ANNUAL REPORT

2014

nanosonics

NANOSONICS LIMITED ABN 11 095 076 896

Contents

Mission statement

We improve the safety of patients, clinics, their staff and the environment by transforming the way infection prevention practices are understood and conducted, and introducing innovative technologies that deliver improved standards of care.

Company overview

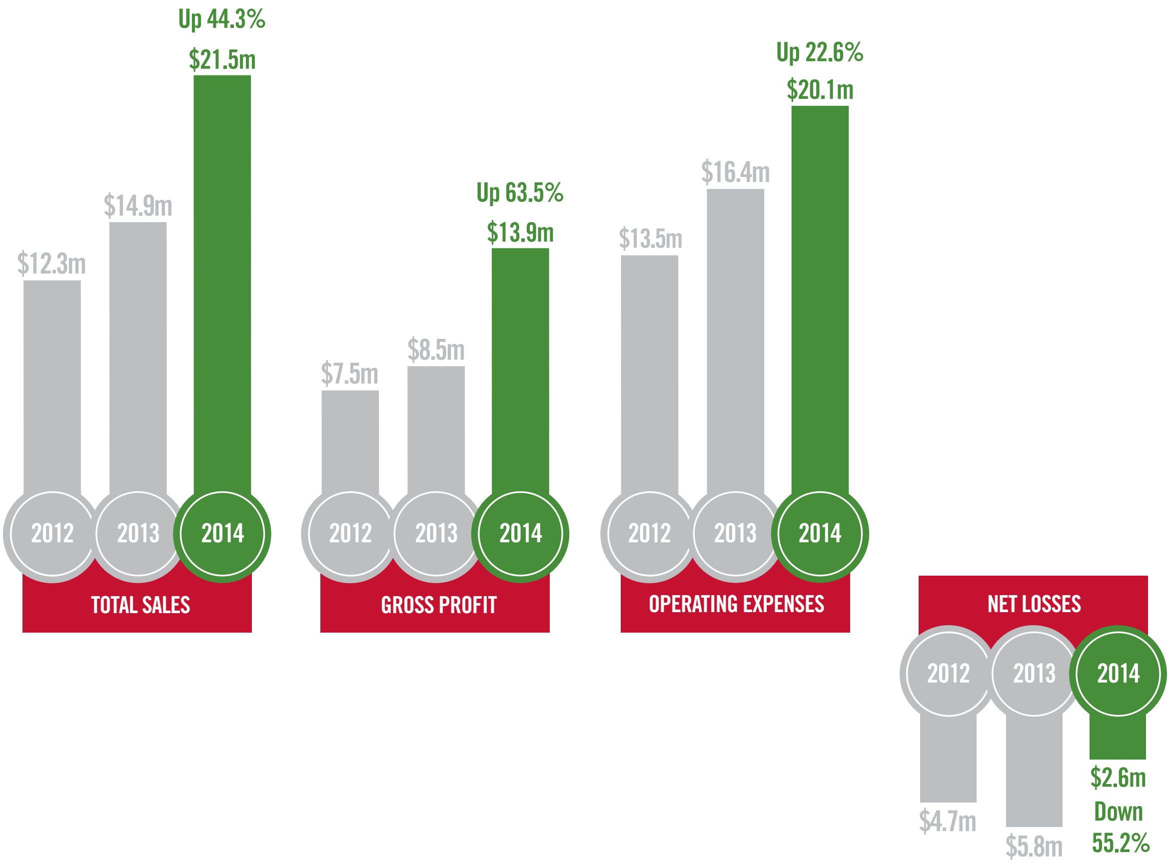
Nanosonics (ASX: NAN) is developing a portfolio of decontamination products designed to reduce the spread of infection. The Company owns intellectual property relating to a unique disinfection and sterilisation technology which can be suited to a variety of markets.

Initial market applications are designed for the reprocessing of reusable medical instruments. The Company's first product, the trophon® EPR, is designed to disinfect ultrasound transducers and is commercially available in Australia, New Zealand, the US, Europe and other markets.

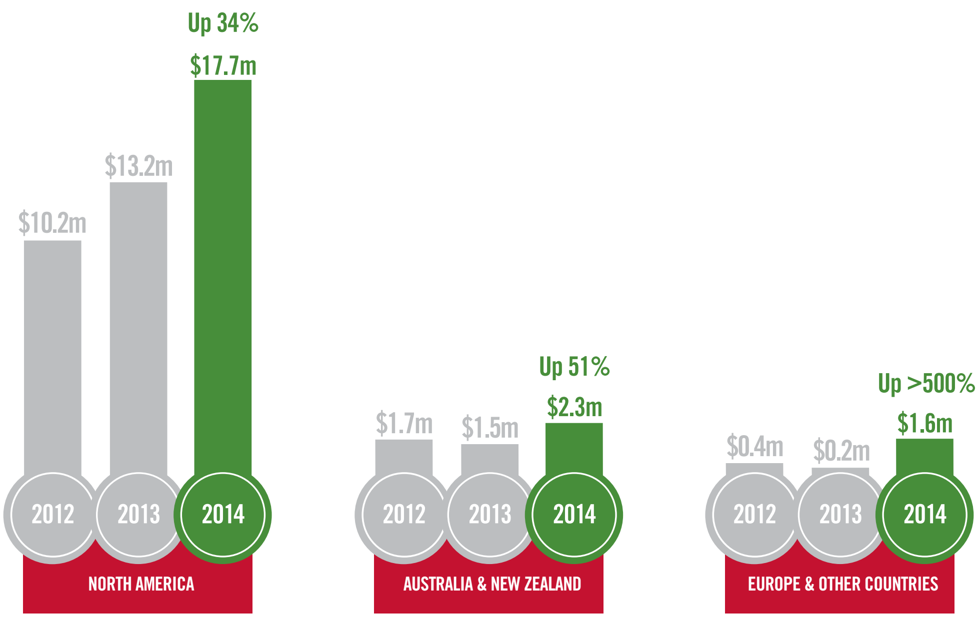
Nanosonics Ltd is headquartered in Sydney, Australia with offices in the US and Europe.

Financials at a glance

The year in numbers



Sales by region



	2014 $'000	2013 $'000	2012 $'000	2011 $'000	2010 $'000	2009 $'000
Revenue						
Operating revenue	21,492	14,899	12,301	2,247	763	309
Less cost of sales	(7,571)	(6,428)	(4,799)	(981)	(284)	(121)
Gross profit	**13,921**	**8,471**	**7,502**	**1,266**	**479**	**188**
Other income						
Government grants received	1,666	1,498	150	–	161	150
Other	1,709	–	–	–	–	–
Expenses						
Operating expenses (excluding depreciation and amortisation)	(19,141)	(15,335)	(12,634)	(13,229)	(8,827)	(9,867)
EBITDA	**(1,845)**	**(5,366)**	**(4,982)**	**(11,963)**	**(8,187)**	**(9,529)**
Depreciation and amortisation	(975)	(1,044)	(914)	(1,010)	(771)	(419)
EBIT	**(2,820)**	**(6,410)**	**(5,896)**	**(12,973)**	**(8,958)**	**(9,948)**
Interest income	739	1,192	586	1,052	785	1,194
Interest expense	(555)	(517)	–	–	–	–
Operating loss before tax	**(2,636)**	**(5,735)**	**(5,310)**	**(11,921)**	**(8,173)**	**(8,754)**
Net income tax benefit	**31**	**(33)**	631	707	–	–
Operating loss after tax	**(2,605)**	**(5,768)**	**(4,679)**	**(11,214)**	**(8,173)**	**(8,754)**
Cash assets						
Cash and cash equivalents	**21,233**	**24,064**	**29,310**	**12,356**	**21,144**	**13,881**

Nanosonics 2014 Highlights

NEW AGREEMENT

GE AND NANOSONICS ANNOUNCE NEW MARKETING AND SALES AGREEMENT FOR NORTH AMERICAN REGION

APPROVED

SOUTH KOREA'S MINISTRY OF FOOD AND DRUG SAFETY APPROVES trophon EPR FOR USE

FIRST UK HOSPITAL ADOPTS trophon® EPR

LEADING UK HOSPITAL, KING'S MILL, ADOPTS trophon EPR

AUSTRALIAN STUDY HIGHLIGHTS RISKS

AUSTRALIAN STUDY HIGHLIGHTS RISKS OF CROSS INFECTION USING CONVENTIONAL DISINFECTION

NEW LEADERSHIP

MICHAEL KAVANAGH COMMENCES AS CEO AND PRESIDENT

HEALTHCARE INDUSTRY'S COMPANY OF THE YEAR

NANOSONICS NAMED HEALTHCARE INDUSTRY'S COMPANY OF THE YEAR AT JANSSEN 2013 INDUSTRY EXCELLENCE AWARDS

trophon EPR RECEIVES AWARD

IN GERMANY, trophon EPR RECEIVED MANAGEMENT & KRANKENHAUS AWARD 2014 IN LABOR AND HYGIENE CATEGORY

STRATEGIC PARTNERSHIP

NANOSONICS SIGNS STRATEGIC PARTNERSHIP WITH MIELE PROFESSIONAL TO DISTRIBUTE trophon EPR IN GERMANY

STUDY PUBLISHED

STUDY PUBLISHED IN *JOURNAL OF INFECTION AND PUBLIC HEALTH* SHOWS trophon EPR MET A RANGE OF MAJOR INTERNATIONAL STANDARDS FOR HIGH LEVEL DISINFECTION

TOP HOSPITAL USE

40 OF 50 US TOP HOSPITALS NOW USE trophon EPR

GUIDELINES UPDATED

NEW AMERICAN INSTITUTE OF ULTRASOUND IN MEDICINE (AIUM) GUIDELINES RECOMMEND “HYDROGEN PEROXIDE NANODROPLET EMULSION” (trophon EPR’S TECHNOLOGY) FOR EFFECTIVE HIGH LEVEL DISINFECTION WITHOUT TOXICITY

Chairman's letter

I am pleased to present, on behalf of the Board of Nanosonics, our 2014 Annual Report.

The past year has seen significant evolution of the Company's growth and performance, with a strong emphasis on our international markets. The Nanosonics team has strengthened globally and the Board recognises the significant contribution of Mr Michael Kavanagh, the CEO and President, together with a number of new international appointments in our European markets.

This 2014 Annual Report highlights achievements in each and every dimension of the Company's activities which have resulted in a year of strong financial results and impressive achievements within our overall strategic plan. On a daily basis we see confirmation of the growing awareness of the need for compliance with infection control guidelines and the increasing recognition that the automated trophon EPR is now the emerging standard of care.

The awareness of imaging-related healthcare acquired infections continues to grow along with a global trend towards strengthening requirements in guidelines for high level disinfection (HLD). In May this year, the American Institute of Ultrasound (AIUM) released updated guidelines reinforcing stricter controls for HLD of ultrasound probes. The AIUM is recognised and respected by the health profession internationally and changes to guidelines from organisations such as this are an important step towards achieving our goal of establishing trophon EPR as the new global standard of care for HLD of ultrasound probes.

Nanosonics, together with its global strategic partners including GE Healthcare, Toshiba and Miele Professional, is leveraging mounting clinical evidence to support high level disinfection technologies like trophon EPR and the rejection of traditional, toxic chemical methods.

There were notable highlights in all markets throughout the year. As reported in August 2013, in North America, the trophon EPR is now being marketed and sold by the Ultrasound Division of GE Healthcare and supported by a substantial sales and marketing investment by GE Ventures. This realigned agreement has resulted in real momentum in the North American market where sales increased 34% for the period. The trophon EPR is now installed at 40 of the top 50 Hospitals in the US (*US News & World Report* rankings).

As recognition of healthcare acquired infections relating to ultrasound grows, audit compliance has become crucial. Customers using the trophon EPR achieved successful audits with no known rejections from third party auditors (The Joint Commission). This is an important endorsement for our product.

Market penetration is tracking well in Europe where we have employed dedicated Country Managers to commence market development in the UK, Germany and France. Sales in the region showed a five fold increase over last year, supported by the adoption of trophon EPR in the UK where Nanosonics has strategic partnerships with Toshiba and GE Healthcare, as well as growing direct sales.

In March, a new strategic partnership for the German market with Miele Professional, a world leading authority and provider of medical disinfection and sterilisation equipment, was announced. Miele launched the trophon EPR at the DGKH-congress (German Society of Hospital Hygiene) in Berlin in March, and has now started broad market awareness and education programs across the country.

Sales in Australia and New Zealand grew 51% driven by sales in leading corporate imaging centres as well as the public sector, and were supported by an underlying growth in sales of consumables as the installed base continued to grow.

Well earned recognition of Nanosonics' achievements came when the Company was named the Australian healthcare industry's Company of the Year for 2013 at the Janssen Industry Excellence Awards.

The Company achieved its first global Environmental Management System (EMS) certification and is now certified to ISO14001-EMS, an important certification for healthcare organisations which require suppliers to demonstrate their commitment to the environment. This certification highlights the many environmental benefits associated with trophon EPR.

Nanosonics continues to demonstrate world leading expertise across the full spectrum of its activities which is driving our increasing commercial success into multiple global markets.

Our commitment is to leverage our technical capabilities, our R&D pipeline and our evolving distribution network to drive shareholder value now and well into the future. The market for microbial control is a large and growing one and Nanosonics is well positioned to help our customers and partners meet the increasing demands for better infection control with integrated solutions underpinned by strong annuity revenue.

I take this opportunity to recognise the enormous efforts and talent of the growing Nanosonics team and the important contribution of our Board. Nanosonics has achieved many milestones during the year and a strong 2014 result.

Finally, our success to date has been underpinned by our shareholders whose support and shared vision will enable Nanosonics to continue on the path of innovation and growth.

Mr Maurie Stang
Chairman
Sydney
21 August 2014

CEO's report

The 2014 financial year has been a period of strong sales growth and global expansion for Nanosonics. This year we laid the foundations to support our next phase of growth and accelerate our transition from an emerging company with proven technology to an internationally recognised leader in the field of infection control.

Global sales momentum building

Global sales were up 44.3% at the end of the year with all regions contributing towards this growth. Sales were up 34% in North America, 51% in Australia and New Zealand, and more than five fold in Europe and other countries.

In the first quarter we announced an updated marketing and sales agreement with GE which included a significant investment by GE Ventures. Nanosonics is now working closely with GE Healthcare and GE Ventures to accelerate growth in the North American market which is a prime region for us.

Momentum is also building in Europe where the appointment of dedicated Country Managers resulted in growing sales figures for the region. The increase in sales for the region was mainly due to adoption of trophon EPR in the UK where Nanosonics has strategic partnerships with Toshiba and GE Healthcare, as well as direct sales operations.

In March we were delighted to announce a new strategic partnership with Miele Professional for the German market. Miele Professional is a world leading authority and provider of medical disinfection and sterilisation equipment.

In light of anticipated changes to UK guidelines and new strategic partnerships, we're looking forward to continued growth in the European region over the next year.

Plans for expansion in Asia Pacific are beginning to take shape. Regulatory approvals were received for both Korea and Japan in the period and we are finalising commercialisation strategies for these markets. Japan is a significant market globally from an ultrasound perspective and hence represents an important opportunity for our technology.

Throughout the year, market fundamentals have strengthened the outlook for our flagship product, the trophon EPR. These fundamentals are transforming our business and, in the process, are creating an opportunity to establish trophon EPR as the global standard of care for ultrasound disinfection. These fundamentals include:

- Growing awareness of imaging procedure Healthcare Acquired Infections (HAIs).
- Trends towards stricter controls for high level disinfection (HLD) and for automation.
- Growing importance of risk mitigation.
- Mounting clinical evidence for trophon EPR adoption.
- Growing recognition and adoption of trophon EPR.
- Current toxic HLD solutions progressively being rejected by customers and regulators.

Growing awareness

Awareness of HAIs associated with imaging is growing. An increasing number of clinical studies demonstrate that, with traditional methods of ultrasound probe disinfection, probes can remain contaminated with pathogens and pose a risk of cross infection. There have been reported cases of hepatitis B and hepatitis C infections being transmitted and, in both cases, improper ultrasound transducer disinfection was pinpointed as a likely cause.

Trends towards stricter controls for HLD and for automation

Guideline changes are key to establishing trophon EPR as the global standard of care. As the issue of poor infection control practices receives greater attention, moves to strengthen and tighten global regulations and guidelines for HLD are underway.

While a number of international healthcare authorities already recommend automated reprocessing over manual methods, changes to the American Institute of Ultrasound (AIUM) guidelines reinforcing stricter controls for ultrasound probe disinfection were a significant highlight this year.

Furthermore, in the UK, health board reviews of ultrasound decontamination procedures and guidelines in England, Scotland and Wales are under review. We expect the resulting changes to be positive for trophon EPR as they should also focus on implementing stricter, more effective controls.

Growing importance of risk mitigation

HAIs are a huge financial burden. With the cost of healthcare a major focus for governments, insurers and consumers worldwide, healthcare facilities are increasingly being required to publically report HAI-related data. As this trend continues, risk mitigation and audit compliance becomes increasingly recognized as an important factor in accountable healthcare models.

In May, The Joint Commission (TJC), which is a third party auditor in the US, released a Quick Safety advisory highlighting improperly sterilised or high level disinfected medical equipment as one of the top five non-compliant accreditation requirements for 2013. On another very positive note for trophon EPR, I'm pleased to report that customers in the US have achieved uniform high compliance and no known rejections from TJC to date. In essence, this validates that adoption of the trophon EPR provides high levels of assurance of compliance for our customers.

Mounting clinical evidence

Clinical evidence supporting adoption of trophon EPR is a key driver of changes to guidelines. During the past year, clinical evidence continued to mount and a number of significant studies were published highlighting the efficacy issues and OHS risks associated with traditional disinfection practices. To summarise, these studies showed:

- Chemicals traditionally used in manual disinfection are suboptimal and may pose a risk of cross contamination.
- Automated systems are more effective than manual methods, which are prone to human errors.
- The superior efficacy of trophon EPR.

We have included further details of the clinical evidence that emerged during the past year in this report. We plan to continue investing in this important aspect of our market growth strategy in FY15.

Growing recognition and adoption of trophon EPR

Our Strategic Growth Plan is tracking well. In the US, trophon EPR is now installed at 40 of the 50 top ranked hospitals (*US News & World Report*). Key to the plan is our strategic partnerships with global brands that position us to penetrate important markets. While our partnerships with GE in North America and Toshiba in the UK are now well established, in March we were delighted to sign a new agreement with Miele Professional in Germany.

Working with these leading global brands is a real testimony to the innovation of the trophon EPR and validation of its market potential.

Nanosonics received further recognition this year when we were named the Australian healthcare industry's Company of the Year for 2013 at the Janssen Industry Excellence Awards while in Germany the trophon EPR received the M&K Award 2014 in the Labor and Hygiene category. Management & Krankenhaus is the leading publication for decision makers in the German health industry.

Current toxic HLD solutions progressively being rejected by customers and regulators

There is a growing awareness of the occupational health risks for healthcare professionals using toxic chemicals to perform traditional ultrasound disinfection procedures. Consequently, customers and regulators are turning to safer alternatives such as the trophon EPR, which addresses the OHS risks posed by traditional chemical soaking methods.

Trend towards Point of Care adoption

The toxic chemicals used in traditional disinfection methods involve soaking in chemicals and usually require a separate room with ventilation. According to reports to TJC's Office of Quality Monitoring, space issues are a contributing factor preventing proper sterilisation or high level disinfection of medical equipment.

One of the many benefits of trophon EPR is that it is safe and easy to use at the point of care. This not only saves space, it creates workflow efficiencies and eliminates transportation of probes, thus reducing the potential for probe damage.

Operations

Operating expenses of $20.1 million and a net loss of $2.6 million represent a substantial reduction of about 55% that supports our path to profitability. R&D activity focused on refining and improving our product offering and identifying new opportunities to leverage our platform technology into the second generation of products. The company has a strong and growing intellectual property portfolio. Since April 2013, the number of granted/accepted patents has more than doubled – from 47 to 95.

Validation work with ultrasound probe manufacturers also progressed and the trophon EPR is now approved for use with more than 600 probe models across 14 manufacturers. This is an important selling point for our product. In addition, the figure includes surface probes, which have the potential to become an important part of our model as evidence emerges supporting the requirement for disinfecting these devices.

We continued to implement our strategic LEAN program to enable scalable manufacturing processes. In addition to achieving improved planning and visibility, we achieved 100% on time delivery throughout the year.

Regulatory and Quality Assurance highlights for the year included successful NRTL, KFDA and TüV recertification audits as well as audits by Miele Professional and the Korean Ministry of Food and Drug Safety. In addition, in August we announced regulatory approval in Japan.

Throughout the year we also expanded our global customer support and service capabilities into each of our international markets with service infrastructure now set up across all regions.

Focusing the varied activities of a global technology company like Nanosonics is crucial to our success. During the year, the Senior Leadership Team formalised a new Corporate Mission statement supported by five Core Corporate Objectives. These objectives are designed to provide a clear direction to support our business and are: Customer Experience, Product Innovation, Operational Excellence, People Engagement and Value Creation. Specific core strategies underpinning the objectives have also been developed and are now directing the three year growth plan for the Company.

Outlook

Looking forward, our aim is to consolidate and expand on the achievements of FY14 to create sustainable value for shareholders.

I'm confident we have the foundations in place to achieve our goals and support our growth strategies, and that our device is uniquely positioned to take advantage of the tremendous opportunities that are presenting as the market fundamentals strengthen.

I would like to thank everyone in the Nanosonics team for their dedication and efforts this year. This is an exciting time for the company as we emerge as a fully-fledged international medical technology organisation. We remain focused on the necessary activities as well as building company and shareholder wealth into the future.

Michael Kavanagh

CEO and President

Sydney

21 August 2014

US regional highlights

2014 was an exciting time in the US. The strategy of implementing trophon EPR with large hospital groups is paying off. Some key highlights this year include:

- Amended contract executed with GE Healthcare to continue as exclusive North America distributor with GE funding the Nanosonics US Sales Force.
- GE Healthcare and GE Ventures sales and marketing investment to accelerate the North American growth strategy.
- trophon EPR installed at 40 of the top 50 Ob/Gyn best US hospitals.*
- The trophon EPR was presented at national trade shows and more than 20 regional infection control scientific meetings.
- Service and repair capability in Indianapolis completed and operational.

Luminary US Institution, The Johns Hopkins Hospital, embraces trophon EPR

"The trophon EPR has been the biggest thing to hit ultrasound since colour Doppler," said the head of ultrasound radiology at The Johns Hopkins Hospital (JHM) following the introduction of trophon EPR.

Headquartered in Baltimore, JHM is a $6.7 billion integrated global health enterprise and widely regarded as one of the world's leading hospitals. It was ranked by *U.S. News & World Report* as the best overall hospital in America for 21 consecutive years (1991-2011), and was rated as the top institution in 2013.

After an evaluation of ultrasound probe disinfection practices, the hospital's Radiology Department decided to move away from chemical soaking methods and purchased 26 trophon EPR units to reprocess its intracavitary and surface transducers.

"The amount of time and energy needed for chemical soaking was greatly impacting patient workflow to the point where I was pushing to hire a person to just HLD the transducers," said Robert De Jong Jr., RDMS, RDCS, RVT, Radiology Technical Manager, Ultrasound.

"The chemicals were also creating a separation between layers of the transducer, causing air to be introduced. This resulted in artefacts and degraded images. I have not had to replace a transducer for these issues since the switch to the trophon EPR."

The hospital has experienced other benefits such as eliminating much of the protective gear that was required for chemical soaking and being able to use the trophon EPR at the point of care. The latter means the department no longer needs a room dedicated to HLD. Word about the trophon EPR spread throughout the hospital and JHM now has more than 40 units across its radiology, obstetrics/gynaecology and emergency departments.

"The reduced time waiting for the transducer to be ready has been a major plus and staff members love the ease of use of the trophon EPR. We're now trying to 'trophon' every transducer after use, not just endocavitary," said Mr De Jong.

"Trophon was an answered prayer! It has solved so many HLD issues while offering more complete and safer protection for our patients and staff – in half the time."

* US News and World Report

Europe regional highlights

Strategic partnerships with leading global brands is a key part of our global expansion strategy. Our partnership with Toshiba is reaping rewards and the Company now has a number of UK sites with multiple trophon EPRs installed. In March Nanosonics signed a strategic partnership with Miele Professional to distribute trophon EPR in Germany. Miele conducted a national launch in March and has started broad market awareness and education programs for trophon EPR across Germany.

Other key highlights this year include:

- The trophon EPR has now been adopted in a number of hospitals throughout the UK including key university hospitals in London and Cardiff.
- Health board reviews are underway in England, Scotland and Wales to amend ultrasound decontamination procedures and guidelines following MHRA alerts*. The changes, which will be released in the foreseeable future, are expected to be positive for trophon EPR.
- In Germany, trophon EPR received Management & Krankenhaus Award 2014.

trophon EPR provides reassurance for staff and patients at King's Mill Hospital

Achieving clinical governance goals is just one of the benefits experienced by the ultrasound department at King's Mill Hospital, UK following the installation of eleven trophon EPR units.

Staff also reported feeling reassured that probes are now being 'deep cleaned' in-line with international best practice. "We like this disinfection process because it removes any user subjectivity, assuring staff that the disinfection process is reproduced perfectly each and every cycle," said Clinical Lead Sonographer, Ann Allen.

"It has also had a positive impact on patient confidence as they know the probe has been automatically reprocessed rather than manually cleaned."

The 600 bed King's Mill Hospital has one of the UK's most highly regarded ultrasound departments and turned to the trophon EPR when it was looking for a solution to high level disinfect its probes following two MHRA alerts*. An initial purchase of six units was quickly followed by a further five units.

"The trophon EPR is extremely easy to use and fits well into our workflow," said Mrs Allen. "It has not caused any extension in examination times, which is crucial in a busy ultrasound department.

"While there is an additional cost required to implement the trophon EPR versus the alternative HLD wipe system we looked at, there are very significant cost savings year on year."

* The first MHRA (Medicines and Healthcare products Regulatory Agency alert advised users to appropriately decontaminate all types of reusable ultrasound probes while the second advised users ensure detergent and disinfectant wipes are compatible with the medical device to avoid damage to the plastic surfaces.

Asia Pacific regional highlights

The Australian market for the trophon EPR continued to grow this year. Two significant studies coming out of Australia added to the mounting clinical evidence that will help us establish trophon EPR as the standard of care globally.

Some key highlights this year include:

- The trophon EPR was approved for use in South Korea following receipt of a product licence from the Korean Food and Drug Administration (KFDA).
- Nanosonics successfully passed its first Environmental Management System (EMS) certification audit and is now certified to ISO14001-EMS.
- Named the healthcare industry's Company of the Year for 2013. The Janssen 2013 Industry Excellence Awards recognise excellence in the commercialisation of innovative healthcare solutions by Australian biotechnology companies.

trophon EPR "offers the best disinfection procedure"

One of the major benefits of the trophon EPR is that it delivers effective, high level disinfection of the entire ultrasound probe, including the shaft and handle. Some probe manufacturers advise against immersing the probe in liquid disinfectant, which Dr Andrew Ngu, Principal of East Melbourne Ultrasound, said may pose a risk of cross infection for patients.

Dr Ngu, who is also President elect for the International Society of Ultrasound in Obstetrics and Gynaecology (ISUOG) and on the executive of the Australasian Society of Ultrasound in Medicine (ASUM), has been using the trophon EPR since February 2012.

"Before trophon we were using various methods, one of which was soaking the probes in chemical solution," Dr Ngu said. "It wasn't very satisfactory as we could only disinfect part of the probe."

Dr Ngu co-authored a study which was presented at the ISUOG World Congress in October 2013.

The study showed that more than 70% of manually disinfected probes still showed signs of contamination on the handles, with a large portion of the contaminants being well known pathogens including methicillin resistant Staphylococcus aureus (MRSA). In comparison, trophon EPR completely eliminated bacteria on the probe handles.

"With the trophon EPR I can be assured that I'm giving patients the best service all round including, most importantly, the best disinfection procedure for probes," Dr Ngu said.

"The staff are also relieved they don't have to do all the [protective equipment] procedures to protect themselves from the chemical solution.

"It's a very easy process to go through and we're very happy with it. In fact, now we wouldn't look at anything else."

trophon® EPR: innovative technology delivering improved standards of care

Nanosonics' trophon EPR provides fast, automated high level disinfection of ultrasound probes. The fully enclosed system reduces the risk of chemical exposure and can be conveniently located at the point of care to improve clinic workflow.

Fast

Fast automated high level disinfection at point of care

Helps Protect

Fully enclosed system limits exposure to harmful chemicals

Consistent

Quality assured consistency

Traceability

Best practice documentation solution

Probe Friendly

Probe friendly process. Compatible with more than 600 probe models

Cost Efficient

Integrates into HLD process at point of care and improves workflows

Effective

Clinically validated trophon EPR disinfects both probe shaft AND handle

Environmentally Friendly

Harmless oxygen and water by-products. More than 70% recyclable components

The trophon EPR product range

Nanosonics has a range of consumables and accessories to meet the needs of customers and allow them to more effectively provide and monitor the high level disinfection process. These products expand Nanosonics' offering in the market and provide additional revenue streams from service contracts and consumables supply.

trophon® Connect

trophon Connect software is an audit and accreditation tool that enables disinfection data to be downloaded from the trophon EPR to a PC to provide fast, non-editable reports.

trophon® Printer

The trophon Printer delivers an easy-to-use traceability solution for quality system documentation requirements. The trophon Printer can print up to four labels per disinfection cycle based on the operator, site or procedure preferences and links the probe and disinfection procedure to the patient.

trophon® Wall Mount and trophon® Cart

Enables the trophon EPR to be mounted on a wall where there are space constraints or makes the device fully mobile for convenient point of care use.

Chemical Indicators

Chemical Indicators validate each disinfection cycle by providing a qualitative colour change.

Sonex™/NanoNebulant™

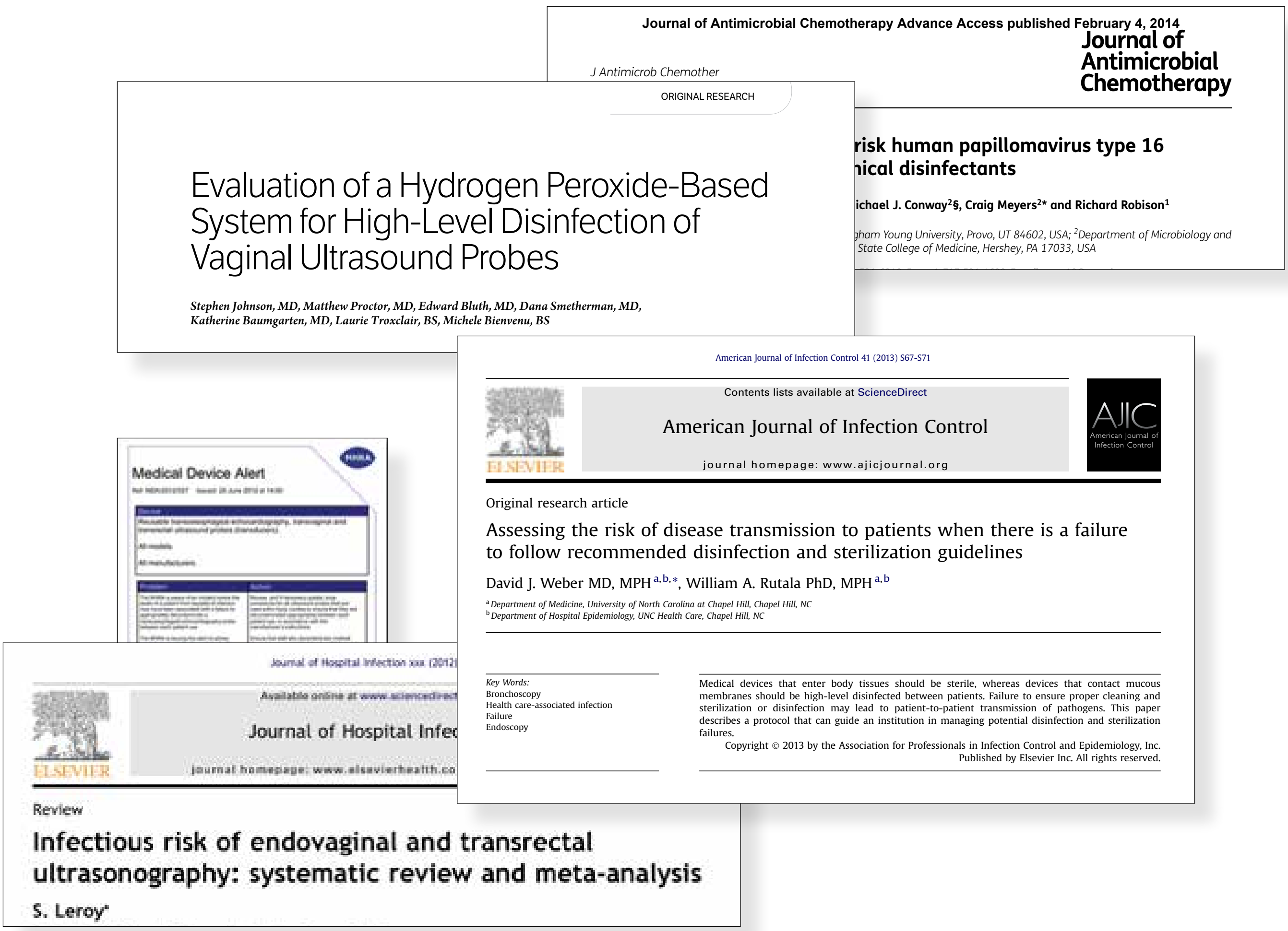
The trophon EPR uses cartridges of Nanosonics' proprietary disinfectant liquid. Each cartridge is sealed and easy to insert into the trophon EPR. The device pierces the cartridge once the cartridge is inserted so the user does not come into contact with the liquid. Empty cartridges are recyclable.

Clinical evidence supporting adoption of trophon EPR continues to mount

Changes to decontamination procedures and guidelines are an important factor in establishing trophon EPR as the new standard of care.

These changes are starting to happen due to growing awareness of healthcare acquired infections (HAIs) related to imaging procedures and recognition of the risks associated with improperly sterilised or high level disinfected medical equipment. Most notable were the recent changes in the new guidelines from the American Institute of Ultrasound Medicine (AIUM). The guidelines reinforce stricter controls for high level disinfection of ultrasound probes and included the statement "a hydrogen peroxide nanodroplet emulsion might provide an effective high level disinfectant without toxicity".

Clinical evidence is another important factor in driving these changes. During the last year some significant findings were published highlighting the efficacy issues and OHS risks associated with traditional disinfection practices, as well as studies that further support the need to adopt automated high level disinfection in ultrasound imaging.



- A study evaluating contamination levels on ultrasound probes covered by a sheath and disinfected using wipes, demonstrated a substantial persistence of potentially pathogenic microorganisms. Human papilloma virus (HPV) DNA was found on 7% of the probes (HPV can cause cervical and other cancers). Staphylococcus aureus on 4% and Chlamydia trachomatis, which can also cause serious illness, were found on 2% of samples post decontamination.[1]
- A meta-analysis of studies involving wipes for disinfection has shown residual pathogenic bacterial contamination (12.9%) and viral contamination (1.0%) on transvaginal and transrectal transducers.[2]
- Manual disinfection of medical devices has been shown to lead to an increased risk of operator error if protocols are not followed correctly and poor protocol compliance can lead to an increased risk of transmission for patients.[3]
- A case of hepatitis C infection was reported in a patient after a prostate biopsy. This follows another case of a fatal hepatitis B infection after an imaging procedure. In both cases improper ultrasound transducer disinfection may have been involved.[4,5]
- A study found that more than 70% of manually disinfected probes still showed signs of contamination on the handles, with a large portion of the contaminants being well known pathogens including methicillin resistant Staphylococcus aureus (MRSA). While handles do not enter body cavities they can harbour pathogens and pose a risk of cross infection for patients. The study called for stricter disinfection standards which require use of devices – such as the trophon EPR – or techniques that ensure high level disinfection of the whole probe, handle included.[6]
- Manual disinfection processes are often difficult to validate to ensure all critical process parameters are consistently met.[7]
- Nurses with regular daily exposure to sterilising agents (including glutaraldehyde) during pregnancy, are more than twice as likely to undergo late spontaneous abortion compared to nurses who are not exposed to these chemicals.[8]
- An evaluation of the trophon EPR concluded that the trophon EPR was proven to be more efficient and viewed to be easier and safer to use than a glutaraldehyde-based method. The study showed that the trophon EPR process took 14 minutes (this figure includes related activities such as pre-cleaning the probe, wiping after disinfection process and logging patient information) compared to 32 minutes for a glutaraldehyde-based disinfection system and that the trophon EPR saved an average of 7.5 hours per week.[9]
- A peer-reviewed study published in the Journal of Infection and Public Health reported on the performance of the trophon EPR when tested against 21 different species of bacteria, fungi and viruses according to accepted international standards for high level disinfection. The study showed trophon EPR met all standards for high level disinfection.[10]

1. M'Zali, F., et al (2014). "Persistence of Microbial Contamination on Transvaginal Ultrasound Probes despite Low-Level Disinfection Procedure." PLoS One 9(4): e93368
2. Leroy, S. (2013). Infectious risk of endovaginal and transrectal ultrasonography: systematic review and meta-analysis. J Hosp Infect 83(2): 99-106.
3. Weber, D. J., Rutala W (2013). Assessing the risk of disease transmission to patients when there is a failure to follow recommended disinfection and sterilization guidelines. Am J Infect Control 41(5 Suppl): S67-71.
4. Ferhi, K., et al., Hepatitis C transmission after prostate biopsy. Case Rep Urol, 2013. 2013: p. 797248.
5. Medicines and Healthcare products Regulatory Agency (UK), Medical Device Alert Ref: MDA/2012/037, Issued: 28 June 2012 at 14:00.
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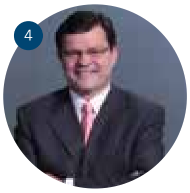
Information on the directors, company secretaries and senior management



1. Maurie Stang

Non-Executive Chairman

Mr Stang has been Non-Executive Director and Chairman since March 2007 and a member of the Board since November 2000.

Mr Stang has more than two decades of experience building and managing companies in the healthcare and biotechnology industry in Australia and internationally. His strong business development and marketing skills have resulted in the successful commercialisation of intellectual property across global markets. He is a Non-Executive Director of Vectus Biosystems and has been Non-Executive Chairman of Aeris Environmental Ltd (ASX:AEI) since 2002.

2. Michael Kavanagh BSc, MBA (Advanced)

CEO and President (from 21 October 2013)

Mr Kavanagh joined Nanosonics as CEO and President effective 21 October 2013. He was a Non-Executive Director of the Board from 30 July 2012 to 20 October 2013.

Mr Kavanagh has more than 20 years of international commercial experience in the healthcare market having held local, regional and global roles in medical device and pharmaceutical industries.

Before joining Nanosonics, he was Senior Vice President of Global Marketing for the major medical device company Cochlear Ltd, a position he held for more than 10 years.

Mr Kavanagh has no other current and former directorships in the last three years.

3. Richard England FCA, MAICD

Non-Executive Director

Mr England joined the Board in February 2010. He is a chartered accountant and professional Non-Executive Director. Since 2002, Mr England has been a director and Chairman of Ruralco Holdings Limited (ASX:RHL). Since February 2008 he has been a director and Chairman of Chandler Macleod Group Limited (ASX:CMG). He has been director of Macquarie Atla Roads Limited (ASX:MQA) since June 2010 and a director of Japara Healthcare Limited (ASX:JHC) since April 2014.

4. David Fisher BRurSc (Hons), MAppFin, PhD, FFin

Non-Executive Director

Dr Fisher has been a member of the Board since July 2001.

Dr Fisher is founding partner of Brandon Capital Partners, a leading Australian venture capital provider. He has more than 25 years' of extensive operating experience in the biotechnology and healthcare industry in Australia and overseas. He held senior positions with Pharmacia AB (now part of Pfizer, Inc) and was CEO of Peptech Limited (now part of Cephalon Inc. (Nasdaq:CEPH). He was a director of Aeris Environmental Ltd (ASX:AEI) from May 2011 to July 2014.

5. Ron Weinberger BSc (Hons), PhD

President Technology Development/Commercialisation (from 21 October 2013)

Dr Weinberger joined the Company in August 2004 and was appointed as Executive Director in July 2008 then Managing Director and Chief Executive Officer in December 2011 with a period as acting CEO from May 2011. Since October 2013, he has been President of Technology Development/Commercialisation and is responsible for the direction of the Company's technology development and commercialisation strategy.

Dr Weinberger has more than two decades of experience in medical research and biotechnology. He is co-inventor of several of Nanosonics' key technology patents.
Dr Weinberger has not had any other directorships of listed companies in the last three years.

6. McGregor Grant BEc, CA, GAICD

Chief Financial Officer and Company Secretary

Mr Grant joined Nanosonics in April 2011 and is responsible for the overall financial management of the Company and, together with Mr Kavanagh, has joint responsibility for investor relations. Mr Grant has more than 18 years of business experience in a number of senior roles in the medical device and healthcare industries located in Australia and the United States. Previously Mr Grant worked for Coopers & Lybrand in Australia and Europe.

7. Gerard Putt BSc

Chief Operations Officer

Mr Putt joined Nanosonics full time in 2011 after 18 months on the Nanosonics advisory board. Mr Putt has more than 15 years of experience in the medical device industry as a leader of development, engineering, production and operations teams. He has particular experience in the implementation of new products into manufacturing and rapid scaling of production to international market needs.

8. Michael Potas BE (E&C)

Head of Research, Design and Development

Mr Potas joined Nanosonics in August 2006 and has more than 16 years' experience in the development and commercialisation of new products and technologies. Since joining Nanosonics in 2006, Mr Potas has been instrumental in the research, design and development of the trophon EPR and associated core intellectual property.

9. Vincent Wang BSc, MSc, MBA

Head of Global Support and Services

Mr Wang has extensive experience in developing and implementing global service and support strategy, establishing and managing customer support, technical service and service marketing functions in global medical device businesses. Before joining Nanosonics in May 2011, Mr Wang led and managed Technical Services and Service Operations for Sonova Hearing Healthcare Group and Cochlear Ltd respectively.

10. Ruth Cremin MSc

Head of Quality and Regulatory

Ms Cremin joined Nanosonics in July 2011 and has extensive regulatory affairs experience. Previously she worked at Cochlear as a Senior Regulatory Affairs Specialist for the Asia Pacific Region; at Pfizer Australia as a QA & Regulatory Officer and at Bio-Medical Research Ltd in Galway, Ireland as a Regulatory Affairs Associate.

11. Kirste Courtney BA

Human Resources Manager

Ms Courtney joined Nanosonics in 2008 and has more than 16 years of human resources experience having worked in a variety of industry sectors including chartered accounting, media, logistics and banking.

Information on the directors, company secretaries and senior management (continued)

12. Ronald J Bacskai BSME, MBA (Hons)

President and CEO, Nanosonics Inc.

Mr Bacskai joined Nanosonics in 2010 and is responsible for leading Nanosonics' business in the United States. Mr Bacskai is an experienced executive having worked in multiple industries with a broad technical, marketing and sales, and technology commercialisation background. Mr Bacskai has significant experience as President, CEO and board member of several public and private organisations as well as serving on the advisory board of a speciality environmental firm.

13. Bryn Tudor-Owens BSc

Country Manager – UK

Mr. Tudor-Owen has 20 years' experience gained within the medical device industry. Prior to Nanosonics he held senior positions with both GE Medical Systems and Cardinal Health for more than 15 years before more recently driving the UK startup operations of a German Healthcare SME. He joined Nanosonics in August 2012.

14. Ralf Schmähling BA (Hons)

Country Manager – Germany

Mr. Schmähling joined Nanosonics in September 2012. He has more than 12 years experience in various business, sales and marketing management and leadership functions within blue chip medical device companies. He has a successful track record on strategic and tactical sales execution in the German health care market.

15. Julien Laronze BBA, BA

Country Manager – France

Mr. Laronze joined Nanosonics in March 2014. He has more than 15 years senior sales management and executive level experience, with a proven track record in driving growth both domestically and internationally, in the medical technology industry with large and small companies. Prior to joining Nanosonics, he held Sales Director positions with Sophysa and Edap-Tms.

16. Robert Waring BEc (Sydney), CA, FCIS, FFin, FAICD

Company Secretary

Mr Waring was appointed Company Secretary in October 2010 and held this position at the time of the Company's IPO in May 2007. He is a director of corporate advisory firm, Oakhill Hamilton Pty Ltd.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Directors' report

Your directors submit their report together with the Consolidated Financial Report of the Group, being Nanosonics Limited and its subsidiaries, for the year ended 30 June 2014.

Principal activities

During the year the principal activities of the Group consisted of:

- Manufacturing and distribution of the trophon® EPR ultrasound probe disinfector and its associated consumables and accessories; and
- Research, development and commercialisation of infection control and decontamination products and related technologies.

There have been no significant changes in the nature of these activities during the year.

Operating and financial review

Revenue from sales for the year amounted to $21,492,000 (2013: $14,899,000), an increase of $6,593,000 or $44.3%. Global sales were up with all regions contributing towards this growth. Sales were up 34% in North America, 51% in Australia and New Zealand, and fivefold in Europe and other countries.

Other income amounted to $4,114,000 (2013: $2,690,000), which included the R&D tax refund of $1,516,000 (2013: $1,348,000); Export Market Development grant of $150,000 (2013: 150,000); reimbursement of costs by a distributor of $1,707,000 (2013: nil) and interest earned on cash investments of $739,000 (2013: $1,192,000).

Operating expenditure for the year amounted to $20,116,000 (2013: $16,379,000), an increase of $3,737,000 or 22.8% driven by higher employment and related operating costs to support the growth of the business.

Other expense for the year of $555,000 ($517,000) relates to borrowing costs on convertible notes.

The consolidated loss after tax amounted to $2,605,000 (2013: $5,768,000), a substantial reduction of 55%.

The Group ended the year with $21,233,000 of cash and equivalents (2013: $24,064,000). The Group has adequate cash to fund the operations of the business.

Other information on the operations of the Group and its business strategies and prospects are discussed in the review of operations included in the CEO report and the regional reviews on pages 8 to 13 of this report.

Significant changes in the state of affairs

In the opinion of the directors, there were no significant changes in the state of affairs of the Group during the financial year under review and to the date of this report.

Dividends – Nanosonics Limited

The directors do not recommend the payment of a dividend for the financial year ended 30 June 2014. No dividends were proposed, declared or paid during the financial year (2013: Nil).

The Company's dividend policy in the future, the extent of future dividends and any franking of dividends will depend upon the profitability and the financial and taxation position of the Group at the relevant time.

Matters subsequent to the end of the financial year

No matter or circumstance has arisen since 30 June 2014 that has significantly affected, or may significantly affect:

a. the Group's operations in future financial years;
b. the results of those operations in future financial years; or
c. the Group's state of affairs in future financial years.

Likely developments and expected results of operations

Comments on expected results of the operations of the Group are included in the review of operations on pages 8 to 13. Further information on likely developments in the operations of the Group and the expected results of operations have not been included in this annual report because the Directors believe it would be likely to result in unreasonable prejudice to the Group.

Environmental regulation

The Group is subject to meeting statutory environmental regulations. To demonstrate its commitment to meeting these regulations, the Group has put in place an Environmental Management system, which is currently certified to ISO14001.

Directors

During the year and to the date of this report, the Board of Nanosonics Limited comprised of Maurie Stang, David Fisher, Richard England, Michael Kavanagh, and Ron Weinberger.

As at the date of this report, Nanosonics Limited has the following committees of the Board: Audit and Risk, Remuneration, Nomination, and R&D and Innovation. Details of members of the committees of the Board during the year are included on page 27.

Information on the directors, company secretaries and senior management is a part of the Directors' report and can be found on pages 18 to 20 of the Annual Report.

Meetings of directors

The number of directors' meetings, including meetings of the committees, held during the year ended 30 June 2014, and numbers of meetings attended by each of the directors were as follows:

	Full meetings of directors		Meetings of committees					
			Audit		Governance and Nomination		Remuneration	
	Held[1]	Attended	Held[1]	Attended	Held[1]	Attended	Held[1]	Attended
Maurie Stang	12	10	3	2	2	2	4	3
Richard England	12	12	3	3	2	2	4	4
David Fisher	12	11	3	3	2	2	4	4
Ron Weinberger	12	12						
Michael Kavanagh	12	11					3	3

[1] Represents the number of meetings that a director is eligible to attend.

Share-based payments

Shares issued under the DESP and options granted under ESOP and GSOP during the year are detailed below.

Shares issued

During the year ended 30 June 2014, the Company issued a total of 1,835,108 (2013:2,005,800) new ordinary shares in Nanosonics Limited as detailed below. To the date of this report, the Company issued a total of 2,169,108 new ordinary shares as detailed below. No amount was unpaid on any of the shares so issued.

Shares issued	Number of shares issued
Share options exercised under Share Option Plans	1,835,108
Total new shares issued during the year	**1,835,108**
Share options exercised under Share Option Plans post balance date	334,000
Total new shares issued and to the date of this report	**2,169,108**

As at 30 June 2014 there were 263,823,826 (2013: 261,988,718) ordinary shares in Nanosonics Limited on issue. At the date of this report, there were 264,157,826 shares on issue. Further information on issued shares is provided in the Contributed equity and the Share-based compensation notes to the financial statements.

Share options granted

During the financial year and to the date of this report, the Company granted, for no consideration, 3,115,869 (2013: 3,023,929) unquoted options over unissued ordinary shares in Nanosonics Limited. Further information on the grants is provided below, in section 5 of the Remuneration report on pages 42 to 47 and in the Share-based compensation note to the financial statements.

Share options granted	Number of options granted
Employee Share Option Plan (ESOP)	2,981,494
General Share Option Plan (GSOP)	–
Total new options granted during the year	**2,981,494**
Employee Share Option Plan (ESOP)	134,375
Total options granted to the date of this report	**3,115,869**

Shares under option

At the date of this report, there were 6,159,975 unissued ordinary shares of Nanosonics Limited under option as detailed below. As at 30 June 2014, there were 6,525,597 (2013: 5,418,625) unissued ordinary shares of Nanosonics Limited under option. Further information on the options is provided in the Share-based compensation note to the financial statements.

Share option plan	Number of shares under option
Employee Share Option Plan (ESOP)	5,972,263
General Share Option Plan (GSOP)	553,334
Total shares under option at 30 June 2014	**6,525,597**
Share options exercised under Share Option Plans post balance date	(334,000)
Share options forfeited under Share Option Plans post balance date	(165,997)
Share options issued under Employee Share Option Plan (ESOP) post balance date	134,375
Total shares under option to the date of this report	**6,159,975**

The options entitle the holder to participate in a share issue of the Company provided the options are exercised on or after their vesting date and prior to their expiry date. No option holder has any right under the options to participate in any other share issue of the Company or any other entity.

Remuneration report - audited

Table of contents

1.0 Introduction

Nanosonics is an emerging medical technology company with operations in a number of locations. The Board has a strong growth focus and the executive remuneration policies are designed to direct behaviours towards achieving sustainable growth in shareholder value over the medium to long term. However, it must be understood that to attract, motivate and retain high performing executives and in the face of strong competition for talent, some flexibility in our approach is required.

The Board's executive remuneration strategy is to provide 'fair and appropriate' remuneration balanced on a risk and reward framework that supports its business strategy in the short and long term. Board and executive remuneration are reviewed independently on a regular basis. The last formal review was undertaken during the year ended 30 June 2014.

The Board believes that Nanosonics' approach to executive Key Management Personnel (KMP) remuneration is appropriately balanced to fairly reward and motivate an experienced executive team to deliver profitable business growth which meets the expectations of our shareholders.

1.1 Scope

This Remuneration report sets out, in accordance with the relevant *Corporations Act 2001* (Cth) (Corporations Act) and accounting standard requirements, the remuneration arrangements in place for Key Management Personnel of Nanosonics Limited (Nanosonics) during the financial year ended 30 June 2014 (2014 Financial Year).

1.2 Key Management Personnel

Key Management Personnel have authority and responsibility for planning, directing and controlling the activities of Nanosonics and comprise the Non-Executive Directors, Executive Directors and Executive KMP. Details of the Key Management Personnel as at year end are set out in the table below.

Name	Title (at year end)	Change in 2014 Financial Year
Non-Executive Directors		
Maurie Stang	Chairman Member, Audit and Risk Committee Member, Remuneration Committee Member, Nomination Committee Member, R&D and Innovation Committee	Full year Appointed member, R&D and Innovation Committee, July 2014
Richard England	Director Chairman, Audit and Risk Committee Chairman, Remuneration Committee Chairman, Nomination Committee	Full year Chairman, Remuneration Committee from 16 October 2013
David Fisher	Director Member, Audit and Risk Committee Member, Remuneration Committee Member, Nomination Committee Chairman, R&D and Innovation Committee	Full year Appointed Chairman, R&D and Innovation Committee, July 2014
Executive Directors		
Michael Kavanagh	Chief Executive Officer (CEO) and President, Managing Director Member, R&D and Innovation Committee	Appointed 21 October 2013 (Non-executive Director from 30 July 2012 to 20 October 2013) Chairman, Remuneration Committee to 15 October 2013 Appointed member, R&D and Innovation Committee, July 2014
Ron Weinberger	Director and President, Technology Development /Commercialisation Member, R&D and Innovation Committee	Full year CEO and Managing Director from 19 December 2011 to 20 October 2013 Appointed member, R&D and Innovation Committee, July 2014
Executive KMP		
McGregor Grant	Chief Financial Officer(CFO) and Company Secretary	Full year
Gerard Putt	Chief Operations Officer	Full year

2.0 Remuneration governance

This section of the Remuneration Report describes the role of the Board, the Remuneration Committee, and the use of Remuneration Consultants when making remuneration decisions.

2.1 Role of the Board and the Remuneration Committee

The Board is responsible for Nanosonics' remuneration strategy and policy. Consistent with this responsibility, the Board has established a Remuneration Committee which comprises a majority of independent Non-Executive Directors. The members of the Remuneration Committee over the 2014 Financial Year were Richard England, Maurie Stang, David Fisher and Michael Kavanagh (until 20 October 2013).

The role and responsibilities of the Remuneration Committee is set out in its Charter, which was last revised and approved by the Board in July 2014. In summary the Remuneration Committee's role is to:

- Review and approve Nanosonics' remuneration strategy and policy and ensure that appropriate processes and procedures are in place to assess the remuneration levels of the Board and executive KMP and all other employees across the Group;
- Consider and propose to the Board the remuneration of the CEO and consider and approve the remuneration of all designated senior executives;
- Review and approve Nanosonics' incentive schemes, including amounts, terms and offer processes and procedures; and
- Determine and approve equity awards in accordance with policy and shareholder approvals, including testing of vesting and termination provisions.

The Remuneration Committee's role and its interaction with the Board, internal and external advisors, are illustrated below:

The Board
Reviews, applies judgement and, as appropriate, approves the Remuneration Committee's recommendations.

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The Remuneration Committee
The Remuneration Committee operates under the delegated authority of the Board.
The Remuneration Committee is empowered to source any internal resources and obtain external independent professional advice it considers necessary to enable it to make recommendations to the Board on the following:

Remuneration policy, composition and quantum of remuneration components for Executive KMP, including STI performance targets	Remuneration policy in respect of Non-Executive Directors	Recruitment, retention and termination policies and practices	Design features of employee and executive LTI Plan awards, including setting of performance and other vesting criteria

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External Consultants	**Internal Resources**

Further information on the Remuneration Committee's role, responsibilities and membership is contained in the Corporate Governance Statement on pages 53 to 57 of this Annual Report. The Remuneration Committee Charter can be viewed in the Corporate Governance section of Nanosonics' website at www.nanosonics.com.au.

2.2 Use of remuneration consultants

From 1 July 2011, all proposed remuneration consultancy contracts (within the meaning of section 206K of the *Corporations Act 2001)* are subject to prior approval by the Board or the Remuneration Committee in accordance with the *Corporations Act 2001*.

During the year ended 30 June 2014, several remuneration consultancy contracts were entered into by Nanosonics and accordingly the disclosures required under section 300A (1) (h) of the *Corporations Act 2001* are set out below.

Advisor/Consultant FY2014	**Service Provided**	**Remuneration Consultant for the purposes of the *Corporations Act 2001***
Ian Crichton, Remuneration Consultant, CRA Plan Managers Pty Limited	Benchmarking of CEO and President, Chairman and Non-Executive Director remuneration.	Yes
Key questions regarding use of remuneration consultants		
Did a remuneration consultant provide remuneration recommendations in relation to any of the Executive KMP for the financial year?	No. Benchmark data and analysis provided only.	
How much was the remuneration consultant paid by the Company for remuneration related and other services?	CRA – Remuneration Services \$21,585; Other Services \$30,624.	
What arrangements did the Company make to ensure that the making of the remuneration recommendation would be free from undue influence by Executive KMP?	The Company made the following arrangements: • The company implemented a protocol to govern the procedure for procuring advice relating to KMP remuneration. The protocol contained a summary of the process for the engagement of remuneration consultants, the provision of information to the remuneration consultant, and the communication of remuneration recommendations. • The remuneration consultant agreed to adhere to the protocol procedures and was required to advise the Remuneration Committee whether or not it had been subjected to undue influence and provided a Statement of Independence.	
Is the Board satisfied that the remuneration recommendation was free from any such undue influence? What are the reasons for the Board being so satisfied?	Yes, the Board is satisfied for the following reasons: • The protocol with respect to the procurement of remuneration related advice was adhered to, including with respect to engagement of the remuneration consultant, the provision of information to the remuneration consultant in the communication of the remit for remuneration recommendations; • At appropriate times, the remuneration consultant provided written confirmation that it had not been subjected to any undue influence; • The Chairman of the Remuneration Committee met with the Remuneration Consultant in the absence of Executive KMP. There were no concerns raised by the Remuneration Consultant with respect to any undue influence being exerted by the Executive KMP; and • The Remuneration Committee did not observe any evidence that undue influence had been applied.	

3.0 Non-executive Director remuneration

3.1 Non-executive Director remuneration philosophy

Principle	Comment
Fees are set by reference to key considerations	Fees for Non-Executive Directors are based on the nature of the directors’ work and their responsibilities, taking into account the nature and complexity of the Company and the skills and experience of the Director. In determining the level of fees, survey data on comparable companies are considered. Non-Executive Directors’ fees are recommended by the Remuneration Committee and determined by the Board. Shareholders approve the aggregate amount available for the remuneration of Non-Executive Directors. During the year the Remuneration Committee engaged a remuneration consultant to conduct a benchmarking study of Chairman and Non-Executive Director remuneration. Following this study the fees for the Non-Executive Directors were increased effective 1 January 2014 to ensure they remain reasonable and appropriate so as to attract and retain directors with the skills and experience commensurate with the requirements of the role. No increase in fees is proposed for the 2015 Financial Year.
Remuneration is structured to preserve independence whilst creating alignment	To preserve independence and impartiality, Non-Executive Directors are not entitled to any form of incentive payments and the level of their fees is not set with references to measures of Company performance.
Aggregate Board Fees are approved by shareholders.	The total amount of fees paid to Non-Executive Directors in the year ended 30 June 2014 is within the aggregate amount approved at a general meeting of the Company on 19 September 2006 of $500,000 a year. No increase in the pool limit is proposed.
Flexibility in how fees are received	Non-Executive Directors can elect how they wish to receive their total fees – i.e. as a contribution of cash, superannuation contributions or charitable donations.

3.2 Non-executive Director fees and other benefits

Elements	Details	
Board fees per annum – 2014[1]	Board Chairman fee	$145,000
	Board NED fee	$80,000
Post-employment benefits		
Superannuation	Superannuation contributions are included in the Board fees and are made at a rate of 9.25% of base fee (up to the Government’s prescribed maximum contributions limit) which satisfies the Company’s statutory superannuation contributions. The rate has been increased to 9.5% effective from 1 July 2014.	
Other benefits		
Equity instruments	Non-Executive Directors do not receive any performance related remuneration, options or performance shares. Options previously granted have either lapsed or been exercised.	
Other fees/benefits	Non-Executive Directors are reimbursed for out-of-pocket expenses that are directly related to Nanosonics’ business.	

1. Committee fees are not paid to the members of each Committee.

3.3 Non-Executive Director total remuneration

	Year	Fees	Options	Superannuation	Total
Maurie Stang	**2014**	**111,362**	**–**	**10,301**	**121,663**
	2013	90,000	–	8,100	98,100
Richard England	**2014**	**66,613**	**–**	**6,162**	**72,775**
	2013	60,000	879	5,400	66,279
David Fisher	**2014**	**66,613**	**–**	**6,162**	**72,775**
	2013	60,000	–	5,400	65,400
Michael Kavanagh[1]	**2014**	**18,043**	**–**	**1,669**	**19,712**
	2013	55,450	–	4,991	60,441
Total	**2014**	**262,631**	**–**	**24,294**	**286,925**
	2013	265,450	879	23,891	290,220

1. Includes remuneration paid to Mr Kavanagh until his appointment as an Executive Director on 21 October 2013.

4.0 Executive remuneration

4.1 Executive KMP remuneration

Nanosonics' executive remuneration strategy is designed to attract, retain and motivate its executives. Fixed remuneration components are determined having regard to the specific skills and competencies of the executive with reference to both internal and external relativities, particularly local market conditions. The 'at risk' components of remuneration are strategically directed to encourage management (and all participating executives) to strive for superior (risk balanced) performance by rewarding the achievement of targets that are challenging, clearly defined, understood and communicated and within the ambit of accountability of the relevant executive.

Executive KMP remuneration objectives are exemplified through three categories of remuneration, as illustrated below:

Executive KMP Remuneration Objectives			
An appropriate balance of 'fixed' and 'at-risk' components.	Attract, motivate and retain executive talent.	The creation of reward differentiation to drive performance and behaviours.	Shareholder value creation through equity components.

Total Target Remuneration (TTR) is set by reference to the relevant market and internal relativities		
Fixed	At risk	
Total Fixed Remuneration (TFR)	**Short-Term Incentives (STI)**	**Long-Term Incentives (LTI)**
Fixed remuneration is set based on relevant market relativities, reflecting responsibilities, performance, qualifications, experience and location.	STI performance criteria are set by reference to Company and Individual performance targets relevant to the specific position.	LTI targets are linked to both Nanosonics group internal (Revenue) and external (relative Total Shareholder Return (TSR)) outperformance measures.

Remuneration for each component will be delivered as:		
Base Salary plus any fixed elements related to local markets, including superannuation or equivalents.	Part cash and part equity. The equity component is deferred for 1 year. The deferred equity component remains' at risk until vesting.	Equity is held subject to performance and service for 3 years from grant date. The equity is 'at risk' until vesting.

Strategic intent and market positioning		
TFR will generally be positioned at the median (+/-) compared to relevant market based data considering expertise and performance in the role.	Performance incentive is directed to achieving demanding growth targets. TFR + STI is intended to be positioned in 3rd quartile of relevant benchmark.	LTI is intended to align executive KMP with long term growth strategy aligned with shareholders' interests. TFR + STI + LTI is intended to be positioned in the 3rd quartile.

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Total Target Remuneration (TTR)

TTR is intended to be positioned in the 3rd quartile compared to relevant market based comparisons. 4th quartile TTR may result if outperformance is achieved. This strategy is intended to ensure that top quartile remuneration is only received if the Company exceeds the performance objectives set by the Board.

4.2 Remuneration mix and timing of receipt

4.2.1 Remuneration mix

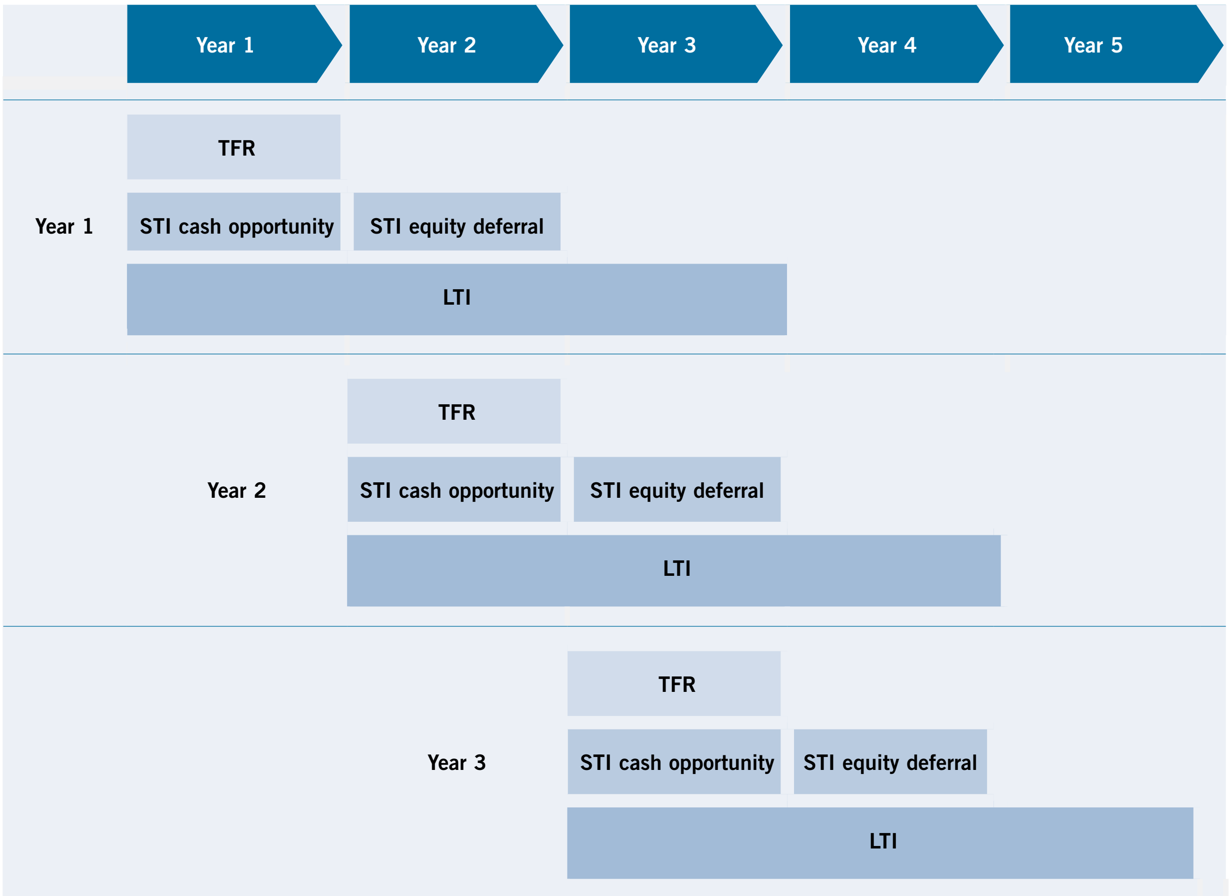
Position	TFR (Cash)	STI (Cash and Equity)	LTI (Equity)
CEO and President	100%	33.3% of Base Salary	33.3% of Base Salary[1]
President, Technology Development/ Commercialisation[2]	100%	33% of Base Salary	33% of Base Salary
Senior Executives (Executive KMP)	100%	25% of Base Salary	25% of Base Salary

1. In connection with the appointment of Mr Kavanagh as CEO and President, at the 2013 AGM shareholders approved the granting of 1,500,000 Performance Rights to Mr Kavanagh. Details of the vesting conditions associated with these Performance Rights are provided in Section 4.4.2 Long Term Incentives.

2. Effective 1 July 2014, the STI and LTI opportunity has been adjusted to 25% of Base Salary.

4.2.2 Remuneration – timing of receipt of the benefit

The three complementary components of Executive KMP remuneration are 'earned' over multiple time ranges. This is illustrated in the following chart.



Each year, fixed remuneration and benefits are paid (monthly) and short term incentives are awarded based on achievement of annual performance targets set. A portion of any STI earned is 'invested' in service rights and deferred for a minimum of 12 months. Each year, a long term equity incentive is provided to eligible and invited executives. The LTI vests after three years if the specified conditions are satisfied. In this way executives are rewarded for short, medium and long term performance aligned to shareholder interests and expectations.

4.3 Total Fixed Remuneration (TFR) explained

Total Fixed Remuneration (TFR) includes all remuneration and benefits paid to an Executive KMP calculated on a Total Employment Cost (TEC) basis. Executive KMP TFR is tested regularly for market competitiveness by reference to appropriate independent and externally sourced comparable benchmark information. Usually, TFR adjustments are only made in response to individual performance (as measured), an increase in job roles, changing market circumstances or promotion. Any adjustment to Executive KMP remuneration is approved by the Board, based on recommendations by the CEO and President and the Remuneration Committee.

4.4 Variable 'at risk' remuneration explained

As set out in Section 4.2, variable remuneration forms a significant portion of the CEO and President and other Executive KMP remuneration opportunity. Apart from being market competitive, the purpose of variable remuneration is to direct executives' behaviours towards maximising Nanosonics' short, medium and long term performance, as measured. The key aspects are summarised below.

4.4.1 Short Term Incentives (STI)

Purpose	The STI arrangements at Nanosonics are designed to reward executives for the achievements against annual performance targets set by the Board at the beginning of the performance period. The STI program is reviewed annually by the Remuneration Committee and approved by the Board. All STI awards to the CEO and President and other Executive KMP are approved by the Remuneration Committee and the Board.
Performance targets	The key performance objectives of Nanosonics are currently directed to achieving a PBT target complemented by the achievement of individual performance goals. The weighting between the PBT target and individual performance goals will depend on the responsibilities and scope of influence of the relevant executive. All targets are set having regard to prior year performance, market conditions and the Board approved budgets. The specific targets are not provided in detail due to their commercial sensitivity. Any anomalies or discretionary elements are approved and validated by the Board.
Rewarding performance	The actual STI awards for Executive KMP in 2014 are as set out in the table in Section 4.6.1.
Payment of STI	To ensure there is an appropriate retention element of STI and to reinforce alignment with shareholders there is a mandatory deferral of a portion of STI. The STI is delivered as follows: • 50% of STI paid in cash • 50% of STI delivered as Nanosonics Performance Rights deferred for one year The equity component will be determined based on the 5 day Volume Weighted Average Market Price of Nanosonics shares as at 31 August each year. As the STI amount awarded as equity has already been earned, there are no further performance measures attached to the Performance Rights. However, they are subject to service conditions until the vesting date.

4.4.2 Long Term Incentives (LTI)

The LTI provides an annual opportunity for selected executives to receive an equity award deferred for three years that is intended to align a significant portion of an executives overall remuneration to shareholder value over the longer term. All LTI awards remain at risk and subject to clawback (forfeiture or lapse) until vesting and must meet or exceed the defined performance hurdles over the vesting period.

Purpose	To retain key executives and align their remuneration opportunity with shareholder value.
Type of equity awarded	Under the Nanosonics Long Term Incentive Scheme (LTIS) selected senior executives are offered Performance Rights (being options to acquire ordinary shares of Nanosonics Limited for a nil exercise price) under the terms of the Nanosonics Employee Share Option Plan (ESOP). See Section 5.1 for further details. Performance Rights do not carry any dividend or voting rights prior to exercise.
Timing	Grants are made each year after shareholder approval to issue securities to Directors has been obtained at the relevant AGM.
LTI allocation	The size of individual LTI grants for the CEO and President and other Executive KMP is determined in accordance with the Board approved remuneration strategy mix. See Section 4.2. The target LTI $ value for each executive once determined is then converted into a number of Performance Rights based on a valuation methodology determined at the grant date, as follows: Performance Rights allocated = LTI $ value divided by 5 day Volume Weighted Average Market Price of Nanosonics shares as at the date of the AGM each year.
Performance hurdles	Equity grants to the CEO and President and other Executive KMP are subject to both internal (Revenue) and external (relative Total Shareholder Return – TSR) Performance Conditions.
CEO and President 2013 Long Term Incentive Scheme (2013 LTIS)	At the 2013 AGM, shareholders approved the granting of 1,500,000 Performance Rights to Mr Kavanagh. The number of Performance Rights granted to Mr Kavanagh was determined at the Board's discretion in connection with Mr Kavanagh's appointment as CEO and President. The 1,500,000 Performance Rights granted to Mr Kavanagh was made in respect of the 2013 and 2014 LTIS grant years. Accordingly, no additional LTIS grant will be made to Mr Kavanagh in respect of the 2014 LTIS. Full details of the vesting conditions associated with the Performance Rights granted to Mr Kavanagh are included in the explanatory notes included with the Notice of the 2013 AGM (Resolution 10) and are summarised below.

CEO and President 2013 Long Term Incentive Scheme (2013 LTIS) – continued

2016 Performance Conditions

Ranking of TSR vs. 2013 LTIS Comparator Group[1]		**Revenue Hurdle**	
Tranche 1: 25% of total Performance Rights granted (375,000)		Tranche 2: 25% of total Performance Rights granted (375,000)	
Performance	% of Performance Rights to vest[(1)]	Revenue in Financial Year 2016	% of Performance Rights to vest[(1)]
< 50th percentile	0%	< $25.7 million	0%
50th to 75th percentile	50% to 100% pro-rata	$25.7 million	25%
At 75th percentile	100%	$29.1 million	50%
		$32.7 million	75%
		$36.7 million	100%

2017 Performance Conditions

Ranking of TSR vs. 2013 LTIS Comparator Group[2]		**Revenue Hurdle**	
Tranche 3: 25% of total Performance Rights granted (375,000)		Tranche 4: 25% of total Performance Rights granted (375,000)	
Performance	% of Performance Rights to vest[1]	Revenue in Financial Year 2017	% of Performance Rights to vest[1]
< 50th percentile	0%	< $30.9 million	0%
50th to 75th percentile	50% to 100% pro-rata	$30.9 million	25%
At 75th percentile	100%	$36.4 million	50%
		$42.6 million	75%
		$49.5 million	100%

1. TSR measurement period is 8 November 2013 to the date of the release of Nanosonics' FY16 financial statements.
2. TSR measurement period is 8 November 2013 to the date of the release of Nanosonics' FY17 financial statements.
3. Straight line interpolation will apply to incremental results.

Service Conditions

In addition to the above performance conditions, the Performance Rights will only vest if Mr Kavanagh remains in continuous employment with Nanosonics from the date of the grant to the respective vesting date of each Tranche.

Special provisions, in accordance with company policies, may apply in the event of termination of employment or a change of control.

Other Executive KMP 2013 Long Term Incentive Scheme (2013 LTIS)	A summary of the vesting conditions associated with the Performance Rights granted to other Executive KMP under the 2013 LTIS are summarised below.

Ranking of TSR vs. 2013 LTIS Comparator Group[1]		Revenue Hurdle	
Tranche 1: 50% of total Performance Rights granted		Tranche 2: 50% of total Performance Rights granted	
Performance	% of Performance Rights to vest[1]	Revenue in Financial Year 2016	% of equity to vest[1]
< 50th percentile	0%	< $25.7 million	0%
50th to 75th percentile	50% to 100% pro-rata	$25.7 million	25%
At 75th percentile	100%	$29.1 million	50%
		$32.7 million	75%
		$36.7 million	100%

1. TSR measurement period is 8 November 2013 to the date of the release of Nanosonics' FY16 financial statements.
2. Straight line interpolation will apply to incremental results.

Service Conditions

In addition to the above performance conditions, the Performance Rights will only vest if the Executive KMP remains in continuous employment with Nanosonics from the date of the grant to the respective vesting date of each Tranche.

Special provisions, in accordance with company policies, may apply in the event of termination of employment or a change of control.

Other Executive KMP 2012 Long Term Incentive Scheme (2012 LTIS)	In August 2013, Performance Rights were granted to other Executive KMP under the 2012 LTIS with an FY15 revenue hurdle of $50.0 million or more and Net Profit After Tax hurdle of 12% of revenue or more. In addition to the performance conditions, the Performance Rights will only vest if the Executive KMP remains in continuous employment with Nanosonics from the date of the grant to the respective vesting date. 100% of the Performance Rights will vest once the performance hurdles and service conditions are achieved.

4.5 Other remuneration elements and disclosures relevant to Executive KMP

4.5.1 Clawback

In accordance with the ASX Corporate Governance Guidelines the Board has clear policies regarding the deferral of performance-based remuneration as set out in Section 4.4.1. Policies concerning the reduction, cancellation or clawback of performance-based remuneration in the event of serious misconduct or a material misstatement in the entity's financial statements have not been determined, as yet. These policies will be developed as clear market trends emerge.

4.5.2 Securities trading restrictions

Under the Nanosonics Limited Securities Trading Policy and in accordance with the *Corporations Act 2001*, securities granted under Nanosonics' equity incentive schemes must remain at risk until vested, or until exercised if options or performance rights. It is a specific condition of grant that no schemes are entered into by an individual or their associates, that specifically protects the unvested value of shares, options or performance rights allocated.

KMPs are not permitted to deal at any time in financial products such as options, warrants, futures or other financial products issued over Nanosonics' securities by third parties such as banks and other institutions without the prior approval of the Board. An exception may apply where the securities form a component of a listed portfolio or index product.

KMPs are not permitted to enter into transactions in products associated with the securities without the prior approval of the Board, which operate to limit the economic risk of their security holding in the Company (e.g. hedging arrangements).

Nanosonics, as required under the ASX Listing Rules, has a formal policy setting down how and when employees, including KMPs of Nanosonics Limited, may deal in Nanosonics securities. A copy of the Company's Securities Trading Policy is available on the Nanosonics website, www.nanosonics.com under Investor Centre, Corporate Governance.

4.5.3 Cessation of employment provisions

The provisions that apply for STI and LTI awards in the case of cessation of employment are detailed in Section 6.

4.5.4 Change of control

The provisions that apply for STI and LTI awards in the case of a change of control are detailed in Section 6.

4.5.5 Conditions of LTI grants

The conditions under which LTI awards (Performance Rights) are granted are approved by the Board in accordance with the relevant scheme rules as summarised in Section 5.

4.6 Relationship between Nanosonics' performance and Executive KMP remuneration

As explained in Section 4.2, Nanosonics' remuneration framework aims to incentivise executive KMP towards sustainable growth of the business and the creation of shareholder value in the short, medium and long term.

4.6.1 Short Term Incentives

Executive KMP STI opportunity and actual 2014 STI awarded are set out in the table below:

Executive KMP	Position	Maximum STI % of 2014 TFR[1]	STI awarded as a % of potential[1]	STI cash award in 2014 ($)[2]	Deferred equity STI award ($)[3]	% Forfeited[4]
Michael Kavanagh	CEO and President, Managing Director	43%	100%	65,305	65,306	–
Ron Weinberger	President, Technology Development/Commercialisation	27%	96%	49,104	49,104	4%
McGregor Grant	CFO and Company Secretary	23%	97.5%	35,751	35,751	2.5%
Gerard Putt	Chief Operations Officer	23%	92.5%	26,551	26,551	7.5%

1. Relates to STI % both cash and deferred equity opportunity. The deferred equity will be awarded the following year.
2. Amounts included in the remuneration for the financial year represent the maximum cash STI opportunity related to the financial year based on the achievement of individual goals and satisfaction of specified performance criteria. The amount was finally determined on 8 August 2014 after performance reviews were completed and approved by the Board.
3. The equivalent number of Performance Rights to be awarded in the following year will be determined as set out in section 4.4.1 of the Remuneration Report.
4. The amounts forfeited are due to the performance criteria not being fully met in relation to the current financial year.

Short Term Incentives have been accrued in respect of the 2014 financial year because the performance conditions set by the Board have been met.

4.6.2 Long Term Incentives

Executive KMP are only entitled to a benefit under the current Company's LTI scheme if both Revenue and relative Total Shareholder Return (TSR) targets are met.

Revenue growth is considered a priority for Nanosonics at this stage of its development, in the opinion of the Board. Relative TSR is a generally accepted proxy for creation of shareholder value. The Board believes a balance between these two performance criteria is a sound guide to medium and long term performance.

Revenue

The table below summarises Nanosonics' revenue for the financial years ended 30 June, 2012, 2013 and 2014.

Financial year	Revenue $'000
2014	21,492
2013	14,899
2012	12,301

A portion of the 2013 LTI grant to all Executive KMP, including the CEO and President, requires that revenues in FY16 equal or exceed $36.7 million for full vesting. A portion of the 2013 LTI grant for the CEO and President requires that revenues in FY17 equal or exceed $49.5 million for full vesting. This represents a 70.8% and 130.3% increase respectively relative to the 2014 Financial Year for the maximum opportunity to be realised. Momentum achieved in the 2014 Financial Year will need to continue into the 2015 Financial Year and beyond for these targets to be met. If they are met the Board believes an appropriate balance of results and benefit will have been achieved.

Relative Total Shareholder Return

Testing of performance against the relevant comparator group will only occur at the vesting date of each grant. To date, no equity grant subject to a TSR hurdle has vested. The TSR hurdle set and the relative vesting schedule meet contemporary market standards according to independent advice received by the Board.

4.7 Executive remuneration tables

		Fixed Remuneration						Variable Remuneration			Total	Proportion of Total Remuneration		
		Short-term benefits			Long-term benefits		Total	Short-term	Equity Compensation	Total		Performance related	Non-performance related[2]	Value of options and rights
	Year	Salary and fees[8]	Non-monetary benefits	Other	Superannuation	Other long term benefits[8]		Cash bonus[6]	Options and performance rights[7]			%	%	%
Michael Kavanagh[1]	**2014**	**267,446**	**–**	**–**	**13,094**	**20,903**	**301,443**	**65,305**	**232,933**	**298,238**	**599,681**	**50%**	**0%**	**39%**
	2013	–	–	–	–	–	–	–	–	–	–	–	–	–
Ron Weinberger	**2014**	**290,923**	**39,459**	**–**	**17,885**	**30,473**	**378,740**	**49,104**	**147,533**	**196,637**	**575,377**	**34%**	**0%**	**26%**
	2013	300,077	42,886	3,100	16,470	24,116	386,649	32,901	125,877	158,778	545,427	28%	1%	23%
McGregor Grant[3]	**2014**	**273,037**	**–**	**506**	**17,775**	**22,933**	**314,251**	**35,751**	**107,373**	**143,124**	**457,375**	**16%**	**15%**	**23%**
	2013	270,892	–	527	16,470	13,909	301,798	29,751	173,075	202,826	504,624	11%	29%	34%
Gerard Putt[4]	**2014**	**214,575**	**–**	**–**	**17,775**	**17,819**	**250,169**	**26,551**	**59,737**	**86,288**	**336,457**	**18%**	**8%**	**18%**
	2013	208,546	–	231	16,470	21,031	246,278	24,227	79,424	103,651	349,929	13%	17%	23%
Total	**2014**	**1,045,981**	**39,459**	**506**	**66,529**	**92,128**	**1,244,603**	**176,711**	**547,576**	**724,287**	**1,968,890**	**5%**	**32%**	**28%**
Total (restated)[5]	2013	779,515	42,886	3,858	49,410	59,056	934,725	86,879	378,376	465,255	1,399,980	15%	18%	27%

1. Includes remuneration paid to Mr Kavanagh since his appointment as an Executive Director on 21 October 2013.
2. Non-performance related remuneration relates to options granted as part of employment contracts subject to service conditions.
3. Mr Grant joined the Company on 28 April 2011 and in connection with his appointment, he was granted 1,000,000 options which vest in 4 tranches, subject to service conditions.
4. Mr Putt joined the Company on 27 April 2011 and in connection with his appointment, he was granted 400,000 options, which vest in 4 tranches, subject to service conditions.
5. The 2013 KMP remuneration disclosure was restated to exclude executives Michael Potas, Kirste Courtney and Vincent Wang who were previously included as one of the five named executives who received the highest remuneration in 2013.
6. The cash bonus is for the performance during the respective financial year based the criteria set out in Section 4.4.1. 2014 amounts represent the maximum cash STI opportunity related to the financial year based on the achievement of individual goals and satisfaction of specified performance criteria. Actual cash STI award is disclosed in Section 4.6.1.
7. The amount disclosed is the amount of the fair value of the options and rights recognised as an expense in each reporting period. The ability to exercise the options and rights are subject to vesting conditions. The fair values of the options and rights that are subject to non-market performance conditions are calculated at the date of the grant using Binomial Approximation model. The fair values of performance rights that are subject to TSR performance conditions are calculated at the date of the grant using the Monte-Carlo simulation model.
8. As disclosed in note 2 to the financial statements, the Group changed its accounting policy in respect of employee benefits with the adoption of AASB119 Employee Benefits. As a result of this change, annual leave is included in other long term benefits, previously shown as a short term employee benefit. Consistent with that change, cash compensated annual leave absences and accrual is now classified as other long term benefit in both current and prior periods. Other long term benefits include annual leave and long service leave benefits.

4.8 Executive remuneration tables – unaudited

This table represents the value to the Executive KMP of cash paid and vested equity awards (intrinsic value) received during the year, and unvested equity awards (IFRS-2 value) granted during the financial year at risk. The LTI equity granted is a value determined under IFRS-2 which may or may not vest depending on future outcomes that are uncertain. Accordingly, this table incorporates data that could represent an accumulation of outcomes arising from multiple years.

		Short-term benefits		Past at-risk remuneration received	Actual remuneration received during year	Future at risk remuneration received during year	
	Year	Fixed Remuneration[2]	Incentives[3]	Value of Performance Rights[4]		STI (deferred as equity)	LTI (Equity) granted [5]
Michael Kavanagh[1]	**2014**	**287,369**	**–**	**–**	**287,369**	**–**	**1,158,938**
	2013	–	–	–	–	–	–
Ron Weinberger	**2014**	**391,189**	**–**	**73,940**	**465,129**	**–**	**103,089**
	2013	372,456	32,901	27,963	433,320	33,861	671,000
McGregor Grant	**2014**	**311,626**	**–**	**52,433**	**364,059**	**–**	**181,902**
	2013	301,798	29,751	–	331,549	30,573	–
Gerard Putt	**2014**	**247,408**	**–**	**42,670**	**290,078**	**–**	**150,093**
	2013	246,278	24,227	–	270,505	24,865	–
Total	**2014**	**1,237,592**	**–**	**169,043**	**1,406,635**	**–**	**1,594,022**
Total	2013	920,532	86,879	27,963	1,035,374	89,299	671,000

1. Includes remuneration paid to Mr Kavanagh since his appointment as an Executive Director on 21 October 2013.
2. Base salary, non-monetary, other cash benefits received during the year (excludes Annual Leave and Long Service Leave accrual).
3. STI received as cash in respect of the 2013 Financial Year. Excludes cash STI accrued in respect of the 2014 Financial Year.
4. Intrinsic value at vesting date of options and performance rights issued in previous periods that vested during the year.
5. Accounting value of performance rights awarded during the year that are unvested and subject to vesting conditions (i.e. achievement of performance conditions and/or service conditions).

5.0 Employee Share Scheme information

This section provides:

1. A description of the Employee Share Schemes (ESS) Nanosonics uses to provide equity rewards to Nanosonics employees;
2. Disclosures required in relation to ESS grants provided to KMP;
3. Disclosures required about ESS instruments that Nanosonics has issued; and
4. Disclosures required in relation to Nanosonics' shares and other ESS instruments held by KMP.

5.1 Employee Share Schemes operated by Nanosonics

Plan Name	Type of Instruments	Purpose	Details
Nanosonics Deferred Employee Share Plan (DESP) Established in 2007 Date last approved by shareholders: 8 November 2013	Ordinary Shares	The purpose of the Share Plans is to provide eligible employees (including Executive Directors but excluding Non-Executive Directors) with performance incentives through opportunities to acquire beneficial ownership of shares in the Company and to access the taxation concessions available under the Income Tax Assessment Act. The DESP is also used for the settlement of shares on exercise of options in the Share Option Plans.	Since the DESP was last approved 673,697 shares (from the exercise of ESOP options) have been issued to the Plan. As at the date of this report 1,111,874 shares remain outstanding.
Nanosonics Exempt Employee Share Plan (EESP) Established in 2007 Date last approved by shareholders: 8 November 2013			No grants to date have been made under the EESP.
Nanosonics Employee Share Option Plan (ESOP) Established in 2007 Date last approved by shareholders: 8 November 2013	Options	The purpose of the Share Option Plans is to permit the Company, as part of its overall remuneration programs, to provide long-term incentives for employees (including Executive Directors), consultants and contractors to Nanosonics who deliver long-term shareholder returns. The Plans provide participants with an opportunity to acquire a beneficial ownership of shares in the Company and to access the taxation concessions available under the Income Tax Assessment Act.	Since the ESOP was last approved 2,402,899 options have been issued and 1,073,697 options exercised. As at the date of this report 5,656,641 options remain outstanding.
Nanosonics General Share Option Plan (GSOP) Established in 2007 Date last approved by shareholders: 8 November 2013			Since the GSOP was last approved 261,666 options have been exercised. There have been no new issues. As at the date of this report 503,334 options remain outstanding.

5.2 ESS grants to KMP

5.2.1 Analysis of share-based payments granted as remuneration

Details of the vesting profiles for the year and as at 30 June 2014 of the Options and Performance Rights granted as remuneration to each Executive KMP are set out below:

	Options/Performance Rights												Vesting in future years			
	Description	Grant Date	Expiry Date	Exercise Price	Number granted	Number vested during the year	% vested during the year	Number vested to date	Number lapsed/ forfeited during the year	% lapsed/ forfeited	Balance at year end	Intrinsic value at year end	2015	2016	2017	2018
Michael Kavanagh	2013 LTIS Tranche 1	Nov-13	30-Sep-16	$0.00	375,000	–	–	–	–	–	375,000	296,250			375,000	
	2013 LTIS Tranche 2	Nov-13	30-Sep-16	$0.00	375,000	–	–	–	–	–	375,000	296,250			375,000	
	2013 LTIS Tranche 3	Nov-13	30-Sep-17	$0.00	375,000	–	–	–	–	–	375,000	296,250				375,000
	2013 LTIS Tranche 4	Nov-13	30-Sep-17	$0.00	375,000	–	–	–	–	–	375,000	296,250				375,000
Ron Weinberger	2013 LTIS Tranche 1	Nov-13	30-Sep-16	$0.00	67,409	–	–	–	–	–	67,409	53,253			67,409	
	2013 LTIS Tranche 2	Nov-13	30-Sep-16	$0.00	67,409	–	–	–	–	–	67,409	53,253			67,409	
	2013 Deferred STI	Apr-13	01-Apr-14	$0.00	38,726	38,726	100%	38,726	–	–	–	–				
	2012 LTIS	Nov-12	30-Sep-15	$0.00	1,220,000	–		–	–	–	1,220,000	963,800		1,220,000		
	2012 Deferred STI	Nov-12	01-Oct-13	$0.00	29,881	29,881	100%	29,881	–	–	–	–				
	Options	Jul-10	19-Jul-14	$0.56	200,000	68,000	34%	200,000	–	–	200,000	46,800				
McGregor Grant	2013 LTIS Tranche 1	Mar-14	30-Sep-16	$0.00	47,888	–	–	–	–	–	47,888	37,832			47,888	
	2013 LTIS Tranche 2	Mar-14	30-Sep-16	$0.00	47,889	–	–	–	–	–	47,889	37,832			47,889	
	2013 Deferred STI	Apr-13	01-Apr-14	$0.00	35,578	35,578	100%	35,578	–	–	–	–				
	2012 LTIS	Aug-13	30-Sep-15	$0.00	145,307	–	–	–	–	–	145,307	114,793		145,307		
	2012 Deferred STI	Nov-12	01-Oct-13	$0.00	26,478	26,478	100%	26,478	–	–	–	–				
	Options	May-11	28-Apr-16	$0.85	1,000,000	333,333	33%	833,334	–	–	1,000,000	–	166,666			
Gerard Putt	2013 LTIS Tranche 1	Mar-14	30-Sep-16	$0.00	39,514	–	–	–	–	–	39,514	31,216			39,514	
	2013 LTIS Tranche 2	Mar-14	30-Sep-16	$0.00	39,515	–	–	–	–	–	39,515	31,217			39,515	
	2013 Deferred STI	Apr-13	01-Apr-14	$0.00	29,357	29,357	100%	29,357	–	–	–	–				
	2012 LTIS	Aug-13	30-Sep-15	$0.00	119,898	–	–	–	–	–	119,898	94,719		119,898		
	2012 Deferred STI	Nov-12	01-Oct-13	$0.00	21,189	21,189	100%	21,189	–	–	–	–				
	Options	May-11	27-Apr-16	$0.85	400,000	133,333	33%	333,334	–	–	400,000	–	66,666			

5.2.2 Exercise of options granted as remuneration

During the financial year, the following shares were issued on the exercise of options previously granted as part of remuneration to Key Management Personnel:

	Number of shares	Amount paid per share ($)	Total amount paid ($)	Net market value ($)
Richard England	50,000	0.55	27,500	14,750
Ron Weinberger	68,607	–	–	57,276
McGregor Grant	62,056	–	–	51,763
Gerard Putt	50,546	–	–	42,132
Total	**231,209**		**27,500**	**165,921**

There are no amounts unpaid on the shares issued as a result of the exercise of the options in prior years.

5.2.3 Analysis of movement in options

The movement in number and value during the financial year of Options and Performance Rights over ordinary shares of Nanosonics Limited held by Key Management Personnel is detailed below.

	Balance at start of the year		Granted in year		Exercised in year		Forfeited in year		Balance at end of the year	
	Number	Value ($)[1]	Number	Value ($)[1]	Number	Value($)[2]	Number	Value ($)[2]	Number	Value ($)[1]
Richard England	50,000	15,075	–	–	50,000	14,750	–	–	–	–
Michael Kavanagh	–	–	1,500,000	1,158,938	–	–	–	–	1,500,000	1,158,938
Ron Weinberger	1,488,607	767,761	134,818	103,089	68,607	58,028	–	–	1,554,818	836,989
McGregor Grant	1,062,056	531,773	241,084	181,902	62,056	52,433	–	–	1,241,084	683,102
Gerard Putt	450,546	224,865	198,927	150,093	50,546	42,670	–	–	598,927	350,093
Total	**3,051,209**	**1,539,474**	**2,074,829**	**1,594,021**	**231,209**	**167,881**	**–**	**–**	**4,894,829**	**3,029,121**

1. The 'fair value' of options granted in the year is the fair value of the options calculated as grant date using the Black-Scholes model and derived applying the valuation methodology prescribed under IFRS-2. The total value of the options granted is included in the table above. This amount is allocated to remuneration over the vesting period (i.e. in years 30 June 2012 to 30 June 2015).
2. The value of options exercised and forfeited during the year is calculated as the market price of shares of the company on the ASX as at close of trading on the date the options were exercised or forfeited after deducting the price paid or payable to exercise the option.

5.3 Fair value of share-based compensation

The following factors and assumptions were used in determining the fair value on grant date of options and performance rights granted to directors and Key Management Personnel under ESOP which were unexpired on 30 June 2014, including those granted during the period:

Option/ Performance Rights Description	Vesting Conditions	Grant date	Expiry date	Share price at grant date($)	Exercise price ($)	Valuation Model	Estimated volatility	Risk free interest rate	Fair Value of option($)
Options	Service Condition	Aug-10	19-Jul-14	0.54	0.56	Binomial	74.87%	4.77%	0.31
Options	Service condition	May-11	28-Apr-16	0.80	0.85	Binomial	73.62%	5.14%	0.50
2012 LTIS	FY15 Revenue, net profit after tax and service	Nov-12	30-Sep-15	0.55	–	Binomial	45.46%	2.58%	0.55
2012 LTIS	FY15 Revenue, net profit after tax and service	Aug-13	30-Sep-15	0.78	–	Binomial	45.49%	2.35%	0.78
2013 LTIS Tranche 1 - CEO	Relative TSR performance and service	Nov-13	30-Sep-16	0.85	–	Monte Carlo	45.00%	3.00%	0.68
2013 LTIS Tranche 2 - CEO	FY16 Revenue and service	Nov-13	30-Sep-16	0.85	–	Binomial	45.00%	3.00%	0.85
2013 LTIS Tranche 3 - CEO	Relative TSR performance and service	Nov-13	30-Sep-17	0.85	–	Monte Carlo	45.00%	3.20%	0.71
2013 LTIS Tranche 4 - CEO	FY17 Revenue and service	Nov-13	30-Sep-17	0.85	–	Binomial	45.00%	3.20%	0.85
2013 LTIS Tranche 1 - Other KMP	Relative TSR performance and service condition	Mar-14	30-Sep-16	0.80	–	Monte Carlo	45.00%	2.68%	0.63
2013 LTIS Tranche 2 - Other KMP	FY16 Revenue and service	Mar-14	30-Sep-16	0.80	–	Binomial	45.00%	2.68%	0.80

5.4 KMP equity interests

In accordance with the Corporations Act (section 205G (1)), Nanosonics is required to notify the interests (shares and rights to shares) of directors to the ASX. In the interests of transparency and completeness of disclosure we have provided this information for each director (as required under the Corporations Act) and all other Executive KMP.

Equity interests as at 30 June 2014	Nanosonics Limited ordinary shares[1]	Options over Nanosonics Limited ordinary shares	Total intrinsic value of NAN securities as at year end ($)[2/3]
Non-Executive Directors			
Maurie Stang	28,402,424	–	22,437,915
Richard England	128,301	–	101,358
David Fisher	812,705	–	642,037
Executive Directors			
Michael Kavanagh	150,000	1,500,000	1,303,500
Ron Weinberger	68,607	1,554,818	1,171,306
Other Executive KMP			
McGregor Grant	77,056	1,241,084	251,331
Gerard Putt	69,046	598,927	211,699

1. Includes the number of Nanosonics shares issued to Executives under the DESP.
2. The intrinsic value of Nanosonics shares calculated as at the closing NAN price on 30 June 2014 times the number of shares.
3. The intrinsic value of options calculated as at the closing NAN price on 30 June 2014 less the applicable exercise price times the number of options.

Equity interests as at the date of this report	Nanosonics Limited ordinary shares[1]	Options over Nanosonics Limited ordinary shares
Non-Executive Directors		
Maurie Stang	28,402,424	–
Richard England	128,301	–
David Fisher	812,705	–
Executive Directors		
Michael Kavanagh	150,000	1,500,000
Ron Weinberger	120,607	1,354,818
Other Executive KMP		
McGregor Grant	77,056	1,241,084
Gerard Putt	69,046	598,927

1. Includes the number of Nanosonics shares issued to Executives under the DESP.

Refer to Section 4.5.2 regarding Securities Trading Restrictions.

5.5 KMP Share movement

The numbers of shares in the Company held during the financial year by Key Management Personnel, including their personally-related parties, are set out below.

	Balance at start of the year	Received during the year on the exercise of options	Other net changes during the year	Balance at end of the year
Non-Executive Directors				
Maurie Stang	28,402,424	–	–	28,402,424
Richard England	78,301	50,000	–	128,301
David Fisher	812,705	–	–	812,705
Executive Directors				
Michael Kavanagh	100,000	–	50,000	150,000
Ron Weinberger	859,672	68,607	(859,672)	68,607
Other Executive KMP				
McGregor Grant	15,000[1]	62,056	–	77,056
Gerard Putt	18,500[1]	50,546	–	69,046

1. This represents shareholding of a close family member of the KMP.

6.0 Employment agreements

6.1 CEO and President

The following sets out the key terms of the employment agreement for the CEO and President, Michael Kavanagh.

Length of contract	Ongoing employment contract until notice is given by either party.
Fixed Remuneration	$410,000 p.a., inclusive of superannuation and reviewed annually. Increased to $430,000 p.a., inclusive of superannuation effective 1 July 2014.
Short-term Incentive	33.3% of Base Salary
Long-term Incentive	33.3% of Base Salary. LTI arrangements in respect of 2013 and 2014 are described in section 4.4.2
Notice periods	In order to terminate the employment arrangements, is required to provide Nanosonics with 9 months written notice. Nanosonics must provide with 9 months written notice.
Resignation	On resignation, unless the Board determines otherwise: • All unvested STI or LTI benefits are forfeited; and • All vested but unexercised STI or LTI benefits are forfeited after 30 days following cessation of employment.
Termination on notice by Nanosonics	Nanosonics may terminate employment by providing 9 months' written notice or payment in lieu of the notice period based on fixed remuneration. Upon termination on notice by Nanosonics, unless the Board determines otherwise: • All unvested STI or LTI benefits are forfeited; and • All vested but unexercised STI or LTI benefits are forfeited after 30 days following cessation of employment.
Change of control	In the event of a takeover or change in control of Nanosonics Limited, any unvested Performance Rights will vest on a pro-rata basis based on the most current financial reports available at the time a change of control occurs, unless otherwise determined by the Board. The pro-rata period will be calculated from the grant date to the change of control date. Performance Rights that vest following a change of control will not generally be subject to restrictions on dealings.
Termination for serious misconduct	Nanosonics may immediately terminate employment at any time in the case of serious misconduct, and Mr Kavanagh will be only be entitled to payment of fixed remuneration up to the date of termination. On termination without notice by Nanosonics in the event of serious misconduct all unvested STI or LTI benefits will be forfeited. The treatment of any vested but unexercised STI or LTI benefits will be at the discretion of the Board.
Statutory Entitlements	Payment of statutory entitlements of long service leave and annual leave applies in all events of separation.
Post-employment Restraints	Mr Kavanagh will be restrained for a period of up to 24 months after termination of his employment by either party from being engaged in any of the following activities: • Engaging with clients of Nanosonics with a view to obtaining the custom of those clients in a business that is the same as or similar to Nanosonics' business; • Interfering with the relationship between Nanosonics, its customers, employees, agents, contractors or suppliers; • Inducing or assisting in the inducement of any employee, agent or contractor of Nanosonics to leave their employment or terminate their contract; or • Carrying-on or becoming in any way involved in any trade or business that is in competition with Nanosonics.

6.2 Other Executive KMP

The following sets out details of the employment agreements relating to other Executive KMP. The terms for all other Executive KMP are similar, but do on occasion, vary to suit different needs.

Length of contract	Ongoing employment contract until notice is given by either party.
Notice periods	In order to terminate the employment arrangements, either Nanosonics or the Executive KMP are required to provide the other party with written notice as summarised below: • Ron Weinberger: 6 months • McGregor Grant: 4 months • Gerard Putt: 3 months
Resignation	On resignation, unless the Board determines otherwise: • All unvested STI or LTI benefits are forfeited; and • All vested but unexercised STI or LTI benefits are forfeited after 30 days following cessation of employment.
Termination on notice by Nanosonics	Nanosonics may terminate employment by providing the relevant written notice or payment in lieu of the notice period based on fixed remuneration. On termination on notice by Nanosonics, unless the Board determines otherwise: • All unvested STI or LTI benefits are forfeited; and • All vested but unexercised STI or LTI benefits are forfeited after 30 days following cessation of employment.
Change of control	In the event of a takeover or change in control of Nanosonics Limited, any unvested Performance Rights will vest on a pro-rata basis based on the most current financial reports available at the time a change of control occurs, unless otherwise determined by the Board. The pro-rata period will be calculated from the grant date to the change of control date. Performance Rights that vest following a change of control will not generally be subject to restrictions on dealings.
Termination for serious misconduct	Nanosonics may immediately terminate employment at any time in the case of serious misconduct, and the Executive KMP will only be entitled to payment of fixed remuneration up to the date of termination. On termination without notice by Nanosonics in the event of serious misconduct, all unvested STI or LTI benefits will be forfeited. The treatment of any vested but unexercised STI or LTI benefits will be at the discretion of the Board.
Statutory Entitlements	Payment of statutory entitlements of long service leave and annual leave applies in all events of separation.
Post-employment Restraints	All Executive KMP will be restrained for a period of up to 24 months after termination of their employment by either party from being engaged in any of the following activities: • Engaging with clients of Nanosonics with a view to obtaining the custom of those clients in a business that is the same as or similar to Nanosonics' business. • Interfering with the relationship between Nanosonics, its customers, employees, agents, contractors or suppliers. • Inducing or assisting in the inducement of any employee, agent or contractor of Nanosonics to leave their employment or terminate their contract. • Carrying-on or becoming in any way involved in any trade or business that is in competition with Nanosonics.

7.0 Key Management Personnel transactions

7.1 Loans to Key Management Personnel and their related parties

During the financial year and to the date of this report, the Group made no loans to directors and other Key Management Personnel and none were outstanding as at 30 June 2014 (2013: Nil).

7.2 Other transactions with Key Management Personnel

Certain directors and Key Management Personnel, or their personally-related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities. A number of these entities transacted with the Company in the 2013 and 2014 Financial Years. The terms and conditions of the transactions were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions with unrelated entities on an arms-length basis.

Directors and Key Management Personnel	Related entities	Transactions
Maurie Stang	Gryphon Capital Pty Ltd	Director fees and services received
Maurie Stang	Novapharm Research (Australia) Pty Ltd	Services received
Maurie Stang	Ramlist Pty Ltd	Rent of premises
Maurie Stang	Regional Healthcare Group Pty Ltd	Products purchased, services received and products sold
Richard England	Angleterre Pty Ltd and Domkirke Pty Ltd	Director fees and services received

The aggregate amounts of each of the above types of transactions with directors and key management personnel of the Group were:

	2014 $'000	2013 $'000
Amounts recognised as revenue		
Products and services sold	**1,812**	1,056
Amounts recognised as expenses		
Products purchased and services received	**357**	553
Rent of premises	**184**	185

The aggregate amounts of assets and liabilities relating to the above types of transactions with directors and key management personnel of the Group were:

	2014 $'000	2013 $'000
Assets		
Current receivables	**450**	53
Liabilities		
Current liabilities	**18**	150

Indemnifying officers or auditor

During the financial year, the Company paid insurance premiums to insure the directors and secretary and Key Management Personnel of the Company and 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 the Group, 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 positions 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 in this report the amount of the premium paid in respect of the insurance policy, as such disclosure is prohibited under the terms of the contract.

No indemnities have been given or insurance premiums paid, during or since the financial year, for any person who is or has been an auditor for the Group.

Proceedings on behalf of the Company

No person has applied to the Court under section 237 of the *Corporations Act 2001* for leave to bring proceedings on behalf of the Company or intervene in any proceedings to which the Company is a party, for the purpose of taking responsibility on behalf of the Company for all or part of those proceedings.

No proceedings have been brought or intervened in on behalf of the Company with leave of the Court under section 237 of the *Corporations Act 2001*.

Rounding

The amounts contained in this report and in the financial report have been rounded to the nearest $1,000 (where rounding is applicable) and where noted ($'000) under the option available to the Company under ASIC CO 98/100. The Company is an entity to which the class order applies.

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 the Company and/or the Group are important.

The Board of directors has considered the position and, in accordance with advice received from the Audit and Risk Committee, is satisfied that the provision of the non-audit services by the auditor, if any, did not compromise the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

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

The auditor of the Group, UHY Haines Norton and its related practice firms did not provide any non-audit services during the year.

Officers of the Company who are former audit partner of UHY Haines Norton

There are no officers of the company who are former audit partners of UHY Haines Norton.

Auditor's independence declaration

A copy of the auditor's independence declaration as required under section 307C of the *Corporations Act 2001* is included on page 59 of this report.

Auditor

UHY Haines Norton continues in office as auditor in accordance with section 327 of the *Corporations Act 2001*.

This report, which includes the review of operations (on pages 8 to 13) and the Information on the directors, company secretaries and senior management (on pages 18 to 20), is made and signed in accordance with a resolution of directors, pursuant to section 298 (2)(a) of the *Corporations Act 2001,* on 21 August 2014.

Richard England

Richard England
Director
Sydney

21 August 2014

Corporate governance statement

The Board of directors of Nanosonics Limited is committed to ensuring that its policies and practices reflect good corporate governance consistent with the ASX Listing Rules and the ASX Corporate Governance Principles and Recommendations with 2010 Amendments (2nd Edition).

The Company has commenced work on implementing the recommendations in the March 2014 Amendments (3rd Edition).

This Corporate Governance Statement sets out Nanosonics Limited's key corporate governance principles and practices and was approved by the Board on 28 July 2014. A copy is available on the Company's website at http://www.nanosonics.com.au/Investor-Centre/Corporate-Governance.

Principle 1 – Lay solid foundations for management and oversight

Role of the Chairman

The Chairman is responsible for leading the Board, its meetings and directors, so that all directors are able to contribute effectively, all matters are properly considered and there is clear decision-making. The Chairman has ultimate responsibility for corporate governance.

Role of the Board

Under the leadership of the Chairman, the role of the Board is to provide strategic guidance to the Company and to provide effective oversight of its management for the benefit of all stakeholders.

The Board acts on behalf of shareholders and is accountable to the shareholders for the overall strategy, governance and performance of the Company. The Board retains ultimate authority over the management of the Group; however day-to-day management of the Group's affairs and the implementation of its strategies are formally delegated by the Board to the CEO and President (Managing Director) and senior executives. The respective roles and responsibilities of the Board and senior executives, and how they are separate, are set out in detail in the Company's Board Charter.

The Board meets regularly in accordance with an agreed schedule and special meetings are held as required. Details of directors' attendances at meetings of the Board are shown in the Directors' report contained in the Company's Annual Report.

Roles of senior executives

The Company sets responsibilities and performance expectations for all senior executives, including executive directors, as described in Information on directors, company secretaries and senior management and in the remuneration report in the Company's Annual Report.

The Nanosonics Performance and Development Program requires individual appraisals by a director at least annually for all senior executives, including executive directors but excluding the CEO and President, who is assessed by the Non-Executive Directors. In accordance with that program, individual appraisals of the performance of all senior executives were undertaken by the CEO and President during the year.

Committees of the Board

The Board is assisted by committees, which are responsible for aspects of the operation of the Group and which act by examining relevant matters and making recommendations to the Board. The Board may establish additional committees to assist it in carrying out its responsibilities. The Board may also delegate specified responsibilities to ad-hoc committees. The directors must be satisfied that the members of a committee are competent and will exercise their delegated functions in accordance with directors' duties.

Currently there are four committees of the Board: the Nomination Committee, the Audit and Risk Committee, the Remuneration Committee and the R&D and Innovation Committee. Details of directors' attendances at meetings of the committees are shown in the Directors' report contained in the Company's Annual Report.

Principle 2 – Structure the board to add value

The Board currently consists of three Non-Executive Directors and two executive directors.

Corporate governance statement (continued)

The role of the Chairman is separate from that of the Chief Executive Officer.

- Mr Maurie Stang is non-executive Chairman: appointed director 14 November 2000.
- Dr David Fisher is an independent non-executive director: appointed director 30 July 2001.
- Mr Richard England is an independent non-executive director: appointed director 5 February 2010.
- Mr Michael Kavanagh is an executive director and CEO and President: appointed non-executive director 30 July 2012 and became an executive director on 21 October 2013.
- Dr Ron Weinberger is an executive director and the President Technology Development / Commercialisation: appointed as an executive director 2 July 2008.

Details of each director, including their qualifications and experience, are set out in the Information on the directors, company secretaries and senior management on pages 18 to 20 of the Annual Report and on the Nanosonics website, www.nanosonics.com.au.

Directors' independence

Directors' independence is assessed according to the provisions set out in the Company's Board Charter and in the ASX Corporate Governance Principles and Recommendations with 2010 Amendments (2nd Edition). Accordingly:

- Mr Stang is not considered to be an independent director as: he is a founder of the Company; he held executive office in the Company until March 2007; he is a major shareholder of the Company; and he is a director and/or shareholder of companies with which the Company had significant transactions during the year (refer to the Directors report included in the Annual Report).
- Mr Kavanagh is not considered to be an independent director as he is an executive of the Company.
- Dr Weinberger is not considered to be an independent director as he is an executive of the Company.
- Dr Fisher is considered to be an independent director, except that he served as interim executive director for the period 14 December 2007 to 16 June 2008. For the period 9 May 2011 to 29 March 2013 Dr Fisher served as Managing Director of Aeris Environmental Ltd where Mr Stang is the non-executive Chairman.
- Mr England is considered to be an independent director.

The Board is considering opportunities to appoint additional suitably qualified and experienced independent directors. At the time when the Company has appointed other independent directors, the Board will also consider its opportunities to appoint an independent chairman.

Nomination Committee

The members of the Nomination Committee are: Mr Richard England (Chairman), Dr David Fisher, and Mr Maurie Stang. The Committee comprises a majority of independent directors and is chaired by an independent director.

The Nomination Committee is appointed by the Board to assist the Board to discharge its responsibilities in relation to:

- The composition, structure and operation of the Board and ensuring the Board is comprised of individuals who are best able to discharge their responsibilities as Directors; and
- Ensuring the Company meets the requirements of the ASX Diversity Guidelines.

A copy of the Nomination Committee Charter is available on the Company's website.

Selection and appointment of directors

The Nomination Committee is responsible for the identification and selection of suitable candidates for appointment as a director. The Committee assesses potential directors to ensure the Board includes an appropriate mix of skills to allow the Board to maximise its effectiveness and contribution to the Company. Selection criteria include relevant experience and qualifications, availability, communication capabilities, community standing and integrity. After assessment, candidates are recommended to the Board by the Committee.

Induction, education and access of directors

Every new director receives an appointment letter accompanied by:

- Director's Deed of Access;
- Director's Handbook (containing Company policies and charters); and
- Induction training.

Directors and the Board have the right, in connection with their duties and responsibilities, to obtain independent professional advice at the Company's expense. Subject to prior approval from within the Board, which will not reasonably be withheld, a director may have direct access to any employee or contractor of the Group and seek any information from any employee in order to perform his or her responsibilities.

Board performance evaluation

The Board requires that each director has the appropriate competencies to fulfil their role and that they perform effectively in their respective role and on the Board. The Nomination Committee is responsible for recommending a framework for the assessment and evaluation of the performance of each director individually, of each committee and of the Board as a whole. The performance of the Board and each of the Board committees is reviewed annually with the most recent being completed in October 2013.

Principle 3 – Promote ethical and responsible decision-making

Code of Conduct

All directors, officers, employees, advisors, consultants and contractors of the Group are expected to act with integrity and objectivity and to maintain the highest possible ethical standards which have been formalised and set out in the Company's Code of Conduct and Ethics which is available on the Company's website.

Securities trading policy

The Company has a Securities Trading Policy, which applies to all Designated Persons, comprising its directors, officers, employees, advisors, consultants and contractors and such other persons as the Board nominates. Designated Persons may only deal in the Company's securities in accordance with the policy and the Company regularly reviews share trading reports and its share register to ensure compliance with the policy. A copy of the Securities Trading Policy is available on the Company's website.

Whistleblower policy

The Company recognises its responsibilities to conduct its business in accordance with both Australian and internationally accepted practices and procedures. As part of this, the Company is committed to maintaining a culture where all directors, staff, contractors and consultants to the Company are encouraged to raise concerns about poor and/or unacceptable practices and misconduct.

The Company has a Whistleblower Policy to provide a process through which staff, contractors and consultants to the Company can express serious concerns and report misconduct. The Whistleblower policy is available on the Company's website.

Diversity

Nanosonics believes that the pursuit of diversity in the workplace increases its ability to attract, retain and develop the best talent available, creates an engaged workforce, delivers the highest quality services to its customers, enhances individual work-life balance, encourages personal achievement, improves co-operation and assists in the optimisation of organisational performance. Diversity in the workplace mirrors the diversity of the broader community, encompassing age, gender, ethnicity, cultural and other personal factors. The Company respects the diversity of all employees, consultants and contractors, and cultivates an environment of fairness, respect and equal opportunity. A copy of Nanosonics' Diversity policy is available on the Company's website.

Set out below are the diversity objectives established by the Board.

- Hiring: The Board will ensure that appropriate selection criteria, based on diverse skills, experience and perspectives, are used when recruiting new staff and directors.
- Job specifications, advertisements, application forms and contracts will not contain any direct or inferred discrimination.
- Training: All internal and external training opportunities will be based on merit, and Company and individual needs. The Board will consider senior management training and executive mentoring programmes to develop skills and experience to prepare employees for senior management and Board positions.
- Career Advancement: All decisions associated with career advancement, including promotions, transfers, and other assignments, will meet the Company's needs, and be determined on skill and merit.

Corporate governance statement (continued)

- Work Environment: The Company will ensure that all officers, employees, consultants and contractors have access to a work environment that is free from harassment and unwanted conduct in relation to personal circumstances or characteristics. Directors, managers and supervisors will ensure that complainants or reports of sexual, racial or other harassment are treated seriously, confidentially and sympathetically by the Company.

The Board assesses annually the above diversity objectives and Company's progress in achieving these objectives.

As at 30 June 2014, women represented 36% (2013: 33%) of the Group's workforce, 31% in key executive positions (2013: 36%) and 0% at Board level (2013: 0%)

Principle 4 – Safeguard integrity in financial reporting

Audit and Risk Committee

The members of the Audit and Risk Committee are: Mr Richard England (Chairman), Dr David Fisher and Mr Maurie Stang. The Committee comprises only Non-Executive Directors and has a majority of independent directors. The Committee Chairman is an independent director who is appropriately qualified and financially literate and who is not Chairman of the Board.

The purpose of the Audit and Risk Committee is to assist the Board to discharge its responsibilities in relation to the oversight and monitoring of:

- Corporate reporting processes, including the financial reporting process;
- External audit;
- Risk management and internal control;
- Compliance with laws, regulations, internal policies and industry standards; and
- Activities to prevent, deter, detect and report on fraud.

A copy of the Audit and Risk Committee Charter is available on the Company's website.

External auditors

The Audit and Risk Committee is responsible for selecting and recommending the appointment of the external auditor. The Committee considers a number of criteria in appointing the external auditor, such as audit approach, governance processes, key personnel and cost. The Committee then provides the Board with its recommendation. In line with current professional standards the external auditor is required to rotate after 5 years and cannot return as auditor for a further 2 years.

It is the external auditor's role to provide an independent opinion that the Company's financial reports are true and fair and comply with the Australian Accounting Standards and the *Corporations Act 2001*.

Principle 5 – Make timely and balanced disclosure

The Company has a Continuous Disclosure and Shareholder Communications Policy to ensure compliance with the disclosure requirements of the ASX Listing Rules and to ensure individual accountability at senior executive level for that compliance. In determining whether information should be disclosed, the Board takes into consideration the needs and interests of the Group's shareholders and other stakeholders in the context of the Board's obligations under the *Corporations Act 2001* and the ASX Listing Rules. ASX announcements are prepared directly when the Board or executive management becomes aware of information required to be disclosed to the market.

A copy of the Continuous Disclosure and Shareholder Communications Policy is available on the Company's website

Principle 6 – Respect the rights of shareholders

The Company recognises and respects the rights of shareholders and seeks to facilitate the effective exercise of those rights within the limitations of the continuous disclosure provisions of the ASX Listing Rules. Nanosonics' policy for communication with shareholders and encouraging their participation at general meetings is contained in the Company's Continuous Disclosure and Shareholder Communications Policy.

The Company encourages shareholder participation, particularly attendance of the general meetings of the Company. The external auditor attends the annual general meeting and is available to answer shareholder questions about the conduct of the audit of the Company and the preparation and content of the auditor's report on the financial statements of the Company.

The Company ensures relevant corporate information is complete and available in a timely manner on its website: www.nanosonics.com.au. Measures include:

- Placing all announcements to the market on the Company website after they have been released to the ASX.
- Posting webcasts or recordings of teleconferences to the website.
- Including at least the last three years' financial data on the website.
- Providing updates and reports to shareholders by email.

Shareholders and prospective shareholders are welcome, by prior appointment, to speak with executive managers responsible for investor relations and to view the Company's operations.

Principle 7 – Recognise and manage risk

The Company has established and documented an enterprise risk management program for the oversight and management of the Company's material business risks. The Audit and Risk Committee is responsible for overseeing and monitoring risk and compliance management. A summary of the Audit and Risk Committee's responsibilities in relation to risk and compliance are included in the Audit and Risk Committee Charter.

Nanosonics' enterprise risk management system is based on the International Risk Standard AS/NZS ISO 31000:2009 and is complemented by an internal control program based upon the principles set out in the Australian Compliance Standard AS 3806:2006.

Nanosonics has developed a common risk language through which it considers internal risks such as those arising from financial and human resource management and external risks such as those arising from dealings with key stakeholders and macro environmental issues such as regulatory changes or economic events beyond the Company's control. In assessing material business risks, each identified risk is individually assessed in terms of the likelihood of the risk event occurring and the potential consequences in the event that the risk event was to occur.

During the year the Company implemented an electronic risk and compliance system, which facilitates linking of material business risks to mitigating controls so that the performance of the Company's enterprise risk and compliance programs can be monitored continuously. Management reports to the Board on the effectiveness of the Company's management of its material business risks with the most recent report being provided in July 2014.

The CEO and President and Chief Financial Officer have jointly confirmed to the Board that the declaration provided in the Annual Report in accordance with section 295A of the *Corporations Act 2001* is founded upon sound systems of internal control and that the systems are operating effectively in all material respects in relation to financial reporting risks.

Principle 8 – Remunerate fairly and responsibly

The Company's remuneration philosophy and policies are set out in the Remuneration Report in the Annual Report. The Remuneration Committee oversees remuneration policies and strategies to ensure that performance is rewarded in a manner that is competitive and appropriate for the results delivered.

Remuneration Committee

The members of the Remuneration Committee are: Mr Richard England (Chairman), Dr David Fisher and Mr Maurie Stang. The Committee is chaired by an independent director and has a majority of independent directors.

The purpose of the Remuneration Committee is to assist the Board to discharge its responsibilities by:

- Recommending appropriate remuneration policies to the Board and monitoring their implementation;
- Establishing systems designed to enhance the performance of individual employees and Directors of the Company and of the Company as a whole;
- Fairly and responsibly rewarding executives and other employees having regard to the performance of the Company, the performance of the executive or employee and the general pay environment; and
- Recommending to the Board a system of performance appraisal for Directors and the Board of the Company as a whole.

A comprehensive summary of the Company's remuneration strategy together with details of securities trading restrictions are set out in the Remuneration Report in the Annual Report.

Contents of the financial statements

For the year ended 30 June 2014

Auditor's independence declaration

UHY Haines Norton
Chartered Accountants

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Auditor's Independence Declaration under section 307C of the *Corporations Act 2001*

To the Directors of Nanosonics Limited

I declare that, to the best of my knowledge and belief, during the year ended 30 June 2014, 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.

UHY Haines Norton

Mark Nicholaeff
Partner

UHY Haines Norton
Chartered Accountants

Sydney

Date: 21 August 2014

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Passion beyond numbers

Consolidated statement of profit or loss and other comprehensive income

For the year ended 30 June 2014

	Notes	2014 $'000	2013 $'000
Continuing operations			
Sale of goods and services	5	21,492	14,899
Cost of sales		(7,571)	(6,428)
Gross profit		13,921	8,471
Other income	6	4,114	2,690
Operating expenses			
Staffing costs	7	12,005	9,177
Intellectual property		594	459
Quality & regulatory management		298	247
Business development		1,094	988
Premises, plant & equipment		1,635	1,567
External consultants & advisors		1,534	1,861
Other operating costs		2,956	2,080
Total operating expenses		20,116	16,379
Other expense			
Borrowing costs	20	555	517
Operating loss before income tax		(2,636)	(5,735)
Income tax benefit (expense)	8	31	(33)
Net loss after income tax expense attributable to owners of the parent entity		(2,605)	(5,768)
Other comprehensive income			
Items that may be reclassified subsequently to profit or loss			
Exchange difference on foreign currency translation		(7)	38
Income tax on items of other comprehensive income		–	–
Total items that may be reclassified subsequently to profit or loss		(7)	38
Total other comprehensive income		(7)	38
Total comprehensive income for the period attributable to owners of the parent entity		(2,612)	(5,730)
(Loss) per share for losses attributable to ordinary shareholders of the company		Cents	Cents
Basic (loss) per share	29	(1.0)	(2.2)
Diluted (loss) per share	29	(1.0)	(2.2)

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

Consolidated statement of financial position

As at 30 June 2014

	Notes	2014 $'000	2013 $'000
Current assets			
Cash and cash equivalents	9	21,233	24,064
Trade and other receivables	10	5,712	4,199
Inventories	11	4,237	2,909
Other current assets	12	440	488
Total current assets		31,622	31,660
Non-current assets			
Property, plant and equipment	13	1,778	1,812
Intangible assets	14	–	37
Other non-current assets	15	144	144
Total non-current assets		1,922	1,993
Total assets		33,544	33,653
Current liabilities			
Trade and other payables	16	3,000	3,002
Derivative financial instruments	3	–	198
Deferred revenue	17	308	209
Employees provisions	18	1,521	783
Borrowings	19	6	6
Total current liabilities		4,835	4,198
Non-current liabilities			
Employees provisions	18	159	183
Borrowings	19	18	24
Convertible notes	20	8,097	7,541
Total non-current liabilities		8,274	7,748
Total liabilities		13,109	11,946
Net assets		20,435	21,707
Equity			
Contributed equity	21	74,410	74,068
Option premium on convertible notes	20	376	376
Reserves	22	3,691	2,700
Accumulated loss		(58,042)	(55,437)
Total equity		20,435	21,707

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 2014

	Contributed equity	Option premium on convertible note	Employee equity benefits reserve	Foreign currency translation reserve	Accumulated losses	Total equity
	Note 21 $'000	Note 20 $'000	Note 22 $'000	Note 22 $'000	$'000	$'000
At 30 June 2012	73,532	376	1,775	(11)	(49,669)	26,003
Loss for the period	–	–	–	–	(5,768)	(5,768)
Other comprehensive income	–	–	–	38	–	38
Total comprehensive income (loss)	–	–	–	38	(5,768)	(5,730)
Transactions with owners in their capacity as owners						
Shares issued	381	–	–	–	–	381
Transaction costs	(48)	–	–	–	–	(48)
Share-based payment	203	–	898	–	–	1,101
At 30 June 2013	**74,068**	**376**	**2,673**	**27**	**(55,437)**	**21,707**
Loss for the period	**–**	**–**	**–**	**–**	**(2,605)**	**(2,605)**
Other comprehensive income	**–**	**–**	**–**	**(7)**	**–**	**(7)**
Total comprehensive income (loss)	**–**	**–**	**–**	**(7)**	**(2,605)**	**(2,612)**
Transactions with owners in their capacity as owners						
Shares issued	**–**	**–**	**–**	**–**	**–**	**–**
Share-based payment	**342**	**–**	**998**	**–**	**–**	**1,340**
At 30 June 2014	**74,410**	**376**	**3,671**	**20**	**(58,042)**	**20,435**

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 2014

	Notes	2014 $'000	2013 $'000
Cash flows from operating activities			
Receipts from customers (inclusive of GST)		**23,027**	14,025
Receipts from government grants (inclusive of refundable R&D tax offset)	**6**	**1,666**	1,498
Payments to suppliers and employees (inclusive of GST)		**(28,020)**	(21,086)
Interest received		**727**	1,096
Income taxes paid		**6**	(39)
Net cash used in operating activities	**28**	**(2,594)**	(4,506)
Cash flows from investing activities			
Purchase of property, plant and equipment		**(479)**	(1,359)
Net cash used in investing activities		**(479)**	(1,359)
Cash flow from financing activities			
Net proceeds from issue of shares and exercise of options		**342**	536
Repayment of borrowings		**(6)**	(6)
Net cash provided by financing activities		**336**	530
Net increase (decrease) in cash and cash equivalents		**(2,737)**	(5,335)
Cash and cash equivalents at the beginning of the financial year		**24,064**	29,310
Effects of exchange rate changes on cash and cash equivalents		**(94)**	89
Cash and cash equivalents at the end of year	**9**	**21,233**	24,064

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

Notes to the financial statements

For the year ended 30 June 2014

1. Corporate information

The financial report on pages 60 to 102 covers Nanosonics Limited as a consolidated entity consisting of Nanosonics Limited (the Company) and its subsidiaries (the Group).

Nanosonics Limited is a publicly listed company, limited by shares, incorporated and domiciled in Australia and listed on the Australian Securities Exchange (ASX code NAN). The Company's registered office and principal place of business is:

Unit 24, 566 Gardeners Road
Alexandria, NSW 2015
Australia

A description of the nature of the Group's operations and its principal activities is included in the review of operations on pages 8 to 13 and in the Directors' report on page 22, both of which are not part of this financial report.

The financial report was authorised for issue in accordance with the resolution of the directors on 21 August 2014.

2. Summary of significant accounting policies

a. Basis of preparation

The financial report is a general purpose financial report, which has been prepared in accordance with the requirements of the *Corporations Act 2001*, Australian Accounting Standards, and other authoritative pronouncements of the Australian Accounting Standards Board. The financial report has also been prepared on a historical cost basis and do not take into account changes in money values, except for derivative financial instruments, which have been measured at fair value.

The Company is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, all financial information presented in Australian dollars has been rounded to the nearest one thousand dollars ($'000) unless otherwise stated.

b. Compliance with IFRS

The financial report of Nanosonics Limited also complies with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

c. New accounting standards and interpretations

1) Changes in accounting policy and disclosures

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended Australian Accounting Standards and AASB Interpretations as of 1 July 2013:

- AASB 10 *Consolidated Financial Statements,* AASB 127 *Separate Financial Statements*
- AASB 11 *Joint Arrangements,* AASB 128 *Investments on Associates and Joint Ventures*
- AASB 12 *Disclosure of Interests in Other Entities*
- AASB 13 *Fair Value Measurement*
- AASB 119 *Employee Benefits (revised 2011*)
- AASB 2012-2 *Amendments to AASB 7 Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities*
- AASB 2012-5 *Improvements to AASBs 2009-2011 Cycle*
- AASB 2012-9 *Withdrawal of interpretation 1039*
- AASB 2011-4 *Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements*
- AASB CF 2013-1 *Australian Conceptual Framework*

The effect of the adoption of the above standards or interpretations or other amendments applied for the first time are disclosed below:

- AASB 119 *Employee Benefits* – The revised standard introduced changes to accounting for defined benefit plans, termination benefits and definition of short term employee benefits. The distinction between short-term and other long-term employee benefits is now based on whether the benefits are expected to be settled wholly within 12 months after the reporting date. Consequential amendments were also made to other standards via AASB 2011-10. The adoption of this standard by the Group impacted the measurement of annual leave obligations. The effect of change in the annual leave expense and provision as previously reported in 2013 is not material.

- AASB 13 *Fair Value Measurement* – AASB 13 establishes a single source of guidance for all fair value measurements. AASB 13 does not change when an entity is required to use fair value, but rather, provides guidance on how to measure fair value under Australian Accounting Standards. AASB 13 defines fair value as an exit price. As a result of the guidance in AASB 13, the Group reassessed its policies for measuring fair values, in particular, its valuation inputs such as non-performance risk for fair value measurement of liabilities. AASB 13 also requires additional disclosures. Application of AASB13 has not materially impacted the fair value measurements of the Group. Additional disclosures where required, are provided in the individual notes relating to the assets and liabilities whose fair values were determined. Fair value hierarchy is provided in note 3.

- AASB 2011-4 *Amendments to Australian Accounting Standards* and revised *Corporations Regulations 2M.3.03* – Transfer of Individual KMP disclosures to the Remuneration Report. The amendments removed the individual Key Management Personnel (KMP) disclosures about equity holdings, loans and other transactions with KMP from the notes to the financial statements and were transferred to the Remuneration Report. Comparative information is not required for these items in the Remuneration Report. Accordingly, individual KMP disclosures are now included in the Remuneration report on page 26 to 50.

Adoption of the other standards affected the disclosures but did not have a material impact on the financial statements of the Group.

2) Accounting Standards and Interpretations issued but not yet effective

Australian Accounting Standards and Interpretations that have recently been issued or amended but are not yet effective and have not been adopted by the Group for the annual reporting period ended 30 June 2014, are outlined below:

Standards effective 1 Jan 2014, applicable to the Group by 1 July 2014

- AASB 2012-3 Amendments to Australian Accounting Standards – *Offsetting Financial Assets and Financial Liabilities.* AASB 2012-3 adds application guidance to AASB 132 to address inconsistencies identified in applying some of the offsetting criteria of AASB 132, including clarifying the meaning of “currently has a legally enforceable right of set-off” and that some gross settlement systems may be considered equivalent to net settlement. When AASB 2012-3 is first adopted for the year ending 30 June 2015, there will be no impact on the entity as this standard merely clarifies existing requirements in AASB 132.

- AASB 2013-3 Amendments to AASB 136 – *Recoverable Amount Disclosure for Non-Financial Assets.* The amendments include the requirement to disclose additional information about the fair value measurement when the recoverable amount of impaired assets is based on fair value less cost of disposal. When these amendments are adopted for the first time, they are unlikely to have any significant impact to the Group given that they are largely of the nature of clarification of existing requirements.

- Annual improvements 2010-2012 Cycle – *Annual Improvements to IFRSs 2010-2012 Cycle*. Annual Improvements to IFRSs 2010-2012 Cycle is a collection of amendments to IFRSs in response to eight issues addressed during the 2010-2012 cycle for annual improvements to IFRSs. The amendments have not yet been adopted by the AASB. Among the items addressed by this standard, the following are relevant to the Group:
  - IFRS 2 – Clarifies the definition of 'vesting conditions' and 'market condition' and introduces the definition of 'performance condition' and 'service condition'. The group is yet to assess the effect if any of this amendment on its accounting of share-based payments.
  - IFRS 8 – Requires entities to disclose factors used to identify the entity's reportable segments when operating segments have been aggregated. An entity is also required to provide reconciliation of total reportable segments' assets to the entity's total assets.
  - IAS 16 & IAS 38 – Clarifies the determination of accumulated depreciation does not depend on the selection of valuation technique and that it is calculated as the difference between the gross and net carrying amounts.
  - IAS 24 – Defines a management entity providing KMP services as a related party of the reporting entity. The amendments added an exemption from the detailed disclosure requirements in paragraph 17 of IAS 24 for KMP services provided by a management entity. Payments made to a management entity in respect of KMP services should be separately disclosed.
- Annual Improvements 2011-2013 Cycle – *Annual Improvements to IFRSs 2011-2013 Cycle*. Annual Improvements to IFRSs 2011-2013 Cycle is a collection of amendments to IFRSs in response to four issues addressed during the 2011-2013 cycle. Among other improvements, the amendments clarify that an entity should assess whether an acquired property is an investment property under IAS 40 Investment Property and perform a separate assessment under IFRS 3 Business Combinations to determine whether the acquisition of the investment property constitutes a business combination. The amendments have not yet been adopted by the AASB.
- AASB 1031 Materiality – The revised AASB 1031 is an interim standard that cross-references to other Standards and the Framework (issued December 2013) that contain guidance on materiality. AASB 1031 will be withdrawn when references to AASB 1031 in all Standards and Interpretations have been removed.

Unless otherwise stated above, the adoption of the above standards is not expected to have a significant effect on the way the Group accounts for and presents its financial results.

Standards to be applied by the Group beyond 1 July 2014

- Amendments to IAS 16 and IAS 38 – Clarification on the Acceptable Methods of Depreciation and Amortisation (Amendments to IAS 16 and IAS 38), effective I January 2016, applicable 1 July 2016. IAS 16 and IAS 38 both establish the principle for the basis of depreciation and amortisation as being the expected pattern of consumption of the future economic benefits of an asset. The IASB has clarified that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The IASB also clarified that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset. This presumption, however, can be rebutted in certain limited circumstances.
- IFRS 15 *Revenue from Contracts with Customers*, effective 1 January 2017, applicable 1 July 2017. IFRS 15 establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity recognises revenue in accordance with that core principle by applying the following steps:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation.

- AASB 9 *Financial Instruments*, effective 1 January 2018, applicable 1 July 2018. AASB 9 includes requirements for the classification and measurement of financial assets. It was further amended by AASB 2010-7 and AASB 2012-6 to reflect amendments to the accounting for financial liabilities. These requirements improve and simplify the approach for classification and measurement of financial assets compared with the requirements of AASB 139.

The Group has not yet assessed the full impact of the above standards that will be applied by the Group beyond 1 July 2014.

d. Basis of consolidation

The consolidated financial statements comprise the financial statements of Nanosonics Limited ('Company' or 'parent entity') and its subsidiaries as at 30 June each year. Nanosonics Limited and its subsidiaries together are referred to in this financial report as the Group or the consolidated entity.

Business combinations

The Group accounts for business combinations using the acquisition method when control is transferred to the Group. The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain or a bargain purchase is recognised in profit or loss immediately. Transaction costs are expensed as incurred, except if related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it 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 over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Information on subsidiaries is contained in note 26 to the financial statements.

The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognised in profit or loss. Any interest retained in the former subsidiary is measured at fair value when control is lost.

Transactions eliminated on consolidation

In preparing the consolidated financial statements, all inter-company balances and transactions between entities in the Group, including any unrealised profits or losses, have been eliminated in full.

e. Operating segments

Operating segments are reported in a manner consistent with the internal reporting provided to the Managing Director and CEO, who is the Group's chief operating decision maker. The chief operating decision maker is responsible for allocating resources and assessing performance of the operating segments.

f. Foreign currency

(i) Functional and presentation currency

Items included in the 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 consolidated financial statements are presented in Australian dollars, which is Nanosonics Limited's functional and presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of profit or loss, except when they are deferred in equity as qualifying cash flow hedges and qualifying net investment hedges or are attributable to part of the net investment in a foreign operation.

Translation differences on assets and liabilities carried at fair value are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets and liabilities are recognised in profit or loss as part of the fair value gain or loss.

(iii) Group companies

The functional currency of the overseas subsidiaries is as follows:

- Nanosonics Europe GMBH is Euro; and
- Nanosonics Inc. is US dollars.

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that statement of financial position
- income and expenses for each income statement are translated at average exchange rates (unless this is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions), and
- all resulting exchange differences are recognised in other comprehensive income – foreign currency translation reserve.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities, and of borrowings and other financial instruments designated as hedges of such investments, are recognised in other comprehensive income. When a foreign operation is sold or any borrowings forming part of the net investment are repaid, a proportionate share of such exchange differences is reclassified to profit or loss, as part of the gain or loss on sale where applicable.

g. Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable, taking into account defined terms of payment and excluding taxes or duty. Amounts disclosed as revenue are net of returns, trade allowances, rebates and amounts collected on behalf of third parties. The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement.

Revenue is recognised for the major business activities as follows:

(i) Sale of goods

Revenue is recognised when the significant risks and rewards of ownership have been transferred to the distributor or end customer. Sales are recorded based on the prices specified in the sales contracts net of any discounts and returns at the time of sale. No element of financing is deemed to be present as the sales are made with credit terms which are consistent with practices in each market.

(ii) Sale of services

Revenue from trophon® EPR maintenance and repairs are recognised as services are rendered. Revenue from service contracts are recognised as services are rendered over the service period, typically over one year. Unearned service revenue is deferred and recognised as liability in the Statement of financial position.

(iii) Interest income

Interest income is recognised on a time proportion basis using the effective interest method.

h. Government grants

Grants from government are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with the attached conditions.

i. Income tax and other taxes

The income tax expense or revenue for the period is the tax payable on the current period's taxable income based on the national 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 and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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. However, deferred income tax is 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 balance date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income 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 and on the assumption that no adverse change will occur in income tax legislation enabling the benefit to be realised and comply with the conditions of deductibility imposed by the law.

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 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.

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.

Tax consolidation

Nanosonics Limited and its wholly-owned Australian controlled entity, Saban Ventures Pty Limited, are part of a tax consolidated group.

The head entity, Nanosonics Limited, and the controlled entity in the tax consolidated group account for their own current and deferred tax amounts. 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, Nanosonics 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.

Goods and services tax (GST), Value added tax (VAT)

Revenues, expenses and assets are recognised net of the amount of associated GST or VAT as applicable, unless the GST/VAT incurred is not recoverable from the taxation authority, in which case, the GST/VAT 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/VAT receivable or payable. The net amount of GST/VAT recoverable from, or payable to, the taxation authority is included with other current receivables or payables in the statement of financial position.

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

j. Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement at inception date, whether fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset, even if that right is not explicitly specified in an arrangement.

Group as a lessee

Finance leases that transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are recognised in finance costs in the profit or loss.

A leased asset is depreciated over the useful life of the asset. However, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the estimated useful life of the asset and the lease term.

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

Group as a lessor

Leases in which the Group does not transfer all the risks and benefits of ownership of an asset are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognized over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

k. Borrowing costs

Borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

l. Cash and cash equivalents

For cash flow statement presentation purposes, cash and cash equivalents includes cash on hand, deposits held at call with financial institutions, other short-term, highly liquid investments presented at market value that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities in the statement of financial position.

m. Inventories

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

Costs of purchased inventory are determined to be actual costs on a batch basis, after including import duties, taxes (other than those subsequently recoverable by the entity), transport, handling and other costs directly attributable to the acquisition of the inventory, and after deducting rebates and discounts.

Costs of work in progress and finished goods comprise purchased materials at cost, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

n. Financial assets

Classification

Financial assets are classified at initial recognition as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

The Group's financial assets include cash and short-term deposits, trade and other receivables, and derivative financial instruments.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. All of the Group's cash term investments are captured in this category. Cash term investments, which are highly liquid irrespective of their maturity dates, are classified as current assets, as they may not necessarily be held for their full term.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade receivables generally have 30 to 60 days credit terms. Loans and receivables are included in current assets, except for those with maturities greater than 12 months after the reporting period which are classified as non-current assets. Receivables are disclosed in trade and other receivables (note 10) in the statement of financial position.

Derivative financial instruments are classified as held for trading unless they are designated as effective hedging instruments.

Recognition and derecognition

All financial assets are recognised initially at fair value plus, in the case of financial assets not recorded at fair value through profit or loss, transaction costs that are attributable to the acquisition of the financial assets.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the trade dates. i.e. the date that the Group commits to purchase or sell the asset.

Financial assets carried at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in profit or loss.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

Subsequent measurement

Receivables and held-to-maturity investments are carried at amortised cost using the effective interest method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The losses arising from impairment are recognised in the statement of profit or loss.

Receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

Investments in controlled entities are carried in the Company's financial statements at the lower of cost and recoverable amount.

Impairment of financial assets

For financial assets carried at amortised cost, at each reporting date, the Group assesses whether there is objective evidence that a financial asset is impaired. For trade receivables, collectability is reviewed on an on-going basis. An impairment exists if one or more events that has occurred since the initial recognition of the assets (an incurred "loss event") has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or group of debtors is experiencing significant financial difficulty, default or delinquency in payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

If any such evidence exists, the amount of any impairment loss is measured as the difference between the assets carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The present value of the estimated future cash flows is discounted at the financial assets original effective interest rate.

The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognised in the statement of profit or loss. Receivables together with the associated allowance are written off when there is no realistic prospect of future recovery. If in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment were recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to other expense in the statement of profit or loss.

o. Derivative financial instruments and hedge accounting

The Group uses derivative financial instruments, i.e. forward currency contracts, to hedge its foreign currency risks. Such derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

The fair values of forward currency contracts are calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

Any gains or losses arising from changes in the fair value of derivatives are taken directly to the income statement, except for the effective portion of cash flow hedges, which is recognised in other comprehensive income.

For the purposes of hedge accounting, hedges are classified as:

- fair value hedges, when they hedge the exposure to changes in the fair value of a recognised asset or liability; or
- cash flow hedges, when they hedge the exposure to variability in cash flows that is attributable either to a particular risk associated with a recognised asset or liability or to a forecast transaction.

Hedges that meet the strict criteria for hedge accounting are accounted as follows:

- For cash flow hedges, the effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised in profit or loss.
- For fair value hedges, the carrying amount of the hedged item is adjusted for gains and losses attributable to the risk being hedged and the derivative is remeasured to fair value. Gains and losses from both are taken to profit or loss.

p. Convertible notes

Convertible notes are compound financial instruments which are separated into liability and equity components based on the terms of the contract.

On issuance of the convertible note, the fair value of the liability component is determined using a market rate for an equivalent non-convertible note. The equity component is initially recognised at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component of the convertible notes is measured at amortised cost using the effective interest method. The equity component is not remeasured.

Interest related to the financial liability is recognised in profit or loss. On conversion, the financial liability is reclassified to equity and no gain or loss is recognised.

q. Property, plant and equipment

All property, plant and equipment is stated at historical cost less depreciation and/or accumulated impairment losses, if any. Historical cost includes expenditure that is directly attributable to the acquisition of the items. 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 assets is derecognised when it is replaced. All other repairs and maintenance are charged to the income statement during the reporting period in which they are incurred. Production tooling used to manufacture component parts qualifies as property, plant and equipment when the Company expects to use it during more than one period.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

All assets have limited useful lives and are depreciated using the straight line method over their estimated useful lives, or in the case of leasehold improvements, over the estimated useful life or lease term, whichever is shorter, taking into account residual values. The assets' residual values, useful lives and depreciation methods are reviewed prospectively and adjusted if appropriate at least annually. Depreciation is expensed. The depreciation rates or useful lives used for each class of assets are as follows:

Depreciation of property, plant and equipment	**2014**	**2013**
Laboratory fit-out	6 years	6 years
Laboratory and manufacturing equipment	5 years	5 years
Office furniture and equipment	7 years	7 years
Computer equipment and software	3 years	3 years
Leasehold improvements	Lease	Lease
Service, test and demonstration equipment	2-3 years	2-3 years

r. Intangible assets

(i) Research and development

Research and development expenditure is expensed as incurred except that 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 directly attributable costs, including costs of materials and services. 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 expenditure which has a finite life is recorded as an intangible asset from the point at which the asset is ready for use and amortised on a straight-line basis over the period during which the related benefits are expected to be realised.

(ii) Patents and Trademarks

The costs of registering and protecting patents and trademarks are expensed as incurred.

s. Impairment of non-financial assets

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. Intangible assets are tested annually for impairment or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the assets carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

Impairment losses of continuing operations, including impairment on inventories, are recognised in the income statement in expense categories consistent with the function of the impaired asset.

t. Trade and other payables

Trade and other payables are carried at amortised cost. These amounts represent liabilities for goods and services provided to the Group prior to the end of financial year which are unpaid and arise when the Group becomes obliged to make future payment in respect of the purchase of these goods and services. The amounts are unsecured and are usually paid within 60 days of recognition.

u. Provisions

Provisions for legal claims, service warranties and other 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 reasonably estimated. Provisions are not recognised for future operating losses.

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

Provision for warranties

Provision is made in respect of the Group's estimated liability on all products under warranty at balance date. The provision is measured at current values estimated to be required to settle the warranty obligation. The initial estimate of warranty-related costs is revised annually. The provision is included in Current liabilities – trade and other payables in the statement of financial position.

v. Employee benefits

Wages, salaries and annual leave and sick leave

Liabilities for employee benefits, including wages, salaries and non-monetary benefits, and accumulating annual and other leave, represent present obligations resulting from employees' services provided to reporting date. Employee benefits have been measured at the amounts expected to be paid when the liability is settled and are recognised in the provision for employee benefits. Sick leaves are recognised when the leave is taken and are measured at the rates paid or payable.

Long service leave

The liability for long-service leave 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 reporting date. 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 reporting date on national government bonds with terms to maturity that match as closely as possible, the estimated future cash outflows.

Bonuses
The Group recognises a liability and an expense for bonuses. The Group recognises a provision where contractually obliged and where there is a past practice that has created a constructive obligation.

Termination benefits
Termination benefits are payable when employment is terminated before the normal retirement or end of employment contract date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a formal plan without possibility of withdrawal or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

Share-based compensation
Share-based compensation benefits are equity-settled transactions provided to employees via the Nanosonics share-based compensation plans. Information relating to the plans is set out in note 30 to the financial statements.

Share option plans
The assessed fair value on the date options are granted is independently determined using the appropriate valuation model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

General Share Option Plan (GSOP)

The assessed fair values of options granted under the GSOP are expensed in full in the month in which they are granted with a corresponding increase in a share based payments reserve as part of shareholders' equity, except where the options are granted as part of a capital raising programme, in which case no cost is recognised.

Employee Share Option Plan (ESOP)

The fair value of options and performance rights granted under the ESOP is recognised as an employee benefit expense with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognised for share-based payments at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The statement of profit or loss expense or credit for a period represents the movement in cumulative expense recognised as at the beginning and end of the period.

No expense is recognised for awards that do not ultimately vest, except for equity-settled transactions for which vesting are conditional upon a market or non-vesting condition. These are treated as vesting irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

When the terms of an equity-settled award are modified, the minimum expense recognised is the expense had the terms had not been modified. If the original terms of the award are met. An additional expense is recognised for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee as measured at the date of modification.

Deferred Employee Share Plan (DESP)
The issue price of DESP shares granted during the year is calculated as the 5-day weighted average market price of shares of the Company on the Australian Securities Exchange as at close of trading on the date the shares are granted. The fair value of DESP shares granted is taken to be the issue price.

The assessed fair values of DESP shares are expensed in full in the month in which they are granted with a corresponding increase in equity, except if they are granted with a vesting condition, in which case the fair value of DESP shares granted is apportioned on a straight line monthly basis over the period between grant date and the date on which the shares all vest.

At the end of a period the Company assesses the probability of achievement of a benefit, being the percentage probability that employees will achieve at least the fair value of the unvested shares. The value of DESP shares with vesting conditions expensed in any period is calculated as that portion of the fair value applicable to the period factored by the probability of achievement and a share based payments reserve is created as part of shareholders' equity.

w. 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.

x. Earnings per share
(i) Basic earnings per share
Basic earnings per share ("EPS") is calculated by dividing the net profit or loss attributable to equity holders of the Company for the reporting period, by the weighted average number of ordinary shares of the Company outstanding during the financial year.

(ii) Diluted earnings per share

Diluted EPS adjusts the figures used in the determination of basic EPS 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 outstanding assuming the conversion of all dilutive potential ordinary shares.

y. Current versus non-current classification

The Group presents assets and liabilities in statement of financial position based on current/non-current classification. An asset is current when it is:

- Expected to be realised or intended to be sold or consumed in normal operating cycle
- Held primarily for the purpose of trading
- Expected to be realised within twelve months after the reporting period, or
- Cash or cash equivalents unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current. A liability is current when it is:

- Expected to be settled in normal operating cycle
- Held primarily for the purpose of trading
- Due to be settled within twelve months after the reporting period, or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period

The Group classifies all other liabilities as non-current.

Deferred tax asset and liabilities, if recognised, are classified as non-current assets and liabilities.

3. Financial risk management

The Group is exposed to financial risks, predominantly interest rate risk, foreign currency risk and credit risk and it has a financial risk management program which seeks to minimise potential adverse effects on financial performance. The Board provides written principles for investment of the Group's cash reserves, so as to ensure operational liquidity whilst optimising interest earnings from a mix of instruments with one or more of Australia's four main banks.

The Group held the following financial instruments and their classification:

Financial assets	Notes	2014 $'000	2013 $'000
Loans and receivables			
Trade and other receivables	**10**	**5,712**	4,199
Other financial assets			
Cash and cash equivalents	**9**	**21,233**	24,064
Total Financial assets		**26,945**	28,263
Financial liabilities			
Fair value through profit or loss			
Derivative financial instruments		**–**	198
Other financial liabilities			
Trade and other payables	**16**	**2,104**	2,553
Convertible notes	**20**	**8,097**	7,541
Borrowings	**19**	**24**	30
Total Financial liabilities		**10,225**	10,322

Notes to the financial statements (continued)

For the year ended 30 June 2014

a. Interest rate risk exposures

Interest rate risk is the risk that the fair value of the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group's exposure to interest rate risk is noted below:

2014	Notes	Floating interest rate $'000	Fixed interest rate maturing in: 1 year or less $'000	Over 1 to 5 years $'000	More than 5 years $'000	Non-interest bearing $'000	Total $'000
Financial assets							
Cash and cash equivalents	**9**	**6,013**	**15,220**	**–**	**–**	**–**	**21,233**
Trade and other receivables	**10**	**–**	**–**	**–**	**–**	**5,712**	**5,712**
Total financial assets		**6,013**	**15,220**	**–**	**–**	**5,712**	**26,945**
Weighted average interest rate		**0.21%**	**3.73%**	**–**	**–**	**–**	**–**
Financial liabilities							
Trade and other payables	**16**	**–**	**–**	**–**	**–**	**2,104**	**2,104**
Convertible notes	**20**	**–**	**–**	**8,097**	**–**	**–**	**8,097**
Borrowings	**19**	**–**	**6**	**18**	**–**	**–**	**24**
Total financial liabilities		**–**	**6**	**8,115**	**–**	**2,104**	**10,225**
Weighted average interest rate		**–**	**8.06%**	**0.00%**	**–**	**–**	**–**
Net financial assets (liabilities)		**6,013**	**15,214**	**(8,115)**	**–**	**3,608**	**16,720**

2013	Notes	Floating interest rate $'000	Fixed interest rate maturing in: 1 year or less $'000	Over 1 to 5 years $'000	More than 5 years $'000	Non-interest bearing $'000	Total $'000
Financial assets							
Cash and cash equivalents	9	5,477	18,587	–	–	–	24,064
Trade and other receivables	10	–	–	–	–	4,199	4,199
Derivative financial instruments		–	–	–	–	–	–
Total financial assets		5,477	18,587	–	–	4,199	28,263
Weighted average interest rate		3.34%	4.20%	–	–	–	–
Financial liabilities							–
Trade and other payables	16	–	–	–	–	2,553	2,553
Derivative financial instruments	3	–	–	–	–	198	198
Convertible notes	20	–	–	7,541	–	–	7,541
Borrowings	19	–	6	24	–	–	30
Total financial liabilities		–	6	7,565	–	2,751	10,322
Weighted average interest rate		–	8.06%	6.01%	–	–	–
Net financial assets (liabilities)		5,477	18,581	(7,565)	–	1,448	17,941

Interest rate sensitivity

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant:

	Increase /decrease in basis points	Effect on profit before tax and other comprehensive income $'000
2014	**+ 25**	**57**
	– 25	**(57)**
2013	+ 75	200
	– 100	(266)

b. Foreign currency risk exposures

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Group's exposure to the risk of changes in foreign exchange rates relates primarily to the Group's operating activities (when revenue or expense is denominated in different currency from the Group's functional currency) and the Group's net investments in foreign subsidiaries. The Group enters into foreign currency forward contracts to mitigate its foreign currency risk on its trade receivables.

The Groups' exposure to foreign currency risk at the reporting date comprised:

	2014			**2013**	
	Euro €'000	**USD $'000**	**GBP £'000**	**Euro €'000**	**USD $'000**
Cash and cash equivalents	**104**	**4,580**	**152**	22	695
Trade and other receivables	**178**	**4,125**	**223**	16	3,503
Trade and other payables	**(88)**	**(525)**	**(83)**	(27)	(174)
	194	**8,180**	**292**	11	4,024

Foreign currency sensitivity

The following table demonstrates the sensitivity to a reasonable possible change in the US dollar, Euro and Sterling pound against the Australian dollar, with all other variables held constant:

	Change in USD rate	Effect on profit before tax and other comprehensive income $'000	Change in EUR rate	Effect on profit before tax and other comprehensive income €'000	Change in GBP rate	Effect on profit before tax and other comprehensive income £'000
2014	**3%**	**245**	**3%**	**6**	**3%**	**9**
	– 8%	**(654)**	**– 10%**	**(19)**	**– 6%**	**(18)**
2013	3%	121	4%	–	–	–
	– 7%	(282)	– 9%	(1)	–	–

c. Operational risk

Operational risk is the risk of direct and indirect loss arising from a wide variety of causes associated with company processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Company's operations.

An objective of the Company is to manage operational risk so as to balance the avoidance of financial losses and damage to the Company's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of control to address operational risk is assigned to the Audit and Financial Risk Management Committee. This responsibility is supported by the development of standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- development of contingency plans;
- training and professional development;
- ethical and business standards; and
- risk mitigation, including insurance where this is effective.

d. Credit risk

Credit risk arises from holdings in cash and cash equivalents, trade receivables, and derivative financial instruments.

The Group invests only in deposits and floating rate notes offered by Australia's four main banks.

The Company has limited number of customers. The Company, by policy, performs customer credit assessment prior to entering into a distribution agreement or sales and routinely assesses the financial strength of its customers and reviews distribution agreements. As a result, the Company believes that its accounts receivable credit risk exposure is mitigated and has not experienced significant write-downs in its accounts receivable balances. As of 30 June 2014, GE Healthcare and Regional Healthcare, combined, accounts for over 91% of the trade receivables (2013: GE Healthcare and Regional Healthcare, combined, accounts for over 99% of the trade receivables).

The credit risk arising from derivative financial instruments is not significant.

The maximum exposure to credit risk as at the reporting date is the carrying amount of the financial assets as set out above. The carrying amount is determined according to the Group's accounting policies.

e. Liquidity risk

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 invested in short and medium term instruments which are tradeable in highly liquid markets.

Maturity profile

Following is the contractual maturity profiles of undiscounted cash flows from financial liabilities:

	On demand $'000	Less than 3 months $'000	3 to 12 months $'000	1 to 5 years $'000	Over 5 years $'000	Total $'000
2014						
Trade and other payables	**–**	**2,104**	**–**	**–**	**–**	**2,104**
Borrowings	**–**	**2**	**6**	**19**	**–**	**27**
Convertible notes	**–**	**–**	**450**	**8,850**	**–**	**9,300**
Total financial liabilities	**–**	**2,106**	**456**	**8,869**	**–**	**11,431**
2013						
Trade and other payables	–	2,553	–	–	–	2,553
Borrowings	–	2	6	28	–	36
Derivative financial instruments	–	198	–	–	–	198
Convertible notes	–	–	–	9,300	–	9,300
Total financial liabilities	–	2,753	6	9,328	–	12,087

Fair values

Set out below is a comparison by class of the carrying amounts and fair value of the Group's financial instruments that are carried in the financial statements

		2014 $'000		2013 $'000	
	Notes	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets					
Cash and cash equivalents	**9**	**21,233**	**21,233**	24,064	24,064
Trade and other receivables	**10**	**5,712**	**5,712**	4,199	4,199
		26,945	**26,945**	28,263	28,263
Financial liabilities					
Fair value through profit and loss					
Derivative financial instruments		**–**	**–**	(198)	(198)
Not measured at fair value					
Other financial liabilities					
Trade and other payables	**16**	**(2,104)**	**(2,104)**	(2,553)	(2,553)
Convertible notes	**20**	**(8,097)**	**(8,097)**	(7,541)	(7,541)
Borrowings	**19**	**(24)**	**(24)**	(30)	(30)
		(10,225)	**(10,225)**	(10,322)	(10,322)

The fair value of the financial assets and liabilities is included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The following methods and assumptions were used to estimate fair values:

- Cash and cash equivalents, trade and other receivables, trade and other payables approximate their carrying amounts largely due to the short term maturities of these instruments.
- The Group enters into derivative financial instruments with various counterparties principally with Australia's major banks. Derivatives valued using valuation techniques with market observable inputs are mainly foreign exchange forward contract. The valuation technique is described below.

Fair value hierarchy

The Group uses the following hierarchy above for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.
- Level 2: other techniques for which all inputs that have a significant effect on the recorded fair value are observable, either directly or indirectly.
- Level 3: techniques that use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

The valuation techniques used in measuring Level 2 fair values:

Type	Valuation technique
Derivative financial instruments – foreign exchange forward contracts	Market comparison technique: The fair values are based on bank quotes. Similar contracts are traded in an active market and the quotes reflect the actual transactions in similar instruments.

As at 30 June 2014, the Group did not hold any derivative financial instruments carried at fair value (2013: derivative financial liability $198,000).

			Level 1	Level 2	Level 3
		$'000	$'000	$'000	$'000
Foreign exchange forward contracts	**30 June 2014**	–	–	–	–
Foreign exchange forward contracts	30 June 2013	(198)	–	(198)	–

4. Critical accounting estimates and judgments

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates and requires management to exercise judgment in the process of applying the Group's accounting policies. Estimates and associated assumptions and judgments affect the recognised amounts of assets, liabilities, revenues and expenses and the disclosure of contingent liabilities and are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

The key estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of certain assets and liabilities are:

Provision for warranty

The Group has recognised a provision in accordance with the accounting policy describe in note 2. The Group has made assumptions in relation to the values estimated to be required to settle the warranty obligation on all products under warranty at balance date.

Share-based payment transactions

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating the fair value for share based payment transactions requires determining the most appropriate valuation model, which is depended on the terms and conditions of the grant. This estimate also requires determining the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share based-payment transactions are disclosed in note 30 to the financial statements.

Recognition of deferred tax assets

Deferred tax assets are only recognised for unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax asset that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies. Details of the unrecognised deferred tax assets on unused tax losses and non-refundable R&D tax offset are disclosed in note 8 to the financial statements.

5. Segment information

The Group has identified its operating segments based on the internal reports that are reviewed and used by the Managing Director and CEO (the chief operating decision maker) in assessing performance and in determining the allocation of resources. The Group operates in a single operating segment, being the healthcare equipment segment.

Types of products and services

The principal products and services of the healthcare equipment segment are the manufacture and commercialisation of infection control and decontamination products and related technologies.

Major customers

The Group has a number of customers to which it provides products and services. The most significant customer accounts for 82% (2013: 88%) of external revenue. The next most significant customer accounts for 8.4% of external revenue (2013: 7%).

Geographical information

Geographically, the Group operates in the global markets. Australia is the home country of the parent entity.

Revenue from external customers by geographical location is detailed below.

	2014 $'000	2013 $'000
North America	**17,665**	13,165
Australia and New Zealand	**2,267**	1,497
Europe and other countries	**1,560**	237
Total revenue	**21,492**	14,899

Revenues above are allocated based on the country in which the customer is located.

The analysis of the location of non-current assets is as follows:

	2014 $'000	2013 $'000
North America	**10**	17
Australia and New Zealand	**1,903**	1,962
Europe and other countries	**9**	14
Total assets	**1,922**	1,993

Non-current assets for this purpose consist of property, plant and equipment, intangible assets and other non-current assets. Assets and capital expenditure are allocated based on where the assets are located.

6. Other income

	2014 $'000	2013 $'000
Government grants	**1,666**	1,498
Interest income	**739**	1,192
Other income	**1,709**	–
Total	**4,114**	2,690

Government grants comprise

- payments under the Export Market Development Grant scheme,
- 45% research and development refundable tax offset received during the year.

There were no unfulfilled conditions or other contingencies attaching to these grants. The Group did not benefit directly from any other form of governmental assistance.

Other income includes reimbursement of cost by a distributor of $1,707,000. The related costs are included in the operating expenses.

7. Loss before income tax expense

	2014 $'000	2013 $'000
The loss from ordinary activities before income tax includes:		
Expenses		
Staffing costs broken into :		
Salaries and wages	**10,118**	7,859
Superannuation and social security contribution	**1,001**	849
Workers compensation costs	**98**	112
Other employee benefits and staffing costs	**2,677**	2,126
Share based payments	**997**	898
Less: Staffing costs included in cost of sales	**(2,886)**	(2,667)
Total staffing costs	**12,005**	9,177
Depreciation and amortisation	**975**	1,044
Research and development costs	**4,103**	3,167
Rental expenses relating to operating leases	**576**	537
Bad debts provision (reversal)	**5**	(1)
Inventories provision / write off	**536**	197
Unrealised loss (gain) on foreign exchange forward contracts	**–**	198
Realised loss (gain) on foreign exchange forward contracts	**32**	40
Net foreign exchange losses (gains)	**414**	(221)

No development costs were capitalised during the year (2013: Nil).

8. Taxation

	2014 $'000	2013 $'000
(a) Income tax expense		
Operating loss from ordinary activities	**2,636**	5,735
The prima facie income tax benefit applicable to the operating loss is calculated at 28.3% (2013:30%)	**745**	1,721
Non-assessable income		
Research and development tax offset received during the year	**455**	404
Other deductible items	**307**	–
Non-deductible items:		
Research and development expense	**(1,231)**	(950)
Equity based benefits	**(282)**	(157)
Entertainment	**(1)**	(13)
Other temporary differences	**(270)**	10
	(277)	1,015
Deferred tax benefit not recognised	**(1,459)**	(1,048)
Non-refundable research and development tax offset	**1,641**	–
Adjustment in respect of current income tax of previous years	**126**	–
Income tax benefit (expense) reported on the Consolidated statement of profit or loss and other comprehensive income	**31**	(33)

(b) Deferred tax assets

The potential deferred tax assets in a controlled entity, which is a company, arising from tax losses, non-refundable tax offsets and timing differences are only recognised when it is probable that future taxable amounts will be available to utilise those tax losses and temporary differences.

	2014 $'000	2013 $'000
Unrecognised deferred tax assets include:		
Estimated tax losses carried forward	**16,241**	16,157
Non-refundable R&D tax offset	**1,375**	–
	17,616	16,157
Estimated tax losses carried forward:		
Beginning of the year unrecognised tax losses carried forward	**53,856**	50,201
Adjustment in respect of unrecognised tax losses carried forward from previous year	**281**	273
Tax losses for the year	**–**	3,382
	54,137	53,856
Estimated non-refundable R&D tax offset at the end of the year	**3,438**	–

The potential future income tax benefit of tax losses carried forward and non-refundable R&D tax offset will only be obtained if:

(i) the Company and the Group derive future assessable income of a nature and an amount sufficient to enable the benefit to be realised

(ii) the Company and the Group continue to comply with the conditions for deductibility imposed by the law; and

(iii) no changes in tax legislation adversely affect the Company and the Group is realising the benefit.

9. Current assets – Cash and cash equivalents

	2014 $'000	2013 $'000
Cash at bank and on hand	**5,705**	972
Deposits on call	**308**	1,005
Short term deposits	**15,220**	22,087
	21,233	24,064

Cash term investments which are highly liquid irrespective of their maturity dates are classified as current assets at market value as they may not necessarily be held by the Company for their full term.

The Group's exposure to interest rate risk is discussed in note 3. The maximum exposure to credit risk at the reporting date is the carrying amount of each class of cash and cash equivalents mentioned above.

10. Current assets – Trade and other receivables

	2014 $'000	2013 $'000
Trade receivables net of allowance for impairment loss	**5,338**	3,972
GST receivable	**59**	91
VAT receivable	**204**	18
Interest and other receivables	**111**	118
	5, 712	4,199

Trade receivables by geographic region were as follows:

	Carrying amount	
	2014 $'000	2013 $'000
North America	**4,382**	3,846
Australia and New Zealand	**472**	97
Europe and other countries	**484**	29
	5,338	3,972

Maximum exposure to credit risk for trade receivable by type of counterparty was as follows:

	Carrying amount	
	2014 $'000	2013 $'000
Distributors	**5,310**	3,944
Others	**28**	28
	5,338	3,972

As at 30 June 2014, the aging analysis of trade receivables is as follows:

			Past due but not impaired		
	Total $'000	Neither past due nor impaired $'000	<30 days $'000	30-60 days $'000	>60 days $'000
2014	**5,338**	**5,295**	**28**	**1**	**14**
2013	3,972	3,964	2	1	5

An analysis of the credit policy of trade receivables that are neither past due nor impaired is as follows:

	2014 $'000	2013 $'000
External financial ratings at least 1A from Dun & Bradstreet	**4,826**	3,878
Other customers:		
Four or more years trading history with the Group	**453**	53
Less than four years of trading history with the Group	**16**	33
	5,295	3,964

Information about the Group's exposure to foreign currency risk in relation to trade and other receivables is provided in note 3.

Due to the short-term nature of the receivables, their carrying amount is assumed to approximate their fair value. The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivables mentioned above. Collateral is not held as security, nor is it the Group's policy to transfer (on-sell) receivables to special purpose entities.

As at 30 June 2014, trade receivables with a nominal value of $5,000 (2013: Nil) were considered impaired.

The movement in allowance for impairment in respect of trade and other receivables during the year was as follows:

	$000
At 1 July 2012	**1**
Increase for the year	–
Utilised	–
Unused amount reversed	(1)
At 30 June 2013	–
Increase for the year	**5**
Utilised	–
Unused amount reversed	–
At 30 June 2014	**5**

Notes to the financial statements (continued)

For the year ended 30 June 2014

11. Current assets – Inventories

	2014 $'000	2013 $'000
Raw materials and stores – at net realisable	**2,211**	1,854
Work in progress – at cost	**737**	673
Finished goods – at net realisable value	**1,289**	382
	4,237	2,909

Write-downs of inventories to net realisable values during the year ended 30 June 2014 amounted to $536,000 (2013:$197,000). The expense has been included in other operating costs in profit or loss.

Roll forward of provision for inventories:	2014 $'000	2013 $'000
Beginning balance	**147**	485
Provided during this year	**536**	197
Utilised during this year	**(326)**	(535)
Ending balance	**357**	147

12. Current assets – Other

	2014 $'000	2013 $'000
Prepaid expenses	**388**	475
Prepaid foreign income tax	**31**	10
Service work in progress	**21**	3
	440	488

13. Non-current assets – Property plant and equipment

	Laboratory fit out	Laboratory equipment	Office furniture & equipment	Leasehold improvements	Manufacturing equipment	Service, test & demo equipment	Computer equipment & software	Capital Work in Progress	Total
Year ended 30 June 2013									
Opening net book amount	13	65	118	149	674	159	290	–	1,468
Additions	–	27	14	6	88	838	275	97	1,345
Retirement and others	–	–	–	–	–	–	–	–	–
Depreciation charge	(3)	(26)	(49)	(138)	(300)	(283)	(205)	–	(1,004)
Foreign currency translation effect (net)	–	–	–	–	–	2	1		3
Closing net book amount at 30 June 2013	10	66	83	17	462	716	361	97	1,812
At 30 June 2013									
Cost	343	351	817	882	1,546	1,462	1,057	97	6,555
Accumulated depreciation	(333)	(285)	(734)	(865)	(1,084)	(746)	(696)	–	(4,743)
Net book amount at 30 June 2013	10	66	83	17	462	716	361	97	1,812
Year ended 30 June 2014									
Opening net book amount	**10**	**66**	**83**	**17**	**462**	**716**	**361**	**97**	**1,812**
Additions	**–**	**32**	**98**	**58**	**96**	**601**	**179**	**17**	**1,081**
Retirement and others	**–**	**–**	**–**	**–**	**–**	**(177)**	**–**	**–**	**(177)**
Depreciation charge	**(3)**	**(29)**	**(41)**	**(37)**	**(250)**	**(353)**	**(225)**	**–**	**(938)**
Foreign currency translation effect (net)	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Closing net book amount at 30 June 2014	**7**	**69**	**140**	**38**	**308**	**787**	**315**	**114**	**1,778**
At 30 June 2014									
Cost or fair value	**343**	**383**	**915**	**940**	**1,642**	**1,804**	**1,235**	**114**	**7,376**
Accumulated depreciation	**(336)**	**(314)**	**(775)**	**(902)**	**(1,334)**	**(1,017)**	**(920)**	**–**	**(5,598)**
Net book amount at 30 June 2014	**7**	**69**	**140**	**38**	**308**	**787**	**315**	**114**	**1,778**

14. Non-current assets – Intangible assets

	2014 $'000	2013 $'000
Development Costs		
At cost	**201**	201
Accumulated amortisation	**(201)**	(164)
Net book value	**–**	37

Development costs relate to the trophon® EPR project and are carried at cost less accumulated amortisation. The intangible asset has been assessed as having a finite life and is amortised using the straight line method over a period of 5 years. Amortisation of $37,000 (2013:$40,000) is included in depreciation and amortisation expense in the statement of profit or loss.

15. Non-current assets – Other

	2014 $'000	2013 $'000
Refundable deposits and bonds	**144**	144
Total	**144**	144

16. Current liabilities – Trade and other payables

	2014 $'000	2013 $'000
Trade payables	**575**	1,302
Other payables	**1,529**	1,251
Provision for warranty	**896**	449
Total	**3,000**	3,002

Roll forward of provision for warranty:

	2014 $'000	2013 $'000
Beginning balance	**449**	368
Provided during this year	**701**	638
Utilised during this year	**(254)**	(557)
Balance as at 30 June	**896**	449

The Group has recognised a provision for warranty in accordance with the accounting policy describe in note 2. The Group has made assumptions in relation to the values estimated to be required to settle the warranty obligation on all products under warranty at balance date.

17. Current liabilities – Deferred revenue

	2014 $'000	2013 $'000
Beginning balance	**209**	91
Deferred during the year	**616**	416
Released to profit or loss	**(517)**	(298)
Ending balance	**308**	209

18. Employee provisions

	2014 $'000	2013 $'000
Provision for bonuses	**723**	157
Provision for annual leave	**690**	607
Provision for long service leave	**267**	202
Total	**1,680**	966
Employee provisions – current		
Provision for bonus	**723**	157
Provision for annual leave	**690**	607
Provision for long service leave	**108**	19
Total	**1,521**	783
Employee provisions – non-current		
Provision for long service leave	**159**	183
Total	**159**	183

The provision for long service leave includes all unconditional entitlements where employees have completed the required period of service and also where employees are entitled to pro-rata payments in certain circumstances.

Superannuation commitments

The Company makes contributions to superannuation plans for the benefit of eligible employees. The Company has a legally enforceable obligation to make these contributions under the auspices of the Superannuation legislation and related guidelines proclaimed by the federal government. The contributions are made as a fixed percentage of salary.

19. Borrowings

	2014 $'000	2013 $'000
Finance lease obligations	**24**	30
Current portion	**6**	6
Non-current portion	**18**	24
Total	**24**	30

20. Convertible notes

	2014 $'000	2013 $'000
Non-current liabilities		
Convertible notes at amortised value	**8,097**	7,541
Equity		
Option premium on convertible notes	**376**	376

On 28 June 2012, the Company issued unsecured Tranche A convertible note of $4,000,000 and Tranche B convertible note of $3,500,000 which matures 4 years after the issue date. The convertible notes bear 6% interest per annum on a simple interest basis calculated on each anniversary of the issue date. No interest repayment will be made to the noteholder in the first two years but the interest will accrue and form part of the face value of the note but will not bear any further interest. After that period, the noteholder may elect whether to receive interest in cash or to have such interest accrue and form part of the Face Value (but this will not bear further interest). The convertible notes may be converted at any time up until the Maturity Date at $0.75 per share, subject to certain adjustments. The effective interest on convertible notes is 7.364%.

As at 30 June 2014, the amortised value of convertible notes recognised in non-current liabilities including accrued interest amounted to $8,097,000 (2013: $7,541,000) and borrowing costs related to the convertible notes amounted to $555,000 (2013: 517,000).

21. Contributed equity

Share capital

263,823,826 ordinary fully paid shares (2013: 261,988,718)

	Number of shares	$'000
Movements in ordinary shares on issue		
At 30 June 2012	259,982,918	73,532
Share options exercised	1,287,604	203
Share issued	718,196	333
At 30 June 2013	**261,988,718**	**74,068**
Share options exercised	1,835,108	**342**
Shares issued	–	–
At 30 June 2014	**263,823,826**	**74,410**

All ordinary shares are fully paid. Ordinary shares carry one vote per share and entitle the holder to participate in dividends and the proceeds on winding up of the Company in proportion to the number of shares held. On a show of hands, every ordinary shareholder present at a meeting in person or by proxy is entitled to one vote and upon a poll each share is entitled to one vote. Ordinary shares have no par value and the Company does not have a limited amount of authorised capital.

At 30 June 2014 there were 6,525,597 (2013: 5,418,625) options to acquire one ordinary share each outstanding, of which 1,705,668 (2013: 1,397,002) had vested and were exercisable.

Information relating to the Company's employee share-based payment schemes, including details of shares and options issued, options exercised and options lapsed during the financial year, as well as options outstanding at the end of the financial year, is set out in note 30.

Capital Management

Management controls the capital of the Group to ensure that the Group can fund its operations and continue as a going concern.

The Group's capital includes ordinary share capital and financial liabilities supported by financial assets. There are no externally imposed capital requirements. Management effectively manages the Group's capital by assessing the Group's financial risks and adjusting its capital structure in response to changes in these risks and in the market. These responses include the management of share issues.

There have been no changes in the strategy adopted by management to control the capital of the Group since the prior year.

22. Reserves

	2014 $'000	2013 $'000
Employee equity benefits reserve	**3,671**	2,673
Foreign currency translation reserve	**20**	27
Balance 30 June	**3,691**	2,700

Employee equity benefits reserve

	2014 $'000	2013 $'000
Balance 1 July	**2,673**	1,775
Share-based payment (ESOP)	**940**	804
Share-based payment (GSOP)	**58**	94
Balance 30 June	**3,671**	2,673

The employee equity benefits reserve is used to record the value of share based payments provided to employees, including KMP, as part of their remuneration. Refer to note 30 for further details of these plans.

Foreign currency translation reserve

	2014 $'000	2013 $'000
Balance 1 July	**(27)**	(11)
Exchange difference on foreign currency translation during the year	**7**	38
Balance 30 June	**20**	(27)

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

23. Dividends

No dividends were proposed, declared or paid during the financial year and to the date of this report (2013: Nil).

24. Capital and leasing commitments

	2014 $'000	2013 $'000
Future operating lease commitments not provided for in the financial statements and payable:		
Within one year	**473**	462
One year or later and no later than five years	**105**	189
	578	651

The Group does not have any non-cancellable capital expense commitments.

Finance lease and hire purchase commitments

	2014		2013	
	$'000	$'000	$'000	$'000
	Minimum payments	Present value of payments	Minimum payments	Present value of payments
Within one year	**8**	**6**	8	6
After one year but not more than 5 years	**19**	**18**	28	24
Total minimum lease payments	**27**	**24**	36	30
Less finance charges	**3**	**–**	6	–
Present value of minimum lease payments	**24**	**24**	30	30

25. Auditor's remuneration

	2014 $'000	2013 $'000
Audit services		
Audit and review of financial reports	**56,000**	52,000
Total remuneration for audit services	**56,000**	52,000
Non-audit services		
Assurance related services		
Audit of regulatory returns	**–**	–
Total remuneration for assurance related services	**–**	–
Total remuneration for non-audit services	**–**	–

26. Information relating to subsidiaries

The consolidated financial statements of the Group include:

Name of controlled entity	Principal activities	Country of incorporation	Class of shares	Equity Holdings 2014	Equity Holdings 2013
Nanosonics Europe GmbH	Provision of sales and customer support services to Nanosonics Limited in Germany	Germany	Ordinary	**100%**	100%
Saban Ventures Pty Limited	Owner of the registered intellectual property of the Group	Australia	Ordinary	**100%**	100%
Nanosonics Inc.	Provision of sales and customer support services to Nanosonics Limited in USA	USA	Ordinary	**100%**	100%

Parent entity

The parent entity within the Group is Nanosonics Limited which is based and listed in Australia.

27. Related party disclosures

Note 26 provides the information about the Group's structure including the details of the subsidiaries and the parent entity.

(a) Transactions with related parties

Certain directors and Key Management Personnel, or their personally-related entities, hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities. Details of the type of transactions that were entered into with directors and KMP are as follows:

Directors and Key Management Personnel	Related entities	Transactions
Maurie Stang	Gryphon Capital Pty Ltd	Director fees and services received
Maurie Stang	Novapharm Research (Australia) Pty Ltd	Services received
Maurie Stang	Ramlist Pty Ltd	Rent of premises
Maurie Stang	Regional Healthcare Group Pty Ltd	Products purchased, services received and products sold
Richard England	Angleterre Pty Ltd and Domkirke Pty Ltd	Director fees and services received

The following transactions occurred with related parties:

	2014 $'000	2013 $'000
Key Management Personnel – Other directors' interests		
Sales of goods and services		
Sale of products to related parties	**1,812**	1,056
Purchases of goods		
Purchases of goods and services from related parties	**357**	553
Other transactions		
Rent of premises and equipment from related parties	**184**	185

(b) Outstanding balances arising from sales/purchases of goods and services

The following balances are outstanding at the reporting date in relation to transactions with related parties:

	2014 $'000	2013 $'000
Key Management Personnel – Other directors' interests		
Current receivables (supply of goods and services)	**450**	53
Current payables (purchases of goods and services)	**18**	37

There were no provisions for doubtful debts relating to the outstanding balances from related parties (2013: Nil) and there were no expenses recognized during the period in respect of doubtful debts from related parties.

Notes to the financial statements (continued)

For the year ended 30 June 2014

(c) Guarantees

No guarantees were provided during the year under review and none were in effect at the year-end between the Company and its subsidiaries (2013: Nil).

(d) Terms and conditions

The terms and conditions of the transactions were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions with unrelated entities on an arms-length basis.

All other transactions were made on normal commercial terms and conditions and at market rates, except that there are no fixed terms for the repayment of loans between the parties.

Outstanding balances are unsecured and are repayable in cash.

(e) Directors and key management personnel compensation

	Group and Company	
	2014 $'000	**2013 (Restated) $'000**
Director fees	**262,631**	265,450
Short-term employee benefits	**1,262,657**	913,138
Long-term benefits	**182,951**	132,357
Termination benefits	**–**	–
Share based payments	**547,576**	379,255
Total compensation	**2,255,815**	1,690,200
Total compensation includes total remuneration for executive and non-executive directors of the parent entity	**1,461,983**	835,647

The 2013 KMP remuneration disclosure was restated to exclude executives who were previously included as among the five named executives who received the highest remuneration in 2013, whose roles and responsibilities were determined to have not met the definition of KMP. Accordingly, the 2013 Directors and KMP compensation as previously reported of $2,347,711 was restated to $1,690,200. In addition, annual leave is now included in other long term benefits (previously shown as short term employee benefit).

Options and performance rights were granted to KMP as part of their compensation. Details of options and performance rights provided as remuneration and shares issued on exercise of such options, together with the terms and conditions of the options, can be found in Sections 4 to 5 of the Remuneration Report on pages 31 to 47.

(f) Loans to directors and key management personnel

During the financial year and to the date of this report, the Group made no loans to directors and key management personnel and none were outstanding at the year ended 30 June 2014 (2013: Nil).

28. Notes to the cash flow statements

(a) Reconciliation of cash

	2014 $'000	2013 $'000
Cash and cash equivalents	**21,233**	24,064

For the purpose of the Statement of cash flows, cash includes cash on hand and at bank, deposits on call and short term deposits, net of outstanding bank overdrafts. Cash at the end of the financial year as shown in the Statement of cash flow is reconciled to the related items in the statement of financial position as follows:

(b) Reconciliation of operating loss after income tax to net cash provided by operating activities

	2014 $'000	2013 $'000
Operating loss after income tax	**(2,605)**	(5,768)
Adjustment for :		
Depreciation and amortisation	**975**	1,044
Share based payments expense	**997**	898
Borrowing costs on convertible notes	**555**	517
Unrealised foreign exchange loss (gain)	**119**	(70)
Changes in assets and liabilities		
(Increase) / decrease in receivables	**(1,573)**	(1,171)
(Increase) / decrease in inventories	**(1,752)**	(512)
(Increase) / decrease in other current assets	**51**	(285)
(Increase) / decrease in other non-current assets	**–**	(3)
Increase / (decrease) in derivative financial instruments	**(198)**	238
Increase /(decrease) in trade and other payables	**(728)**	130
Increase /(decrease) in provisions	**717**	(151)
Increase / (decrease) in other current liabilities	**854**	623
Increase / (decrease) in current tax liabilities	**(6)**	4
Net cash used in operating activities	**(2,594)**	(4,506)

(c) Credit standby arrangements unused

		Facility Limit $'000	Facility used by $'000	Facility available at $'000
Borrowing facilities	**30 June 2014**	**256**	**50**	**206**
	30 June 2013	256	74	182

29. Loss per share

	2014 Cents	2013 Cents
(a) Basic loss per share		
Loss attributable to ordinary shareholders of the Company	**(1.0)**	(2.2)
(b) Diluted loss per share		
Loss attributable to ordinary shareholders of the Company	**(1.0)**	(2.2)
(c) Losses used in calculating loss per share		
Net loss after income tax expense attributable to shareholders	**(2,605)**	(5,768)
(d) Weighted average number of shares used		
For basic earnings per share	**263,072,467**	261,201,368
For diluted earnings per share	**263,072,467**	261,201,368

(e) Information concerning options granted

Options granted under the Nanosonics Employee Share Option Plan and the Nanosonics General Share Option Plan are considered to be potential ordinary shares and have been excluded from the calculation of diluted loss per share as the effect would have been anti-dilutive. Details relating to the options are set out in note 30 to these financial statements.

30. Share-based compensation

The Company's share based compensation schemes comprise option plans and share plans. Options have been granted under the option plans. Shares have been granted under the Deferred Employee Share Plan. To the date of this report no shares have been granted under the Exempt Employee Share Plan.

(a) Option plans

The Nanosonics Employee Share Option Plan (ESOP) and the Nanosonics General Share Option Plan (GSOP) were established in 2007 and last approved by the shareholders in the 2013 Annual General Meeting (AGM) on 8 November 2013. Under the plans, participants are granted options for no consideration. Options may only be excercised on or after any vesting dates specified by the Board at the time of offer. The exercise price of options is determined by the Board at the time of issue. Participation in the plans is at the Board's discretion and no individual has a contractual right to participate in a plan or to receive any guaranteed benefits.

General Share Option Plan (GSOP)

The General Share Option Plan is designed to provide incentive, recognition and reward for non-employees, usually consultants and contractors, who create long-term value for the Company.

No share options were issued under the GSOP during the financial year (2013: 536,038 issued).

Employee Share Option Plan (ESOP)

The Employee Share Option Plan is designed to provide the deferred equity component of the short-term incentive and long-term incentives for employees (including executive directors) to deliver long-term shareholder returns. All employees and directors are eligible to participate in the ESOP at the invitation of the Board. The maximum number of options able to be on issue under the ESOP during any five-year period is 5% of the total number of shares on issue. 2,981,494 share options were issued under the ESOP during the financial year (2013: 2,487,891 issued).

(b) Exercise of options

Options are granted under the plans for no consideration and options carry no dividend or voting rights. When exercisable, each option is convertible into one ordinary share that ranks equally with any other share on issue in respect of dividends and voting rights. The exercise prices of all options issued to the date of this report were fixed on the dates the options were granted. Details are provided in section (c) of this note.

(c) Reconciliation of outstanding share options and performance rights

The number and weighted average exercise price (WAEP) of share options and performance rights under the share option plans were as follows:

Number of Options	ESOP				GSOP				All Option Plans	
	2014		2013		2014		2013		2014	2013
	Number of options and rights	WAEP ($)	Number of options and rights	WAEP ($)	Number of options and rights	WAEP ($)	Number of options and rights	WAEP ($)	Number of options and rights	Number of options and rights
Unexpired options as at 1 July	**4,603,625**	**0.35**	3,330,719	0.54	**815,000**	**0.55**	427,550	0.56	**5,418,625**	3,758,269
Granted during the year	**2,981,494**	**–**	2,487,891	–	**–**	**–**	536,038	0.45	**2,981,494**	3,023,929
Exercised during the year	**(1,573,442)**	**0.13**	(1,173,016)	0.16	**(261,666)**	**0.53**	(114,588)	0.15	**(1,835,108)**	(1,287,604)
Forfeited during the year	**(39,414)**	**–**	(41,969)	–	**–**	**–**	(34,000)	0.35	**(39,414)**	(75,969)
Expired during the year	**–**	**–**	–	–	**–**	**–**	–	–	**–**	–
Unexpired options as at 30 June	**5,972,263**	**0.24**	4,603,625	0.35	**553,334**	**0.57**	815,000	0.55	**6,525,597**	5,418,625
Number of holders as at 30 June	**20**		68		**5**		6		**25**	74

Notes to the financial statements (continued)

For the year ended 30 June 2014

Set out below are details of unexpired options granted under the plans as at 30 June 2014:

Option Plan	Exercise price	Grant date	Assessed fair value at grant date	Expiry date	Number at start of the year	Number granted during the year	Number exercised during the year	Number forfeited during the year	Number at end of the year	Number vested and exercisable at end of year
GSOP	$0.55	Jan-10	$0.30	05-Jan-14	50,000	–	(50,000)	–	–	–
ESOP	$0.56	Aug-10	$0.31	19-Jul-14	500,000	–	(166,000)	–	334,000	334,000
GSOP	$0.78	Oct-10	$0.49	01-Oct-14	100,000	–	–	–	100,000	100,000
ESOP	$0.56	Mar-11	$0.63	19-Jul-14	200,000	–	(200,000)	–	–	–
ESOP	$0.92	Mar-11	$0.58	23-Feb-15	30,000	–	–	–	30,000	30,000
ESOP	$0.85	May-11	$0.50	28-Apr-16	1,400,000	–	–	–	1,400,000	1,166,668
GSOP	$0.53	Nov-11	$0.38	21-Nov-15	195,000	–	(80,000)	–	115,000	50,000
ESOP	$0.00	Jun-12	$0.49	01-Apr-15	13,537	–	(6,768)	–	6,769	–
ESOP	$0.00	Nov-12	$0.55	30-Sep-15	1,220,000	–		–	1,220,000	–
ESOP	$0.00	Nov-12	$0.55	01-Oct-13	544,191	–	(533,745)	(10,446)	–	–
GSOP	$0.51	Nov-12	$0.27	24-Nov-16	195,000	–	(40,000)	–	155,000	25,000
GSOP	$0.52	Dec-12	$0.20	21-Nov-16	275,000	–	(91,666)	–	183,334	-
ESOP	$0.00	Apr-13	$0.45	01-Apr-14	695,897	–	(666,929)	(28,968)	–	–
ESOP	$0.00	Aug-13	$0.78	30-Sep-15	–	712,970	–	–	712,970	–
ESOP	$0.00	Nov-13	$0.68	30-Sep-16	–	442,409	–	–	442,409	–
ESOP	$0.00	Nov-13	$0.85	30-Sep-16	–	442,409	–	–	442,409	–
ESOP	$0.00	Nov-13	$0.71	30-Sep-17	–	375,000	–	–	375,000	–
ESOP	$0.00	Nov-13	$0.85	30-Sep-17	–	375,000	–	–	375,000	–
ESOP	$0.00	Mar-14	$0.63	30-Sep-16	–	316,847	–	–	316,847	–
ESOP	$0.00	Mar-14	$0.80	30-Sep-16	–	316,859	–	–	316,859	–
Total					**5,418,625**	**2,981,494**	**(1,835,108)**	**(39,414)**	**6,525,597**	**1,705,668**

(d) Fair value of options and performance rights granted

The assessed fair value on the date options were granted was independently determined using an appropriate option valuation model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield and the risk-free interest rate for the term of the option.

Terms and condition of the options and performance rights granted and the inputs to the valuations of options and performance rights granted and not expired to 30 June 2014 included:

Option type	Vesting Conditions	Exercise price	Grant date	Expiry date	Estimated share price at grant date	Valuation model	Expected price volatility of the company's shares	Expected dividend yield	Risk-free interest rate	Assessed fair value at grant date
Granted during the year:										
ESOP (a)	FY15 Revenue, net profit after tax and service condition	$0.00	Aug-13	30-Sep-15	$0.78	Binomial	45.49%	0%	2.35%	$0.78
ESOP (b)	Relative TSR performance and service condition	$0.00	Nov-13	30-Sep-16	$0.85	Monte Carlo	45.00%	0%	3.00%	$0.68
ESOP (c)	FY16 Revenue, net profit after tax and service condition	$0.00	Nov-13	30-Sep-16	$0.85	Binomial	45.00%	0%	3.00%	$0.85
ESOP (d)	Relative TSR performance and service condition	$0.00	Nov-13	30-Sep-17	$0.85	Monte Carlo	45.00%	0%	3.20%	$0.71
ESOP (e)	FY17 Revenue, net profit after tax and service condition	$0.00	Nov-13	30-Sep-17	$0.85	Binomial	45.00%	0%	3.20%	$0.85
ESOP (f)	Relative TSR performance and service condition	$0.00	Mar-14	30-Sep-16	$0.80	Monte Carlo	45.00%	0%	2.68%	$0.63
ESOP (g)	FY16 Revenue, net profit after tax and service condition	$0.00	Mar-14	30-Sep-16	$0.80	Binomial	45.00%	0%	2.68%	$0.80
Granted in prior periods and unexpired at report date:										
ESOP	Service Condition until first exercise date of each tranche	$0.56	Aug-10	19-Jul-14	$0.54	Black & Scholes	74.87%	0%	4.77%	$0.31
GSOP	Not applicable	$0.78	Oct-10	01-Oct-14	$0.80	Black & Scholes	77.58%	0%	4.95%	$0.49
ESOP	Service Condition until first exercise date of each tranche	$0.92	Mar-11	23-Feb-15	$0.93	Black & Scholes	80.48%	0%	5.15%	$0.58
ESOP	Service Condition until first exercise date of each tranche	$0.85	May-11	28-Apr-16	$0.80	Black & Scholes	73.62%	0%	5.14%	$0.50
GSOP	Service Condition until first exercise date of each tranche	$0.53	Nov-11	21-Nov-15	$0.63	Black & Scholes	73.09%	0%	3.44%	$0.38
ESOP	Service Condition until first exercise date of each tranche	$0.00	Jun-12	01-Apr-15	$0.49	Binomial	49.04%	0%	2.43%	$0.49
ESOP (a)	FY15 Revenue, net profit after tax and service condition	$0.00	Nov-12	30-Sep-15	$0.55	Binomial	45.46%	0%	2.58%	$0.55
GSOP	Service Condition until first exercise date of each tranche	$0.51	Nov-12	24-Nov-16	$0.56	Binomial	54.96%	0%	2.71%	$0.27
GSOP	Service Condition until first exercise date of each tranche	$0.52	Dec-12	21-Nov-16	$0.49	Binomial	53.13%	0%	2.87%	$0.20

Options marked as per below were granted to key management personnel. Further information is included in section 5 of the Remuneration report.

a. 2012 LTIS granted to key management personnel
b. 2013 LTIS - Tranche 1 granted to the CEO and the Executive Director
c. 2013 LTIS - Tranche 2 granted to the CEO and the Executive Director
d. 2013 LTIS - Tranche 3 granted to the CEO
e. 2013 LTIS - Tranche 4 granted to the CEO
f. 2013 LTIS - Tranche 1 granted to other key management personnel and senior employees
g. 2013 LTIS - Tranche 2 granted to other key management personnel and senior employees

(e) Recognition of expense of options granted

General Share Option Plan (GSOP)

The assessed fair values of options granted under the GSOP are expensed in full in the month in which they are granted and a share based payments reserve is created as part of shareholders' equity, except where the options are granted as part of a capital raising program, in which case no cost is recognised.

Employee Share Option Plan (ESOP)

Options granted under the ESOP require the holder to be an employee of the Company at the time the options are exercised, except that they may be exercised, if vested, up to 30 days after voluntary termination of employment. The assessed fair value of ESOP options granted is apportioned on a straight line monthly basis over the period between grant date and the date on which the options all vest. At the end of a period the Company assesses the probability of achievement of a benefit, being the percentage probability that employees will achieve a benefit if the options are exercised. The value of ESOP options expensed in any period is calculated as that portion of the assessed fair value applicable to the period factored by the probability of achievement and a share based payments reserve is created as part of shareholders' equity.

(f) Employee share plans

The Company has two Employee Share Plans, being the Exempt Employee Share Plan ("EESP") and the Deferred Employee Share Plan ("DESP").

The EESP and DESP was established in 2007 and last approved at a general meeting of shareholders on 8 November 2013. Shareholder approval was also granted to enable the Company to grant financial assistance under both the EESP and the DESP in accordance with the *Corporations Act 2001*.

Exempt Employee Share Plan ("EESP")

The EESP enables eligible employees, including directors, to acquire up to $1,000 worth of Nanosonics shares each year on a tax-exempt basis in accordance with enabling tax legislation. As a contemporary company the Board believes allowing employees to acquire equity in the Company on tax-preferred terms should be encouraged. No shares have been issued under the EESP to the date of this report.

Nanosonics Deferred Employee Share Plan ("DESP")

The DESP allows invited eligible employees, including directors, to receive Nanosonics shares as a bonus or incentive or as remuneration sacrifice and, subject to certain conditions, not to pay tax for up to 10 years on the benefit in accordance with enabling tax legislation. The DESP is designed to allow the Company to meet contemporary executive equity incentive practices. No shares were issued under the DESP during the financial year.

(g) Shares granted

During the financial year there were no shares directly granted under the DESP. Details of shares granted under the DESP to the date of this report are set out below.

Share Plan	Share issue price	Grant date	Assessed fair value at grant date	Closing share price on grant date	Number granted
DESP	0.2880	23 March 2009	0.2880	0.2950	336,424
DESP	0.4251	26 June 2009	0.4251	0.4100	176,400
DESP	0.4251	26 June 2009	0.4251	0.4100	75,000
DESP	0.9080	3 May 2011	0.9080	0.9080	102,403
Total Employee Shares granted to date					**690,227**

Share issued on the exercise of zero-priced options granted to employees as part of their performance bonus or short term incentive has been issued to the DESP.

No shares have been granted to the date of this report under the EESP.

(h) Fair value of shares granted

The issue price for shares granted is calculated as the 5-day weighted average market price of shares of the Company on the Australian Securities Exchange as at close of trading on the date the shares were granted. The fair value of shares granted is taken to be the issue price.

(i) Recognition of expense of shares granted

Deferred Employee Share Plan (DESP)

The assessed fair values of shares granted under the DESP are expensed in full in the month in which they are granted, except if they are granted with a vesting condition, in which case the fair value of DESP shares granted is apportioned on a straight line monthly basis over the period between grant date and the date on which the shares all vest. At the end of a period, the Company assesses the probability of achievement of a benefit, being the percentage probability that employees will achieve at least the fair value of the unvested shares. The value of DESP shares expensed in any period is calculated as that portion of the fair value applicable to the period factored by the probability of achievement. A share based payments reserve is created as part of shareholders' equity.

(j) Shares on issue under employee share plans

	DESP		EESP		All Share Plans	
Number of Shares	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
Employee Shares on issue as at 1 July	**779,053**	305,483	**–**	–	**779,053**	305,483
Granted during the year	**–**	–	**–**	–	**–**	–
Issued on exercise of zero-priced options during the year	**1,207,442**	626,416	**–**	–	**1,207,442**	626,416
Issued on share purchase plan allotment during the year	**–**	7,548	**–**	–	**–**	7,548
Withdrawn during the year	**(861,026)**	(160,394)	**–**	–	**(861,026)**	(160,394)
Forfeited during the year			**–**	–	**–**	–
Employee Shares on issue as at 30 June	**1,125,469**	779,053	**–**	–	**1,125,469**	779,053
Number of holders as at 30 June	**40**	37	**–**	–	**40**	37

(k) Expenses arising from share-based compensation transactions

	2014 $'000	**2013 $'000**
Options issued under ESOP	**940**	804
Options issued under GSOP	**57**	94
Shares issued under DESP	**–**	–
Total share-based compensation	**997**	**898**

31. Parent entity information

As at and throughout the financial year ended 30 June 2014, the parent entity of the Group was Nanosonics Limited. Set out below is the supplementary information about the parent entity.

	2014 $'000	2013 $'000
Financial position of parent entity at year end		
Current assets	**31,157**	31,335
Total assets	**33,147**	33,385
Total current liabilities	**4,567**	3,964
Total liabilities	**12,855**	11,926
Total equity of the parent entity comprising of:		
Contributed Equity	**74,410**	74,068
Convertible Notes	**376**	376
Share option reserve	**3,502**	2,562
Accumulated losses	**(57,996)**	(55,547)
Total equity	**20,292**	21,459
Result of parent entity		
Profit or loss for the year	**(2,448)**	(5,819)
Total comprehensive income (loss)	**(2,448)**	(5,819)
Hire purchase commitment		
For acquisition of Manufacturing equipment	**24**	30

Contingent liabilities

The parent entity had no contingent liabilities.

32. Events subsequent to reporting date

No other matter or circumstance has arisen since 30 June 2014 that has significantly affected, or may significantly affect:

a. the Group's operations in future financial years;

b. the results of those operations in future financial years; or

c. the Group's state of affairs in future financial years.

Directors’ declaration

In the directors’ opinion:

1. the financial statements and notes set out on pages 60 to 102 are in accordance with the *Corporations Act 2001*, including:
   a. complying with Accounting Standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements, and
   b. giving a true and fair view of the Company’s and Group’s financial position as at 30 June 2014 and of their performance for the financial year ended on that date; and
2. there are reasonable grounds to believe that the Company and its subsidiaries will be able to pay their debts as and when they become due and payable.

The directors have been given the declarations by the Managing Director and CEO and Chief Financial Officer required by section 295A of the *Corporations Act 2001*.

This declaration is made in accordance with a resolution of directors.

Richard England
Director
Sydney
21 August 2014

Independent auditor's report to the members

UHY Haines Norton
Chartered Accountants

INDEPENDENT AUDITOR'S REPORT

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To the Members of Nanosonics Limited

Report on the Financial Report

We have audited the accompanying financial report of Nanosonics Limited (the Company), which comprises the consolidated statement of financial position as at 30 June 2014, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the Company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the Corporations Act 2001 and for such internal controls as the directors determine are necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In Note 2b, the directors also state, in accordance with Accounting Standard AASB 101: Presentation of Financial Statements, that the financial statements comply with International Financial Reporting Standards.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit, we have complied with the independence requirements of the Corporations Act 2001.

An association of independent firms in Australia and New Zealand and a member of UHY International, a network of independent accounting and consulting firms.
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Liability limited by a scheme approved under Professional Standards Legislation.

Passion beyond numbers

Auditor's Opinion

In our opinion:

(a) The financial report of Nanosonics Limited is in accordance with the Corporations Act 2001, including:
  i. giving a true and fair view of the consolidated entity's financial position as at 30 June 2014 and its performance for the year ended on that date; and
  ii. complying with Australian Accounting Standards and the Corporations Regulations 2001; and

(b) The consolidated financial report also complies with International Financial Reporting Standards as disclosed in Note 2b;

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 26 to 50 of the directors' report for the year ended 30 June 2014. The directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with s 300A of the Corporations Act 2001. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion, the Remuneration Report of Nanosonics Limited for the year ended 30 June 2014, complies with s 300A of the Corporations Act 2001.

UHY Haines Norton

Mark Nicholaeff
Partner

UHY Haines Norton
Chartered Accountants

Sydney
Date: 21 August 2014

Shareholder information

The shareholder information set out below was applicable as at 12 August 2014.

A. Equity security holders

Twenty largest holders of quoted equity securities

Ordinary shares	Number of quoted shares held	Percentage
Mr Maurie Stang[1]	28,402,424	10.75%
Mr Bernard Stang	27,713,255	10.49%
Citicorp Nominees Pty Limited	26,169,408	9.91%
National Nominees Limited	25,006,402	9.47%
J P Morgan Nominees Australia Limited	23,198,503	8.78%
Mr Steve Kritzler	10,651,439	4.03%
HSBC Custody Nominees (Australia) Limited	8,337,727	3.16%
Link Traders (Aust) Pty Ltd	3,252,381	1.23%
Asia Union Investments Pty Ltd	3,000,000	1.14%
BNP Paribas Noms Pty Ltd <drp>	2,256,243	0.85%
Dr Harry Hirschowitz	2,010,000	0.76%
Armada Trading Pty Ltd	2,000,000	0.76%
Bennelong Resources Pty Limited <John Egan super fund a/c>	1,500,000	0.57%
Citicorp Nominees Pty Limited <Colonial First State Inv a/c>	1,491,521	0.56%
RBC Investor Services Australia Nominees Pty Limited <gsam a/c>	1,295,489	0.49%
Bevan Holdings Pty Ltd <Phillip David Stricker family >	1,229,317	0.47%
Hofbauer Nominees Pty Ltd	1,200,000	0.45%
Nan Employee Share Plan Managers Pty Limited <desp a/c>	1,111,874	0.42%
Moore Family Nominee Pty Ltd <Moore family super fund a/c>	1,044,315	0.40%
Bentale Pty Ltd <Allambi Road family a/c>	1,025,000	0.39%
Total top 20 holders	**171,895,298**	**65.07%**
Total all other holders	92,262,528	34.93%
Total shares on issue	**264,157,826**	**100%**

[1] Includes indirect holdings of 116,368 shares.

Unquoted equity securities	Number of options over ordinary shares	Number of holders
Options on issue		
General Share Options to take up unissued ordinary shares	**503,334**	**4**
Employee Share Options to take up unissued ordinary shares	**5,656,641**	**24**
Total options on issue	**6,159,975**	**28**

B. Distribution of equity securities

Analysis of numbers of ordinary shares and options by size of holding:

	Quoted ordinary shares	Unquoted options
1 - 1,000	341	–
1,001 - 5,000	974	–
5,001 - 10,000	647	1
10,001 - 100,000	1,259	15
100,001 and over	190	12
Total Holders	**3,411**	**28**

There were 141 holders of less than a marketable parcel of 599 ordinary shares.

C. Substantial holders

Substantial holders in the Company are shown below:

	Number of ordinary shares	Percentage
Mr Maurie Stang[1]	28,402,424	10.75%
Mr Bernard Stang	27,713,255	10.49%
Citicorp Nominees Pty Limited	26,169,408	9.91%
National Nominees Limited	25,006,402	9.47%
J P Morgan Nominees Australia Limited	23,198,503	8.78%

[1] Includes indirect holdings of 116,368 shares.

D. Voting rights

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

(a) Ordinary shares

On a show of hands every member present at a meeting in person or by proxy shall have one vote and on a poll each share shall have one vote.

(b) Options

Options have no voting rights.

Glossary

AASB	Australian Accounting Standards Board
AGM	Annual General Meeting
AIUM	American Institute of Ultrasound
ANZ	Australia and New Zealand
ASIC	Australian Securities and Investments Commission
ASUM	Australasian Society for Ultrasound in Medicine
ASX	Australian Securities Exchange Limited
BBSW	Bank bill swap reference rate
CEO	Chief Executive Officer
CFO	Chief Financial Officer
Company	Nanosonics Limited
Date of this report	21 August 2014
DESP	Deferred Employee Share Plan
EESP	Exempt Employee Share Plan
EMS	Environmental Management System
EPS	Earnings Per Share
ESOP	Employee Share Option Plan
Financial Year	Year to 30 June
Fiscal Year	Year to 30 June
FY	Financial year, eg. FY2014 is the financial year ended 30 June 2014
Glutaraldehyde	Organic compound used as a disinfectant and sterilizing agent in medical and dental settings, as well as other uses.
Group	Nanosonics Limited and its wholly owned subsidiary companies
GSOP	General Share Option Plan
GST	Goods and Services Tax
HAI	Healthcare Acquired Infection
HLD	High Level Disinfection – involves the complete elimination of all microorganisms in or on an instrument, except for small numbers of bacterial spores
HPV	Human papilloma virus
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
ISO 13485	Quality Management System for Medical Devices – Requirements for Regulatory Purposes
ISO 14001	Environmental Management System – An international standard developed by the International Organisation for Standardisation through dedicated technical committees representing approximately 150 countries around the world. Its purpose is to enable organisation of any type or size to develop and implement a policy committing it to prevention of pollution, compliance with legal and other requirements and continual improvement.
ISUOG	International Society for Ultrasound in Obstetrics and Gynecology
KFDA	Korean Food and Drug Administration
KMP	Key management personnel
LEAN Program	Program designed to maximize customer value while minimizing waste.
LTI	Long Term Incentives
LTIS	Long Term Incentive Scheme
M&K	Management & Krankenhaus, the leading publication for decision makers in the German health industry
MHRA	Medicines and Healthcare Products Regulatory Agency (MHRA)
MRSA	Methicillin resistant staphylococcus aureus, a bacterium resistant to broad-spectrum antibiotics
NanoNebulant™	The biocide used in Nanosonics' technological process
NED	Non-executive Director
NRTL	Nationally Recognised Testing Laboratory
OHS	Occupational Health & Safety
PBT	Profit before tax
Q1, 2, 3, or 4	3-monthly periods beginning 1 July, 1 October, 1 January and 1 April respectively
R&D	Research and Development
Reporting period	Year to 30 June 2014
STI	Short Term Incentives
TEC	Total Employment Cost
TFR	Total Fixed Remuneration
TJC	The Joint Commission, an independent, non-for-profit organisation, that accredits and certifies more than 20,500 health care organisations and programs in the United States of America
TSR	Total Shareholder Return
TTR	Total Target Remuneration
trophon®	The brand representing Nanosonics' range of infection control solutions designed specifically for healthcare settings
trophon® EPR	The brand of Nanosonics' device specifically designed to disinfect intracavity and surface ultrasound probes. See also www.trophon.com.au
TÜV	TÜVs are German organisations that validate product safety and provide certification for international standards such as ISO9001.
UK	United Kingdom
VAT	Value Added Tax
WAEP	Weighted Average Exercise Price

Corporate directory and information for investors

Nanosonics Limited ABN 11 095 076 896 incorporated 14 November 2000

Directors
Maurie Stang
Richard England
David Fisher
Michael Kavanagh
Ron Weinberger

Company Secretaries
McGregor Grant
Robert Waring

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Dibbs Barker
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Sydney NSW 2000 Australia

Bankers
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National Australia Bank Limited
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North Sydney NSW 2060 Australia

Deutsche Bank AG,
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PNC
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Ambler PA 19002 USA

Stock Exchange Listings
Nanosonics Limited shares are listed on the
Australian Securities Exchange
ASX code: NAN
Industry Group: Healthcare Equipment & Services

2014 Annual General Meeting
The 2014 AGM of Nanosonics Limited will be held:
At 11.00am on Friday 7th November 2014
Level 3, Sydney Harbour Marriott Hotel
30 Pitt Street Sydney

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