

EARGLOW PTY LIMITED ACN 055 664 769

Applicant

**SIGMA PHARMACEUTICALS LIMITED
ACN 088 417 403**

Respondent

DEFENCE

By way of Defence to the Amended Statement of Claim dated 18 April 2011 the respondent says:

1. It admits the allegations in paragraph 1.
2. It does not admit the allegations paragraph 2.
3. It does not admit the allegations in paragraph 3.
4. It admits the allegations in paragraph 4.
5. It admits the allegations in paragraph 5.
6. It admits the allegations in paragraph 6.
- 7.1 As to paragraph 7.1:
 - (a) it admits that on 23 March 2009:
 - (i) it made a results presentation, which included (at page 21) the statement "*Expectation for modest growth in 2009/10.*"
 - (ii) it issued a media release, which included, under the heading 'Outlook', the statement:

"Due to the continuing uncertain environment, the Company is not providing detailed guidance at this time, however we expect to deliver modest growth for the 2009/10 financial year."

Filed on behalf of the respondent
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- (iii) its Chief Executive Officer, Elmo de Alwis, took part in an interview on ABC Lateline Business in which the following statements were made:

Ali Moore: "... you're not giving detailed guidance for the [current] year because of uncertain market conditions."

Elmo de Alwis: "...we felt it was prudent to deploy the guidance that we had as opposed to a more precise level of guidance at this stage."

...

Elmo de Alwis: "We're saying that our five-year plan, strategy plan, is looking for five to 10 per cent growth over the five-year period. And I think if you look at the profile of products coming off patents, generic products that is slightly back loaded in that five-year period. So I think that a modest growth will be something between one and five per cent."

- (b) it admits that on 8 April 2009 it issued its Annual Report for the 2008/2009 financial year which included, under the heading 'Outlook', the statement (at page 13):

"Due to the continuing uncertain environment, the Company is not providing detailed guidance at this time, however we expect to deliver modest growth for the 2009/10 financial year."

- (c) it admits that on 7 September 2009:

- (i) it made a presentation to investors, which included the statements (at pages 17, 20 and 28):

"Sigma maintains its previous guidance of modest growth in NPAT for the full year ending 31 January 2010.

– Assumptions:

- *No changes to regulatory environment*
- *No major business disruptions*
- *No major changes in consumer or customer demand*
- *New product launches as scheduled and as budgeted*
- *No unusual competitor activities or initiatives or introduction of significant competitors*
- *Stable industrial climate*
- *No non-recurring items are anticipated in FY2010 H2.*

– Also refer to Risk Factors in Appendix."

"Key Risks

General Risks

- *Share price and volume fluctuations*
- *Economic risks*
- *Government policies and legislation*
- *Taxation implications*
- *Changes in accounting policy*
- *Asset impairment*

See Appendix for further details"

"Asset impairment ...Sigma has a high level of intangible assets and has grown by brand acquisition. Consistent with accounting standards, Sigma is periodically required to assess the carrying value of its assets, including its brands. Where the value of an asset is assessed to be less than its carrying value, Sigma is obliged to recognise an impairment charge in its profit and loss account. Impairment charges can be significant and operate to reduce the level of a company's profits and, potentially, its capacity to pay dividends. Impairment charges are a non-cash item."

(ii) it issued an announcement, which included the statement:

"Sigma maintains its previous guidance of modest growth in net profit after tax for the full year ending 31 January 2010."^{7,8,9}

⁷ *Excluding impact of equity raising and Acquisition*

⁸ *Assumptions include: No changes to regulatory environment; no major business disruptions; no major changes in consumer or customer demand; new product launches as scheduled and as budgeted; no unusual competitor activities or initiatives or introduction of significant competitors; stable industrial climate; no non-recurring items are anticipated in FY2010 H2*

⁹ *Also refer to Risk Factors in Appendix of the Investor Presentation "*

(d) it admits that on 14 September 2009 it issued:

(i) an announcement, which included the statement:

"Sigma maintains its previous guidance of modest growth in NPAT for the full year ending 31 January 2010, assuming:

- *No changes to regulatory environment*
- *No major business disruptions*
- *No major changes in consumer or customer demand*
- *New product launches as scheduled and as budgeted*
- *No unusual competitor activities or initiatives or introduction of significant competitors*
- *Stable industrial climate*
- *No non-recurring items are anticipated in FY2010 H2"*

(ii) a Retail Entitlement Offer booklet, which contained the following statements (at pages 25, 28 and 36):

"Sigma maintains its previous guidance of modest growth in NPAT for the full year ending 31 January 2010.

– Assumptions:

- *No changes to regulatory environment*
- *No major business disruptions*
- *No major changes in consumer or customer demand*
- *New product launches as scheduled and as budgeted*
- *No unusual competitor activities or initiatives or introduction of significant competitors*
- *Stable industrial climate*
- *No non-recurring items are anticipated in FY2010 H2*

– Also refer to Risk Factors in Appendix."

*"Key Risks**General Risks*

- *Share price and volume fluctuations*
- *Economic risks*
- *Government policies and legislation*
- *Taxation implications*
- *Changes in accounting policy*
- *Asset impairment*

See Appendix for further details"

"Asset impairment ... The Sigma Board regularly monitors impairment risk. Sigma has a high level of intangible assets and has grown by brand acquisition. Consistent with accounting standards, Sigma is periodically required to assess the carrying value of its assets, including its brands. Where the value of an asset is assessed to be less than its carrying value, Sigma is obliged to recognise an impairment charge in its profit and loss account. Impairment charges can be significant and operate to reduce the level of a company's profits and, potentially, its capacity to pay dividends. Impairment charges are a noncash item."

- (iii) its Interim report for the half year ended 31 July 2009, which contained the following statements (at page 15) under the heading 'Estimates':

"The preparation of an interim financial report in conformity with AASB 134: Interim Financial Reporting requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities, income and expenses.

These estimates and associated assumptions 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 the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

...

Management has considered reasonable possible shifts in the movements in key assumptions and is comfortable that no impairment arises.

...

Whilst management has satisfied itself that the carrying value of all assets does not exceed its recoverable amount at balance date, prima facie, there is an increased risk of impairment write-downs given changes in market conditions."

- (e) It otherwise denies each allegation in paragraph 7.1.

7.2 As to paragraph 7.2:

- (a) it admits that on 23 March 2009 it issued its Preliminary Final Report for the financial year ended 31 January 2009, which contained the following statement (at page 13):

"The consolidated entity assesses whether goodwill and intangible assets with indefinite useful lives are impaired at least annually. ...management has considered reasonable possible shifts in the movements of key assumptions and is comfortable that no impairment arises."

- (b) it refers to paragraph 7.1(b) above and admits that its Annual Report for the financial year ended 31 January 2009, also contained the following statements (at page 70):

"Reassessment of Cash Generating Units in prior period

During the prior period management has reassessed the CGU's (sic) to which assets have been allocated. The assessment of CGU's (sic) was updated reflecting changes to managements (sic) internal reporting and integration of the various businesses. The aim of this exercise was to ensure correct allocation of assets to the CGUs that best reflect the way that our business is currently managed.

...

Impact of possible changes in key assumptions

Management has considered reasonable possible shifts in the movements in key assumptions and is comfortable that no impairment arises."

- (c) it refers to paragraph 7.1(d)(ii) above in relation to the Retail Entitlement Offer booklet;
- (d) it refers to paragraph 7.1(d)(iii) above in relation to its Interim report for the half year ended 31 July 2009; and
- (e) it otherwise denies each allegation in paragraph 7.2.

8. It admits the allegations in paragraph 8.

9.1 It:

- (a) admits that the February 2009 Operations Report provided to the board for its meeting on 23 March 2009 stated (at page 5) that:
- (i) the NPAT budget for the first half of FY2010 (1 February 2009 to 31 July 2009) was \$24.341m;
 - (ii) the NPAT budget for the second half of FY2010 (1 August 2009 to 31 January 2010) was \$59.778m;
 - (iii) the NPAT budget for the full FY2010 was \$84.119m;
- (b) admits that the July Operations Report provided to the board for its meeting on 24 August 2009:
- (i) stated (at page 1) that the reported NPAT for the first half of FY2010 was \$32.216m;
 - (ii) stated (at page 1) that the underlying NPAT for the first half of FY2010 was \$30.207m;

- (c) admits that a paper entitled 'Sigma Promotional Analysis Paper' provided to the board for its meeting on 27 July 2009 stated that:
- (i) (at slide 7) the NPAT achieved from promotional activity in Q4 2008/09 was \$18.828m; and
 - (ii) (at slide 10) the NPAT achieved from promotional activity in July 2009 was \$11.735m;
- (d) admits that it had achieved:
- (i) reported NPAT of \$37.206m in the period November 2008 to January 2009;
 - (ii) reported NPAT of \$19.351m in July 2009;
- (e) admits that as at 7 September 2009 its NPAT forecast for the period November 2009 to January 2010 was \$42.785m;
- (f) admits that the CFO report for the period ended 31 July 2009 provided to the board for its meeting on 24 August 2009 stated (at page 6) under the heading 'Underlying Second Half Forecast':
- *"Full year forecast now updated and reflects forecasted January 2010 promotional activity.*
 - *The declines in consumer discretionary spending and the performance of the Herron business combined with manufacturing volume shortfalls is expected to adversely affect the full year result. Above forecast performances from Wholesale, Generics, Ethical's [sic] and Orphan are the current mitigates. Adequate mitigation will require a three month generics promotional program in late 2009 and/or the launch of a major generic molecule, Clopidogrel, currently subject to an Arrow patent challenge due for hearing in August 2009.*
 - *Run rate for second half is broadly in line with same period prior year."*
- (g) admits that it had achieved sales of \$826.4m in the period November 2008 to January 2009;
- (h) admits that in its budget for the 2009/10 financial year (at page 7) its budget for net sales:
- (i) in the first half of FY2010 was \$1.470b;
 - (ii) in the second half of FY2010 was \$1.739b;
- (i) admits that on 14 September 2009 in its Interim report for the half year to 31 July 2009 (at page 3) it reported sales revenue of \$1.517b in the first half of FY2010;

- (j) says that the allegation in paragraph 9.1 that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it achieved sales volumes in its Healthcare Division and its Pharmaceuticals Division that were both 'significantly higher' than its average monthly sales volumes over the financial year to date and 'significantly higher' than its sales volumes achieved over the corresponding period in FY2009; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (k) otherwise denies each allegation in paragraph 9.1.

9.2 It:

- (a) admits that Appendix Four (at page 18) to its FY2010 Budget paper dated 20 February 2009 set out the following table under the heading 'New Products':

		Board FINAL budget	
Generic/Branded	PBS Listing / Launch	Sig 09/10 sales	Sig 09/10 GP
Cyprot/estradiol	1/05/2009	\$1,215,000	\$729,000
Meloxicam Capsules	1/02/2009	\$1,600,000	\$80,000
Metformin SR	1/05/2009	\$570,000	\$28,500
Finasteride	1/05/2009	\$1,152,000	\$691,200
Cabergoline	1/08/2009	\$670,000	\$402,000
Morphine Sulfate CR	1/08/2009	\$1,770,000	\$885,000
Ropinirole	1/04/2009	\$183,333	\$55,000
Sodium Valproate	1/12/2009	\$726,667	\$290,667
Escitaloplam – Risk Litigation	1/08/2009	\$0	\$0
Topiramate tabs/caps	1/12/2009	\$350,000	\$105,000
Venlafaxine	1/08/2009	\$10,500,000	\$4,200,000
Clopidogrel – Risk Litigation	1/12/2009	\$0	\$0
New products total		\$18,737,000	\$7,466,367

- (b) admits that on 3 June 2009 Sigma Pharmaceuticals (Australia) Pty Ltd ACN 004 118 594 was restrained by orders of the Federal Court of Australia from exploiting in Australia products listed as Exelexa-XR without the licence of Wyeth or Wyeth Australia Pty Ltd;
- (c) refers to paragraph 9.1(f) above in relation to the CFO report for the period ended 31 July 2009;

- (d) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
 - (i) it launched and was able to recognise 'significant profits' from sales of new products in Generics; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (e) otherwise denies each allegation in paragraph 9.2.

9.3 It:

- (a) admits that in its Full Year Financial Report for the financial year ended 31 January 2010 it stated (at page 38) under the heading 'Revenue Recognition':

"...some sales are recognised on a Bill and Hold basis. Bill and Hold sales relate to circumstances whereby the delivery of the goods is delayed at the customer's request but the buyer takes title and accepts billing. Revenue is recognised on Bill and Hold sales provided: it is probable that delivery will be made, the inventory item is on hand and ready for delivery at the time the sale is recognised, the buyer specifically acknowledges the deferred delivery instructions and the agreed payment terms apply.";

- (b) admits that:

- (i) on 25 August 2009 Jordan Lomax of PricewaterhouseCoopers (**PwC**) sent an email to Julian Coppini of Sigma which stated (in part):

"Keen to feedback and get your thoughts on accounting implications of the cut off sample for Orphan and Pharmaceuticals. In terms of the accounting debate we understand that most of our sampled API/Symbion sales were despatched pre 31 July, however delivered post half year and want to get your view on revenue recognition.

...

We have not landed on a view on this yet but would be keen to work through your thoughts and introduce any other relevant factors we may need to consider (e.g. agreements etc.)"

- (ii) on 26 August 2009 Julian Coppini responded to the email referred to in paragraph 9.3(b)(i) above as follows:

"My view as follows:

The terms of the invoice are very clear "the risk in the goods purchased shall, unless otherwise agreed in writing, pass to the Customer upon dispatch of the goods". End of story - as the goods were all dispatched."

- (c) admits that in its draft Report to the Risk Management & Audit Committee dated 3 September 2009 (**PwC Draft Report**) and Report to the Risk Management &

Audit Committee dated 9 September 2009 (**PwC Final Report**), PwC stated (at page 6):

"Due to the significant sales close to half year and year end, we highlighted to management that cut-off would be an area of focus. As part of our review, we identified sales that were in transit from Sigma to the customer at year end (approximately \$2.5 million of EBIT contribution at the half year). On review of the contract documentation, we noted that it was not clear when ownership of the goods transferred. We recommended to management that they clarify this matter in future contracts.";

- (d) denies that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010 it was able to recognise in its FY2010 accounts revenues from sales:
 - (i) made on a 'bill and hold' basis; and/ or
 - (ii) of goods that were despatched by it in the second half of FY2010 but not received by the customer until the next reporting period; and
- (e) otherwise denies each allegation in paragraph 9.3.

9.4 It:

- (a) denies that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010 it avoided material increases in its discount rate based on WACC; and
- (b) otherwise denies each allegation in paragraph 9.4.

9.5 It:

- (a) admits that in June 2009 it made a staff announcement which stated (in part):

"...Sigma plans to consolidate our manufacturing facilities and commence a staged closure of the Tennyson site over the next 2 years.

Production at the Baulkham Hills facility will reduce slightly over the next 2 years...

The Dandenong site will be expanded to include additional packing suites, upgraded manufacturing suites, and a larger packaging warehouse. ...

...

Impacted employees at the Tennyson and Baulkham Hills facilities will have the opportunity to apply for transfers to other positions or sites within Sigma to which they will have priority, subject to appropriate skills and experience. ..."

- (b) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
 - (i) it avoided having to recognise or make provision for 'significant' redundancy expenses; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (c) otherwise denies each allegation in paragraph 9.5.

9.6 It:

- (a) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
 - (i) it avoided having to recognise 'significant' expenses in consequence of closing out interest-rate hedge contracts; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (b) otherwise denies each allegation in paragraph 9.6.

9.7 It:

- (a) admits that as at 7 September 2009 it held two non-exclusive licences from Arrow Group ApS to distribute, market, promote and sell certain products in 16 foreign territories (**Arrow Export Licences**);
- (b) admits that as at 7 September 2009, the Arrow Export Licences had a carrying value of \$8.9m;
- (c) admits that the carrying value of the Arrow Export Licences was written off in full in FY2010;
- (d) admits that in the PwC Draft Report and the PwC Final Report, PwC stated (at page 4):

"Management's high level analysis does not indicate an impairment of the licences and therefore no detailed valuation exercise was performed. We highlight there remains a risk that the carrying value of the licences may need to be impaired at January 2010 if the sales and registrations do not occur in accordance with the revised plan."

- (e) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
 - (i) it avoided having to recognise 'an impairment' of the Arrow Export Licences; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (f) otherwise denies each allegation in paragraph 9.7.

9.8 It:

- (a) admits that in its Full Year Financial Report for the financial year ended 31 January 2010 it stated (at pages 4 and 5):

"...the synergies expected from the merger of Sigma Pharmaceuticals Limited and Sigma Company Limited in 2005 have not been achieved.

...

Ultimately the synergies expected from the merger of Sigma Pharmaceuticals Limited (formerly Arrow) and Sigma Company Limited in 2005 have not been achieved, and in light of the level of increased competition and discounting which we have seen in the market Sigma has revised the Pharmaceuticals cash flow forecasts.

...

Ultimately the synergies expected from the merger of Sigma Pharmaceuticals Limited and Sigma Company Limited in 2005 have not been achieved, and in light of the level of increased competition and discounting which we have seen in the market Sigma has revised the Healthcare cash flow forecasts.";

- (b) admits that a paper entitled 'Accounting Position Paper – Operating Segments and CGU's April 2009' provided to the Risk Management and Audit Committee for its meeting on 22 June 2009 stated:

"Arrow

The goodwill arising upon acquisition of Arrow is derived from:

- a) The potential pipeline of Arrow generic drugs – These drugs are produced within our manufacturing operations and sold to both our Healthcare business.*
- b) The Arrow generics increases – Allows Sigma's offering to Pharmacies as a one-stop shop with Wholesale, Generics and OTC products and sales are driven through our Embrace program which offers unique discounts.*
- c) The integration of the Arrow back-office – Has provided substantial synergies with administration as well as sales.*

...

We have reviewed the synergies noted above and believe they still exist."

- (c) admits that an earlier draft of the paper entitled 'Accounting Position Paper – Operating Segments and CGU's April 2009' stated that:

"We could not reliably estimate the cross synergies that would be attributable to the wholesaling business without a whole of business model.";

- (d) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it achieved 'certain synergies associated with its Arrow business'; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (e) otherwise denies the allegations in paragraph 9.8.

9.9 It:

- (a) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it was able to defer until FY2011 'recognition of rebates offered to customers as incentives to trade with Sigma, whilst recognising in FY2010 the revenue from resulting sales to those customers'; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (b) otherwise denies each allegation in paragraph 9.9.

9.10 It:

- (a) admits that in its Group Strategic Plan (2008-2013) (at page 4) it identified 'Price reductions due to PBS reform' under 'Challenges/ Risks';
- (b) admits that in its Audit plan for the year ending 31 January 2010 dated 15 June 2009, PwC stated (at page 7) that the carrying value of goodwill and other intangibles was a significant area of focus for a number of reasons, one of which was stated to be:

"Impact of low cost generic suppliers, PBS pricing, and customer buying strength on future cash flows";

- (c) admits that in the Strategy Day discussion materials prepared by Lazard Pty Ltd in August 2009 (**Lazard Strategy Day materials**) (at page 7) under 'Threats for Sigma' Lazard identified (among other things):

*"Generics – increasing competition, government price downs, 19% EBIT currently
...
Continued price / regulation squeeze by Government;"*

- (d) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it avoided 'significant negative impact on margins from regulatory reforms to the Pharmaceuticals Benefit Scheme'; or
- (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (e) otherwise denies each allegation in paragraph 9.10.

9.11 It:

- (a) admits that in the Lazard Strategy Day materials (at page 7) under 'Threats for Sigma' Lazard identified (among other things)

"Generics – increasing competition, government price downs, 19% EBIT currently;"

- (b) admits that the minutes of the board meeting held on 22 June 2009 record that:

"Mr de Alwis ... noted that ... the results ... were impacted by a number of factors, such as increased competition in the generic market, the impact of Effexor being restrained from going to market this year and manufacturing not delivering the expected efficiencies to date."

- (c) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it 'recovered market share lost during the first half of FY2010'; or
- (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (d) otherwise denies each allegation in paragraph 9.11.

9.12 It:

- (a) admits that in the PwC Draft Report and the PwC Final Report, PwC said (at page 3) that stock to a value of \$8.6m was 'at risk' and stated:

"In addition, we highlight those items which are 'at risk' and may require write-off in the second half of the year if specific plans are not successful."

- (b) admits that the minutes of the meeting of the Risk Management and Audit Committee meeting held on 3 September 2009 record that:

"Ms Waldron walked the Committee through the key areas of Inventory risk and noted that if management action plans failed to eventuate then there could be additional proposed adjustments at year end."

- (c) says that the allegation that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT Forecast unless in the period before 31 January 2010:
- (i) it avoided having to recognise or make provision for a write down of inventory to net realisable value; or
 - (ii) one or more of the other contingencies specified in paragraph 9 occurred – is vague and embarrassing, and it denies that allegation; and
- (d) otherwise denies each allegation in paragraph 9.12.

9.13 It:

- (a) refers to paragraphs 9.1 to 9.12 above;
- (b) denies that as at 7 September 2009 it was unlikely to achieve its 2010 NPAT forecast unless one or more of the contingencies alleged in paragraphs 9.1 to 9.12 of the Amended Statement of Claim occurred; and
- (c) otherwise denies each allegation in paragraph 9.

10. It:

- (a) refers to paragraphs 9.1 to 9.12 above;
- (b) says that as at 7 September 2009 divisional forecasts were set after consultation with the divisional general managers but otherwise does not admit that they were set without approval of the divisional general managers;
- (c) admits that sales of Herron products were behind forecast in June 2009, July 2009 and August 2009;

- (d) denies that as at 7 September 2009 the information referred to in paragraph 9 of the Amended Statement of Claim or the particulars to paragraph 10 of the Amended Statement of Claim was relevant to the continuing accuracy of its public statements concerning its FY2010 NPAT forecast;
 - (e) refers to paragraphs 7.1(c) and (d) above;
 - (f) otherwise denies each allegation in paragraph 10.
11. It:
- (a) refers to paragraphs 7.1(c) and (d) above; and
 - (b) otherwise denies each allegation in paragraph 11.
12. It:
- (a) admits that on 7 September 2009 it announced a '1 for 3' fully underwritten accelerated renounceable entitlement offer (**AREO**) to raise gross proceeds of \$297m;
 - (b) admits that it stated that the net proceeds from the AREO would be used to fund the acquisition of an established pharmaceutical brand portfolio and manufacturing facility from Bristol-Myers Squibb and to reduce its gearing;
 - (c) otherwise denies each allegation in paragraph 12.
13. It:
- (a) admits that as at 7 September 2009 it had carried out impairment reviews of its goodwill and other intangible assets since 1 February 2009;
 - (b) admits that in its impairment review in September 2009 it made the assumptions set out in paragraph 13.2;
 - (c) denies that it used (deliberately or otherwise) incorrect, inaccurate or exaggerated integers for its calculation of the value of working capital for the Healthcare Division;
 - (d) denies that it used an incorrect value for goodwill for the Healthcare Division;
 - (e) admits that in an email dated 22 August 2009 from Mr de Alwis he said:

"The increase in sales is despite opportunities to grow sales at marginal profit increase being declined.";

- (f) admits that in an email dated 24 August 2009 from Mr de Alwis he said:

"The numbers presented here tie directly into our management accounts – so it paints the same picture – i.e. Wholesale growth and Pharmaceutical decline";

- (g) says that the allegation in paragraph 13.4(a) is vague and embarrassing, and it denies that allegation;
- (h) denies the allegation in paragraph 13.4(b);
- (i) denies the allegations in paragraph 13.4(c);
- (j) otherwise denies each allegation in paragraph 13.4;
- (k) admits that in the PwC Draft Report and the PwC Final Report , PwC noted (at page 1) that:

"Management has continued to refine and improve their value in use discounted cash flow models during the year. We have reviewed the model and underlying assumptions and observe the following:

- *Sigma's discount rate of 10.25% pre-tax WACC is below the acceptable range and outside of other observable market participants as summarised in the table opposite.*
- *Growth rated of 6% per annum have been assumed across each segment of the business for the 5 year period through to January 2014.*

This is above the recent growth rates for the business, although we note the Wholesale division has achieved over 10% growth in the half year.

- *A long term growth rate of 3.3% which is above the generally accepted long tern range of 2.5% - 3%. We understand management is confident that the long term growth of the health sector will be above the general market.*
- *An assumes improvement in terms of trade with Gance from 2011.*

Benchmark analysis	31 July 2009			
	Sigma	Sigma brokers	PwC Estimate	Overall Healthcare
Pre-tax WACC (%)	10.25	12.0 – 15.3	11.4 – 12.7	12.7

- (l) otherwise denies each allegation in paragraph 13.

14. It:

- (a) admits that it had the information in the PwC Draft Report by not later than 7 September 2009;
- (b) otherwise denies each allegation in paragraph 14.

15. It denies the allegations in paragraph 15.

16. It denies the allegations in paragraph 16.

17.1 It:

- (a) denies that between 7 September 2009 and 31 January 2010 it was not achieving new sales in sufficient volumes to make achievement of its FY2010 NPAT forecast reasonably foreseeable;
- (b) denies that there was a shortfall against forecast sales each month between 7 September 2009 and 31 January 2010;
- (c) denies that there was a shortfall against forecast NPAT each month between 7 September 2009 and 31 January 2010;
- (d) admits that between 7 September 2009 and 31 January 2010 it reviewed its NPAT forecast each month and maintained its underlying group forecast NPAT for FY2010;
- (e) otherwise denies each allegation in paragraph 17.1.

17.2 It:

- (a) admits that in September 2009 it was aware that clopidogrel would not be launched prior to 31 January 2010;
- (b) admits that in September 2009 its forecast workings for the second half of FY2010 included '*Assumed Pantoprazole GP \$4,500*' in the '*January 2010 Generics GP target*';
- (c) otherwise denies each allegation in paragraph 17.2.

17.3 It denies the allegations in paragraph 17.3.

17.4 It admits the allegations in paragraph 17.4.

17.5 It:

- (a) admits that it identified redundancy expenses which were provided for in the sum of \$5.177m in FY2010;
- (b) otherwise denies each allegation in paragraph 17.5.

17.6 It denies the allegations in paragraph 17.6.

17.7 It denies the allegations in paragraph 17.7.

17.8 It refers to paragraph 9.8(a) above and otherwise denies the allegation in paragraph 17.8.

17.9 It denies the allegations in paragraph 17.9.

17.10 It:

- (a) admits that in its Full Year Results Report for the Financial Year ended 31 January 2010 (at page 4) it stated:

"The Group's reported revenue increased by \$139,143,000 to \$3,220,430,000 against a back ground of absorbing PBS price reforms and highly competitive generic pricing."

- (b) otherwise denies each allegation in paragraph 17.10.

17.11 It:

- (a) does not admit that it lost market share during the first half of FY2010;
- (b) otherwise denies each allegation in paragraph 17.11.

17.12 It:

- (a) admits that in its report to the Risk Management & Audit Committee December update for year ending 31 January 2010 dated 4 December 2009, PwC stated (at page 2):

"Our analysis at the half year highlighted \$1.9m of inventory requiring a provision based on known clearance rates. Our review identified a further \$8.6m of inventory "at risk" to the year end result which management responded as follows:

- *Inventory of \$1.5m with 13 – 24 months short dated would be promoted before reaching terminal expiry (0 – 6 months)*
- *Herron Complete stock in quarantine of \$0.8m to be returned to the supplier at full cost if unable to market or subject to write off*
- *Xndo inventory of \$4.1m would be subject to sustained promotion activity or returned to supplier at full cost or written off*
- *Excess stock (1-10 years) based on current demand would be subject to provision should clearance rates not improve*
- *Short dated Nicotine products of \$0.8m which were re-aged for a further 12 months under TGA approval. We understand from management that this has been substantially cleared.*

Our year end audit procedures will be risk-based, focussing on products with significant excess stock (compared with current and forecast demand), short dated stock, low margin products, and management schemes to clear stock as discussed at the half year."

- (b) admits that inventory in the amount of \$34.595m was written down at FY2010;
- (c) otherwise denies each allegation in paragraph 17.12.

17.13 It:

- (a) admits that sales of its Herron products were below budget in the months of September, October, November and December 2009;
- (b) denies that sales of its Herron products were below budget in January 2010;
- (c) denies that sales of its Herron products were below YTD forecast as at January 2010;
- (d) otherwise denies each allegation in paragraph 17.13.

18. It denies the allegations in paragraph 18.

19. It denies the allegations in paragraph 19.

20.1 It denies the allegations in paragraph 20.1.

20.2 It:

- (a) admits that it did not achieve its monthly NPAT forecasts in the period September to December 2009;
- (b) denies that it did not achieve its monthly NPAT forecast for January 2010;
- (c) otherwise denies each allegation in paragraph 20.2.

20.3 It:

- (a) denies that in September 2009 its WACC rate for impairment testing ought reasonably to have been higher than 10.25%;
- (b) admits that in October 2009 it reviewed its model and tested for impairment using a WACC rate of 11.13%;
- (c) admits that in December 2009 it reviewed its model and tested for impairment using a WACC rate of 11.91%;
- (d) admits that during its FY2010 audit it reviewed its model and tested for impairment as at 31 January 2010 using
 - (i) a WACC rate of 12.1% for Healthcare;
 - (ii) a WACC rate of 11.77% for Pharmaceuticals;
 - (iii) a WACC rate of 12.1% for Orphan;
- (e) otherwise denies each allegation in paragraph 20.3.

- 20.4 It denies the allegations in paragraph 20.4.
21. It denies the allegations in paragraph 21.
22. It:
- (a) admits that compliance with the impairment accounting standard AASB136 required it to recognise an impairment of goodwill as at 31 January 2010 (which it did);
 - (b) denies that prior to 31 January 2010 there was a material risk that compliance with the impairment accounting standard AASB136 required it to recognise an impairment of goodwill as at 31 January 2010.
23. It denies the allegations in paragraph 23.
24. It denies the allegations in paragraph 24.
25. It denies the allegations in paragraph 25.
26. It denies the allegations in paragraph 26.
27. It denies the allegations in paragraph 27.
28. It denies the allegations in paragraph 28.
29. It denies the allegations in paragraph 29.
30. It denies the allegations in paragraph 30.
31. It denies the allegations in paragraph 31.
32. It denies the allegations in paragraph 32.
33. It denies the allegations in paragraph 33.
34. It denies the allegations in paragraph 34.
35. It denies the allegations in paragraph 35.
36. It denies the allegations in paragraph 36.
37. It denies the allegations in paragraph 37.

38. It denies the allegations in paragraph 38.

39. It denies the allegations in paragraph 39.

40. It denies the allegations in paragraph 40.

41. It admits that on 31 March 2010 it published its Full Year Financial Report for the financial year ended 31 January 2010, which contained the following:

41.1 at pages 5, 59 and 60:

(a) (page 5 and 59) under the headings 'Pharmaceuticals Division: Financial Results (Reported)' and '*Pharmaceuticals CGU*' respectively:

"The period to 31 January 2010 saw continued aggressive discounting within the Generics market in which we compete leading to lower future cash flow forecasts for this business."

(b) (pages 5 and 60) under the headings 'Healthcare Division: Financial Results (Reported)' and 'Healthcare' respectively:

"The effects of these conditions around competition and associated aggressive discounting were not fully realised until the completion of our January 2010 promotional activity."

41.2 at pages 5 and 60 under the headings 'Healthcare Division: Financial Results (Reported)' and 'Healthcare' respectively:

"Ultimately this has resulted in a loss of market share for the Sigma Group."

41.3 at pages 5 and 59 under the headings 'Pharmaceuticals Division: Financial Results (Reported)' and '*Pharmaceuticals CGU*' respectively:

"The period saw additional investment within the Consumer division in order to raise the level of brand awareness within our direct Grocery channel."

41.4 at pages 4, 5, 8, 59 and 60:

(a) (pages 4 and 8) under the headings '*Sales revenue and earnings*' and 'Review and Results of Operations' respectively:

"Additionally, the synergies expected from the merger of Sigma Pharmaceuticals Limited and Sigma Company Limited in 2005 have not been achieved."

- (b) (pages 5, 59 and 60) under the heading 'Pharmaceuticals Division: Financial Results (Reported)', 'Healthcare Division: Financial Results (Reported)', '*Pharmaceuticals CGU*' and 'Healthcare' respectively:

"Ultimately the synergies expected from the merger of Sigma Pharmaceuticals Limited (formerly Arrow) and Sigma Company Limited in 2005 have not been achieved, ..."

- 41.5 at pages 4 and 8 under the headings '*Sales revenue and earnings*' and 'Review and Results of Operations' respectively:

"The carrying value of the group's goodwill was reassessed in light of a progressive deterioration in competitive conditions and a changing regulatory environment.... The change in competitive conditions and the industry impact of new regulations have directly and negatively impacted the short and long term growth rates for our healthcare and pharmaceutical businesses."

- 41.6 at pages 4, 5, 8, 59 and 60:

- (a) (pages 4 and 8) under the headings '*Sales revenue and earnings*' and 'Review and Results of Operations' respectively:

"The future cash flow forecasts were revised and an impairment was taken against goodwill."

- (b) (page 5 and 59) under the headings 'Pharmaceuticals Division: Financial Results (Reported)' and '*Pharmaceuticals CGU*' respectively:

"... and in light of the level of increased competition and discounting which we have seen in the market, Sigma has revised the Pharmaceutical's cash flow forecasts."

- (c) (pages 5 and 60) under the headings 'Healthcare Division: Financial Results (Reported)' and 'Healthcare' respectively:

"... and in light of the level of increased competition and discounting which we have seen in the market, Sigma has revised the Healthcare cash flow forecasts."

- 41.7 at pages 54 and 64:

- (a) (page 64) in note 18 Provisions:

"Redundancy provisions 5,177 "

- (b) (page 54) in note 11 Inventories:

"Provision for obsolescence (28,099) "

- 41.8 at pages 4, 8 and 59:

"Changes in the risk profile of the Company have contributed to an increase in the Company's weighted average cost of capital. "

41.9 at pages 4, 5, 8 and 30:

- (a) (page 4) under the heading '*Sales revenue and earnings*':

"The carrying value of the group's goodwill was reassessed in light of a progressive deterioration in competitive conditions and a changing regulatory environment. "

- (b) (pages 4 and 8) under the headings '*Sales revenue and earnings*' and '*Review and Results of Operations*' respectively:

"These factors combined to result in a material adjustment to the carrying value of goodwill of \$424,230,000 (note 14 has further details around the goodwill impairment)."

- (c) (page 30) under '*Statement of comprehensive income*':

"Impairment of goodwill (424,230) "

- (d) (page 5) under the heading '*Pharmaceuticals Division: Financial Results (Reported)*':

"Goodwill impairment recognised in relation to the Pharmaceuticals Division was \$184.4m."

- (e) (page 5) under the heading '*Healthcare Division: Financial Results (Reported)*':

"Goodwill impairment recognised in relation to the Healthcare Division was \$239.8m."

41.10 at pages 2, 4 and 8:

- (a) (page 2) in the table headed '*Group Results*':

...
Net loss after tax attributable to members	down	585.5%	to	(389,042)

- (b) (page 4) under the heading '*Group Financial Results – Reported*':

Group Results (on a reported basis)	31 January 2010 \$000	31 January 2009 \$000	Change %
...
(Loss)/Net profit after tax	(389,042)	80,124	Down 585.5%
...

- (c) (page 8):

"The Group reported a net loss after tax for the financial year of (\$389,042,000) compared with a profit of \$80,124,000 for prior year. "

41.11 otherwise denies each allegation in paragraph 41.

42. It:

- (a) admits that the trading price for its shares traded on the ASX closed:
 - (i) on 24 February 2010 at \$0.900;
 - (ii) on 31 March 2010 at \$0.465;
- (b) otherwise denies the allegations in paragraph 42.

43. It:

- (a) denies that its shares traded at inflated prices;
- (b) otherwise does not admit the allegations in paragraph 43.

44. It:

- (a) refers to paragraph 39 above;
- (b) otherwise does not admit the allegations in paragraph 44.

45. It denies the allegations in paragraph 45.

46. It denies the allegations in paragraph 46.

Date: 1 July 2011



Ross Freeman
MINTER ELLISON
Solicitors for the respondent

This pleading was prepared by Minter Ellison and settled by C. Scerri Q.C. and P.D. Crutchfield SC.

EARGLOW PTY LIMITED ACN 055 664 769

Applicant

**SIGMA PHARMACEUTICALS LIMITED
ACN 088 417 403**

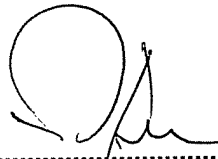
Respondent

CERTIFICATE OF LAWYER

I, **ROSS FREEMAN**, certify to the Court that, in relation to the pleading dated 1 July 2011 filed on behalf of the respondent, the factual and legal material available to me at present provides a proper basis for:

- (a) each allegation in the pleading; and
- (b) each denial in the pleading; and
- (c) each non-admission in the pleading.

Date: 1 July 2011



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