

Hills Limited
Annual report
for the year ended 30 June 2020

ABN 35 007 573 417

Hills Limited

Annual report

for the year ended 30 June 2020

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Contents

Shareholders' letter	2
Directors' report	5
Remuneration report.....	15
Auditor's independence declaration	30
Consolidated financial statements.....	31
Directors' declaration.....	84
Independent auditor's report to the members of Hills Limited.....	85
Shareholder information.....	90
Corporate directory	92

Shareholders' letter

Dear Shareholder,

The past financial year has seen two distinct halves in the performance of your Company with the second half impacted by the onset of COVID 19 and various one-off costs.

We commenced financial year 2020 (FY20) on the cusp of an exciting new period for Hills with a simplified and focused business structure that positioned us to maximise returns for shareholders.

Our key strategic focus during FY20 was to continue to:

- grow the Hills Health Solutions business (HHS) by expanding our range of products and services to hospitals and healthcare facilities such as Aged Care facilities; and
- streamline the Distribution business by continuing to implement the strategic and operational initiatives outlined at our AGM last November.

Our FY20 first half results demonstrated our ability to execute our strategies with both Health and Distribution businesses reporting a profit and the Company reporting:

- NPAT of \$2.6M – up from \$0.242 million in the first half (1H) 2019;
- Net Debt of \$20.6M (pre AASB16) - a like for like reduction of 27% over the prior year; and
- Operating expenses reduced by \$3.3m

During the first half we also successfully divested our non-core AV, Antenna and STEP businesses and at the commencement of the second half of FY20, Hills was well positioned to deliver solid results for the remainder of FY20.

However, the onset of the coronavirus pandemic (COVID-19), presented unexpected challenges in the second half (2H) unlike anything faced in the 75-year history of your Company. During this period the board and management of Hills focused on three priorities:

- looking after our people;
- continuing to deliver the highest level of products and services to our customers and partners; and
- managing the economic and social impacts caused by the COVID-19 crisis.

Actions undertaken included:

- Maintaining a strong focus on our sales, expenses and cashflow, with weekly Board and management reviews during Q4.
- Implementing safeguards to ensure all our employees, have been able to operate in safe working environments without affecting their productivity or work ethic.
- Reducing salaries across the Company to preserve cashflow and mitigate the impact of COVID-19 on the business. Further details on this are in the Remuneration Report.
- Receipt of JobKeeper assistance from the Australian Government, and similar support from the New Zealand Government. We are very appreciative of these programs which, together with the generosity of our employees, have played a significant role in helping Hills manage the impacts from COVID 19 on the business.
- Focusing on our business continuity plans, to ensure our services and products continued to be available to all our customers, while also protecting the safety of customers, suppliers and our employees.

Notwithstanding this action, and despite recording an improved underlying segment EBITDA of \$12.6M, compared to \$9.6M in the previous year, we were disappointed that we were unable to build on the profitable performance of the prior period, recording a statutory loss for the FY20 year of \$6.2M after taking into account one-off costs of \$6.8M in non-operating expenses largely comprising one-off items including FX adjustments as well as \$1.2M in redundancies. This compares to a statutory loss of \$8.8M in FY19.

Pleasingly, our strong focus on our sales, expenses and cash utilisation during the year resulted in a stronger balance sheet at 30 June 2020 with:

- Net Debt at \$8.2M - down by \$20.2M from \$28.4M as at June 2019 and down by \$12.5M since December 2019, reflecting strong management of inventory and debtors, and
- Net Inventory of \$25.2M - down by \$16.5M from \$41.6M as at 30 June 2019, and down by \$10.8M during the second half.

Our cashflow outlook to December 2020 remains strong, but is subject to developments in Victoria, and any further COVID 19 outbreaks elsewhere in Australia for the remainder of the current financial year.

Hills Limited

Shareholders' letter

For the year ended 30 June 2020

Hills Health Solutions

Our Health business reported an Underlying Segment EBITDA of \$8.6M for the year compared with \$11.0M in FY19. During the period, we experienced site closures and/or restricted site access, to hospitals and Aged Care facilities, leading to:

- delays and deferrals in Nurse Call projects; and
- reduced revenues from our patient engagement business, coupled with the national deferral of elective surgery. This revenue impact was somewhat mitigated by pivoting from a "user pays" to a temporary fixed rental model (hospital pays), impacting 2,700 installed beds.

During the year we also reviewed our health inventory based on the success of our IP7500 nurse call platform resulting in additional inventory provisions for the IP7000 series products, which will continue to be used for the expansion, maintenance and support of current sites.

Pleasingly during the year, we delivered 6,400 new beds of our Nurse call IP7500 into Westmead, Casey Hospital Tower, Western Health, Alfred and Royal Hobart hospitals. The team also completed the development of the New IP Series wireless platform which is now available in market receiving initial encouraging support, but sales performance will be hampered by COVID-19 as the target market for this product is Aged Care facilities. During the onset of the COVID crisis our team undertook additional works at the Royal North Shore Hospital in preparation for increased patients.

The patient entertainment business added 1,060 new beds and renewed contracts across 15 hospitals representing 3,000 beds. We have also seen sales momentum continue to build for our GetWell Network patient engagement platform which were installed:

- at the Calvary Hospital in Adelaide - 400 beds installed and operating
- at the Royal Hobart Hospital - 350 beds installed and operating

Our key strategic focus for Hills Health in FY21 will be driven by:

- market share gains
- continued investment in Nurse Call product development; and
- a \$175 M pipeline of orders and tenders over the next 3 years.

Hills is actively reviewing all opportunities to accelerate growth in our health business with the support of specialist health sector advisory firm Paxton Partners. We look forward to providing more details on this review at the upcoming AGM.

Hills Distribution

Our Distribution business recorded an improved profit in FY20 reporting a profit before tax of \$1.3M, compared to a loss before tax for the year ended 30 June 2019 of \$3.2M.

Pleasingly the continuing operations, (following the divestments of our AV, Antenna and STEP businesses), delivered an Underlying Segment EBITDA improvement of \$5.6M to \$5.7M over the prior year where Underlying Segment EBITDA was \$0.1M, reflecting a significant reduction in operating expenses.

Overall revenue for the continuing operations was down on prior year of 7.3% as a result of a number of commercial/enterprise projects being delayed and/or cancelled as a result of COVID 19 which was partially offset by the increase in our Small To Medium business (SMB) over the prior year.

Following the review our Distribution inventory, we made a further provision to reflect our ongoing requirements following the business divestments and further streamlining of the continuing businesses.

Hills Technical Services business (HTS) (formerly Hills Connection Solutions) recorded a solid result as it continued to fulfil the contract with Ericsson to supply home installation services for NBN Co.'s fixed wireless product. Hills has been advised that this contract will be extended until 2023 ensuring we continue to have a solid foundation on which to grow the HTS business in FY21.

Hills Limited

Shareholders' letter

For the year ended 30 June 2020

Outlook

Whilst the general economic outlook remains uncertain, the Health, Security, IT and Technical Services markets in which the Group operates, continue to experience demand for products and services. We remain confident of the Group's ability to emerge from this period of unprecedented disruption in a strong competitive position.

While trading in July was encouraging, the medium-term economic outlook remains clouded by the uncertainty created by the COVID-19 pandemic.

The recent movement in exchange rates, however, has had an adverse impact on current foreign exchange contracts given their scale and duration, which has caused uncertainty around FY21 financial performance. At the same time, a review has been instigated into the circumstances relating to the foreign exchange contracts giving rise to the uncertainty.

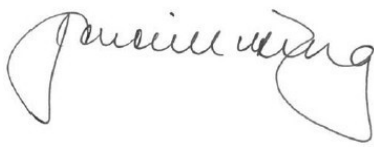
At the commencement of FY21 we announced the appointment of David Chambers to the Board as a non-executive director with significant experience in the Health industry and listed Australian companies. David has been instrumental in assisting Andy Hall, head of our Health business in leading the Strategic review of Hills Health Solutions.

At the same time, we also announced that Philip Bullock AO intends to retire from the Board at this year's AGM. On behalf of the Company we would like to thank Philip for his outstanding contribution as a Director and mentor over the last 6 years.

In closing we would like to acknowledge our employees who have worked tirelessly to support our customers, vendors and suppliers during these difficult times, and we thank them for their ongoing dedication and commitment.

Please join us at the Annual General Meeting, when 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 2020

Directors' report

The Directors of Hills Limited present their report together with the consolidated financial statements of Hills Limited (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 2020 and the independent auditor's report thereon.

Operating and financial review

The operating and financial review forms part of the Directors' report and has been prepared in accordance with section 299A of the Corporations Act 2001(Cth). The information provided aims to assist users better understand the operations and financial position of the Group. To assist users, financial information included in this review contains non-IFRS financial information.

About the Group

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. In December 2019 the Group exited its AV, Antenna and STEP businesses following an Operational and Strategic business review completed during the financial year ended 30 June 2019, thereby reducing exposure to non-performing assets and reducing the overall complexity of the business. This enabled the Company to streamline and narrow the focus of our Distribution business and increase our investment in our Health business.

The Group operates in Australia and New Zealand and the principal activities of the Group is as a supplier of technology solutions in the Health market and a value-added distributor of technology products and services in the Security, Surveillance and IT markets.

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 and solutions remain market leaders. As an Australian owned company, we are proud to manufacture our new Nurse Call platform in Australia.

Hills Distribution

Hills Distribution is a leading value-added provider of technology for homes, hospitals and healthcare facilities, places of learning, entertainment venues, retail spaces, transport and infrastructure, banking and finance, workplaces and government institutions.

Together with maintaining strong vendor relationships and contracts, Hills also invests in expert resources across Australia and New Zealand to offer products and solutions that allow customers to manage:

- 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)
- Smoke Alarms

We also provide pre and post installation services and technician management services.

Group performance highlights

The following table provides an overview of the financial performance of the Group for the year ended 30 June 2020 as detailed in the financial report:

Summary of Group performance	Total	Total ⁽²⁾	% change
	30-Jun-20 \$million	30-Jun-19 \$million	
Sales Revenue	220.1	267.4	(17.7%)
Cost of goods and services sold	(153.9)	(183.5)	(16.1%)
Gross margin	66.2	83.9	(21.2%)
Other operating costs	(53.5)	(74.3)	(27.9%)
Underlying segment EBITDA⁽¹⁾	12.6	9.7	30.9%
Statutory net loss before tax	(6.2)	(14.4)	57.2%
Tax (expense) / benefit	-	5.6	>100%
Statutory net loss after tax (NPAT)	(6.2)	(8.8)	29.9%
Cash flows from operating activities	22.0	(4.0)	>100%
Net debt⁽³⁾	8.2	28.4	71.1%

(1) Hills' Financial Report complies with Australian Accounting Standards and International Financial Reporting Standards. The underlying (non-IFRS) segment EBITDA is unaudited but is derived from the audited accounts by removing the impact of non-recurring items from the reported (IFRS) audited profit; including restructure costs (\$1.2 million), foreign exchange losses of (\$4.1 million) and other items (\$1.5 million). Hills believe this reflects a more meaningful measure of the Group's underlying performance.

(2) Prior period has not been adjusted to reflect the sale of 3 business units. Further detail can be found in note 2.1, Segment information, of the audited financial statements.

(3) Net debt excludes lease liabilities associated with the introduction of AASB16 Leases. For further information refer Note 4.6, Financial instruments: Measurement and risk management, of the audited financial statements.

NOTE: numbers may not add due to rounding.

Hills Limited

Directors' report

For the year ended 30 June 2020

Revenue

Sales revenue for the year ended 30 June 2020 was down 18%, from \$267.4 million to \$220.1 million which includes the impact of the decision to divest the AV, Antenna and STEP businesses which were completed in December 2019, from our Distribution business.

Sales for the continuing Distribution and Health businesses were down \$16.2 million, or 8%, as a result of COVID-19 for both the Health and the continuing Distribution.

The Company now has a clear focus on our streamlined distribution business whilst investing to support further growth in our Health business.

Net loss

The FY20 net loss of \$6.2 million was impacted by a number of one-off items largely comprised of FX adjustments as well as redundancies. The underlying business performance was a continuation of improved financial results over recent years despite the challenges impacting the business through COVID-19. Underlying EBITDA of \$12.6 million significantly improved over prior year.

Operating expenses, inclusive of \$8.6 million depreciation and amortisation have declined significantly during the year to \$62.1 million down \$18.8 million or 23% from \$80.9 million with reductions achieved across all 3 major expense areas and includes the impact of the business exits completed in December 2019 and the ongoing cost reduction programs.

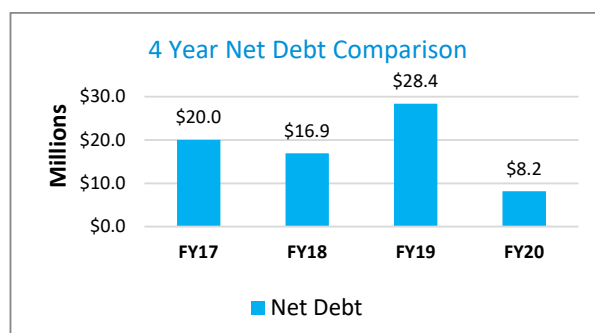
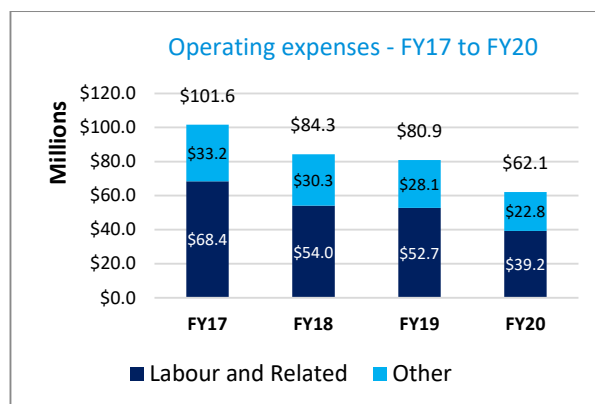
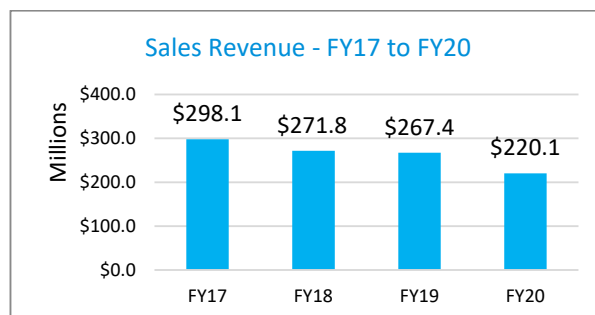
Labour and related costs reduced by \$13.5 million, or 25.6% reflecting the impact of the business exits and cost reductions programs, \$3m in JobKeeper and \$1.5m in temporary wage reductions from employees during Q4.

Net finance expenses of \$3.6 million compares favourably with prior year (\$3.3 million) when the impact of \$0.7 million related to the introduction of AASB16 Leases is excluded, reflecting the reduction in net debt.

Financial Position

Excluding the lease liability introduced into the balance sheet on adoption of AAB16 Leases, net debt is down to \$8.2 million at 30 June 2020, from \$28.4 million as at 30 June 2019. The Group maintained a focus on managing working capital balances and the cashflow benefits from the business exits in December.

The improved net debt position was supported by an operating cash inflow for the year of \$22.0 million, this includes the benefit of COVID-19 related government subsidies including JobKeeper and \$3.8 million in deferred GST payments. This net cash inflow compares to a net cash outflow in the previous corresponding period of \$4.0 million.



Hills Limited

Directors' report

For the year ended 30 June 2020

COVID-19

The coronavirus pandemic (COVID-19) has presented challenges for the Group as the business environment in the markets we service adjust to a new operating norm. During this period the board and management has focused on three priorities; looking after our people; continuing to deliver the highest level of products and services to our customers and partners; and managing the economic and social impacts caused by the COVID-19 crisis. Risk mitigation strategies and actions taken include:

- Implementing safeguards to ensure all our employees have safe working environments with no adverse impact on productivity or work ethic.
- Receipt of \$3.0 million JobKeeper assistance from the Australian government and similar assistance New Zealand government.
- Reducing salaries from April to June 2020 across the Company to preserve cashflow which resulted in a saving of approximately \$1.5 million (for further information refer to the Remuneration Report).
- Maintaining a strong focus on our sales, expenses and cashflow with implementation of weekly Board and management reviews.
- Focusing on our business continuity plans, to ensure our services and products continued to be available to all our customers, while also protecting the safety of customers, suppliers and our own people.

The Company has continued to trade, having been considered an essential service provider on the basis of the customers we service in the health care and security markets. Notwithstanding the decline in sales, up to the date of this report there has been no noticeable change in customer payment behaviour and there have been no specific instances of COVID-19 related bad or doubtful trade receivables.

The provision for Expected Credit Loss (bad debts) and inventory provisions have been reviewed and reflect the current and expected future economic environment and we are confident the provisions we have in place are appropriate at this time.

Outlook - Opportunities and strategy

Whilst we have seen unprecedented times over the past 6 months the Company is confident its strategy to:

- Continue building a health services business remains our strategic priority;
- Actively explore growth opportunities informed by the strategic review that is currently underway in Health with Paxton Partners; and
- Continue to deliver further business improvement and profitability from our value-added distribution business.

Material business risks

While trading in July was encouraging, the medium-term economic outlook remains clouded by the significant uncertainty created by the COVID-19 pandemic. However, with a strong pipeline in Health and a sharpened focus on higher-margin growth in the Distribution business, Hills is confident of delivering sustainable earnings growth over the medium to long-term.

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.

Hills utilises foreign exchange contracts to cover purchases of products from overseas, usually for planned purchases over a three to four month period. During the year, in an effort to protect Hills forward purchasing capability, finance personnel took out longer term foreign exchange contracts; outside of both policy and practice. A full review of the circumstances is being undertaken.

Due to exchange rate movements, Hills incurred a mark-to-market loss of \$4.085 million in FY20 on ineffective foreign exchange hedges, with a potential for further losses or gains in FY21 depending on exchange rate movements. In response to this, management and the Board have established strategies to mitigate further losses.

Directors qualification and experience

The directors of the Company at any time during or since the end of the financial year are as follows:

Director	Experience
Jennifer Helen Hill-Ling LLB (Adel) FAICD <i>Chairman and Non-Independent Director</i> Special responsibilities Chairman of the Board Member of the Nomination and Remuneration Committee.	Experience and expertise Appointed Director in August 1985. Appointed Deputy Chairman in June 2004. Appointed Chairman 28 October 2005. Ms 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. Other current listed company directorships None. Former listed company directorships in last 3 years None.
Fiona Rosalyn Vivienne Bennett BA (Hons) FCA FAICD <i>Independent Non-Executive Director</i> Special responsibilities Chairman of the Audit, Risk and Compliance Committee.	Experience and expertise Appointed non-executive Director on 31 May 2010. Ms 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 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 and a director of Select Harvests Limited and BWX Limited. She was formerly a director of Beach Energy Limited. Other current listed company directorships Director of BWX Limited (since November 2019) Director of Select Harvests Limited (since July 2017) Former listed company directorships in last 3 years Director of Beach Energy Limited (retired in November 2017)
Philip Bullock AO BA, MBA, GAICD, Dip. Ed. <i>Independent Non-Executive Director</i> Special responsibilities Chairman of the Nomination and Remuneration Committee; Member of the Audit, Risk and Compliance Committee	Experience and expertise Appointed non-executive Director on 23 June 2014. 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 and Managing Director of IBM Australia and New Zealand. Mr Bullock AO is a former non-executive director of Perpetual Limited, Healthscope Limited and CSG Limited. He has also provided advice to the Federal Government, through a number of organisations, most notably as Chair of Skills Australia. Other current listed company directorships None. Former listed company directorships in last 3 years Non-executive director of Perpetual Limited

Hills Limited
 Directors' report
 For the year ended 30 June 2020

Director	Experience
<p>Kenneth James Dwyer BCom, GMQ, GAICD <i>Independent Non-Executive Director</i></p> <p>Special responsibilities Member of the Nomination and Remuneration Committee; Member of the Audit, Risk and Compliance Committee</p>	<p>Experience and expertise Appointed non-executive Director on 20 September 2016 Mr Dwyer formerly worked in banking, including investment banking in the US and Australia specialising in M&A, debt and equity funding. 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. 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>David Chambers BSC, Dip Bus Mgt <i>Independent Non-Executive Director</i></p> <p>Special responsibilities None</p>	<p>Experience and expertise Appointed non-executive Director on 8 July 2020 Mr Chambers has more than 30 years of international experience in the healthcare and technology sectors and recently retired as the Managing Director of Asia Pacific operations at Allscripts Healthcare Solutions Inc., a Nasdaq-listed global leader in healthcare information technology. He is a former chief executive of ASX-listed health software business Pro Medicus Limited and has worked in senior executive roles in Australia, the US, Europe and Asia. He is currently chairman of ASX-listed healthcare software provider Mach7 Technologies Ltd.</p> <p>Other current listed company directorships Chair of Mach7 Technologies Ltd.</p> <p>Former listed company directorships in last 3 years None.</p>
<p>David John Joseph Lenz <i>Executive Director</i> Special responsibilities Chief Executive Officer</p>	<p>Experience and expertise Appointed Managing Director 19 February 2019 and Chief Executive Officer on 1 September 2016. 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. Mr Lenz was appointed Chief Executive Officer of Hills on 1 September 2016 and Managing Director and Chief Executive Officer on 19 February 2018.</p> <p>Other current listed company directorships None.</p> <p>Former listed company directorships in last 3 years None.</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 Hills. 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.

Directors interests

	As at 30 June 2020			At the date of this report		
	Shares held	Options held	Rights held	Shares held	Options held	Rights held
J Hill-Ling ⁽¹⁾	18,346,677	-	-	18,346,677	-	-
F Bennett	378,444	-	-	378,444	-	-
P Bullock AO	300,000	-	-	300,000	-	-
K Dwyer	450,000	-	-	450,000	-	-
D Lenz	503,787	-	162,242	503,787	-	162,242

(1) 18,346,677 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).

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 2020, 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	17	17	-	-	5	5
F Bennett	17	17	4	4	-	-
P Bullock AO	17	17	4	4	5	5
K Dwyer	17	17	4	4	5	5
D Lenz	17	17	-	-	-	-

(1) Number of meetings held during the period that the Director held office as a Director or was a member of the Committee.

Environmental regulation

Manufacturing

Hills ceased to operate a manufacturing facility at O'Sullivan Beach in South Australia from 20 February 2020, following the divestment of the Antenna business in December 2019. No significant environmental incidents were reported during the 2020 financial year and Hills continued to meet the requirements specified in relevant licenses and authorisations.

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 June 2020

Hills Limited

Directors' report

For the year ended 30 June 2020

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.

Dividends

No dividend has been proposed or paid since the start of the year.

Remuneration report

The Remuneration report set out on pages 15 to 29 forms part of the Directors report for the year ended 30 June 2020.

Corporate governance statement

Details of the Company's corporate governance practices are included in the Corporate Governance Statement set out on the Company's website.

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 30.

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 2020

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. 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:

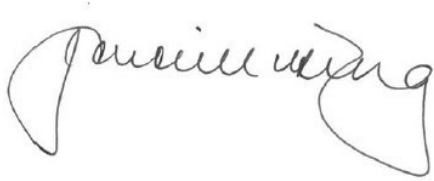
	2020	2019
	\$	\$
KPMG audit and non-audit services		
Audit and other assurance services		
KPMG Australia – audit and review of the financial statements	263,000	288,000
Overseas KPMG firms – audit and review of the financial statements	43,500	43,500
Total remuneration for audit and other assurance services	306,500	331,500
KPMG Australia – other assurance services	-	-
Total remuneration for audit and other assurance services	306,500	331,500
Taxation services		
KPMG Australia – taxation and other services	900	15,425
Overseas KPMG firms – taxation services	-	4,619
Total remuneration for taxation services	900	20,044
Other services		
Other consulting services	-	2,285
Total remuneration for other services	-	2,285
Total remuneration of KPMG	307,400	353,829

Hills Limited
Directors' report
For the year ended 30 June 2020

Subsequent events

Subsequent to balance date, there have been further exchange rate movements impacting the company's foreign exchange hedges, amounting to a mark-to-market loss of \$2.3 million, based on exchange rates immediately prior to the release of these financial statements. This amount has not been adjusted in the reported consolidated statement of profit and loss. Management and the Board have established strategies to minimise further losses.

There were no other events subsequent to balance date that would have a material effect on the Group's financial statements at 30 June 2020.



Jennifer Hill-Ling
Director



Philip Bullock AO
Director

Sydney
31 August 2020

Remuneration report

Letter from the Chairman of the Nomination and Remuneration Committee

On behalf of your Board, I am pleased to present Hills' FY20 Remuneration Report which sets out remuneration information for the Chief Executive Officer and Managing Director (CEO and 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 370 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 all 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. Over the last 3 years, approximately 70-80% of these measures have been financial as we have tried to guide Hills through a transition to a more profitable and sustainable business.

We believe this approach provides alignment to our shareholders and importantly, clarity to our executives by setting expectations regarding what the Board feels are acceptable targets

FY20 Remuneration Outcomes

Following the outbreak of the COVID-19 pandemic, our full year financial objectives did not meet our expectations and hence variable incentives payments were significantly reduced.

At the conclusion of FY19, we believed that the team had put in place a strategy that would show much improved profit performance in FY20. In addition we were further buoyed by a strong July 2019.

Hence, in an effort to deliver a profitable 1H FY20 and cement the FY19 improvements, our FY20 scorecard included specific financial targets for the 1H FY20 as well as full year financial and non-financial objectives.

As it turned out our 1H FY20 delivered very positive results with a significant improvement in NPAT for the 1H, up from \$0.242 million in 1H FY19 to \$2.636 million in 1H FY20. Our Distribution business returned to profit, and our Hills Health Solutions division continued to deliver strong profit contributions. In addition, the executive had embarked on further streamlining our Distribution business with the sale of our Audio Visual, Antenna and STEP business units.

As a result we were pleased to provide 1H bonuses to our CEO and CFO of approximately 30% of their full year potential incentive.

At the same time, while financial performance is critical, we continued to focus on our employee development during the 1H FY20, through activities such as:

- A strategy workshop for all senior and middle managers in August 2019 to align business stakeholders and management, helping to consolidate a high-performance culture and to identify tactical opportunities and initiatives for immediate attention and action.
- Coaching and mentoring of senior managers as part of Hills succession and retention planning.
- A schedule of ongoing compliance training for all employees was continued with the training focused on employee roles and responsibilities. Some of the more recent compliance training programs that were completed during the abovementioned period included:
 - o Workplace Bullying and Harassment
 - o Code of Conduct
 - o Travel & Entertainment
 - o Securities Trading
 - o Competition and Consumer Law
 - o IT Security.

As we moved into 2H FY20 we knew we had a strong opportunity to deliver a positive NPAT, restart dividends and set Hills on a path of greater profitability.

Unfortunately, COVID-19 brought some challenges to Hills, just as it did for many organisations. We anticipated that our distribution revenues would fall as new large projects were deferred or cancelled and our health business would be impacted as elective surgery was

Hills Limited

Directors report

For the year ended 30 June 2020

stopped and hospitals emptied in preparation for potential COVID-19 patients. We had a choice, stand down or retrench employees or ask our employees to take a reduction in their salaries and hopefully weather the storm.

To their enduring credit, our employees chose to take a reduction in their wages for the 3-month period from 1st April to the 30th June. These reductions were as follows:

- Directors, 50% reduction
- Senior Executives, 35% reduction
- Other employees, 25% to 10% reductions, depending on their salary (lower paid employees were not asked to reduce their salaries).

At the same time Hills applied for and received JobKeeper support for our approximately 350 employees from the Australian Federal Government. and support from a similar program from the New Zealand Government.

These combined measures contributed over \$4 million in reduced costs during this period, and helped retain jobs for our employees through to 30 June. We were naturally very appreciative of the support from Australian and New Zealand Governments and together with the generosity of our employees, they played a significant role in helping Hills manage the 2H FY20 and allowed Hills to prepare for a post COVID-19 world as we move into FY21.

These are extraordinary times, and while Hills was not alone in reducing wages, the fact that our employees chose to reduce their take home pay, is a great tribute to them as individuals, the culture that has developed throughout Hills and the leadership of our executives and managers.

We could not be prouder of the team.

FY20 CEO & MD Remuneration:

With the appointment of David Lenz from September 2016, we adopted a new market-based compensation framework. In FY2020 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 remuneration with the results of the Company and hence our shareholders. After a strong turnaround in FY18, we lifted the CEO Variable Pay from \$200,000 to \$250,000 from 1 September 2018. As in the past, the Variable Pay to be determined as a result of the performance of Hills over the FY2019 and paid 50% in cash and 50% in Performance Rights (unless the Board determines otherwise). The performance rights vest 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 in FY20 were as follows:

Element	Measure
Financial (80%)	<ul style="list-style-type: none">• Net Profit After Tax (NPAT) (Full Year)• Deliver Technology Distribution Trading Profit in 1H and H2• Reduction in Aged Inventory
Non-Financial (20%)	<ul style="list-style-type: none">• Employee Engagement• Board Discretion

As outlined earlier, our 1H FY20 demonstrated a strong turnaround in NPAT, and our Distribution Business returned to profitability. We were pleased to reward our CEO and CFO for this performance.

Primarily, because of the COVID-19 environment, our second half and full year financial objectives were not met. In addition, Hills had benefitted from Government support, as a result management and the Board agreed that no 2H bonuses or unpaid full year bonuses would be paid.

Hills Limited

Directors report

For the year ended 30 June 2020

Despite the challenges of FY20, the Board was extremely grateful for the tireless effort and leadership displayed by our executive team. Finally, there are no plans to amend the CEO Base Pay nor Variable Incentive components of his remuneration for FY21.

Non-Executive Director Remuneration:

Effective 1 July 2019, Non-Executive Director (NED) compensation was 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 Chair from \$16,000 to \$10,000
- The Remuneration and Nomination Committee Chair Fee of \$16,000 was removed.
- The Audit Committee Membership fee of \$6,000 was removed.

With the outbreak of COVID-19 the Board agreed to reduce its fees by 50% from 1 April 2020. For example non-executive fees would reduce from \$60,000 to \$30,000 p.a.

FY21 Outlook

Setting targets in a COVID-19 environment is a difficult process as the marketplace is changing and the “new business” conditions are not clear. As a result, we have opted to put in place the full year framework (scorecard), as we have done in prior years and will revisit its appropriateness at the conclusion of 1H FY21.

Hence the scorecard for our CEO is as follows:

Element	Measure
Financial (80%)	<ul style="list-style-type: none">• FY2021 Net Profit After Tax (NPAT)• Reduce Working Capital• Reduce Aged Inventory
Non-Financial (20%)	<ul style="list-style-type: none">• Improve Employee Engagement• Board Discretion

The variable incentive targets for our CFO are closely linked with those of the CEO but also include a focus on reducing our debtors outstanding. Division Heads are rewarded primarily on profit contribution for their division.
Thank you for taking the time to review the FY20 Remuneration Report.

This is my last report prior to stepping down from the Hills Board and retiring from all public company boards and I wanted to thank our shareholders for taking the time to read these reports, their feedback and importantly the patience they have shown.

Finally I would like to conclude by thanking my fellow Committee members for their support and a special message of thanks to the employees of Hills for their ongoing loyalty and dedication to our customers and suppliers, you have and continue to make a significant difference for Hills in the marketplace.

Thank you.



Philip Bullock AO

Chairman

Remuneration report

The directors of Hills Ltd (“Hills” the “Company”, or the “consolidated entity”) present the Remuneration Report prepared in accordance with section 300A of the Corporations Act 2001 (“the Act”) for the consolidated entity for the year ended 30 June 2020.

This Remuneration Report which forms part of the Directors Report outlines the remuneration strategy, framework and practices adopted by Hills in accordance with the requirements of the Act and its regulations. The information provided in the Remuneration Report has been audited as required by Section 308 (3C) of the *Corporations Act 2001*.

This report details remuneration information pertaining to directors and executives who are the “Key Management Personnel” (“KMP”) of Hills. KMP are defined as those persons having authority and responsibility for planning directing and controlling the activities of the consolidated entity.

The Remuneration Report comprises the following sections:

- 1 Key Management Personnel
- 2 Remuneration Governance
- 3 Executive Remuneration
- 4 Executive Contracts and Termination Arrangements
- 5 Remuneration Outcomes of MD & CEO and Senior Executives
- 6 Remuneration Outcomes of Non-Executive Directors’
- 7 Equity Instrument Disclosures Relating to Key Management Personnel

Abbreviations used in this report

Act	Corporations Act 2001 (cth)	FY	Financial year
AGM	Annual General Meeting	1H	First Half
ASX	Australian Stock Exchange	2H	Second Half
CEO & MD	Chief Executive Officer & Managing Director	KMP	Key Management Personnel
CFO	Chief Finance Officer	KPI	Key Performance Indicator
ED	Executive director	NED	Non-executive director

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

1. Key Management Personnel

The following non-executive directors (“NEDs”) and executives have been identified as KMP for the purpose of this report.

Name	Position	Term as KMP in FY20
Non-executive 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. Retirement will be effective at the conclusion of the Hills 2020 AGM.
K Dwyer	Independent, Non-Executive Director	Full Year
Executive director and 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. Resigned 7 May 2020
A Hall	Head of Health Solutions	Full Year

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

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 Remuneration & Nomination 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 retained.

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.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

3. Executive Remuneration

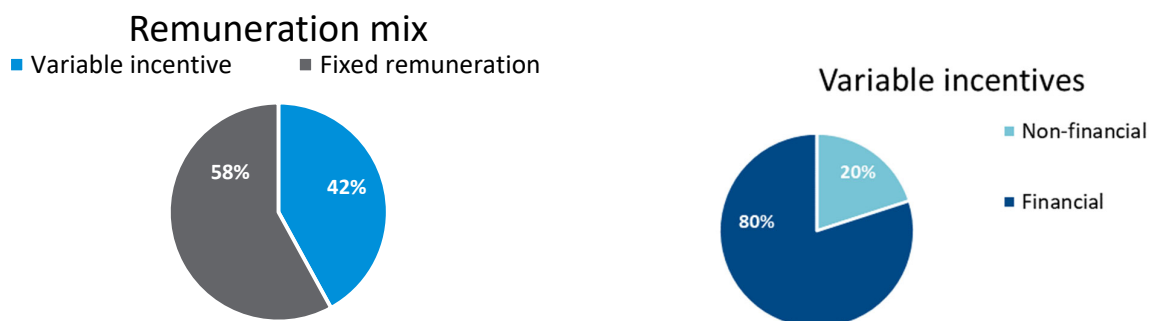
3.1 Alignment of Remuneration Strategy with Business Strategy

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

To achieve this alignment, senior executive remuneration is comprised of Fixed Remuneration (made up of base salary and superannuation), and variable incentive.

The CEO & MD remuneration is 58% Fixed remuneration and 42% Variable Incentive. Variable Incentive is assessed against financial measures (80%) and non-financial measures (20%) as illustrated below:



Other executives have a split of approximately 60-80% Fixed Remuneration and 20-40% Variable Incentive, dependent on their role.

3.3 Chief Executive Officer and Managing Director Remuneration

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

The CEO & MD, Mr David Lenz has a fixed remuneration of \$350,000 per annum (inclusive of superannuation). There have been no changes to his base salary since his appointment on 1st September 2016. However, for the 3 months ended 30 June 2020, Mr Lenz took a 35% temporary salary reduction in response to the COVID-19 pandemic.

Variable Incentive FY20

Mr Lenz had a variable incentive opportunity of up to \$250,000. The variable incentive for FY20 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 (80%)	<ul style="list-style-type: none">• Net Profit After Tax (NPAT) (1H and Full Year)• Deliver Technology Distribution Trading Profit in 1H and Full Year• Reduction in Aged Inventory
Non-Financial (20%)	<ul style="list-style-type: none">• Employee Engagement• Board Discretion

Weighting is distributed across these measures.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

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.

3.4 Senior Executive Remuneration FY20

There were no changes to the fixed remuneration of the named senior executives; however, in immediate response to the COVID-19 pandemic, for the 3-month period ended 30 June 2020 each executive took a 35% temporary salary reduction.

Variable Incentive FY20

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. Each senior executive has specific objectives which are relevant to the divisions in which they operate or tied to the overall company performance.

The variable incentive performance period was from 1 July 2019 to 30 June 2020.

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.

The following table summarises the potential FY20 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 FY20 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 FY20 were delivered as cash payments following approval by the Board. Details of Variable Incentive payments are provided in section 3.5.

3.5 FY20 Variable Incentive Performance and Outcomes

FY20 has been a year of contrasting performances as we moved from 1H to 2H due to the impact of COVID-19.

At the conclusion of 1H FY20:

- NPAT for the first half was up from \$0.242 million (1H FY19) to \$2.636 million (1H FY20) (>100%)
- The distribution business had returned to profitability
- We had further stream-lined the Distribution business with the sale of the Audio Visual, Antenna and STEP businesses and,
- Hills Health and Hills Technical Service continued to deliver strong profit outcomes.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

However, our 2H FY results did not perform to our expectations. This was due largely to the COVID-19 pandemic. Our distribution business was impacted through deferral or cancellation of larger projects and our Health Solutions business saw revenues decline through lower numbers of elective surgery and the deferral and cancellation of some Nurse Call projects.

As a result, while our FY20 EBITDA showed stronger year on year results our major FY financial targets (NPAT and inventory reductions) were not achieved, thus reducing the level of variable incentive paid. Specifically, given the overall 2H performance and the level of Government support, the Board and Management agreed that no 2H bonuses nor any unpaid FY bonuses would be paid.

	Target Variable Incentive opportunity	% of fixed remuneration	Financial outcome	Non-financial outcome	Total variable Incentive outcome	Achieved	Forfeited
	\$	%	\$	\$	\$	%	%
Executive Director							
D Lenz	250,000	71%	75,000	-	75,000	30%	70%
Senior Executive							
C Jacka	150,000	61%	45,000	-	45,000	30%	70%
D Fox	80,000	29%	-	-	-	-	100%
A Hall	137,500	50%	-	-	-	-	100%
R Edgar	72,000	30%	28,800	-	28,800	40%	60%
Total	689,500		148,800	-	148,800		

Please Note:

1. The financial outcome of the variable incentive presented in the table above is inclusive of compulsory superannuation contributions.
2. Incentives paid to the CEO and CFO relate to performance achieved in the first half of FY20.

Further details of variable incentive payments are set out in section 5.1.

3.6 Five Year Snapshot – Business and Remuneration Outcomes

As described above in section 3.1, 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		FY20	FY19	FY18	FY17	FY16	FY15
Shareholder funds	\$000	44,640	52,357	61,308	60,931	69,077	136,600
Statutory net (loss) / profit	\$000	(6,156)	(8,826)	359	(7,932)	(68,305)	(85,780)
Basic (loss) / earnings per share	cents	(2.7)	(3.8)	0.2	(3.4)	(29.4)	(37.0)
Dividends	cents	-	-	-	-	-	2.1
Share price - as at 30 June	\$	0.165	0.180	0.230	0.155	0.245	0.455
Variable Incentive Payments - % of Target Opportunity ⁽¹⁾	%	22%	40%	30%	29%	19%	4%

- (1) The FY19 variable incentive payment % was driven by a significant over achievement in our Health Solutions segment. The CEO variable incentive payment was 17% of the potential for FY19.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

3.7 FY21 Variable Incentive Design for CEO & MD and senior executives

For FY2021 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 the CEO & MD 50% cash and 50% Performance Rights (unless determined otherwise by the Board).

The Performance Rights 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 measure.

Element	Measure
Financial 80% of variable incentive	(a) FY21 Net Profit After Tax (NPAT) (b) Reduce Working Capital (c) Reduce Aged Inventory
Non-financial 20% of variable Incentive	(a) Employee Engagement – 5%-point improvement on prior year (b) Board Discretion

Other executives had similar scorecards which reflect their specific roles.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

4. Executive Contracts and Termination Arrangements

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 commenced on 1 September 2016 for an initial term of 12 months, following which the Chief executive Officer will continue to be employed till either party provides notice.▪ Hills or the Chief Executive Officer & 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.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

5. Remuneration Outcomes of MD and CEO and Senior Executives

5.1 Remuneration tables

Details of the nature and amount of each element of remuneration of the Managing Director and each of the named senior executives are as follows:

	Short-term benefits			Long-term benefits	Post-employment benefits	Share-based payments	Total remuneration	Proportion of remuneration that is performance based %	Proportion of remuneration that consists of rights %
	Salary package ⁽¹⁾	Cash Bonus ⁽²⁾	Other short-term benefits ⁽³⁾	Long service leave ⁽⁴⁾	Superannuation benefits ⁽⁵⁾	Performance Rights ⁽⁶⁾			
	\$	\$	\$	\$	\$	\$	\$	%	%
2020									
D Lenz	303,415	75,000	13,541	10,442	24,494	10,686	437,578	17%	-
C Jacka	209,529	41,096	8,016	4,742	24,596	-	287,980	14%	-
D Fox	227,756	-	7,555	16,255	22,747	-	274,312	-	-
A Hall	244,310	-	3,198	4,081	24,588	-	276,177	-	-
R Edgar ⁽⁷⁾	215,070	26,301	-	-	23,096	-	264,467	0	-
	1,200,080	142,397	32,310	35,520	119,521	10,686	1,540,514	9%	1%
2019									
D Lenz	328,100	38,000	-	7,802	21,689	13,378	408,969	9%	3%
C Jacka	229,001	30,250	-	3,786	22,393	-	285,430	11%	-
D Fox	245,338	12,800	9,407	19,382	23,888	-	310,815	4%	-
A Hall	266,057	180,000	5,000	2,921	20,310	-	474,288	38%	-
R Edgar	247,115	11,250	8,443	242	22,476	-	289,526	4%	-
	1,315,611	272,300	22,850	34,133	110,756	13,378	1,769,028	15%	1%

Notes in relation to the remuneration table above.

- Salary package amounts include salary sacrificed superannuation.
- Cash bonus represents a variable incentive payment for performance during the respective financial year. It is paid in cash for all executives; in the case of the CEO and MD, 50% of the incentive payment is paid in Performance Rights which vest over a 3-year period (unless the Board determines otherwise). In FY20, the Board determined that incentive payments for the CEO and CFO would be paid in cash, based upon 1H performance. Further details about the variable incentive payments are set out in section 3 of this Remuneration report. The cash bonus amount is net of any superannuation required to be contributed by the Company.
- Other short-term benefits represent annual leave accrued but not taken.
- Long service leave accrued but not taken.
- Superannuation benefits include the amount required to be contributed by the Company and exclude amounts salary sacrificed.
- Performance right represents the value of the share rights expensed over the 3-year vesting period. Further details are set out below in section 5.2. The value does not represent cash received.
- Roger Edgar resigned on 7th May 2020.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

5.2 Variable performance benefits – Performance Rights

As described in section 3.3 above, the variable incentive opportunity available to the CEO & MD is generally paid 50% cash and 50% 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.

The cost of these equity settled transactions is determined by reference to the fair value at the date at which they are granted. The expense recognised for these equity settled performance rights is recognised over the vesting period.

No Performance Rights were awarded in respect of the current financial year. For the financial year ended 30 June 2019, Performance Rights to the value of \$19,000 were awarded; this represented 78,649 Rights. The grant date for this 2019 award was 30 August 2019. The first tranche, representing 20% of the award of the 2019 award vested on 30 June 2020 and the remaining tranches will vest on 30 June 2021 (30%) and 30 June 2022 (50%).

Performance Rights	Opening balance	Granted ⁽¹⁾	Vested ⁽²⁾	Forfeited	Closing balance
2020					
D Lenz	238,493	78,649	(154,900)	-	162,242
2019					
D Lenz	227,322	198,646	(187,475)	-	238,493

(1) The FY2019 grant of 78,649 performance rights is granted subsequent to year end and consequently the grant is recorded in the current financial year.

(2) The performance rights which vested during the current financial year are a comprises grants from the financial years, 2017, 2018 and 2019.

The Performance Rights which vested in the current financial year include grants from the 3 previous years as follows:

Performance Rights which vested during the year	Total grant	% vested	Number vested
2020			
FY2017 grant	159,152	50%	79,576
FY2018 grant	198,646	30%	59,594
FY2019 grant	78,649	20%	15,730
			154,900
2019			
FY2016 grant	200,000	50%	100,000
FY2017 grant ⁽¹⁾	159,152	30%	47,746
FY2018 grant ⁽¹⁾	198,646	20%	39,729
			187,475

- (1) Subject to the terms and conditions of the Plan Rules, these performance rights, representing the 2nd Tranche of the FY17 performance rights and the 1st Tranche of the FY18 performance rights, representing 87,475 rights were converted into 87,475 shares in the Company. (Refer section 7.1, Share Holdings for a reconciliation of 87,475 rights which converted into 87,475 shares).

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

6. Remuneration Outcomes of Non-Executive Directors

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 fee which includes any statutory superannuation contributions. Non-executive directors do not receive any performance-based pay.

6.1 Fee Pool and Board fee reduction

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.

Board fee reductions were adopted in FY20; however, in response to the economic downturn due to the COVID-19 pandemic, an additional 50% fee reduction was agreed commencing 1 April 2020. The table below sets out the reductions to Board and committee fees:

	Chair fee \$	Member fee \$	Chair fee \$	Member fee \$	Chair fee \$	Member fee \$
	From 1st April 2020	From 1st April 2020	1 Jul 2019 to 31 Mar 2020	1 Jul 2019 to 31 Mar 2020	2019	2019
Board	50,000	30,000	100,000	60,000	160,000	80,000
Audit and Risk Committee	5,000	-	10,000	-	16,000	8,000
Nomination and Remuneration Committee	-	-	-	-	16,000	-

6.2 Non-executive Directors' remuneration details

	Fees	Non-monetary benefits \$	Superannuation \$	Total remuneration \$	Proportion of remuneration that consists of rights %
2020					
J Hill-Ling	80,611	-	25,000	105,611	-
F Bennett	58,869	-	3,009	61,878	-
P Bullock AO	48,367	-	4,595	52,962	-
K Dwyer	48,859	-	4,642	53,501	-
	236,706	-	37,246	273,952	-
2019					
J Hill-Ling	146,120	-	13,880	160,000	-
F Bennett	87,672	-	8,328	96,000	-
P Bullock AO	94,978	-	9,022	104,000	-
K Dwyer	80,366	-	7,634	88,000	-
A Kinkade ⁽¹⁾	22,761	-	2,162	24,923	-
	431,897	-	41,026	472,923	-

(1) Mr Kinkade resigned from the Board 19 June 2019.

6.3 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.

Directors report

Remuneration report (Audited) – continued

For the year ended 30 June 2020

7. Equity Instrument Disclosures Relating to Key Management Personnel

7.1 Share Holdings

The number 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.

Effective 1 July 2018. The Board has adopted a practice requiring each Director to acquire (directly or indirectly) Hills securities over a reasonable period having regard to fluctuations in share price to an approximate value equivalent to one year's director's fees (post tax). For newly appointed directors, this period will commence from the date of appointment.

	Balance at start of the year	Received during the year on the exercise of rights	Other changes during the year	Balance at the end of the year
Ordinary shares				
Non-executive directors				
J Hill-Ling	18,246,677	-	100,000	18,346,677
F Bennett	178,444	-	200,000	378,444
P Bullock AO	300,000	-	-	300,000
K Dwyer	350,000	-	100,000	450,000
	19,075,121	-	400,000	19,475,121
Senior-executives				
D Lenz ⁽¹⁾	231,830	87,475	184,482	503,787
D Fox	833,888	-	666,112	1,500,000
C Jacka	-	-	50,000	50,000
A Hall	-	-	393,246	393,246
	1,065,718	87,475	1,293,840	2,447,033

(1) The shares acquired during the year on exercise of Performance rights relate to the conversion of the 2nd Tranche of the FY17 performance rights and the 1st Tranche of the FY18 performance rights. Refer to section 5.2 for further details.

7.2 Loans to Key Management Personnel

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

7.3 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.



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 2020 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
KPMG

A handwritten signature in black ink, appearing to read 'Paul Cenko'.

Paul Cenko
Partner
Adelaide
31 August 2020

Consolidated financial statements

for the year ended 30 June 2020

Contents

Financial statements

Consolidated statement of profit or loss	Page 32
Consolidated statement of comprehensive income	Page 33
Consolidated statement of financial position	Page 34
Consolidated statement of changes in equity	Page 35
Consolidated statement of cash flows	Page 36

Notes to the consolidated financial statements

Section 1: Basis of preparation	Page 37
---------------------------------	---------

Section 2: Business performance

2.1 Segment information	Page 39
2.2 Revenue	Page 41
2.3 Other income	Page 41
2.4 Expenses	Page 42
2.5 Finance income and expenses	Page 44
2.6 Income tax	Page 45
2.7 Earnings per share	Page 49

Section 3: Operating assets and liabilities

3.1 Cash and cash equivalents	Page 50
3.2 Trade and other receivables	Page 51
3.3 Inventories	Page 53
3.4 Trade and other payables	Page 53
3.5 Property, plant and equipment	Page 54
3.6 Leases	Page 55
3.7 Intangible assets	Page 57
3.8 Provisions	Page 58

Section 4: Capital and financing

4.1 Contributed equity	Page 59
4.2 Reserves	Page 60
4.3 Dividends	Page 61
4.4 Borrowings	Page 61
4.5 Derivative financial instruments	Page 63
4.6 Financial instruments: Measurement and	

Section 5: Group structure

5.1 Interests in other entities	Page 73
5.2 Parent entity financial information	Page 74

Section 6: Unrecognised items

6.1 Contingencies	Page 77
6.2 Commitments	Page 77

Section 7: Other

7.1 Share-based payments	Page 79
7.2 Related party transactions	Page 80
7.3 Events after the reporting period	Page 81
7.4 Remuneration of auditors	Page 81
7.5 New and amended accounting standards and interpretations	Page 82

Signed reports

Directors' declaration	Page 84
Independent auditor's report	Page 85

ASX information

Shareholder information	Page 90
Corporate directory	Page 92

Consolidated statement of profit or loss

For the year ended 30 June 2020

	Notes	2020 \$'000	2019 \$'000
Revenue	2.2	220,083	267,362
Cost of sales	2.4	(153,919)	(183,488)
Gross Margin		66,164	83,874
Other income	2.3	115	551
Expenses excluding net finance expenses			
Labour and related expenses	2.4	(39,239)	(52,733)
Operational and equipment expenses	2.4	(3,664)	(6,322)
Property expenses	2.4	(1,427)	(7,596)
Depreciation and amortisation	2.4, 3.5	(8,554)	(6,617)
Other expenses	2.4	(15,964)	(22,306)
Expenses excluding net finance expenses		(68,848)	(95,574)
Loss before net finance expense and income tax		(2,569)	(11,149)
Finance income	2.5	51	121
Finance expenses	2.5	(3,638)	(3,386)
Net finance expenses	2.5	(3,587)	(3,265)
Loss before income tax		(6,156)	(14,414)
Income tax benefit / (expense)	2.6	-	5,588
Loss after tax		(6,156)	(8,826)
Total loss for the year attributable to members of the Company		(6,156)	(8,826)
Earnings per share		Cents	Cents
Basic and diluted profit/(loss) per share	2.7	(2.65)	(3.80)

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

Consolidated statement of comprehensive income

For the year ended 30 June 2020

		2020	2019
Other comprehensive income	Notes	\$'000	\$'000
Loss for the year		(6,156)	(8,826)
Items that may be reclassified subsequently to profit or loss			
Foreign operations - foreign currency translation differences		(400)	260
Cash flow hedges - effective portion of changes in fair value		(387)	(198)
Income tax relating to components of other comprehensive income	2.6	175	-
Other comprehensive (loss) / income for the year, net of tax		(612)	62
Total comprehensive income / (loss) for the year, attributable to owners of Hills Limited		(6,768)	(8,764)

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

Consolidated statement of financial position

As at 30 June 2020

	Notes	2020 \$'000	2019 \$'000
ASSETS			
Current assets			
Cash and cash equivalents	3.1	12,236	10,867
Trade and other receivables	3.2	40,136	59,194
Inventories	3.3	25,178	41,636
Total current assets		77,550	111,697
Non-current assets			
Investments		2	2
Property, plant and equipment	3.5	12,276	15,281
Right-of-use asset	3.6	10,821	-
Intangible assets	3.7	3,749	2,072
Deferred tax assets	2.6	16,744	16,733
Total non-current assets		43,592	34,088
Total assets		121,142	145,785
LIABILITIES			
Current liabilities			
Trade and other payables	3.4	29,262	40,646
Lease liabilities	3.6	4,258	-
Borrowings	4.4	6,113	15,927
Provisions	3.8	5,627	8,731
Derivative financial instruments	4.5	4,578	106
Total current liabilities		49,838	65,410
Non-current liabilities			
Lease liabilities	3.6	9,645	-
Borrowings	4.4	14,300	23,331
Provisions	3.8	2,719	4,687
Total non-current liabilities		26,664	28,018
Total liabilities		76,502	93,428
Net assets		44,640	52,357
EQUITY			
Contributed equity	4.1	278,439	278,439
Reserves	4.2	10,527	11,128
Accumulated losses		(244,326)	(237,210)
Total equity		44,640	52,357

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

Consolidated statement of changes in equity

For the year ended 30 June 2020

	Attributable to owners of Hills Limited					Total \$'000
	Notes	Contributed equity	Equity compensation reserve	Translation & other reserves	Accumulated losses	
		\$'000	\$'000	\$'000	\$'000	
Balance at 1 July 2018		278,439	738	10,315	(228,184)	61,308
Adjustment on initial application of AASB9		-	-	-	(200)	(200)
Loss for the year ended 30 June 2019		-	-	-	(8,826)	(8,826)
Other comprehensive income		-	-	-	-	-
Foreign currency translation differences for foreign operations		-	-	260	-	260
Net change in fair value of hedges net of tax		-	-	(198)	-	(198)
Employee share schemes	2.4	-	13	-	-	13
Balance at 30 June 2019		278,439	751	10,377	(237,210)	52,357
Balance at 1 July 2019		278,439	751	10,377	(237,210)	52,357
Adjustment on initial application of AASB16	7.5	-	-	-	(960)	(960)
Loss for the year ended 30 June 2020		-	-	-	(6,156)	(6,156)
Other comprehensive income		-	-	-	-	-
Foreign currency translation differences		-	-	(400)	-	(400)
Net change in fair value of hedges net of tax		-	-	(212)	-	(212)
Employee share schemes	2.4	-	11	-	-	11
Balance at 30 June 2020		278,439	762	9,765	(244,326)	44,640

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

Consolidated statement of cash flows

For the year ended 30 June 2020

	Notes	2020 \$'000	2019 \$'000
Cash flows from operating activities			
Receipts from customers (inclusive of goods and services tax)		264,302	292,109
Payments to suppliers and employees (inclusive of goods and services tax)		(239,216)	(293,324)
		25,086	(1,215)
Net finance costs paid		(3,099)	(2,775)
Net income taxes paid		-	(14)
Net cash flows from / (used in) operating activities	3.1	21,987	(4,004)
Cash flows from investing activities			
Payments for property, plant and equipment		(1,670)	(2,646)
Payments for intangible assets		(2,494)	(3,019)
Proceeds from sale of property, plant and equipment and intangible assets		43	24
Proceeds from sale of business operations		7,324	-
Net cash flows from / (used in) investing activities		3,203	(5,641)
Cash flows from financing activities			
Proceeds from borrowings		2,506	7,650
Repayment of borrowings		(20,765)	(3,000)
Payment of lease liabilities		(4,535)	-
Net cash flows (used in) / from financing activities		(22,794)	4,650
Net increase / (decrease) in cash and cash equivalents		2,396	(4,995)
Cash and cash equivalents at the beginning of the year		10,867	15,783
Effects of exchange rate changes on cash and cash equivalents		73	79
Cash and cash equivalents at end of the year	3.1	12,236	10,867

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

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 1: Basis of Preparation

1.1. Reporting entity

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") for the year ended 30 June 2020 and were authorised for issue in accordance with a resolution of the Directors on 31 August 2020.

Hills Limited is a for profit company limited by shares, incorporated and domiciled in Australia whose shares are publicly traded on the Australian Securities Exchange.

The Group operates in Australia and New Zealand and the Principal activities of the Group is as a supplier of technology solutions in the Health market and a value-added distributor of technology products and services in the Security, Surveillance and IT markets.

1.2. Basis of accounting

These general purpose consolidated financial statements:

- are presented in Australian dollars, which is the Company's functional and presentation currency;
- 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 4.6.

1.3. What's new in this report

- AASB16 *Leases* has been applied for the first time; the impact of which is described in notes 3.6 Leases and 7.5 New and amended accounting standards and interpretations.
- Segment information has been restated to align with reports used by the Chief Operating Decision Maker's (CODM) to assess business performance, determine the allocation of resources and strategic decision making within the Group. The segments, Hills Health Solutions, Hills Distribution and Corporate are described in note 2.1, Segment information. Prior period information has been restated where relevant.

1.4. Going Concern

The consolidated financial statements have been prepared on a going concern basis. The Company's existing \$18.3 million facility with AssetSecure (the Facility) expires on 31 July 2021. The Company is in advanced discussions with the existing financier and alternate financiers to either extend or refinance the Facility. The Board are confident the Facility will be extended or refinanced with similar terms and conditions before its expiry

1.5. 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. 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 2.6	Tax losses for which a deferred tax asset has been recognised
Note 3.3	Net realisable value of inventory
Notes 3.6 & 7.5	Leases and New and amended accounting standards and interpretations
Notes 3.5 and 3.7	Measurement of the useful lives of property, plant and equipment and intangible assets
Notes 3.8 and 6.1	Provisions and contingencies
Note 4.6	Financial instruments: Measurement and financial risk management

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

1.6. Principles of consolidation

Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of the Company as at 30 June 2020 and the results of all subsidiaries for the year then ended. A list of subsidiaries is included in note 5.1.

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.

1.7. 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.

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.

1.8. 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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 2: Business performance

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

- 2.1 Segment information
- 2.2 Revenue
- 2.3 Other income
- 2.4 Expenses
- 2.5 Finance income and expenses
- 2.6 Income tax
- 2.7 Earning per share

2.1. Segment information

Description of segments

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses. The operating segments operating results are reviewed regularly by the Chief Operating Decision Maker (CODM) to assess performance of the business and to make decisions about resources to be allocated to the segment.

Segment results that are reported to the CODM include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. The Group has three reportable segments as summarised below:

Hills Health Solutions	A market leader and comprises the design, supply and installation of health technology solutions, nurse call and patient engagement and other related solutions including security, Wi-Fi and telephony into the health and aged care sectors.
Hills Distribution	The Distribution business provides a diverse range of products and solutions to assist our customers support end users within the Antenna, Audio Visual, Satellite, Security, Surveillance and IT markets. The AV, Antenna and STEP businesses were divested in December 2019.
Corporate	This includes Group costs not allocated to Health or Distribution.

Segment information

Segment revenue

The revenue from external customers reported to the 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 2.2.

Major customers

The Group did not derive 10% or more of its revenues from any single external customer.

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 goodwill and other intangible asset impairments when the impairment is the result of an isolated, non-recurring event and business combination acquisition transaction costs which, although expensed under IFRS, are considered to otherwise distort the operational view of the business.

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Information about reportable segments

	Distribution		Health		Corporate		Total Continuing operations		Operations divested (the "Disposal group")		Total operations	
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Sales revenue	164,169	175,966	33,723	38,103	-	-	197,892	214,069	22,191	53,293	220,083	267,362
Underlying segment EBITDA	5,738	129	8,553	10,974	(2,649)	(2,664)	11,642	8,439	999	1,180	12,641	9,619
Depreciation and amortisation	(5,418)	(4,284)	(3,114)	(2,102)	-	-	(8,532)	(6,386)	(22)	(231)	(8,554)	(6,617)
Redundancy, restructure and transformation costs	-	-	-	-	(1,197)	(1,902)	(1,197)	(1,902)	-	-	(1,197)	(1,902)
Onerous lease provision	-	-	-	-	-	(2,500)	-	(2,500)	-	-	-	(2,500)
Inventory provision	-	-	-	-	-	(3,800)	-	(3,800)	-	-	-	(3,800)
Impairment of non-current assets	-	-	-	-	-	(6,500)	-	(6,500)	-	-	-	(6,500)
Foreign exchange losses	-	-	-	-	(4,085)	-	(4,085)	-	-	-	(4,085)	-
Other income	-	-	-	-	115	551	115	551	-	-	115	551
Other expense	-	-	-	-	(1,489)	-	(1,489)	-	-	-	(1,489)	-
Net financing expense	-	-	-	-	(3,587)	(3,265)	(3,587)	(3,265)	-	-	(3,587)	(3,265)
Net profit /(loss) before income tax	320	(4,155)	5,439	8,872	(12,892)	(20,080)	(7,133)	(15,363)	977	949	(6,156)	(14,414)
	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019	2020	2019
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Segment assets												
Trade and other receivables	35,300	42,315	4,836	7,671	-	-	40,136	49,986	-	9,208	40,136	59,194
Inventory	20,158	27,014	5,020	7,047	-	-	25,178	34,061	-	7,575	25,178	41,636
Property plant and equipment	3,064	3,585	9,212	11,102	-	-	12,276	14,687	-	594	12,276	15,281
Intangible assets	2,420	872	1,329	1,200	-	-	3,749	2,072	-	-	3,749	2,072
	60,942	73,786	20,397	27,020	-	-	81,339	100,806	-	17,377	81,339	118,183
Corporate and unallocated assets					39,803	27,602	39,803	27,602	-	-	39,803	27,602
Total assets	60,942	73,786	20,397	27,020	39,803	27,602	121,142	128,408	-	17,377	121,142	145,785

Note: Prior period segment information has been restated to ensure consistency with current operating segments; Hills Health Solutions, Hills Distribution and Corporate.

As a result of AASB16, corporate assets include Right of Use Assets of \$10.821 million (2019: nil).

Divested Operations

In December 2019 the Group divested three businesses within the Hills Distribution segment; AV, Antenna Business and STEP businesses (collectively the Disposal Group) thereby reducing exposure to non-performing assets and reducing the overall complexity of the business. The businesses sold were not a major line of business and do not represent a discontinued operation.

The sale of the Disposal Group comprised sale of specific assets and liabilities, with Hills retaining the trade receivable and trade creditor balances at the disposal date. The sale resulted in a net loss of \$0.250 million, which is incorporated within Other Expenses (refer note 2.4).

There were no divestments in the prior period.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

2.2. Revenue

	2020	2019
	\$'000	\$'000
Sales revenue		
Sale of goods	172,430	215,133
Services	47,653	52,229
	220,083	267,362

Recognition and measurement

Revenue is recognised when performance obligations are satisfied, and the control of goods or services is transferred.

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

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 occurs 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. 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 at the point the performance obligation is completed. Amounts collected for services not yet provided are recorded as deferred revenue in the balance sheet.

2.3. Other income

	2020	2019
	\$'000	\$'000
Net gain/(loss) on disposal of non-current assets	44	(12)
Other income	71	563
	115	551

Net loss on disposal of non-current assets

The net gain on disposal of non-current assets for the year ended 30 June 2020 relates to gains on the sale of motor vehicles as well as furniture and fittings.

The net loss on disposal of non-current assets for the year ended 30 June 2019 related to the disposal of company owned vehicles.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

2.4. Expenses

Profit / (loss) before income tax includes the following specific expenses:

	2020	2019
	\$'000	\$'000
Cost of Sales		
Cost of goods sold (inventories)	135,037	163,657
Direct cost of services provided	18,882	19,831
Total cost of sales	153,919	183,488
Employee benefits expenses		
Wages and salaries	31,647	41,811
Superannuation contributions	2,351	2,999
Other employee benefit expense	1,956	1,975
Equity settled share-based payment transactions	11	13
Temporary staff and other costs	3,274	5,935
Total employee benefit expenses	39,239	52,733
Operational and equipment expenses		
Repairs and maintenance	816	1,712
Freight	2,309	3,663
Consumables / other	539	947
	3,664	6,322
Property expenses		
Occupancy Costs	860	6,779
Utilities	567	817
Total property expenses	1,427	7,596
Depreciation		
Plant and equipment	3,830	4,350
Right of use assets	4,278	-
Total depreciation	8,108	4,350
Amortisation		
Software	391	2,202
Development costs	55	65
Total amortisation	446	2,267
Total depreciation and amortisation	8,554	6,617
Other		
General and administrative expenses	8,946	7,598
Restructuring expenses	1,197	502
Loss on disposal of business	247	-
Foreign exchange losses - ineffective portion of changes in fair value	4,085	-
Other costs	1,489	14,206
Total Other	15,964	22,306

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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 and other labour and related expenses such as third-party logistics, labour hire, employee training and recruitment. The benefit of JobKeeper (\$3.190 million) and wage reduction (\$1.200 million) offset current year labour and related expenses.
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.
Depreciation and amortisation	Refer note 3.5 and 3.7.
Other expenses	<p>General and administrative expenses include overhead expenses (such as insurance, advertising and marketing, professional and consulting fees, telecommunications and information technology related expenses).</p> <p>Other costs include legal fees. Prior year Other costs of \$14.708 million include an impairment expense of \$6.500 million related to non-current assets, additional inventory provisions of \$3.800 million, an onerous lease provision of \$2.500 million as well as redundancy and restructure costs of \$1.902 million.</p>

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

2.5. Finance income and expenses

	2020	2019
	\$'000	\$'000
Interest and finance charges paid / payable	(2,216)	(2,018)
Amortisation of deferred borrowing costs	(489)	(489)
Lease finance costs	(678)	-
Other financing costs	(228)	(879)
Unwinding discount on provisions	(27)	-
Total finance expenses	(3,638)	(3,386)
Finance income		
Interest income	51	121
Net finance costs expensed	(3,587)	(3,265)

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

2.6. Income tax

Income tax expense

	2020	2019
	\$'000	\$'000
Income tax expense:		
Income tax (benefit) / expense comprises:		
Current tax	-	-
Deferred tax	-	(5,588)
	-	(5,588)
Numerical reconciliation of income tax (benefit) / expense to prima facie tax payable:		
Profit / (loss) from continuing operations before income tax expense	(6,156)	(14,414)
Tax at the Australian tax rate of 30% (2019: 30%)	(1,847)	(4,324)
Tax effect of amounts which are not deductible / (taxable) in calculating taxable income:		
Non-deductible expenses	58	181
Acquisition costs	-	1
(Recognition) / derecognition of deferred tax assets	(4,480)	(1,739)
Tax losses for which no deferred tax asset is recognised	6,269	292
Total income tax expense / (benefit)	-	(5,589)
Difference in overseas tax rates	-	1
Total income tax expense / (benefit)	-	(5,588)
	2020	2019
	\$'000	\$'000
Income tax expense relating to items of other comprehensive income:		
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	175	-
Aggregate income tax benefit	175	-

Income tax receivable / (payable)

Income tax receivable / (payable) is nil. (2019: nil)

Notes to the consolidated financial statements (continued)
For the year ended 30 June 2020

Deferred tax assets and liabilities

	Balance at 1 July	Recognised in profit or loss	Recognised in other comprehensive income	Balance at 30 June
	\$'000	\$'000	\$'000	\$'000
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
Exchange differences	-	343	23	366
	11,122	5,588	23	16,733
Movements 2020				
Property, plant and equipment	5,692	(2,065)	-	3,627
Inventories	6,092	(2,930)	-	3,162
Employee benefits	1,665	(321)	-	1,344
Receivables	146	(301)	-	(155)
Payables	-	(225)	-	(225)
Provisions	2,426	(1,249)	-	1,177
Other accruals	314	(27)	-	287
Derivative financial instruments	32	1,166	175	1,373
Other	366	321	-	687
Tax losses	-	5,467	-	5,467
	16,733	(164)	175	16,744

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Unrecognised tax losses

The Company has estimated tax losses across the Group as follows:

	Jurisdiction	
	Australia \$AUD'000	New Zealand \$NZD'000
Non-recognised tax losses - revenue items		
Balance at the beginning of the period	206,943	775
Movement during the period	(293)	2,925
Balance at the end of the period	206,650	3,700
Non-recognised tax losses - capital items		
Balance at the beginning of the period	31,012	-
Movement during the period	-	-
Balance at the end of the period	31,012	-
Total revenue and capital losses not recognised	237,662	3,700
Total potential tax benefit	71,299	1,036
Rate of income tax	30%	28%

Revenue and capital tax losses do not expire under current legislation but must continue to satisfy the requirements of the relevant tax legislation relating to continuity of ownership and same business test.

Revenue losses Deferred tax assets related to revenue losses have been recognised in respect of the period over which the Group expects to utilise the benefits of these losses; which is a 3-year to 5-year time horizon.

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.

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.

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.

Tax funding agreement

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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.

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

2.7. Earnings per share

	2020	2019
	\$'000	\$'000
Earnings used in calculating earnings per share		
Basic and diluted loss - attributable to the ordinary equity holders of the Company	(6,156)	(8,826)
	2020	2019
	Number	Number
Weighted average number of shares used as denominator		
Issued ordinary shares	231,985,526	231,985,526
Effect of performance rights on issue	-	-
Weighted average number of ordinary shares used as the denominator	231,985,526	231,985,526
	2020	2019
	Cents	Cents
Basic and diluted earnings per share		
Attributable to the ordinary equity holders of the Company	(2.65)	(3.80)

Recognition and measurement

Basic earnings per share

Basic earnings per share is calculated by dividing:

- 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 on issue during the reporting period

Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- 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 on issue assuming the conversion of all dilutive potential ordinary shares

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 3: Operating assets and liabilities

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

- 3.1 Cash and cash equivalents
- 3.2 Trade and other receivables
- 3.3 Inventories
- 3.4 Trade and other payables
- 3.5 Property, plant and equipment
- 3.6 Leases
- 3.7 Intangible assets
- 3.8 Provisions

3.1. Cash and cash equivalents

	2020 \$'000	2019 \$'000
Cash at bank and in hand	3,752	6,427
Short term deposits	8,484	4,440
	12,236	10,867
Reconciliation of cash flows from operating activities		
Loss for the period	(6,156)	(8,826)
Adjustments to reconcile loss to net cash flows:		
Depreciation and amortisation	8,554	6,617
Net loss / (gain) on sale of non-current assets	(44)	12
Impairment of property plant and equipment / intangibles	-	6,500
Impairment of inventories	(390)	3,800
Share-based payments	11	13
Amortisation of capitalised borrowing costs	489	489
Fair value adjustment on derivatives	4,085	-
Unwinding of discount on provisions	27	-
Other non-cash items	(210)	3,900
<i>Change in operating assets and liabilities:</i>		
Decrease / (increase) in trade and other receivables	20,129	(392)
Decrease / (increase) in inventories	8,396	(1,720)
Decrease in trade and other payables	(10,239)	(8,163)
Increase in provisions	(2,665)	(633)
(Increase) / decrease in deferred tax assets	-	(5,601)
Net cash flows from/(used in) operating activities	21,987	(4,004)

There has been a significant decrease in trade and other receivables, inventory and payables. This is principally due to the divestment of three business units as described in note 2.1 Segment information and lower receivables correlating with the lower sales in the fourth quarter of FY20 as a result of the COVID-19 pandemic.

Recognition and measurement

Cash and cash equivalents

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

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.2. Trade and other receivables

	2020 \$'000	2019 \$'000
Trade receivables	31,137	50,682
Less: Provision for impairment of receivables	(683)	(487)
	30,454	50,195
Other receivables	8,477	7,092
Prepayments	1,205	1,907
	40,136	59,194

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

Not past due	17,719	31,136
Past due 0 – 30 days	6,168	8,067
Past due 31 – 90 days	4,613	8,016
Past due more than 90 days	2,637	3,463
Total trade receivables	31,137	50,682

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

At 1 July	487	402
Adjustments on adoption of AASB 9	-	200
Provision for impairment recognised / (released)	313	(27)
Receivables written off during the period as uncollectable	(117)	(88)
At 30 June	683	487

Trade receivables

Impairment

The provision for impaired receivables for the Group is \$0.683 million (2019: \$0.487 million).

The Group uses an allowance for credit loss matrix to measure the Expected Credit Loss (ECL) of trade receivables which incorporates an aging analysis as well as case by case assessment of receivables where appropriate.

Management has specifically reassessed trade receivables and the adequacy of the ECL in light of the COVID-19 pandemic and its expected future economic impact. Up to the 30 June 2020 reporting date, management has not observed any material change in the payment behaviour of customers and the ageing profile of trade receivables, consequently COVID-19 has not had a significant impact on the ECL provisions. The Group has however anticipated in its ECL provision calculations, the possibility of a future adverse impact.

Credit insurance has been in place for several years, which should if required reduce any impact of COVID-19 related default.

Transfer of trade receivables

The Group has entered a Receivables Purchase Facility, as described in note 4.4 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 shown below:

	2020 \$'000	2019 \$'000
Carrying amount of trade receivables transferred	20,210	36,708
Amount drawn down under facility	(18,305)	(32,303)

The amount drawn down under the Asset Secure facility forms part of total borrowings (Note 4.4).

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Other receivable and prepayments

Other receivables include \$1.200 million in respect of the JobKeeper subsidy.

Prepayments of \$1.205 million relates to insurance, subscriptions and software licences.

Financial risk

Refer note 4.6 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 are non-derivative financial instruments that 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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.3. Inventories

	2020 \$'000	2019 \$'000
Raw materials and work in progress	1,755	3,060
Finished goods	26,842	46,836
Total inventory	28,597	49,896
Less provision	(3,419)	(8,260)
Net inventory	25,178	41,636
Movements in the provision for impairment of inventory is as follows:		
At 1 July	(8,260)	(4,370)
Provision for impairment recognised	(2,868)	(4,150)
Provision utilised during the period	7,709	260
At 30 June	(3,419)	(8,260)

Key estimate: Carrying value of inventory

The assessment of the carrying value of inventory requires management judgement based on experience and industry practice. Management reassesses the carrying value when there are indications of a change in economic circumstances that may impact the inventory.

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.

3.4. Trade and other payables

	2020 \$'000	2019 \$'000
Trade payables	19,576	29,095
Other payables and accrued expenses	9,686	11,551
	29,262	40,646

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.5. Property, plant and equipment

	2020 \$'000	2019 \$'000
Property plant and equipment - at cost	54,740	65,796
Less accumulated depreciation	(42,464)	(50,515)
Total property plant and equipment	12,276	15,281
Reconciliation of movement		
Opening balance	15,281	14,915
Additions	1,202	5,193
Depreciation	(3,830)	(4,350)
Disposals	(104)	(36)
Exchange differences	31	63
Impairment	(304)	(504)
Closing balance	12,276	15,281

Impairment testing

The Group has undertaken impairment testing over its cash generating units at 30 June 2020. The Group has two cash generating units being Hills Health Solutions and Hills Distribution. The recoverable value of cash generating units was determined in accordance with the value in use methodology. Cash flows are forecast for five years after which a terminal value calculated. No impairment has been identified at 30 June 2020. Significant assumptions used to determine value in use are:

- Forecast cash-flows are based on Board approved budgets.
- Post tax discount rate: 10.2%
- Terminal growth rate: 2.5%

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):

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.6. Leases

Amounts recognised in the statement of financial position	Year end 30/06/2020 \$'000	Transition 1/07/2019 \$'000
Right-of-use asset		
Buildings	9,500	15,293
Plant, machinery and equipment	1,321	1,928
Total right-of-use assets	10,821	17,221
Reconciliation of movement		
Opening balance	-	
Balance on adoption of AASB16 with effect from 1 July 2019	17,221	
Transfer: Onerous lease provision on transition	(1,814)	
Transfer: Lease incentive on transition	(1,110)	
Additions	802	
Depreciation charge for the year	(4,278)	
Closing balance	10,821	
Lease liabilities		
Current	4,258	5,580
Non-current	9,645	12,601
Total lease liabilities	13,903	18,181
Maturity analysis - undiscounted		
Less than one year	4,258	
One to five years	9,904	
More than five years	-	
Total undiscounted lease liabilities at 30 June 2020	14,162	
Amounts recognised in the statement of profit or loss	2020 \$'000	2019 \$'000
Interest on lease liabilities	(678)	-
Depreciation of right-of-use asset	(4,278)	-
Lease payments relating to leases of low value and short-term leases not included in lease liabilities	(193)	-
Amounts recognised in the statement cash flows	2020 \$'000	2019 \$'000
Total cash outflow for leases	(4,535)	-

The Group leases various offices, warehouses, equipment and vehicles.

Prior to adoption of AASB16 Leases on 1 July 2019, leases were accounted for by applying the principles of AASB117 *Leases*, which classified arrangements as either finance leases or operating leases.

On 1 July 2019, the Group transitioned to AASB16 *Leases* using the modified retrospective approach and therefore the comparative information has not been restated and the cumulative effect of initial application is recognised in retained earnings at 1 July 2019.

When measuring lease liabilities for leases that were previously classified as operating leases, the Group discounted lease payments using a borrowing rate of 4.6%.

In the comparative period the Group applied AASB117 *Leases* and only lease arrangements that the Group had were considered to be operating leases and therefore the lease payments were recognised in profit and loss on a straight-line basis over the term of the lease.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Impact on transition

. Further information regarding the impact of the transition to AASB16 on the Group is disclosed in Note 7.5.

Policy applicable from 1 July 2019

At the inception of a lease arrangement, the Group assesses whether a contract is, or contains, a lease which will be the case if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

At inception or modification of a contract that contains a lease the Group recognises a right-of-use asset and a lease liability. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying assets or to restore the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate and the Group determined its incremental borrowing rate by obtaining indicative interest rates from its lenders.

The lease liability is subsequently measured at amortised cost using the effective interest rate method. It is remeasured when there is a change in future lease payments arising from a change in index or rate or if the Group changes its assessment of whether it will exercise an extension option.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of use asset has been reduced to zero.

Short term and low value leases

The Group has elected to not recognise a right-of-use asset and lease liability for short term and low value leases. For these leases the Group recognises the lease payments as an expense on a straight-line basis over the lease term. (refer note 6.2, Commitments).

Key estimate: lease term and discount rate

The assessment of the lease term and discount rate requires management judgement based on past experience and industry practice. Management reassess the lease terms and discount rates when there are indications of a change in economic circumstances that may impact the assets.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.7. Intangible assets

	2020 \$'000	2019 \$'000
Intangible assets - at cost	25,728	27,317
Less accumulated amortisation	(21,979)	(25,245)
Total intangible assets	3,749	2,072
Reconciliation of movement		
Opening balance	2,072	6,267
Additions	2,566	4,068
Amortisation	(446)	(2,267)
Disposals	(393)	-
Impairment	(50)	(5,996)
Closing balance	3,749	2,072
Comprising		
Software	1,801	219
Development	1,948	1,853
Closing net book value	3,749	2,072

Additions of \$2.566 million (2019 \$4.068 million) include \$1.300 million related to the Digital transformation of Hills website to offer customers online sales, product information, customer portals etc. Other additions included Microsoft Dynamics software to enhance sale and customer experience, an upgrade to the Inventory management systems and other Business intelligence tools.

Key estimate: useful lives of intangible assets

The assessment of the useful lives of intangible assets 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

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 2 to 5 years.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

3.8. Provisions

	2020 \$'000	2019 \$'000
Current		
Employee benefits	3,779	4,657
Warranty claims	436	573
Restructuring	1,194	1,672
Environmental and other	218	1,829
Total provisions - current	5,627	8,731
Non-current		
Employee benefits	569	604
Warranty claims	142	351
Restructuring	44	284
Environmental and other	1,964	3,448
Total provisions - non-current	2,719	4,687
Total provisions	8,346	13,418
Reconciliation of movement - Employee benefits		
Opening net book amount	5,261	5,562
Provisions made during the year	8,568	9,990
Provisions used during the year	(9,481)	(10,291)
Total employee benefits provision	4,348	5,261
Reconciliation of movement - Warranty claims		
Opening net book amount	924	1,205
Provisions made during the year	-	245
Provisions used during the year	(165)	(83)
Write back of unused provisions	(181)	(443)
Total outstanding warranty claims provision	578	924
Reconciliation of movement - Restructuring		
Opening net book amount	1,956	786
Provisions made during the year	931	1,885
Provisions used during the year	(1,649)	(320)
Write back of unused provisions	-	(395)
Total restructuring provision	1,238	1,956
Reconciliation of movement - Environmental and other		
Opening net book amount	5,277	2,588
Provisions made during the year	57	3,247
Provisions used during the year	(1,338)	(290)
Transfer of onerous lease to Right of Use Asset	(1,814)	-
Write back of unused provisions	-	(268)
Total environmental and other provisions	2,182	5,277
Total provisions	8,346	13,418

Employee provisions	Provisions for employee benefits include liabilities for annual leave and long service leave.
Warranty claims	Warranty provisions includes amounts set aside for estimated warranty claims associated with the existing product range of \$0.150 million as well as legacy products of \$0.427 million.
Restructuring provision	Includes \$0.931 million related to redundancy and outplacement services and other costs associated with closing and restructuring businesses.
Environmental and other provisions	Includes environmental monitoring and clean-up costs associated with several sites in South Australia.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Recognition and measurement

Provisions

Provisions for service warranties and make good obligations are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. 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 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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 4: Capital and financing

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

- 4.1 Contributed equity
- 4.2 Reserves
- 4.3 Dividends
- 4.4 Borrowings
- 4.5 Derivative financial instruments
- 4.6 Financial instruments: Measurement and financial risk management

4.1. Contributed equity

	2020 Number	2019 Number	2020 \$'000	2019 \$'000
Ordinary shares - fully paid	231,985,526	231,985,526	278,439	278,439

Ordinary shares

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.

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

4.2. Reserves

	2020 \$'000	2019 \$'000
Hedging reserve - cash flow hedges	(345)	(133)
Equity compensation reserve	762	751
Foreign currency translation reserve	(23)	377
Profits reserve	10,133	10,133
Total reserves	10,527	11,128
Reconciliation of movement		
Hedging reserve – cash flow hedges		
Opening balance	(133)	65
Revaluation	(212)	(198)
Closing balance	(345)	(133)
Equity compensation reserve		
Opening balance	751	738
Employee share plan expense / (credit)	11	13
Closing balance 30 June	762	751
Foreign currency translation reserve		
Opening balance	377	117
Currency translation differences arising during the year	(400)	260
Closing balance	(23)	377
Profits reserve		
Opening balance 1 July	10,133	10,133
Closing balance	10,133	10,133

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

4.3. Dividends

	2020 \$'000	2019 \$'000
Dividends	-	-
Franking credits available	1,787	1,787

No dividends were paid during the year and no final dividend has been declared.

Franking credits available for subsequent reporting periods are based on an income tax rate of 30% (2019: 30%). The franking credits 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.

4.4. Borrowings

	2020 \$'000	2019 \$'000
Current		
Borrowings	6,113	15,927
Total current borrowings	6,113	15,927
Non-current		
Borrowings	14,725	24,245
Less capitalised borrowing costs	(425)	(914)
Total non-current borrowings	14,300	23,331
Total borrowings	20,413	39,258
Reconciliation of movement		
Opening balance	39,258	32,696
Proceeds from loans and borrowings	2,506	7,650
Repayment of borrowings	(21,840)	(3,000)
Amortisation of capitalised borrowing costs	489	489
New finance leases	-	1,423
Closing balance	20,413	39,258

Capitalised transaction costs are directly attributable to the borrowings, as at 30 June 2020, unamortised borrowing costs totalled \$0.425 million (2019: \$0.914 million).

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Bilateral Facility	<p>The CBA facility was amended in May 2020 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 \$27.000 million (denominated in AUD), with funding provided based upon the Group's accounts receivable book. The facility is secured on the Group's Accounts Receivable book, with a second mortgage over the other assets of the Group. Interest is charged at prevailing market rates plus a fixed margin.</p> <p>The facility expires on 31 July 2021, discussions are however progressing with multiple financiers with a view to extending the current facility or replacing it with a new facility.</p>
DLL Financing	<p>The DLL financing facility was established to provide finance within the Hills Health Solutions business for patient entertainment equipment at hospital locations. The facility incorporates a Progressive Payment Agreement (PPA), an interest only facility to support cashflow as the equipment is installed.</p> <p>Upon installation of the equipment, the PPA is replaced by a set term Chattel Mortgage which is repaid progressively over a 5-year term.</p> <p>At 30 June 2020, the Group had drawn down \$2.302 million. (2019: \$3.374 million)</p>

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 4.6, 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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

4.5. 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 4.6).

	2020 \$'000	2019 \$'000
Derivative financial instruments	(4,578)	(106)
Comprising		
Cash flow hedge	(400)	(106)
Foreign exchange loss	(4,178)	-
Closing balance	(4,578)	(106)
Reconciliation of movement		
Opening balance	(106)	93
Foreign exchange movements	(4,472)	(199)
Closing balance	(4,578)	(106)

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 2020, no gain or loss was recognised in profit or loss for the ineffective portion of these hedging contracts (2019: nil), however \$0.212 million loss, net of tax (2019: loss of \$0.198 million) was recognised in the statement of comprehensive income.

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. Changes in the fair value of these contracts is taken directly to the profit and loss.

During the year, foreign exchange contracts beyond the normal three to four month time frame were taken out for the purpose of mitigating exchange fluctuations.

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 fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

4.6. Financial instruments: Measurement and Financial risk management

Classification and measurement

The carrying values of financial assets and liabilities of the Group approximate their fair value.

The Group measures and recognises in the statement of financial position on a recurring basis certain assets and liabilities at fair value in accordance with AASB 13 Fair Value Measurement. The fair value must be estimated for recognition and measurement in accordance with the following 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
As at 30 June 2020				
Assets				
Derivatives financial instruments	-	-	-	-
Liabilities				
Derivatives financial instruments	-	(4,578)	-	(4,578)
	-	(4,578)	-	(4,578)
As at 30 June 2019				
Assets				
Derivatives financial instruments	-	-	-	-
Liabilities				
Derivatives financial instruments	-	(106)	-	(106)
	-	(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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Financial risk management

Framework

The Group is involved in activities which expose it to a variety of financial risks including:

- i. Capital risk management,
- ii. Credit risk,
- iii. Liquidity risk, and
- iv. Market risk related currency fluctuations, interest rates and commodity pricing.

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

Management identifies, evaluates and manages financial risks in close cooperation with the Group's business units. under policies approved by the Board.

The objective of the financial risk management strategy is to minimise the impact of volatility in financial markets on the financial performance, cash flows and shareholder returns. This requires the identification and analysis of relevant financial risks and possible impact on the achievement of the Groups objectives.

The Group normally uses derivative financial instruments such as foreign exchange contracts exclusively for risk mitigation and not as trading or other speculative instruments. During the year, foreign exchange contracts beyond the normal three to four month time frame were taken out to mitigate exchange rate fluctuations.

The Group holds the following financial instruments:

	2020 \$'000	2019 \$'000
Financial assets		
Cash and cash equivalents	12,236	10,867
Trade and other receivables	40,136	59,194
Investments	2	2
	52,374	70,063
Financial liabilities		
Trade and other payables	29,262	40,646
Lease liabilities	13,903	-
Borrowings	20,413	39,258
Derivative financial instruments	4,578	106
	68,156	80,010

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).

The identified financial risks are discussed below.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

(i) 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:

net debt	Net debt	Total borrowings as shown in the consolidated statement of financial position less cash and cash equivalents
net debt + total equity	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 of less than 40%. For comparability purposes the gearing ratio set out below as at 30 June 2020 has been calculated inclusive and exclusive of the additional lease liabilities introduced into the balance sheet following the adoption of AASB16 Leases (refer to notes 3.6 and 7.5):

	Note	2020 \$'000	2019 \$'000
Total borrowings	4.4	20,413	39,258
Less: cash and cash equivalents	3.1	(12,236)	(10,867)
Net debt		8,177	28,391
Total equity		44,640	
Gearing ratio - excluding impact of AASB16 Lease		15.5%	35.2%
Total lease liabilities	3.6	13,903	
Net debt adjusted to include lease liabilities		22,080	
Gearing ratio - including lease liabilities calculated under AASB16		33.1%	

(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>

The ageing of the Group's trade receivables is analysed in note 3.2.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

(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 4.4. The Group had access to the following undrawn borrowing facilities from its bankers at the end of the reporting period:

	Note	2020 \$'000	2019 \$'000
Floating rate			
Expiring within one year (bank overdraft)		-	-
Expiring beyond one year (loans)		1,904	3,697
		1,904	3,697

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 \$'000
At 30 June 2020						
Trade and other payables	29,262	-	-	-	29,262	29,262
Borrowings	864	5,703	13,835	2,877	23,279	20,413
Lease liabilities	2,129	2,129	3,328	6,576	14,162	13,903
Derivative financial instruments	3,243	1,335	-	-	4,578	4,578
Total	35,498	9,167	17,163	9,453	71,281	68,156
At 30 June 2019						
Trade and other payables	40,646	-	-	-	40,646	40,646
Borrowings	1,878	1,878	38,235	2,807	44,798	39,258
Derivative financial instruments	79	-	-	-	79	106
Total	42,603	1,878	38,235	2,807	85,523	80,010

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

(iv) 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 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. The Group's main foreign exchange risk exposure is to US dollars. Group Entities and business units are required to hedge their foreign exchange risk exposure using forward exchange contracts.

The Group's policy is to hedge approximately three to four months of anticipated cash flows (mainly purchases of inventories) in US dollars. During the year, foreign exchange contracts beyond this time frame were taken out to mitigate exchange rate fluctuations.

Interest rate risk Borrowings issued at variable rates expose the Group to interest rate risk. See details of the Group's borrowings in note 4.4.

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:

	Note	USD A\$'000	EUR \$'000	GBP \$'000	Total \$'000
30-Jun-20					
Cash at bank		1,851	-	-	1,851
Trade receivables		103	-	-	103
Trade payables		(10,960)	(419)	(11)	(11,390)
Forward exchange contracts ⁽¹⁾		(59,608)	-	-	(59,608)
30-Jun-19					
Cash at bank		33	-	-	33
Trade receivables		663	-	-	663
Trade payables		(11,424)	(314)	(36)	(11,774)
Forward exchange contracts		(9,421)	-	-	(9,421)

(1) Forward exchange contracts are presented at the gross cash flow amount and these USD contracts will be consumed over the next 6 to 9 months by USD purchases.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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 2020 and 2019, 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:

	2020		2019	
	Weighted average interest rate %	Balance \$'000	Weighted average interest rate %	Balance \$'000
Bank overdrafts and loans	4.38%	(20,413)	5.82%	(38,446)
Cash and cash equivalents	0.17%	12,236	1.32%	10,867
Other loans	2.33%	(234)	3.06%	(812)

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

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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 sensitivity of the Group's profit and loss and Other equity to a possible 100 basis point change in interest rates and a possible 5% strengthening or weakening in the US dollar exchange rate are shown in the table below. The analysis assumes that all other variables remain constant.

	Carrying amount \$'000	Interest rate risk		Foreign exchange risk			Other equity \$'000
		-100 bps Profit \$'000	+100 bps Profit \$'000	-5% Profit \$'000	Other equity \$'000	+5% Profit \$'000	
30-Jun-20							
Financial assets							
Cash and cash equivalents	12,236	(22)	155	206	-	(169)	-
Trade and other receivables	40,136			12	-	(9)	-
Total increase / (decrease) in financial assets		(22)	155	218	-	(178)	-
Financial liabilities							
Trade & other payables	(29,262)	-	-	(1,265)	-	1,035	-
Borrowings	(20,413)	219	(219)	-	-	-	-
Derivatives - cash flow hedges	(4,578)			2,492	422	(2,255)	(382)
Total increase / (decrease) in financial liabilities		219	(219)	1,227	422	(1,220)	(382)
Total increase / (decrease)		197	(64)	1,445	422	(1,398)	(382)
30-Jun-19							
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	1,078	(784)
Total increase / (decrease)		172	(127)	(1,239)	1,135	1,015	(784)

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 5: Group structure

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

- 5.1 Interests in other entities
- 5.2 Parent entity financial information
- 5.3 Deed of cross guarantee

5.1. Interests in other entities

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 controlled entities are a party to a Deed of Cross Guarantee between those group entities and the Company pursuant to ASIC Corporations (wholly owned Companies) Instrument 2016/785 and are not required to prepare and lodge financial statements and directors report (refer note 5.3). The Company and those group entities are the "Closed Group".

● 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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

5.2. Parent entity financial information

Summary financial information

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

	2020	2019
	\$'000	\$'000
Balance sheet		
Current assets	77,550	97,660
Non-current assets	44,702	42,924
Total assets	122,252	140,584
Current liabilities	45,064	81,665
Non-current liabilities	32,547	39,549
Total liabilities	77,611	121,214
Net assets	44,641	19,370
Shareholders' equity		
Contributed equity	278,439	278,439
Reserves		
Hedging reserve - cash flow hedges	(423)	(134)
Equity compensation reserve	762	751
Profits reserve	32,859	32,859
Retained earnings	(266,996)	(292,545)
Total equity	44,641	19,370
Loss for the year	(6,438)	(15,447)
Total comprehensive income	(25,549)	(15,245)

Parent entity guarantees, contingent liabilities and commitments

Guarantees	Bank guarantees given by the Company in favour of customers and suppliers amounted to \$2.062 million (2019: \$2.466 million). Cross guarantees are given by the Company and its wholly owned subsidiaries as described in note 5.3. 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 6.1. For information about guarantees given by the parent entity, please see above.
Contractual commitments	As at 30 June 2020, the Company had \$nil contractual commitments for the acquisition of plant, equipment or intangible assets (2019: \$2.061 million). These commitments are not recognised as liabilities as the relevant assets have not yet been received.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

5.3. Deed of cross guarantee

The Company and each of the wholly owned subsidiaries identified in note 5.1 are relieved from the *Corporations Act 2001* requirements for preparation, audit and lodgement of their financial report pursuant to *ASIC Corporations (Wholly-owned Companies) Instrument 2016/785*.

The Company and each of these subsidiaries have entered 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.

A summarised consolidated income statement, a summarised consolidated statement of comprehensive income, a summary of movements in consolidated retained earnings for the year ended 30 June 2020 and a summarised consolidated statement of financial position as at 30 June 2020 of the Company and controlled entities that are a party to the Deed (the Closed Group), after eliminating all transactions between parties is set out as follows:

	2020	2019
	\$'000	\$'000
Summarised consolidated income statement		
Revenue from continuing operations	209,905	251,566
Other income	67	533
Finance costs	(3,532)	(3,273)
Other expenses	(209,441)	(262,472)
Loss before income tax	(3,001)	(13,646)
Income tax expense	-	5,603
Profit/ (Loss) for the year	(3,001)	(8,043)
Summarised other comprehensive income		
<i>Items that may be reclassified to profit or loss:</i>		
Changes in the fair value of cash flow hedges	(387)	(198)
Income tax relating to these items	175	-
Other comprehensive profit / (loss) for the period, net of tax	(212)	(198)
Total comprehensive profit / (loss) for the year	(3,213)	(8,241)
Summary of movements in consolidated retained earnings		
Accumulated losses at the beginning of the reporting period	(241,029)	(232,786)
Adjustment on initial application of AASB 9	-	(200)
Adjustment on initial application of AASB 16	(842)	-
Profit / (Loss) for the year	(3,001)	(8,043)
Accumulated losses at the end of the reporting period	(244,872)	(241,029)

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

	2020	2019
Summarised statement of financial position	\$'000	\$'000
Current assets		
Cash and cash equivalents	10,952	9,935
Trade and other receivables	39,187	56,693
Inventories	22,359	37,879
Total current assets	72,498	104,507
Non-current assets		
Investments	814	814
Property, plant and equipment	12,118	14,969
Intangible assets	3,745	2,069
Deferred tax assets	16,322	16,295
Total non-current assets	32,999	34,147
Total assets	105,497	138,654
Current liabilities		
Trade and other payables	31,757	41,407
Borrowings	6,113	15,299
Provisions	5,399	8,522
Derivative financial instruments	4,578	106
Total current liabilities	47,847	65,334
Non-current liabilities		
Borrowings	12,896	22,555
Provisions	2,510	4,478
Total non-current liabilities	15,406	27,033
Total liabilities	63,253	92,367
Net assets	42,244	46,287
Equity		
Contributed equity	278,439	278,439
Reserves	8,677	8,877
Accumulated losses	(244,872)	(241,029)
Total equity	42,244	46,287

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 6: 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.

- 6.1 Contingencies
- 6.2 Commitments

6.1. Contingencies

The Group had contingent liabilities at 30 June 2020 in respect of:

Claims 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.

Three claims are the subject of legal expenses and these form part of Other costs as disclosed in note 2.4 to these financial statements. One claim relates to a dispute concerning a third-party contract. The other two claims are employee related. In all cases liability is denied and the Group is defending the claims.

Based on legal advice, 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 or the amount of the obligation cannot be measured with sufficient reliability.

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.

Guarantees Bank guarantees in favour of customers and suppliers totalling \$2.062million (2019: \$2.466million).

6.2. Commitments

	2020 \$'000	2019 \$'000
Capital commitments		
Plant, equipment and intangible assets	-	58
Lease commitments - Group as Lessee		
Commitments for minimum lease payments in relation to non-cancellable operating leases are payable as follows:		
Within one year	175	5,938
Later than one year but not later than five years	45	13,939
Later than five years	-	978
	220	20,855
Lease commitments - Group as Lessor		
Within one year	-	368
Later than one year but not later than five years	-	185
	-	553

Lease commitments due within one year represent short term and low value lease liabilities for which the Group elected to not recognise a right-of-use asset and lease liability. For these leases, the Group recognises the lease payments as an expense on a straight-line basis over the lease term.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Until the end of the comparative period, leases were accounted for by applying the principles of AASB117 *Leases*, which classified arrangements as either finance leases or operating leases and accordingly future lease commitments were disclosed. From 1 July 2019, the Group accounting policy changed so that leases are recognised by applying the principles of AASB16 *Leases*. Under the new standard, leases are recognised as right-of-use assets with a corresponding lease liability.

Refer to note 3.6 for further information.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Section 7: Other information

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:

- 7.1 Share-based payments
- 7.2 Related party transactions
- 7.3 Events after the reporting period
- 7.4 Remuneration of auditors
- 7.5 New and amended accounting standards and interpretations

7.1. Share-based payments

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).

The only current participant is the CEO and MD, Mr David Lenz.

Details of performance rights under the Incentive Share Plan are as follows:

Grant date	Expiry date	Share price at grant date \$	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
2020								
31/7/17	30/6/20	0.195	79,576	-	(79,576)	-	-	-
27/8/18	30/6/21	0.195	158,917	-	(59,594)	-	99,323	-
30/8/19	30/8/22	0.195	-	78,649	(15,730)	-	62,919	-
Total			238,493	78,649	(154,900)	-	162,242	-
2019								
1/9/16	1/9/18	0.340	100,000	-	(100,000)	-	-	-
31/7/17	30/6/20	0.195	127,322	-	(47,746)	-	79,576	-
27/8/18	30/6/21	0.195	-	198,646	(39,729)	-	158,917	-
Total			227,322	198,646	(187,475)	-	238,493	-

The fair value is assessed in accordance with AASB 2 *Share Based Payments* at the grant date of the performance rights.

Expenses arising from share-based payment transactions

Total expense arising from share-based payment transactions recognised during the period as part of employee benefit expense were \$10,686 (2019: \$13,378), as disclosed in note 2.4.

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

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

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 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.

7.2. Related party transactions

Non-Key management personnel disclosures

The Group has a related party relationship with its controlled entities (Note 5.1). The Company and its controlled entities engage in a variety of related party transactions in the ordinary course of business. These transactions are conducted on normal terms and conditions.

Loans

Group entity trading transactions and borrowings result in balances arising in respect of current and non-current assets and liabilities. These balances are eliminated in full on consolidation.

Transactions

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

Key management personnel disclosures

Key remuneration disclosures

	2020	2019
	\$	\$
Short-term employee benefits (fixed and variable incentive remuneration)	1,611,493	2,042,928
Post-employment benefits (superannuation)	156,767	151,886
Long term benefits (cash variable component under the Incentive Share Plan and accrued long service leave)	35,520	34,133
Termination benefits	-	-
Share-based payments (performance rights variable component under the Incentive Share Plan and employee share bonus plan expense)	10,686	13,378
	1,814,466	2,242,325

Detailed remuneration disclosures are provided in the Remuneration Report.

Loans and other transactions with Key Management Personnel

No KMP have loans to or from the Group (2019: nil).

During the current financial year, there were no related party transactions with KMP or their related entities (2019: nil).

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.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

7.3. Events after the reporting period

Subsequent to balance date, there have been further exchange rate movements impacting the company's foreign exchange hedges, amounting to a mark-to-market loss of \$2.3 million, based on exchange rates immediately prior to the release of these financial statements. This amount has not been adjusted in the reported consolidated statement of profit and loss. Management and the Board have established strategies to minimise further losses.

There were no other events subsequent to balance date that would have a material effect on the Group's financial statements at 30 June 2020.

7.4. 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:

	2020	2019
	\$	\$
KPMG audit and non-audit services		
Audit and other assurance services		
KPMG Australia – audit and review of the financial statements	263,000	288,000
Overseas KPMG firms – audit and review of the financial statements	43,500	43,500
Total remuneration for audit and other assurance services	306,500	331,500
KPMG Australia – other assurance services	-	-
Total remuneration for audit and other assurance services	306,500	331,500
Taxation services		
KPMG Australia – taxation and other services	900	15,425
Overseas KPMG firms – taxation services	-	4,619
Total remuneration for taxation services	900	20,044
Other services		
Other consulting services	-	2,285
Total remuneration for other services	-	2,285
Total remuneration of KPMG	307,400	353,829

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

7.5. New and amended accounting standards and interpretations

Newly effective standards for the year ended 30 June 2020 adopted by the Group

The following standards and interpretations became effective and were applied for the first time during the year ended 30 June 2020:

AASB2018-7 Amendments to accounting standards – Definition of material.	Clarifies the definition of material and its application across AASB Standards and other pronouncements. The principle amendments are to AASB101 Presentation of Financial Statements.
AASB2019 -1 Conceptual Framework	The Conceptual Framework for Financial Reporting is the foundation on which the IASB develops new accounting standards. The revised framework includes some new concepts, provides updated definitions and recognition criteria for assets and liabilities and clarifies some important concepts. The changes may affect the application of accounting standards in situations where no standard applies to a particular transaction or event.
AASB16 Leases	Effective 1 July 2019, the group adopted AASB16 Leases. As described in note 3.6, AASB16 introduced a comprehensive model for the identification and accounting treatments of lease arrangements for both lessors and lessees. AASB16 superseded AASB 117 Leases and the related interpretations when it became effective on 1 July 2019. AASB16 requires the recognition of lease liabilities and right of use assets in relation to leases which had previously been classified as operating leases under AASB117. Short-term leases (less than 12 months) and leases of low value assets (such as personal computers) are exempt from the lease accounting requirements.

Except for AASB16 Leases, these had no material impact on the Group's consolidated financial statements. The impact of AASB16 Leases is detailed below.

Adoption of AASB16 Leases – Impact

	Transition 1/07/2019 \$'000		
Right-of-use asset			17,221
Retained earnings- AASB16 transition adjustment			960
Lease Liabilities			(18,181)
<hr/>			
Operating lease commitments at 30 June 2019 as disclosed in the Group's consolidated financial statements			20,855
Discounted using the incremental borrowing rate at 1 July 2019			18,181
<hr/>			
	Property	Cars and forklifts	Total
	\$'000	\$'000	\$'000
Right-of-use assets			
Balance at 1 July 2019	15,293	1,928	17,221
Onerous lease adjustment	(1,814)	-	(1,814)
Lease incentive	(1,110)	-	(1,110)
Depreciation of right of use asset	(3,640)	(638)	(4,278)
Additions	771	31	802
Balance at 30 June 2020	9,500	1,321	10,821
<hr/>			
			Total \$'000
Lease liabilities			
Balance at 1 July 2019			18,181
Reduction in liability			(4,278)
Balance at 30 June 2020			13,903
<hr/>			
Comprising:			
Current lease liability			4,258
Non-current lease liability			9,645
Balance at 30 June 2020			13,903

When measuring lease liabilities for leases that were previously classified as operating leases, the Group discounted lease payments using a borrowing rate of 4.6%.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

New accounting standards and interpretations not yet adopted by the Group

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2020 reporting periods and have not been early adopted by the Group. The impact of these new standards and interpretations is not considered material.

Notes to the consolidated financial statements (continued)

For the year ended 30 June 2020

Directors' declaration

For the year ended 30 June 2020

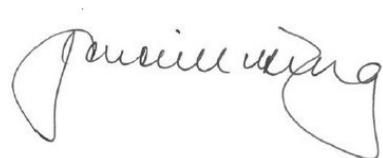
In the opinion of the Directors of Hills Limited (the Company):

- (a) the consolidated financial statements and notes set out on pages 31 to 83 and the Remuneration Report on pages 16 to 29 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 2020 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 5.1 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 1 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
31 August 2020



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 2020 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 2020;
- 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 ended 30 June 2020;
- 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 (including Independence Standards) (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:

- Valuation of finished goods inventory;
- Impairment assessment of non-financial assets; and
- 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.

Valuation of finished goods inventory (Finished goods - \$26.842 million, inventory provision \$3.419 million)

Refer to Note 3.3 to the Financial Report

The key audit matter

Valuation of finished goods inventory is a key audit matter due to the:

- Size of the finished goods inventory balance, which is significant to the Group's financial position (22% of total assets).
- Group's 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.
- Extent of judgement involved in determining the recoverable value, particularly in relation to slow moving and obsolete inventory.

The most significant areas of judgement we focused on was in assessing the Group's:

- Expected selling price of inventory.
- Ageing of inventory.
- Future inventory usage.

We involved our senior audit team members in assessing this key audit matter.

How the matter was addressed in our audit

Our procedures included:

- We assessed the appropriateness of the Group's accounting policies for the valuation of finished goods inventory against the requirements of the accounting standards and our understanding of the business.
- We attended cyclical stocktakes in significant locations which included observing the stocktake procedures, and the process of identifying slow moving and potentially obsolete inventory.
- We used 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.
- We obtained the calculation of the inventory provision and compared it to the Group's accounting policies, the Group's analysis of slow moving inventory and current year actual sales and usage.
- We assessed the level of provision in light of our understanding of the business and knowledge of the industry in which the Group operates.



Impairment assessment of non-financial assets

Refer to Note 3.5 to the Financial Report

The key audit matter

The impairment assessment using AASB 136 *Impairment of non-financial assets* is a key audit matter given the carrying amount of the net assets of the Group exceeded the Group's market capitalisation at year end, increasing the possibility of non-financial assets being impaired.

The Group has incurred a loss during the year, as a result of COVID-19 trading conditions, foreign exchange adjustments and inventory provisions. COVID-19 trading conditions have impacted the Group through a reduction in the demand for products and services and project deferrals.

We focussed on the significant forward looking assumptions the Group applied in their value in use models, including:

- Forecast operating cash flows, growth rates and terminal growth rates - the Group have not met prior forecasts, and has incurred a loss in the current year, raising our concern over reliability of current forecasts. The current economic conditions increase the risk of inaccurate forecasts for us to consider.
- Forecast growth rates - the Group's models are sensitive to small changes in these assumptions, reducing available headroom. This drives additional audit effort specific to their feasibility and consistency of application given the Group's strategy.
- Discount rate - the Group's modelling is sensitive to small changes in the discount rate. We involve our valuations specialists in the assessment.

The VIU models are internally developed and use a range of internal and external data as inputs. Forward looking assumptions may be prone to greater risk of potential bias or error.

We involved valuation specialists to supplement our senior team members in assessing this key audit matter.

How the matter was addressed in our audit

Our procedures included:

- We considered the appropriateness of the value in use method applied by the Group to perform impairment testing against the requirements of the accounting standards.
- We assessed the integrity of the value in use models, including the accuracy of the underlying calculations.
- We compared the forecast cash flows contained in the value in use models to Board approved forecasts.
- We checked the consistency of the Group's forecast cash flows to the Group's stated plans and strategy.
- We assessed the accuracy of previous Group forecasts to inform our evaluation of forecasts included in the value in use models.
- We considered the sensitivity of the value in use models by varying key assumptions such as forecast operating cash flows and growth rates within a reasonably possible range, to identify those assumptions at higher risk of bias and to focus our further procedures.
- Working with our valuation specialists we independently developed a discount rate range considered comparable using publicly available market data for comparable entities.
- We assessed the Group's disclosures against the requirements of Australian Accounting Standards.



Revenue cut-off (Revenue - \$220.083 million)

Refer to Note 2.2 to the Financial Report

The key audit matter

Revenue cut-off is a key audit matter due to the:

- The high number of transactions.
- Extent of 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.

We involved our senior audit team members in assessing this key audit matter.

How the matter was addressed in our audit

Our procedures included:

- We assessed the appropriateness of the Group's accounting policies for the recognition of revenue against the requirements of the accounting standards and our understanding of the business.
- We sample tested significant sales recorded pre and post balance date to verify they had been recorded in the correct financial period.
- We checked the percentage of completion at balance date for a sample of projects where the performance obligation is satisfied over time, by obtaining customer confirmation.
- We assessed the disclosures in the financial report using our understanding obtained from our testing and against the requirements of the accounting standard.

Other Information

Other Information is financial and non-financial information in 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 and will 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: http://www.aasb.gov.au/auditors_responsibilities/ar1_2020.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 2020, 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 pages 19 to 30 of the Directors' report for the year ended 30 June 2020.

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
31 August 2020

Shareholder information

The shareholder information set out below was applicable as at 6 August 2020.

Distribution of equity securities

Analysis of numbers of ordinary shareholders by size of holding:

Size of holding	Number of holders	Percentage
1 to 1,000	3,679	30.16%
1,001 to 5,000	4,731	38.78%
5,001 to 10,000	1,766	14.48%
10,001 to 100,000	1,777	14.57%
100,001 and Over	247	2.02%
Total	12,200	100%

There were 7,099 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	16,668,441	7.19%
Poplar Pty Limited	16,550,845	7.13%
Greybox Holdings Pty Ltd	7,373,738	3.18%
Cariste Pty Ltd (CARISTE PTY LTD S/FUND A/C)	6,891,872	2.97%
Jacaranda Pastoral Pty Ltd	5,868,699	2.53%
Ace Property Holdings Pty Limited	4,700,000	2.03%
Cambrose Pty Limited	4,676,510	2.02%
Mr Keith Knowles	4,500,000	1.94%
Mr Alan Richard Bignell & Mrs Glenda Ellen Bignell	3,653,530	1.57%
Hart Capital Partners Ltd	2,392,343	1.03%
V M Nominees Pty Ltd	2,250,000	0.97%
Mr Rahmon Charles Coupe & Mrs Julia Deborah Coupe	2,009,000	0.87%
Wilson Asset Management	1,900,000	0.82%
Mr John Gassner	1,673,751	0.72%
JMID Pty Ltd	1,542,549	0.66%
AcomeA	1,503,972	0.65%
Troca Enterprises Pty Ltd	1,500,000	0.65%
Mrs Penelope Alice Fox	1,500,000	0.65%
Mr Peter Howells	1,463,564	0.63%
Mr Joseph Zanca & Mrs Szerenke Zanca (ZANACORP SUPER FUND A/C)	1,450,000	0.63%

Substantial shareholders

Substantial holders in the Company are set out below:

Name	Number held	% of shares issued
Poplar Pty Ltd ⁽¹⁾	17,845,724	7.69%
Hills Associates Limited	16,668,441	7.19%

(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

Shareholder information (continued)

Voting rights

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

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 maybe 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 registry in writing.

Securities exchange

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

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

David Chambers

Company secretary

David Robert Fox

Share registry

Link Market Services Limited

Locked Bag A14, Sydney South, NSW 1235, Australia

Telephone

- Australia: +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