

**Priory Group Limited (formerly Priory
Healthcare Acquisition Co Limited)**

Directors' report and financial statements

Year ended 31 December 2003

Registered number 04433255



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Directors' report

The directors present their annual report and the audited financial statements for the year ended 31 December 2003.

The company changed its name from Priory Healthcare Acquisition Co Limited to Priory Group Limited on 20 May 2003.

Principal activities

The principal activity of the company is to act as an intermediate holding company and to raise finance on behalf of fellow subsidiary undertakings.

Business review

The results for the year are set out in the profit and loss account on page 5.

On 11 June 2003, the company disposed of its investments in Jacques Hall Development Limited and Jacques Hall Limited to Priory Securitisation Limited (a subsidiary undertaking) for a consideration of £4 to be left outstanding as a debt repayable on demand. The resulting profit on sale was £nil.

On the same date, the company also disposed of its investment in The Nottingham Clinic Limited to Blenheim Healthcare Limited (a subsidiary undertaking) for a consideration of £437,000 to be left outstanding as a debt repayable on demand. The resulting profit on sale was £nil.

On 4 July 2003, the company disposed of its investment in Highbank Private Hospital Limited to Priory Securitisation Limited (a subsidiary undertaking) for a consideration of £351,000 to be left outstanding as a debt repayable on demand. The resulting profit on sale was £nil.

On 10 June 2003, the company subscribed for one ordinary share in Priory Securitisation Holdings Limited for a consideration of £1.

On 12 August 2003 the company disposed of 51% of its investment in Priory Securitisation Limited to Priory Securitisation Holdings Limited (a subsidiary undertaking) for a consideration of £85 million. The consideration was satisfied by the issue of 999 ordinary shares in Priory Securitisation Holdings Limited. The resulting profit on sale was £nil.

On 29 August 2003, the company disposed of its remaining 49% interest in Priory Securitisation Limited to Priory Securitisation Holdings Limited (a subsidiary undertaking) for a consideration of £82 million to be left outstanding as a debt repayable on demand. The resulting profit on sale was £nil.

On 4 September 2003, the company subscribed for a further 7,687,088 ordinary shares in Priory Securitisation Holdings Limited for a consideration of £7,687,088.

Dividends

The directors do not recommend the payment of a dividend (2002: £nil).

Directors' report *(continued)*

Directors and directors' interests

The directors who held office during the year were as follows:

Dr CB Patel
KJ Terry (resigned 19 February 2004)
RJ Hanson
PJ Greensmith

On 19 February 2004, REJ Savage was appointed as a director of the company.

In accordance with the articles of association, no directors retire by rotation. None of the directors who held office at the end of the financial year had any disclosable interest in the shares of the company.

The interests of the directors in the shares of Priory Healthcare Investments Limited (the ultimate parent company) are disclosed in the financial statements of that company.

Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of PricewaterhouseCoopers LLP as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

By order of the board



PJ Greensmith
Company secretary

Priory House
Randalls Way
Leatherhead
Surrey
KT22 7TP

23 February 2004

Statement of directors' responsibilities

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

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

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

Independent auditors' report to the members of Priory Group Limited (formerly Priory Healthcare Acquisition Co Limited)

We have audited the financial statements which comprise the profit and loss account, the balance sheet and the related notes.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable United Kingdom law and accounting standards are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 2003 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.



PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

23 February 2004

Profit and loss account
for the year ended 31 December 2003

	Note	Year ended 31 December 2003 £000	Period from 8 May to 31 December 2002 £000
Administrative expenses		-	(900)
Operating loss		-	(900)
Income from shares in group undertakings		63,000	-
Amounts written off investments		(16,900)	-
Net interest payable and similar charges	3	(44,615)	(19,257)
Profit/(loss) on ordinary activities before taxation		1,485	(20,157)
Tax on profit/(loss) on ordinary activities	4	8,852	2,065
Profit/(loss) for the financial year		10,337	(18,092)

The company has no recognised gains or losses other than the loss for the year.

The historical cost retained loss and the reported retained loss are the same.

The results for the year derive from continuing activities.

Balance sheet
 at 31 December 2003

	Note	2003 £000	2002 £000
Fixed assets			
Investments	5	92,918	184,919
Current assets			
Debtors	6	41,114	163,333
Cash at bank and in hand		80	-
		<u>41,194</u>	<u>163,333</u>
Creditors: amounts falling due within one year	7	(86)	(50,908)
Net current assets			
Due within one year		10,102	112,425
Debtors due after more than one year	6	31,006	-
		<u>41,108</u>	<u>112,425</u>
Total assets less current liabilities		134,026	297,344
Creditors: amounts falling due after more than one year	8	(141,281)	(314,936)
Net liabilities		(7,255)	(17,592)
Capital and reserves			
Called up share capital	9	250	250
Share premium	10	250	250
Profit and loss account	10	(7,755)	(18,092)
Shareholders' deficit – equity	10	(7,255)	(17,592)

These financial statements were approved by the board of directors on 23 February 2004 and were signed on its behalf by:



PJ Greensmith
 Director

Notes

(forming part of the financial statements)

1 Accounting policies

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

Basis of preparation

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

The company is exempt by virtue of section 228 of the Companies Act 1985 from the requirement to prepare group accounts. These financial statements present information about the company as an individual undertaking and not about its group.

Under Financial Reporting Standard 1 (revised) the company is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the company in its own published consolidated financial statements.

As the company is a wholly owned subsidiary of Priory Healthcare Investments Limited, the company has taken advantage of the exemption contained in Financial Reporting Standard 8 and has therefore not disclosed transactions or balances with entities which form part of the group.

Fixed assets

Fixed asset investments are stated at cost less provision for any impairment in value.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS19.

Group relief

Payment is generally made for group relief at a rate of 30% at the time of first estimating the tax provision. To the extent that amendments are subsequently made to the group relief plan, there is generally no payment or receipt in respect of the change.

2 Auditors and directors' remuneration

The remuneration of the auditors in the year and the prior period was borne by another group undertaking.

The directors received no emoluments for services to the company during the year (*prior period: £nil*).

Notes (continued)

3 Net interest payable and similar charges

	2003 £000	2002 £000
<i>Interest payable and similar charges</i>		
On bank loans and overdrafts	9,280	7,150
Inter-company interest payable	18,123	9,130
Amortisation of issue costs	4,037	3,065
Reverse premium on novation of swap	14,513	-
	<hr/>	<hr/>
	45,953	19,345
<i>Interest receivable and similar income</i>		
On bank deposits	-	(17)
Inter-company interest receivable	(1,338)	(71)
	<hr/>	<hr/>
	44,615	19,257

4 Taxation

	2003 £000	2002 £000
Corporation tax credit on result for the year at 30%	(8,264)	(2,065)
Adjustment relating to prior year	(588)	-
	<hr/>	<hr/>
	(8,852)	(2,065)

The tax credit of £8,264,000 in the year (*prior period: £2,065,000*) is to be surrendered to other group companies in exchange for payment of the same amount.

The standard rate of tax for the year, based on the UK standard rate of corporation tax is 30%. The actual tax charge for the year is above the standard rate for the reasons set out in the following reconciliation:

	2003 £000	2002 £000
Profit/(loss) on ordinary activities before tax	1,485	(20,157)
Tax on profit/(loss) on ordinary activities at standard rate	445	(6,047)
<i>Factors affecting charge for the year</i>		
Income from shares in group undertakings	(18,900)	-
Losses on non-qualifying assets	5,070	-
Expenses not deductible for tax purposes	4,354	235
Other timing differences	-	2,739
Tax losses not recognised	767	1,008
Adjustment to tax charge in respect of prior years	(588)	-
	<hr/>	<hr/>
Total actual amount of current tax	(8,852)	(2,065)

Notes (continued)

4 Taxation (continued)

No provision has been made for a deferred tax asset of £767,000 (prior period: £1,008,000) in respect of tax losses due to there being insufficient current year group taxable profits available to utilise those losses. The recoverability of the tax losses in future years is dependent on the future profitability of the company.

5 Fixed asset investments

	Total £000
Shares in group undertakings	
Cost	
At beginning of the year	184,919
Additions	92,687
Disposals	(184,688)
	<hr/>
At end of the year	92,918
Provisions	
At beginning of the year	-
Provided in the year	16,900
Disposals	(16,900)
	<hr/>
At end of the year	-
Net book value	
At 31 December 2003	92,918
	<hr/>
At 31 December 2002	184,919

Notes (continued)

5 Fixed asset investments (continued)

The principal undertakings in which the company's interest at the year end is more than 20% are as follows:

	Principal activities	Class and percentage of share held
Subsidiary undertakings		
Priory Securitisation Holdings Limited *	Intermediate holding company	100% ordinary
Priory Securitisation Limited	Intermediate holding company	100% ordinary
Priory Healthcare Limited	Psychiatric and other specialist healthcare Services	100% ordinary
Priory Education Services Limited	Specialist schools for children with behavioural difficulties	100% ordinary
Farleigh Schools Limited	Specialist school for children with Asperger Syndrome	100% ordinary
North Hill House Limited	Specialist school for children with Asperger Syndrome	100% ordinary
Eastwood Grange Limited	Specialist school for children with behavioural difficulties	100% ordinary
Chelham Senior School Limited	Specialist school for children with behavioural difficulties	100% ordinary
Priory Services for Young People (IOM) Limited	Specialist schools for children with behavioural difficulties	100% ordinary
Priory Rehabilitation Services Limited	Brain injury rehabilitation services	100% ordinary
Blenheim Healthcare Limited	Forensic psychiatric services	100% ordinary
Priory Central Services Limited	Management services	100% ordinary
Priory Finance Company Limited	Financing company	100% ordinary
Priory Specialist Health Limited	Procurement company	100% ordinary
Priory Healthcare Holdings Limited	Intermediate holding company	100% ordinary
Priory Specialist Health Division Limited	Intermediate holding company	100% ordinary
The Nottingham Clinic Limited	Development company	100% ordinary
Jacques Hall Development Limited	Development company	100% ordinary
Highbank Private Hospital Limited	Development company	100% ordinary
Jacques Hall Limited	Development company	100% ordinary
Priory Healthcare Europe Limited *	Non-trading	100% ordinary
Community Addiction Services Limited *	Non-trading	100% ordinary
Care Continuums Limited *	Non-trading	100% ordinary
Employee Management Services Limited *	Non-trading	100% ordinary
Public Health Solutions Limited *	Non-trading	100% ordinary
Nottcor6 Limited *	Non-trading	100% ordinary
Sturt House Clinic Limited *	Non-trading	100% ordinary
Priory Behavioural Health Limited *	Non-trading	100% ordinary
Medical Imaging (Essex) Limited *	Non-trading	100% ordinary

* interests held directly by the company.

All subsidiary and associated undertakings are registered in England and Wales with the following exceptions:

Priory Finance Company Limited	registered in Cayman Islands
Priory Services for Young People (IOM) Limited	registered in the Isle of Man

Notes (continued)

6 Debtors

	2003 £000	2002 £000
<i>Due within one year</i>		
Amounts due from group undertakings	164	161,268
Group relief recoverable	9,944	2,065
	<hr/>	<hr/>
<i>Due after more than one year</i>	10,108	163,333
12% Sub-ordinated loans owed by subsidiary undertakings	31,006	-
	<hr/>	<hr/>
	41,114	163,333

7 Creditors: amounts falling due within one year

	2003 £000	2002 £000
Bank loans and overdrafts	-	18,097
Amounts due to group undertakings	22	31,109
Accruals and deferred income	64	1,702
	<hr/>	<hr/>
	86	50,908

Notes (continued)

8 Creditors: amounts falling due after more than one year

	2003 £000	2002 £000
Bank loans and overdrafts	-	194,843
Discounted unsecured loan stock 2012 issued at 25.567% owed to Immediate parent undertaking	141,281	124,130
Un-amortised issue costs	-	(4,037)
	<u>141,281</u>	<u>314,936</u>
<i>External debt can be analysed as falling due:</i>		
More than two years but not more than five years	-	2,460
More than five years	-	192,383
	<u>-</u>	<u>194,843</u>
<i>Amounts wholly repayable in more than five years:</i>		
Bank loan – LIBOR plus 2.5% 2010	-	190,000
<i>Amounts repayable by instalments some of which fall due in more than five years:</i>		
Bank loan – LIBOR plus 2.25% 2005 to 2009	-	2,383
	<u>-</u>	<u>192,383</u>

9 Called up share capital

	2003 £000	2002 £000
Authorised		
232,000,000 (2002: 232,000,000) ordinary shares of 50 pence each	116,000	116,000
Allotted, called up and fully paid		
500,000 (2002: 500,000) ordinary shares of 50 pence each	250	250

10 Reconciliation of movement in shareholders' funds

	Share capital £000	Share premium £000	Profit and loss account £000	2003 Total £000	2002 Total £000
At beginning of the year	250	250	(18,092)	(17,592)	-
Issue of shares	-	-	-	-	500
Retained profit/(loss) for the year/period	-	-	10,337	10,337	(18,092)
	<u>250</u>	<u>250</u>	<u>(7,755)</u>	<u>(7,255)</u>	<u>(17,592)</u>

Notes *(continued)*

11 Ultimate parent company

The company is a subsidiary undertaking of Priory Healthcare Finance Co Limited, which is incorporated in England.

The largest group in which the results of the company are consolidated is that headed by Priory Healthcare Investments Limited. No other group accounts include the results of the company.