PHG Management Limited

Directors' report and financial statements

Registered number 4250960

For the year ended 31 March 2005

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Directors' report

The directors present their annual report and audited financial statements for the year ended 31 March 2005.

Principal activity

The principal activity of the company is that of an intermediate holding company.

Business review

The primary purpose of the company is a vehicle for paying interest. The directors believe the company will continue in this manner for the foreseeable future.

Results and dividend

The results for the period are set out in detail on page 4.

The directors do not recommend the payment of a dividend *(2004: £Nil)*.

Directors and directors' interests

The directors who served during the period and to the date of these financial statements were as follows:

J Brock
J Harper (resigned 29 September 2004)
N Harris
N Moreton
D Quinn
J Robinson
C Margerit (appointed 29 September 2004)

The directors who held office at the period end had no disclosable interest in the shares of the company.

According to the register of directors' interests, no rights to subscribe for shares or debentures of the company were granted to any of the directors or their immediate families, or exercised by them during the financial period.

The directors' interests in the shares of other group companies are disclosed in the directors' report of the parent company, Paragon Healthcare Group Limited.

Auditors

In accordance with Section 385 of the Companies Act 1985, a resolution for the re-appointment of KPMG LLP as auditors of the company, is to be proposed at the forthcoming Annual General Meeting.

By order of the board

NK Moreton

9 December 2005

NK Moreton
Company Secretary

Garrick House
2 Queen Street
Lichfield
Staffordshire
WS13 6QD

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the company and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

KPMG LLP
2 Cornwall Street
Birmingham
B3 2DL

Independent auditors' report to the members of PHG Management Limited

We have audited the financial statements on pages 4 to 12.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the directors' report and, as described on page 2, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the company is not disclosed.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the directors' remuneration report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the directors' remuneration report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the directors' remuneration report to be audited.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 March 2005 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG LLP

9 December 2005

KPMG LLP
Chartered Accountants
Registered Auditor

Profit and loss account
for the year ended 31 March 2005

	Note	**2005**	2004
		£	£
Operating expenses	*2*	**20,764**	(11,939)
Operating profit/(loss)		**20,764**	(11,939)
Income from interest in group undertakings		**30,419**	-
Interest receivable and similar income	*3*	**4,211,285**	3,285,225
Interest payable and similar charges	*4*	**(16,298,097)**	(11,085,634)
Loss on ordinary activities before taxation		**(12,035,629)**	(7,812,348)
Tax on loss on ordinary activities	*7*	**3,246,281**	2,605,790
Retained loss for the financial period	*14*	**(8,789,348)**	(5,206,558)

There are no recognised gains or losses other than the loss for the current and preceding years.

There is no material difference between the reported profit and the historical cost profit. Accordingly, no note of historical cost profits and losses has been prepared.

Movements in reserves are set out in note 14 to the financial statements.

Balance sheet
at 31 March 2005

	Note	2005 £	2005 £	2004 £	2004 £
Fixed assets					
Investments in subsidiary undertakings	8		**71,136,074**		71,136,074
Current assets					
Debtors	9	**78,154,063**		40,252,298	
Cash		**688,559**		1,342	
		78,842,622		40,253,640	
Creditors: Amounts falling due within one year	10	**(73,651)**		(5,045,148)	
Net current assets					
Due within one year		**7,839,479**		(880,791)	
Debtors due after more than one year	9	**70,929,492**		36,089,283	
			78,768,971		35,208,492
Total assets less current liabilities			**149,905,045**		106,344,566
Creditors: Amounts falling due after more than one Year	11		**(169,022,609)**		(116,672,782)
Net liabilities			**(19,117,564)**		(10,328,216)
Capital and reserves					
Called up share capital	12		**2,000,000**		2,000,000
Profit and loss account	13		**(21,117,564)**		(12,328,216)
Shareholders' funds	14		**(19,117,564)**		(10,328,216)

These financial statements were approved by the board of directors on 9 December 2005 and were signed on its behalf by:

N Moreton

N Moreton
Director

Notes
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the company's financial statements:

Basis of preparation

The financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards and financial reporting standards.

The accounts have been prepared on a going concern basis, notwithstanding net liabilities of £19,117,564 which the directors believe to be appropriate for the following reasons. The company is dependent on committed loan facilities from its bankers which are only repayable if Paragon Healthcare Group Limited does not comply with banking covenants. The group's forecasts for the next year show that the group should materially be in compliance with all covenants.

The directors therefore believe it remains appropriate to prepare the financial statements on a going concern basis. The financial statements do not include any adjustments that would result from the basis of preparation being inappropriate.

The company is exempt by virtue of s228 of the Companies Act from the requirement to prepare group accounts. These financial statements present information about the company as an individual undertaking and not about its group.

At 31 March 2005, the company was a wholly owned subsidiary of Paragon Healthcare Group Limited, which prepares consolidated group financial statements including a group cash flow statement. In accordance with FRS 1, no cash flow statement is, therefore, included in these financial statements.

Turnover

Turnover represents total fees and amounts receivable for services provided in the United Kingdom.

Taxation including deferred taxation

The charge for taxation is based on the loss for the period and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred taxation is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Related party transactions

As permitted by paragraph 3(a) of Financial Reporting Standard 8 "Related party disclosures", the company has taken advantage of the exemption for 90% subsidiaries not to disclose related party transactions with group entities. There were no other related party transactions entered into by the company during the period.

Notes *(continued)*

2 Operating expenses

	2005 £	2004 £
Operating expenses are stated		
after charging		
Direct expenses and consumables	**(28,514)**	-
Auditors' remuneration including expenses:*		
Audit fee	**5,500**	5,875
Other external charges	**2,250**	6,064
	(20,764)	11,939

* In addition, £349,492 *(2004: £209,032)* has been capitalised within debt issue costs.

3 *Interest receivable and similar income*

	2005 £	2004 £
Interest received from fellow subsidiary undertakings	**4,089,156**	3,283,848
Bank interest received	**122,129**	1,377
	4,211,285	3,285,225

4 Interest payable and similar charges

	2005 £	2004 £
On bank loans and overdrafts	**10,467,259**	5,918,718
On all other loans	**5,454,493**	4,771,014
Interest payable to fellow subsidiary undertakings	**376,345**	395,902
	16,298,097	11,085,634

Included within interest payable on bank loans is debt issue cost amortisation and write-off of £2,496,577 *(2004: £641,564)*.

5 Directors' emoluments

The directors received the following emoluments in respect of their services to this company and its subsidiaries:

	2005 £	2004 £
Emoluments	**495,964**	788,344
Pension contributions	**75,165**	67,080
	571,129	855,424

Notes *(continued)*

5 Directors' emoluments *(continued)*

Emoluments of the highest paid director are as follows:

	2005 £	2004 £
Emoluments	**190,642**	312,745
Pension contributions	**31,140**	28,080
	221,782	340,825
	Number	Number
Number of directors with benefits accruing under a defined contribution scheme	**3**	3

6 Staff costs and numbers

The company had no employees (other than the directors).

7 Tax credit on loss on ordinary activities

	2005 £	2004 £
UK corporation tax		
Current tax on income for the period	**(3,246,218)**	(2,344,727)
Adjustment in respect of prior periods	**(63)**	(261,063)
Tax on loss on ordinary activities	**(3,246,281)**	(2,605,790)

Factors affecting the tax credit for the current period

The current tax credit for the period is higher *(2004: lower)* than the standard rate of corporation tax in the UK (30%, *2004: 30%*). The differences are explained below:

	2005 £	2004 £
Current tax reconciliation		
Loss on ordinary activities before tax	**(12,035,629)**	(7,812,348)
Current tax at 30%	**(3,610,689)**	(2,343,704)
Effects of:		
Losses not utilised via group relief	**373,597**	-
UK dividends not taxable	**(9,126)**	-
Other timing differences	**-**	(1,023)
Adjustments to tax charge in respect of previous periods	**(63)**	(261,063)
Total current tax credit (see above)	**(3,246,281)**	(2,605,790)

Factors that may affect future tax charges

The company has an unprovided deferred tax asset of £1,003,303 *(2004: £635,541)* in respect of losses carried forward.

The potential deferred tax asset has not been recognised as there is insufficient evidence that it would be realised in the foreseeable future as the company is likely to generate losses in excess of the profits generated by other group companies.

Notes *(continued)*

8 Investments

	Shares in subsidiary undertaking £
Cost	
At beginning and end of year	71,136,074

The principal subsidiary undertakings of the company all of which are 100% owned and registered in Great Britain are summarised as follows:

Subsidiary	Nature of business	Country of incorporation	Holding	Proportion held
Paragon Healthcare Limited	Intermediate holding company	England	Ordinary	100%
Milbury Community Services Limited*	Community Care	England	Ordinary	100%
Milbury Care Services Limited*	Community Care	England	Ordinary	100%
Voyage Limited	Community Care	England	Ordinary	100%
Opportunities UK Limited*	Employment Services	England	Ordinary	100%
HFF Limited*	Employment services	England	Ordinary	100%
Burymill Limited	Dormant	England	Ordinary	100%
Headwind Limited	Dormant	England	Ordinary	100%
Milbury Partnerships Limited*	Intermediate holding company	England	Ordinary	100%

* Held by a subsidiary undertaking

9 Debtors

	2005 £	2004 £
Amounts falling due within one year:		
Prepayments	**12,500**	197,225
Group relief receivable	**7,212,071**	3,965,790
	7,224,571	4,163,015
Amounts falling due after more than one year:		
Amounts owed by group undertakings (see note 11)	**70,929,492**	36,089,283
	78,154,063	40,252,298

10 Creditors: Amounts falling due within one year

	2005 £	2004 £
Bank loans and overdrafts	**(19,970)**	4,992,164
Other creditors	**93,621**	52,984
	73,651	5,045,148

Bank loans and overdrafts comprises a bank loan repayment of £1,176,900 and debt cost amortisation of £1,196,870.

Notes *(continued)*

11 Creditors: Amounts falling due after more than one year

	2005	2004
	£	£
Bank loans and overdrafts	**105,112,182**	62,127,763
Other loans	**47,170,671**	49,986,178
Amounts due to group undertakings	**16,739,756**	4,558,841
	169,022,609	116,672,782

Analysis of debt:

	£	£
Debt can be analysed as falling due:		
In one year or less, or on demand	**(19,970)**	4,992,164
Between one and two years (see note below)	**(1,196,870)**	5,892,164
Between two and five years	**106,309,052**	32,527,322
In five years or more	**47,170,671**	73,694,455
	152,262,883	117,106,105
Amounts repayable in more than 5 years:		
Bank loans	**-**	23,708,277
Other loans	**47,170,671**	49,986,178
	47,170,671	73,694,455

Included within bank loans and overdrafts is an amount of £5,107,788 *(2004: £1,817,240)* in respect of unamortised loan costs. These costs are being written off over 5 years, therefore £1,196,870 of debt cost amortisation in 2006 has been classified as debt due between one and two years in the analysis above.

Bank loans comprise Term Loans of £85,000,000 (being part of a £95,000,000 facility) and a Capex Facility Loan of £25,200,000 (being part of a £62,000,000 facility).

Other loans due after more than one year comprise subordinated fixed rate Loan Notes.

The interest rate and repayment terms of these loans is as follows:

Debt instrument	*Loan balance (£)*	*Interest rate*	*Repayment terms*
Term Loan A	50,000,000	LIBOR + 1.75%	July 2009*
Term Loan B	25,000,000	LIBOR + 3.00%	July 2009*
Term Loan C	10,000,000	LIBOR + 4.25%	July 2009*
	85,000,000		
Capex Facility Loan	25,200,000	LIBOR + 2.75%	July 2009*
Subordinated fixed rate loan notes	47,170,671	10% / 15%	2011

Notes *(continued)*

11 Creditors: Amounts due after more than one year *(continued)*

*Part repayment is required if certain events and cash flows occur prior to July 2009. As it is not possible to accurately determine whether these events and cash flows will occur, all bank loans have been classified as due between two and five years, except £1,176,900 which was repaid in April 2005.

A revolving credit facility of £5,000,000 is also available to the company. Interest on any amounts drawn down is charged at LIBOR + 2.25%.

The company has entered into an interest rate swap arrangement which fixes the LIBOR payable on part of the bank loans at 5.735%.

The company has provided security for the bank borrowings of itself, and fellow subsidiary undertakings by way of a first legal mortgage on property assets and a fixed and floating charge on all other assets.

The amounts receivable and repayable with group undertakings have no fixed repayment date, but are due after more than one year and bear interest at a rate based on the group's weighted average cost of capital.

12 Called up share capital

	2005	2004
	£	£
Authorised:		
2,500,000 ordinary shares of £1 each	**2,500,000**	2,500,000
Allotted, called up and fully paid:		
2,000,000 ordinary shares of £1 each	**2,000,000**	2,000,000

13 Profit and loss account

	£
At beginning of year	(12,328,216)
Retained loss for the year	(8,789,348)
At end of year	**(21,117,564)**

14 Reconciliation of movements in shareholders' deficit

	2005	2004
	£	£
Opening shareholders' deficit	**(10,328,216)**	(5,121,658)
Loss for the financial period	**(8,789,348)**	(5,206,558)
Closing shareholders' deficit	**(19,117,564)**	(10,328,216)

15 Contingent liabilities

The company has provided security for the bank borrowings of itself, it's parent and fellow subsidiary undertakings by way of a first legal mortgage on property assets and fixed and floating charges on all other assets.

Notes *(continued)*

16 Ultimate parent undertaking

The company's immediate and ultimate parent undertaking is Paragon Healthcare Group Limited which is registered in England and Wales.

Group financial statements of Paragon Healthcare Group Limited can be obtained from:

The Company Secretary
Paragon Healthcare Group Limited
Garrick House
2 Queen Street
Lichfield
Staffordshire
WS13 6QD