22. RELATED PARTIES

(i) Key management personnel compensation

Non-Executive Directors

Mr B McHarrie

Mr J Curnock Cook

Dr D Wilson

Dr B Hockings (Appointed 23 January 2014)

Executive Directors

Mr N Woolf (Resigned 19 July 2013)

Dr Paul Watt (Resigned 19 July 2013)

Dr R Hopkins (Appointed 19 July 2013 - Chief Executive Officer)

Executives

Dr P Watt (Appointed 19 July 2013 - Chief Scientific Officer)

Mr G Boden (Appointed additional role of Chief Financial Officer from 19 July 2013)

Dr R Hopkins (Role transitioned from Chief Scientific Officer to Chief Executive Officer on 19 July 2013)

The key management personnel compensation included in 'personnel expenses' (see note 7) is as follows:

- Short-term employee benefits

- Post-employment benefits

- Long term employee benefits

- Share based payments

Total compensation

Consolidated	
2014	2013
\$	\$
752,949	921,600
40,762	53,010
13,484	19,073
170,691	257,894
977,886	1,251,577



Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014

22. RELATED PARTIES (CONT.)

(ii) Key management personnel transactions

Apart from details disclosed in this note, no director has entered into a material contract with the Group since the end of the previous financial year and there were no material contracts involving directors' interests existing at year-end.

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

A number of these entities transacted with the Group or its subsidiaries in the reporting period. The terms and conditions of the transactions with management persons and their related parties were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to non-director related entities on an arm's length basis.

The aggregate amounts recognised during the year relating to key management personnel and their related parties were as follows:

Key management persons	Transaction	Note	2014	2013
			\$	\$
Mr B McHarrie	Contract research services	(a)	3,302,802	3,149,597
Mr G Boden	Corporate services	(b)	145,625	101,601

- (c) The Telethon Kids Institute, of which Mr McHarrie is the Director of Operations, has signed a Research and Development agreement with the Group for provision of research and development services in relation to the Group's technology. Service fees were billed based on normal market rates for such services and were due and payable under normal payment terms.
- (d) Boden Corporate Services Pty Ltd, of which Mr Boden is a director, has provided services in company secretarial, accounting and administration roles for which services fees were billed based on normal market rates, and were due and payable under normal payment terms.
- (e) Amounts payable to key management personnel at reporting date arising from these contract services were as set below:

	Consolidated	
	2014	2013
	\$	\$
Current payables:		
Trade and other payables	306,951	573,823
	306,951	573,823

(vi) Subsidiaries

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

Name	Country of Incorporation	Equity Interest (%)		Investment (\$)	
		2014	2013	2014	2013
Dynamic Microbials Limited	Australia	100	100	1,012,500	1,012,500

Phylogica Limited is the ultimate Australian parent entity and ultimate parent of the Group.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2014



23. PARENT ENTITY DISCLOSURES

(i) Financial position

Assets

Current assets

Non-current assets

Total assets

Liabilities

Current liabilities

Non-current liabilities

Total liabilities

Equity

Issued capital

Accumulated losses

Reserves - Share-based payments

Total equity

2014 \$	2013 \$
4,193,933	1,925,603
330,202	336,858
4,524,135	2,262,461
799,971	1,049,090
5,505	18,498
805,476	1,067,588
39,666,296	34,055,506
(36,492,739)	(34,374,842)
545,102	1,514,209
3,718,659	1,194,873

(ii) Financial performance

(Loss) for the year

Other comprehensive income

Total comprehensive loss

Year Ended 30 June 2014 \$	30 June 2013 \$
(3,257,695)	(3,439,624)
-	-
(3,257,695)	(3,439,624)

24. AUDITOR'S REMUNERATION

Audit services

- Audit and review of financial reports

- Other regulatory audit services

Non audit services

Consolidated 2014 \$	2013 \$
31,495	30,000
-	-
31,495	30,000
-	-
31,495	30,000



Directors' Declaration

FOR THE YEAR ENDED 30 JUNE 2014

.....

1. In the opinion of the directors of Phylogica Limited (the Company):
 - (a) the financial statements and notes and the audited remuneration disclosures that are contained in the Remuneration Report in the Directors' Report, set out on pages 12 to 28, are in accordance with the Corporations Act 2001, including:
 - (i) giving a true and fair view of the financial position of the Group as at 30 June 2014 and of its performance, as represented by the results of operations and its cash flows, for the financial year ended on that date; and
 - (ii) complying with Australian Accounting Standards and the Corporations Regulations 2001, professional reporting requirements and other mandatory requirements; and
 - (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 2 (a); and
 - (c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.
2. The directors have been given the declarations by the chief executive officer and chief financial officer for the financial year ended 30 June 2014 pursuant to Section 295A of the Corporations Act 2001.

Dated at Perth this 28th day of August 2014

Signed in accordance with a resolution of the directors:

Mr Bruce McHarrie
Director

INDEPENDENT AUDITOR'S REPORT

To the members of Phylogica Limited

Report on the Financial Report

We have audited the accompanying financial report of Phylogica Limited ("the company"), which comprises the consolidated statement of financial position as at 30 June 2014, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration for 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), the directors also state, in accordance with Accounting Standard AASB 101: *Presentation of Financial Statements*, that the financial report complies with International Financial Reporting Standards.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those 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 company'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 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 audit did not involve an analysis of the prudence of business decisions made by directors or management.

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*.



Accountants | Business and Financial Advisers

Auditor's opinion

In our opinion:

- (a) the financial report of Phylogica 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 2014 and of its performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- (b) the financial report also complies with International Financial Reporting Standards as disclosed in Note 1(a).

Report on the Remuneration Report

We have audited the remuneration report included in the directors' report for the year ended 30 June 2014. The directors of the company are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's opinion

In our opinion the remuneration report of Phylogica Limited for the year ended 30 June 2014 complies with section 300A of the *Corporations Act 2001*.

HLB Mann Judd

HLB Mann Judd
Chartered Accountants

Perth, Western Australia
28 August 2014

M R W Ohm
Partner

Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014



This statement outlines the main corporate governance practices in place throughout the financial year, which comply with the ASX Corporate Governance Council recommendations (2nd Edition), unless otherwise stated.

As the framework of how the Board of Directors at Phylogica Limited ("Company") carries out its duties and obligations, the Board has considered the eight principles of corporate governance as set out in the ASX Corporate Governance Principles and Recommendations (2nd Edition).

Principle 1 – Lay solid foundations for management and oversight

Companies should establish and disclose the respective roles and responsibilities of Board and management.

Recommendation 1.1: Companies should establish the functions reserved to the Board and those delegated to senior executives and disclose those functions.

The Directors monitor the business affairs of the Company on behalf of Shareholders and have formally adopted a corporate governance policy which is designed to encourage Directors to focus their attention on accountability, risk management and ethical conduct.

The Company's main corporate governance policies and practices are outlined below:

THE BOARD OF DIRECTORS

The Company's Board of Directors is responsible for corporate governance of the Company. The Board develops strategies for the Company, reviews strategic objectives and monitors performance against those objectives.

The goals of the corporate governance processes are to:

- (a) maintain and increase Shareholder value;
- (b) ensure a prudential and ethical basis for the Company's conduct and activities; and
- (c) ensure compliance with the Company's legal and regulatory objectives.

Consistent with these goals, the Board assumes the following responsibilities:

- (a) developing initiatives for profit and asset growth;
- (b) reviewing the corporate, commercial and financial performance of the Company on a regular basis;
- (c) acting on behalf of, and being accountable to, the Shareholders; and
- (d) identifying business risks and implementing actions to manage those risks and corporate systems to assure quality.

The Company is committed to the circulation of relevant materials to Directors in a timely manner to facilitate Directors' participation in the Board discussions on a fully-informed basis.

COMPOSITION OF THE BOARD

Election of Board members is substantially the province of the Shareholders in general meeting. However, subject thereto, the Company is committed to the following principles:

- (a) the Board is to comprise Directors with a blend of skills, experience and attributes appropriate for the Company and its business; and
- (b) the principal criterion for the appointment of new Directors is their ability to add value to the Company and its business.

No formal nomination committee or procedures have been adopted for the identification, appointment and review of the Board membership, but an informal assessment process, facilitated by the Chairman in consultation with the Company's professional advisors, has been followed by the Board, generally at two year intervals.



Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014

INDEPENDENT PROFESSIONAL ADVICE

The Directors may obtain independent professional advice on issues arising in the course of their duties.

REMUNERATION ARRANGEMENTS

The remuneration of an Executive Director will be decided by the Board, without the affected Executive Director participating in that decision-making process.

The total cash remuneration of Non-Executive Directors is the subject of a Shareholder resolution in accordance with the Company's Constitution, the Corporations Act and the ASX Listing Rules, as applicable. The determination of Non-Executive Directors' remuneration within that maximum will be made by the Board having regard to the inputs and value to the Company of the respective contributions by each Non-Executive Director. The current limit, which may only be varied by Shareholders in general meeting, is an aggregate cash amount of \$200,000 per annum.

The Board may award additional remuneration to Non-Executive Directors who are called upon to perform extra services or make special exertions on behalf of the Company.

EXTERNAL AUDIT

The Company in general meeting is responsible for the appointment of the external auditor of the Company, and the Board from time to time will review the scope, performance and fees of those external auditors.

AUDIT COMMITTEE

The Company has established a separately constituted audit committee.

IDENTIFICATION AND MANAGEMENT OF RISK

The Board's collective experience will enable accurate identification of the principal risks that may affect the Company's business. Key operational risks and their management are recurring items for deliberation at Board meetings.

ETHICAL STANDARDS

The Board is committed to the establishment and maintenance of appropriate ethical standards.

Recommendation 1.2: Companies should disclose the process for evaluating the performance of senior executives.

The Board and senior executives collaborate on the company's strategic direction at regular intervals, and at monthly intervals review operational progress. During these review sessions the roles of the senior executives are assessed for their contributions to the corporate goals and to new and ongoing contract deliverables. Annual appraisals are conducted by line managers around KPIs set at the beginning of the financial year.

Principle 2 – Structure the Board to add value

Companies should have a Board of an effective composition, size and commitment to adequately discharge its responsibilities and duties.

Recommendation 2.1: A majority of the Board should be independent directors.

The Board has five Directors comprising a non-executive chairman, one executive director and three non-executive directors, one of whom is classified as non-independent because of his employment by the major contractor to the Company, and another because of a substantial shareholding.

Recommendation 2.2: The chair should be an independent director.

The chairman is not yet considered independent because of his previous executive chairman role. The Board has other directors and believes that the position of the Chairman as a former executive does not preclude him from bringing independent judgement to bear on decisions affecting the Company, nor does it prejudice the Company's corporate governance.

Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014



Recommendation 2.3: The roles of the chair and Chief Executive Officer should not be exercised by the same individual.

The roles of chief executive officer and chairman are not held by the same person.

Recommendation 2.4: The Board should establish a nomination committee.

The Board has not established a separate nomination committee. The Board, as a whole, deals with areas that would normally fall within the charge of the Nomination Committee. These include matters relating to the renewal of Board Members and Board Performance.

Recommendation 2.5: Companies should disclose the process for evaluating the performance of the Board, its committees and individual directors.

The Board, acting as the Nomination Committee, has developed a formal process for performance evaluation of the Board. An evaluation of the performance of the board and its members was carried out during January 2012. The evaluation process was an internal self- assessment based on questions and analysis of answers with round table discussions. All members of the Board at that time participated in the assessment.

Principle 3 – Promote ethical and responsible decision-making

Companies should actively promote ethical and responsible decision-making.

Recommendation 3.1: Companies should establish a code of conduct and disclose the code or a summary of the code as to:

- The practices necessary to maintain confidence in the company's integrity.
- The practices necessary to take into account their legal obligations and the reasonable expectations of their stakeholders.
- The responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

The Company is committed to Directors and employees maintaining high standards of integrity and ensuring that activities are in compliance with the letter and spirit of both the law and Company policies.

Directors acquaint themselves with obligations imposed on them and the Company by the Corporations Act. They will also familiarise themselves with other documents prepared by the Company to meet corporate governance requirements:

- the Employee Code of Conduct –sets out minimum standards of conduct and integrity to be observed by all employees and Directors; and
- the Corporate Governance Statement – advises Shareholders and ASX of the corporate governance practices put in place by the Board.

Recommendation 3.2: Companies should establish a policy concerning diversity and disclose the policy or a summary of that policy. The policy should include requirements for the board to establish measureable objectives for achieving gender diversity for the board to assess annually both the objectives and the progress in achieving them.

The Company has not yet established a diversity policy. Notwithstanding this the company has policies in accordance with its code of conduct which:

- provide for equal opportunity in employment;
- has recruitment and selection processes which are based on the merits of appropriate candidates; and
- has grievance procedures to manage conflict, misconduct, discrimination and harassment.

Recommendation 3.3: Companies should disclose in each annual report the measureable objectives for achieving gender diversity set by the board in accordance with the diversity policy and progress towards achieving them.

The Company has not established measurable guidelines in relation to diversity and may not. In an organisation of a handful of people establishing diversity on the basis of gender, age, ethnicity and cultural background is going to be difficult to design let alone achieve.



Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014

Recommendation 3.4: Companies should disclose in each annual report the proportion of women employees in the whole organisation, women in senior executive position and women on the board.

The gender balance throughout the organisation at 30 June was as follows:

	2014		2013	
	Female	Total	Female	Total
Board	-	5	-	5
Other Key Management Personnel	-	2	-	2
Professional Staff	2	2	2	2
Research Contractor	15	20	15	22

Principle 4 – Safeguard integrity in financial reporting

Companies should have a structure to independently verify and safeguard the integrity of their financial reporting.

Recommendation 4.1: The Board should establish an audit committee.

The board has established an Audit Committee consisting of three non-executive directors.

Recommendation 4.2: The audit committee should be structured so that it:

- consists of only non-executive directors
- consists of a majority of independent directors
- is chaired by an independent chair, who is not chair of the Board
- has at least three members.

The Company's current Audit Committee consists of 3 board members, two of whom are non-independent directors. The Chairperson is a non-independent non-executive director and the other members are a non-independent non-executive director (formerly executive chairman) and an independent non-executive director.

Recommendation 4.3: The audit committee should have a formal charter.

The audit committee charter is available on the Company website.

Principle 5 – Make timely and balanced disclosure

Companies should promote timely and balanced disclosure of all material matters concerning the company.

Recommendation 5.1: Companies should establish written policies designed to ensure compliance with ASX Listing Rule disclosure requirements and to ensure accountability at a senior executive level for that compliance and disclose those policies or a summary of those policies.

The Company has obligations under the Corporations Act and ASX Listing Rules to keep the market fully informed of information which may have a material effect on the price or value of its securities. The Company discharges these obligations by releasing information to ASX in the form of an ASX release or disclosure in other relevant documents (e.g. the Annual Report).

The Company has a continuous disclosure program in place designed to ensure the compliance with ASX Listing Rule disclosure and to ensure accountability at a senior executive level for compliance and factual presentation of the Company's financial position.

Principle 6 – Respect the rights of shareholders

Companies should respect the rights of shareholders and facilitate the effective exercise of those rights.

Recommendation 6.1: Companies should design a communications policy for promoting effective communication with shareholders and encouraging their participation at general meetings and disclose their policy or a summary of that policy.

The Company is committed to the promotion of investor confidence by ensuring that trade in its securities takes place in an efficient, competitive and informed market. The Board Charter recognises the importance of forthright communication as a key plank in building shareholder value and that to prosper and achieve growth the Company must (among other things) earn the trust of employees, customers, suppliers, communities and security holders by being forthright in its communications and consistent in its fulfilment of obligations.

Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014



Principle 7 – Recognise and manage risk

Companies should establish a sound system of risk oversight and management and internal control.

Recommendation 7.1: Companies should establish policies for the oversight and management of material business risks and disclose a summary of those policies.

Management determines the Company's risk profile and is responsible for overseeing and approving risk management strategy and policies, internal compliance and internal control. The Company's process of risk management and internal compliance and control includes:

- establishing the Company's goals and objectives, and implementing and monitoring strategies and policies to achieve these goals and objectives;
- continuously identifying and reacting to risks that might impact upon the achievement of the Company's goals and objectives, and monitoring the environment for emerging factors and trends that affect these risks;
- formulating risk management strategies to manage identified risks and designing and implementing appropriate risk management policies and internal controls; and
- monitoring the performance of, and continuously improving the effectiveness of, risk management systems and internal compliance and controls, including an ongoing assessment of the effectiveness of risk management and internal compliance and control.

Recommendation 7.2: The Board should require management to design and implement the risk management and internal control system to manage the company's material business risks and report to it on whether those risks are being managed effectively. The Board should disclose that management has reported to it as to the effectiveness of the Company's management of its material business risks.

The responsibility for undertaking and assessing risk management and internal control effectiveness is delegated to management. Management is required by the Board to report back on the efficiency and effectiveness of risk management, inter alia, by benchmarking the Company's performance against industry standards.

The risk profile of the Company contains both financial and non-financial factors including material risks arising from pricing, competitive position, currency movements, operational efficiency, product quality and investments in new projects.

To mitigate these risks, the company has in place an experienced Board, regular Board meetings, financial annual audit and half year review, rigorous appraisal of new investments, and advisers familiar with the company. The Board's collective experience will enable accurate identification of the principal risks that may affect the Company's business. Key operational risks and their management are recurring items for deliberation at Board Meetings.

Recommendation 7.3: The Board should disclose whether it has received assurance from the chief executive officer (or equivalent) that the declaration provided in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks.

The Chief Executive Officer and the Chief Financial Officer confirm in writing to the Board that the financial reports of the Company for the financial year:

- present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards;
- the statement given in paragraph (a) above is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Board; and
- the company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

Principle 8 – Remunerate fairly and responsibly

Companies should ensure that the level and composition of remuneration is sufficient and reasonable and that its relationship to performance is clear.



Corporate Governance Statement

FOR THE YEAR ENDED 30 JUNE 2014

Recommendation 8.1: The Board should establish a remuneration committee.

The Board has established a remuneration committee. The Committee consists three non-executive directors.

Recommendation 8.2: Companies should clearly distinguish the structure of non-executive directors' remuneration from that of executive directors and senior executives.

Executive Directors remuneration packages may comprise:

- (a) salary and associated superannuation;
- (b) performance based bonuses; and
- (c) equity based long term incentives.

Non-Executive Directors receive fixed directors fees only, and do not participate in any performance-based remuneration. Fixed directors' fees may be paid in the form of cash, shares, share options or a combination of these. Shares and share options are issued on similar terms to previous issues by the entity and are considered to be in lieu of cash, not based on performance of the entity.

Full remuneration disclosure, including superannuation entitlements, and the number of meetings of the Remuneration Committee is provided by the Company in its annual report. The Remuneration Committee ensures that all equity based executive remuneration is made within the guidelines set by plans approved by Shareholders.

Departure from Best Practice Recommendations

From 1 July 2013 to 30 June 2014, the Company complied with each of the Eight Essential Corporate Governance Principles and Best Practice Recommendations published by the ASX Corporate Governance Council, other than in relation to the table below.

Recommendation	Notification of Departure	Explanation from Departure
2.1	The majority of the Board is not comprised of independent directors.	The Board has reviewed its composition and considers that the relationships which define four of the five directors as non-independent have been and continue to be of benefit to the Company. It is not considered that the relationships of non-independent directors affect their capacity to bring independent judgement to bear on Board decisions.
2.2	The chair should be an independent director.	The Board has four other directors and believe that the position of the Chairman as a former executive does not prejudice the Company's corporate governance.
2.4	The Board has not established a nomination committee.	The whole Board carries out the duties which would otherwise be undertaken by the nomination committee. The need for a nomination committee will be reviewed annually.
4.2	The audit committee is not comprised of a majority of independent directors, with an independent chair.	The audit committee is comprised of three directors, two of whom are defined as non-independent. The Board considers that the membership of the audit committee is the most appropriate which can be made from the present membership of the Board. The Board considers that the expertise of the audit committee enables it to fulfil its charter and does not consider the appointment of further or different directors to be desirable merely to change the composition of the audit committee.

The Phylogica Limited Corporate Governance Principles & Practices Manual is available on the Company's website www.phylogica.com

ASX Additional Information

FOR THE YEAR ENDED 30 JUNE 2014



1. Quoted Securities

The security holder information set out below was applicable as at 22 August 2014.

(a) Distribution of Security Numbers

Category (size of holding)	Ordinary Shares		Quoted Options	
	Shareholders	Shares	Optionholders	Options
1 – 1,000	96	22,857	4	103
1,001 – 5,000	98	315,869	1	4,000
5,001 – 10,000	157	1,363,582	-	-
10,001 – 100,000	748	34,535,637	27	1,587,102
100,001 and over	629	965,831,422	92	163,066,075
Total	1,728	1,002,069,367	124	164,657,280

There are 724 shareholders holding less than a marketable parcel at a price of \$0.013, totalling 9,819,253 shares.

There are 53 optionholders holding less than a marketable parcel at a price of \$0.002, totalling 5,966,358 options.

(b) Voting Rights

On a show of hands every person present who is a member or a proxy, attorney or representative of a member has one vote and upon a poll every person present who is a member or a proxy, attorney or representative of a member shall have one vote for each share held.

(c) Twenty Largest Security Holders

The names of the twenty largest holders of ordinary shares are listed below:

Name	Number of Ordinary Shares	% of Issued Capital
HOCKINGS B E + D C	225,406,101	22.49
SIETSMA HOLDINGS PTY LTD	82,000,000	8.18
SALVATORE BONADDIO	39,581,834	3.95
ANDREW SWIFT	28,709,467	2.87
TELETHON INSTITUTE FOR CHILD HEALTH RESEARCH	20,605,501	2.06
JOHN BAIRD	18,483,430	1.84
NAVIGATOR AUSTRALIA LTD	16,000,000	1.60
CITICORP NOMINEES PTY LTD	15,101,673	1.51
ADAM BONADDIO	15,066,797	1.50
CUSTOM BINDERS PTY LTD	14,095,613	1.41
MONSLIT PTY LTD	14,000,000	1.40
PATRICK SIMON HASSETT	13,771,930	1.37
WITTENOON SURVIVAL SUPER	13,443,263	1.34
WATT P M & ENRIQUEZ-WATT M	12,480,660	1.25
SUSAN ELIZABETH EVANS	10,000,000	1.00
JELBART J A & M H	9,837,398	0.98
RICHARD MILES HOPKINS	9,333,333	0.93
MARIA ENRIQUEZ-WATT	9,000,000	0.90
GTC IND PTY LTD	7,761,298	0.77
GDM SERVICES PTY LTD	7,395,765	0.74
Total	582,074,063	58.09



ASX Additional Information

FOR THE YEAR ENDED 30 JUNE 2014

The names of the twenty largest holders of listed options are listed below:

Name	Number of Listed Options	% of Issued Capital
HOCKINGS BE & DC	61,902,329	37.59
BERNARD HOCKINGS	15,941,927	9.68
JELBART JA & MH	8,773,811	5.33
CITICORP PTY LTD	8,474,576	5.15
PATRICK SIMON HASSETT	5,847,953	3.55
ADAM BONADDIO	5,847,953	3.55
CUSTOM BINDERS PTY LTD	4,385,965	2.66
GTC IND PTY LTD	3,237,289	1.97
JOHN BAIRD	2,923,977	1.78
DEREK RONALD SLANEY	2,556,567	1.55
GREGORY STEWART MCDONALD	1,669,393	1.01
CADEX PETROLEUM PTY TLD	1,606,900	0.98
ANTHONY DALBOSCO	1,402,667	0.85
GRAHAM NORMAN WENDT	1,259,862	0.77
SALVATORE BONADDIO	1,257,862	0.76
ADRIAN BONADDIO	1,257,862	0.76
SYBIL MARIE GIDDY	1,229,167	0.75
FINESSE CORPORATION PTY LTD	1,158,459	0.70
FAIRBURN PTY LTD	1,098,167	0.67
RIJEAN PTY LTD	1,000,000	0.61
Total	132,832,686	80.67

(d) Substantial Shareholders

The names of the substantial shareholders listed in the Company's share register as at 22 August 2014 were:

Name	Number of Ordinary Shares	% of Issued Capital
B Hockings Superannuation Fund	225,406,101	22.49
Sietsma Holdings Pty Ltd	82,000,000	8.18
Total	307,406,101	30.67

(e) On Market Buy Back

There is no on-market buy-back scheme in operation for the company's quoted shares or quoted options.

2. Unquoted Security Holder Information

The information on unquoted securities set out below was applicable as at 28 August 2014.

(a) Unquoted Option Holders

(i) Distribution of unquoted option holder numbers.

Category (size of holding)	No of Option Holders	No of Options
100,001 and over	20	8,125,000
Total	20	8,125,000

(ii) Voting Rights.

Unlisted options do not entitle the holder to any voting rights.

(iii) Holders of more than 20% of unquoted options.

There are no holders, holding more than 20% of the unquoted options on issue.





PHYLOGICA LIMITED

