

Hills Limited
Annual report
for the year ended 30 June 2019

ABN 35 007 573 417

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Hills Limited

Shareholders' letter

For the year ended 30 June 2019 (continued)

Dear Shareholder,

Hills Limited is entering an exciting new period in its long history – one your board and management believe will deliver strong, long-term returns for all shareholders.

Our strategy over the past few years has been to establish Hills as a major player in the health market, providing best-in-class patient care systems, while continuing to enhance our Distribution business. That strategy has now paid off, with Hills Health Solutions the clear market leader in providing nurse call and patient engagement solutions to Australian hospitals.

Unfortunately, our overall profitability has been significantly impacted by the disappointing performance of our Distribution business despite a strong performance from our Hills Connection Solutions business in FY19.

As a result we reported an improved small underlying net profit after tax of \$0.5 million before one-off items, and a statutory loss of \$8.8 million following one-off provisions and costs of \$7.7 million related to the restructure of the Distribution business and a non-cash impairment of \$6.5 million of intangibles and non-current assets following a review of asset carrying values.

While this was a disappointing outcome, we are confident that these one-off impairments and provisions together with the implementation of our Operational and Strategic Reviews will position us to deliver a material increase in profitability in the current year.

Hills FY19 accounts includes a breakdown of our results by operating division which shows the exciting potential of the Health business, having increased EBITDA by 49 percent over prior year.

Operational and Strategic Reviews

Your Board and management commenced an Operational Review of the Distribution business, in January this year with the assistance of external consultants. We continue to implement changes and recommendations which will deliver annualised productivity improvement and operational costs savings of approximately \$3 - 5 million and providing the Distribution business with a clear path to profitability in FY20.

No company can stand still in fast-moving sectors such as healthcare and technology, and in April this year the Board commissioned a major Strategic Review of Hills underlying businesses with the assistance of AquAsia. This process included a review of each businesses performance, growth prospects and an over-arching need to ensure their value is properly reflected in the Hills share price.

While the Strategic Review is ongoing, we have actioned many of the recommendations, including the decision to exit our underperforming Antenna and STEP satellite services businesses and to discontinue our contract to supply satellite dishes to Foxtel following declining orders. These decisions are a reflection of market reality.

We have also received a conditional offer to purchase the assets in our Antenna business that will ensure our iconic Black Arrow range will continue to be manufactured in South Australia.

Hills Health Solutions

Hills success in the nurse call and patient engagement markets – and its potential for growth – is measured by its strong FY19 results, with our systems implemented in more than 40 percent of Australian public hospital beds and more than 20 percent of Australian private hospital beds.

In May, your Company was appointed the sole distributor in Australia of GetWellNetwork's interactive best-in-class patient engagement platform and we have been awarded the contract to install GetWell at the New Calvary Hospital in Adelaide with more than 400 beds. We also released the next generation of its our IP7500 Nurse Call platform during the period and completed its successful installation at the Joan Kirner hospital in Victoria.

Hills Limited

Shareholders' letter

For the year ended 30 June 2019 (continued)

Other key wins during the year included:

- Installation of the first Wi-Fi patient entertainment system at Joan Kirner Hospital in Victoria
- A successful trial of 14 new Wi-Fi sites with eHealth NSW
- Major Nurse Call wins at Hammond Care (aged care, multiple sites); Concord Hospital, Westmead Hospital, Blacktown Hospital, Prince of Wales Private Hospital, Calvary St Francis and Calvary Health Care Kogarah in NSW; Alfred Health, Western Health, Casey Hospital in Victoria; Churches of Christ (multiple sites)
- New patient entertainment contracts covering more than 2000 beds at Balmain, Canterbury, Concord, Royal Prince Alfred and Northern Beaches hospitals in NSW
- The re-signing of patient entertainment contracts with Barwon Health, Western Health and Mildura hospital in Victoria.

Hills Distribution

The decline in profitability in the Distribution business in FY19 was driven primarily by:

- changes to the vendor mix;
- lower than expected performance in the small to medium business sector;
- continued decline of Foxtel revenues; and
- pressure from a deterioration in the AUD/USD exchange rate.

The impact of these factors was partially offset by cost reductions achieved during the year.

Pleasingly, sales across our top five vendors, which together represent more than 50 percent of revenue, grew 8 percent in FY19 and Hills Connection Solutions business (HCS) continued to benefit from the nationwide NBN roll-out. New partnerships with Downer EDI Limited and Lendlease Group for the provision of HCS services will deliver growth in FY20.

Wins and awards during the year included:

- Department of Educations & Sydney Trains - Williams AV
- Rod Laver Arenas - Community Loudspeakers
- Stations PA upgrade for NSW Fire & Rescue – Australian Monitor
- Connect East Tunnel – Genetec & Axis
- Major roadways & tunnel projects – Genetec & Axis
- Law enforcement and correctional facilities wins – Genetec & Axis
- Williams AV International Distributor of the Year
- Genetec Asia Pacific Distributor of the Year
- Ruckus ANZ Distributor of the Year
- Axis Communications Oceania Distributor of the Year

Hills Limited

Shareholders' letter

For the year ended 30 June 2019 (continued)

Outlook

As mentioned at the outset, we are on the cusp of an exciting new period for Hills, with a simplified and focused business structure that will allow us to maximise the value of the Company for shareholders.

Our key strategic focus in FY20 will be to:

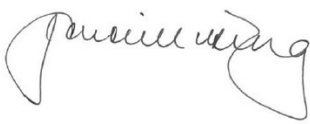
- Continue to grow the Health Solutions business by expanding our range of products and services to hospitals and healthcare facilities such as Aged Care facilities;
- Continue to implement the strategic and operational initiatives to maximise the performance of the Distribution business.

We expect to deliver an improved trading profit in FY20 and to position your Company to resume paying dividends to shareholders, subject to the capital and growth requirements of the business.

Our employees have worked tirelessly to support our customers and vendors as well as executing the Operational Review of the Distribution business and the strategic initiatives under way. We thank them for their ongoing dedication and commitment.

Please join us at the Annual General Meeting, where we will provide you with an update on the Company's first quarter performance.

Yours sincerely



Jennifer Hill-Ling
Chairman



David Lenz
Chief Executive Officer & Managing Director

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

The Directors present their report on the consolidated entity (referred to hereafter as Hills, the Company or the Group) consisting of Hills Limited and the entities it controlled at the end of, or during, the year ended 30 June 2019 (FY19), and the independent auditor's report thereon.

Directors

The following persons were Directors of the Company during the whole of the financial year and up to the date of this report:

Jennifer Helen Hill-Ling
Fiona Rosalyn Vivienne Bennett
Philip Bullock AO
Kenneth James Dwyer
David John Joseph Lenz

Alan Kinkade was appointed a Director on 26 February 2019 and resigned on 19 June 2019.

Principal activities

The principal activities of Hills during the year are outlined within the Review of Operations.

Review of operations

About the Group

The Group operates in Australian and New Zealand and is a value-added distributor of technology products and services in the Security & Surveillance and Audio-Visual markets, and the supplier of Technology solutions in the Health market.

Hills commenced business in Adelaide, South Australia in 1945 and has a long history of developing and innovating products over the years whilst diversifying and divesting as market conditions and customer demands have changed.

Our business activities

The Principal activities of the Group are the valued-added distribution of technology products and services that connect, entertain and secure people's lives into the environments that people need and trust most: their homes, hospitals and healthcare facilities, places of learning, entertainment venues, retail spaces, houses of worship, workplaces and government institutions.

Hills Health Solutions

Hills Health Solutions (HHS) is a market leader and comprises the design, supply and installation of health technology solutions, nurse call and patient entertainment and other related solutions including security, Wi-Fi and telephony, into the health and aged care sectors.

We continue to undertake research and development activities in Australia to enhance and develop our Nurse Call IP ensuring our products remain market leaders.

Hills Distribution

Hills Distribution provides a diverse range of products and solutions to assist our customers support end users with the following needs in the Security, Surveillance and IT market:

- Access control solutions
- Alarms & intruder solutions
- Card access control
- CCTV cameras
- Video management solutions
- Wireless & networking solutions
- Analytics software for facial recognition & people counting solutions
- HillsTrak (asset management)
- Fire detectors and alarms
- Antenna, set top boxes, digital TV systems
- Satellite dishes
- Pre and post installation service

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Review of operations (continued)

In the Audio Visual markets Hills solutions offerings include:

- Unified communication
- Hearing augmentation
- Professional LCD displays
- Projectors
- Australian Monitor – Hills owned and designed product
- Professional Audio solutions for indoor and outdoor applications

Hills Distribution also has strong capability in providing workforce scheduling services for infrastructure projects such as the National Broadband Network (NBN) via the Hills Connection Solutions business.

In August 2019 Hills announced that it would cease manufacturing TV antennas, satellite dishes and associated products by December 2019 following changes in customer sales volumes including lower demand from Foxtel.

Group performance highlights

The Group has announced a statutory net loss after tax of \$8.8 million for the year ended 30 June 2019, compared to the prior year profit of \$0.4 million as summarised in the table below. The statutory result for FY19 was impacted by non-operating expenses of \$14.7 million relating to further restructure activities within the Hills Distribution business. Adjusting for these transactions underlying net profit after tax was \$0.5 million vs the prior year of \$0.1 million.

A\$ million	2019	2018
Sales Revenue	267.4	271.8
Gross Margin (excluding other income)	83.9	86.7
Gross Margin%	31.4%	31.9%
Other Income	0.6	0.9
Operating Expenses (excluding non-operating) ¹	(80.9)	(84.3)
Non-operating expenses	(14.7)	(0.1)
Interest	(3.3)	(3.2)
Tax	5.6	0.3
Net Profit / (Loss) After Tax	(8.8)	0.4
Add non-operating expenses	14.7	0.1
Less non-operating other income	-	(0.4)
Tax effect of non-operating transactions	(5.4)	0.1
Underlying Profit / (Loss) After Tax	0.5	0.1

Hills Health Solutions business continues to deliver strong growth in revenue and profitability whilst Hills Distribution business continued to experience challenges including changes in vendor portfolios and the negative impact on margins resulting from changes to the AUD/USD exchange rate during FY19.

¹ Non-operating expenses detail is provided in note 1(b) of the Consolidated Financial Statements

Hills Limited

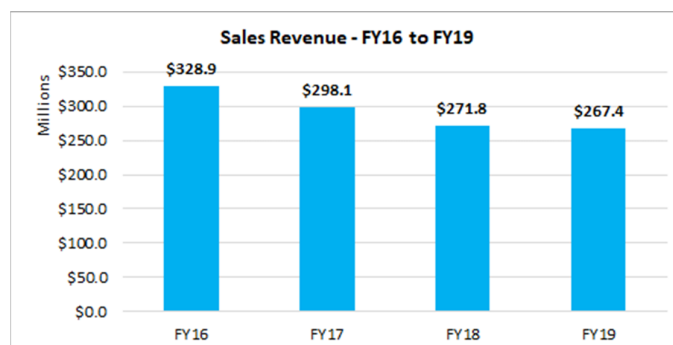
Directors' report

For the year ended 30 June 2019 (continued)

Review of operations (continued)

Revenue

Sales revenue was down by \$4.4 million, or 1.6%, from \$271.8 million to \$267.4 million following changes to the vendor portfolio, lower Foxtel revenue and lower sales in the small to medium business (SMB) sector of our Distribution business which were offset in part by improved revenue for the Hills Health Solution business which recorded revenue of \$38.1 million, up from \$30.9 million in the prior year.

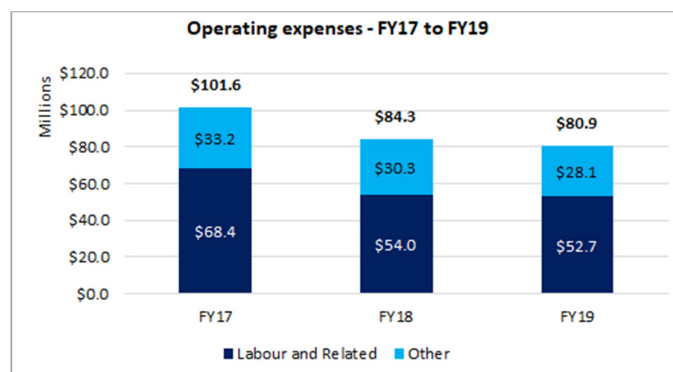


Net Profit

The FY19 net loss of \$8.8 million was impacted by \$14.7 million (before tax) of non-operating expenses.

Gross margin was 31.4% for FY19, down from 31.9% in FY18 and reflecting the impact of changes in the AUD/USD exchange rates during the year and our ability to pass on the cost increases as we looked to hold market share. On 1 July 2019 we increased prices and will look to do so again should the declining exchange rate trend continue.

Operating expenses (excluding non-operating) declined during the year to \$80.9 million down \$3.4 million or 4.0% from \$84.3 million with reductions achieved across all major expense areas and continuing the trend seen since FY15.



Labour and related costs reduced by \$1.3 million, or 2.4% as we continue to streamline our operations and mitigate revenue and margin risks.

Other expenses were lower by a further \$2.2 million, or 7% in FY19 as we continued to drive reductions across most expense lines as the Group continues to make efforts to reduce costs.

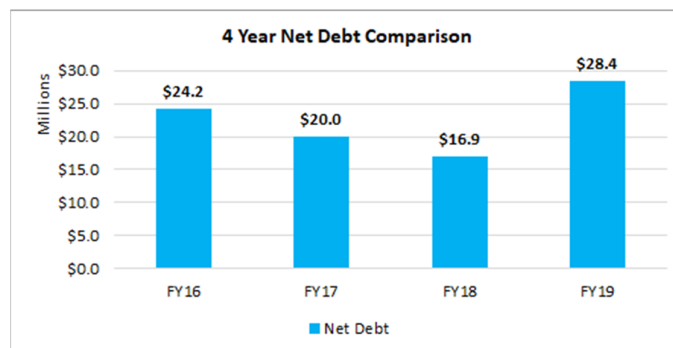
Interest expenses were up 3.2% on the prior year.

A tax benefit of \$5.6 million was booked in FY19 primarily from deferred tax benefits from the FY19 non-operating expenses. The Group retains significant unrecognised tax losses which remain available to reduce tax expenses for future periods as the Group's profitability continues to improve subject to meeting the requirements of the 'continuity of ownership' and 'same or similar business tests'.

Review of operations (continued)

Financial Position

Net debt at June 2019 was \$28.4 million, up from \$16.9 million as outlined in the chart below.



Net debt levels of the Group were impacted by the working capital needs of the business as well as additional debt to fund equipment installations at hospitals for the Health Solutions business with \$1.4 million of new debt taken out during the year.

Operating cashflow in FY19 was an outflow of \$4.0 million vs an inflow of \$12.0 million in FY18 with revenue down by \$4.4 million and lower trade and other payable balances by \$7.0 million being the primary drivers of the outflow in FY19.

Inventory levels decreased by \$2.4 million during the year to \$41.6 million which includes the impact of the additional inventory provision of \$3.8 million.

Subsequent events

There were no events subsequent to balance date that would have a material effect on the Group's financial statements at 30 June 2019.

Dividends

Year ended 30 June 2019	No dividends were paid during the year and no final dividend has been declared.
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Year ended 30 June 2018	No dividends were paid during the year and no final dividend was declared.
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For more information regarding dividends please refer to note 16 of the financial statements.

Significant changes in the state of affairs

Significant changes in the state of affairs of Hills during the financial year are set out in the Review of Operations section of the Directors' report.

FY20 Outlook

Our key strategic focus in FY20 will be to:

- Continue to grow the Health Solutions business by expanding our range of products and services to hospitals and healthcare facilities such as Aged Care facilities;
- Continue to implement the strategic and operational initiatives to maximise the performance of the Distribution business.

We expect to deliver an improved trading profit in FY20 and to position your Company to resume paying dividends to shareholders, subject to the capital and growth requirements of the business.

As with any technology distribution business, Hills is exposed to the risk of potential loss of vendors, customers or employees; slippages associated with contracts; supply issues; general economic conditions; and exposure to foreign exchange rate fluctuations.

Information on Directors

Name	Details
Jennifer Helen Hill-Ling LLB (Adel) FAICD <i>Chairman Non-Independent Non-Executive Director</i> Age 57	<p>Experience and expertise Appointed Director in August 1985. Appointed Deputy Chairman in June 2004. Appointed Chairman 28 October 2005.</p> <p>Jennifer Hill-Ling has extensive experience in corporate and commercial law, specialising in corporate and business structuring, mergers and acquisitions, joint ventures and related commercial transactions. She practiced law for some 25 years and was a senior partner in two Sydney law firms in that time. She was formerly a director of Tower Trust Limited and MS Limited. She is a fellow of the Australian Institute of Company Directors.</p> <p>Other current listed company directorships None.</p> <p>Former listed company directorships in last 3 years None.</p> <p>Special responsibilities Chairman of the Board Member of the Nomination and Remuneration Committee.</p> <p>Interests in shares and options at the date of this report 18,246,677 ordinary shares in Hills Limited (including 1,188,918 shares owned by Hills Associates Limited and Poplar Pty Ltd (jointly held) and 16,768,441 shares owned by Hills Associates Limited of which JH Hill-Ling is a Director).</p> <p>She does not hold any options over ordinary shares in Hills Limited.</p>

Name	Details
Fiona Rosalyn Vivienne Bennett BA (Hons) FCA FAICD <i>Independent Non-Executive-Director</i> Age 63	<p>Experience and expertise Appointed non-executive Director on 31 May 2010.</p> <p>Fiona Bennett is a Chartered Accountant with over 30 years' experience in business and financial management, corporate governance, risk management and audit. She has previously held senior executive positions at BHP Billiton Limited and Coles Group Limited and has been a Chief Financial Officer at several organisations in the health sector. She is currently Chairman of the Victorian Legal Services Board.</p> <p>Other current listed company directorships Director of BWX Limited (since November 2018) Director of Select Harvests Limited (since July 2017)</p> <p>Former listed company directorships in last 3 years Director of Beach Energy Limited (retired in November 2017)</p> <p>Special responsibilities Chairman of the Audit, Risk and Compliance Committee.</p> <p>Interests in shares and options at the date of this report 178,444 ordinary shares in Hills Limited.</p> <p>She does not hold any options over ordinary shares in Hills Limited.</p>

Information on Directors (continued)

Name	Details
<p>Philip Bullock AO BA, MBA, GAICD, Dip. Ed. <i>Independent Non-Executive-Director</i> Age 66</p>	<p>Experience and expertise Appointed non-executive Director on 23 June 2014.</p> <p>Mr Bullock AO was formerly Vice President of the Systems and Technology Group, IBM Asia Pacific, based in Shanghai, China. Prior to that he was CEO & Managing Director of IBM Australia and New Zealand. Mr Bullock AO is a non-executive director of Perpetual Limited, and formerly of CSG Limited and Healthscope Limited. He has also provided advice to the Federal Government, through a number of organisations, most notably as Chair of Skills Australia.</p> <p>Other current listed company directorships Non-executive director of Perpetual Limited (since June 2010)</p> <p>Former listed company directorships in last 3 years None.</p> <p>Special responsibilities Chairman of the Nomination and Remuneration Committee; Member of the Audit, Risk and Compliance Committee.</p> <p>Interests in shares and options at the date of this report 300,000 ordinary shares in Hills Limited.</p> <p>He does not hold any options over ordinary shares in Hills Limited.</p>
<p>Kenneth James Dwyer BCom, GMQ, GAICD <i>Independent Non-Executive-Director</i> Age 61</p>	<p>Experience and expertise Appointed non-executive Director on 20 September 2016</p> <p>Mr Dwyer formerly worked in banking, including investment banking in the US and Australia specialising in M&A, debt and equity funding.</p> <p>Mr Dwyer has established and grown two businesses in the highly competitive audio industry in Australia and New Zealand via a combination of organic growth and acquisitions.</p> <p>Mr Dwyer also has experience in the distribution of premium European machinery for textile manufacturing.</p> <p>Other current listed company directorships None.</p> <p>Former listed company directorships in last 3 years None.</p> <p>Special responsibilities Member of the Nomination and Remuneration Committee; Member of the Audit, Risk and Compliance Committee.</p> <p>Interests in shares and options at the date of this report 350,000 ordinary shares in Hills Limited.</p> <p>He does not hold any options over ordinary shares in Hills Limited.</p>

Information on Directors (continued)

Name	Details
David John Joseph Lenz <i>Executive Director</i> <i>Age 56</i>	<p>Experience and expertise</p> <p>Appointed Managing Director 19 February 2018 and Chief Executive Officer on 1 September 2016.</p> <p>Mr Lenz has over 30 years of proven experience in sales, business development, management and operational leadership across Australia and New Zealand, Asia Pacific and the Global ICT markets.</p> <p>Other current listed company directorships</p> <p>None.</p> <p>Former listed company directorships in last 3 years</p> <p>None.</p> <p>Special responsibilities</p> <p>Chief Executive Officer</p> <p>Interests in shares and options at the date of this report</p> <p>231,830 ordinary shares in Hills Limited.</p> <p>He holds performance rights as detailed in section 6.3 of the Remuneration Report.</p>
Alan Kinkade BEc(Syd),CA,FCPA,FIML,MAICD <i>Independent Non-Executive-Director</i> <i>Age 64</i>	<p>Experience and expertise</p> <p>Alan Kinkade was appointed a Director on 26 February 2019 and resigned on 19 June 2019.</p> <p>Mr Kinkade has over 30 years senior executive experience in the public and private health sector. In 2017 he retired from his role as Group CEO of Epworth HealthCare.</p> <p>Prior to his role at Epworth he was engaged in senior executive roles at Ramsay Health Care, HCF, Concord Repatriation General Hospital, Northern Sydney Area Health Service and the Royal North Shore Hospital. Mr Kinkade commenced his career at Price Waterhouse..</p> <p>Other current listed company directorships</p> <p>None.</p> <p>Former listed company directorships in last 3 years</p> <p>None.</p> <p>Special responsibilities</p> <p>None.</p> <p>Interests in shares and options at the date of this report</p> <p>None.</p> <p>He does not hold any options over ordinary shares in Hills Limited.</p>

Company Secretary

David Robert Fox LLB/LP, BA

Mr Fox was appointed to the position of General Counsel on 11 March 2013 and as General Counsel and Company Secretary on 22 December 2016.

As General Counsel and Company Secretary, Mr Fox is responsible for legal, risk and company secretarial matters associated with the Company. Mr Fox is an experienced corporate lawyer. He was first admitted to practise law in 2001 and previously held the position of Partner at a Sydney based law firm.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Meetings of Directors

The numbers of meetings of the Company's Board of Directors and of each Board Committee held during the year ended 30 June 2019, and the numbers of meetings attended by each Director were:

	Full meetings of Directors		Audit, Risk and Compliance Committee		Nomination & Remuneration Committee	
	Held ¹	Attended	Held ¹	Attended	Held ¹	Attended
J Hill-Ling	19	19	-	-	5	5
F Bennett	19	19	4	4	-	-
P Bullock AO	19	19	4	4	5	5
K Dwyer	19	19	4	4	5	5
A Kinkade ²	8	8	-	-	-	-
D Lenz	19	19	-	-	-	-

Insurance of officers

Since the end of the previous financial year, the Company has paid insurance premiums in respect of Directors' and officers' liability and legal expenses for current and former Directors and officers, including senior executives of the Company and Directors, senior executives and secretary of its controlled entities.

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

The Directors have not included details of the nature of the liabilities covered or the amount of the premiums paid in respect of the Directors' and officers' liability and legal expenses insurance contracts as such disclosure is prohibited under the terms of the contracts.

Indemnification of officers

The Company has agreed to indemnify the Directors and officers of the Company against all liabilities to another person (other than the Company or a related body corporate) that may arise from their position as Directors of the Company and its controlled entities, except where the liability arises out of conduct involving a lack of good faith.

The agreement stipulates that the Company will meet the full amount of any such liabilities, including costs and expenses.

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

Environmental regulation

Manufacturing

Hills holds all required environmental licences, registrations and permits for its sole remaining manufacturing site in O'Sullivan Beach in South Australia. No significant environmental incidents were reported during the 2019 financial year and Hills continued to meet the requirements specified in relevant licenses and authorisations.

¹ Number of meetings held during the period that the Director held office as a Director or was a member of the committee during the year.

² A Kinkade was appointed a Director on 26 February 2019 and resigned as a Director on 19 June 2019.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Environmental regulation (continued)

Australian Packaging Covenant

The Australian Packaging Covenant (APC) is a voluntary initiative by Government and industry to reduce the environmental impact of packaging. Hills became a signatory to the APC in 2010 and established ongoing action plans aimed at optimising packaging design, material recovery, recycling and product stewardship. Hills remains supportive of the goals and initiatives of the APC and remains compliant following the submission of its annual report during May 2019.

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is set out on page 29.

Non-audit services

The Company may decide to employ the auditor on assignments additional to their statutory audit duties where the auditor's expertise and experience with Hills are important.

Details of the amounts paid or payable to the auditor of Hills, KPMG, and its related practices for audit and non-audit services provided during the year are set out below.

The Board of Directors has considered the position and, in accordance with advice received from the Audit, Risk and Compliance Committee, is satisfied that the provision of the non-audit services is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The Directors are satisfied that the provision of non-audit services by the auditor, as set out below, did not compromise the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services have been reviewed by the Audit, Risk and Compliance Committee to ensure they do not impact the impartiality and objectivity of the auditor; and
- none of the services undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*.

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

	2019	2018
	\$	\$
KPMG audit and non-audit services		
Audit and other assurance services		
KPMG Australia – audit and review of the financial statements	331,500	259,000
Taxation services		
KPMG Australia – taxation and other services	15,425	16,000
Overseas KPMG firms – taxation services	4,619	4,390
Total remuneration for taxation services	20,044	20,390
Other services		
Other consulting services	2,285	7,250
Total remuneration for other services	2,285	7,250
Total remuneration of KPMG	353,829	286,640

Rounding of amounts

The Company is an entity to which the *ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191* applies. Amounts have been rounded off in accordance with the instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Letter from the Chairman of the Nomination and Remuneration Committee

Dear Shareholder,

On behalf of your Board, I am pleased to present Hills FY19 Remuneration Report which sets out remuneration information for the Chief Executive Officer and Managing Director (CEO & MD), the Key Management Personnel (KMP), the Non-Executive Directors and the broader employee group.

The Board recognises that the performance of Hills depends on the quality and motivation of its people, including our managers and approximately 500 employees across Australia and New Zealand. Our remuneration strategy aims to appropriately reward, incentivise and retain talent necessary to achieve our operational and strategic goals. Core to our remuneration philosophy is a strong performance framework, where the contribution of our employees is aligned to the interests of our shareholders. For our senior executives, this is managed through a balanced scorecard which includes both financial and non-financial measures.

FY19 Remuneration Outcomes

As we exited FY18, we felt confident regarding our ability to deliver improved results in FY19. As a result, the targets we set were aggressive. As the year unfolded, we saw that our Health Solutions business continued to gain momentum and exceeded our plans however our Distribution business continued to struggle and fell short of expectations. This led to an Operating Review of our Distribution business in 2H FY19 and an ongoing Strategic Review of Hills Limited. While these reviews have helped chart a path forward, the performance of our Distribution business impacted our overall financial results for FY19 and significantly reduced the variable pay of our senior managers with the exception of those engaged directly in our Health Solutions division.

The overall disappointing outcome in FY19 did not reflect the effort and leadership of our managers and we remain grateful for their ongoing contributions.

Executive, Management and Employee Development

As indicated in our FY18 report, we wanted to enhance the capabilities of our staff and especially our managers to help them deliver the results and employee engagement we require in these challenging times. Some of these activities are listed below:

- During October 2018, the Executive Team undertook an externally facilitated development day that focused on the alignment of individual and team Strategy, Vision & Goals and an actionable plan with facilitated quarterly reviews during December 2018 and March 2019.
- Our senior and middle managers were engaged in a leadership program aimed at better equipping them to operate as managers at Hills. An initial 2-day workshop was followed and reinforced by subsequent 6 weekly coaching circles that provided practical re-enforcement.
- Approximately 95% of the Hills sales, vendor & product sales managers attended a combination of the following practical training programs:
 - Sales Planning,
 - Negotiations and Presentation skills.
- A schedule of ongoing compliance training for all employees has been initiated with the training focused on employee roles & responsibilities. Some of the more recent compliance training programs that have been completed include:
 - Anti-Bribery & Corruption
 - Drugs & Alcohol
 - Privacy law
 - Injury management
 - Communications & Market Disclosure

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Letter from the Chairman of the Nomination and Remuneration Committee

Let me now turn to CEO & MD remuneration.

CEO & MD Remuneration

With the appointment of David Lenz in September 2016, we adopted a new market-based compensation framework. In FY19 the framework was as follows:

- Base Pay (including superannuation): \$350,000
- Variable Pay: \$250,000

The Base Pay, was set after a review of similar roles in the marketplace. It has not been adjusted since David's appointment in September 2016. In establishing the amount of Variable Pay we seek to strongly align our CEO & MD remuneration with the results of the Company and hence our shareholders. After a strong turnaround in FY18, we lifted the CEO & MD Variable Pay from \$200k to \$250k from 1 September 2018. As in the past, the Variable Pay to be determined as a result of the performance of Hills over the FY19 and paid 50% in cash and 50% in equity. The equity vests over three years at the rate of:

- 20% in year one
- 30% in year two
- 50% in year three.

The hurdles associated with the variable pay for FY19 were as follows:

Element	Measure
Financial (70%)	Net Profit After Tax (NPAT) Operating Cash Flow Inventory Management
Non-financial (30%)	Vendor Commitment Employee Engagement Board discretion

Despite the outstanding results of our Health Solutions division the overall Hills Limited financial targets were not met. With regard to the Non-Financial targets, we have not lost any major vendors, in fact the total revenue and margin from our top 5 distribution vendors has increased. We have seen a concerted effort to enhance employee skills with employee engagement improving by 2 points over our FY18 results. This is a pleasing outcome given the difficult nature of the year. At the same time, our CEO & MD has worked hard to implement the results of our Strategic and Operating Reviews which were conducted in 2H FY19 and helped lay a path for an improved FY20.

Based upon these results the Board has determined that the CEO & MD has earned 16% of his variable pay.

There are no plans to amend the CEO & MD remuneration for FY20.

Non-Executive Director Remuneration:

In light of the financial results and to bring fees in line with similar sized companies, effective 1 July 2019, Non-Executive Director (NED) compensation has been reduced by approximately 25-40% per annum as follows:

- Company Chair from \$160,000 to \$100,000
- Non-executive director from \$80,000 to \$60,000
- Audit Committee Chair from \$16,000 to \$10,000
- The Nomination and Remuneration Committee Chair Fee of \$16,000 has been removed.
- The Audit Committee Membership fee of \$8,000 has been removed.

In addition, we continue to review the skill mix and size of our Board in light of the recent Strategic Review and have no plans to increase our Board size beyond four non-executive members.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Letter from the Chairman of the Nomination and Remuneration Committee (continued)

FY20 Outlook

As indicated earlier, we have been very pleased with the growth and profitability of our Health Solutions division, however the performance of our Distribution business continued to impact Hills overall performance and had not sustained the momentum of the FY18 turnaround.

As a result, we instigated a Strategic Operating Review of our Distribution division in the 2H of FY19. This review identified a number of areas where improvements could be made. These improvements have been included in our plans and we are determined that we should return our Distribution business to profitability in FY20 while continuing to grow and expand our Health Solutions division.

In light of this, we have adjusted the FY20 scorecard to increase the weighting of our financial measures from 70% to 80%. In addition, we have shortened the Aged Inventory target from 180 to 90 days to reflect our need for not only inventory reduction, but the mix and currency of our inventory.

We recognise that we have a significant weighting of financial measures for our CEO & MD, however we feel that at this stage of our transformation it is critical.

Element	Measure
Financial (80%)	Net Profit After Tax (NPAT) Deliver Hills Distribution Profit in FY20 Reduce Aged Inventory > 90 days
Non-financial (20%)	Employee Engagement Board Discretion

The variable incentive targets for our CFO are linked closely with those of the CEO & MD but also include a focus on improving our Debtors Outstanding. Division Heads are rewarded primarily on profit contribution for their division.

Thank you for taking the time to review the FY19 Remuneration Report. We are disappointed that we have not delivered the results our shareholders would have expected nor those our team had planned for and this is reflected in the variable compensation paid. Despite this it is important to conclude by thanking the employees of Hills for their ongoing loyalty and dedication to our customers and suppliers. Our employees' efforts continue to help differentiate Hills in the marketplace.

Yours sincerely



Philip Bullock AO

Chairman, Nomination and Remuneration Committee

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

Remuneration report – audited

This Remuneration Report explains Hills approach to executive remuneration, performance and remuneration outcomes for Hills and its Key Management Personnel (KMP) for the year ended 30 June 2019 (FY19). In this report, 'senior executives' refers to the KMP excluding non-executive directors.

The information provided in the Remuneration Report has been audited as required by Section 308 (3C) of the *Corporations Act 2001*.

The Remuneration Report comprises the following sections:

- 1 Key Management Personnel
- 2 Remuneration Governance
- 3 Executive Remuneration
- 4 Executive Contracts and Termination Arrangements
- 5 Five Year Snapshot - Business and Remuneration Outcomes
- 6 Statutory Remuneration Tables
- 7 Non-Executive Directors' Remuneration
- 8 Equity instrument disclosures relating to Key Management Personnel

1 Key Management Personnel

KMP encompasses all Directors, as well as those senior executives who had specific responsibility for planning, directing and controlling material activities of Hills during FY19.

Name	Position	Term as KMP in FY19
Directors		
J Hill-Ling	Chairman, Non-Independent and Non-Executive Director	Full Year
F Bennett	Independent, Non-Executive Director	Full Year
P Bullock AO	Independent, Non-Executive Director	Full Year
K Dwyer	Independent, Non-Executive Director	Full Year
D Lenz	Executive Director	Full Year
A Kinkade	Independent, Non-Executive Director	Commenced 26 February 2019. Resigned 19 June 2019
Senior Executives		
D Lenz	Chief Executive Officer & Managing Director	Full Year
C Jacka	Chief Finance Officer	Full Year
D Fox	Company Secretary & General Counsel	Full Year
R Edgar	Head of Security, Surveillance, IT and ATV	Commenced 5 July 2018
A Hall	Head of Health Solutions	Full Year

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

2 Remuneration Governance

2.1 Role of the Nomination and Remuneration Committee

The Board, with assistance from the Nomination and Remuneration Committee, is ultimately responsible for ensuring that the Hills remuneration framework is consistent with the business strategy and performance, supporting increased shareholder wealth over the long term.

The Nomination and Remuneration Committee, consisting of non-executive directors: Philip Bullock (Chairman), Jennifer Hill-Ling and Ken Dwyer have responsibility for reviewing the remuneration strategy annually and advises the Board on remuneration policies and practices generally.

The Nomination and Remuneration Committee is responsible for:

- the ongoing appropriateness and relevance of the remuneration framework for the Chairman, the Board Committees and the non-executive Directors;
- Hills remuneration policy for the CEO & MD, his direct reports and other senior executives, any changes to the policy, and the implementation of the policy including any shareholder approvals required; and
- incentive plans for the CEO & MD, his direct reports and other senior executives.

Further detail on the Nomination and Remuneration Committee's responsibilities is set out in its Charter, which is reviewed annually, and which is available on the Hills website at: <http://www.corporate.hills.com.au/about-us/governance>.

2.2 Use of Independent Remuneration Consultants

In accordance with the Nomination and Remuneration Committee Charter, the Committee seeks advice and market data from independent remuneration consultants as required.

During the year no advisors were engaged.

2.3 Hills Share Trading Policy

The Hills Share Trading Policy imposes trading restrictions on all Hills employees who are considered to be in possession of 'inside information' and additional restrictions in the form of trading windows for senior executives. Board members, senior executives and members of the broader management team are prohibited from trading in Hills shares during specific periods prior to the announcement of the half and full year results. This policy applies equally to shares received as part of remuneration. The Securities Policy is available on the Hills website at: <http://www.corporate.hills.com.au/about-us/governance>.

2.4 Hills Clawback Policy

To strengthen the governance of the remuneration strategy, Hills has an executive remuneration Clawback Policy in place. The policy is designed to further align the remuneration outcomes of the Hills senior executive team with the long-term interests of Hills and its shareholders, to ensure that excessive risk taking is not rewarded, and to provide the Board with the ability to claw back incentives paid, where there has been a material misstatement in Hills Financial Statements.

3. Executive Remuneration

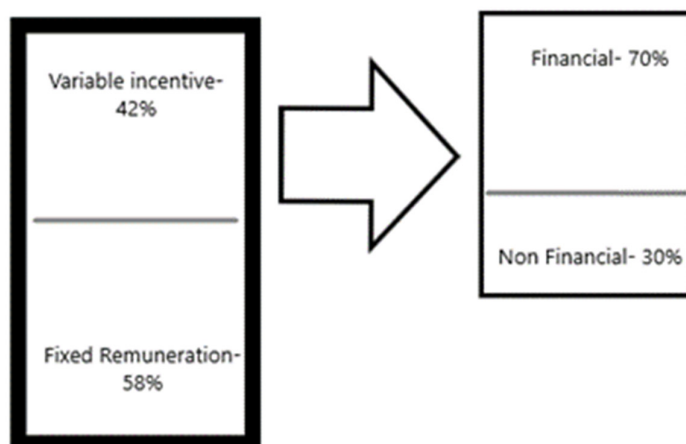
3.1 Alignment of Remuneration Strategy with Business Strategy

The Board has established a Remuneration Strategy that supports and drives the achievement of the Hills Business Strategy. The Board is confident that the remuneration framework aligns the remuneration of the senior executives with shareholder interests. Hills is a business that is heavily focused on key performance indicators (KPIs) and rewards its people at all levels on achievement of those KPIs.

3.2 Remuneration Mix

In FY19, senior executive remuneration was comprised of Fixed Remuneration (made up of base salary and superannuation), and variable incentive. The CEO & MD split was approximately 55-60% Fixed Remuneration and 40-45% Variable Incentive. Other executives had a split of approximately 60-80% Fixed Remuneration and 20-40% Variable Incentive, dependent on their role.

Chart 3.2: CEO & MD Remuneration Mix FY19



Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

3 Executive Remuneration (continued)

3.3 Chief Executive Officer (CEO) and Managing Director (MD) Remuneration

In FY19, the CEO & MD, Mr David Lenz had a fixed remuneration of \$350,000 per annum (inclusive of superannuation).

Fixed Remuneration is reviewed annually by the Board with reference to performance of the Company, performance of the CEO & MD, and market information.

Variable Incentive FY19

Mr Lenz had a variable incentive opportunity of up to \$250,000.

The variable incentive for FY19 adopted a balanced scorecard approach which was aligned to the Company's strategic plan. The balanced scorecard focused on the following key areas:

Element	Measure
Financial (70%)	Net Profit After Tax (NPAT)
	Operating Cash Flow
	Inventory Management
Non-financial (30%)	Board Discretion
	Vendor Commitment
	Employee Engagement

Weighting was distributed across these measures.

The variable incentive is paid 50% as cash and 50% as Performance Rights (unless the Board determines otherwise), with vesting to take place over a 3-year period in the following manner:

- 20% after 1 year;
- 30% after 2 years; and
- 50% after 3 years.

Mr Lenz was awarded an initial sign-on bonus of 200,000 Hills Performance Rights on 1 September 2016. The first tranche of 100,000 shares vested in September 2017 and the second tranche vested in September 2018.

3.4 Senior Executive Variable Incentive FY19

Variable Incentive – How It Works

The variable incentive is an at risk component of remuneration and is designed to reward performance against the achievement of a balanced scorecard which is aligned to the Company's strategic plan. Senior executive variable incentives were determined on similar measures to the CEO & MD.

The variable incentive performance period was from 1 July 2018 to 30 June 2019.

The maximum variable incentive available to each senior executive was set at a level based on role, responsibilities and market data for the achievement of targets against specific KPIs. The maximum variable incentive opportunity for each senior executive is listed at section 3.5 as an absolute dollar amount and as a percentage of the senior executive's fixed remuneration.

3 Executive Remuneration (continued)

The following table summarises the potential FY19 variable incentive payments where a senior executive ceased employment with Hills:

Resignation and retirement	Any entitlement to a payment was subject to the participant being employed by Hills at the time of payment.
Company initiated termination	Any entitlement to a payment would be for completed months, with no pro-rata for partly completed months. The calculation of an entitlement was based on actual results for the year and paid on the scheduled date.
Summary dismissal	If summarily dismissed, a participant forfeits all rights to any payments under the FY19 variable incentive which had not already vested or been made.

Assessment of Performance and Approval of Payment

The Remuneration & Nomination Committee assessed the individual senior executive's performance based on the CEO & MD's recommendations, against the KPIs set at the beginning of the financial year. The assessment of individual performance was combined with the achievement of financial results to determine the amount of payment for each senior executive. The Remuneration & Nomination Committee recommended the variable incentive payment outcome to the Board for approval. Variable incentive payments for FY19 were delivered as cash payments following approval by the Board. Details of Variable Incentive payments are provided in section 3.5.

3.5 FY19 Variable Incentive Performance and Outcomes

FY19 was a year of mixed results. Our Health Solutions and Hills Connection Solutions businesses continued to grow and make significant profit contributions to our business. Unfortunately, our Distribution business did not perform to expectations thus significantly reducing the overall Hills Limited results. These outcomes are reflected in the variable incentive plan results detailed in this report. A summary of Company performance compared to previous years is provided in section 5.

The KPIs for the senior executives were aligned to the CEO & MD's KPIs. The variable incentives received by the CEO & MD and senior executives for FY19 (if any) are set out in the following table:

	Target Variable Incentive opportunity (pro-rata)	% of fixed remuneration	Actual Variable Incentive outcome	% Achieved	% Forfeited
Executive Director					
D Lenz	\$237,500	66%	\$38,000	16%	84%
Other Senior Executive					
C Jacka	\$137,500	54%	\$30,250	22%	78%
D Fox	\$80,000	27%	\$12,800	16%	84%
A Hall	\$125,000	42%	\$180,000	144%	0%
R Edgar	\$71,211	25%	\$11,520	16%	84%
TOTAL	\$651,211	46%	\$272,570	42%	58%

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

3 Executive Remuneration (continued)

3.6 FY20 Variable Incentive Design for CEO & MD

Variable Incentive Plan – FY20

For FY20 it has been decided to continue the variable incentive plan which involves remunerating selected executives on their annual performance by cash and in the case of our CEO & MD by shares which vest over a 3-year period according to the following vesting scale:

- 20% after 1 year;
- 30% after 2 years; and
- 50% after 3 years.

The annual performance against which the CEO & MD will be measured is in accordance with the balanced scorecard which has the following measures.

Element	Measure
Financial (80%)	Net Profit After Tax (NPAT) Deliver Hills Distribution Profit in FY20 Reduce Aged Inventory > 90 days
Non-financial (20%)	Employee Engagement Board Discretion

Other executives had similar scorecards which reflected their specific roles.

4 Executive Contracts and Termination Arrangements

Employment contracts

The remuneration and other terms of employment for the CEO & MD, and senior executives are covered in their individual employment contracts and are summarised in this table:

Chief Executive Officer & Managing Director	<ul style="list-style-type: none">▪ The contract for the Chief Executive Officer and Managing Director commenced on 1 September 2016 for an initial term of 12 months, following which the Chief executive Officer and Managing Director will continue to be employed till either party provides notice.▪ Hills or the Chief Executive Officer and Managing Director may terminate employment at any time by giving three months' written notice.
Senior Executives	<ul style="list-style-type: none">▪ The contracts may be terminated by either party by giving 3 months written notice.
Chief Executive Officer and Senior Executives	<ul style="list-style-type: none">▪ There are no guaranteed base pay increases included in any senior executive contract.▪ In the instance of serious misconduct, Hills may terminate employment at any time. The executive will only receive payment to the date of termination and any statutory entitlements.▪ Retirement benefits comprise employer contributions to defined contribution superannuation funds.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

5 Five Year Snapshot – Business and Remuneration Outcomes

An underlying principle of the Hills remuneration strategy is that remuneration must be linked to the performance of Hills.

The following is a summary of financial performance and share price information over the last five years.

Key Financials		FY19	FY18	FY17	FY16	FY15
Shareholders' funds	\$000	52,357	61,308	60,931	69,077	136,600
Statutory net profit / (loss)	\$000	(8,826)	359	(7,932)	(68,305)	(85,780)
Basic earnings / (loss) per share	cents	(3.8)	0.2	(3.4)	(29.4)	(37.0)
Dividends	cents	-	-	-	2.1	2.1
Share Price – as at 30 June	\$	0.18	0.23	0.16	0.25	0.46
Variable Incentive Payments for KMP's as recorded in each financial year- % of target opportunity	%	40% ¹	30%	29%	19%	4%

6 Statutory Remuneration Tables

6.1 Senior Executive Remuneration

The following table of senior executives' remuneration has been prepared in accordance with accounting standards and the Corporations Act 2001 requirements. The amounts shown are equal to the amounts expensed (and not necessarily paid) in the Company's financial statements.

Name	Short-term benefits			Post-employment benefits	Long term benefits	Share based payments		TOTAL
	Cash salary & fees	Cash bonus ²	Other	Superannuation	LSL ³	Termination benefits ⁴	Performance rights	
FY19								
\$								
Executive Director								
D Lenz	328,100	38,000	-	21,689	7,802	-	13,378	408,969
Senior Executives								
C Jacka	229,001	30,250	-	22,393	3,786	-	-	285,430
D Fox	245,338	12,800	9,407	23,888	19,382	-	-	310,815
A Hall	266,057	180,000	5,000	20,310	2,921	-	-	474,288
R Edgar	247,115	11,520	8,443	22,476	242	-	-	289,796
Total Senior Executives	1,315,611	272,570	22,850	110,756	34,133	-	13,378	1,769,298

¹ Excluding the Health Solutions business this metric would have been 17%.

² MD & CEO cash bonus reflects the 50% of variable incentive paid as performance share rights as noted in Section 3.3 of this report.

³ Long Service Leave.

⁴ In accordance with statutory and legal obligations.

6 Statutory Remuneration Tables (continued)

FY18 \$	Short-term benefits			Post-employment benefits	Long term benefits	Share based payments		TOTAL
	Cash salary & fees	Cash bonus ¹	Other	Superannuation	LSL ²	Termination benefits ³	Performance rights	
Executive Director								
D Lenz	327,756	37,500	-	21,978	3,736	-	32,075	423,045
Senior Executives								
C Jacka	211,305	44,000	-	19,727	1,562	-	-	276,594
D Fox	246,040	31,643	-	22,257	20,767	-	-	320,707
Former Senior Executives								
D Osborne ⁴	278,410	-	-	24,696	-	-	-	303,106
Total Senior Executives	1,063,511	113,143	-	88,658	26,065	-	32,075	1,323,452

6.2 Remuneration components as a proportion of total remuneration paid or expensed

The following table reflects the fixed remuneration and Variable Incentive for FY19 calculated in accordance with the accounting standards as a proportion of the total.

Name	Full Year Potential Variable Incentive	Pro-rata Potential Variable Incentive ⁵	Actual Variable Incentive paid / payable	Actual Variable Incentive paid / payable as % of Full Year Potential	Actual Variable Incentive paid / payable as % of Pro-rata	Variable Incentive paid / payable as % of Fixed Remuneration
Executive Director						
D Lenz	\$250,000	\$237,500	\$38,000	15%	16%	11%
Senior Executives						
C Jacka	\$150,000	\$137,500	\$30,250	20%	22%	12%
D Fox	\$80,000	\$80,000	\$12,800	16%	16%	4%
A Hall	\$125,000	\$125,000	\$180,000	144%	144%	61%
R Edgar	\$72,000	\$71,211	\$11,520	16%	16%	4%

¹ MD & CEO cash bonus reflects the 50% of variable incentive paid as performance share rights as noted in Section 3.3 of this report.

² Long Service Leave.

³ In accordance with statutory and legal obligations.

⁴ D Osborne resigned as Head of Hills Health Solutions on 26 June 2018.

⁵ Incentive applicable from 1 September 2018

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

6 Statutory Remuneration Tables (continued)

6.2 Remuneration components as a proportion of total remuneration paid or expensed (continued)

The following table reflects the fixed remuneration, Variable Incentive and total performance-based remuneration for FY19 calculated in accordance with the accounting standards as a proportion of the total remuneration.

Name	Fixed remuneration %	At risk Variable Incentive paid or payable %	Value of performance rights %	Total performance based %
Executive Director				
D Lenz	88%	9%	3%	12%
Senior Executives				
C Jacka	89%	11%	-	11%
D Fox	96%	4%	-	4%
A Hall	62%	38%	-	38%
R Edgar	96%	4%	-	4%

The following table shows the proportion weighting of each element of remuneration for each of the senior executives employed during FY19 based on maximum potential outcome.

Name	Fixed remuneration %		Maximum Variable Incentive %		Maximum Long-Term Incentive %	
	FY19	FY18	FY19	FY18	FY19	FY18
Executive Director						
D Lenz	59%	62%	39%	35%	2%	3%
Senior Executives						
C Jacka	65%	70%	35%	30%	-	-
D Fox	79%	78%	21%	22%	-	-
A Hall	70%	-	30%	-	-	-
R Edgar	80%	-	20%	-	-	-

6.3 Number of performance rights granted, vested and expired / forfeited in FY19

	At 1 July 2018	Granted	Vested	Forfeited	At 30 June 2019
Executive Director					
D Lenz	227,322	198,646	(187,475)	-	238,493

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

7 Non-Executive Directors' Remuneration

The Board sets non-executive Director Remuneration at a level which enables the attraction and retention of directors of the highest calibre, while incurring a cost which is acceptable to shareholders. The remuneration of the non-executive directors is determined by the Board on recommendation from the Nomination and Remuneration Committee within a maximum fee pool.

Non-executive directors receive a base fee and statutory superannuation contributions. Non-executive directors do not receive any performance-based pay. Fees for non-executive directors were decreased in FY16. They were decreased again from 1 July 2019, as noted earlier in the letter from the Chairman.

7.1 Fee Pool

The maximum amount of fees that can be paid to non-executive directors is capped by a pool approved by shareholders. At the FY11 Annual General Meeting, shareholders approved the current fee pool of \$1.2 million which is recorded on an accrual basis. The fee pool did not change in FY19.

7.2 Directors' FY19 Fee Structure

The following table outlines the main Board and Committee fees as at 30 June 2019.

	Chair fee \$	Member fee \$
Board	160,000	80,000
Audit and Risk Committee	16,000	8,000
Nomination and Remuneration Committee	16,000	Nil

As indicated earlier from 1 July 2019 the Board and Committee fees are:

	Chair fee \$	Member fee \$
Board	100,000	60,000
Audit and Risk Committee	10,000	Nil
Nomination and Remuneration Committee	Nil	Nil

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

7 Non-Executive Directors' Remuneration (continued)

7.3 Non-executive Directors' remuneration details

Non-Executive Directors	Year	Board and Committee fees \$	Superannuation \$	Total \$
J Hill-Ling	2019	146,120	13,880	160,000
	2018	146,119	13,881	160,000
F Bennett	2019	87,672	8,328	96,000
	2018	87,671	8,329	96,000
P Bullock AO	2019	94,978	9,022	104,000
	2018	94,978	9,022	104,000
K Dwyer	2019	80,366	7,634	88,000
	2018	80,367	7,633	88,000
A Kinkade	2019	22,761	2,162	24,923
TOTAL	2019	431,897	41,026	472,923
	2018	409,135	38,865	448,000

7.4 Retirement Allowance for Non-Executive Directors

Ms J Hill-Ling is the only Director entitled to receive benefits on retirement under a scheme that was discontinued on 1 August 2003. Under the scheme, Ms J Hill-Ling is entitled to a maximum retirement benefit of twice her annual Director's fee (calculated as an average of her fees over the last three years) with a vesting period of eight years, which has been achieved. Since the scheme was discontinued, no new Directors have become entitled to any benefit and the benefit multiple (up to a maximum of two times fees) remains fixed. The benefit is fully provided for in the financial statements.

Hills Limited

Directors' report

For the year ended 30 June 2019 (continued)

8 Equity instrument disclosures relating to Key Management Personnel

8.1 Share Holdings

The numbers of shares in the Company held during the financial year by each Director of Hills Limited and other key management personnel of the Company, including their personally related parties, are set out below. There were no shares granted during the reporting period as compensation.

The Company has a policy requiring directors to hold a minimum number of shares. Specifically, directors are required to hold a minimum number of shares and are required to attain this shareholding within a reasonable period.

Ordinary shares				
	Balance at start of the year	Received during the year on the exercise of options / rights	Other changes during the year	Balance at the end of the year
Directors and Key Management Personnel				
J Hill-Ling	18,146,677	-	100,000	18,246,677
F Bennett	178,444	-	-	178,444
P Bullock AO	200,000	-	100,000	300,000
K Dwyer	250,000	-	100,000	350,000
A Kinkade	-	-	-	-
D Lenz	100,000	131,830	-	231,830
D Fox	-	-	833,888	833,888

Messrs Jacka, Hall and Edgar did not hold any shares in the Company at the start of the year or at any point during the year.

8.2 Loans to Key Management Personnel

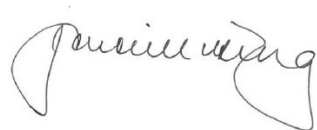
There were no outstanding loans to KMP or their related parties at the reporting date.

8.3 Other Transactions with Key Management Personnel

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

From time to time, KMP of the Company or its controlled entities, or their related entities, may purchase goods or services from Hills or make sales of goods or services to Hills. These purchases or sales are on the same terms and conditions as those entered into by Hills employees, customers or suppliers and are trivial and domestic in nature.

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



Jennifer Hill-Ling
Director



Philip Bullock AO
Director

Sydney
30 August 2019



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

To the Directors of Hills Limited

I declare that, to the best of my knowledge and belief, in relation to the audit of Hills Limited for the financial year ended 30 June 2019 there have been:

- i. no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- ii. no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Paul Cenko
Partner

Adelaide

30 August 2019

Consolidated financial statements for the year ended 30 June 2019

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Consolidated statement of profit or loss
For the year ended 30 June 2019

	Notes	2019 \$'000	2018 \$'000
Continuing operations			
Revenue	2	267,362	271,781
Cost of sales	4a	(183,488)	(185,101)
Gross Margin		83,874	86,680
Other income	3	551	910
Expenses excluding net finance expenses			
Labour and related expenses		(52,733)	(54,044)
Operational and equipment expenses		(6,322)	(7,163)
Property expenses		(7,596)	(7,711)
Depreciation and amortisation	4a	(6,617)	(6,519)
Other expenses	4b	(22,306)	(8,950)
Expenses excluding net finance expenses		(95,574)	(84,387)
(Loss) / Profit before net finance expense and income tax		(11,149)	3,203
Finance income		121	121
Finance expenses		(3,386)	(3,284)
Net finance expenses	4a	(3,265)	(3,163)
(Loss) / Profit before income tax		(14,414)	40
Income tax benefit from continuing operations	5	5,588	319
(Loss) / Profit from continuing operations		(8,826)	359
(Loss) / Profit for the year, attributable to owners of Hills Limited		(8,826)	359
Profit/(Loss) per share for loss from continuing operations attributable to the ordinary equity holders of the Company:			
		Cents	Cents
Basic and diluted profit/(loss) per share	6	(3.8)	0.2

The above consolidated statement of profit or loss should be read in conjunction with the accompanying notes.

Hills Limited

Consolidated statement of comprehensive income

For the year ended 30 June 2019

	Notes	2019 \$'000	2018 \$'000
(Loss) / Profit for the year		(8,826)	359
Other comprehensive income			
<i>Items that may be reclassified to profit or loss</i>			
Changes in the fair value of cash flow hedges	15	(198)	318
Exchange differences on translation of foreign operations	15	260	(237)
Income tax relating to components of other comprehensive income	5	-	(95)
Other comprehensive income / (loss) for the year, net of tax		62	(14)
Total comprehensive (loss) / income for the year, attributable to owners of Hills Limited		(8,764)	345

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

Hills Limited
Consolidated statement of financial position
As at 30 June 2019

	Notes	2019 \$'000	2018 \$'000
ASSETS			
Current assets			
Cash and cash equivalents	7	10,867	15,783
Trade and other receivables	8	59,194	59,651
Inventories	9	41,636	44,043
Derivative financial instruments	18	-	93
Total current assets		111,697	119,570
Non-current assets			
Investments		2	2
Property, plant and equipment	11	15,281	14,915
Intangible assets	12	2,072	6,267
Deferred tax assets	5	16,733	11,122
Total non-current assets		34,088	32,306
Total assets		145,785	151,876
LIABILITIES			
Current liabilities			
Trade and other payables	10	40,646	47,731
Borrowings	17	15,927	6,357
Provisions	13	8,731	6,206
Derivative financial instruments	18	106	-
Total current liabilities		65,410	60,294
Non-current liabilities			
Borrowings	17	23,331	26,339
Provisions	13	4,687	3,935
Total non-current liabilities		28,018	30,274
Total liabilities		93,428	90,568
Net assets		52,357	61,308
EQUITY			
Contributed equity	14	278,439	278,439
Reserves	15	11,128	11,053
Accumulated losses		(237,210)	(228,184)
Total equity		52,357	61,308

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

Hills Limited

Consolidated statement of changes in equity

For the year ended 30 June 2019

		Attributable to owners of Hills Limited			
Notes	Contributed equity \$'000	Reserves \$'000	Accumulated losses \$'000	Total \$'000	
	278,439	11,035	(228,543)	60,931	
Balance at 1 July 2017					
Total comprehensive income / (loss) for the year	-	(14)	359	345	
Transactions with owners in their capacity as owners:					
Employee share schemes	-	32	-	32	
Balance at 30 June 2018	278,439	11,053	(228,184)	61,308	
Balance at 1 July 2018	278,439	11,053	(228,184)	61,308	
Adjustment for initial application of AASB9	-	-	(200)	(200)	
Total comprehensive income for the year	-	62	(8,826)	(8,764)	
Transactions with owners in their capacity as owners:					
Employee share schemes	-	13	-	13	
Balance at 30 June 2019	278,439	11,128	(237,210)	52,357	

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

Hills Limited
Consolidated statement of cash flows
For the year ended 30 June 2019

	Notes	2019 \$'000	2018 \$'000
Cash flows from operating activities			
Receipts from customers (inclusive of goods and services tax)		292,109	300,312
Payments to suppliers and employees (inclusive of goods and services tax)		(293,324)	(285,947)
		(1,215)	14,365
Net finance costs paid		(2,775)	(2,607)
Net income taxes received / (paid)		(14)	219
Net cash flows (used in) / from operating activities	7	(4,004)	11,977
Cash flows from investing activities			
Payments for property, plant and equipment	11	(2,646)	(1,233)
Payments for intangible assets	12	(3,019)	(5,193)
Proceeds from sale of property, plant and equipment and intangible assets		24	188
Net cash flows (used in) / from investing activities		(5,641)	(6,238)
Cash flows from financing activities			
Proceeds from borrowings		7,650	3,461
Repayment of borrowings		(3,000)	(1,961)
Net cash flows from financing activities	17	4,650	1,500
Net (decrease) / increase in cash and cash equivalents		(4,995)	7,239
Cash and cash equivalents at the beginning of the year		15,783	8,651
Effects of exchange rate changes on cash and cash equivalents		79	(107)
Cash and cash equivalents at end of the year	7	10,867	15,783

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

Section A: About this report

These consolidated financial statements are for the group consisting of Hills Limited (the "Company" or "parent entity") and its subsidiaries (together referred to as the "Group" or "Consolidated Entity" and individually as "Group Entities").

The notes to the consolidated financial statements that follow present information relevant to understanding the Group's:

- business performance;
- operating assets and liabilities;
- capital and financing arrangements, including the Group's approach to risk;
- structure, including related party transactions and parent entity information; and
- unrecognised items at the end of the reporting period.

Other information that is required to be disclosed to comply with the accounting standards, the *Corporations Act 2001* or the Corporations Regulations, but are not considered significant to understand the financial performance or financial position of the Group are provided at the end of the notes.

Hills Limited is a for profit company limited by shares, incorporated and domiciled in Australia.

The consolidated financial statements were authorised for issue by the Directors on 30 August 2019. The Directors have the power to amend and reissue the consolidated financial statements.

Basis of preparation

These general purpose consolidated financial statements:

- are presented in Australian dollars;
- have been prepared in accordance with Australian Accounting Standards (AASBs), other authoritative pronouncements of the Australian Accounting Standards Board, and the *Corporations Act 2001*;
- comply with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB); and
- have been prepared on the basis of historical costs, except for financial instruments (derivatives) at fair value. The methods used to measure fair values are discussed further in note 20.

Key accounting estimates

In preparing these financial statements, management are required to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

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 and in any future periods affected.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

Key accounting estimates (continued)

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements are described in the following notes:

Note 2	Recognition of revenue accounted for using the percentage of completion method
Note 5	Tax losses for which no deferred tax asset has been recognised
Note 9	Net realisable value of inventory
Notes 11 and 12	Measurement of property, plant and equipment and intangible assets
Notes 13 and 25	Provisions and contingencies
Note 20	Measurement of fair value

Principles of consolidation

Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of the Company as at 30 June 2019 and the results of all subsidiaries for the year then ended. A list of subsidiaries is included in note 21.

Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power to direct the activities of the entity.

Subsidiaries are fully consolidated from the date on which control was obtained by the Group. They are de-consolidated from the date that control ceases.

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

Changes in ownership interests

The Group treats transactions with non-controlling interests that do not result in a loss of control as transactions with equity owners of the Group. A change in ownership interest results in an adjustment between the carrying amounts of the controlling and non-controlling interests to reflect their relative interests in the subsidiary. Any difference between the amount of the adjustment to non-controlling interests and any consideration paid or received is recognised in a separate reserve within equity attributable to owners of Hills.

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

Foreign currency translation

Functional and presentation currency

Items included in the consolidated financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The Australian dollar is the Company's functional and presentation currency and the functional and presentation currency of the majority of the Group.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

Foreign currency translation (continued)

Transactions and balances

Transactions in foreign currencies are translated to the respective functional currencies of Group Entities using exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the foreign exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary assets and liabilities that are measured in terms of historical cost are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are recognised in profit or loss.

Group entities

The results and financial position of all Group Entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

Closing rate	Assets and liabilities for each statement of financial position
Average rate	Income and expenses for each income statement: average rates, unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transactions dates (in which case, the rates on the transaction dates are used)

All resulting exchange differences are recognised in other comprehensive income.

Rounding

The Company is an entity to which the *ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191* applies. Amounts have been rounded off in accordance with the instrument to the nearest thousand dollars, or in certain cases, the nearest dollar.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

Section B: Business performance

This section contains information relevant to understanding the results and performance of the Group during the reporting period:

- 1 Segment information
- 2 Revenue
- 3 Other income
- 4 Expenses
- 5 Income tax
- 6 Profit / (Loss) per share

1 Segment information

Considering the continued growth of the Health business a decision was made to review the reportable segments. This has resulted in a change to the reported financial metrics below. In accordance with accounting standards, comparative information has been reclassified in the same format.

Although the Group's divisions are managed on a products and services basis, they operate in two main geographical areas:

Australia	Comprises manufacturing facilities in South Australia and sales offices and customers in most states and territories.
Overseas	Comprises sales offices and customers in New Zealand and customers in the Pacific Islands, the Middle East, Europe, Asia and North America.

(a) Information about reportable segments

	Revenue ¹		EBITDA ²	
	2019 \$'000	2018 \$'000	2019 \$'000	2018 \$'000
Reportable segment				
Distribution	229,295	240,835	1,747	4,522
Health	38,067	30,946	11,087	7,433
Corporate	-	-	(2,664)	(2,584)
Total segment result	267,362	271,781	10,170	9,371

(b) Other segment information

Segment revenue

The revenue from external customers reported to the Chief Operating Decision Maker (CODM) is measured in a manner consistent with that in the consolidated income statement. There are no sales between segments. Segment revenue reconciles to total revenue per note 2.

The Group did not derive 5% or more of its revenues from any single external customer.

¹ Total segment revenue represents revenue from external customers.

² Earnings before interest, tax, depreciation, amortisation and impairment of intangible assets, goodwill and other receivables (EBITDA) is a non-IFRS measure not subject to audit or review. Segment EBITDA excludes the impact of certain income and costs associated with the restructuring of the Company to support future growth opportunities. This non-IFRS measure is relevant because it is consistent with the measures used internally by management and some in the investment community to assess the operating performance of the business.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

1 Segment information (continued)

Segment EBITDA

The CODM assesses performance based on a measure of EBITDA. This excludes the effects of non-recurring expenditure from the operating segments such as restructuring costs and intangible asset impairments when the impairment is the result of an isolated, non-recurring event and business combination acquisition transaction costs which, although expensed, are considered to otherwise distort the operational view of the business.

Segment EBITDA reconciles to the loss before income tax as follows:

	Notes	2019 \$'000	2018 \$'000
Segment EBITDA		10,170	9,371
Depreciation and amortisation	4	(6,617)	(6,519)
Net finance expenses	4	(3,265)	(3,163)
Net costs not considered part of segment EBITDA		(14,702)	(67)
Other income not considered part of segment EBITDA		-	418
(Loss) / Profit before income tax from continuing operations		(14,414)	40

Net costs not considered part of segment EBITDA comprise:

	2019 \$'000	2018 \$'000
Costs related to proposed demerger of the Hills Health Solutions business	-	(121)
Reversal of impairment of property, plant and equipment	-	165
Other net costs related to the Company's restructure and transformation program	(502)	(111)
Onerous lease provision	(2,500)	-
Inventory provision	(3,800)	-
Provision for redundancy	(1,400)	-
Impairment of non-current assets	(6,500)	-
	(14,702)	(67)
Other income relating to recovery of previously written off bad debt (see note 3)	-	418
Total net (costs) / income not considered part of segment EBITDA	(14,702)	351

Segment assets and liabilities No information regarding segment assets and liabilities has been disclosed, as these amounts are not reported to the CEO for the purpose of making strategic decisions.

Geographical information

Segment revenue and non-current assets (excluding financial instruments and deferred tax assets) by geographical location are shown below. Segment revenues are allocated based on the country in which the customer is located. Segment assets are allocated based on where the assets are located.

	Revenue		Non-current assets	
	2019 \$'000	2018 \$'000	2019 \$'000	2018 \$'000
Australia	248,601	252,326	17,043	20,703
Other countries	18,761	19,455	312	481
	267,362	271,781	17,355	21,184

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

1 Segment information (continued)

Recognition and measurement

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker (CODM). The CODM, who is responsible for allocating resources and assessing the performance of the operating segments, has been identified as the Board of Directors.

Operating segments that exhibit similar long-term economic characteristics, and have similar products, processes, customers, distribution methods and regulatory environments are aggregated.

2 Revenue

	2019 \$'000	2018 \$'000
<i>Sales revenue</i>		
Sale of goods	215,133	225,739
Services	52,229	46,042
Total revenue from continuing operations	267,362	271,781

Recognition and measurement

Revenue

The Group has adopted AASB 15 *Revenue from contracts with customers* from 1 July 2018, which replaces AASB 118 *Revenue*.

AASB 15 establishes a principles-based approach for revenue recognition whereby revenue is recognised when performance obligations are satisfied, and the control of goods or services is transferred. The standard applies a five-step approach to the timing of revenue recognition and is applicable to all contracts with customers, except those in the scope of other standards, replacing the separate models for goods, services and construction contracts under the previous accounting standards. The major sources of the Group's revenue are from the sale of goods and rendering of services, which are each considered below:

Sale of goods

The adoption of AASB 15 has not impacted the timing of revenue recognition on the sale of goods, which continues to be recognised on a point in time basis.

In previous reporting periods, revenue from the sale of goods was recognised when the customer accepted the risks and rewards of ownership, which occurred at the point of sale or when the goods were collected/delivered. In applying AASB 15, revenue associated with the sale of goods is recognised when the performance obligation of the sale has been fulfilled and control of the goods has transferred to the customer, which continues to occur at the point of sale or when the goods are collected / delivered.

Rendering of services

The Group generates revenue from the provision of various services including design and installation of health technology solutions, information technology, audio visual and customer support services.

Under AASB 15, revenue relating to design, installation, IT, and AV services is principally recognised on a point in time basis, which occurs upon completion of the service given the short time period over which the services are provided. Revenue relating to longer term installation services and customer support services is recognised over the period that the services are provided where the Group retains the responsibility for the performance obligations associated with the services, and at point of agreement execution when a third party assumes the responsibility for the performance obligations associated with the services. Amounts collected for services not yet provided are recorded as deferred revenue in the balance sheet. The adoption of AASB 15 has not impacted the timing of revenue recognition for services revenue.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

3 Other income

	2019 \$'000	2018 \$'000
Net gain/(loss) on disposal of non-current assets	(12)	52
Other income	563	858
	551	910

Other income

Other income for the year ended 30 June 2019 includes \$0.15 million from chargeable repair income and income of \$0.12 million from payout from a customer contract.

4 Expenses

	2019 \$'000	2018 \$'000
(a) (Loss) / Profit before income tax includes the following specific expenses:		
Cost of Sales		
Cost of goods sold (inventories)	163,657	165,955
Direct cost of services provided	19,831	19,146
Total cost of sales	183,488	185,101
Depreciation		
Plant and equipment	4,350	5,018
Total depreciation	4,350	5,018
Amortisation		
Software	2,202	1,442
Development costs	65	59
Total amortisation	2,267	1,501
Total depreciation and amortisation	6,617	6,519

	2019 \$'000	2018 \$'000
Wages and salaries	41,811	40,203
Defined contribution superannuation expense	2,999	3,829
Other employee benefit expenses	1,975	2,910
Equity-settled share-based payment transactions	13	32
Total employee benefits expenses	46,798	46,974

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

4 Expenses (continued)

(a) Profit / (Loss) before income tax includes the following specific expenses (continued):

Finance expenses

Interest and finance charges paid/payable	(3,386)	(3,243)
Unwinding of discount on provisions	-	(41)

(3,386)	(3,284)
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Finance income

Interest income	121	121
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121	121
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Net finance costs expensed

(3,265)	(3,163)
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(b) Information on expenses

Accounting standards require that an analysis of expenses is presented using a classification based on either their nature or their function. The Group presents expenses classified by nature in order to provide information that is relevant and consistent with how management monitors business performance.

Further information on expenses as shown in the Consolidated statement of profit and loss is provided below:

Cost of goods sold (inventories)	Cost of goods sold include expenses relating to the change in inventories of finished goods and work in progress, and raw materials used.
Direct costs of services provided	Direct costs of services provided include subcontractor costs, commissions and subscriptions payable, and other direct costs associated with provision of services by Group entities. This balance does not include internal labour costs related to carrying out services, which are included in Labour and related expenses.
Labour and related expenses	Labour and related expenses include employee benefits expenses of \$46.798 million (as shown in note 4a above) and other labour and related expenses such as third-party logistics, labour hire, employee training and recruitment.
Operational and equipment expenses	Operational and equipment expenses include costs of freight, consumables, motor vehicle and other equipment expenses, repairs and maintenance.
Property expenses	Property expenses include rent, rates, utilities, cleaning and security expenses related to properties leased by the Group.
Other expenses	Other expenses include overhead expenses (such as insurance, advertising and marketing, professional and consulting fees, telecommunications and information technology related expenses) and other net costs not considered part of segment EBITDA (as shown in note 1b).

Recognition and measurement

Depreciation and amortisation

Refer to notes 11 and 12 for recognition and measurement of depreciation and amortisation.

Employee benefits expense

Refer to note 13 for information relating to employee benefits expense.

Finance income and expense

Finance income comprises interest income on funds invested. Interest income is recognised in profit or loss as it accrues. Finance expenses comprise interest expense on borrowings and unwinding of the discount on provisions. Borrowing costs are recognised in profit or loss using the effective interest method.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

5 Income tax

	2019 \$'000	2018 \$'000
(a) Income tax benefit		
Current tax	-	-
Deferred tax	(5,588)	(319)
	(5,588)	(319)
(b) Numerical reconciliation of income tax (benefit) / expense to prima facie tax payable		
Profit / (Loss) from continuing operations before income tax expense	(14,414)	40
Tax at the Australian tax rate of 30% (2018: 30%)	(4,324)	12
Tax effect of amounts which are not deductible / (taxable) in calculating taxable income:		
Non-deductible expenses	181	54
Acquisition costs	1	(22)
Recognition of deferred tax assets	(1,739)	(3,429)
Tax losses for which no deferred tax asset is recognised	292	3,305
Tax effect of prior year adjustments	-	(231)
	(5,589)	(311)
Difference in overseas tax rates	1	(8)
Total income tax benefit	(5,588)	(319)
(c) Income tax expense relating to items of other comprehensive income		
	2019 \$'000	2018 \$'000
Aggregate current and deferred tax arising in the reporting period and not recognised in net profit or loss but directly debited or credited to other comprehensive income:		
Income / (Losses) on cash flow hedges	-	95
Aggregate income tax benefit	-	95

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

5 Income tax (continued)

(d) Tax losses

At the end of the reporting period, the Group had unused tax losses in respect of revenue items of \$207.7 million (2018: \$205.7 million) and capital items of \$31.0 million (2018: \$31.0 million).

	Revenue items		Capital items	
	2019 \$'000	2018 \$'000	2019 \$'000	2018 \$'000
Unused losses for which no deferred tax asset has been recognised	207,667	205,744	31,012	31,012
Potential tax benefit	62,286	61,715	9,304	9,304

Revenue and capital tax losses do not expire under current legislation and can be used to offset future taxable income but must satisfy the requirements of the relevant tax legislation relating to continuity of ownership, and same or similar business tests.

Revenue losses Deferred tax assets have not been recognised in respect of revenue tax losses because the period over which the Group expects to utilise the benefits of these items extends beyond 3 years (the time horizon during which their recovery is considered probable).

Capital losses Deferred tax assets have not been recognised in respect of capital losses because it is not probable that future capital gains will be available against which the Group can utilise the benefits from these items.

(e) Current tax assets and liabilities

There were no current tax assets for the Group at 30 June 2019 (2018: nil).

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

5 Income tax (continued)

(f) Deferred tax

	Balance at 1 July	Recognised in profit or loss	Recognised in other comprehensive income	Balance at 30 June
	\$'000	\$'000	\$'000	\$'000
Movements 2018				
Property, plant and equipment	450	2,503	-	2,953
Inventories	5,614	(846)	-	4,768
Employee benefits	2,054	(389)	-	1,665
Receivables	178	(58)	-	120
Provisions	2,039	(776)	-	1,263
Other accruals	515	(134)	-	381
Derivative financial instruments	67	-	(95)	(28)
Exchange differences	-	19	(19)	-
	10,917	319	(114)	11,122
Movements 2019				
Property, plant and equipment	2,953	2,739	-	5,692
Inventories	4,768	1,324	-	6,092
Employee benefits	1,665	-	-	1,665
Receivables	120	26	-	146
Provisions	1,263	1,163	-	2,426
Other accruals	381	(67)	-	314
Derivative financial instruments	(28)	60	-	32
Other	-	343	23	366
	11,122	5,588	23	16,733

(g) Tax consolidation legislation

The Company and its wholly owned Australian controlled entities have implemented the tax consolidation legislation.

Tax sharing agreement	On adoption of the tax consolidation legislation, the entities in the tax consolidated group entered into a tax sharing agreement that, in the opinion of the Directors, limits the joint and several liability of the wholly owned entities in the case of a default by the head entity, Hills Limited.
Tax funding agreement	The entities have also entered into a tax funding agreement under which the wholly owned entities fully compensate the Company for any current tax payable assumed and are compensated by the Company for any current tax receivable and deferred tax assets relating to unused tax losses or unused tax credits that are transferred to the Company under the tax consolidation legislation. The funding amounts are determined by reference to the amounts recognised in the wholly owned entities' financial statements.
	The amounts receivable / payable under the tax funding agreement are due upon receipt of the funding advice from the head entity, which is issued as soon as practicable after the end of each reporting period. The head entity may also require payment of interim funding amounts to assist with its obligations to pay tax instalments. The funding amounts are recognised as current intercompany receivables or payables and eliminated on consolidation.
	Assets or liabilities arising under tax funding agreements with the tax consolidated entities are recognised as amounts receivable from or payable to other entities in the Group.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

5 Income tax (continued)

Recognition and measurement

Income tax

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

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Company's subsidiaries operate and generate taxable income.

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

Deferred tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements.

Deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill. Deferred income tax is also not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised, or the deferred income tax liability is settled.

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

Deferred tax liabilities and assets are not recognised for temporary differences between the carrying amount and tax bases of investments in foreign operations where the Company is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Offsetting

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

Tax consolidation

The head entity, Hills Limited, and the controlled entities in the tax consolidated group account for their own current and deferred tax amounts arising from temporary differences. These tax amounts are measured as if each entity in the tax consolidated group continues to be a standalone taxpayer in its own right.

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

Key estimate: unrecognised deferred tax assets

Deferred tax assets are only recognised for deductible temporary differences and tax losses to the extent that it is probable that taxable profits will be available to utilise them. The financial projections used in assessing the probability of taxable profits are inherently subject to management judgement.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

6 Profit/(loss) per share

	2019 Cents	2018 Cents
(a) Basic and diluted Profit/(loss) per share		
From Profit/(loss) attributable to the ordinary equity holders of the Company	(3.8)	0.2
	2019 \$'000	2018 \$'000
(b) Reconciliation of earnings used in calculating Profit/(loss) per share		
Profit/(loss) attributable to the ordinary equity holders of the Company used in calculating basic Profit/(loss) per share	(8,826)	359
	2019 Shares '000	2018 Shares '000
(c) Weighted average number of shares used as denominator		
Weighted average number of ordinary shares used as the denominator in calculating basic Profit/(loss) per share	231,986	231,986
Weighted average number of ordinary and potential ordinary shares used as the denominator in calculating diluted Profit/(loss) per share	231,986	231,986

Performance rights have not been included in the weighted average number of shares for diluted Profit/(loss) per share as no shares are expected to be issued to satisfy performance rights.

Recognition and measurement

Earnings per share

Basic earnings per share	<p>Basic earnings per share is calculated by dividing:</p> <ul style="list-style-type: none"> ▪ the profit attributable to owners of the Company, excluding any costs of servicing equity other than ordinary shares ▪ by the weighted average number of ordinary shares outstanding during the reporting period.
Diluted earnings per share	<p>Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:</p> <ul style="list-style-type: none"> ▪ the after-income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and ▪ the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

Section C: Operating assets and liabilities

This section provides information on the operating assets used and the operating liabilities incurred by the Group:

7	Cash and cash equivalents
8	Trade and other receivables
9	Inventories
10	Trade and other payables
11	Property, plant and equipment
12	Intangible assets
13	Provisions

7 Cash and cash equivalents

	2019 \$'000	2018 \$'000
Cash at bank and in hand	6,427	10,704
Deposits	4,440	5,079
	10,867	15,783

(a) Reconciliation of profit/(loss) after income tax to net cash flow from operating activities

Profit/(loss) for the period	(8,826)	359
Depreciation and amortisation	6,617	6,519
Net loss / (gain) on sale of non-current assets	12	(52)
Impairment of property, plant and equipment/intangibles	6,500	-
Impairment of inventories	3,800	-
Non-cash employee benefits expense / (credit) - share-based payments	13	32
Fair value adjustment to derivatives	-	(59)
Amortisation of capitalised borrowing costs	489	552
Other non-cash items	3,900	-
<i>Change in operating assets and liabilities:</i>		
(Increase)/Decrease in trade and other receivables	(392)	(257)
(Increase)/Decrease in inventories	(1,720)	2,300
Increase/(Decrease) in trade and other payables	(8,163)	7,571
(Increase)/Decrease in provisions	(633)	(4,888)
Increase/(Decrease) in provision for income taxes receivable	-	220
(Increase)/Decrease in deferred tax assets	(5,601)	(320)
Net cash flows from operating activities	(4,004)	11,977

Recognition and measurement

Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held at call with financial institutions, other short term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and that are subject to an insignificant risk of changes in value.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

8 Trade and other receivables

	2019			2018		
	Current \$'000	Non-current \$'000	Total \$'000	Current \$'000	Non-current \$'000	Total \$'000
Trade receivables	50,682	-	50,682	51,483	-	51,483
Provision for impairment of receivables (a)	(487)	-	(487)	(402)	-	(402)
	50,195	-	50,195	51,081	-	51,081
Other receivables	7,092	-	7,092	5,819	-	5,819
Prepayments	1,907	-	1,907	2,751	-	2,751
	59,194	-	59,194	59,651	-	59,651

	2019 \$'000	2018 \$'000
(a) Impaired trade receivables		

The ageing of the Group's trade receivables at the reporting date is as follows:

Not past due	31,136	33,476
Past due 0 – 30 days	8,067	12,851
Past due 31 – 90 days	8,016	3,115
Past due more than 90 days	3,463	2,041
	50,682	51,483

The following table sets out the movement in lifetime expected credit losses (ECL) that has been recognised for trade receivables in accordance with the simplified approach adopted under AASB 9:

At 1 July	402	594
Adjustments on adoption of AASB 9	200	-
Provision for impairment recognised / (released) during the period	(27)	(108)
Receivables written off during the period as uncollectable	(88)	(84)
At 30 June	487	402

Based on ECL provision calculation and management judgement, the Group believes that no impairment allowance is necessary in respect of trade receivables not yet past due.

The provision for impaired receivables for the Group of \$0.487 million (2018: \$0.402 million) relates to receivables past due more than 30 days, on a case by case assessment. Receivables past due between 0 and 30 days are not considered impaired.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

8 Trade and other receivables (continued)

(b) Transfer of trade receivables

The Group has entered into a Receivables Purchase Facility, as described in note 17, under which trade receivables have been sold with recourse. These receivables have not been derecognised from the statement of financial position as the Group retains substantially all of the risks and rewards (primarily credit risk).

The carrying amount of transferred trade receivables not derecognised is show below:

	2019 \$'000	2018 \$'000
Carrying amount of trade receivables transferred	36,708	35,016
Carrying amount of associated liabilities	<u>(32,303)</u>	(31,091)

(c) Financial risk

See note 19 for information about the Group's exposure to foreign currency risk, interest rate risk and credit risk in relation to trade and other receivables.

The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivables mentioned above. The fair value of securities held for certain trade receivables is insignificant as is the fair value of any collateral sold or re-pledged.

Recognition and measurement

Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Trade receivables are generally due for settlement within 30 to 90 days. They are presented as current assets unless collection is not expected for more than 12 months after the reporting date.

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. Cash flows relating to short term receivables are not discounted if the effect of discounting is immaterial.

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

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

9 Inventories

	2019 \$'000	2018 \$'000
Raw materials and work in progress	3,060	2,674
Finished goods	38,576	41,369
	41,636	44,043

Inventories stated above are net of provisions for net realisable value of \$8.26 million (2018: \$4.37 million)

Recognition and measurement

Inventories

Raw materials, work in progress and finished goods are stated at the lower of cost and net realisable value.

Cost comprises direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity. Cost includes the reclassification from equity of any gains/losses on qualifying cash flow hedges relating to purchases of inventory.

Costs are assigned to individual items of inventory on the basis of weighted average costs. Costs of purchased inventory are determined after deducting rebates and discounts. Net realisable value is the estimated selling price less the estimated costs of completion and the estimated costs necessary to make the sale.

The fair value of inventories acquired in a business combination is determined based on its estimated selling price in the ordinary course of business less the estimated costs of completion and sale, and a reasonable profit margin based on the effort required to complete and sell the inventories.

10 Trade and other payables

	2019 \$'000	2018 \$'000
Trade payables	29,095	33,521
Other payables and accrued expenses	11,551	14,210
	40,646	47,731

Other payables and accrued expenses include amounts payable in respect of employee benefits (including wages and salaries, superannuation / pension contributions, commissions and bonuses, payroll tax), Goods and Services Tax (GST), customer rebates and other sundry accrued expenses.

Recognition and measurement

Trade and other payables

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost.

They represent liabilities for goods and services provided to the Group prior to the end of the reporting period that are unpaid. The amounts are unsecured and are paid in accordance with the Group's terms of trade.

Trade and other payables are presented as current liabilities unless payment is not due within twelve months after the reporting period.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

11 Property, plant and equipment

	Plant & equipment \$'000
Year ended 30 June 2018	
Opening net book amount	16,600
Exchange differences	(24)
Additions	3,489
Disposals	(297)
Depreciation charge	(5,018)
Impairment reversal	165
Closing net book amount	<u>14,915</u>
At 30 June 2018	
Cost	60,611
Accumulated depreciation and impairment	<u>(45,696)</u>
Net book amount	<u>14,915</u>
Year ended 30 June 2019	
Opening net book amount	14,915
Exchange differences	63
Additions	5,193
Disposals	(36)
Depreciation charge	(4,350)
Impairment	(504)
Closing net book amount	<u>15,281</u>
At 30 June 2019	
Cost	65,796
Accumulated depreciation and impairment	<u>(50,515)</u>
Net book amount	<u>15,281</u>

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

11 Property, plant and equipment (continued)

There were no additions (2018: \$0.30 million) for the estimated costs to remove leasehold improvements from properties leased by the Group and restore the premises on which they are located.

Additions include an amount of \$1.58 million (2018: \$1.95 million) for equipment installed at hospitals to generate service rental income which have been funded by finance leases (See note 17(a) for further details of these loans.) and \$1.0 million (2018: nil) of amounts transferred from inventory balances during the year.

Payments for property, plant and equipment of \$2.65 million (2018: \$1.23 million) as shown in the Consolidated statement of cash flows do not include either of these non-cash additions and in FY19.

During the year ended 30 June 2019 the Group impaired \$0.5m of property, plant and equipment using a value in use model as outlined in note 12.

During the year no fully depreciated assets were written off (2018: \$2.39 million).

(a) Assets in the course of construction

The carrying amounts of the assets disclosed above and in note 12 Intangible assets include the following expenditure recognised in relation to non-current assets which are in the course of construction:

	2019 \$'000	2018 \$'000
Plant and equipment, leasehold improvements and software development	2,065	5,986

Key estimate: useful lives of property, plant and equipment

The assessment of the useful lives of property, plant and equipment requires management judgement based on past experience and industry practice. Management reassess the useful lives when there are indications of a change in economic circumstances that may impact the assets.

Recognition and measurement

Property, plant and equipment

Plant and equipment

Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

Depreciation

Depreciation is calculated using the straight-line method as considered appropriate to allocate their cost or revalued amounts, net of their residual values, over their estimated useful lives, as follows (current and comparative periods):

Buildings	2.5%	Plant and equipment, including leasehold improvements	5.0% to 66.7%
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Impairment

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in profit or loss. When revalued assets are sold, it is Group policy to transfer any amounts included in other reserves in respect of those assets to the profits reserve.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

12 Intangible assets

	Software ¹ \$'000	Development costs ² \$'000	Total \$'000
Year ended 30 June 2018			
Opening net book amount	2,358	220	2,578
Additions	4,379	814	5,193
Disposals	28	(28)	-
Amortisation charge	(1,445)	(59)	(1,504)
Closing net book amount	5,320	947	6,267

At 30 June 2018			
Cost	20,531	2,681	23,217
Accumulated amortisation and impairment	(15,211)	(1,734)	(16,950)
Net book amount	5,320	947	6,267

Year ended 30 June 2019			
Opening net book amount	5,320	947	6,267
Additions	3,097	971	4,068
Amortisation charge	(2,202)	(65)	(2,267)
Impairment charge	(5,996)	-	(5,996)
Closing net book amount	219	1,853	2,072

At 30 June 2019			
Cost	23,644	3,673	27,317
Accumulated amortisation and impairment	(23,425)	(1,820)	(25,245)
Net book amount	219	1,853	2,072

There were no additions for the year incurred but not yet paid at the end of the period (2018: nil).

During the year ended 30 June 2019, no fully amortised or impaired intangible assets were written off (2018: \$1.1 million).

During the year ended 30 June 2019 the Group impaired \$5.996m of intangible assets. A value in use model was used to discount the Groups future cash flows by cash generating unit and based on the output of this model management made the decision to impair intangibles relating to ecommerce assets. This decision impaired the assets value to nil. Per AASB 136 *Impairment of Assets* its recoverable value was determined based on its value in use. The discount rate applied in the model was 10.2%. This asset was within the Distribution segment.

¹ Software includes capitalised development costs, being an internally generated intangible asset.

² Development costs includes capitalised development costs, being an internally generated intangible asset.

12 Intangible assets (continued)

Recognition and measurement

IT development and software

Costs incurred in developing products or systems and costs incurred in acquiring software and licenses that will contribute to future period financial benefits through revenue generation and/or cost reduction are capitalised to software and systems. Costs capitalised include external direct costs of materials and service and direct payroll and payroll related costs of employees' time spent on the project. Amortisation is calculated on a straight-line basis over periods generally ranging from 3 to 5 years.

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

Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will, after considering its commercial and technical feasibility, be completed and generate future economic benefits and its costs can be measured reliably. The expenditure capitalised comprises all directly attributable costs, including costs of materials, services, direct labour and an appropriate proportion of overheads. Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use on a straight-line basis over its useful life, which is estimated to be 5 to 20 years.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

13 Provisions

	2019			2018		
	Current \$'000	Non-current \$'000	Total \$'000	Current \$'000	Non-current \$'000	Total \$'000
Employee benefits	4,657	604	5,261	5,087	475	5,562
Outstanding claims	573	351	924	545	660	1,205
Restructuring costs	1,672	284	1,956	118	668	786
Other provisions	1,829	3,448	5,277	456	2,132	2,588
	8,731	4,687	13,418	6,206	3,935	10,141

(a) Description of provisions

Employee benefits	Provisions for employee benefits include liabilities for annual leave and long service leave.
Outstanding claims	The provision for claims comprises the amounts set aside for estimated warranty claims. In the prior year, it also included the estimated future liability of the Group's self-insurance arrangements.
Restructuring costs	The restructuring costs provision comprises redundancy costs and other costs of closing and restructuring businesses (including onerous lease and make-good costs related to properties affected by restructure). This amount includes a \$1.4m redundancy provision.
Other provisions	Other provisions comprise provisions for environmental monitoring of a site, make good obligations, onerous lease costs and other provisions as required. In FY19 an onerous lease provision of \$2.5m was recorded following changes to the use of leased properties with the Group.

(b) Movements in provisions

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

	Outstanding claims \$'000	Restructuring costs \$'000	Other \$'000	Total \$'000
Movements 2019				
Carrying amount at the start of the year	1,205	786	2,588	4,579
Additional provisions made during the period	245	1,885	3,247	5,377
Amounts used (incurred or charged against provision)	(83)	(320)	(290)	(693)
Unused amounts reversed during the period	(443)	(395)	(268)	(1,106)
Carrying amount at the end of the year	924	1,956	5,277	8,157

13 Provisions (continued)

Recognition and measurement

Provisions

Provisions for legal claims, service warranties, make good obligations and onerous leases are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Warranty provisions are recognised when the underlying products or services are sold. Restructuring provisions are recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or been announced publicly. Provisions are not recognised for future operating losses.

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

Employee benefits

Short-term obligations

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months after the end of the period in which the employees render the related service are recognised in respect of employees' services up to the end of the reporting period and are measured at the amounts expected to be paid when the liabilities are settled. The liability for annual leave is recognised in the provision for employee benefits. All other short-term employee benefit obligations are presented as payables.

Other long-term employee benefits obligations

The liability for long service leave and annual leave which is not expected to be settled within 12 months after the end of the period in which the employees render the related service is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the end of the reporting period. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service.

Expected future payments are discounted using market yields at the end of the reporting period on corporate bonds rates with terms to maturity and currency that match, as closely as possible, the estimated future cash outflows.

The obligations are presented as current liabilities in the consolidated statement of financial position if the Group does not have an unconditional right to defer settlement for at least twelve months after the reporting date, regardless of when settlement is expected to occur.

Retirement benefit obligations

A defined contribution plan is a post-employment benefit plan which receives fixed contributions from Group Entities and the Group's legal or constructive obligation is limited to these contributions.

Contributions to defined contribution plans are recognised as an expense as they become payable.

Profit-sharing and bonus plans

A liability is recognised for the amount expected to be paid under short term cash bonus or profit sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably, or where there is past practice that has created a constructive obligation.

Section D: Capital and financing

This section provides information on how the Group manages its capital structure and financing, including its exposure to financial risk:

- 14 Contributed equity
- 15 Reserves
- 16 Dividends
- 17 Borrowings
- 18 Derivative financial instruments
- 19 Capital and financial risk management
- 20 Fair value measurements

14 Contributed equity

(a) Share capital

	2019 Shares	2018 Shares	2019 \$'000	2018 \$'000
Ordinary shares - fully paid	231,985,526	231,985,526	278,439	278,439

(b) About share capital

Ordinary shares	<p>Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. Ordinary shares have no par value. The Company does not have a limited amount of ordinary share capital.</p>
Performance rights	<p>Information relating to the Incentive Share Plan, including details of performance rights issued, exercised, lapsed and forfeited during the reporting period and performance rights outstanding at the end of the reporting period, is set out in note 28.</p>

Recognition and measurement

Contributed equity

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

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

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

15 Reserves

	2019 \$'000	2018 \$'000
Hedging reserve - cash flow hedges	(133)	65
Equity compensation reserve	751	738
Foreign currency translation reserve	377	117
Profits reserve	10,133	10,133
	11,128	11,053

(a) Movements in reserves

Hedging reserve – cash flow hedges

Opening balance 1 July	65	(158)
Revaluation - gross	(198)	318
Deferred tax	-	(95)
Closing balance 30 June	(133)	65

Equity compensation reserve

Opening balance 1 July	738	706
Employee share plan expense / (credit)	13	32
Closing balance 30 June	751	738

Foreign currency translation reserve

Opening balance 1 July	117	354
Currency translation differences arising during the year	260	(237)
Closing balance 30 June	377	117

Profits reserve

Opening balance 1 July	10,133	10,133
Closing balance 30 June	10,133	10,133

(b) Nature and purpose of reserves

Hedging reserve – cash flow hedges	The hedging reserve is used to record changes in the fair value of derivative financial instruments designated in a cash flow hedge relationship that are recognised in other comprehensive income. Amounts are reclassified to profit or loss when the associated hedged transaction affects profit or loss.
Equity compensation reserve	The equity compensation reserve represents the value of performance rights held by an equity compensation plan of the Group. This reserve will be reversed against share capital when the underlying performance rights are exercised and shares vest in the employee. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of the Group's own equity instruments.
Foreign currency translation reserve	Exchange differences arising on translation of the financial statements of a foreign controlled entity are recognised in other comprehensive income and accumulated in this reserve. The cumulative amount is reclassified to profit or loss when the net investment is disposed of.
Profits reserve	Current period and realised profits are transferred from retained earnings and other reserves to the profits reserve and dividends are paid out of the profits reserve.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

16 Dividends

(a) Ordinary shares

Year ended 30 June 2018	No dividends were paid during the year and no final dividend has been declared.
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Year ended 30 June 2019	No dividends were paid during the year and no final dividend has been declared.
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(b) Franked dividends

	2019 \$'000	2018 \$'000
Franking credits available for subsequent reporting periods based on a tax rate of 30% (2018: 30.0%)	1,787	1,787

The above amounts represent the balance of the franking account as at the end of the reporting period, adjusted for franking credits that will arise from:

- the payment of the amount of the provision for income tax;
- the payment of dividends recognised as a liability at the reporting date; and
- the receipt of dividends recognised as receivables at the reporting date.

The consolidated amounts include franking credits that would be available to the Company if distributable profits of subsidiaries were paid as dividends.

Recognition and measurement

Dividends

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

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

17 Borrowings

	2019			2018		
	Current \$'000	Non-current \$'000	Total \$'000	Current \$'000	Non-current \$'000	Total \$'000
Loans	15,927	24,245	40,172	6,357	27,743	34,100
Transaction costs	-	(914)	(914)	-	(1,404)	(1,404)
Total borrowings	15,927	23,331	39,258	6,357	26,339	32,696

Non-current borrowings include transactions costs directly attributable to the issue of the borrowings. At 30 June 2019, unamortised borrowing costs totalled \$0.914 million (2018: \$1.404 million).

Current borrowings include an estimate of the expected to be repaid for the Loans outlined below based on expected cashflows over the next 12 months.

Under the terms of the Receivables Purchase Facility, as noted below amounts repaid can be drawn down again depending on the level of the Accounts Receivables balance and amount already drawn down under the facility up to the facility limit.

(a) Loans

The Group has its financing facilities with Commonwealth Bank of Australia (CBA) through a Bilateral Facility and Recfin Nominees Pty Ltd through a Receivables Purchase Facility.

Bilateral Facility	<p>The CBA facility was amended in May 2019 and now comprises a facility for contingent liabilities (bank guarantees / letter of credit), with the following limits (denominated in AUD):</p> <ul style="list-style-type: none"> Contingent liabilities: \$2.600 million. <p>Interest is charged at prevailing market rates plus a fixed margin.</p>
Receivables Purchase Facility	<p>The Recfin Nominees Pty Ltd facility totals \$36 million (denominated in AUD), with funding provided based upon the Group's accounts receivable book. The facility expires on 13 May 2021.</p> <p>The facility is secured on the Group's Accounts Receivable book, with a second mortgage over the other assets of the Group.</p> <p>Interest is charged at prevailing market rates plus a fixed margin.</p>
DLL Financing	<p>In December 2017, the Group entered into a Progressive Payment Agreement (PPA) with DLL for the provision of finance for equipment purchases in the Hills Health Solutions business. At 30 June 2019, the Group had drawn down \$3.374 million (2018: \$1.95m).</p> <p>The PPA is an unsecured, interest only facility, which will be replaced by a set term Chattel Mortgage once the equipment is installed.</p>

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

17 Borrowings (continued)

(b) Reconciliation of movements of liabilities to cashflows arising from financing activities

	Total \$'000
Balance at 30 June 2017	28,690
Changes from financing cash flows	
Proceeds from loans and borrowings	3,461
Repayment of borrowings	(1,961)
Total changes from financing cash flows	<u>1,500</u>
Other changes	
Amortisation of capitalised borrowing costs	554
New finance leases	1,952
Total other changes	<u>2,506</u>
Balance at 30 June 2018	32,696
Balance at 30 June 2018	32,696
Changes from financing cash flows	
Proceeds from loans and borrowings	7,650
Repayment of borrowings	(3,000)
Total changes from financing cash flows	<u>4,650</u>
Other changes	
Amortisation of capitalised borrowing costs	489
New finance leases	1,423
Total other changes	<u>1,912</u>
Balance at 30 June 2019	39,258

The Company and its wholly owned subsidiaries have provided an interlocking guarantee and indemnity to its financiers for these facilities. An assessment of the contractual maturities of financial liabilities is provided in note 19, together with details of undrawn borrowing facilities at the period end.

Recognition and measurement

Borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in profit or loss over the period of the borrowings using the effective interest method. Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. Fees paid on the establishment of loan facilities are capitalised as a prepayment and amortised over the period of the facility to which it relates.

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

Borrowing costs

Borrowing costs incurred for the construction of any qualifying asset are capitalised during the period of time that is required to complete and prepare the asset for its intended use or sale. Other borrowing costs are expensed.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

18 Derivative financial instruments

The Group is party to derivative financial instruments in the normal course of business in order to hedge exposure to fluctuations in interest and foreign exchange rates in accordance with the Group's financial risk management policies (refer to note 19).

	2019 \$'000	2018 \$'000
Current assets		
Forward foreign exchange contracts - cash flow hedges	-	93
Total current derivative financial instrument assets	-	93
Current liabilities		
Forward foreign exchange contracts - cash flow hedges	(106)	-
Total current derivative financial instrument liabilities	(106)	-
Net derivative financial instrument assets / (liabilities)	(106)	93

(a) Instruments used by the Group

Forward exchange contracts: cash flow hedges

The Group purchases goods and materials from overseas, principally in US dollars. In order to protect against exchange rate movements, the Group has entered into forward exchange contracts to purchase US dollars. These contracts are hedging highly probable forecasted purchases for approximately the following two to three months.

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in other comprehensive income. When the cash flows occur, the Group adjusts the initial measurement of the component recognised in the consolidated statement of financial position by removing the related amount from other comprehensive income.

During the year ended 30 June 2019, no gain or loss was recognised in profit or loss for the ineffective portion of these hedging contracts (2018: nil).

Forward exchange contracts: held-for-trading

Group Entities have entered into forward foreign exchange contracts that are economic hedges but do not satisfy the requirements for hedge accounting. These contracts are subject to the same risk management policies as all other derivative contracts, see note 19 for details. However, they are accounted for as held for trading.

Recognition and measurement

Derivatives and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges).

The Group documents at the inception of the hedging transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions.

The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions have been and will continue to be highly effective in offsetting changes in fair values or cash flows of hedged items.

The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months; it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as a current asset or liability.

The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then

18 Derivative financial instruments (continued)

(a) Instruments used by the Group (continued)

fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds). The fair value of interest rate swaps is determined by discounting estimated future cash flows based on the terms and maturity of each contract and using market rates at the measurement date.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and within the hedging reserve in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

Amounts accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss. The gain or loss relating to the effective portion of interest rate swaps hedging variable rate borrowings is recognised in profit or loss within 'finance income' or 'finance costs'. The gain or loss relating to the effective portion of forward foreign exchange contracts hedging export sales is recognised in profit or loss within 'sales'. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory or plant and equipment) the gains and losses previously deferred in equity are reclassified from equity and included in the initial measurement of the cost of the asset. The deferred amounts are ultimately recognised in profit or loss as cost of goods sold in the case of inventory, or as depreciation or impairment in the case of plant and equipment.

When a hedging instrument expires or is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately reclassified to profit or loss.

Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

19 Capital and financial risk management

(a) Capital risk management

The Group's objective when managing capital is to safeguard its ability to continue as a going concern to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

To maintain or adjust the capital structure, the Group may vary the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors capital by assessing its gearing ratio. The gearing ratio is calculated as:

$\frac{\text{net debt}}{\text{net debt} + \text{total equity}}$	Net debt	Total borrowings as shown in the consolidated statement of financial position less cash and cash equivalents
	Total equity	Equity as shown in the consolidated statement of financial position (including non-controlling interests)

The Group continues to maintain a strategy of a target gearing ratio (calculated as net debt divided by net debt plus equity) of less than 40%. The gearing ratios at 30 June 2019 and 30 June 2018 were as follows:

	Notes	2019 \$'000	2018 \$'000
Total borrowings	17	39,258	32,696
Less: cash and cash equivalents	7	(10,867)	(15,783)
Net debt		28,391	16,913
Total equity		52,357	61,308
Gearing ratio		35.2%	21.6%

(b) Financial risk management

Management manages the Group's exposure to financial risks under policies approved by the Board. Management identifies, evaluates and manages financial risks in close cooperation with the Group's business units. The Board provides written principles for overall risk management, as well as policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of financial instruments and investment of excess liquidity.

The risk management approach focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Group.

The Group uses derivative financial instruments such as foreign exchange contracts exclusively for risk mitigation and not as trading or other speculative instruments.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

19 Capital and financial risk management (continued)

(b) Financial risk management (continued)

The Group holds the following financial instruments:

	2019 \$'000	2018 \$'000
Financial assets		
Cash and cash equivalents	10,867	15,783
Trade and other receivables	59,194	59,651
Derivative financial instruments	-	93
Investments	2	-
	70,063	75,527
Financial liabilities		
Trade and other payables	40,646	47,731
Borrowings	39,258	32,696
Derivative financial instruments	106	-
	80,010	80,427

The Group uses different methods to measure different types of risk, including sensitivity analysis (for interest rate, foreign exchange and other price risks) and aging analysis (for credit risk).

(i) Market risk

Price risk	The Group has no material financial exposure to other market price risk as it is not exposed to equity securities price risk. The Group does not enter into commodity contracts other than to meet the Group's expected usage requirements.
Foreign exchange risk	<p>Foreign exchange risk arises when future commercial transactions and recognised financial assets and financial liabilities are denominated in currencies other than the Group's functional currency. The risk is measured using sensitivity analysis and cash flow forecasting.</p> <p>The Group's main foreign exchange risk exposure is to US dollars.</p> <p>Group Entities and business units are required to hedge their foreign exchange risk exposure using forward exchange contracts.</p> <p>The Group's policy is to hedge approximately three months of anticipated cash flows (mainly purchases of inventories) in US dollars.</p>
Cash flow and fair value interest rate risk	Borrowings issued at variable rates expose the Group to cash flow interest rate risk. See details of the Group's borrowings in note 17.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

19 Capital and financial risk management (continued)

(b) Financial risk management (continued)

(i) Market risk (continued)

Foreign exchange risk

The Group's exposure to foreign exchange risk at the reporting date, expressed in Australian dollars at the closing exchange rates, was:

	USD \$'000	EUR \$'000	GBP \$'000	Total \$'000
30 June 2018				
Cash at bank	-	-	-	-
Trade receivables	413	-	-	413
Trade payables	(10,028)	(280)	(12)	(10,320)
Forward exchange contracts				
• buy foreign currency (cash flow hedges)	6,366	-	-	6,366
• buy foreign currency (FVTPL1)	543	-	-	543
30 June 2019				
Cash at bank	33	-	-	33
Trade receivables	663	-	-	663
Trade payables	(11,424)	(314)	(36)	(11,774)
Forward exchange contracts:				
• buy foreign currency (cash flow hedges)	9,421	-	-	9,421

Cash flow interest rate risk

The Group's financing arrangement is principally a Receivables Purchase Facility, where the balance outstanding changes daily. Accordingly, the Group does not use interest rate swaps to hedge cash flow interest rate risk.

During 2019 and 2018, the Group's cash and borrowings at variable rate were denominated in Australian Dollars and NZ Dollars.

As at the end of the reporting period, the Group had the following variable rate cash and borrowings outstanding:

	2019		2018	
	Weighted average interest rate %	Balance \$'000	Weighted average interest rate %	Balance \$'000
Bank overdrafts and loans	5.82%	(38,446)	5.86%	(31,639)
Cash and cash equivalents	1.32%	10,867	1.43%	15,783
Other loans	3.06%	(812)	4.91%	(1,057)

¹ Fair Value Through Profit and Loss.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

19 Capital and financial risk management (continued)

(b) Financial risk management (continued)

(i) Market risk (continued)

An analysis by maturities is provided in section (iii) below.

Sensitivity analysis

Foreign exchange rates	The sensitivity of profit or loss to changes in exchange rates arises mainly from US dollar denominated financial instruments and the impact on other components of equity arises from forward exchange contracts designated as cash flow hedges.
Interest rates	Profit or loss is sensitive to higher / lower interest income and interest expense from cash and cash equivalents and borrowings respectively, as a result of changes in interest rates. Other components of equity change as a result of an increase / decrease in the fair value of the cash flow hedges of borrowings.

The following table summarises the sensitivity of the Group's financial assets and financial liabilities to interest rate risk and foreign exchange risk.

	Carrying amount \$'000	Interest rate risk				Foreign exchange risk			
		-100 bps		+100 bps		-10%		+10%	
		Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000
30 June 2018									
Financial assets									
Cash and cash equivalents	15,783	(162)	-	225	-	-	-	-	-
Trade and other receivables	59,651	-	-	-	-	46	-	(38)	-
Derivatives - cash flow hedges	272	-	-	-	-	45	-	(62)	-
Total increase / (decrease) in financial assets		(162)	-	225	-	91	-	(100)	-
Financial liabilities									
Trade & other payables	(47,731)	-	-	-	-	(1,169)	-	956	-
Borrowings	(32,696)	341	-	(341)	-	-	-	-	-
Derivatives - cash flow hedges	(179)	-	-	-	-	-	849	-	(463)
Total increase / (decrease) in financial liabilities		341	-	(341)	-	(1,169)	849	956	(463)
Total increase / (decrease)		179	-	(116)	-	(1,078)	849	856	(463)

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

19 Capital and financial risk management (continued)

(b) Financial risk management (continued)

	Carrying amount \$'000	Interest rate risk				Foreign exchange risk			
		-100 bps		+100 bps		-10%		+10%	
		Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000	Profit \$'000	Other equity \$'000
30 June 2019									
Financial assets									
Cash and cash equivalents	10,867	(103)	-	148	-	4	-	(3)	-
Trade and other receivables	59,194	-	-	-	-	74	-	(60)	-
Total increase / (decrease) in financial assets		(103)	-	148	-	78	-	(63)	-
Financial liabilities									
Trade & other payables	(40,646)	-	-	-	-	(1,317)	-	1,078	-
Borrowings	(39,258)	275	-	(275)	-	-	-	-	-
Derivatives - cash flow hedges	(106)	-	-	-	-	-	1,135	-	(784)
Total increase / (decrease) in financial liabilities		275	-	(275)	-	(1,317)	1,135	1,015	(784)
Total increase / (decrease)		172	-	(127)	-	(1,239)	1,135	1,015	(784)

(ii) Credit risk

Nature of the risk	Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's customers.
Risk management	<p>Credit risk is managed at a Group level through a credit policy and trade credit insurance, which is carried for the majority of Group debtors.</p> <p>Each new customer is assessed for creditworthiness including external credit risk ratings before the Group's standard terms and conditions are offered.</p> <p>Purchase limits are established for each customer, which represent the maximum open amount without requiring further approval. These limits are reviewed periodically, and credit worthiness is continually monitored. Limits in excess of \$150,000 must be endorsed by the trade credit insurer. Customers that fail to comply with the terms of the Trade Credit Insurance Policy or the Group's benchmark creditworthiness may only transact with the Group on a prepayment basis.</p> <p>In most cases, goods are sold subject to retention of title clauses and this security is registered on the Personal Property Securities Register, so that in the event of non-payment the Group may have a priority claim. Depending upon the Group's assessment of industry or company risk, the Group may require personal guarantees from customer company directors and charging clauses over real property.</p>

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

19 Capital and financial risk management (continued)

(b) Financial risk management (continued)

The ageing of the Group's trade receivables is analysed in note 8.

(iii) Liquidity risk

Nature of the risk	Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.
Risk management	The Group manages liquidity risk by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities. Surplus funds are generally only invested in instruments that are tradeable in highly liquid markets.

Financing arrangements

Details of the Group's borrowings are discussed in note 17. The Group had access to the following undrawn borrowing facilities from its bankers at the end of the reporting period:

	2019 \$'000	2018 \$'000
Floating rate		
- Expiring within one year (bank overdraft)	-	-
- Expiring beyond one year (loans)	3,697	3,925
	3,697	3,925

Maturities of financial liabilities

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

	Less than 6 months \$'000	6 – 12 months \$'000	Between 1 and 2 years \$'000	Between 2 and 5 years \$'000	Total contractual cash flows \$'000	Carrying amount liabilities \$'000
At 30 June 2018						
Trade and other payables	47,731	-	-	-	47,731	47,731
Borrowings	2,221	6,117	2,234	29,035	39,607	32,696
Derivative financial instruments	(113)	-	-	-	(113)	(93)
Total	49,839	6,117	2,234	29,035	87,225	80,334
At 30 June 2019						
Trade and other payables	40,646	-	-	-	40,646	40,646
Borrowings	1,768	5,931	1,686	21,189	30,574	39,258
Derivative financial instruments	79	-	-	-	79	106
Total	42,493	5,931	1,686	21,189	71,299	80,010

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

20 Fair value measurements

(a) Fair value measurements for financial assets and liabilities

The fair values of cash and cash equivalents, trade receivables, trade payables and borrowings approximate their carrying amounts due to their short-term nature and the impact of discounting not being significant.

The Group measures and recognises derivative financial assets at fair value on a recurring basis.

AASB 13 requires disclosure of fair value measurements by reference to the following fair value measurement hierarchy:

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

The Group's financial assets and financial liabilities at fair value are as follows:

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
30 June 2018				
Assets				
Derivatives financial instruments	-	93	-	93
Total Assets	-	93	-	93
30 June 2019				
Liabilities				
Derivatives financial instruments	-	(106)	-	(106)
Total Liabilities	-	(106)	-	(106)

The Group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the transfer has occurred. There were no transfers between levels 1, 2 and 3 for recurring fair value measurements during the year.

The fair value of financial instruments that are not traded in an active market (for example, derivatives used for hedging) is determined using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. All significant inputs required to fair value derivatives used for hedging are observable, and hence the instruments are included in level 2. There have been no movements between levels during the year ended 30 June 2019.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

Section E: Group structure

This section provides information on the Hills Limited Group structure, including business acquisitions and disposals, controlled entities and related parties:

- 21 Interests in other entities
- 22 Related party transactions
- 23 Parent entity financial information
- 24 Deed of cross guarantee

21 Interests in other entities

(a) Investments in subsidiaries

The controlled entities of the Group listed below were wholly owned during the current and prior year, unless otherwise stated.

Australia

Hills Finance Pty Ltd ▲
Hills Group Operations Pty Ltd ▲
Hills Integrated Solutions Pty Ltd ▲
Audio Products Group Pty Ltd ▲
EMG Finance Pty Ltd
Pacific Communications (PACOM) Pty Ltd
Pacom Security Pty Ltd ▲
Hills Health Solutions Pty Ltd ▲
New-Tone (Aust) Pty Ltd ▲
T.V. Rentals Pty Ltd ▲
Hospital Telecommunications Pty Ltd ▲
Hills Polymers Pty Ltd ▲
Hills Hoists Pty Ltd ▲
Hills Share Plans Pty Ltd
Step Electronics 2005 Pty Ltd ●
Lan 1 Pty Ltd ▲
Woodroffe Industries Pty Ltd ▲
ACN 091 954 442 Pty Ltd ▲
ACN 099 403 139 Pty Ltd
Zen 99 Pty Ltd ▲
ACN 010 853 817 Pty Ltd ▲
ACN 094 103 090 Pty Ltd ▲
ACN 093 760 895 Pty Ltd
Access Television Services Pty Ltd ▲
ACN 614 478 090 Pty Ltd

New Zealand

Hills NZ Limited

▲ These entities are party to a Deed of Cross Guarantee – see note 24.

● 50% ownership interest. Step Electronics 2005 Pty Ltd is controlled by virtue of the Company's control of this entity's Board through the Chairman's casting vote, effective management of the entity and exposure to the risks and benefits of ownership, or control of voting rights through the dilution of the minority shareholders. This is a dormant entity.

(b) Non-controlling interests (NCI)

There is no individual subsidiary that has non-controlling interests that are material to the Group in either the current or the prior reporting period.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

22 Related party transactions

(a) Parent entities

The parent entity within the Group and the ultimate parent entity is Hills Limited.

(b) Subsidiaries

Interests in subsidiaries are set out in note 21.

(c) Key management personnel

	2019	2018
	\$	\$
Short-term employee benefits (fixed and variable incentive remuneration)	2,042,928	1,585,791
Post-employment benefits (superannuation)	151,886	127,521
Long term benefits (cash variable component under the Incentive Share Plan and accrued long service leave)	34,133	26,065
Share-based payments (performance rights variable component under the Incentive Share Plan and employee share bonus plan expense)	13,378	32,075
	2,242,325	1,771,452

Detailed remuneration disclosures are provided in the Remuneration Report.

(d) Loans to / from related parties

Subsidiaries

Group entity trading transactions and borrowings result in balances arising in respect of current and non-current assets and liabilities.

(e) Transactions with other related parties

The following transactions occurred with related parties:

Transactions with Director related entities

During the year no related party transactions with director related entities took place.

Amounts for any related party transactions are billed and payable under normal commercial terms and conditions as a supplier and as a customer.

There were no other transactions during the reporting period with KMP and their related parties. From time to time, KMP of the Company or its controlled entities, or their related entities, may purchase goods or services from Hills or make sales of goods or services to Hills. These purchases or sales are on the same terms and conditions as those entered into by Hills employees, customers or suppliers and are trivial or domestic in nature.

Subsidiaries

All transactions with partly owned controlled entities are on normal commercial terms and conditions. Transactions with controlled entities are determined on a cost basis.

Sales of goods and services	Sales of goods and services within the Group, that eliminated with cost of goods sold and services provided amounted to \$4.256 million (2018: \$2.977 million).
Loans and borrowings	Loans and borrowings with Australian wholly owned controlled entities are interest free and payable on demand while loans to or from non-wholly owned subsidiaries and overseas wholly controlled entities are charged interest at rates no more favourable than current market rates. Intragroup interest paid and received during the year was nil (2018: \$nil).
Dividends	There were no intragroup dividends paid and received during the year (2018: \$nil).

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

23 Parent entity financial information

(a) Summary financial information

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

	2019 \$'000	2018 \$'000
Balance sheet		
Current assets	97,660	96,204
Non-current assets	42,924	42,562
Total assets	140,584	138,766
Current liabilities	81,665	76,743
Non-current liabilities	39,549	27,022
Total liabilities	121,214	103,765
Net assets	19,370	35,001
<i>Shareholders' equity</i>		
Contributed equity	278,439	278,439
Reserves		
Hedging reserve - cash flow hedges	(134)	65
Equity compensation reserve	751	738
Profits reserve	32,859	32,859
Retained earnings	(292,545)	(277,100)
	19,370	35,001
Loss for the year	(15,447)	(4,963)
Total comprehensive income	(15,245)	(4,740)

(b) Guarantees, contingent liabilities and commitments of the parent entity

Guarantees	Bank guarantees given by the Company in favour of customers and suppliers amounted to \$2.466 million (2018: \$2.778 million). Cross guarantees are given by the Company and its wholly owned subsidiaries as described in note 24. Under the terms of the Deed of Cross Guarantee the Company and its wholly owned subsidiaries have guaranteed the debt in each other's companies.
Contingent liabilities	The parent entity had a contingent liability in respect of claims, as disclosed in note 25. For information about guarantees given by the parent entity, please see above.
Contractual commitments	As at 30 June 2019, the Company had \$2.061 million contractual commitments for the acquisition of plant, equipment or intangible assets (2018: \$2.9 million). These commitments are not recognised as liabilities as the relevant assets have not yet been received.

Recognition and measurement

Parent entity financial information

The financial information for the parent entity has been prepared on the same basis as the consolidated financial statements.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

24 Deed of cross guarantee

The wholly owned subsidiaries identified with a '▲' in note 21 are relieved from the *Corporations Act 2001* requirements for preparation, audit and lodgement of financial reports and Directors' reports, under *ASIC Corporations (Wholly-owned Companies) Instrument 2016/785*.

The Company and each of these subsidiaries have entered into a Deed of Cross Guarantee (the "Deed"), under which each company guarantees the debt of the others. No entities have become a party to the Deed during the reporting period.

Hills Limited is the Holding company and Pacom Security Pty Ltd is the Trustee under the Deed.

The entities identified with a '▲' in note 21 represent a 'closed group' for the purposes of the ASIC Instrument, and as there are no other parties to the Deed that are controlled by Hills Limited, they also represent the 'extended closed group'.

Set out below is a consolidated income statement, a consolidated statement of comprehensive income, a summary of movements in consolidated retained earnings for the year ended 30 June 2019 and a consolidated statement of financial position as at 30 June 2019 of the Company and controlled entities that are a party to the Deed, after eliminating all transactions between parties.

(a) Consolidated statement of profit or loss and other comprehensive income and summary of movements in consolidated retained earnings

	2019	2018
	\$'000	\$'000
Consolidated statement of profit or loss and other comprehensive income		
Revenue from continuing operations	251,566	255,360
Other income	533	787
Finance costs	(3,273)	(3,189)
Other expenses	(262,472)	(253,299)
Loss before income tax	(13,646)	(341)
Income tax expense	5,603	478
Profit/ (Loss) for the year	(8,043)	137
Other comprehensive income		
<i>Items that may be reclassified to profit or loss:</i>		
Changes in the fair value of cash flow hedges	(198)	318
Income tax relating to these items	-	(95)
Other comprehensive profit / (loss) for the period, net of tax	(198)	223
Total comprehensive profit / (loss) for the year	(8,241)	360
Summary of movements in consolidated retained earnings		
Accumulated losses at the beginning of the reporting period	(232,786)	(232,923)
Adjustment on initial application of AASB 9	(200)	-
Profit / (Loss) for the year	(8,043)	137
Accumulated losses at the end of the reporting period	(241,029)	(232,786)

Hills Limited
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For the year ended 30 June 2019
(continued)

24 Deed of cross guarantee (continued)

(b) Consolidated statement of financial position

	2019 \$'000	2018 \$'000
Current assets		
Cash and cash equivalents	9,935	13,195
Trade and other receivables	56,693	55,211
Inventories	37,879	40,903
Derivative financial instruments	-	93
Total current assets	104,507	109,402
Non-current assets		
Investments	814	814
Property, plant and equipment	14,969	14,433
Intangible assets	2,069	6,267
Deferred tax assets	16,295	10,693
Total non-current assets	34,147	32,207
Total assets	138,654	141,609
Current liabilities		
Trade and other payables	41,407	45,877
Borrowings	15,299	6,357
Provisions	8,522	5,985
Derivative financial instruments	106	-
Total current liabilities	65,334	58,219
Non-current liabilities		
Borrowings	22,555	24,935
Provisions	4,478	3,739
Total non-current liabilities	27,033	28,674
Total liabilities	92,367	86,893
Net assets	46,287	54,716
Equity		
Contributed equity	278,439	278,439
Reserves	8,877	9,063
Accumulated losses	(241,029)	(232,786)
Total equity	46,287	54,716

Section F: Unrecognised items

This section contains information about items that are not recognised in the financial statements but may have a significant impact on the Group's financial position or performance.

25	Contingencies
26	Commitments
27	Events after the reporting period

25 Contingencies

(a) Contingent liabilities

The Group had contingent liabilities at 30 June 2019 in respect of:

Claims	In consultation with the Environmental Protection Authority, ground water contamination potentially originating from two of the Company's former Adelaide sites continues to be monitored by the Company. It is anticipated that ongoing monitoring will be required to be undertaken by Hills. The Company has provided for the anticipated costs of ongoing assessments. The Group has various commercial legal claims common to businesses of its type that constitute contingent liabilities, none of which are deemed material to the Group's financial position. The Directors are of the opinion that provisions are not required in respect of these matters, as it is not probable that a future outflow of economic benefits will be required.
Guarantees	Bank guarantees in favour of customers and suppliers totalling \$2.466 million (2018: \$2.778 million).

26 Commitments

(a) Capital commitments

Capital expenditure contracted for at the reporting date but not recognised as liabilities is as follows:

	2019 \$'000	2018 \$'000
Plant, equipment and intangible assets	58	2,931

(b) Lease commitments: Group as lessee

Non-cancellable operating leases

The Group leases a number of offices, warehouse and factory facilities under operating leases.

The leases run for a period from 1 to 6 years with the majority running for a period of 2 to 5 years, with options to renew the lease after that date. Lease payments are increased each renewal period to reflect market rentals. Some leases provide for additional rent payments that are based on changes in the consumer price index, local capital city consumer price indices or a fixed percentage.

The Group also leases motor vehicles and materials handling equipment under operating leases.

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

26 Commitments (continued)

(b) Lease commitments: Group as lessee (continued)

	2019 \$'000	2018 \$'000
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:		
Within one year	5,938	6,579
Later than one year but not later than five years	13,939	11,526
Later than five years	978	2,159
	20,855	20,264

(c) Lease commitments: where a Group company is the lessor

The future minimum lease payments receivable under non-cancellable operating leases are as follows:

	2019 \$'000	2018 \$'000
Within one year	368	150
Later than one year but not later than five years	185	-
	553	150

Recognition and measurement

Leases

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

27 Events after the reporting period

There have been no events subsequent to balance date that would have a material effect on the Group's financial statements at 30 June 2019.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

Section G: Other

This section contains disclosures required for the Group to comply with the accounting standards and other pronouncements, the *Corporations Act 2001* or the Corporations Regulations but are not considered to be significant in understanding the financial position or performance of the Group:

28	Share-based payments
29	Remuneration of auditors
30	Other accounting policies

28 Share-based payments

(a) Executive share options

All executive share options were forfeited or cancelled during the previous reporting period.

(b) Employee performance rights

In 2010, the Group established the Incentive Share Plan. The Incentive Share Plan was designed to provide long term incentives to eligible senior employees of the Group and entitled them to acquire shares in the Company, subject to the successful achievement of performance hurdles related to earnings per share (EPS) and total shareholder returns (TSR). Details of performance rights under the Incentive Share Plan are as follows:

Grant date	Expiry date	Exercise price	Balance at start of the year Number	Granted during the year Number	Exercised /vested during the year Number	Forfeited / cancelled during the year Number	Balance at the end of the year Number	Vested & exercisable at the end of the year Number
2018								
Performance rights								
1 Sep 2016	1 Sep 2017	-	100,000	-	(100,000)	-	-	-
1 Sep 2016	1 Sep 2018	-	100,000	-	-	-	100,000	-
31 Jul 2017	30 Jun 2020	-	-	159,152	(31,830)	-	127,322	-
Total			200,000	159,152	(131,830)	-	227,322	-
2019								
Performance rights								
1 Sep 2016	1 Sep 2018	-	100,000	-	(100,000)	-	-	-
31 Jul 2017	30 Jun 2020	-	127,322	-	(87,475)	-	39,847	-
27 Aug 2018	30 Jun 2021	-	-	198,646	-	-	198,646	-
Total			227,322	198,646	(187,475)	-	238,493	-

Fair value of performance rights granted

The fair value assessed in accordance with AASB 2 *Share Based Payments* at grant date of performance rights granted on 1 September 2016 was 34.0 cents per performance right, based on the quoted share price at grant date.

The fair value assessed in accordance with AASB 2 *Share Based Payments* at grant date of performance rights granted on 31 July 2017 was 18.9 cents per performance right, based on the quoted share price at grant date.

The fair value assessed in accordance with AASB 2 *Share Based Payments* at grant date of performance rights granted on 27 August 2018 was 18.9 cents per performance right, based on the quoted share price at grant date.

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

28 Share-based payments (continued)

(c) Expenses arising from share-based payment transactions

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

	2019 \$'000	2018 \$'000
Performance rights issued under Incentive Share Plan	13	32

Recognition and measurement

Share-based payments

Share based compensation benefits are provided to employees via the Incentive Share Plan – see below:

Incentive Share Plan

The Incentive Share Plan allows Group executives to acquire shares of the Company.

The fair value of performance rights granted under the Incentive Share Plan is recognised as an employee benefits expense with a corresponding increase in equity. The total amount to be expensed is determined by reference to the fair value of the performance rights granted, measured at the grant date, which includes any market performance conditions and the impact of any non-vesting conditions but includes the probability of meeting any service and non-market performance vesting conditions.

The valuation method takes into account the exercise price of the performance right, the life of the performance right, the current price of the underlying shares, the expected volatility of the share price, the dividends expected of the shares and the risk-free interest rate for the life of the performance right.

Non-market vesting conditions are included in assumptions about the number of rights that are expected to vest.

The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each period, the entity revises its estimates of the number of rights that are expected to vest based on the non-market vesting conditions. It recognises the impact of the revision to original estimates, if any, in profit or loss, with a corresponding adjustment to equity. No change is made for changes in market conditions.

29 Remuneration of auditors

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

	2019 \$	2018 \$
KPMG audit and non-audit services		
Audit and other assurance services		
KPMG Australia – audit and review of the financial statements	331,500	259,000
Taxation services		
KPMG Australia – taxation and other services	15,425	16,000
Overseas KPMG firms – taxation services	4,619	4,390
Total remuneration for taxation services	20,044	20,390
Other services		
Other consulting services	2,285	7,250
Total remuneration for other services	2,285	7,250
Total remuneration of KPMG	353,829	286,640

Hills Limited
Notes to the consolidated financial statements
For the year ended 30 June 2019
(continued)

30 Other accounting policies

(a) New and amended standards adopted by the Group

Effective 1 July 2018, the group adopted AASB 9 Financial Instruments (AASB 9) and AASB 15 Revenue with Contracts with Customers (AASB 15). The impact of the adoption of these standards is disclosed below.

Title	Effective date	Details
AASB 9 <i>Financial Instruments</i>	1 January 2018 Hills Group: Applicable for the year ending 30 June 2019	<p>This standard changes the classification and measurement of financial instruments, introduces new hedge accounting requirements including changes to hedge effectiveness testing, treatment of hedging costs, risk components that can be hedged and disclosures, and introduce a new expected-loss impairment model that will require more timely recognition of expected credit losses.</p> <p>The Group has completed a preliminary assessment of the requirements of the standard and expects that there will not be a significant impact on the financial statements on transition to AASB 9.</p> <p><i>(i) Classification and measurement</i></p> <p>At transition the impact on the balance sheet was an increase in expected credit loss provision of \$0.2m. This was put through equity. Financial assets currently held at fair value will continue to be measured at fair value. Trade and other receivables are held to collect contractual cash flows and these contractual cash flows are solely payments of principle and interest. These receivables will be measured at amortised cost.</p> <p><i>(ii) Impairment</i></p> <p>The revised methodology for calculation of impairment did not have a significant impact on the financial statements. The Group will use the simplified approach to determine the expected credit loss provision.</p> <p><i>(iii) Hedge accounting</i></p> <p>As permitted by AASB 9 the group has chosen to continue to apply the hedge accounting requirements of AASB 139 <i>Financial Instruments: Recognition and Measurement</i>.</p>
AASB 15 <i>Revenue from Contracts with Customers</i>	1 January 2018 Hills Group: Applicable for the year ending 30 June 2019	<p>The standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The core principle is that an entity recognises revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive.</p> <p>The Group's analysis and assessment of the impact of AASB 15 on its financial results included an analysis of the specific requirements of the standard and the consideration of material contracts entered into by the Group that give rise to revenue.</p> <p>Sale of goods represent around 80% of total revenue. Product sales include a number of variable considerations such as discounts, rebates and rights of return, which may change the way that revenue is recognised under AASB 15.</p> <p>Services revenue represents around 20% of total revenue. Revenue recognition for contracts within the Hills Health Solutions division had no material impact on revenue recognition.</p> <p>The new standard also introduces expanded disclosure requirements and changes in presentation. These are reflected in Note 2 Revenue.</p>

(b) Early adoption of standards

The Group has not elected to early adopt any new accounting standards and amendments.

30 Other accounting policies (continued)

(c) New accounting standards and interpretations not yet adopted

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2019 reporting periods and have not been early adopted by the Group. The Group's assessment of the impact of these new standards and interpretations is set out below.

<p>AASB 16 <i>Leases</i></p>	<p>1 January 2019 (early adoption permitted) Hills Group: Applicable for the year ending 30 June 2020</p>	<p>AASB 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. AASB 16 will supersede the current lease guidance AASB 117 <i>Leases</i> when it becomes effective on 1 July 2019.</p> <p>Distinctions of operating leases (off balance sheet) and finance leases (on balance sheet) are removed and replaced by a model where a right-of-use asset ('RoU') and a corresponding liability have to be recognised for all leases by the lessee except for short term leases and leases of low value assets.</p> <p>The RoU asset is initially measured as equal to the corresponding lease liability, less any adjustments in respect of lease incentives, initial direct costs and other required items. It is subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the future lease payments. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications. Recognition of RoU asset and respective lease liabilities leads to an increase in depreciation and finance charges. These charges will replace the operating lease expense that is currently reported in the Group's financial report. Furthermore, the classification of cash flows will also be affected as operating lease payments under AASB 117 are presented as operating cashflows; whereas under the AASB 16 model, the lease payments will be split into a principal and an interest portion which will be presented as financing and operating cashflows respectively.</p> <p>Furthermore, extensive disclosures are required by AASB 16.</p> <p>AASB16 will be adopted by the Group on 1 July 2019 applying the modified retrospective transition approach. AASB16 will have a material impact on the Group's Financial Statements and whilst the amount has not been quantified the Group has lease commitments of \$20.8 million as at 30 June 2019 as disclosed in note 26(b). The Group is finalising the impact assessment. The key assumptions used to determine the RoU and corresponding lease liability are: the lease term, options to extend the original lease terms, discount rate used, and termination options.</p>
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Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

30 Other accounting policies (continued)

(d) Goods and Services Tax (GST)

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

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from, or payable to, the taxation authority is included with other receivables or payables in the consolidated statement of financial position.

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

Hills Limited

Notes to the consolidated financial statements

For the year ended 30 June 2019

(continued)

Directors' declaration

For the year ended 30 June 2019

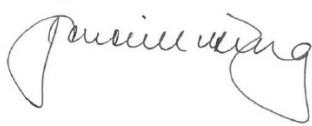
In the opinion of the Directors of Hills Limited (the Company):

- (a) the consolidated financial statements and notes set out on pages 30 to 84 and the Remuneration Report on pages 14 to 28 are in accordance with the *Corporations Act 2001*, including:
 - (i) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
 - (ii) giving a true and fair view of the Group's financial position as at 30 June 2019 and of its performance for the financial year ended on that date; and
- (b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable; and
- (c) there are reasonable grounds to believe that the Company and the Group Entities identified in note 21 will be able to meet any obligations or liabilities to which they are, or may become, subject to by virtue of the Deed of Cross Guarantee between the Company and those Group Entities pursuant to *ASIC Corporations (Wholly-owned Companies) Instrument 2016/785*.

Section A of the notes confirms that the consolidated financial statements also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board.

The Directors have been given the declarations by the Chief Executive Officer & Managing Director, and Chief Financial Officer required by section 295A of the *Corporations Act 2001*.

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



Jennifer Hill-Ling
Director



Philip Bullock AO
Director

Sydney
30 August 2019



Independent Auditor's Report

To the shareholders of Hills Limited

Report on the audit of the Financial Report

Opinion

We have audited the Financial Report of Hills Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Group's financial position as at 30 June 2019 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The Financial Report comprises:

- Consolidated statement of financial position as at 30 June 2019;
- Consolidated statement of profit or loss, Consolidated statement of comprehensive income, Consolidated statement of changes in equity, and Consolidated statement of cash flows for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

The Group consists of the Company and the entities it controlled at the year-end or from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Group in accordance with *the Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

The Key Audit Matters we identified are:

- 1 Impairment assessment of the Hills Distribution cash-generating unit
- 2 Valuation of inventories; and
- 3 Revenue cut-off.

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Report of the current period.



These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Impairment assessment of the Hills Distribution cash-generating unit ('CGU')	
Refer to Note 11 and 12 to the financial report	
The key audit matter	How the matter was addressed in our audit
<p>A key audit matter was the Group's testing of assets attributable to the Hills Distribution CGU. Given the performance of the CGU during the year ended 30 June 2019 and the existence of intangible assets, we exercised significant judgement in evaluating audit evidence available.</p> <p>In addition to the above:</p> <ul style="list-style-type: none"> • the carrying amount of the net assets of the Group exceeded the Company's market capitalisation at year end, increasing the possibility of impairment. • the Group recorded an impairment charge of \$5.996 million against intangible assets and \$0.500 million in respect of property, plant and equipment, increasing the sensitivity of management's 'value-in-use' ('VIU') model to small changes. <p>We focussed on the significant forward looking assumptions the Group applied in their VIU model, including:</p> <ul style="list-style-type: none"> • The forecast cash flows – the CGU incurred a loss during the year as a result of changes in vendor portfolio and challenging market conditions for some products, in particular communication products. This impacted the Group through reduced sales. These conditions increase the risk of inaccurate forecasts and the possibility of the CGUs assets being impaired. • Terminal growth rate – the model is sensitive to changes in the terminal growth rate. This drives additional audit effort in relation to the feasibility of the terminal growth rate. We involve our valuations specialists and senior audit team members with the assessment. • Discount rate – these are complicated in nature and vary according to the conditions and environment the specific CGU is subject to from time to time. The Group's modelling is sensitive to small changes in the discount rate. We involve our valuations specialists and senior audit team members with the assessment. <p>This further increased our audit effort in this key audit area.</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> • We considered the appropriateness of the VIU model prepared by management and applied by the Group to perform the impairment test against the requirements of the accounting standards. • We assessed the integrity of the VIU model used, including the accuracy of the underlying calculation formulas. • We checked the forecast cash flows contained in the model were approved by the Board. • We assessed the accuracy of previous budgets to inform our evaluation of forecasts included in the VIU model. • We assessed the Group's underlying methodology and documentation for the allocation of corporate costs to the forecast cash flows contained in the VIU model, for consistency with our understanding of the business and the criteria in the accounting standards. • We challenged the sustaining capital assumptions including consideration of the forecast against actual capital expenditure incurred over prior periods and future plans. We used our knowledge of the CGU to assess the feasibility of these plans. • Working with our valuation specialists we: <ul style="list-style-type: none"> - compared forecast growth rates and terminal growth rates to published economic trends and expectations, and considered differences for the CGU's operations. We used our knowledge of the CGU, their past performance, business and customers, and our industry experience. - analysed the CGU's discount rate against publicly available data of a group of comparable entities. • We assessed the disclosures in the financial report using our understanding of the issue obtained from our testing and against the requirements of the accounting standards. • We recalculated the impairment charge against the recorded amount disclosed.

Valuation of inventories (\$41.636 million)

Refer to Note 9 to the financial report

The key audit matter

The audit of the carrying value of inventory is a key audit matter due to the extent of judgement involved in determining the recoverable value, particularly in relation to slow moving, obsolete or excessive inventory.

The Group has a broad range of technology products that are at risk of being superseded by technological advances or have been sourced under specific distribution arrangements, or for a specific customer, which increases the amount of judgement required in assessing the carrying value of inventory.

In addition to the above, the Group:

- Announced a strategic review of the Distribution business during the year.
- Recorded a net realisable value impairment of \$3.800 million increasing the sensitivity of the inventory net realisable value calculation to small changes.

This further increased our audit effort in this key audit area.

We particularly focused on the estimates listed below which significantly impact the valuation:

1. Expected selling price of inventory.
2. Ageing of inventory.
3. Future inventory usage.

In assessing this key audit matter, we utilised senior audit team members who understand the Group's business, industry and the relevant economic environment.

How the matter was addressed in our audit

Our procedures included:

- Assessing the appropriateness of the Group's policies for the valuation of inventory against the requirements of the accounting standards.
- Attending year-end stocktakes in significant locations which included observing the Group's process of identifying slow moving and potentially obsolete inventory.
- Using the current year selling price and resulting gross margin for each product to identify evidence of negative gross margin products. We compared these negative gross margin products to the inventory obsolescence provision.
- Obtaining the calculation of the inventory obsolescence provision and comparing it to the Group's accounting policies, the Group's analysis of slow moving inventory and current year actual sales and usage.
- Assessing the level of provision in light of our understanding of the business, and knowledge of the industry in which the Group operates.

Revenue cut-off

Revenue \$267.362 million – Refer to Note 2 to the financial report

The key audit matter

The Group derived revenue from two main sources, being the sale of goods and provision of services.

The audit of revenue cut-off is a key audit matter due to the high number of transactions and the judgement involved in recording revenue in the appropriate financial period. This includes consideration of when a customer obtains control of the goods, or in proportion to the stage of completion for services rendered.

How the matter was addressed in our audit

Our procedures included:

- Evaluating the Group's accounting policy against the requirements of AASB 15 *Revenue from Contracts with Customers*, which was adopted at the commencement of the year.
- Sample testing significant sales recorded pre and post balance date to verify they had been recorded in the correct financial period.
- Obtaining and assessing the appropriateness of management's adjustment for sales invoiced, but not despatched by balance date.
- Verifying the percentage of completion at balance date for sample of projects where the performance obligation is satisfied over time, by obtaining customer confirmation.



Other Information

Other Information is financial and non-financial information Hills Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*;
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Group and Company's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Group and Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the Financial Report.

A further description of our responsibilities for the audit of the Financial Report is located at the *Auditing and Assurance Standards Board* website at: http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf. This description forms part of our Auditor's Report.



Report on the Remuneration Report

Opinion

In our opinion, the Remuneration Report of Hills Limited for the year ended 30 June 2019, complies with *Section 300A of the Corporations Act 2001*.

Directors' responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A of the Corporations Act 2001*.

Our responsibilities

We have audited the Remuneration Report included in the Directors' report for the year ended 30 June 2019.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with *Australian Auditing Standards*.

KPMG

Paul Cenko
Partner

Adelaide

30 August 2019

Shareholder information

The shareholder information set out below was applicable as at 5 July 2019.

Distribution of equity securities

Analysis of numbers of ordinary shareholders by size of holding:

Size of holding	Number of holders
1 - 1000	3,746
1,001 - 5,000	4,942
5,001 - 10,000	1,895
10,001 - 100,000	1,893
100,001 and over	239

There were 6,764 holders of less than a marketable parcel of ordinary shares.

Twenty largest shareholders

The names of the 20 largest holders of ordinary shares are listed below:

Name	Number of shares	% of shares issued
Hills Associates Limited	16,768,441	7.23
Poplar Pty Ltd	16,550,845	7.13
The Trust Company (Australia) Limited	7,042,416	3.04
Cariste Pty Ltd	6,891,872	2.97
Jacaranda Pastoral Pty Ltd	5,868,699	2.53
Cambrose Pty Limited	4,676,510	2.02
Greybox Holdings Pty Ltd	3,650,042	1.57
Mr & Mrs Alan R Bignell	3,453,530	1.49
Glennon Capital	3,300,355	1.42
Ace Property Holdings Pty Limited	3,200,000	1.38
JMID Pty Ltd	3,200,000	1.38
Hart Capital Partners Ltd	2,982,052	1.29
V M Nominees Pty Limited	2,250,000	0.97
AcomeA	2,100,000	0.91
Mr John Gassner	1,537,751	0.66
Mr & Mrs Joseph Zanca	1,500,000	0.65
Carrier International Pty Limited	1,475,288	0.64
Mr Gregory V Shalit & Ms Miriam Faine	1,435,000	0.62
Mr Alan G Rochford	1,250,000	0.54
Mr Peter Howells	1,183,608	0.51

Shareholder information (continued)

Substantial holders

Substantial holders in the Company are set out below:

Name	Number held	% of shares issued
Poplar Pty Ltd ¹	17,775,724	7.65
Hills Associates Limited	16,768,441	7.23
The Trust Company (Australia) Limited ²	13,224,468	5.71

Voting rights

The voting rights attaching to each class of equity securities are set out below:

Ordinary shares	On a show of hands every member present at a meeting in person or by proxy shall have one vote and upon a poll each share shall have one vote.
Rights/options	No voting rights.

On-market buyback

There is no current on-market buyback in place.

Direct payment to shareholder accounts

Dividends may be paid directly to bank, building society or credit union accounts in Australia. Payments are electronically credited on the dividend date and confirmed by mailed payment advice. Shareholders who want their dividends paid this way should advise the Company's share register in writing.

Securities exchange

The Company is listed on the Australian Securities Exchange. The home exchange is Sydney.

¹ The total number of shares held includes the joint shareholding held by Poplar Pty Ltd and Hills Associates Limited and the shareholding held by Ling Nominees Pty Ltd.

² The total number of shares held by The Trust Company (Australia) Limited (Merchant/Merchant Opportunities Fund), JMID Pty Limited and Hart Capital Partners (refer to ASX:HIL Becoming a substantial holder notice dated 5 March 2019).

Corporate directory

Registered office

Unit 1, Building F, 3-29 Birnie Avenue, Lidcombe, NSW 2141

Telephone: (02) 9216 5510

Facsimile: (02) 9216 5999

Web: <http://www.hills.com.au>

Executives

David John Joseph Lenz, *Chief Executive Officer and Managing Director*

Christopher Stuart Jacka, *Chief Financial Officer*

Non-executive directors

Jennifer Helen Hill-Ling

Fiona Rosalyn Vivienne Bennett

Philip Bullock AO

Kenneth James Dwyer

Company secretary

David Robert Fox

Share registry

Link Market Services Limited

Locked Bag A14, Sydney South, NSW 1235, Australia

Telephone

- Australia and International: +61 1300 554 474

Facsimile

- Australia and International: +61 2 9287 0303

ASX code: HIL

Email: registrars@linkmarketservices.com.au

Web: www.linkmarketservices.com.au