Priory Rehabilitation Services Limited

Directors' report and financial statements

Year ended 31 December 2004

Registered number 3074698

Contents

Directors' report

The directors present their annual report and the audited financial statements for the year ended 31 December 2004.

Principal activities

The principal activities of the company are the provision of assessment services and acute, post-acute and continuing care services for children and adults with an acquired brain injury, stroke or other form of neurological disorder.

Business review

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

Proposed dividend

The directors do not recommend the payment of a dividend (2003: £nil).

Directors and directors' interests

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

Dr CB Patel
PJ Greensmith

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 Dr CB Patel and PJ Greensmith in the shares of Priory Healthcare Investments Limited (the ultimate parent company) are disclosed in the financial statements of that company.

Employees

The directors recognise that the continued position of the company in the health care industry depends on the quality and motivation of its employees and as such the company is committed to pursue employment policies, which will continue to attract, retain and motivate its employees.

Good and effective employee communications are particularly important, and throughout the business it is the directors' policy to promote the understanding by all employees of the company's business aims and performance. This is achieved through internal publications, presentations on performance and a variety of other approaches appropriate for a particular location.

The directors believe that it is important to recruit and retain capable and caring staff regardless of their sex, marital status, race or religion. It is the company's policy to give full and fair consideration to applications for employment from people who are disabled, to continue wherever possible the employment of and to arrange appropriate training for, employees who become disabled and to provide equal opportunities for the career development, training and promotion of disabled employees.

Directors' report *(continued)*

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

P J Greensmith
Company Secretary

Priory House
Randalls Way
Leatherhead
Surrey
KT22 7TP

28 June 2005

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 Rehabilitation Services Limited

We have audited the financial statements which comprise the profit and loss account, the balance sheet, the statement of total recognised gains and losses, the note of historical cost profits and losses, the reconciliation of movement in shareholders' funds 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 2004 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

28 June 2005

Profit and loss account

for the year ended 31 December 2004

	Note	**2004**	2003
		£000	£000
Turnover	*2*	**13,734**	12,384
Cost of sales		**(11,493)**	(10,155)
Gross profit		**2,241**	2,229
Administrative expenses		**(900)**	(702)
Operating profit		**1,341**	1,527
Profit on disposal of fixed assets		**14**	-
Profit on ordinary activities before interest and tax		**1,355**	1,527
Net interest payable and similar charges	*6*	**(2,357)**	(745)
(Loss)/profit on ordinary activities before taxation	*2,3*	**(1,002)**	782
Tax on (loss)/profit on ordinary activities	*7*	**160**	(264)
Retained (loss)/profit for the financial year		**(842)**	518

The results for both the current and prior year derive from continuing activities.

Balance sheet
at 31 December 2004

	Note	£000	2004 £000	£000	2003 £000
Fixed assets					
Tangible assets	8		**32,293**		24,885
Investments	9		**-**		-
			32,293		24,885
Current assets					
Stocks	10	**29**		29	
Debtors	11	**26,655**		23,426	
Cash at bank and in hand		**889**		12,792	
		27,573		36,247	
Creditors: amounts falling due within one year	12	**(18,799)**		(27,262)	
Net current assets/(liabilities)			**8,774**		8,985
Total assets less current liabilities			**41,067**		33,870
Creditors: amounts falling due after more than one year	13		**(25,440)**		(24,020)
Provisions for liabilities and charges	14		**-**		-
Net assets			**15,627**		9,850
Capital and reserves					
Called up share capital	15		**-**		-
Revaluation reserve	16		**16,894**		10,275
Profit and loss account	16		**(1,267)**		(425)
Shareholders' funds – equity			**15,627**		9,850

These financial statements were approved by the board of directors on 28 June 2005 and were signed on its behalf by:

PJ Greensmith
Director

Statement of total recognised gains and losses
for the year to 31 December 2004

	2004 £000	2003 £000
(Loss)/profit for the financial year	**(842)**	518
Unrealised surplus on revaluation of properties	**6,619**	8,668
Total recognised gains for the year	**5,777**	9,186

Note of historical cost profits and losses
for the year to 31 December 2004

	2004 £000	2003 £000
Reported (loss)/profit on ordinary activities before taxation	**(1,002)**	782
Difference between a historical cost depreciation charge and the actual depreciation charge calculated on the re-valued amount	**154**	12
Historical cost (loss)/profit on ordinary activities before taxation	**(848)**	794
Historical cost (loss)/profit for the period retained after taxation and dividends	**(688)**	530

Reconciliation of movements in shareholders' funds
for the year to 31 December 2004

	2004 £000	2003 £000
(Loss)/profit for the financial year	**(842)**	518
Revaluation surplus	**6,619**	8,668
Net addition to shareholders' funds	**5,777**	9,186
Opening shareholders' funds	**9,850**	664
Closing shareholders' funds	**15,627**	9,850

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 accounting standards and under the historical cost accounting rules, modified to include the revaluation of certain land and buildings.

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 FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the group.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost or valuation, net of depreciation and any provision for impairment.

Assets in course of construction represent the direct costs of purchasing, constructing and installing tangible fixed assets ahead of their productive use. No depreciation is provided on an asset that is in the course of construction until it is completed and transferred to an asset heading that is appropriate.

Depreciation is provided to write off the cost or valuation less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Freehold buildings and long leasehold properties	-	50 years
Short leasehold properties	-	over the period of the lease
Plant, fixtures and fittings	-	3 to 16 years
Motor vehicles	-	over the shorter of the lease and 4 years

Land is not depreciated on the basis that land has an unlimited life. Where the valuation of land and buildings cannot be split, the Directors have estimated that the value attributable to land is 22% of the valuation of the land and buildings.

Revaluation of properties

The company has adopted a policy of revaluation of its properties, as permitted by Financial Reporting Standard 15 - Tangible Fixed Assets. The assets are valued by independent Chartered Surveyors each year at the balance sheet date, on a rolling basis designed to ensure that all properties are specifically valued at least every five years. Any surplus or deficit on book value is transferred to the revaluation reserve, except that a deficit, which is in excess of any previously recognised surplus over depreciated cost relating to the same property, or the reversal of such a deficit, is charge (or credited) to the profit and loss account.

Leases

Assets acquired under finance leases are capitalised and the outstanding future lease obligations are shown in creditors. Operating lease rentals are charged to the profit and loss account on a straight-line basis over the period of the lease.

Notes *(continued)*

1 Accounting policies *(continued)*

Investments

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

Stocks

Stocks are stated at the lower of cost and net realisable value.

Post-retirement benefits

The company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the company in an independently administered fund. The amount charged against profits represents the contributions payable to the scheme in respect of the accounting period.

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 FRS 19.

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 change.

Turnover and revenue recognition

Turnover represents the amounts (excluding value added tax) derived from the provision of services. Revenue is recognised as the services are provided.

2 Analysis of turnover and (loss)/profit on ordinary activities before taxation

The company's turnover, (loss)/profit before taxation and net assets arise primarily from its principal activity of the provision of rehabilitation and ongoing care facilities for people with head injuries in the United Kingdom.

3 (Loss)/profit on ordinary activities before taxation

	2004	2003
	£000	£000
(Loss)/profit on ordinary activities before taxation is stated after charging:		
Auditors' remuneration (inclusive of VAT):		
Audit	**20**	20
Depreciation and other amounts written off tangible fixed assets:		
Owned	**841**	486
Leased	**59**	46
Rentals under operating leases:		
Hire of plant and machinery	**55**	26
Other operating leases	**8**	-

Notes *(continued)*

4 Remuneration of directors

The directors received no emoluments for services to the company during the year *(2003: £nil)*.

5 Staff numbers and costs

The average number of persons employed by the company (including directors) during the year, analysed by category, was as follows:

	Number of employees	
	2004	2003
Nursing and other clinical staff	**382**	354
Administrative staff	**109**	100
	491	454

The aggregate payroll costs of these persons were as follows:

	2004	2003
	£000	£000
Wages and salaries	**6,516**	5,840
Social security costs	**574**	494
Other pension costs	**44**	48
	7,134	6,382

6 Net interest payable and similar charges

	2004	2003
	£000	£000
Interest payable and similar charges		
On bank loans and overdrafts	**130**	39
Inter-company interest payable	**2,165**	676
Amortisation of issue costs	**134**	45
Finance charges payable in respect of finance leases	**11**	12
	2,440	772
Interest receivable and similar income		
Reverse premium on novation of swap	**(83)**	(27)
	2,357	745

Notes *(continued)*

7 Taxation

	2004	2003
	£000	£000
UK corporation tax on income	**(123)**	390
Adjustment in respect of prior years	**(37)**	(81)
	(160)	309
Deferred tax (see note 14)	**-**	(45)
	(160)	264

The tax credit of £123,000 in the year is to be surrendered to other group companies in exchange for payment of the same amount.

The tax charge of £390,000 on profits in the prior year has been relieved by the surrender of losses by 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% *(2003: 30%)*. The actual tax charge for the year is above the standard rate for the reasons set out in the following reconciliation:

	2004	2003
	£000	£000
(Loss)/profit on ordinary activities before tax	**(1,002)**	782
Tax on (loss)/profit on ordinary activities at standard rate	**(301)**	235
Factors affecting charge for the year		
Capital allowances for year in excess of depreciation	**74**	-
Other timing differences	**(18)**	-
Depreciation of non-qualifying assets	**119**	74
Expenses not deductible for tax purposes	**3**	10
Tax losses not recognised	**-**	71
Adjustment to tax charge in respect of prior years	**(37)**	(81)
Total actual amount of current tax	**(160)**	309

Notes *(continued)*

8 Tangible fixed assets

	Freehold land and buildings £000	Assets in course of construction £000	Fixtures and fittings £000	Motor vehicles £000	Total £000
Cost or valuation					
At beginning of the year	23,804	-	2,340	295	26,439
Additions	640	424	314	123	1,501
Disposals	-	-	(723)	(156)	(879)
Surplus on revaluation	6,219	-	-	-	6,219
At end of the year	30,663	424	1,931	262	33,280
Depreciation					
At beginning of the year	19	-	1,367	168	1,554
Charge for the year	381	-	229	59	669
On disposals	-	-	(722)	(114)	(836)
Transfer on revaluation	(400)	-	-	-	(400)
At end of the year	-	-	874	113	987
Net book value					
At 31 December 2004	**30,663**	**424**	**1,057**	**149**	**32,293**
At 31 December 2003	23,785	-	973	127	24,885

Included in the total net book value of motor vehicles is £148,000 *(2003: £127,000)* in respect of assets held under finance leases. Depreciation for the year on these assets was £59,000 *(2003: £46,000).*

Analysis of land and buildings at cost or valuation

	2004 £000	2003 £000
At cost	-	2,262
At valuation	**30,663**	21,523
	30,663	23,785

The Company's land and buildings were re-valued at 31 December 2004, on the basis of existing use value by independent qualified valuers. The valuations were undertaken in accordance with the Practice Statements set out in the Royal Institution of Chartered Surveyors Appraisal and Valuation Standards – 5th Edition, as amended, by Colliers Conrad Ritblat Erdman, a firm of independent Chartered Surveyors.

Notes *(continued)*

8 Tangible fixed assets *(continued)*

The valuations have been incorporated into the financial statements and the resulting revaluation adjustments have been taken to the revaluation reserve. The revaluations during the year ended 31 December 2004 resulted in a revaluation surplus of £6,619,000 (note 16).

The historical net book value of land and buildings is given below:

	2004	2003
	£000	£000
Historical cost of land and buildings	**14,562**	13,922
Aggregate depreciation thereon	**(568)**	(341)
Historical cost net book value	**13,994**	13,581

No deferred tax is provided on timing differences arising from the revaluation of fixed assets unless, by the balance sheet date, a binding commitment to sell the asset has been entered into and it is unlikely that any gain will be rolled over.

9 Fixed asset investments

	Total
	£000
Shares in group undertakings	
Cost	
At beginning and end of the year	1,229
Provision	
At beginning and end of the year	1,229
Net book value	
At 31 December 2004	-
At 31 December 2003	-

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

	Country of incorporation	**Principal Activity**	**Class and Percentage of shares Held**
Subsidiary undertaking			
Robinson Kay House (Bury) Limited	England	Dormant	100% ordinary

Notes *(continued)*

10 Stocks

	2004 £000	2003 £000
Consumable supplies	**29**	29

11 Debtors

	2004 £000	2003 £000
Trade debtors	**2,241**	1,407
Amounts owed by group undertakings	**24,146**	21,964
Other debtors	**11**	11
Group relief recoverable	**123**	-
Prepayments and accrued income	**134**	44
	26,655	23,426

12 Creditors: amounts falling due within one year

	2004 £000	2003 £000
Obligations under finance leases (see note 13)	**54**	50
Trade creditors	**266**	340
Amounts owed to group undertakings	**17,876**	25,978
Corporation tax	**-**	22
Group relief payable	**-**	390
Other taxes and social security	**162**	146
Other creditors	**26**	22
Accruals and deferred income	**415**	314
	18,799	27,262

Notes *(continued)*

13 Creditors: amounts falling due after more than one year

	2004	2003
	£000	£000
Bank loans and overdrafts	**2,145**	1,454
Obligations under finance leases	**109**	110
Amounts due to group undertakings	**22,790**	22,055
Un-amortised issue costs	**(327)**	(454)
Accruals and deferred income	**723**	855
	25,440	24,020

Obligations under finance leases are payable as follows:

	2004	2003
	£000	£000
Within one year or less	**54**	50
Within one to two years	**54**	50
Within two to five years	**55**	60
	163	160

14 Provisions for liabilities and charges

	£000
Deferred tax	
At beginning and end of the year	-

No provision has been made for deferred tax on gains recognised on revaluing property to its market value. Such tax would become payable only if the property were sold without it being possible to claim rollover relief. At 31 December 2004, the total amount un-provided for was £4.9 million *(31 December 2003: £2.6 million)*. At present it is not envisaged that any such tax will become payable in the foreseeable future.

Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the period in which timing differences reverse, based on tax rates and laws substantively enacted at the balance sheet date.

Notes *(continued)*

15 Called up share capital

	2004 £	2003 £
Authorised		
100 *(2003: 100)* Ordinary shares of £1 each	**100**	100
Allotted, called up and fully paid		
100 *(2003: 100)* Ordinary shares of £1 each	**100**	100

16 Reserves

	Revaluation reserve £000	Profit and loss account £000
At beginning of the year	10,275	(425)
Retained loss for the year	-	(842)
Revaluation surplus	6,619	-
At end of the year	**16,894**	**(1,267)**

17 Contingent liabilities

(a) The company has entered into banking facilities set-off agreements in respect of which guarantees have been given. The aggregate amount outstanding under the agreements was £nil at 31 December 2004 *(2003: £nil)*.

(b) A fellow subsidiary undertaking has issued secured fixed and floating rate notes amounting to £201.1 million as at 31 December 2004 *(31 December 2003: £206.2 million)*. These notes are secured on the freehold and leasehold properties of certain of its fellow subsidiaries. In addition, the company's share capital has been pledged as security for this loan.

Notes *(continued)*

18 Commitments

a) Capital commitments at the end of the financial year, for which no provision has been made, are as follows:

	2004	2003
	£000	£000
Contracted	**1,042**	-

b) Annual commitments under non-cancellable operating leases are as follows:

	2004		2003	
	Land and buildings	**Other**	Land and buildings	Other
	£000	**£000**	£000	£000
Operating leases which expire:				
Within one year	**-**	**14**	-	-
In the second to fifth years inclusive	**-**	**29**	-	17
Over five years	**-**	**-**	-	-
	-	**43**	-	17

19 Pension scheme

The company operates a defined contribution pension scheme. The pension cost charge for the year represents contributions payable by the company to the fund and amounted to £44,000 *(2003: £48,000)*.

As at 31 December 2004, there were outstanding contributions of £3,000 *(31 December 2003: £4,000)*.

20 Ultimate parent company

The company is a subsidiary undertaking of Priory Securitisation 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.