

**Cygnet Health Care Limited**

**Directors' report and financial  
statements**

**Registered number - 02141256**

**Year ended 31 October 2010**

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## Chairman's statement

Cygnnet Health Care Limited is the main trading entity in the Cygnnet 2008 Limited Group ("Cygnnet")

Cygnnet is a leading provider of psychiatric care services and during the year has continued its strategy of moving into more specialist areas, including the opening and development of new facilities. During the year we completed the development of a 12 bed step down lodge on our Kewstoke site. We also completed the development and opened a new 47 bed unit in Derby which provides an in-patient mental health service in a low secure setting. Further, a project is well underway to develop a 16 bed low secure service at our hospital in Godden Green.

Our business is supported by strong relationships with its customers – Cygnnet did business with 149 NHS purchasing bodies during 2010, with formal agreements in place with 31 of these bodies.

The NHS, our main purchasing customer, has been learning more about how it will be expected to deliver financial cost cutting without affecting front line services. This will be a very difficult task to achieve and, as a major provider of services to the NHS, we see our role of working in partnership with them as key to both their and our success in the future.

This will mean that we have to ensure that we provide the best quality in our services that our customers want at the right price. Remaining competitive in a market full of providers, both NHS and the Independent Sector, will be a challenge that we are fully geared up to meeting. With the support of all our dedicated staff across the Company, we look forward to being the most successful independent sector provider to the NHS and our private patients. Cygnnet strives to maintain an active dialogue with all of its customers to meet their needs.

"This is my life and I need to make the most of it" – the words of one of our many Service Users who have made progress on their path of recovery in one of our hospitals. The road to recovery can be a rocky one for some Service Users and we have been working hard to focus on tools that we can use to provide an environment to assist them on their way. The roll out of Recovery Training across the whole Group is well underway and this helps us identify what the Service Users want and how they see themselves getting there.

This focus on delivering more to our Service Users is part of the Cygnnet Vision which is being launched (details below in our COO review), to give staff, customers and Service Users alike, clarity about what they can expect from Cygnnet Health Care and how we intend to improve and grow our business by focussing on key issues like quality and value.

### Our people

We are delighted to welcome Gerry Magee as a Non Executive Director on our Board, following the resignation of Mike Parsons. In addition to his role as CFO, Mark Ground has taken on the role of Company Secretary for Cygnnet 2008 Limited.

2010 has seen the influx of several new members to our hospital teams who have bolstered our existing management and staff. I believe we have a first class team who together are able to do such a fantastic job of caring for our patients and improving their lives day by day.

### Results and Outlook

Overall, Cygnnet had a respectable year. The Group's results in 2010 showed a solid performance helped by a number of good performances across our sites. We remain cautiously optimistic about our prospects in what, for the Independent Sector is an evolving market.

I would like to take this opportunity to thank all management and staff for their commitment and skill.

**Ken Wilson**  
Executive Chairman and Chief Executive Officer

## Chief Operating Officer's review

In 2010 we made further commitment to our Vision statement **Service Users are at the heart of our business, as are our customers**

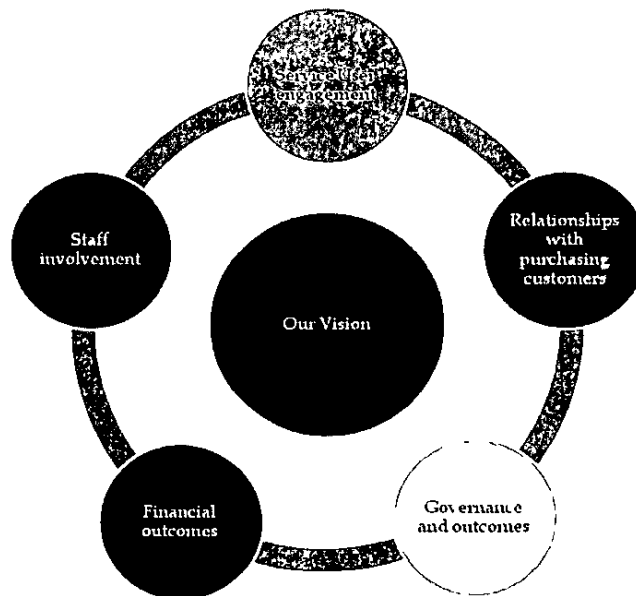
In order to ensure that we have the right skills to deliver our services and evidence our successes through outcomes, we have grown our Corporate Governance team with the addition of a Quality Assurance Manager and recruited a number of other experienced clinicians into our senior team. In addition, to ensure we can seize opportunities in the rapidly changing market place we have appointed a NHS Partnership Development Director, responsible for enhancing and growing our business with the NHS

### Our strategic vision

Our Vision is to strive to develop our business by

- delivering outstanding quality and value for money as defined by Outcomes,
- engaging with our Service Users to make a difference, and
- inspiring our staff to deliver and share in achieving these goals

Our strategic vision has **five key areas**



### Service User Engagement

We are committed to helping our Service Users to live their lives to the full and we aim to listen to what Service Users want and to help them in their recovery path

- Encouraging service user participation in all decisions we make that affect their futures,
- Using tools such as Recovery Star to help staff and Service Users focus on the way forward, and
- Listening to feedback and comments on our services and acting on their ideas

### **Relationship with purchasing customers**

We aim to offer services that exceed accepted quality standards and deliver outstanding value. We listen to our customers requirements and are responsive and adaptive in creating solutions, not only for current needs but what they may need in the future.

- using outcome measurements that evidence our commitment to delivering a quality service – all our hospitals have met all their CQUIN outcomes to date,
- delivering information in a format that customers can use and using that information ourselves to improve practice, and
- adding value to our services without adding cost

### **Governance and Outcomes**

We are a professional organisation which applies integrity in creating services that are required by Service Users and customers. We aim to be transparent in demonstrating simple yet powerful proof of our success and failures and how we constantly strive for improvement.

- we continue to invest in our Clinical Governance team,
- we will deliver a quarterly report and action plan, always striving to achieve excellence, and
- we will work to develop Outcome measurements and to collate Service User and staff feedback

### **Financial Outcomes**

We offer quality services at a fair price by understanding customers' needs in the market. We offer efficient services by controlling costs, spending wisely and investing in people and infrastructure. We demonstrate value through evidence on episode costs, outcomes, shorter lengths of stay and completed care pathways.

- the CQUIN delivery helps to evidence value for money,
- we aim to deliver a quality service at the right price,
- we will work hard to achieve good cost control but not at the expense of clinical standards, and
- we will continue to invest in the development and growth of the business

### **Staff involvement**

Our staff are central to delivering an efficient, high quality service to Service Users. Working in a supportive yet dynamic environment provides staff with the opportunity to be involved in decisions whilst encouraging them to take responsibility in their own areas. We deliver value to our staff through training, personal development, remuneration, ownership of the Company and team spirit.

- we believe in regular and constructive appraisals, competency models, and having the right supervision, development and training for all our staff

Having a clear focus on the direction the Company is travelling and what our core values are, allows all of our staff, customers and Service Users to join in making Cygnnet Health Care the Company to work with, the Company to commission with and the Company to recover with.

**Nicky McLeod**  
Chief Operating Officer

## Chief Financial Officer's review

The year to 31 October 2010 was another solid year for Cygnnet. The financial highlights for the Group for 2010 are as follows.

- revenue of £81.7 million (2009: £82.2 million),
- Group EBITDA of £22.5 million, up £0.4 million (2%) on 2009,
- Net cash inflow from operating activities, before interest and tax of £22.7 million, up £2 million (10%) on the prior year,
- capital expenditure of £6.7 million during the year,
- repayment of term debt of £2.8 million and draw down on the development facility of £1.0 million, and
- cash at bank and in hand of £4.9 million at year end

Group revenue remained stable at £81.7 million, perhaps less than expected, due to the requirement to retool a number of our wards during the year. The retools are in response to our customer needs. Available beds increased by 59 (9%) following the opening of Derby and Kewstoke Lodge.

Operating expenses for the year remained at circa £68 million, despite pre and post opening costs at our new hospital in Derby, and increased costs for Oakdale – the fastest growing part of the business. Subject to the tough tariff environment, we would expect operating margins to improve as some of the more recently opened sites mature.

The consolidated loss before taxation attributable for the year was £5.6 million (2009 loss: £6.9 million). The loss is predominantly as a result of the negative change by £8.5 million in fair value of the interest rate swap contract, noted below.

## Financing and cash flow

Net cash inflow from operating activities, before interest and tax of £22.7 million, up £2 million (10%) on the prior year. Aside from bank interest and repaying loans, a significant proportion of operating cash flow is reinvested into the business to fund Capital Expenditure. During the year the business spent £6.7 million on capital expenditure of which only £1 million was funded using the Groups' development facility.

In addition to internally generated cash flow, the financing in 2008 continues to facilitate Cygnnet's expansion plans. At year end the Group had a term loan of £138.3 million (2009: £141.1 million) and a development loan of £15 million which was £4.7 million drawn (2009: £3.7 million). In addition the Group has a £5 million revolving credit facility which was not being used at year end.

Financing costs were £19.2 million in 2010, compared to £21.3 million in 2009. £8.5 million (2009: £10.5 million) of the financing cost was due to an accounting adjustment, which arose from the recognition of change in the fair value of the Group's 25 year interest rate swap contracts on a mark to market basis. The interest swap is expected to amortise over the term of the swap contracts as payments are made in line with the originally agreed interest payment profile. Accordingly no adverse cash impact is expected.

The bank credit agreements require compliance with certain financial covenants including maintenance of certain ratios and security. During the year, these continued to be maintained.

**Mark Ground**  
Chief Financial Officer

## **Cygnnet 2008 Limited Directors and Senior Officers**

### **Ken Wilson, Executive Chairman and Chief Executive Officer**

Ken was appointed Executive Chairman in 1991. In collaboration with Cygnnet's founder, John Hughes, Ken has worked hard to build a market leading independent provider of mental health care, primarily to the NHS. Ken has over 20 years of experience at Board level in various organisations and since 2004 he has also been a Non-Executive Director of Barchester Healthcare. Ken was appointed Chief Executive Officer of Cygnnet in 2008.

### **John Hughes, Founder and Executive Director**

After developing twelve new psychiatric hospitals in the United States, John acquired the loss making Priory Hospital in London in 1980. John was subsequently responsible for developing the first seven Priory hospitals. John founded Cygnnet in 1988 and has seen the organisation flourish and grow to become one of Britain's largest providers of psychiatric services. In 2008 John won the Outstanding Contribution Award at the Laing & Buisson Independent Healthcare Awards.

### **Nicky McLeod, Chief Operating Officer**

Nicky comes from a clinical background having initially completed training as a RGN in 1980. After developing her management career with a pharmaceutical company Nicky joined Cygnnet in 1998 as a Hospital Director. After two years Nicky was promoted to Regional Director with responsibility for three Cygnnet hospitals. Nicky became the Managing Director of five Cygnnet hospitals before being appointed Chief Operating Officer with responsibility for operations at all Cygnnet units.

### **Mark Ground, Chief Financial Officer**

Mark is an FCA and comes from a strong professional background, having spent eight years with Arthur Andersen, the last four as a management consultant, before moving on to work for the listed Whitehead Mann Group plc for six years, where he held the position of Group Finance Director and Company Secretary. Mark joined Cygnnet in 2008 and is responsible for all matters financial including leading the finance function, management and statutory reporting, treasury and cash management and commercial analysis.

### **Paul Brosnan, Non Executive Director**

Paul represents the interests of Grove Investments UK Ltd, Cygnnet's second largest shareholder. Paul is a business graduate from Dublin City University and also has a Masters Degree from University College Dublin. He worked for Allied Irish Bank in their Capital Markets division and latterly the Kerry Group before starting his first company, Casterbridge Care & Education Limited, a premium operator of children's day nurseries and preschools.

### **Craig Hughes, Non Executive Director**

Craig is a serial entrepreneur, having created a number of successful technology companies in Silicon Valley, including Trickplay (Internet TV software platform), Gumstix (embedded Linux hardware), Deersoft (open source anti-spam acquired by McAfee), and Panop (real time optimization acquired by Kana).

### **Gerry Magee, Non Executive Director**

Gerry also represents the interests of Grove Investments UK Ltd, Cygnnet's second largest shareholder. Gerry joined the Board in November 2010, replacing Mike Parsons. Gerry holds a number of Directorships including being Chairman of Wellness Foods. Gerry is a Chartered Accountant and a former senior partner at Deloitte.

## Directors' report

The directors present their report and audited financial statements for the year ended 31<sup>st</sup> October 2010

### Directors

The following directors have held office during the year

K A R Wilson  
J C Hughes  
M G Ground  
N J McLeod

None of the directors held any beneficial interest in shares of the Company during the year

### Principal activities

The principal activity of Cygnnet Health Care Limited ("the Company") is that of an operating company, operating psychiatric and elderly healthcare facilities. Cygnnet Health Care Limited is able to continue to carry out this trade as it leases the psychiatric hospitals and elderly health care facilities from Cygnnet PropCo Limited (a related undertaking), through a master lease agreement, and Stac Healthcare Limited through a lease agreement.

### Business review

Cygnnet now operates 751 beds (2009 692 beds) spread through a portfolio of 18 quality facilities. The key performance measures that the Board of Directors ("The Board") uses to monitor progress of the Company and its subsidiaries ("The Group") against its objectives are

- Occupancy rates,
- Customer satisfaction and patient care outcomes,
- User experience and involvement,
- Staff and management skills development,
- Careful attention to clinical risk management,
- Fee levels and pricing,
- EBITDA,
- Margin,
- Staff and agency costs, and
- Staff turnover

### Future prospects

Cygnnet's strategy is to continue to grow and develop the business through

- furthering geographical coverage,
- development and broadening of current service lines,
- extension of service lines and care pathways,
- reacting to changing dynamics of our market and customers, in particular the NHS, and
- providing an environment and culture which promotes excellence in what we do and a fulfilling place for staff to pursue their careers

### Key risks and uncertainties

The Board considers that the key risk and uncertainty facing the Group is fluctuations in interest rates given its level of gearing post the refinancing. However, the Group has hedged 97% of its term debt borrowings which mitigates the risk of any increase in interest rates but also prevents the Group benefiting from any reduction in rates. This hedging fixes the cost of funds allowing the Group to plan the long term cash flow with certainty.

The business is supported by strong future demand based on the demographics of the UK population. These factors combined should protect the Group from the current difficult economic environment. The Group's strategy is one of continued growth through maintaining close links with customers and developing services to meet their requirements.



## Directors' report *(continued)*

The Group believes that due to the economic situation, another area that may be perceived as a risk is the ability in the future to secure financing to enable the Group to continue to finance any acquisitions and developments. Due to existing facilities held and the ability to generate cash the Group does not consider this is a major risk.

Other areas of financial risk which include credit risk, liquidity risk and cash flow risk are considered to be well controlled and are dealt with in note 16 to the accounts.

Other non-financial risks include

- **Regulatory risk** arising from adverse healthcare commission inspections and breaches of Health and Safety regulations. The Company engages in clinical audit, internal audit of systems, controls and continuous monitoring of performance of employees and customer and patient satisfaction. Additionally, internal managers' inspections are carried out twice a year at each unit. The Board is also sensitive to the need to comply with Health and Safety regulations and is engaged on continuous training and upgrading of manuals and management responsible for ensuring that the Company remains up to date.
- **Reputational risk** arising from adverse publicity. The Group believes this is only likely to occur in relation to poor customer and/or patient care and has multilayered systems to prevent this occurring and manage any challenges arising.
- **Competition**. The Company monitors competition closely to ensure that it remains competitive in the market place. The Group manages the risk associated with demand fluctuations by offering diversified services and monitoring demand, converting unused capacity to alternative services when appropriate. Cygnnet monitors prices charged both internally and externally to ensure that its services are appropriately priced to compete and provide value for customers.

### Employee involvement

The directors recognise the importance of human resources. The Company's policy is to encourage active involvement of employees in the management of its facilities and in matters affecting employees' interests. Each facility has a Staff Relations Group ('SRG'). The elected chairperson of the SRG attends the thrice yearly Board meetings at their facility and serves as a conduit for interaction between the Board and employees. The SRG also takes an active role in quality assurance and the accreditation process which all the Company's facilities embrace. In addition, the Company encourages personal career development for all employees through providing access to training and promotional opportunities.

In June 2009, the Company launched a new Inland Revenue approved Share Incentive Plan ("SIP") under which Group employees are able to buy shares in the Company out of pre-tax income. The new scheme represents a renewal of prior schemes in which over 500 employees have become shareholders in the Company. In conjunction with the SIP, the executive directors will undertake to produce and circulate half year reports on the performance of the Company to SIP subscribers. A separate HM Revenue & Customs approved share option scheme has been established for managers.

Further, the Company launched a B Ordinary Share Plan in December 2008 whereby managers were invited to purchase B shares for nominal value. These B shares would realise value above a hurdle level ('the Hurdle'), on a capital winding up or other realisation event ('an Event'). There are two classes of ordinary shares, of which 56.0 million A shares were in issue or under option as at 31<sup>st</sup> October 2010. On an Event the A shareholders will be entitled to proceeds equal to the Hurdle. Thereafter, the A and B shares will share in the proceeds equally as though all shares were of the same class. The Hurdle was set as the value of the Company at which share options were awarded in December 2008, computed as £155,500,000 based on the then current number of A shares in issue and/or under option and equivalent to £2.75 per A share. During the year the Company issued 415,250 B shares to bring the total B shares in issue to 2,062,750.

### Disabled persons

It is Group policy to give fair consideration to the employment needs of disabled people and to comply with current legislation with regard to their employment. Wherever practicable, we continue to employ and promote the careers of existing employees who become disabled and to consider disabled persons for employment, subsequent training, career development and promotion on the basis of their aptitudes and abilities.

**Directors' report (*continued*)**

**Political and charitable contributions**

The Group made no political or charitable contributions during the year (*2009 Nil*)

**Proposed dividend**

The directors do not recommend the payment of a dividend (*2009 Nil*)

**Creditor payment policy**

It is the Group's policy to pay approved liabilities to creditors promptly and within agreed terms

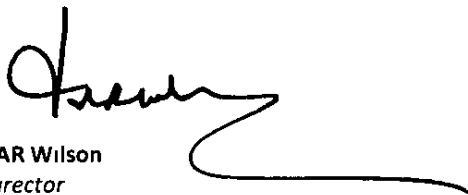
**Disclosure of information to auditors**

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware, and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information

**Auditors**

Pursuant to a shareholder's resolution, the Company is not obliged to reappoint its auditors annually and KPMG LLP will until further notice continue in office

By order of the Board



KAR Wilson  
Director  
179 Kings Road  
Kingston Upon Thames  
KT2 5JH

9 February 2011

## **Statement of directors' responsibilities in respect of the Directors' Report and the financial statements**

The directors are responsible for preparing the Directors' Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable law.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgments and estimates that are reasonable and prudent,
- state whether they have been prepared in accordance with IFRSs as adopted by the EU, and
- 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 adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. 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**

Plym House  
3 Longbridge Road  
Plymouth  
PL6 8LT  
United Kingdom

**Independent auditors' report to the members of Cygnet Health Care Limited**

We have audited the financial statements of Cygnet Health Care Limited for the year ended 31 October 2010 set out on pages 12 to 38. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by EU.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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 auditors' 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**

As explained more fully in the Directors' Responsibilities Statement set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

**Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the APB's web-site at [www.frc.org.uk/apb/scope/UKNP](http://www.frc.org.uk/apb/scope/UKNP).

**Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 October 2010 and of its profit for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the EU, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

**Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

**Independent auditors' report to the members of Cygnet Health Care Limited**  
*(continued)*

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit



**I J Brokenshire (Senior Statutory Auditor)**  
**for and on behalf of KPMG LLP, Statutory Auditor**  
Chartered Accountants

**17** February 2011

## Income Statement

for year ended 31 October 2010

	Note	2010 £000	2009 £000
Revenue	1	78,829	80,239
Operating expenses		(77,039)	(77,245)
<b>Operating profit before net financing costs</b>		<b>1,790</b>	<b>2,994</b>
Impairment of leasehold land and buildings	8	(992)	(2,788)
		<b>798</b>	<b>206</b>
Financial income	5	9	4
Financial expenses	5	(131)	(108)
<b>Net financing expense</b>		<b>(122)</b>	<b>(104)</b>
Impairment of leasehold land and buildings	8	(992)	(2,788)
All other net income and expenditure		1,668	2,890
<b>Profit before tax</b>	2	<b>676</b>	<b>102</b>
Taxation	6	1,247	(1,300)
<b>Profit/(loss) for the financial year</b>		<b>1,923</b>	<b>(1,198)</b>
<b>Attributable to equity holders</b>		<b>1,923</b>	<b>(1,198)</b>

There were no acquisitions or discontinued activities, in the current or prior year

## Statement of Comprehensive Income

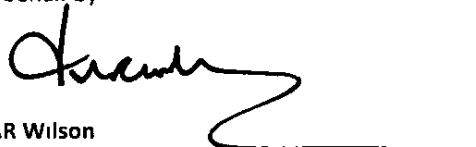
for year ended 31 October 2010

	2010 £000	2009 £000
<b>Profit/(loss) for the year</b>	<b>1,923</b>	<b>(1,198)</b>
Revaluation of property	(10,150)	21,205
Deferred tax recognised on revaluation recognised directly in equity	2,659	(7,118)
<b>Net income recognised directly in equity</b>	<b>(7,491)</b>	<b>14,087</b>
<b>Total recognised income and expense attributable to equity holders of the Company</b>	<b>(5,568)</b>	<b>12,889</b>

**Statement of Financial Position**  
**at 31 October 2010**

	Note	2010 £000	2009 £000
<b>Non-current assets</b>			
Property, plant and equipment	8	24,817	34,872
Intangible assets	9	5,123	5,206
		<u>29,940</u>	<u>40,078</u>
<b>Current assets</b>			
Amounts owed by group undertakings		142,359	141,284
Trade and other receivables	11	9,802	10,103
Cash and cash equivalents	12	4,750	3,485
Tax receivable		2,148	-
		<u>159,059</u>	<u>154,872</u>
<b>Total assets</b>		<u>188,999</u>	<u>194,950</u>
<b>Current liabilities</b>			
Trade and other payables	13	18,990	14,441
Tax payable		-	1,020
		<u>18,990</u>	<u>15,461</u>
<b>Non-current liabilities</b>			
Deferred tax liabilities	10	3,545	7,132
<b>Total liabilities</b>		<u>22,535</u>	<u>22,593</u>
<b>Equity attributable to equity holders of the parent</b>			
Share capital	14	715	715
Share premium	14	178	178
Revaluation reserve	14	7,242	16,941
Other reserve	14	4,839	4,839
Retained earnings	14	153,490	149,684
<b>Total equity</b>		<u>166,464</u>	<u>172,357</u>
<b>Total equity and liabilities</b>		<u>188,999</u>	<u>194,950</u>

These financial statements were approved by the Board of directors on 9 February 2011 and were signed on its behalf by

  
KAR Wilson  
Director

Registered number. 02141256

**Statement of Cash Flows**  
*for year ended 31 October 2010*

	Note	2010 £000	2009 £000
<b>Cash flows from operating activities</b>			
Profit/(loss) for the year		1,923	(1,198)
Adjustments for			
Depreciation, amortisation and impairment	8,9	3,404	3,763
Financial income	5	(9)	(4)
Financial expense	5	131	108
Gain on sale of property, plant and equipment		(1)	(2)
Share based payment expense	15	146	270
Taxation	6	(1,247)	1,300
		<hr/> 4,347	<hr/> 4,237
 Increase in trade and other receivables		 (771)	 (5,140)
Increase in trade and other payables		4,078	3,121
		<hr/> 7,654	<hr/> 2,218
 Interest paid		 (131)	 (108)
Tax paid		(2,850)	-
		<hr/> 4,673	<hr/> 2,110
<b>Net cash from operating activities</b>		<hr/> 4,673	<hr/> 2,110
 <b>Cash flows from investing activities</b>			
Interest received		9	4
Acquisition of property, plant and equipment	8	(3,417)	(750)
		<hr/> (3,408)	<hr/> (746)
<b>Net cash from investing activities</b>		<hr/> (3,408)	<hr/> (746)
 Net increase in cash and cash equivalents		 1,265	 1,364
Cash and cash equivalents at 31 October 2009		3,485	2,121
		<hr/> 4,750	<hr/> 3,485
<b>Cash and cash equivalents at 31 October 2010</b>	12	<hr/> 4,750	<hr/> 3,485



## Notes

*(forming part of the financial statements)*

### 1 Accounting policies

Cygnnet Health Care Limited is a company incorporated in the UK

The address of the Company's registered office is,

Godden Green Clinic  
Godden Green  
Sevenoaks  
Kent  
TN15 0JR

#### **Statement of compliance**

The financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs")

#### **Basis of preparation**

##### **Going Concern**

These financial statements have been prepared on the going concern basis. The Group is profitable, notwithstanding the movements on the swap accrual, and generates positive cashflows. The Group does have term borrowings which have financial covenants attached. However, management perform detailed forecasting for the next twelve months and the foreseeable future, which includes covenant compliance forecasting. The renewal dates of the term borrowings do not fall within the next twelve months. Therefore there is no reason to suppose that the Group will not continue to be a going concern for the foreseeable future.

##### **Basis of measurement**

The financial statements are presented in sterling, rounded to the nearest thousand. They are prepared on the historical cost basis. Land and buildings are revalued to fair value.

##### **Significant accounting policies**

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, and have been applied consistently by the Company.

The preparation of financial statements in conformity with Adopted IFRS 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 revision and future periods if the revision affects both current and future periods.

Judgements and estimates made by management in the application of Adopted IFRS that have significant effect on the financial statements are discussed in note 20.

The following are financial reporting standards applicable to the Company for future financial periods and have not been applied in preparing these financial statements:

- IAS 24 Related Party Disclosures is effective from 1 January 2011 and amends the definition of a related party. The main amendments to the standard results in entities that are influenced by associates and close family members of controlling shareholders being defined as related parties for the entity. This is not expected to have an impact currently for the Group.

## Notes (continued)

### 1 Accounting policies (continued)

- IAS 17 Leases is an ongoing project by the IASB to reconsider the accounting treatment for leasing arrangements. The project is being conducted jointly by the FASB. The discussion paper that has been issued proposes for lessees, to eliminate the requirement to classify a lease contract as an operating or finance lease, and to require a single accounting model to be applied to all leases. The paper proposes that a lessee recognize in its financial statements a "right of use" asset representing its right to use the leased asset, and a liability representing its obligation to pay lease rentals. The proposals for lessor accounting are still being discussed. The IASB have proposed an exemption from these requirements for lessors of investment property measured at fair value. This will result in Cygnnet Health Care Limited having to recognise in their statement of financial position the lease arrangements with Cygnnet Propco Limited and Stac Health Care Limited if this standard comes into force.

#### Revenue

Revenue relates to income received from operating psychiatric facilities and residents of the Group's nursing homes and arises entirely in the United Kingdom. Revenue from operating psychiatric facilities and residents of the Group's nursing homes is recognised, as earned, through the provision of contracted services.

Revenue is recognised in the accounting period in which the Company provides the service.

#### Segmental reporting

Cygnnet internal organisational and management structure and its system of internal financial reporting to the Board of directors is not based on geography. It reports between psychiatric facilities as one segment and nursing homes as another segment, however the size of the nursing home business is such that it has been deemed there is only one business segment and one geographical segment.

#### Expenses

##### Operating lease payments

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

##### Finance lease payments

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

##### Net financing costs

Net financing costs comprise interest payable, finance charges on shares classified as liabilities and finance leases, interest receivable on funds invested and dividend income (see derivative financial instruments and hedging accounting policy).

Interest income and interest payable is recognised in the income statement as it accrues, using the effective interest method. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established.

#### Employee benefits

##### Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

##### Share-based payment transactions

## Notes (continued)

### 1 Accounting policies (continued)

The fair value of the amount payable to employees in respect of share options, which are equity settled, are recognised as an expense with a corresponding increase in equity. The fair value of options is measured at grant date.

The Company took advantage of the option available in IFRS 1 to apply IFRS 2 only to equity instruments that were granted after 7 November 2002 and that had not vested by 1 November 2007.

#### Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement 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 substantively enacted at the statement of financial position date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination, and differences relating to investments in subsidiaries and associates 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 statement of financial position 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.

#### Property, plant and equipment

Properties are initially recorded at cost and are subsequently revalued at their fair value less accumulated depreciation and impairment losses.

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

Leases in which the Company assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Where land and buildings are held under leases, the accounting treatment of the land is considered separately from that of the buildings. Leased assets acquired by way of finance lease are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses. Lease payments are accounted for as described below.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of the property, plant and equipment and are recognised net within 'other operating income' in the income statement.

Depreciation is charged to the income statement to write off the cost less the estimated residual value on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Freehold land is not depreciated. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. The estimated useful lives are as follows:

- |  |                            |
|--|----------------------------|
| • Short leasehold buildings            | over the life of the lease |
| • Long leasehold buildings             | 40 years                   |
| • Fixtures, fittings and equipment     | 4 to 10 years              |
| • Motor vehicles                       | 5 years                    |
| • Assets in the course of construction | not depreciated            |

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

## Notes (continued)

### 1 Accounting policies (continued)

#### **Policy for interest and capitalisation**

The cost of land and buildings includes interest on the capital employed in hospital developments, nursing home developments and development costs associated with initiating and monitoring the construction of hospital developments or nursing homes. Such interest is capitalised only until the date of completion of the relevant hospital or home. The rate of interest used is the applicable cost of funds during the period.

#### **Intangible assets and goodwill**

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of trade and assets. In respect of business combinations that have occurred since 1 November 2007, goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired. Identifiable intangibles are those which can be sold separately or which arise from legal rights regardless of whether those rights are separable.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment.

In respect of acquisitions prior to 1 November 2007, goodwill is included on the basis of its deemed cost, which represents the amount recorded under UK GAAP which was broadly comparable save that only separable intangibles were recognised and goodwill was amortised.

Negative goodwill arising on an acquisition is recognised in the income statement immediately.

#### **Other intangibles**

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

Other intangible assets that are acquired by the Company are stated at cost less accumulated amortisation and impairment losses.

#### **Amortisation of intangibles**

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Other intangible assets are amortised from the date they are available for use over their estimated useful lives. The estimated useful lives are as follows:

- Goodwill Indefinite life
- Patents and trademarks 10 years
- Customer contracts 15 years

The valuation of patents and trademarks is based on a fully-loaded royalty relief method. The valuation of customer contracts is based on an income approach method.

## Notes (continued)

### 1 Accounting policies (continued)

#### *Impairment*

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

For goodwill, the recoverable amount is reviewed at each statement of financial position date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit on a pro rata basis. A cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

Goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use were tested for impairment as at 1 November 2007, the date of transition to Adopted IFRSs, even though no indication of impairment existed.

#### *Reversals of impairment*

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed when there is an indication that the impairment loss may no longer exist or there has been a change in the estimates used to determine the recoverable amount.

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

#### *Trade and other receivables*

Trade and other receivables are stated at amortised cost.

#### *Cash and cash equivalents*

Cash and cash equivalents comprise cash balances and call deposits.

## Notes (continued)

### 1 Accounting policies (continued)

#### *Classification of financial instruments issued by the Company*

##### *Objectives and policies*

Following the adoption of IAS 32, financial instruments issued by the Company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions

- (a) they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Company, and
- (b) where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company's exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the Company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of finance expenses. Finance payments associated with financial instruments that are classified in equity are dividends and are recorded directly in equity.

##### *Interest-bearing borrowings*

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

##### *Provisions*

A provision is recognised in the statement of financial position when the Company has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. 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, where appropriate, the risks specific to the liability.

### 2 Expenses and auditors' remuneration

*Included in profit are the following*

	2010 £000	2009 £000
Amortisation of intangibles	83	83
Loss on sale of plant, property and equipment	1	2
Depreciation of plant, property and equipment	2,329	892
Operating lease payments	19,110	19,019
Impairment of property, plant and equipment	992	2,788
	<u>          </u>	<u>          </u>

##### *Auditors' remuneration*

	2010 £000	2009 £000
Audit of these financial statements	64	59
Other services relating to taxation	35	31
	<u>          </u>	<u>          </u>

## Notes (continued)

### 3 Staff numbers and costs

The average number of persons employed by the Company (including directors) during the year on a full time equivalent basis, analysed by category, was as follows

	2010 No	2009 No
Nursing care staff	884	833
Support staff	203	207
Admin staff	184	177
	<u>1,271</u>	<u>1,217</u>

The aggregate payroll costs of these persons were as follows

	2010 £000	2009 £000
Wages and salaries	37,379	37,204
IFRS 2 Share based payments (see note 15)	146	270
Social security costs	3,523	3,679
Other pension costs	419	437
	<u>41,467</u>	<u>41,590</u>

### 4 Directors' remuneration

	2010 £000	2009 £000
Directors' emoluments	463	948
Company contributions to money purchase pension plans	23	15
	<u>486</u>	<u>963</u>

The aggregate of emoluments and amounts receivable under long term incentive schemes of the highest paid director was £188,000 (2009 £291,000), and company pension contributions of £7,000 (2009 £7,000) were made to a money purchase scheme on their behalf. No share options were exercised (2009 nil)

### 5 Financing income and expense

	2010 £000	2009 £000
Interest income	9	4
<i>Finance income</i>	<u>9</u>	<u>4</u>
<i>Interest expense</i>		
On bank loans and overdrafts	(131)	(108)
<i>Financial expenses</i>	<u>(131)</u>	<u>(108)</u>
<i>Net financial expense</i>	<u>(122)</u>	<u>(104)</u>

## Notes (continued)

### 6 Taxation

#### Recognised in the income statement

	2010 £000	2009 £000
Current tax expense		
Current year	1,475	1,126
Adjustments for prior years	(1,794)	-
	<u>(319)</u>	<u>1,126</u>
Deferred tax expense		
Origination and reversal of temporary differences	(806)	174
Current year adjustment for prior years	(122)	-
	<u>(928)</u>	<u>174</u>
Total tax in income statement	<u>(1,247)</u>	<u>1,300</u>

#### Reconciliation of effective tax rate

	2010 £000	2009 £000
Profit/(loss) for the period	1,923	(1,198)
Total tax (credit)/expense	(1,247)	1,300
Profit excluding taxation	<u>676</u>	<u>102</u>
Tax using the UK corporation tax rate of 28% (2009 28%)	189	29
Depreciation of assets not eligible for capital allowances	66	-
Impairment	278	781
Transfer pricing	1,884	876
Group relief	(1,314)	(576)
Other adjustments	(434)	190
Adjustment in relation to tax charge in prior years	(1,916)	-
Total tax (credit)/expense	<u>(1,247)</u>	<u>1,300</u>

### 7 Dividend

	2010 £000	2009 £000
Dividend paid	<u>-</u>	<u>-</u>



## Notes (continued)

### 8 Property, plant and equipment

	<i>Leasehold land and buildings £000</i>	<i>Fixtures, fittings and equipment £000</i>	<i>Motor vehicles £000</i>	<i>Total £000</i>
<b>Cost or valuation</b>				
Balance at 1 November 2008	16,143	1,765	417	18,325
Additions	582	253	41	876
Transfers	82	(82)	-	-
Revaluation	19,995	-	-	19,995
Disposals	-	-	(11)	(11)
<b>Balance at 31 October 2009</b>	<b>36,802</b>	<b>1,936</b>	<b>447</b>	<b>39,185</b>
Balance at 1 November 2009	36,802	1,936	447	39,185
Additions	2,680	672	65	3,417
Disposals	-	(2)	(4)	(6)
<b>Balance at 31 October 2010</b>	<b>39,482</b>	<b>2,606</b>	<b>508</b>	<b>42,596</b>
<b>Depreciation and impairment</b>				
Balance at 1 November 2008	749	839	264	1,852
Depreciation charge for the year	663	165	64	892
Revaluation	(1,210)	-	-	(1,210)
Impairment	2,788	-	-	2,788
Disposals	-	-	(9)	(9)
<b>Balance at 31 October 2009</b>	<b>2,990</b>	<b>1,004</b>	<b>319</b>	<b>4,313</b>
Balance at 1 November 2009	2,990	1,004	319	4,313
Depreciation charge for the year	2,042	220	67	2,329
Impairment	11,142	-	-	11,142
Disposals	-	(2)	(3)	(5)
<b>Balance at 31 October 2010</b>	<b>16,174</b>	<b>1,222</b>	<b>383</b>	<b>17,779</b>
<b>Net book value</b>				
At 1 November 2008	15,394	926	153	16,473
At 31 October 2009	33,812	932	128	34,872
<b>At 31 October 2010</b>	<b>23,308</b>	<b>1,384</b>	<b>125</b>	<b>24,817</b>

## Notes (continued)

### 8 Property, plant & equipment (continued)

#### Revaluation

Freehold land and buildings and leasehold land and buildings are measured using the revaluation model

The fair value of the Company's freehold land and buildings has been determined at year end using values consistent with the formal valuation conducted by Grimleys GVA in October 2010

The GVA review was conducted in accordance with the practice statements in the valuation standards (The Red Book) published by the Royal Institution of Chartered Surveyors. Grimleys GVA are members of the Royal Institution of Chartered Surveyors and have appropriate qualification and recent experience in the valuation of properties in the relevant locations

The properties consist entirely of independent private hospital and nursing care home facilities which, having due regard to the Red Book, are to be treated as i) Land and buildings fully equipped as an operational entity and valued having regard to trading potential and, ii) Land and buildings owner-occupied for the purposes of the undertaking

#### Leased land and buildings

At 31 October 2010, had the leasehold land and building been measured using the cost model (historical cost less accumulated depreciation and impairment losses) their carrying value would be £3,380,000 (2009 £3,357,000)

The net book value of leasehold land and buildings comprises long leasehold of £6,300,000 (2009 £7,238,000) and short leasehold of £14,227,000 (2009 £25,692,000)

### 9 Intangible assets

	<i>Goodwill</i> £000	<i>Customer contracts and trademarks</i> £000	<i>Total</i> £000
<b>Cost</b>			
Balance at 1 November 2008 and 31 October 2009	4,466	1,030	5,496
Balance at 1 November 2009 and 31 October 2010	4,466	1,030	5,496
<b>Amortisation and impairment</b>			
Balance at 1 November 2008	-	207	207
Amortisation for the year	-	83	83
Balance at 31 October 2009	-	290	290
Balance at 1 November 2009	-	290	290
Amortisation for the year	-	83	83
Balance at 31 October 2010	-	373	373
<b>Net book value</b>			
At 1 November 2008	4,466	823	5,289
At 31 October 2009	4,466	740	5,206
At 31 October 2010	4,466	657	5,123

## Notes (continued)

### 9 Intangible assets – Group (continued)

#### *Amortisation and impairment charge*

The amortisation charge is recognised in the following line items in the income statement

	2010 £000	2009 £000
Operating costs	83	83

Patents and trademarks are amortised over their useful economic life of 10 years. As at 31 October 2010 the remaining amortisation period for patents and trademarks is 5 year 6 months.

Customer contracts are amortised over their useful life of 15 years. As at 31 October 2010 the remaining amortisation period for customer contracts is 10 years and 6 months.

Goodwill is considered to have an indefinite useful life. It is tested at least annually for impairment in accordance with IAS 36 'Impairment of assets' and IAS 38 'Intangible assets'.

#### *Impairment*

The directors have reviewed the portfolio for impairment and consider no impairment has arisen.

The recoverability of goodwill and trademarks, patents and customer contracts is assessed in comparison to the cash generating units to which it is associated.

The impairment tests at 31 October 2010 using value in use resulted in no charge to goodwill impairment expense within the income statement. In determining whether a goodwill impairment charge is required, the carrying value of goodwill is compared to the recoverable amount of cash generating units (CGUs), which is determined based on value in use calculations. These calculations use earnings before interest, tax, depreciation and amortisation (EBITDA) analysis based on financial budgets approved by management. In all cases, the growth rate is a conservative estimate which does not exceed the long-term average growth rate of the industry in which the CGUs operate. Any reasonable possible change in the key assumptions on which recoverable amounts are based would not cause the carrying amount of CGUs to exceed its recoverable amount.

Goodwill of £3,529,000 and intangible assets of £1,030,000 have been allocated against the cash generating unit of The Springs Community a residential care facility.

The basis on which the intangibles and goodwill has been determined is on a cost basis (fair value at the date of the acquisition).

The Company instructed an independent third party, Globalview Advisors, to value the intangibles that the Group had acquired, at the date of acquisition.

The assumption that the third party had made in valuing the intangible assets are as follows:

#### *For customer contracts*

The income approach method has been used which firstly projects the total cash flow expected to accrue. The second step involves discounting these cash flows to present value at a discount rate that considers the degree of risk (or uncertainty) associated with the realisations of the projected monetary benefit. The discount rate used is commensurate with the risk of investment, which is 8% for the Springs Community.

#### *Trade names*

For trade names, the intangible was valued by means of royalty savings (relief-from-royalty) method of income approach. Under this approach, it is assumed that a company, without a similar trade name, would licence the right to use the Springs Community trade name and pay a royalty related to turnover achieved in this industry.

## Notes (continued)

### 9 Intangible assets (continued)

In order to determine an appropriate royalty rate a review of actual royalty rates have been taken into account as follows

- Royalties paid by companies in similar industries such as Comfort Keepers Home, Instead Senior Care, Karen Bass, and Senior Adult Recreation and Health Adult Day Services Inc

The above had rates in the region of 5% to 7% The Springs Community is able to charge a premium price compared to its competitors and hence a discount rate of 9%, equal to the Company's return on equity has been used in its calculation

In developing the discount rates, the following factors were considered

- Valuation of business acquired, using management's projections over 13 years Considering the arms-length nature of the transactions, they computed the implied IRR
- Considered the risk and required return characteristics for various asset categories
- In the weighted average return on assets analysis, the overall required return was computed, using the appropriate discount rate for each asset

Goodwill of £937,000 has been allocated against the cash generating unit of Westlands Lodge, Kenton Road

The basis on which goodwill was determined was on a cost basis (fair value at date of acquisition)

There were no customer contracts or trade names acquired Management and workforce skill were acquired, which are considered goodwill under IFRS 38

### 10 Deferred tax assets and liabilities

#### Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following

	Assets		Liabilities	
	2010 £000	2009 £000	2010 £000	2009 £000
Property, plant and equipment	-	-	3,485	6,925
Intangible assets	-	-	177	207
Other	(117)	-	-	-
	<hr/>	<hr/>	<hr/>	<hr/>
Tax (assets) / liabilities	(117)	-	3,662	7,132
Net off tax liabilities/(assets)	117	-	(117)	-
	<hr/>	<hr/>	<hr/>	<hr/>
Net tax (assets) / liabilities	-	-	3,545	7,132
	<hr/>	<hr/>	<hr/>	<hr/>

#### Movement in deferred tax during the year

	1 November 2009 £000	Recognised in income £000	Recognised in equity £000	31 October 2010 £000
Property, plant and equipment	6,925	(781)	(2,659)	3,485
Intangible assets	207	(30)	-	177
Other	-	(117)	-	(117)
	<hr/>	<hr/>	<hr/>	<hr/>
	7,132	(928)	(2,659)	3,545
	<hr/>	<hr/>	<hr/>	<hr/>

## Notes (continued)

### 10 Deferred tax assets and liabilities (continued)

#### Movement in deferred tax during the prior year

	1 November 2008 £000	Recognised in income £000	Recognised in equity £000	31 October 2009 £000
Property, plant and equipment	(450)	257	7,118	6,925
Intangible assets	230	(23)	-	207
Other	60	(60)	-	-
	<u>(160)</u>	<u>174</u>	<u>7,118</u>	<u>7,132</u>

The Emergency Budget on 22 June 2010 announced that the UK corporation tax rate will reduce from 28% to 24% over a period of 4 years from 2011. The first reduction in the UK corporation tax rate from 28% to 27% was substantively enacted on 20 July 2010 and will be effective from 1 April 2011. This will reduce the Company's future current tax charge accordingly. It has not yet been possible to quantify the full anticipated effect of the announced further 3% rate reduction, although this will further reduce the Company's future current tax charge and reduce the Company's deferred tax liabilities/assets accordingly.

### 11 Trade and other receivables

	2010 £000	2009 £000
Trade receivables	7,210	8,879
Other receivables and prepayments	2,592	1,224
	<u>9,802</u>	<u>10,103</u>

The Group regularly reviews the ageing profile of the trade receivables and actively seeks to collect any amounts that have fallen outside the defined credit terms.

The ageing of trade receivables that have not been provided for are

	2010 £000	2009 £000
Not yet due		
0-29 days	5,098	6,169
Overdue		
30-59 days	1,212	1,311
60+ days	900	1,399
	<u>7,210</u>	<u>8,879</u>

The Company's exposure to credit risks related to trade and other receivables are disclosed in note 16.

### 12 Cash and cash equivalents

	2010 £000	2009 £000
Cash and cash equivalents per statement of financial position	4,750	3,485
Cash and cash equivalents per statement of cash flows	<u>4,750</u>	<u>3,485</u>

The Company's exposure to interest rate risk is disclosed in note 16.

## Notes (continued)

### 13 Trade and other payables

	2010 £000	2009 £000
Trade payables	1,451	1,389
Non-trade payables and accrued expenses	17,539	13,052
	<u>18,990</u>	<u>14,441</u>

The Company's exposure to liquidity risks related to trade and other payables is disclosed in note 16

### 14 Capital and reserves

#### Reconciliation of movement in capital and reserves

	Share capital £000	Share premium £000	Revaluation reserve £000	Capital redemption reserve £000	Retained earnings £000	Total equity £000
Balance at 1 November 2008	715	178	2,854	4,839	150,612	159,198
Total recognised income and expense	-	-	-	-	(1,198)	(1,198)
Revaluation	-	-	14,087	-	-	14,087
IFRS 2 adjustment	-	-	-	-	270	270
Balance at 31 October 2009	<u>715</u>	<u>178</u>	<u>16,941</u>	<u>4,839</u>	<u>149,684</u>	<u>172,357</u>
Balance at 1 November 2009	715	178	16,941	4,839	149,684	172,357
Total recognised income and expense	-	-	-	-	1,923	1,923
Transfer from revaluation reserve	-	-	(2,208)	-	2,208	-
Revaluation	-	-	(7,491)	-	-	(7,491)
IFRS 2 adjustment	-	-	-	-	(325)	(325)
Balance at 31 October 2010	<u>715</u>	<u>178</u>	<u>7,242</u>	<u>4,839</u>	<u>153,490</u>	<u>166,464</u>

#### Revaluation reserve

Where property, plant and equipment is revalued, the cumulative increase in the fair value of the property at the date of reclassification in excess of any previous impairment losses is included in the revaluation reserve

## Notes (continued)

### 14 Capital and reserves (continued)

Share capital	2010 £	2009 £
<b>Authorised</b>		
2,787,125,000 Ordinary shares of 1p each	278,712	278,712
800,000 redeemable preference shares of £1 each	800,000	800,000
	<hr/>	<hr/>
	1,078,712	1,078,712
	<hr/>	<hr/>
<b>Allotted and fully paid and called up</b>		
11,499,300 Ordinary shares of 1p each	114,993	114,993
600,000 redeemable preference shares of £1 each	600,000	600,000
	<hr/>	<hr/>
	714,993	714,993
	<hr/>	<hr/>

The Company is a wholly owned subsidiary of Cygnet 2002 Limited and the redemption of the preference shares and the entitlement to dividends has been waived

### 15 Employee benefits

#### Share-based payments

The Cygnet Group operates three share schemes, Company Share Option Plan ("CSOP"), the Share Incentive Plan ("SIP") and the B share scheme. These allow employees to acquire shares in the ultimate parent company.

All employees are employed by Cygnet Health Care Limited, and so the charge is borne by Cygnet Health Care Limited.

#### CSOP scheme

The CSOP scheme awards options over ordinary A shares in the Company to employees. During the year there were no shares awarded.

#### SIP scheme

A new SIP scheme was launched in June 2009 in Cygnet 2008 Limited. The SIP is a standard HMRC approved plan which allows eligible employees to purchase shares in the Company.

#### B share scheme

During the previous year a B share scheme was launched which invited employees to purchase "growth shares" – B ordinary shares with a nominal value of 0.01p (over £2.75) and thereby a share in the return in growth of the business over a certain preset value. The Company issued a further 412,250 B ordinary shares in October 2010.

## Notes (continued)

### Share-based payments (continued)

The terms and conditions of the option grants are as follows, whereby all options are settled by physical delivery of shares

<i>Grant date / employees entitled</i>	<i>Number of Instruments granted</i>	<i>Vesting conditions</i>	<i>Contractual life of options</i>
<b>Award date</b>			
17 September 2003	447,500	No performance conditions attach	16 September 2013
6 May 2004	25,000	No performance conditions attach	5 May 2014
18 May 2004	15,000	No performance conditions attach	17 May 2014
22 April 2005	244,000	No performance conditions attach	21 April 2015
16 September 2005	10,000	No performance conditions attach	15 September 2015
12 December 2005	60,500	No performance conditions attach	11 December 2015
22 May 2006	221,300	No performance conditions attach	21 May 2016
7 November 2006	20,000	No performance conditions attach	6 November 2016
14 June 2007	241,330	No performance conditions attach	13 June 2017
1 December 2008	278,550	No performance conditions attach	30 November 2018

The number and weighted average exercise prices of share options are as follows

	<i>Weighted average exercise price 2010 £</i>	<i>Number of options 2010</i>	<i>Weighted average exercise price 2009 £</i>	<i>Number of options 2009</i>
Outstanding at the beginning of the year	1 72	881,000	1 25	673,100
Forfeited during the year	1 63	(173,600)	1 65	(23,650)
Granted during the year	-	-	2 75	278,550
Vested during the year	1 46	(6,250)	1 13	(47,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Outstanding at the end of the year	1 70	701,150	1 72	881,000
	<hr/>	<hr/>	<hr/>	<hr/>
Exercisable at the end of the year	1 24	464,600	1 12	402,800
	<hr/>	<hr/>	<hr/>	<hr/>

The options outstanding at the year end have an exercise price in the range of £0.36 to £2.75 and a weighted average contractual life of 6.36 years

The fair value of employee share options is measured using a binomial lattice model. Measurement inputs and assumptions are as follows:

The expected volatility is based on the historic volatility over the three year periods (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.

The share options have been granted under a non-market based performance condition. The expected dividends have been assumed to be zero.



## Notes (continued)

### Share-based payments (continued)

	<b>Exercise price</b>	<b>Market price at grant date</b>	<b>Volatility of share return</b>	<b>Risk free discount rate</b>	<b>Fair value per award</b>
<b>Award date</b>					
19 September 2003	36p	36p	50% pa	4.7% pa	23p
6 May 2004	36p	36p	50% pa	5.0% pa	23p
18 May 2004	36p	36p	50% pa	5.1% pa	23p
22 April 2005	105p	105p	50% pa	4.6% pa	66p
16 September 2005	105p	105p	50% pa	4.2% pa	65p
12 December 2005	115p	115p	50% pa	4.4% pa	71p
22 May 2006	125p	125p	50% pa	5.8% pa	97p
7 November 2006	135p	135p	50% pa	4.9% pa	85p
14 June 2007	150p	150p	50% pa	5.8% pa	97p
1 December 2008	275p	275p	60% pa	4.0% pa	146p

The fair values for the SIP are equal to the share prices at each date of grant

The total expenses recognised for the year and the total liabilities recognised at the end of the year arising from share based payments are as follows

	<b>Expense</b>	
	<b>2010</b>	<b>2009</b>
	<b>£000</b>	<b>£000</b>
<b>Award date</b>		
22 April 2006	-	10
22 May 2007	-	22
7 November 2007	-	3
14 June 2008	12	70
1 December 2008	100	110
	<hr/>	<hr/>
<b>Total CSOP</b>	<b>112</b>	<b>215</b>
<b>SIP (various dates)</b>	<b>34</b>	<b>55</b>
	<hr/>	<hr/>
<b>Total all awards</b>	<b>146</b>	<b>270</b>
	<hr/>	<hr/>
	<b>2010</b>	<b>2009</b>
	<b>£000</b>	<b>£000</b>
<b>Total intrinsic carrying amount of liabilities in respect of vested benefits</b>	<b>702</b>	<b>658</b>
	<hr/>	<hr/>

## Notes (continued)

### 16 Financial instruments

Cygnnet Health Care Limited is the primary operating subsidiary of Cygnnet 2008 Limited. This note sets out the risks faced by the Group since they both directly and indirectly affect Cygnnet Health Care Limited.

The Group has exposure to the following risks from its normal course of the Group's business:

- Credit risk,
- Liquidity risk, and
- Interest rate risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout the Group consolidated financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework.

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

The Board of Directors oversees the adequacy of the risk management framework in relation to the risks faced by the Group.

The Group obtains finance from a mixture of sources including bank loans and capital market issues in sterling at fixed and floating rates of interest. Facilities are monitored against predicted borrowing levels and are increased or cancelled as necessary to ensure that there is sufficient committed headroom to accommodate foreseen operational requirements. Uncommitted bank facilities are maintained and used to provide flexibility and more advantageous terms. The Group's main financial covenants in longer term facilities are in respect of Loan to Value, EBITDA ratio, Group Leverage (Debt to EBITDA), Fixed Charge cover (rent plus interest) and Interest cover.

The Treasury policy is that deposits will only be made, and other financial instruments entered into, with bank counterparties, that have been approved by the Board.

#### *Capital risk management*

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence to sustain future development of the business.

The capital structure of the Company consists of shareholders' equity comprising issued share capital, reserves and retained earnings disclosed in note 14.

The capital structure of the Group is reviewed annually with reference to the costs applicable to each element of capital, future requirements of the Group, flexibility of capital drawdown and availability of further capital should it be required.

The Group has hedged 97% of its term debt borrowings which mitigates the risk of an increase in interest rates but also prevents the Group from benefitting from a reduction in interest rates. The Group's agreed facilities include additional funding capacity which can be drawn down to facilitate Cygnnet's expansion plans.

The lenders of debt have imposed capital requirements over the debt. The Group must report to the bank monthly management accounts and quarterly covenant calculations, to ensure there are no breaches.

## Notes (continued)

### 16 Financial instruments (continued)

#### *Interest rate swap*

The Group has an interest rate swap (held in Cygnnet PropCo Limited and Stac Healthcare Limited)

All swap hedges are remeasured to fair value at the statement of financial position date

#### *Credit risk*

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

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. The demographics of the Group's customer base, including the default risk of the industry and country in which the customers domicile has less of an influence on credit risk. The Group did business with 146 NHS purchasing bodies. Cygnnet maintains an active dialogue with all of its customers in order to meet their needs and reduce individual reliance on them.

Geographically there is no concentration of credit risk. Any potential credit risk arises on UK customers. The trade receivable profile and hence maximum exposure is set out in note 11.

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain predetermined amount. The Group's privately funded customer are required to pay for services in advance unless covered by insurance in which case pre-authorisation is required from the insurer. The NHS purchasing bodies are invoiced monthly in arrears but charges are pre-authorised at the point of admission except for emergencies where these are completed with 48 hours of admission.

At the statement of financial position date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the statement of financial position.

The carrying amount of Cygnnet Health Care Limited financial assets represents the maximum credit exposure.

The exposure to credit risk for trade receivables at the reporting date was in the UK.

#### *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 uses financial instruments, comprising bank overdraft and various items including trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group seeks to manage liquidity risk by ensuring sufficient liquidity is available to meet foreseeable needs and to invest cash assets safely and profitably. Short-term flexibility is achieved by overdraft facilities. The Group maintains the following line of credit:

- Revolving Credit Facility that is unsecured. Interest would be payable at the rate of LIBOR plus 2.25%.

## Notes (continued)

### 16 Financial instruments (continued)

The following tables detail the Company's remaining contractual maturity in respect of income earning financial assets and interest bearing financial liabilities

As at 31 October 2010

	<i>Total</i>	<i>Less than 1 year</i>	<i>1-2 years</i>	<i>2-5 years</i>	<i>5 years+</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Cash and cash equivalent	4,750	4,750	-	-	-
Trade and other payables	(18,990)	(18,990)	-	-	-

As at 31 October 2009

	<i>Total</i>	<i>Less than 1 year</i>	<i>1-2 years</i>	<i>2-5 years</i>	<i>5 years+</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>£000</i>
Cash and cash equivalent	3,485	3,485	-	-	-
Trade and other payables	(14,441)	(14,441)	-	-	-

#### Interest rate risk

Interest rate risk is the risk that the Group will be susceptible to large fluctuations in interest rates and hence the interest payable on its bank debts. As noted above, the Group has fully hedged against this risk.

#### Sensitivity analysis

As noted above, the Group has interest rate swaps in place so they believe they are not sensitive to changes in interest rates.

#### Interest rate profile of financial instruments at the year end

The cash and liquid resources, where interest bearing, attract interest at floating rates based on LIBOR for three months or less. Any variable rate loan liabilities have been hedged to eliminate the interest rate risk.

#### Fair value

The estimated fair value of the Company's financial instruments is set out below.

#### Financial assets

	2010		2009	
	Carrying amount	Fair value	Carrying amount	Fair value
	£000	£000	£000	£000
Trade and other receivables	9,802	9,802	10,103	10,103
Cash at bank	4,750	4,750	3,485	3,485
	<u>14,552</u>	<u>14,552</u>	<u>13,588</u>	<u>13,588</u>

#### Financial liabilities

	2010		2009	
	Carrying amount	Fair value	Carrying amount	Fair value
	£000	£000	£000	£000
Trade and other payables	18,990	18,990	14,441	14,441
	<u>18,990</u>	<u>18,990</u>	<u>14,441</u>	<u>14,441</u>

## Notes (continued)

### 16 Financial instruments (continued)

#### Repricing analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their periods in which they mature or, if earlier, are repriced at the statement of financial position date

Note	2010				2009			
	Less than one year £000	1 to 2 years £000	2 to 5 years £000	5 years and over £000	Total £000	Less than one year £000	1 to 2 years £000	2 to 5 years £000
1	4,750	4,750	-	-	3,485	3,485	-	-
Cash and cash equivalents	4,750	4,750	-	-	3,485	3,485	-	-

### 1. Cash and cash equivalents

Cash assets are secured by a fixed and floating charge over the assets of the Group

## Notes (continued)

### 17 Operating leases

Non-cancellable operating lease rentals are payable as follows

	2010 £000	2009 £000
Less than one year	18,935	18,907
Between one and five years	74,234	75,518
More than five years	401,594	422,522
	<u>494,763</u>	<u>516,947</u>

The Company leases two nursing homes and two hospital units under operating leases. Land and buildings have been considered separately for lease classification.

- Tabley House lease is based on a 125 year lease. The lease is reviewed every 25 years.
- Blackheath lease is a 20 year lease which is reviewed every 3 years and increases with RPI every year.
- The Ealing lease is a 20 year lease which is reviewed every 5 years. Cygnet have the right to cancel this lease, giving nine months notice.
- Harrow is a five year lease.
- The internal lease arrangement between the operating company Cygnet Health Care Limited and Cygnet PropCo Limited, is treated as an operating lease. The lease is a 30 year lease which allows Cygnet Health Care Limited to operate the psychiatric hospital trade from the properties owned by Cygnet PropCo Limited.

During the year £19,110,000 was recognised as an expense in the income statement in respect of operating leases (2009 £19,019,000)

### 18 Capital commitments

The Company had capital contracted commitments of £1,783,000 (2009 *£nil*)

### 19 Related parties

*Identity of related parties with which the Company has transacted*

The ultimate controlling party and parent of the Company is Cygnet 2008 Limited

*Transactions with key management personnel*

The compensation of key management personnel (including the directors) is as follows

	Group 2010 £000	2009 £000
Key management emoluments including social security costs	949	1,398
Company contributions to money purchase pension plans	34	26
	<u>983</u>	<u>1,424</u>

A director, KAR Wilson was paid a commercial rent of £9,600 (2009 £9,600) during the year, for the use of office premises.

## Notes (continued)

### 19 Related parties (continued)

The Company has taken advantage of the exemption contained in IAS 24 and has therefore not disclosed transactions or balances with entities which form part of the Group

The related party transactions stated above were conducted on an arm's length basis

#### *Transactions with companies within the Group but not 100% owned*

During the year the Company provided accounting support services to Oakdale Services Limited, which were conducted on an arms length basis. The value of services provided amounted to £6,470 (2009 £17,098). Oakdale Services Limited is a 67.5% owned subsidiary undertaking of Cygnnet 2002 Limited.

### 20 Accounting estimates and adjustments

Management discussed the development, selection and disclosure of the Company's critical accounting policies and estimates and the application of these policies and estimates.

#### *Key sources of estimation uncertainty*

Note 8 gives detailed analysis about the useful economic lives of depreciable assets. Note 9 gives an analysis about goodwill.

#### *Critical accounting judgements in applying the Company's accounting policies*

Certain critical accounting judgements in applying the Company's accounting policies are described below.

#### *Determining whether a lease is a finance lease or an operating lease*

The internal lease arrangement between the operating company Cygnnet Health Care Limited and Cygnnet PropCo Limited, is treated as an operating lease.

The lease is a 30 year lease which allows the Company to operate the psychiatric hospital trade from the properties owned by Cygnnet PropCo Limited.

If the lease was not deemed to be an operating lease under IAS 17 'leases', and was classified as a finance lease, the investment Properties held by Cygnnet PropCo Limited would not be held on the statement of financial position of Cygnnet PropCo Limited but instead would be held by the Company. This would increase the Property, plant and equipment balance by £199.369 million and would impact the statement of financial position position of the Company.

The internal lease arrangement between the Company and Stac Healthcare Limited is treated as an operating lease.

If the lease was not deemed to be an operating lease under IAS 17 'leases', and was classified as a finance lease, the investment Property held by Stac Healthcare Limited would not be held on the statement of financial position of Stac Healthcare Limited but instead would be held by the Company. This would increase the Property, plant and equipment balance by £2.088 million and would impact the statement of financial position position of the Company.

#### *Intangible Assets 'IAS 38'*

That it is appropriate not to recognise any impairment losses in relation to the intangible fixed assets and tangible fixed assets, except as otherwise stated.

#### *IFRS 2 'Share-based payments'*

The Company believes it is appropriate to account for the share options as equity settled.

#### *The valuation of properties*

In determining the value of the properties, the directors rely on external valuations carried out by professionally qualified valuers in accordance with the appraisal and valuation standards of the Royal Institution of Chartered Surveyors.

## **Notes (continued)**

The properties consist entirely of independent private hospital and nursing care home facilities which, having due regard to the Red Book, are to be treated as i) Land and buildings fully equipped as an operational entity and valued having regard to trading potential and, ii) Land and buildings owner-occupied for the purposes of the undertaking

The Directors do not believe that there has been any impairment in the carrying value of the properties, plant and equipment or intangible fixed assets, except as disclosed in the financial statements

The directors believe it is appropriate to classify the preference shares as debt, as they are redeemable at the option of the holder

### **21 Ultimate parent company**

The Company is a wholly owned subsidiary of Cygnnet 2002 Limited, a company registered in the UK

The Company's ultimate parent undertaking is Cygnnet 2008 Limited a company incorporated and registered in the UK

The results of the Company are consolidated into the Group that is headed by Cygnnet 2008 Limited The consolidated accounts of Cygnnet 2008 Limited are available to the public and may be obtained from

179 Kings Road  
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### **22 Guarantees**

The Company has guaranteed the overdraft of its fellow Group Company - Cygnnet 2002 Limited, the amount outstanding at the year end was £477,011 (2009 £477,011)

Where the Company has entered into financial guarantee contracts to guarantee the indebtedness of another Company within its Group, the Company consider these to be insurance arrangements, and accounts for them as such In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee The Group's policy is to provide financial guarantees only to wholly owned subsidiaries