The TEP Exchange

# TEP Exchange Group PLC

## Report and Financial Statements

for the year ended 31 December 2011

# Contents and company details



**Directors**

| | |
|---|---|
| G Kynoch | *Chairman (Non-Executive)* |
| A Weitz | *Non-Executive* |
| M Kraus | *Non-Executive* |
| D Roxburgh | *Managing Director (Executive)* |

**Company secretary, registered office and principal place of business**

J Murphy
12 Grosvenor Court
Foregate Street
Chester
Cheshire CH1 1HG

**Company registered number and legal form**

03877125 Public limited company
incorporated in England

**Independent auditors**

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
101 Barbirolli Square
Lower Mosley Street
Manchester M2 3PW

**Registrars**

Capita Registrars Limited
Northern House
Woodsome Park
Fenay Bridge
Huddersfield HD8 0GA

**Nominated adviser and broker**

Merchant Securities Limited
51-55 Gresham Street
London EC2V 7EL

**Bankers**

Bank of Scotland plc
3rd Floor
150 Fountainbridge
Edinburgh EH3 9PE

# Chairman's statement

I am duly reporting the results for the company and subsidiaries (together "the group") for the year ended 31 December 2011. Revenue for the year totalled £1,044,472 (2010: £164,776) resulting in a profit from operations of £687,734 (2010: loss £56,797). The profit before and after taxation was £666,082 compared to the loss before and after taxation of £86,458 in 2010. The basic earnings per share was 0.14 pence (2010: loss per share 0.02 pence).

Revenue increased significantly in 2011 compared with 2010 due to the receipt of fees from licensing of the electronic platform and all technology to SL Investment Management Limited, ("SL"), a 48 per cent. shareholder in the company. The licensing arrangements with SL were set out in the company's announcement of the contract on 12 November 2010. In summary the company has licensed its electronic platform and all technology to SL and in consideration will receive a quarterly fee of £20,000 and in addition, SL has been granted exclusive rights to develop and modify the electronic platform for a quarterly fee of £230,000 ("the Licence Agreement"). The Licence Agreement is for a period of ten years; however, SL may terminate the agreement on 30 April of each year. On 2 April 2012 the company announced that SL had informed the company that the income generated during the 12 month period ending 30 April 2012 was unlikely to be £250,000 or more and, therefore, it may terminate the Licence Agreement in accordance with its terms. The company agreed with SL that it would provide a 61 day extension to the termination notice period to allow SL to further assess the benefits of the Licence Agreement. A further announcement by the company was issued on 31 May 2012 setting out that the agreement can now be terminated on 30 August 2012 by SL giving 30 day's prior written notice to the company.

As a result of these arrangements the directors consider it appropriate to prepare the financial statements on a going concern basis.

The market demand for traded endowment policies still remains extremely depressed but the company continues to work closely with market makers in anticipation of increasing demand for policies. In the meantime, the Directors are continuing to maintain strong controls over the company's cost base and are also exploring additional opportunities to generate income.

Your Board is not proposing a dividend for the year under review.

**G Kynoch**
Chairman

19 June 2012

# Corporate governance statement

TEP Exchange Group PLC is highly committed to high standards of corporate governance and the company is supportive of the provisions set out in Section 1 of the Combined Code on Corporate Governance laid out in the Financial Services Authority Listing Rules.

Companies on the Alternative Investment Market of the London Stock Exchange are not required to comply with the Combined Code.

**The Board**

The Board of TEP Exchange Group PLC consisted of one Executive Director and three Non-Executive Directors. The composition of the Board ensures no one individual or group of persons dominates the decision making process.

The Board is responsible to the shareholders for setting the direction of the company through the establishment of strategic objectives and key policies. The Board meets on a regular basis and considers the strategic direction, approves major capital expenditure, and any other matters having a material effect on the company. Presentations are made to the Board on the activities and both the Executive and Non-Executive Directors undertake visits to operations.

All Directors have access to management, including the Company Secretary, and to such information as is needed to carry out their duties and responsibilities fully and effectively.

Furthermore, all Directors are entitled to seek independent professional advice concerning the affairs of the company at its expense. All Directors are subject to election by shareholders at the first annual general meeting following their appointment. In addition, Directors will retire and stand for re-election at least once every three years in accordance with the company's Articles of Association.

The interests of the Directors in the shares and share options of the company serve to align their interests with the shareholders generally and the company does not consider this to have an adverse effect on their independence.

**Nominations Committee**

The Directors do not consider that, given the size of the Board, it is appropriate to have a Nominations Committee. The appropriateness of such a committee will, however, be kept under regular review by the company.

**Internal controls**

The Directors are responsible for the group's systems of internal control and reviewing its effectiveness. Any such system is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable assurance against material misstatement or loss.

Internal controls and business risks were monitored in the course of 2011 through regular Board meetings. A formal review of internal controls is scheduled for 2012. The key business risks monitored by the Board are set out in the directors' report.

# Corporate governance statement

continued

### Communication with shareholders

The Board recognises it is accountable to shareholders for the performance and activities of the group.

The forthcoming Annual General Meeting of the company will provide an opportunity for the Chairman to present to the shareholders a report on current operations and developments and enable the shareholders to express their views about the company's business.

### Remuneration Committee

The Directors do not consider that, given the size of the group, it is appropriate to have a Remuneration Committee. The appropriateness of such a committee will, however, be kept under regular review by the Board. At present, remuneration of Directors and senior management is determined at the Board meetings.

### Audit Committee

The Audit Committee, comprising solely of independent Non-Executive Directors, meets at least twice a year and considers the company's financial reporting (including accounting policies) and internal financial controls.

Meetings are normally attended, by invitation, by a representative of the auditors.

The audit committee presently comprises G Kynoch and M Kraus.

# Report of the Directors

for the year ended 31 December 2011

The Directors present their report together with the audited consolidated financial statements of the group and company for the year ended 31 December 2011.

**Principal activities and business review**

The principal activity of the company and its subsidiary undertakings during the year was the licensing of its proprietary electronic platform and the provision of on-line advertising services for with profit endowment policies utilising its platform.

A review of the business and future developments is given in the Chairman's statement on page 2.

The Directors have determined that the following key performance indicators are the most effective measures of progress towards achieving the group's objectives.

| | **2011** | **2010** |
|---|---|---|
| | **£** | **£** |
| Turnover | 1,044,472 | 164,776 |
| Profit/(loss) from operations | 687,734 | (56,797) |

The key business risks continue to be the depressed market for traded endowment policies, and liquidity risk, although the liquidity risk significantly reduced in 2011 due to the commencement of the licence agreement during 2010.

Further details of the principal risks and financial instruments are disclosed in note 16. Details of the going concern basis of preparation are given below.

**Results and dividends**

The consolidated statement of comprehensive income is on page 13 and shows the result for the year of £666,082 profit (2010: £86,458 loss). The Directors do not recommend the payment of a dividend (2010: £nil).

During the year the company undertook a subscription for new ordinary shares and warrants by the company's largest existing shareholder and certain other connected companies.

**Directors and their interests**

The Directors who served in office during the year and up to the date of signing the financial statements and their interests in the company's shares are as follows:

**Ordinary shares of 0.001p (2010: 0.01p) each held at:**

| | **31 December 2011** | | **31 December 2010** | |
|---|---|---|---|---|
| | **Number** | **%** | **Number** | **%** |
| M Kraus | 22,034,698* | 2.59 | 22,034,698* | 5.51 |
| A Weitz | 10,000,000** | 1.18 | 10,000,000** | 2.50 |
| G Kynoch | 468,241 | 0.06 | 468,241 | 0.12 |
| D Roxburgh | – | – | – | – |

*Of these shares, M Kraus holds 3,125,000 ordinary shares. The remaining shares are held by the M Kraus Family Foundation pursuant to the terms of which M Kraus and members of his family are potential beneficiaries.

**PINVEX Limited which holds 10,000,000 ordinary shares in the company, and A Weitz has a 50% shareholding in PINVEX Limited.

# Report of the Directors

continued

**Directors and their interests** continued

**Deferred shares of 0.001p (2010: 0.99p) each held at:**

| | 31 December 2011 | | 31 December 2010 | |
|---|---|---|---|---|
| | **Number** | **%** | **Number** | **%** |
| M Kraus | 22,012,663,302 | 9.74 | 22,034,698 | 9.81 |
| A Weitz | 90,000,000 | 0.04 | – | – |
| G Kynoch | 325,139,499 | 0.14 | 324,167 | 0.14 |
| D Roxburgh | – | – | – | – |

D Roxburgh retires by rotation in accordance with the Articles of Association. The terms of the Directors' service contracts or terms of engagement are set out below. M Kraus, G Kynoch and A Weitz consider themselves to be independent Non-Executive Directors. M Kraus has been nominated as Senior Non-Executive Director.

**Share options**

The Directors' interests in share options are set out below:

| Interest held at: | 31 December 2011 | 31 December 2010 |
|---|---|---|
| M Kraus | – | 287,273 |
| A Weitz | – | 295,545 |
| G Kynoch | – | – |
| D Roxburgh | – | – |

Share options were granted to M Kraus and A Weitz on 16 February 2001 pursuant to the rules of the Enterprise Management Incentive Scheme ("the EMI Rules"). The subscription price payable under the terms of the share options granted to M Kraus and A Weitz were 10 pence per share. The terms of the share options granted under the EMI Rules permit exercise after the expiry of three years from the date of grant and before ten years after date of grant. There are no other restrictions preventing exercise under the terms of the share options or EMI Rules.

On 14 March 2007, the company issued warrants to PINVEX Limited, a company in which A Weitz has a 50% shareholding, to subscribe for up to 10,000,000 ordinary shares in cash at 0.2p per share. The warrant confers on the warrantholder, PINVEX Limited, the right to subscribe in cash for ordinary shares to be issued to the warrantholder or such person as the warrantholder may direct. Ordinary shares issued on the exercise of warrants will qualify for all dividends and distribution declared, made or paid after their date of issue.

The warrants issued to PINVEX Limited can only be exercised in the event that the income of the company arising from PINVEX Limited related transactions in each of any two consecutive financial periods of the company, beginning on 1 January 2007 and ending on 31 December 2011 shall exceed £100,000. The warrants may be exercised in whole or in part or in parts. Any warrants not exercised prior to 30 June 2012 will lapse on that date.

# Report of the Directors

continued

**Directors' service contracts**

On 29 August 2001, the company entered into a letter of appointment with Drumduan Associates, to provide the services of George Kynoch to act as a non-executive director and chairman of the company. The appointment is terminable by either party giving to the other not less than six months' written notice. In return for the provision of the services of the company will pay Drumduan Associates an annual fee. This amounted to £9,000 in 2011 (2010: £25,000). In the event that Mr Kynoch is required to provide his services in excess of three days per calendar month, the company shall pay an additional fee of £800 per eight hours for such excess time. The letter of appointment contains a customary confidentiality clause. Upon termination, no benefits (other than those accruing during the notice period) are due to Drumduan Associates and Mr Kynoch shall resign as a director.

Mr Weitz has a letter of engagement dated 15 February 2007. The appointment is terminable by either party giving not less than three months' written notice. Mr Weitz will receive a monthly fee of £300 (exclusive of VAT).

Mr Kraus has a letter of engagement dated 15 February 2007. The appointment is terminable by either party giving not less than three months' written notice. Mr Kraus will receive a monthly fee of £300 (exclusive of VAT) during the period of his appointment.

Save as disclosed above, there are no existing or proposed service agreements, between any Director and the company or any of its subsidiaries, whether providing for benefits upon termination of employment or otherwise and no such agreements have been entered into, replaced or amended within the six months preceding the date of this document.

**Directors' profile**

**George Kynoch (Non-Executive Chairman)**, aged 65, has over 30 years' experience in industry and was Chief Executive of G & G Kynoch plc (the predecessor of Kynoch Group plc, now called Bioquell PLC, the Officially Listed designer and manufacturer of healthcare equipment for use in contamination control). He was Grampian Industrialist of the Year in 1988 and received the Highland Business Award. Mr Kynoch was the Scottish Office Industry and Local Government Minister from 1995 to 1997, while serving as a Member of Parliament for Kincardine and Deeside between 1992 and 1997. He is chairman of ITWP Acquisitions Limited, and a Non-Executive Director of Talent Group Plc, which is admitted to trading on AIM.

**Abraham Weitz (Non-Executive Director),** aged 47, has many years of experience in the property industry, having joined Highdorn Co. Limited, a property management company, in early 1992. Mr Weitz has for some time had an interest in merging the new e-commerce ideas with more traditional business and is joint founder of the company.

# Report of the Directors

continued

**Directors profile** continued

**Moses Kraus (Non-Executive Director),** aged 54, has been an active participant in the TEP market for several years. After finishing Rabbinical and Talmudic studies in 1980, Mr Kraus was a teacher in a religious school in Zurich between 1981 and 1985. In 1983 he trained as a life insurance salesman, in his spare time, with Winterthur Insurance in Zurich, where he was first exposed to the endowment policy market. In 1984 he became a significant shareholder in Caruso AG, which was formed in 1983 to sell life insurance and associated products. It held endowment policies with a value of approximately CHF 200 million in its clients' portfolios. Mr Kraus' shareholding in Caruso AG has now reduced to less than 10 per cent and he has no executive role in that company. He moved from Switzerland to the United Kingdom in 1994 with residential status of "Person of Independent Means" which prevented him from working as an employee or engaging in business in the United Kingdom until he obtained indefinite residence in March 1999. He founded TEP Exchange Group PLC in November 1999.

**David Roxburgh (Managing Director),** aged 48, a member of the Institute of Certified Public Accountants in Ireland and is Managing Director of the Fitzwilton group of Companies. One of Fitzwilton's investments is a 36% shareholding in Portfolio Design Group International Limited (the parent company of SL Investment Management Limited). The business of Portfolio Design Group International Limited includes, inter alia, the purchase, sale and valuation of secondary life policies, the valuation and procurement of US traded senior life interest policies and investment adviser on specialist investment products.

## Substantial shareholdings

Excluding Directors whose shareholdings are set out above, the following had declared an interest of 3% or more in the company's issued ordinary share capital at 31 December 2011:

| Name | Ordinary shares | Percentage of ordinary shares |
|---|---|---|
| SL Investment Management Limited | 408,032,798 | 48.00% |
| Close Horizons Limited | 186,833,333 | 21.98% |
| Preferred Asset Management Limited | 85,000,000 | 10.00% |
| Strategic German Investments Limited | 40,000,000 | 4.71% |

None of the Directors are aware of any interest, apart from those listed above which represents 3% or more of the issued share capital of the company or which directly or indirectly, jointly or severally, exercises or could exercise control of the company.

The market price of the company's shares at the end of the financial year was 0.125p; the highest and lowest share prices during the year were 0.35p and 0.10p respectively.

## Group policy on payment of creditors

It is the group's policy to agree terms of payment prior to commencing business with suppliers. The average creditor payment period for the company at 31 December 2011 was 60 days (2010: 96 days).

# Report of the Directors

continued

### Going concern

During the year ended 31 December 2011 the group made a profit of £666,082 (2010: loss £86,458) and at 31 December 2011 had net assets of £22,866 (2010: net liabilities £728,446).

In reaching a decision as to whether the company is a going concern, the directors have given due regard to the following factors:

- During 2010, the group entered in to a 10-year licence agreement ("the Licence Agreement") with SL Investment Management Limited ("SL"), which is generating significant revenue and cash for the group. As a result the group is now in a net asset position and the directors believe that the group will be able to meet its liabilities as they fall due for the foreseeable future.
- The current financial position of SL.

On the basis of the above, and all other available information, the Directors consider that it is appropriate to prepare the financial statements on the going concern basis.

### Statement of Directors' responsibilities

The directors are responsible for preparing the Annual Report and financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group and parent company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and the company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable IFRSs as adopted by the European Union 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 adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the group and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# Report of the Directors

continued

**Website publication**

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the directors, whose names and functions are listed on pages 7 and 8 confirm that, to the best of their knowledge:

- the group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the group; and
- the directors' report and related disclosures include a fair review of the development and performance of the business and the position of the group, together with a description of the principal risks and uncertainties that it faces.

**Disclosure of information to Auditors**

Each of the persons who are directors at the time when this directors' report is approved has confirmed that:

- so far as that directors are aware, there is no relevant audit information of which the company's auditors are unaware; and
- that directors have taken all the steps that ought to have been taken as directors in order to be aware of any information needed by the company's auditors in connection with preparing their report and to establish that the company's auditors are aware of that information.

**Independent Auditors**

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office and a resolution concerning their re-appointment will be proposed at the Annual General Meeting.

By order of the Board

**D Roxburgh**
Director

19 June 2012

# Independent auditors' report

**to the members of TEP Exchange Group PLC**

We have audited the group and parent company financial statements (the ''financial statements'') of TEP Exchange Group PLC for the year ended 31 December 2011 which comprise the Consolidated Statement of Comprehensive Income, the Consolidated and Company Statement of Changes in Equity, the Consolidated and Company Statements of Financial Position, the Consolidated and Company Statements of Cash Flows and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

### Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement, set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, 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.

### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and parent company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2011 and of the group's profit and group's and parent company's cash flows for the year then ended;
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

# Independent auditors' report

**to the members of TEP Exchange Group PLC** continued

### Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

**David Roper** (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Manchester

19 June 2012

# Consolidated statement of comprehensive income

for the year ended 31 December 2011

| | Note | 2011 £ | 2010 £ |
|---|---|---|---|
| **Revenue** | 2 | 1,044,472 | 164,776 |
| Administrative expenses | | (356,738) | (221,573) |
| **Profit/(loss) from operations** | 4 | 687,734 | (56,797) |
| Finance costs | 5 | (21,652) | (29,661) |
| **Profit/(loss) before income tax** | | 666,082 | (86,458) |
| Income tax expense | 6 | – | – |
| **Profit/(loss) attributable to the owners of the parent and total comprehensive income for the year** | | 666,082 | (86,458) |
| **Earnings/(loss) per share** | | | |
| Basic and diluted earnings/(loss) per share | 8 | 0.14p | (0.02)p |

The notes on pages 19 to 30 form part of these financial statements.

# Consolidated and Company statements of changes in equity

for the year ended 31 December 2011

| | Note | Share capital £ | Share premium £ | Accumulated losses £ | Total £ |
|---|---|---|---|---|---|
| **Group** | | | | | |
| At 1 January 2010 | | 2,262,980 | 3,951,948 | (6,856,916) | (641,988) |
| Total comprehensive income for the year | | – | – | (86,458) | (86,458) |
| At 1 January 2011 | | 2,262,980 | 3,951,948 | (6,943,374) | (728,446) |
| Share issue in year | | 4,500 | 80,730 | – | 85,230 |
| Total comprehensive income for the year | | – | – | 666,082 | 666,082 |
| At 31 December 2011 | 14 | 2,267,480 | 4,032,678 | (6,277,292) | 22,866 |

| | Note | Share capital £ | Share premium £ | Accumulated losses £ | Total £ |
|---|---|---|---|---|---|
| **Company** | | | | | |
| At 1 January 2010 | | 2,262,980 | 3,951,948 | (8,639,589) | (2,424,661) |
| Total comprehensive income for the year | | – | – | (47,545) | (47,545) |
| At 1 January 2011 | | 2,262,980 | 3,951,948 | (8,687,134) | (2,472,206) |
| Share issue in year | | 4,500 | 80,730 | – | 85,230 |
| Total comprehensive income for the year | | – | – | 774,480 | 774,480 |
| At 31 December 2011 | 14 | 2,267,480 | 4,032,678 | (7,912,654) | (1,612,496) |

Share capital is the amount subscribed for ordinary shares and deferred shares at nominal value.

Share premium represents the excess of the amount subscribed for share capital over the nominal value of these shares net of share issue expenses.

Accumulated losses represent cumulative losses of the group or the company attributable to equity shareholders.

The notes on pages 19 to 30 form part of these financial statements.

# Consolidated statement of financial position

at 31 December 2011

| | Note | 2011 £ | 2011 £ | 2010 £ | 2010 £ |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| **Non-current assets** | | | | | |
| Property, plant and equipment | 9 | | – | | – |
| **Total non-current assets** | | | – | | – |
| **Current assets** | | | | | |
| Inventories | 11 | 3,525 | | 3,403 | |
| Trade and other receivables | 12 | 150,736 | | 323,073 | |
| Cash and cash equivalents | | 73,593 | | 49,043 | |
| **Total current assets** | | | 227,854 | | 375,519 |
| **Total assets** | | | 227,854 | | 375,519 |
| **Liabilities** | | | | | |
| **Current liabilities** | | | | | |
| Borrowings | 15 | – | | (534,000) | |
| Trade and other payables | 13 | (204,988) | | (569,965) | |
| **Total current liabilities** | | (204,988) | | (1,103,965) | |
| **Total liabilities** | | | (204,988) | | (1,103,965) |
| **Net assets/(liabilities)** | | | 22,866 | | (728,446) |
| **Equity attributable to owners of the parent** | | | | | |
| Share capital | 14 | | 2,267,480 | | 2,262,980 |
| Share premium account | | | 4,032,678 | | 3,951,948 |
| Accumulated losses | | | (6,277,292) | | (6,943,374) |
| **Total equity** | | | 22,866 | | (728,446) |

The financial statements were approved by the Board of Directors and authorised for issue on 19 June 2012.

**G Kynoch**
Chairman

**D Roxburgh**
Director

Company registered number 03877125

The notes on pages 19 to 30 form part of these financial statements.

# Company statement of financial position

at 31 December 2011

| | Note | 2011 £ | 2011 £ | 2010 £ | 2010 £ |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| **Non-current assets** | | | | | |
| Property, plant and equipment | 9 | | – | | – |
| Investments in subsidiary undertakings | 10 | | 100,006 | | 100,006 |
| | | | 100,006 | | 100,006 |
| **Current assets** | | | | | |
| Trade and other receivables | 12 | | 296,106 | | 493,316 |
| Cash and cash equivalents | | | 62,302 | | 48,949 |
| **Total assets** | | | 458,414 | | 642,271 |
| **Liabilities** | | | | | |
| **Current liabilities** | | | | | |
| Borrowings | 15 | – | | (534,000) | |
| Trade and other payables | 13 | (2,070,910) | | (2,580,477) | |
| **Total current liabilities** | | (2,070,910) | | (3,114,477) | |
| **Total liabilities** | | | (2,070,910) | | (3,114,477) |
| **Net liabilities** | | | (1,612,496) | | (2,472,206) |
| **Equity attributable to owners of the parent** | | | | | |
| Share capital | 14 | | 2,267,480 | | 2,262,980 |
| Share premium account | | | 4,032,678 | | 3,951,948 |
| Accumulated losses | | | (7,912,654) | | (8,687,134) |
| **Total equity** | | | (1,612,496) | | (2,472,206) |

The financial statements were approved by the Board of Directors and authorised for issue on 19 June 2012.

**G Kynoch**
Chairman

**D Roxburgh**
Director

Company registered number 03877125

The notes on pages 19 to 30 form part of these financial statements.

# Consolidated statement of cash flows

for the year ended 31 December 2011

| | Note | 2011<br>£ | 2010<br>£ |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating profit/(loss) | | 666,082 | (86,458) |
| Increase in inventories | 11 | (122) | (118) |
| Decrease/(increase) in trade and other receivables | 12 | 172,337 | (300,323) |
| (Decrease)/increase in trade and other payables | 13 | (364,977) | 262,597 |
| Cash generated in operating activities | | 473,320 | (124,302) |
| **Cash flows from financing activities** | | | |
| (Decrease)/increase in borrowings | | (534,000) | 171,000 |
| Issue of ordinary share capital | | 85,230 | – |
| **Net increase in cash and cash equivalents** | 16 | 24,550 | 46,698 |
| Cash and cash equivalents at beginning of year | 16 | 49,043 | 2,345 |
| **Cash and cash equivalents at the end of year** | 16 | 73,593 | 49,043 |
| Cash and cash equivalents comprise: | | | |
| Cash available on demand | | 73,593 | 49,043 |

The notes on pages 19 to 30 form part of these financial statements.

# Company statement of cash flows

for the year ended 31 December 2011

| | Note | 2011<br>£ | 2010<br>£ |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating profit/(loss) | | 774,480 | (47,545) |
| Decrease/(increase) in trade and other receivables | 12 | 197,210 | (298,960) |
| (Decrease)/increase in trade and other payables | 13 | (509,567) | 222,279 |
| Cash generated in operating activities | | 462,123 | (124,226) |
| **Cash flows from financing activities** | | | |
| (Decrease)/increase in borrowings | | (534,000) | 171,000 |
| Issue of ordinary share capital | | 85,230 | – |
| **Net increase in cash and cash equivalents** | 16 | 13,353 | 46,774 |
| Cash and cash equivalents at beginning of year | 16 | 48,949 | 2,175 |
| **Cash and cash equivalents at the end of year** | 16 | 62,302 | 48,949 |
| Cash and cash equivalents comprise: | | | |
| Cash available on demand | | 62,302 | 48,949 |

The notes on pages 19 to 30 form part of these financial statements.

# Notes forming part of the financial statements

for the year ended 31 December 2011

## 1 Accounting policies

The principal accounting policies adopted in the preparation of the financial statements are set out below. The policies have been consistently applied to the company and the group to all the years presented, unless otherwise stated. These financial statements have been prepared in accordance with International Financial Reporting Standards, International Accounting Standards and EU adopted IFRICs (collectively IFRS) issued by the International Accounting Standards Board (IASB) as adopted by European Union ("adopted IFRSs"), and in accordance with those parts of the Companies Act 2006 applicable to those companies preparing their accounts under IFRS.

As described in the Chairman's Statement on page 2, the directors have a reasonable expectation that the group has adequate resources to continue in operational existence for the foreseeable future. The group therefore continues to adopt the going concern basis in preparing its consolidated financial statements.

**Standards, amendments and interpretations to published standards not yet effective**

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not yet been adopted by the EU):

- IFRS 1 Amendment – Limited exemption from IFRS 7 Disclosures for first time adopters
- Amendments to IFRS 1 Additional Exemptions for First-time Adopters
- IFRS 1 Amendments Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopters
- Amendments to IFRS 7 Financial Instruments Disclosures
- IFRS 9 Financial Instruments
- IAS 12 Amendments to Deferred tax: Recovery of Underlying Assets
- IFRIC 14 (Amendment) Prepayments of a minimum funding requirement
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
- Revised IAS 24 Related Party Disclosures (Issued 4 November 2009)
- Amendment to IAS 32 Classification of Rights Issues

Adoption of these Standards and Interpretations is not expected to have a material impact on the results of the company or group.

**Basis of consolidation**

Where the company has the power, either directly or indirectly, to govern the financial and operating policies of another entity or business so as to obtain benefits from its activities, it is classified as a subsidiary. The consolidated financial statements present the results of the company and its subsidiaries ("the group") as if they formed a single entity. Intercompany transactions and balances between group companies are therefore eliminated in full. Uniform accounting policies are adopted across the group.

**Revenue**

Revenue represents fees and commission (exclusive of value added tax) from licensing of the group's proprietary electronic platform and advertising the purchase of with profit endowment policies by market makers registered on the electronic platform. Fees and commission income is recognised when the group's contractual obligations are complete.

**Expenses**

Expenses are recognised in the period in which the related revenue is recognised.

# Notes forming part of the financial statements

continued

## 1 Accounting policies continued

### Financial assets

The group classifies its financial assets into categories as set out below, depending on the purpose for which the asset was acquired.

### Trade and other receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise principally through the provision of goods and services to customers (e.g. trade receivables), but also incorporate other types of contractual monetary asset. They are initially recognised at fair value plus transaction costs that are directly attributable to their acquisition or issue, and are subsequently carried at cost, less provision for impairment, if appropriate.

Impairment provisions are recognised when there is objective evidence (such as significant financial difficulties on the part of the counterparty or default or significant delay in payment) that the group will be unable to collect all of the amounts due under the terms receivable, the amount of such a provision being the difference between the net carrying amount and the present value of the future expected cash flows associated with the impaired receivable. For trade receivables, which are reported net, such provisions are recorded in a separate allowance account with the loss being recognised within administrative expenses in the statement of comprehensive income. On confirmation that the trade receivable will not be collectable, the gross carrying value of the asset is written off against the associated provision.

The group's loans and receivables comprise trade and other receivables and cash and cash equivalents in the statement of financial position. Those of the company also include amounts due from subsidiary undertakings.

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short term highly liquid investments with original maturities of three months or less, and bank overdrafts. Bank overdrafts are shown within loans and borrowings in current liabilities on the statement of financial position.

### Financial liabilities

The group classifies its financial liabilities into one of the following categories, depending on the purpose for which the liability was acquired:

- Trade payables and other short-term monetary liabilities, which are initially recognised at fair value and subsequently carried at amortised cost using the effective interest method.
- Bank and other borrowings are initially recognised at fair value net of any transaction costs directly attributable to the issue of the instrument.
- Income received in advance is recorded as deferred income on the balance sheet.

### Share capital

Financial instruments issued by the group are treated as equity only to the extent that they do not meet the definition of a financial liability. The group's ordinary and deferred shares are classified as equity instruments.

### Investments in subsidiary undertakings

Investments in subsidiary undertakings are held as non-current assets and are stated at cost less provision for impairment in value.

# Notes forming part of the financial statements

continued

## 1 Accounting policies continued

### Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and accumulated impairment losses. Such cost includes the cost of replacing part of the plant and equipment when that cost is incurred, if the recognition criteria are met. All other repair and maintenance costs are recognised in profit or loss as incurred.

Depreciation is calculated on a straight line basis over the useful life of the asset as follows:

| | | |
|---|---|---|
| Computer equipment | – | 3 years |
| Fixtures, fittings and equipment | – | 4 years |

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the year the asset is derecognised.

The assets' residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end.

### Stocks

Stock is valued at the lower of cost and net realisable value. Cost includes the cost of endowment policies acquired together with associated charges and premiums paid. Net realisable value is the estimated price at which stocks can be realised in the normal course of business which will be based on the surrender value of policies.

### Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in the income statement, 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.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date 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 and 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, the 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 sheet 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 to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, expect where the timing of the reversal of the temporary difference is controlled by the group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

# Notes forming part of the financial statements

continued

## 1 Accounting policies continued

### Segmental reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Board.

### Deferred Income

License fees received in advance are recorded as deferred income on the balance sheet.

### Share based payments

The group operates a number of equity-settled, share-based compensation plans, under which the entity receives services from employees as consideration for equity instruments (options) of the group. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions;
- excluding the impact of any service and non-market performance vesting conditions (for example, profitability, sales growth targets and remaining an employee over a specified time period) and
- including the impact of any non-vesting conditions (for example the requirement for the employee too save).

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognised over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting period, the entity revises its estimates of the number of options that are expected to vest based on the non-marketing vesting conditions. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

When the options are exercised, the company issues new shares. The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

## 2 Revenue

The group's main revenue is generated in the United Kingdom from the licensing of its electronic platform for trading endowment policies. The group also earns fees from advertising the purchase of with profit endowment policies by market makers registered on the electronic platform. The group has no other geographical or operating segments.

Transactions with major customers are disclosed in note 15.

## 3 Staff and director costs

### Group

Staff costs, including directors, consist of:

| | 2011<br>£ | 2010<br>£ |
|---|---|---|
| Fees and remuneration for management services | 28,200 | 47,200 |

The group had no employees other than the executive director. No pension contributions were made in respect of the directors (2010: £nil). The key management personnel of the group are the board of directors and their compensation is disclosed above.

# Notes forming part of the financial statements

continued

## 4 Profit/(loss) from operations

**Group**

Profit/(loss) from operations is stated after charging:

| | 2011 £ | 2010 £ |
|---|---|---|
| Fees payable to the company's auditor for the audit of: | | |
| Parent company and consolidated financial statements | 9,000 | 9,000 |
| Fees payable to the company's auditor and its associates for other services: | | |
| – The audit of the company's subsidiaries pursuant to legislation | 6,000 | 6,000 |
| – Taxation services | 10,500 | – |

## 5 Finance costs

**Group and Company**

| | 2011 £ | 2010 £ |
|---|---|---|
| Interest payable on other borrowings | 21,652 | 29,661 |

## 6 Income tax expense

No liability to corporation tax arises on the results for the year due to the utilisation of losses brought forward.

The tax assessed for the year varies from the standard rate of corporation tax in the UK. The differences are explained below:

| | 2011 £ | 2010 £ |
|---|---|---|
| Profit/(loss) on ordinary activities before income tax | 666,082 | (86,458) |
| Profit/(loss) on ordinary activities before income tax multiplied by the standard rate of UK corporation tax of 26.49% (2010: 28.0%) | 176,445 | (24,208) |
| Utilisation of tax losses | (176,445) | – |
| Tax loss not recognised as a deferred tax asset | – | 24,208 |
| Current year income tax charge | – | – |

At 31 December 2011 the group had a deferred income tax asset of £1,525,144 (2010: £1,701,589) in respect of losses which has not been recognised in these financial statements.

## 7 Profit/(loss) for the year attributable to the members of TEP Exchange Group PLC

| | 2011 £ | 2010 £ |
|---|---|---|
| Dealt with in financial statements of the parent company | 774,480 | (47,545) |

The company has taken advantage of the exemption allowed under section 408 of the Companies Act 2006 and has not presented its own statement of comprehensive income in these financial statements.

# Notes forming part of the financial statements

continued

## 8 Earnings per share

The calculation of the basic and diluted earnings per share is based upon:

| | 2011 | 2010 |
|---|---|---|
| Basic and diluted earnings per share (pence) | 0.14p | (0.02)p |
| Profit/(loss) attributable to equity shareholders | £666,082 | £(86,458) |
| | **Number** | **Number** |
| Weighted average number of shares | 471,506,848 | 399,999,999 |

The options, warrants and deferred shares in issue at 31 December 2011 and 31 December 2010, which are disclosed in note 14, are antidilutive and have therefore been excluded from the calculation of diluted earnings per share. However, such options may be dilutive in future periods.

## 9 Property, plant and equipment

| Group and Company | Computer equipment £ | Fixtures, fittings and equipment £ | Total £ |
|---|---|---|---|
| **Cost** | | | |
| At 1 January 2010, 31 December 2010, 1 January 2011 and 31 December 2011 | 173,446 | 65,474 | 238,920 |
| **Accumulated depreciation** | | | |
| At 1 January 2010, 31 December 2010, 1 January 2011 and at 31 December 2011 | 173,446 | 65,474 | 238,920 |
| **Net book value** | | | |
| At 31 December 2011 | – | – | – |
| At 31 December 2010 | – | – | – |

## 10 Investments in subsidiary undertakings – Company

| | 2011 £ | 2010 £ |
|---|---|---|
| Subsidiary undertakings – shares at cost and net book value | 100,006 | 100,006 |

The following were subsidiary undertakings held directly by company at the end of the year:

| Name | Country of incorporation | Proportion of voting rights and ordinary share capital held | Nature of business |
|---|---|---|---|
| TEP-Exchange Limited | England | 100% | Advertising services to the traded endowment policy market |
| TEP-Exchange Interim Portfolio Limited | England | 100% | Trading of traded endowment policies |
| TEP Transfer Limited | England | 100% | Dormant |
| Interactive Intelligence Limited | England | 100% | Dormant |

# Notes forming part of the financial statements

continued

## 11 Inventories

| | 2011 Group £ | 2010 Group £ | 2011 Company £ | 2010 Company £ |
|---|---|---|---|---|
| Endowment policy | 3,525 | 3,403 | – | – |

## 12 Trade and other receivables

| | 2011 Group £ | 2010 Group £ | 2011 Company £ | 2010 Company £ |
|---|---|---|---|---|
| Trade receivables | 3,598 | 295,736 | – | 293,750 |
| Amounts due from subsidiary undertakings | – | – | 150,000 | 172,229 |
| Other receivables | 130,719 | 6,902 | 130,719 | 6,902 |
| Prepayments and accrued income | 16,419 | 20,435 | 15,387 | 20,435 |
| | 150,736 | 323,073 | 296,106 | 493,316 |

At the year end, there were no receivables which are past due or impaired.

Included in amounts due from subsidiary undertakings is an amount of £150,000 (2010: £150,000) in respect of an unsecured loan to TEP-Exchange Limited and is subject to a tripartite agreement with TEP Exchange Group PLC (the lender) and the Financial Services Authority. Interest can be demanded by TEP Exchange Group PLC and if so demanded will be calculated at the annual rate of 5% above the London Inter-Bank Offered Rate for deposits of pounds sterling.

## 13 Trade and other payables

| | 2011 Group £ | 2010 Group £ | 2011 Company £ | 2010 Company £ |
|---|---|---|---|---|
| Trade payables | 120,198 | 199,980 | 119,598 | 199,258 |
| Other payables | 3,500 | 3,500 | 3,500 | 3,500 |
| Amounts due to subsidiary undertakings | – | – | 1,873,859 | 2,011,234 |
| Creditors for taxation and social security | 53,120 | 86,035 | 46,083 | 86,035 |
| Accrued liabilities and deferred income | 28,170 | 280,450 | 27,870 | 280,450 |
| | 204,988 | 569,965 | 2,070,910 | 2,580,477 |

For the amounts owing to subsidiary undertakings, there are no scheduled repayment terms, no interest is charged, and no security is held.

# Notes forming part of the financial statements

continued

## 14 Share capital

| | 2011 Number | 2010 Number | 2011 £ | 2010 £ |
|---|---|---|---|---|
| **Allotted, called up and fully paid** | | | | |
| Ordinary shares 0.001p/0.01p each | 849,999,999 | 399,999,999 | 8,500 | 40,000 |
| Deferred shares of 0.001p/0.99p each | 225,897,991,731 | 224,543,426 | 2,258,980 | 2,222,980 |
| | | | 2,267,480 | 2,262,980 |

Details of the movement in share options in the year:

| | Enterprise Management Incentive Scheme Number | Unapproved Share Option Plan Number |
|---|---|---|
| Outstanding at the beginning of the year | 3,710,697 | 200,000 |
| Lapsed in year | (3,710,697) | (200,000) |
| Outstanding at the end of the year | – | – |

On 14 March 2007, each of the 224,543,426 issued ordinary shares of 1p each in the company was subdivided into one ordinary share of 0.01p each and one deferred share of 0.99p each credited as fully paid. On 15 March 2007, the company issued 175,456,573 ordinary shares of 0.01p each at a premium of 0.19p per share.

The main rights and restrictions attaching to the deferred shares are as follows:

- no entitlement to receive dividends or other distributions;
- no entitlement to receive notice of or attend of vote at any general meeting of the company; and
- on a return of capital on a winding in the holders of deferred shares shall only be entitled to receive the amount paid up on such shares after the holders of the ordinary shares have received the sum of £1,000,000 for each ordinary share held by them and shall have no other right to participate in the assets of the company.

During the year the company undertook a subscription for new ordinary shares and warrants by the company's largest existing shareholder and certain other connected companies.

On 3 November 2011, each of the issued deferred shares of 0.99p was subdivided into 990 new deferred shares of 0.001p each and each of the existing ordinary shares of 0.01p was sub-divided and re-designated into one new ordinary share of 0.001p and nine new deferred shares.

The main rights and restrictions attaching to the new deferred shares are as follows:

- no voting rights;
- no entitlement to attend any general meeting of the company; and
- a right to participate in any return of capital to the extent of £1 in aggregate over the class and a right to participate in any dividend or other distribution to the extent of £1 in aggregate over the class.

The new deferred shares are, for all practical purposes, valueless and it is the Board's intention, at an appropriate time, to have the new deferred shares cancelled.

The subscribers agreed to subscribe for the subscription shares at 0.02p to raise £90,000 to fund current short term working capital requirements. The subscribers also received 10 subscription warrants for each subscription share and these are exercisable at 0.002p per new ordinary share. The warrants may only be exercised if the company (and its wholly owned subsidiaries) meet certain performance criteria over the three financial years ending 31 December 2013. In any case the company will have to have declared, made and paid dividends of at least £250,000 to all shareholders before the warrants may be exercised. The warrants may only be exercised together as a whole and not in part.

# Notes forming part of the financial statements

continued

## 14 Share capital continued

**Capital Management**

The group's capital comprises the ordinary shares of 0.001p (2010: 0.01p) each and the deferred shares of 0.001p (2010: 0.99p) each shown above.

The group's objectives when maintaining capital are:

- to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and
- to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk.

The group sets the amount of capital it requires in proportion to risk. The group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or sell assets to reduce debt.

Consistent with others in the industry, the group monitors capital on the basis of the debt to equity ratio. This ratio is calculated as net debt to equity. Net debt is calculated as total debt (as shown in the statement of financial position) less cash and cash equivalents. Total equity (as shown in the statement of financial position) includes components of equity (i.e. share capital, share premium, and retained earnings).

During 2011, the group repaid its external borrowings in full.

## 15 Related party transactions

During the year, the group earned fees of £1,037,691 (2010: £138,587) from SL Investment Management Limited ("SL"), a major shareholder in the group. At the end of the year SL owed the group £3,598.

These fees relate predominantly to amounts earned from a licence agreement with SL, allowing SL to develop and exploit the TEP Exchange platform and software.

During the year the group was charged £145,649 (2010: £113,958) by SL. At the end of the year the group owed SL £39,649 (2010: £68,149).

A loan of £534,000 from SL which was owed at the beginning of the year was repaid during the year.

During the year the group has loaned £125,000 to SL. The loan is repayable upon demand and interest is chargeable at 2% above base rate.

As described in the Chairman's Statement on page 2, on 2 April 2012 the company announced that SL had informed the company that the income generated during the 12 month period ending 30 April 2012 was unlikely to be £250,000 or more and, therefore, it may terminate the Licence Agreement in accordance with its terms. The company agreed with SL that it would provide a 61 day extension to the termination notice period to allow SL to further assess the benefits of the Licence Agreement. A further announcement by the company was issued on 31 May 2012 setting out that the agreement can now be terminated on 30 August 2012 by SL giving 30 day's prior written notice to the Company.

# Notes forming part of the financial statements

continued

## 16 Financial instruments

### Financial risk management

The Board of Directors sets the treasury policies and objectives of the group, which includes controls over the procedures used to manage financial market risks.

It is, and has been throughout the period under review, the group's policy that no trading in financial instruments shall be undertaken. The main risks arising from the group's financial instruments are:

- interest rate risk;
- liquidity risk;
- credit risk.

### Interest rate risk

The group borrows only in sterling at both fixed and floating rates of interest. At the year end, all borrowings were at variable rates.

### Liquidity risk

The group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and overdrafts as well as funding from its largest shareholder.

### Credit risk

The group has no significant concentration of credit risk. The main operating subsidiary has strict verification procedures in place prior to credit being advanced to customers and there are systems in place to ensure that there is a regular monitoring of each customer's credit levels.

The Board agrees and reviews policies and financial instruments for risk management. The primary objectives of the treasury function are to provide competitively priced funding for the activities of the group and to identify and manage financial risk.

### Principal financial instruments

The principal financial instruments used by the group and the company from which financial instrument risk arises, are as follows:

| **Financial assets** | **2011 Group £** | **2010 Group £** | **2011 Company £** | **2010 Company £** |
|---|---|---|---|---|
| Trade receivables | 3,598 | 295,736 | – | 293,750 |
| Amount due from subsidiary undertakings | – | – | 150,000 | 172,229 |
| Other receivables | 130,719 | 6,902 | 130,719 | 6,902 |
| Cash and cash equivalents | 73,593 | 49,043 | 62,302 | 48,949 |
| Total financial assets classified as loans and receivables | 207,910 | 351,681 | 343,021 | 521,830 |

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivable set out above.

At 31 December 2011 and 2010 the carrying amounts of financial assets approximate to their fair values.

# Notes forming part of the financial statements

continued

## 16 Financial instruments continued

**Financial liabilities**

| | 2011 Group £ | 2010 Group £ | 2011 Company £ | 2010 Company £ |
|---|---|---|---|---|
| Trade payables – current | 120,198 | 199,980 | 119,598 | 199,258 |
| Other payables | 3,500 | 3,500 | 3,500 | 3,500 |
| Amounts due to subsidiary undertakings | – | – | 1,873,859 | 2,011,234 |
| Accrued liabilities | 28,170 | 280,450 | 27,870 | 280,450 |
| Creditors for taxation and social security | 53,120 | 86,035 | 46,083 | 86,035 |
| Other borrowings | – | 534,000 | – | 534,000 |
| Total financial liabilities measured at amortised cost | 204,988 | 1,103,965 | 2,070,910 | 3,114,477 |

To the extent trade and other payables are not carried at fair value in the consolidated statement of financial position, book value approximates to fair value at 31 December 2011 and 2010.

All financial assets and liabilities are due in less than 1 year.

The group and company are exposed through its operations to one or more of the following financial risks:

**Liquidity risk**

Liquidity risk arises from the group's management of working capital and the finance charges and principal repayments on its debt instruments. It is the risk that the group will encounter difficulty in meeting its financial obligations as they fall due.

Short term liquidity risk is managed by preparing forecasts together with obtaining and reviewing the adequacy of banking facilities. There is currently no long term liquidity risk.

**Market operational and pricing risks**

The group operates only in the United Kingdom. The group's revenues are derived from fee and commission income chargeable to customers. The level of fees and commission is entirely dependent upon the level of activity in the traded endowment policy market.

**Credit risk**

Credit risk represents the loss that the company would incur if the counterparty failed to perform its contractual obligations. The group is exposed to credit risk in respect of fees and commission income chargeable to companies with whom it had a contractual relationship and interest receivable from its investments. Credit risk is mitigated through regular credit review of counterparties. As these counterparties are regulated by the Financial Services Authority, the credit reviews allow for the fact that they are subject to the regulatory capital requirements.

The group's maximum exposure to credit risk is £250,000 plus VAT, on the net quarterly licence fee agreement. No collateral is held as security. The credit qualities of financial assets that are neither past nor impaired are considered to be good, as they are primarily trade receivables from FSA regulated businesses and cash held with the Bank of Scotland. There are no financial assets which are past due or impaired.

Credit risk also arises from cash and cash equivalents and deposits with banks and financial institutions. For banks and financial institutions, only independently rated parties with minimum rating "AA" are accepted.

# Notes forming part of the financial statements
continued

## 16 Financial instruments continued

### Cash flow interest rate risk

Interest is chargeable on a loan to SL at 2.5% per annum. There are no differences between the book values and fair values of this financial asset.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the group's and company's profit before tax and equity (through the impact on floating rate investments and borrowings).

| | **2011 Change in rate** | **2011 Effect £** |
|---|---|---|
| Interest rate | +0.5% | 625 |
| | +1.0% | 1,250 |
| | +1.5% | 1,875 |
| | –0.5% | (625) |

### Currency risk

The group is not directly exposed to currency risk as its assets, liabilities, revenue and expenditure are denominated in Sterling.

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