



Epistem Holdings Plc
Annual Report and Accounts 2010

epistem

Controlling life-long tissue renewal

**Divisional development
and core company strength**

Business Overview

Introductory Highlights	
What We Do	
Epistem: Contract Research Services	
Epistem: Personalised Medicine	
Epistem: Novel Therapies	
Our Business and Strategy	

Review of the Year

Strength in Depth	12
Chairman's Statement	14
Chief Executive's Review	16

Governance

IFC	20
Board of Directors	20
Directors' Report	22
Directors' Remuneration Report	24
Corporate Governance Report	26
Independent Auditors' Report	27

Accounts

Consolidated Statement of Comprehensive Income	29
Consolidated Statement of Changes in Equity	30
Consolidated Balance Sheet	31
Consolidated Statement of Cash Flows	32
Notes to the Financial Statements	33
Company Balance Sheet	48
Company Statement of Changes in Equity	49
Company Statement of Cash Flows	50
Notes to the Company Financial Statements	51
Directors, Secretary and Advisers	IBC

2nd

Year of profit

45%

Revenue growth year-on-year

5.4m

Cash balance (£million)

Welcome

Epistem is a biotechnology and personalised medicine company commercialising its expertise in epithelial stem cells in the areas of oncology, gastrointestinal disease, dermatology and ageing

Every person develops from one cell – the fertilised egg. In the early stages of development, stem cells differentiate and become committed to generating a specific tissue or organ. Adult stem cells remain capable of regenerating tissue in our organs throughout our lives.

As we get older, the ability of stem cells to regenerate new cellular tissue diminishes, leading to tissue ageing and disease.

Epistem is focused on understanding how cells function and are controlled, so that we can identify new drug therapies to address the major diseases of oncology, gastrointestinal disease, dermatology and ageing.

Epistem also identifies patient specific gene biomarkers, gene mutations and disease pathogens as part of its Personalised Medicine development.

2010 marks the 10 year anniversary of the formation of the Company.

Highlights

- Year-on-year revenue growth up 45%
- All divisional revenues increased over the year
- Formation of a new Personalised Medicine division
- Development of Genedrive™ 'Point of Care' mobile molecular diagnostic device
- Growth in profit and increased Earnings Per Share
- Strengthened cash balance with continuing strong trading outlook
- 10 year anniversary of company formation



Scientific research services, personalised medicine and innovative therapeutics

Life-long Tissue Renewal Explained

Epithelial stem cells

Epithelial stem cells are rare cells which represent the 'building blocks' of tissue growth and renewal. Stem cells are essential for tissue repair, since they are responsible for replacement of all cells.

Expertise

Epistem is applying its know-how and expertise to identify genes and proteins responsible for controlling cell production to develop drugs to treat cancer and other epithelial diseases.

Vision

Epistem's vision is to exploit its leading stem cell technology to identify Novel Therapeutics and advance its next generation developments in personalised medicine.



▶ Contract Research Services (page 4)

Contract Research Services provide specialised preclinical efficacy services primarily for drug development companies on a 'fee for service' basis. The division is growing strongly, is cash generative and profitable. Our Contract Research Services division has a well established record of providing a specialist range of testing services to major pharmaceutical and biotechnology companies globally.

We assist client companies with preclinical development of their drug therapies to treat epithelial diseases including:

- Cancer
- Cancer supportive care (Mucositis)
- Inflammatory bowel disease
- UV-induced skin damage
- Wound healing
- Skin and hair disorders



▶ **Personalised Medicine** (page 6)

1 Biomarkers

Epistem has developed a range of innovative technologies allowing highly sensitive analysis of small numbers of cells. These technologies are used by pharmaceutical companies to measure drug-induced gene expression changes, primarily in the area of oncology. Our biomarker libraries assist in identifying changes in gene expression that result from treatment with an oncology drug. We work closely with top-tier pharmaceutical groups to better understand drug-induced gene expression changes in a subject during treatment.

2 Diagnostics

We have expanded our technology reach into diagnostics with the development of Genedrive™, a 'point of care' molecular diagnostic device. Genedrive™ is targeted at providing a 'near patient' diagnosis in less than 30 minutes. Rapid, sensitive and accurate testing offers to revolutionise the field of medical diagnosis by enabling viral, pathogen and gene mutation diagnosis to be made readily available at minimal cost.



▶ **Novel Therapies** (page 8)

Epistem is discovering key regulators (proteins and peptides) of epithelial cells and developing therapeutics to control cell production, initially targeting the areas of oncology and inflammatory bowel disease. With over 80% of adult cancers arising from epithelial tissue, we believe that applying our understanding of epithelial stem cells and cell production will identify new targets and pathways for drug development.

Our Novel Therapies division continues to develop the regenerative medicine collaboration with Novartis and is identifying the key regulators of stem cells and epithelial cell production. The collaboration is now beginning to yield initial hits/leads. The division's primary focus is to discover new drug leads across major epithelial diseases and expand its technology and intellectual property portfolio alongside other collaborative opportunities.



£2.5m

Turnover

Divisional development and strengthened operating margin

The Contract Research Services division provides preclinical efficacy testing services in the areas of oncology, oncology supportive care (mucositis), inflammatory bowel disease and dermatology. The division saw continued growth and a broadening of its customer base over the year.

The raised profile of the division and growing awareness of our technical expertise continued to build demand for our specialised drug efficacy and ‘mechanism of action’ models. Whilst revenue growth over the year was modest at 10%, the overall quality of business was significantly better with operating margin up 28% year on year, based on an improved mix of high margin service business.

Strengthening partnerships

Over the year the division grew its average contract value, increased the size of its customer base and enhanced its service offering. The division is focused on developing key client relationships with large pharmaceutical groups to generate a solid foundation for growth in the current economic climate.

Biodefence

Our collaboration with the US National Institutes of Health (NIH) continues to expand around the testing and efficacy of agents under the MCART (Medical Counter measures Against Radiological Threats) programme designed to address exposure to radiation or nuclear attack. Through the expanding scope of the collaboration we anticipate that our relationship with the US NIH and NIAID (National Institute of Allergy and Infectious Diseases) will develop further over the coming year.

Immunohistochemistry

During the year the division launched a new hair immunohistochemistry (IHC) model. Our contract research services group has seen a significant growth in interest in this area. Immunohistochemistry is widely used to understand the distribution and localisation of differentially expressed proteins in biological tissue.

Outlook

A strengthened service offering, coupled with increased expertise across each disease area, has ensured that the division is well positioned for the year ahead. We will continue to nurture our key customer relationships, together with extending into selected territories through new business development and distributor opportunities. Through increasing recognition of our core cell biology expertise and the planned expansion of our service offerings, we anticipate that the division will continue to deliver sustainable growth over the coming year.

Highlights

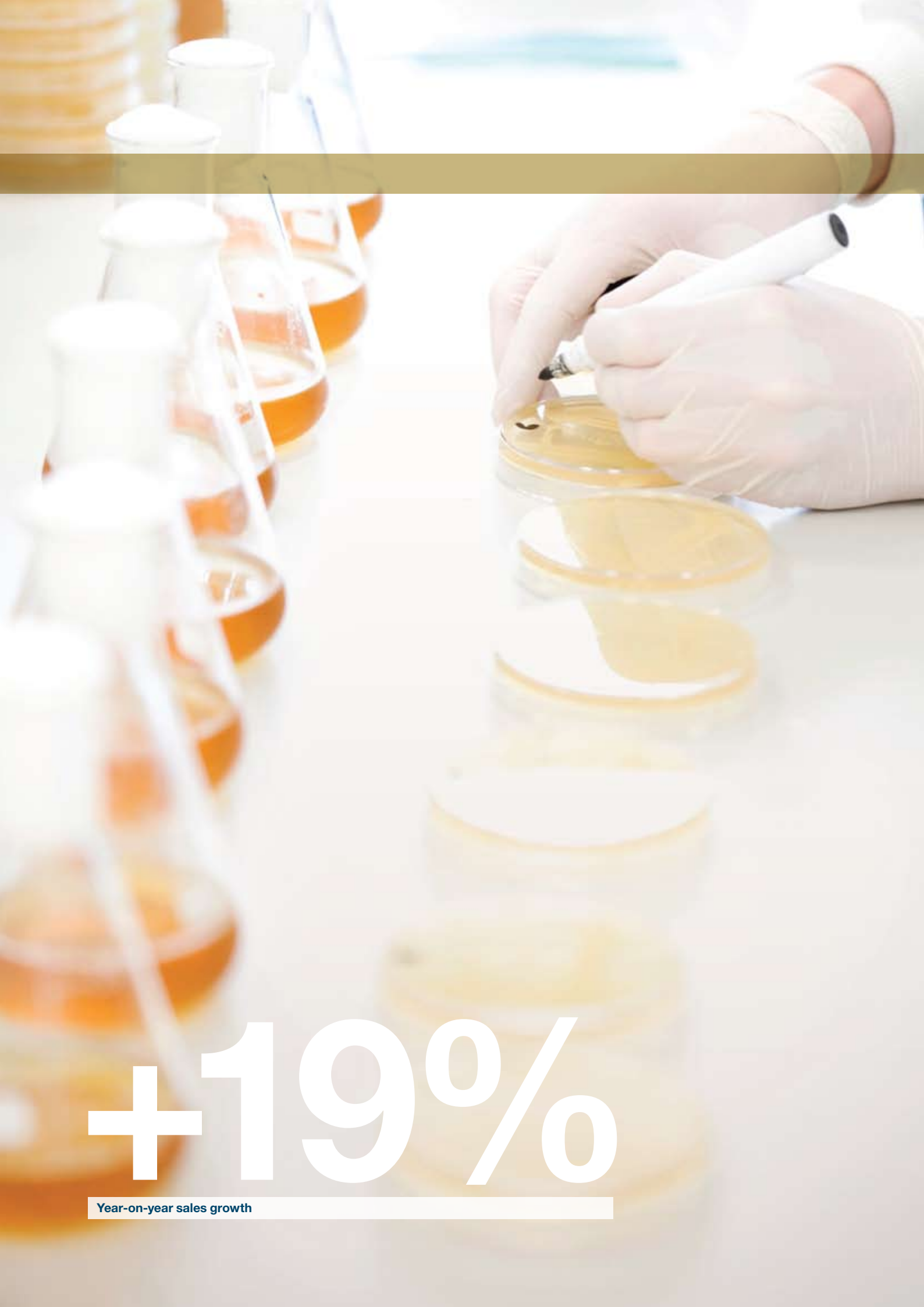
- Increased demand for oncology, mucositis and IHC service offerings
- Growth in US National Institutes of Health bio-defence programme
- Strengthening recognition of science base
- Operating profit increased 28% year on year

Contract Research Services turnover

2010	£2.5m
2009	£2.3m

Case Study: US National Institutes of Health

Epistem’s Contract Research Services division provides scientific expertise and preclinical research models to the NIH’s research programme on Medical Countermeasures Against Radiological and Nuclear Threats (MCART).



+19%

Year-on-year sales growth

Globally leading biomarker and diagnostic technology

1 Biomarkers

Biomarkers provide measures of biological processes that can improve the precision with which we can guide drug development and disease treatment. Epistem's GenetRx™ technology measures drug-induced changes in gene expression for drug development.

Following the creation of the division last year, the newly formed group has continued to advance its technology with top tier pharmaceutical partners and has extended its proprietary offering to both tissue and blood biomarkers alongside its hair biomarker position. The biomarker division is currently collaborating with a number of major pharmaceutical groups including Novartis, AstraZeneca and Johnson and Johnson.

Year-on-year revenues improved 19%, but this masked the significant development underway to prepare the division for growth in the coming year. With GCLP accreditation status now approved, we have extended our business presence in the US through the set up of our US office to provide a closer relationship with our key pharmaceutical and biotechnology partners.

The biomarker division has developed a library of oncology pathway markers through its bioinformatic dataset Pathway Direct™. This dataset and our novel application technologies will be used to provide partner access to specific drug biomarkers in oncology signal pathways.

Outlook

We anticipate a further strengthening in the growth of our biomarker business division over the coming year underpinned by the extension of our key collaborative relationships now unfolding in broader clinical phase studies. We continue to search for a suitable partner to help bolster our international coverage and growth ambition.

Case Study: GCLP Accreditation

The Biomarker division conducts gene expression analysis to support clinical drug development programs within pharmaceutical and biotechnology organisations, with an increasing focus on providing valuable biomarker information that can be used in drug development.

2 Genedrive™ (Point-of-Care molecular diagnostic device)

Molecular diagnostic testing is making headway into decentralised settings such as hospitals, clinics and smaller labs. Molecular diagnostic tests are being developed to provide rapid test results with decentralised labs and 'near patient' settings viewed as the emerging and growing market. The Point-of-Care (POC) market for tests in infectious disease is particularly broad and captures: hospital emergency rooms, GP/physician offices, community health centres and health outreach programmes, such as sexually transmitted disease (STD) and HIV clinics.

Trends show that hospital testing is expected to decrease as POC tests becomes the preferred choice of diagnostic testing 'near patient' and in the community. The main objective is to keep patients out of hospitals and to reduce the need to go to hospitals and to diagnose patients in shorter timeframes to improve the quality of care. In addition, rapid result generation is sought so that appropriate treatment can be implemented without delay, leading to an improved clinical and economic outcome.

Outlook

Epistem is unveiling Genedrive™, a 'first to market' proprietary and disruptive technology positioned to provide a new paradigm in Personalised Medicine and point-of-care diagnostics. It builds on our biomarker technology and existing assay expertise to provide a novel simple to use and cost effective platform that will diagnose a range of bacterial infections, pathogens and SNP gene mutations in less than 30 minutes. We anticipate formally launching Genedrive™ in 2011.

Highlights

- Good Clinical Laboratory Practice (GCLP) accreditation status
- Launch of proprietary GenetRx™ brand
- Unfolding biomarker technology across top-tier pharmaceutical groups
- Development of Genedrive™

Personalised Medicine turnover

2010	£0.8m
2009	£0.7m



£2.4m

Turnover

Continued progress towards new drug targets

The Novel Therapies division is discovering the body's own key regulators of epithelial stem cells and tissues. The body's own key (protein) regulators are largely unknown because of the difficulties in accessing and evaluating their effect in epithelial tissue. These key regulators are responsible for restoring damaged tissue and for maintaining 'life-long tissue renewal' throughout our lives.

The division is primarily focused on identifying the key regulators of cells in the disease areas of cancer (based on 80% of cancer originating from epithelial tissue), gastrointestinal disease, wound healing and ageing.

Novartis collaboration

The discovery and development collaboration with Swiss based Novartis AG continued to progress over the year with the Novel Therapies division reporting its first full year revenue of £2.4m. This collaboration revenue includes £1.4m amortisation of upfront income. New drug targets are continuing to emerge, with the division positioning itself to create a pipeline of early stage development targets. The discovery programme has been constructed to identify and map regulators which control the activity of cells and stem cells. Once regulators are identified, our development 'route map' enables each hit to be characterised for activity with a view to prioritising leads for further development. This carefully constructed process is driving a comprehensive understanding of cell inhibition, proliferation and self renewal, which alongside signalling pathways and identified regulators will allow us to better understand tissue control. The accounts for the year do not include any license income and the timings of license opportunities for targets and future development funding with Novartis remain difficult to accurately predict.

Partnerships

Based on our programme of discovery and early stage development, interest continues to build around our core biology and molecular pathway understanding. We have extended our in-house expertise in signalling pathway bioinformatics and protein production to firmly establish our internal discovery position. We continue to evaluate other drug discovery opportunities with major industry players and have recently commenced an internal small molecule programme to identify our own proprietary leads for cell receptor regulation.

Outlook

We continue to build our understanding of the body's key regulators and we remain focused on identifying novel drug agents. We look forward to continued progress under our Novartis collaboration and to advancing other partnerships from our emerging hits/lead pipeline.

Highlights

- Progress towards new drug targets
- Discovering and developing leads targeting cancer (oncology) and gastrointestinal disease
- Building intellectual property in identified regulators of epithelial cells

Novel Therapies turnover



Case Study: Novartis

At the first anniversary of the collaboration, we are pleased with progress towards advancing our first therapeutic hits/leads.

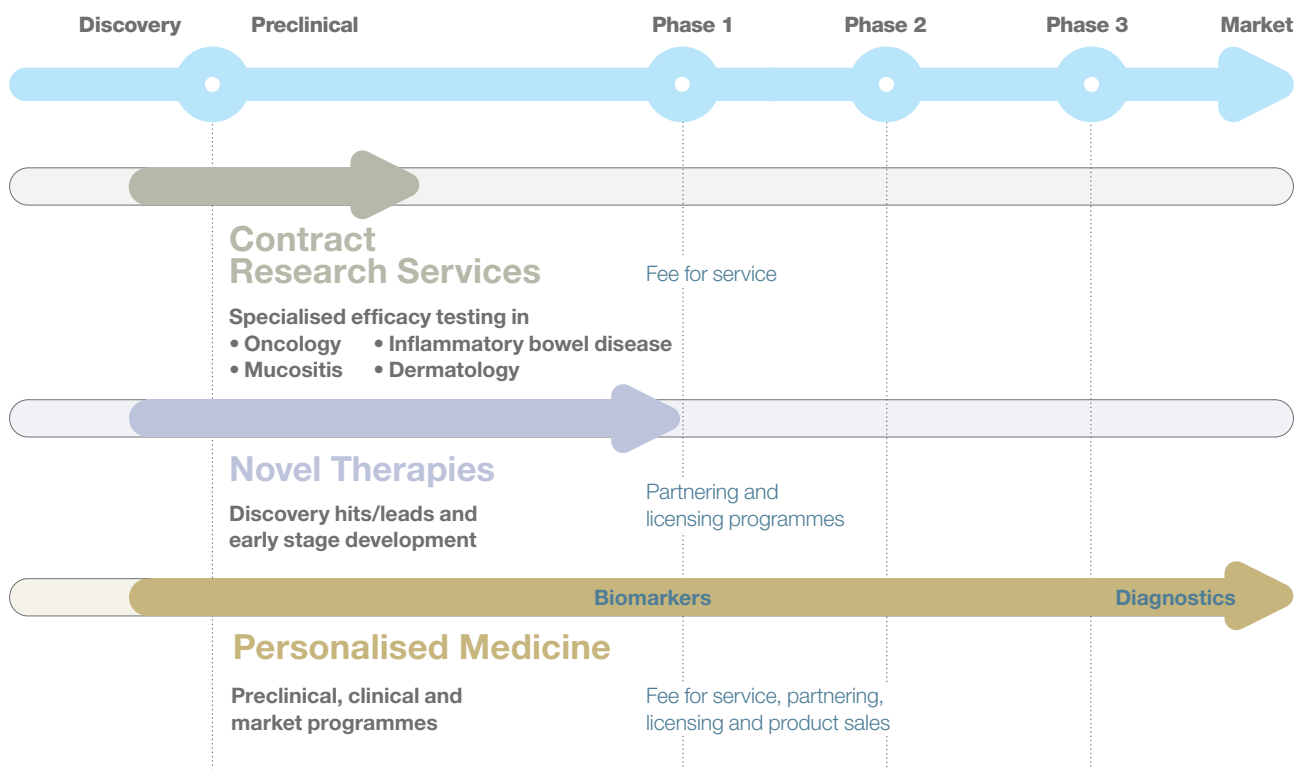
Our Business and Strategy

A strengthening business model based on sustaining future growth

Epistem has an unrivalled knowledge of epithelial tissue behaviour and an extensive array of stem cell assays, which is increasingly a key consideration in the development of new epithelial drugs.

Epistem has also developed an innovative library of oncology biomarkers which coupled with our advance into disease diagnostics will build a leading position in personalised medicine.

Future Strategy





Combined business model

Epistem's combined business model has now yielded a profitable and growing business across each of our three business divisions. The Contract Research Services business has established robust relationships with pharmaceutical and biotechnology leaders worldwide and these relationships and our wide-ranging stem cell services have provided the basis for partnering strategies for our emerging Novel Therapies and Personalised Medicine businesses.

Partnering programme

We continue to work closely with our partners and customers to build strong business relationships based on leading scientific discovery and development. In addition to our first major collaboration with Novartis, we are now nurturing other relationships to advance our emerging hits/leads.

Licensing opportunities

The strength of our discovery platform underpinning the Company's Novel Therapies division continues to grow and this is partly reflected in the number of potential drug candidates which the Company has now identified. These candidates are undergoing development to drive Epistem's emerging drug development pipeline.

Epistem's new Personalised Medicine division expands on last year's newly formed Biomarker division to advance a new 'Point of Care' diagnostic device. We will continue to maintain our strong intellectual property position in this area and develop our deepening understanding of drug effect biomarkers and disease diagnosis.

Strategic Goals:

Growth:

We expect to deliver sustained revenue growth and increased visibility and awareness of the Company and its achievements over the forthcoming year.

Technical:

We will continue to exploit our core stem cell expertise and build industry recognition around our stem cell science and gene expression technology. We will advance new product developments, Personalised Medicine partnerships and therapeutic leads to underpin our continued commercial success.

Financial:

Continued revenue growth over the coming year is anticipated with accelerated commercial delivery across all of our divisions. Our combined business model will continue to strengthen and our portfolio will enable us to accelerate investment across the Group and consider acquisition opportunities where appropriate.

Investor:

Continued development across each of our business divisions offers an increasingly attractive investment opportunity for both our existing and new investors. The impressive revenue growth across each of our divisions alongside increasing forecast revenues and growing profitability demarks Epistem as an exciting growth stock with significant potential upside.

Strength in Depth

Epistem continues to expand its technology offering, to maintain a high rate of growth and profitability

The 2009/10 financial year saw Epistem continue its rapid growth with year-on-year sales up 45%.

Highlights

- Year-on-year sales up 45% to £5.7m
- All divisional revenues increased over the year
- Contract Research Services operating profit up 28%
- Expansion of Biomarker division to form new Personalised Medicine division
- Group operating profit up at £0.3m from a loss of £(0.7)m
- Strengthened cash balance with improved trading outlook

Market dynamics

International market conditions remained challenging during the year with the healthcare sector continuing to pursue merger and ongoing rationalisation. The Company has continued its strategy of focusing on bringing new globally leading technology to market whilst driving organic growth and cash generation.

Group revenues

2010	£5.7m
2009	£4.0m

Against a challenging economic background, Epistem's year-on-year consolidated revenues increased 45% to £5.7m. Each division recorded increased revenues over the previous year. Territory revenues were split US 79%, EU 14% and UK 7%.

2010
£5.7m

Contract Research Services revenues

2010	£2.5m
2009	£2.3m

The CRS division reports sales of £2.5m, a 10% increase over the previous year. The division saw increased demand for its oncology and mucositis service offerings along with expansion in the US NIH biodefence contract.

2010
£2.5m

Personalised Medicine and Novel Therapies revenue

2010	£3.2m
2009	£1.7m

Strong growth driven primarily by the Novartis collaboration together with Biomarker revenues helped sales rise significantly over the year.

2010
£3.2m

Discovery, development and admin cost

2010	£2.7m
2009	£2.2m

Investment in our Novel Therapies drug discovery and development programme accounted for £1.4m of the 2010 reported figure with the remaining £1.3m cost relating to central business overheads and administrative operating costs.

2010
£2.7m

Profit before tax

2010	£0.4m
2009	£(0.7)m

Profit before tax for the period was underpinned by a £1.1m profit improvement from a loss of £(0.7)m to £0.4m.

2010
£0.4m

Cash reserves

2010	£5.4m
2009	£3.7m

Cash reserves were strengthened over the year by the successful placing of shares in November 2009.

2010
£5.4m

Chairman's Statement

David Evans Non-executive Chairman



Dear Shareholder,

I am delighted to report significant growth and ongoing improvement in Epistem's results for the year ended 30 June 2010.

Whilst market and trading conditions have remained volatile, the Company continues to invest in and strengthen its foundations and enjoyed a further exceptional year in difficult times.

Results

Further details of the results for the period are covered in the Chief Executive Officer's review, but operationally and financially the year to 30 June 2010 saw the Company increase revenues by 45% to £5.7m (2009: £4.0m) with a Group profit on ordinary activities before taxation of £0.4m (2009: Loss £0.7m). Based on this improved trading performance the Company generated an after tax profit of £0.3m (2009: £0.1m). Cash reserves at the end of the period were £5.4m (2009: £3.7m).

‘Strengthening foundations in preparation for continued growth’

During the year the Company continued to make significant progress across each of its divisions:

- Contract Research Services revenues grew by 10% to £2.5m (2009: £2.3m). The extension of our service offerings and continued expansion of our US government bio-defence contract enabled the division to deliver a solid performance over the year. With market uncertainties still persisting, the division continues to build on its core scientific strengths to provide a firm platform for future growth.
- Biomarker revenue growth was marginally increased over the year at £0.8m (2009: £0.7m), though this masked the significant effort underway to position the division for future growth. As part of our growth strategy to continue to develop this arm of the business whether through the addition of new technologies or through M&A, we are today announcing the creation of our Personalised Medicine division which expands on our Biomarker technology to provide a newly created ‘Point Of Care’ offering and the unveiling of our ‘on the spot’ molecular diagnostic platform Genedrive™.
- The Novel Therapies division research and development collaboration with Swiss based Novartis AG continued to develop over the year with the division reporting its first full year revenue of £2.4m (2009: £1.0m). New drug targets are continuing to emerge, with the Novel Therapies division positioning itself to create a pipeline of early stage development targets. The timings of license opportunities and future development funding though remains difficult to accurately predict.
- Strengthened investor relations continue to advance the visibility of the Company, with the £2.9m placing in November 2009 bringing several new institutional investors to the share register.
- The Company now reports its second year of profits and a growth in its earnings per share to 3.8p (2009: 1.1p).

Outlook

Epistem continues to build on its scientific and technical strengths as it transforms into a diverse, technology leading, and profitable biotechnology and personalised medicine group underpinned by strong revenue growth. Against a backdrop of market uncertainty, Epistem remains vigilant, with the outlook for the expanding group increasingly positive.

Despite the tough market conditions, each divisional business is establishing itself for growth in its chosen segment. The Contract Research Services division buoyed by the expansion and anticipated extension of the US biodefence contract is expected to perform well over the coming year, with the newly formed Personalised Medicine division and its disruptive biomarker and diagnostic technologies providing further support for Epistem’s future growth. The Novel Therapies drug discovery collaboration with Novartis is nearing completion of its first phase, with the emergence of a newly formed group of identified hits/leads. Whilst the timing of license and development opportunities remains difficult to judge, we remain optimistic about the growing strength of our hit/lead programme. Epistem continues to refine its discovery and development technology to position itself as a world leader in therapeutic discovery in the field of epithelial stem cell regulation. With the profile and visibility of each of our business divisions increasing, we expect to see the Company advance quickly over the coming year.

I would like to thank the Chief Executive Officer for his leadership and navigation of the Company during these difficult times. I would also like to thank the Board and our employees for their effort and commitment in driving Epistem’s progress over the past year, as well as our investors whose valued support has provided a stable platform for our continued growth.

David Evans

Non-executive Chairman
5 October 2010

Chief Executive's Review

Matthew Walls Chief Executive Officer



Dear Shareholder,

Against the backdrop of changing times and economic uncertainty, Epistem continues to make excellent progress in building itself into a globally recognised Drug Discovery and Personalised Medicine company.

The financial results for the Group presented in this announcement reflect the results for the Group's sole trading subsidiary for the year to 30 June 2010 and for the comparative period to 30 June 2009.

Headline progress over the year included:

- Year-on-year net sales up 45%.
- The Company reports its second year of profit growth and an increase in earnings per share.
- Novel Therapies sales increased to £2.4m, £1.4m increase over the previous year.
- Biomarker sales increased 19% year-on-year and now forms part of the newly created Personalised Medicine division.
- Development of our new Genedrive™ 'Point of Care' mobile molecular diagnostic device.
- Contract Research sales increased by 10% over the previous year.
- A strengthened cash balance of £5.4m and improved trading outlook.

‘Divisional growth and globally leading technology’

Integrated business model

The Company continues to progress its integrated business model, with each division targeting revenue growth and profitability. The establishment of independent divisions has created a strong portfolio of growing and profitable business units rarely seen in a biotechnology business model. Epistem provides a financially robust business, whilst offering the potential of significant financial upside from our Novel Therapies, Personalised Medicine and Contract Research Services divisions. We continue to enhance and exploit our integrated core competence in epithelial cell biology, whilst retaining commercial independence across each of our divisions.

Financial review

The Company reports a turnover of £5.7m (2009: £4.0m) for the year ended 30 June 2010. Revenues were underpinned by the Contract Research Services division, which delivered sales of £2.5m (2009: £2.3m) a 10% year-on-year growth. The Biomarker division (now forming part of the Personalised Medicine division) saw sales marginally increased to £0.8m (2009: £0.7m), with the Novel Therapies division reporting increased sales of £2.4m (2009: £1.0m).

Consolidated territory revenues were split US 79% (63%), EU 14% (19%) and UK 7% (18%), the US territory figures continue to be strengthened by our US government and Novartis collaborations and represents a major growth market for the Company.

Sales growth in Contract Research Services delivered a 28% increase in operating profit of that division, with operating profit up to £0.7m (2009: £0.6m). Increased Biomarker sales were partly offset by

growing investment in our Biomarker and Diagnostics developments and the set up of our new US Biomarker operations to record a small loss for the year. Novel Therapies reported a significant increase in operating profit of £1.0m (2009: Loss £0.2m) driven by a full year's funding of £1.0m from the Novartis collaboration and £1.4m revenue recognition from the up-front payment which is being spread over the length of the contract. Central administration costs increased by £0.2m to £1.3m (2009: £1.1m) primarily due to increased staff costs and professional fees.

The Groups reported profit for the year was £0.3m (2009: £0.1m) with headcount in the company now at 51 (2008: 45).

Cash reserves at the end of the year were £5.4m (2008: £3.7m) benefiting from improved trading and funding from the November 2009 £2.9m placing.

Earnings per share increased to 3.8p per share (2009: 1.1p).

Clear investor communication of the Company's strategy and performance remains a key element of our success and we will continue to strengthen communications as we embark upon our next phase of growth.

The Company's annual audit was completed in October 2010 by HW Chartered Accountants, and their audit report is included in the annual accounts.

2000

Company formation

Company sets up Contract Research Services group.

2002

Drug discovery

Commencement of research into epithelial stem cell regulators.

2004

New disease models

Company announces new models in inflammatory bowel disease.

2005

Fundraising

Epistem closes £2.0m fundraising.

2007

LSE: AIM Admission

Successful IPO and AIM Admission April 2007.

'Building shareholder value by providing a high margin, diverse and rapidly growing portfolio of world class technologies'

Operating review

Contract Research Services

Over the financial year, Contract Research Services delivered a 10% year-on-year growth in revenue. Whilst market conditions remained challenging, our specialist preclinical services continued to expand and develop its business mainly with the larger pharmaceutical/ Biotechnology groups.

Revenue increases were seen in our major US and EU markets, with the UK territory now representing the smallest territory in terms of revenue generation. Interestingly, only 4 years ago, the UK had been our major market. Our mucositis and inflammatory bowel disease models showed the greatest gain over the year supported by our new assays and technical developments. Our new client relationships and aggregate contract values also continued their trend of year-on-year increase over the year.

The US National Institutes of Health's biodefence programme continues to make good progress and continues to expand marking a significant milestone in our tests for agents which may treat radiation sickness following a nuclear incident. We enjoy a business relationship with the US biodefence group which is based on many years of close working and we expect this to continue over the forthcoming years.

A solid start to the new financial year and our focus on specialist testing of preclinical drug compounds in our core disease areas continues to provide an attractive business model from which we anticipate further growth over the coming year.

Personalised Medicine

Following last year's formation of the Biomarker division, we have now expanded our Diagnostic assay developments alongside our Biomarker technology to create a new 'Personalised Medicine' division. The oncology Biomarker business saw continued revenue growth over the year and the set up of the new US Biomarker office.

We anticipate that US business expansion will continue to underpin our business development with the division poised to accelerate its revenue generation over the coming year. Our hair biomarker continues to engage with a growing customer base and provides a powerful measure of drug-induced gene expression for use in pre-clinical and clinical studies. Use of our technology to identify drug induced oncology genes (oncogenes) in molecular pathways is driven by the regulatory authority requirements to show that developmental drugs are effectively targeting these oncogenes. Our highly sensitive amplification technology, RNA-Amp™ which underpins our Biomarker technology has also recently been launched in a simple to use kit form.

We are also unveiling our new Genedrive™ 'Point Of Care' (POC) molecular diagnostic device for 'on the spot' patient diagnosis. Genedrive™ is a unique, mobile and proprietary electronic device which targets a rapid molecular diagnostic assessment (sub 30 mins) for use in clinics, hospitals, surgeries as well as lending itself to OTC opportunities. The device is expected to have other marketing opportunities in veterinary, food and industrial use. We expect the device to bring a new 'standard of care' to the rapid diagnosis of pathogens and other molecular diseases.

Whilst technical and development risks may still arise around each of our platforms, over time these continue to reduce. Validation of the new Genedrive™ system is now underway, with beta site clinical testing expected to start towards the end of this year with the launch of the device anticipated in the first half of next year.

The Personalised Medicine market is forecast to grow considerably over the next few years driven by effective patient treatment, increasing regulatory requirements and patient specific drug development and our platform technologies are well positioned to capitalise on this market growth.



2008

Biomarker

Epistem creates new Biomarker division.

2009

Discovery collaboration

Epistem enters research and development collaboration with Novartis AG.

Placing

Epistem completes £2.9m share placing.

2010

March

10 year anniversary.

July

Epistem reports 2nd year of profitable growth.

Novel Therapies

The Novel Therapies collaboration with Novartis is now in its second year and we are seeing the emergence of the first hits/leads from the Regenerative Medicine programme. Whilst these hits/leads are still at the discovery stage, the core cell biology and signalling pathways which regulate the cell/stem cell are becoming clearer and better understood as we identify which genes and pathways regulate specific characteristics of the cell. Our relationship with Novartis remains strong and we will be advancing each of our hit/leads under the collaboration over the coming year as we move into the next phase of development. Despite our confidence in the collaboration programme, the timing of potential licenses and future funding remains difficult to judge with accuracy. With the first phase of the discovery collaboration now nearing completion, discussions around the second phase of hit/lead development and future licensing/funding will continue into next year.

Aside from the Novartis collaboration, we have also commenced a focused small molecule programme to establish our own proprietary agents which regulate the signalling pathways and biology of the cell. This will allow us to develop our own drug leads and reinforce our lead position in the regulation of epithelial cells and stem cells, focused in the disease areas of regenerative medicine and oncology.

We will continue to evaluate our other drug discovery and development opportunities with the major industry players over the forthcoming year to identify new lead developments and to expand our discovery and early stage development platform.

Current trading and outlook

Epistem continues to diversify its portfolio of business opportunities and strengthen its technology whilst maintaining profitable and sustainable growth. The past year has seen further strong operational and financial development across each of our divisions with each division developing its own independent strategy for growth.

Trading in the first three months of the new financial year continues strong with revenues 15% ahead of the comparative period last year.

The next phase of Epistem growth will continue to strengthen and build on each of our divisional operations. We continue to supplement our management team with world class, innovative individuals who fit with the culture and dynamism of the Company. We will also build on our corporate and board strength and supplement our scientific advisory board and advisory committees as appropriate.

Our shareholder interest and support remains strong and we will ensure that our ongoing investor communications continue to grow this relationship.

A strengthening operational and financial position confirms our belief that the year ahead will continue to generate substantial increases in our forecast revenues and growth ambitions. We remain selective in considering complementary technology, acquisitions and in-licensing, with few opportunities thus far meeting our high expectations. We continue to remain vigilant in our outlook in these uncertain times.

Our ambition remains firmly fixed on building shareholder value by providing a high margin, diverse and rapidly growing portfolio of world class technologies.

I would like to thank the Board, management and employees for their outstanding performance over the past year. I would also like to thank our investors for their continued close support and interest in our exciting and rapidly growing Company.

Matthew H Walls

Chief Executive Officer
5 October 2010

Board of Directors

1. David Evans (50)

Non-executive Chairman

David joined Epistem as a Non-executive Director in June 2005 and became Executive Chairman in March 2006 until the flotation in April 2007, when he reverted to a non-executive position. David, a qualified accountant, has many years' experience both as an executive and as a non-executive of publicly listed diagnostic and life science companies. In addition to his chairmanship of Epistem, he is currently Non-executive Chairman of the following AIM listed companies: Immunodiagnostic System Holdings plc, Omega Diagnostics Group plc and Scancell Holdings Plc.

2. Matthew Walls (46)

Chief Executive Officer

Matthew joined Epistem in February 2007 as Chief Executive Officer. He is an experienced CEO, most recently with Oxford Biosignals Limited, where he led the strategic collaboration with Rolls-Royce Plc and Covance Inc. Matthew spent the early part of his career with ICI Plc, progressing through to AstraZeneca Plc prior to its plant crop biotechnology group merger with Novartis to form Syngenta Plc. Matthew has led the growth of several technology and biotechnology companies as CEO, including Internexus Limited and Zylepsis Limited. He holds a non-executive post at Continuum Limited and Riyadh Oxford Investments Limited and is a chartered accountant and a member of CIMA.

3. John Rylands (55)

Financial Director

John originally joined Epistem as an investor and Non-executive Director, and in 2005 took over his current role. John provided corporate finance advice to private companies before joining Epistem. Until 1999 he was an investor in and consultant to the SDS group of companies. John holds a degree in Economics and Accountancy from Manchester University and is a member of ICAEW.

4. Jeffrey Moore, Ph.D. (51)

Managing Director, Novel Therapies

Jeffrey joined Epistem in 2005 in his current role. Prior to joining Epistem he had been at Phylogix, a US biotechnology company which he founded in 1998. Jeffrey has held two postdoctoral fellowships, at DNAX Research Institute of Molecular and Cellular Biology Inc and the Walter and Eliza Hall Institute of Medical Research, following which he joined Imclone Systems Inc. Throughout his career, Jeffrey has kept a strong interest in stem cell regulation and in identifying the potential commercial application of these factors. He holds a Ph.D. from George Washington University.

5. Prof. Chris Potten (69)

Chief Scientific Adviser

Chris is a co-founder of Epistem and the Company capitalises on the results of the research that was produced by him and his team at the Paterson Institute over the past three decades. Chris acts as Chief Scientific Adviser to the Company, although he does not participate in the day-to-day management of the Company. Chris retains a strong interest in the progress and success of the Company and prior to Epistem's AIM listing was its biggest individual shareholder.

6. Catherine Booth, Ph.D. (45)

Managing Director, Contract Research Services

Catherine is a co-founder of Epistem and prior to starting Epistem, she worked for ten years with Prof. Chris Potten at the Paterson Institute. Whilst at the Paterson Institute, she developed many pre-clinical assays. This knowledge is at the core of the Epistem Contract Research Service. Catherine received her Ph.D. from Emmanuel College, University of Cambridge.

7. Gerard Brady, Ph.D. (54)

Research Director

Gerard joined Epistem shortly after its inception from Manchester University, where he was a lecturer, and was previously a Zeneca Fellow. He brought with him important technological expertise gained through working on blood stem cells. Of particular importance to Epistem, is his expertise in single cell gene analysis, which enables the examination of rare cells such as stem cells. Gerard previously held scientific positions in Canada and at EMBL, Heidelberg.

8. Robert Nolan, Ph.D. (67)

Non-executive Director

Robert has been a Non-executive Director of the Company since 2004. He brings with him a wealth of expertise in partnering and licensing negotiations with both small biotechnology and large pharmaceutical companies. Prior to his retirement he was Director, Global Licensing, at AstraZeneca Plc. He is also a Non-executive Director of Phico Therapeutics Ltd.

9. Roger Lloyd, Ph.D. (62)

Non-executive Director

Trained as a biochemist, Roger has almost 35 years' experience in the healthcare and biotechnology sector, particularly in the areas of strategic planning and business development. International business management with ICI Plc and AstraZeneca Plc included living and working in the US and Germany, and having territorial responsibilities for Europe, Japan, Korea, Mexico and the Middle East. As Executive Director of Global Licensing at AstraZeneca, he personally completed 24 transactions, including strategic alliances with Abgenix and CAT, and acquisitions of KuDOS Pharmaceuticals and CAT. He operates as a Board Adviser in the biotech sector.

Directors' Report

For the year ended 30 June 2010

The Directors present their report for Epistem Holdings Plc (the Company) and its subsidiaries (together Epistem or the Group) for the year ended 30 June 2010.

Principal activities and review of the business

The principal activity of the Group during the year was the provision of services to the biotechnology and pharmaceutical industries, covering pre-clinical testing and gene biomarker services and the development of novel therapeutics for partner companies. The trading activities of the Group are currently principally undertaken in the subsidiary undertaking, Epistem Limited, and a detailed overview of these activities is outlined in the Business Overview on the inside front cover to page 11 of this report. During the year, the Group established a US business development office in Boston, MA, trading through its wholly owned subsidiary Epistem Inc., incorporated during the year.

A review of the business during the year which summarises overall progress, research and development and Key Performance Indicators, as well as risks and developments is detailed in the Business Overview and Review of the Year on the inside front cover of this report.

Results and dividends

The trading results for the year and the Group's financial position at the end of the financial year are shown in the Financial Statements on pages 29–51 of this report.

The Directors do not recommend payment of a final dividend.

Going concern

After due consideration, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Directors and their interests in shares

The Directors of the Company who held office throughout the year, unless otherwise stated, and their interests in the share capital of the Company, including family and pension scheme trust interests, were as follows:

	1 July 2009	30 June 2010
David Evans	80,645	80,645
Chris Potten	919,320	519,320
Catherine Booth	980,419	981,538
Gerard Brady	419	1,538
Roger Lloyd	–	–
Jeffrey Moore	14,919	16,038
Robert Nolan	8,065	8,065
John Rylands	190,317	191,436
Matthew Walls	6,064	7,183

Significant shareholdings

In addition to the Directors' holdings, the Company has been advised of the following interests of over 3% of the issued ordinary shares:

	Ordinary shares	Percentage holding
Managed by Calculus Capital Ltd	947,707	11.9%
Helium Special Situations Fund	807,500	10.2%
Gartmore Investments Limited	605,000	7.6%
Generali Finances	400,000	5.0%
Northwest Business Investment Scheme	294,780	3.7%

Policy on payments to suppliers

It is the policy of the Company in respect of all of its suppliers, where reasonably practicable, to settle the terms of payment with those suppliers when agreeing the terms of each transaction, to ensure that those suppliers are made aware of the terms of payment, and to abide by those terms. The Group has complied with this policy during the year. The average number of creditor days for the Group was 83 (2009: 66) based on the average daily amount invoiced by suppliers during the year.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the 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 Financial Statements in accordance with International Reporting Standards (IFRSs) as adopted by the European Union.

In preparing those Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make suitable judgements and estimates that are reasonable and prudent;
- state that the Financial Statements comply with IFRSs as adopted by the European Union, subject to any material departures being adequately disclosed and explained; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors confirm that they have complied with the above requirements in preparing the Financial Statements.

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 Group and enable them to ensure that the Financial Statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of Financial Statements may differ from legislation in other jurisdictions.

Principal risks

The Board meets regularly to review operations and to discuss risk areas. The Review of the Year on pages 12–19 reports on the factors which are key to the ongoing development of the Company. The Corporate Governance Report contains details of the Group's system of internal control. Details of the financial risks are disclosed in Note 19 to the Financial Statements.

Provision of information to auditors

The Directors who were members of the Board at the time of approving the Directors' Report are listed on pages 20 and 21. Having made enquiries of fellow Directors and of the Group's auditors, each of these Directors confirms that:

- to the best of each Director's knowledge and belief, there is no information (that is information needed by the Group's auditors in connection with preparing their report) of which the Group's auditors are unaware; and
- each Director has taken all the steps that a Director might reasonably be expected to be taken to be aware of relevant audit information and to establish that the Group's auditors are aware of that information.

Approved by the Board

H J J Rylands

Company Secretary
5 October 2010

Directors' Remuneration Report

For the year ended 30 June 2010

Introduction

This report has been prepared in accordance with the requirements of Schedule 2 Pt1 to the Companies Act 2006 (the Schedule) and also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the Principles of Good Governance relating to Directors' Remuneration. In accordance with Section 439 of the Companies Act 2006 (the Act), a resolution to approve the report will be proposed at the Annual General Meeting of the Company at which the Financial Statements are to be approved.

Section 495 of the Act requires the auditors to report to the Company's members on the 'auditable part' of the Directors' Remuneration Report and to state whether, in their opinion, that part of the report has been properly prepared in accordance with Part 3 of the Schedule. This report has therefore been divided into separate sections for unaudited and audited information.

Unaudited information

Remuneration policy

Executive remuneration packages are prudently designed to attract, motivate and retain Directors of the necessary calibre and to reward them for enhancing value to shareholders. The performance measurement of the Executive Directors and key members of senior management and the determination of their annual remuneration package is undertaken by the Remuneration Committee. The remuneration of the Non-executive Directors is determined by the Board within limits set out in the Articles of Association.

Executive Directors are entitled to accept appointments outside the Company providing the Board's permission is sought.

Non-executive Directors' terms of engagement

The Non-executive Directors have specific terms of engagement. Their remuneration is determined by the Board. In the event that a Non-executive undertakes additional assignments for the Company, the Non-executive's fee will be agreed by the Company in respect of each assignment.

Audited information

Aggregate Directors' remuneration

	Salary & fees £	Bonus £	Pension £	2010 Total £	2009 Total £
Executive					
Catherine Booth	118,644	15,000	7,169	140,813	133,667
Gerard Brady	115,000	–	–	115,000	121,667
Jeffrey Moore	125,000	15,000	–	140,000	147,667
John Rylands	115,000	15,000	–	130,000	121,667
Matthew Walls	200,000	100,000	–	300,000	300,000
Non-executive					
David Evans	34,992	–	–	34,992	25,000
Chris Potten	43,943	–	–	43,943	64,029
Roger Lloyd	24,000	–	–	24,000	24,000
Robert Nolan	24,000	–	–	24,000	24,000
	800,579	145,000	7,169	952,748	961,697

Directors' share options

Details of the options for Directors who served during the year are as follows:

	As at 1 July 2009	Options granted	As at 30 June 2010	Exercise price	Earliest exercise date	Expiry date
Executive						
Catherine Booth ⁽²⁾	15,528	–	15,528	£1.20	Exit	09/01/2016
Gerard Brady ⁽²⁾	88,800	–	88,800	£0.50	Exit	06/01/2012
Gerard Brady ⁽²⁾	3,200	–	3,200	£0.75	Exit	30/03/2013
Gerard Brady ⁽²⁾	2,200	–	2,200	£0.75	Exit	06/04/2013
Gerard Brady ⁽²⁾	1,800	–	1,800	£0.75	Exit	20/07/2014
Gerard Brady ⁽²⁾	24,224	–	24,224	£1.20	Exit	24/11/2015
Gerard Brady ⁽²⁾	12,653	–	12,653	£1.67	Exit	27/07/2017
Gerard Brady ⁽⁴⁾	57,727	–	57,727	£1.60	15/10/2010	15/10/2017
Jeffrey Moore ⁽³⁾	83,333	–	83,333	£1.20	04/04/2007	09/01/2016
Jeffrey Moore ⁽¹⁾	100,000	–	100,000	£1.20	04/04/2007	09/01/2016
Jeffrey Moore ⁽¹⁾	83,333	–	83,333	£1.20	01/09/2007	09/01/2016
Jeffrey Moore ⁽¹⁾	83,333	–	83,333	£1.20	01/09/2008	09/01/2016
John Rylands ⁽³⁾	83,333	–	83,333	£1.20	04/04/2007	09/01/2016
John Rylands ⁽¹⁾	127,847	–	127,847	£1.20	04/04/2007	09/01/2016
Matthew Walls ⁽⁵⁾	177,653	–	177,653	£1.24	31/10/2010	27/03/2017
Matthew Walls ⁽⁶⁾	80,644	–	80,644	£1.24	31/10/2010	27/03/2017
Non-executive						
David Evans ⁽¹⁾	62,112	–	62,112	£1.20	04/04/2007	09/01/2016
Robert Nolan ⁽¹⁾	78,000	–	78,000	£1.29	31/05/2005	30/03/2015
Robert Nolan ⁽¹⁾	15,528	–	15,528	£1.20	10/01/2006	09/01/2016
Chris Potten ⁽²⁾	15,528	–	15,528	£1.20	Exit	09/01/2016

1. Unapproved stand-alone agreement, no performance criteria.
2. EMI Company scheme, no performance criteria.
3. EMI stand-alone scheme, no performance criteria.
4. EMI and Unapproved stand-alone scheme, with performance criteria which require the Board to determine whether certain identified technical developments have been completed.
5. EMI and Unapproved stand-alone scheme, with performance criteria which allow the options to vest (i) when the audited accounts for the year ended 30 June 2010 become available and (ii) when the earnings per share of the financial year are a positive figure.
6. EMI stand-alone scheme, with performance criteria as detailed in (5) above.

Share Investment Plan

The details of the Epistem Share Investment Plan are outlined in Note 18(b) to the accounts. The Directors' interests in the shares of the Company include shares acquired under the Share Investment Plan as follows:

	Partnership shares No.	Cost of matching shares £	Total matching shares No.	Total SIP shares 30 June 2010 No.	Total SIP shares 30 June 2009 No.
Catherine Booth	512	2,991	1,026	1,538	419
Gerard Brady	512	2,991	1,026	1,538	419
Jeffrey Moore	512	2,991	1,026	1,538	419
John Rylands	512	2,991	1,026	1,538	419
Matthew Walls	512	2,991	1,026	1,538	419

Approved by the Board

D Evans

Non-executive Chairman
5 October 2010

Corporate Governance Report

For the year ended 30 June 2010

The Group is subject to the continuing requirements of the AIM Rules and is committed to adhering to corporate governance standards appropriate for a company of its size. The Group follows the Quoted Companies Alliance guidelines and has Remuneration, Audit and Nominations committees with written terms of reference and a schedule of matters reserved for the Board, which generally meets each month.

The Board has established an Audit Committee, a Remuneration Committee and a Nominations Committee. The membership of these committees and attendance at meetings is as follows:

	Audit Committee	Remuneration Committee	Nominations Committee
David Evans (Non-executive Chairman)	3	3	1
Robert Nolan (Non-executive Director)	3	3	1
Roger Lloyd (Non-executive Director), Remuneration and Nominations Committees only	N/A	3	1

Remuneration Committee

The Remuneration Committee will review the scale and structure of the Executive Directors' and senior management's remuneration and the terms of their service contracts. The remuneration and terms of appointment of the Non-executive Directors will be set by the Board. The Remuneration Committee will also approve the issue of share options under schemes approved by the Board.

None of the Committee have any personal financial interest (other than as shareholders), conflicts of interest arising from cross-directorships, or day-to-day involvement in the running of the business. No Director plays a part in any discussion about his or her own remuneration.

Audit Committee

The Audit Committee has responsibility for receiving accounts and reviewing reports from the management and the Company's auditors, relating to Annual and Interim Accounts and the accounting and internal controls in place throughout the Group. At this stage of the Group's size and development, the Committee has decided that an internal audit function is not required as the Group's internal controls system in place is appropriate for its size. The Audit Committee has met three times during the year.

Nominations Committee

The Nominations Committee has responsibility for reviewing the size, structure and composition of the Board, as well as retirements and appointments of replacement and additional Directors, and for making appropriate recommendations to the Board.

Relations with shareholders

The Group recognises the importance of communicating with its shareholders to ensure that its strategy and performance is understood and that it remains accountable to shareholders. The Board as a whole is responsible for ensuring that a satisfactory dialogue with shareholders takes place, while the Chairman and Chief Executive ensure that the views of the shareholders are communicated to the Board as a whole. The Board ensures that the Group's strategic plans have been carefully reviewed in terms of their ability to deliver long-term shareholder value.

Internal controls

The Board acknowledges its responsibility for establishing and maintaining the Group's system of internal controls and will continue to ensure that management keeps these processes under regular review and improves them where appropriate. The system of internal controls is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss.

Social, environmental and ethical matters

The Board recognises the growing awareness of social, environmental and ethical matters and it endeavours to take into account the interests of the Group's stakeholders, including its investors, employees, suppliers and business partners, when operating the business.

Employment

At a subsidiary level the individual company has established policies which address key corporate objectives in the management of employee relations, communications and employee involvement, training and personal development and equal opportunities.

Health, safety and environmental issues

The Board recognises its legal responsibilities to ensure the well-being, safety and welfare of its employees and to maintain a safe and healthy working environment for them and for its visitors and subcontractors. Health and Safety is on the agenda for regularly scheduled Board meetings.

By their nature, the Group's regular operations are judged to have a low environmental impact and are not expected to give rise to any significant inherent environmental risks over the next twelve months.

The Group is committed to maintaining high standards in implementing appropriate health, safety and environmental protection policies. The Group has an excellent health and safety record. Waste materials are recycled where appropriate, and hazardous waste is catalogued and handled by licensed specialist disposal companies.

Independent Auditors' Report to the Members of Epistem Holdings Plc

For the year ended 30 June 2010

We have audited the group and parent company Financial Statements (the Financial Statements) of Epistem Holdings Plc for the year ended 30 June 2010 which comprise the group income statement, the group and parent company balance sheets, the group and parent company cash flow statements, the group and parent company statements of changes in equity 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's Financial Statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

As explained more fully in the Statement of Directors' responsibilities set out in the Directors' Report 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 the Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). These standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

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 the parent company's circumstances and have been consistently applied and adequately disclosed; and
- the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the Financial Statements.

Opinion on the Financial Statements

In our opinion:

- the Financial Statements give a true and fair view of the state of the group's and the parent company's affairs as at 30 June 2010, and of the group's profit 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 the IFRSs as adopted by the European Union and as applied in accordance with the requirements of the Companies Act 2006; and
- the Financial Statements have been prepared in accordance with the requirements of Companies Act 2006 and as regards the group Financial Statements, Article 4 of the IAS regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- 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:

Under the Companies Act 2006, we are required 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 and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures or directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we required for our audit.

Independent Auditors' Report to the Members of Epistem Holdings Plc

(continued)

Under the Listing Rules we are required to review:

- the Directors' statement, set out in the Directors' Report, in relation to going concern; and
- the part of the Corporate Governance Statement relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Carol Graham FCA
(Senior Statutory Auditor)

For and on behalf of:

HW

Chartered Accountants & Statutory Auditors

Bridge House

157 Ashley Road

Hale

Altrincham

Cheshire

WA14 2UT

25 October 2010

Consolidated Statement of Comprehensive Income

For the year ended 30 June 2010

	Notes	2010 £'000	2009 £'000
Revenue	2	5,740	3,968
Contract costs		(2,697)	(2,424)
Discovery and development costs		(1,433)	(1,131)
General administrative costs		(1,298)	(1,114)
Operating profit/(loss)	3	312	(701)
Finance income	6	40	41
Finance costs	6	(2)	(9)
Profit/(loss) on ordinary activities before taxation		350	(669)
Taxation on ordinary activities	7	(60)	752
Total comprehensive income for the financial year		290	83
Earnings per share (pence)			
– Basic	9	3.8p	1.1p
– Diluted	9	3.3p	1.0p

All of the activities of the Group are classed as continuing.

The Company has taken advantage of section 408 of the Companies Act 2006 not to publish its own income statement.

Consolidated Statement of Changes in Equity

For the year ended 30 June 2010

	Equity share capital £'000	Share premium account £'000	Employee share incentive plan reserve £'000	Share options reserve £'000	Reverse acquisitions reserve £'000	Retained earnings £'000	Total equity £'000
Balance at 1 July 2008	108	8,437	–	547	(2,484)	(4,026)	2,582
Allotment of ordinary shares	–	24	–	–	–	–	24
Exercise of options	–	6	–	(6)	–	–	–
Lapse of options	–	–	–	(6)	–	6	–
Recognition of equity-settled share-based payments	–	–	–	71	–	–	71
Total comprehensive income for the year	–	–	–	–	–	83	83
At 30 June 2009	108	8,467	–	606	(2,484)	(3,937)	2,760
Balance at 1 July 2009	108	8,467	–	606	(2,484)	(3,937)	2,760
Allotment of ordinary shares	11	2,873	–	–	–	–	2,884
Share issue costs	–	(135)	–	–	–	–	(135)
Purchase of own shares (SIP)	–	–	(43)	–	–	–	(43)
Exercise of options	–	1	–	(1)	–	–	–
Recognition of equity-settled share-based payments	–	–	–	28	–	–	28
Total comprehensive income for the year	–	–	–	–	–	290	290
At 30 June 2010	119	11,206	(43)	633	(2,484)	(3,647)	5,784

Consolidated Balance Sheet

As at 30 June 2010

	Notes	2010 £'000	2009 £'000
Non-current assets			
Intangible assets	10	135	139
Plant and equipment	11	608	465
Deferred taxation	12	536	594
		1,279	1,198
Current assets			
Trade and other receivables	13	1,011	820
Tax receivables		150	150
Cash and cash equivalents	14	5,371	3,748
		6,532	4,718
Liabilities			
Current liabilities			
Deferred income	15	974	1,380
Trade and other payables	16	1,014	721
Obligations under finance leases	17	37	46
Corporation taxation		2	–
Bank overdrafts and loans		–	52
		2,027	2,199
Net current assets		4,505	2,519
Total assets less current liabilities		5,784	3,717
Non-current liabilities			
Deferred income	15	–	(920)
Obligations under finance leases	17	–	(37)
Net assets		5,784	2,760
Capital and reserves			
Called-up equity share capital	22	119	108
Share premium account	23	11,206	8,467
Employee share incentive plan reserve	23	(43)	–
Share options reserve	23	633	606
Reverse acquisition reserve	23	(2,484)	(2,484)
Retained earnings	23	(3,647)	(3,937)
Total shareholders' equity		5,784	2,760

These Financial Statements were approved by the Directors and authorised for issue on 5 October 2010 and are signed on their behalf by:

D Evans
Non-executive Chairman

H J J Rylands
Company Secretary

Consolidated Statement of Cash Flows

For the year ended 30 June 2010

	2010 £'000	2009 £'000
Cash flows from operating activities		
Operating profit/(loss) for the year	312	(701)
Depreciation, amortisation and impairment	169	131
Share-based payment expense	28	71
Operating profit/(loss) before changes in working capital and provisions	509	(499)
(Increase) in trade and other receivables	(191)	(383)
(Decrease)/increase in deferred income	(1,326)	2,300
Increase in trade and other payables	293	293
Net cash (outflow)/inflow from operations	(715)	1,711
Interest received	40	41
Tax received	–	183
	40	224
Net cash (outflow)/inflow from operating activities	(675)	1,935
Cash flows from investing activities		
Acquisition of fixed assets	(308)	(328)
Net cash outflow from investing activities	(308)	(328)
Cash flows from financing activities		
Proceeds from issue of share capital	2,884	24
Expenses of share issue	(135)	–
Purchase of own shares	(43)	–
Repayment of borrowings	(48)	(53)
Net cash inflow/(outflow) from financing activities	2,658	(29)
Net increase in cash equivalents	1,675	1,578
Cash and cash equivalents at beginning of year	3,696	2,118
Cash and cash equivalents at end of year	5,371	3,696
Analysis of net funds		
Cash at bank and in hand	5,371	3,748
Bank overdrafts	–	(52)
Net funds	5,371	3,696

Notes to the Financial Statements

For the year ended 30 June 2010

1. Significant accounting policies

Basis of accounting

The Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and therefore comply with Article 4 of the EU IAS Regulation, International Financial Reporting Interpretations Committee (IFRIC) interpretations and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

Epistem Holdings Plc is a company incorporated in the UK.

The Financial Statements consolidate those of the Company and its subsidiaries (together referred to as the Group). They are presented in pounds sterling and all values are rounded to the nearest one thousand (£k) except where otherwise indicated.

The Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods represented in these consolidated Financial Statements.

The preparation of the Financial Statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, duration of contracts, income, expenses and taxation.

- Determining the value of Deferred income and expenditure requires an assessment of the duration of the contract to which the Deferred income and expenditure relates which informs decisions as to when to recognise revenue and whether to carry forward costs.
- Determining the value of Intangible assets requires a judgement about the extent to which the relevant asset will be brought into economic use by the Company. The filing of a patent will generally lead to a judgement that the cost of filing the patent will have future economic use. Research and development expenditure will generally be expensed unless associated income can be identified.
- Determining the value of the deferred tax asset requires an estimation of future taxable profits against which the accumulated tax losses may be utilised.

Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Basis of consolidation

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. The Financial Statements of subsidiaries are included in the consolidated Financial Statements from the date that control commences until the date that control ceases. Transactions between Group companies are eliminated on consolidation.

On 16 March 2007, Epistem Holdings Plc merged with Epistem Limited, and on that date the shareholders of Epistem Limited exchanged their shares for equivalent shares in Epistem Holdings Plc. As Epistem Holdings Plc was newly incorporated at the time of the transaction under the terms of IFRS 3 Business Combinations, this transaction has been accounted for as a reverse acquisition, on the basis that the shareholders of Epistem Limited gained a controlling interest in the Group. The Financial Statements therefore represent a continuation of the Financial Statements of Epistem Limited.

Revenue

Revenue is measured at the fair value of the consideration received or receivable and net of discounts and sales-related taxes.

Revenue recognition

a. Contract revenue

Contract revenue is recognised by reference to the stage of completion of its related transaction at the end of the reporting period.

b. Collaboration and licensing revenue

Contractually agreed up-front payments and similar non-refundable payments in respect of collaboration or licence agreements which are not directly related to ongoing research activity are recorded as deferred income and recognised as revenue over the anticipated duration of the agreement. Where the anticipated duration of the agreement is modified, the period over which revenue is recognised is also modified. Non-refundable milestone and other payments that are linked to the achievement of significant and substantive technological or regulatory hurdles in the research and development process are recognised as revenue upon the achievement of the specified milestone.

Income which is related to ongoing research activity is recognised as the research activity is undertaken, in accordance with the contract.

Notes to the Financial Statements

(continued)

1. Significant accounting policies (continued)

Segment reporting

A segment is a group of assets, liabilities and operations engaged in providing products or services that are subject to risks and returns that are different from those of other parts of the business. The Group's primary format for segment reporting is based on business segments.

Research and development

Research and development expenditure is written off in the year in which it is incurred, unless associated income has been identified.

Intangible assets

Intangible assets are stated at cost less accumulated amortisation and any accumulated impairment losses. Amortisation is calculated so as to write off the cost of an intangible asset, less its estimated residual value, over the useful economic life of that asset, as follows:

Intellectual property – 5% straight line basis

Patents – over their estimated useful lives on a straight line basis

No amortisation is charged on those assets which are not yet available for use.

Plant and equipment

Plant and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is calculated so as to write off the cost of an asset, less its estimated residual value, over the useful economic life of that asset as follows:

Plant & machinery – 25% reducing balance basis

Fixtures & fittings – 25% reducing balance basis

Equipment – 25% reducing balance basis

Finance lease agreements

Assets held under finance lease agreements are capitalised and disclosed as Plant and equipment. The capital element of the future payments is treated as a liability and the interest is charged to the consolidated income account so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Operating lease agreements

Rentals applicable to operating leases where substantially all of the benefits and risks of ownership remain with the lessor are charged against profits over the period of the lease.

Foreign currencies

Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. Non-monetary items carried at fair value and denominated in foreign currencies are retranslated at the rates prevailing on the date when fair value is determined. The foreign currency risks relating to assets and liabilities are detailed in Note 19.

Exchange differences arising on the settlement of monetary items and on the retranslation of monetary items are taken to the income account. Exchange differences arising on non-monetary items, carried at fair value, are included in the income account, except for such non-monetary items in respect of which gains and losses are recorded in equity.

Share-based payments

The Group issues equity-settled and cash-settled share-based payments to certain employees (including Directors). Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight line basis over the vesting period, together with a corresponding increase in equity, based upon the Group's estimate of the shares that will eventually vest.

Fair value is measured using the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

Where the terms of an equity-settled transaction are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled transaction is cancelled, it is treated as if it had vested on the date of the cancellation, and any expense not yet recognised for the transaction is recognised immediately. However, if a new transaction is substituted for the cancelled transaction, and designated as a replacement transaction on the date that it is granted, the cancelled and new transactions are treated as if they were a modification of the original transaction, as described in the previous paragraph.

The issuance by the Company of share options to employees of its subsidiary represents additional capital contributions and the fair value of such options and awards is therefore recognised as an increase in the Company's investment in Group undertakings with a corresponding increase in total equity shareholders' funds.

Share Incentive Plan

The Company operates an HMR&C qualifying Share Incentive Plan. Under the scheme, the Company may contribute Matching shares to employees who elect to invest in Epistem shares under the scheme.

The Matching shares have vesting conditions, which require participants to remain employed with the Company and retain their investment in Epistem shares for at least three years. The cost of the Matching shares is expensed as and when the vesting conditions have been satisfied.

Pension contributions

Contributions to personal pension plans of employees on a defined contributions basis are charged to the income statement in the year in which they are payable.

Financial instruments

Financial instruments are classified and accounted for, according to the substance of the contractual arrangement, as either financial assets, financial liabilities or equity instruments. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Trade and other receivables

Trade and other debtors are recognised and carried forward at invoiced amounts less provisions for any doubtful debts. Bad debts are written off when identified.

Cash and cash equivalents

Cash and cash equivalents are included in the balance sheet at cost. Cash and cash equivalents comprise cash at bank and in hand and short-term deposits with an original maturity of three months or less.

Interest-bearing loans and borrowings

All loans and borrowings are recognised initially at cost, which is the fair value of the consideration received, net of issue costs associated with the borrowing.

After initial recognition, interest-bearing loans and borrowings are measured at amortised cost using the effective interest method. Gains or losses are recognised in the consolidated income account when liabilities are derecognised or impaired, as well as through the amortisation process.

Investments

Investments in subsidiaries are stated at cost less any provisions for impairment. An impairment is recognised when the recoverable amount of the investment is less than the carrying amount.

Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted, or substantially enacted, by the balance sheet date.

Deferred tax is recognised in respect of all temporary differences identified at the balance sheet date, except to the extent that the deferred tax arises from the initial recognition of goodwill (if amortisation of goodwill is not deductible for tax purposes) or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting profit nor taxable profit and loss. Temporary differences are differences between the carrying amount of the Group's assets and liabilities and their tax base.

Deferred tax liabilities may be offset against deferred tax assets within the same taxable entity. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxation profits, within the same jurisdiction, in the foreseeable future against which the deductible temporary difference can be utilised.

Deferred tax is provided on temporary differences arising in subsidiaries, jointly controlled entities and associates, except where the timing of reversal of the temporary difference will not reverse in the foreseeable future. Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date. Measurement of deferred tax liabilities and assets reflects the tax consequence expected from the manner in which the asset or liability is recovered or settled.

Notes to the Financial Statements

(continued)

1. Significant accounting policies (continued)

New standards and interpretations not applied

The International Accounting Standards Board (IASB) and IFRIC have issued the following standards and interpretations with an effective date for financial years beginning on or after 1 January 2010:

IFRS 3 (revised)	Business combinations
IFRS 7 (revised)	Statement of cash flows arising from 2009 Annual Improvements
IAS 1 (revised)	Presentation of Financial Statements, comprehensive revision
IAS 7 (revised)	Statement of cash flows, arising from 2009 Annual Improvements
IAS 32 (revised)	Puttable financial instruments
IAS 36 (revised)	Impairment of assets, arising from 2009 Annual Improvements
IAS 38 (revised)	Intangible assets, arising from 2009 Annual Improvements
IFRIC 15	Agreements for construction of real estate

The Directors do not anticipate that the adoption of these standards and interpretations will have a material effect on the Group's Financial Statements in the period of initial application.

2. Segment information

The Group's primary reporting format is business segments and the secondary format is geographical segments.

Business segments

	Contract Research Services £'000	Personalised Medicine £'000	Novel Therapies £'000	Unallocated £'000	Total £'000
Twelve months ended 30 June 2010					
Revenue	2,519	800	2,421	–	5,740
Segment trading result	759	(51)	1,067	(1,265)	510
– less depreciation and amortisation	(31)	(36)	(80)	(22)	(169)
– less equity-settled share-based payments	(6)	(12)	–	(11)	(29)
Operating profit/(loss)	722	(99)	987	(1,298)	312
Twelve months ended 30 June 2009					
Revenue	2,295	670	1,003	–	3,968
Segment trading result	607	51	(103)	(1,054)	(499)
– less depreciation and amortisation	(37)	(24)	(53)	(17)	(131)
– less equity-settled share-based payments	(7)	(19)	(2)	(43)	(71)
Operating profit/(loss)	563	8	(158)	(1,114)	(701)
Twelve months ended 30 June 2010					
Segment assets	739	218	736	6,118	7,811
Segment capital expenditure	60	17	192	39	308
Twelve months ended 30 June 2009					
Segment assets	521	–	423	2,218	3,162
Segment capital expenditure	24	–	38	25	86

Geographical segments

The Group's operations are located in the United Kingdom. The following table provides an analysis of the Group's revenue by geographical market:

	2010 £'000	2009 £'000
United Kingdom	412	687
Europe	782	762
United States of America	4,524	2,508
Asia	22	11
	5,740	3,968

Revenues from customers accounting for more than 10% of turnover are detailed below:

- (a) £2,880k revenue, of which £1,380k represents recognition of deferred income, was derived from international pharmaceutical company, Novartis, with revenue included in all divisions (2009: £1,222k). No milestone or licensing revenue was receivable in the year (2009: £nil); and
- (b) £692k revenue was derived from the University of Maryland on behalf of the US Government with revenue included within Contract Research Services (2009: £514k).

3. Operating profit/(loss)

The Group operating profit/(loss) is stated after charging:

	2010 £'000	2009 £'000
Discovery and development expenditure	1,433	1,131
Amortisation	4	4
Depreciation of owned fixed assets	143	80
Depreciation of assets held under finance lease agreements	22	47
Auditors' remuneration		
– as auditors	23	20
– for other services	–	5
Operating lease costs – property rent	173	153

4. Particulars of employees

The average number of staff employed by the Group during the financial year amounted to:

	2010 No.	2009 No.
Contract services	29	28
Research and development	12	9
Administrative	6	5
	47	42

The aggregate payroll costs of the above were:

	2010 £'000	2009 £'000
Wages and salaries	2,144	2,022
Social security costs	250	218
Equity-settled share-based payments	28	71
Pension payments	13	–
	2,435	2,311

Notes to the Financial Statements

(continued)

5. Directors' remuneration

	2010 £'000	2009 £'000
Remuneration	946	961
Pension contribution	7	–
Equity-settled share-based payments	11	53
Total	964	1,014

Full details of the Directors' remuneration and Directors' options are contained in the Directors' Remuneration Report.

6. Finance income and costs

	2010 £'000	2009 £'000
Finance income		
– interest receivable	8	41
– differences in foreign exchange	32	–
Total finance income	40	41
Finance costs (finance leases)	(2)	(9)

7. Taxation on ordinary activities

(a) Recognised in the income statement

	2010 £'000	2009 £'000
Current tax		
Research and development tax credits	–	(150)
UK corporation tax on profits for the period	2	–
Adjustment relating to a previous period	–	(8)
Total current tax	2	(158)
Deferred tax		
Prior year tax losses now recognised	(8)	(423)
Current year tax losses	20	(74)
Prior year capital allowances in excess of depreciation now recognised	–	26
Current year capital allowances in excess of depreciation	52	49
In respect of prior year share options charges now recognised	–	(153)
In respect of current year share options charges	(6)	(19)
Total deferred tax	58	(594)
Total tax charge/(credit) for the year	60	(752)

(b) Reconciliation of the total tax charge

	2010 £'000	2009 £'000
Profit/(loss) before taxation	350	(669)
Tax using the UK corporation tax rate of 28% (2009: 28%)	98	(187)
Expenditure not deductible for tax purposes	5	2
Transfers from previously unrecognised deferred tax	0	(550)
Adjustments in respect of research and development tax credits	(35)	(9)
Adjustment relating to a previous year	(8)	(8)
Total tax in income statement	60	(752)

The Group had losses, as computed for tax purposes, of approximately £1,749k (2009: £1,764k) available to carry forward to future periods.

In accordance with the provisions of the Finance Act 2000 in respect of research and development allowances, the Group is entitled to claim tax credits for certain research and development expenditure. The amount included in the Financial Statements in respect of the year ended 30 June 2010 is £nil (2009: £150k).

8. Profit attributable to members of the parent company

The profit dealt with in the accounts of the parent company was £6k (2009: £34k).

9. Earnings per share

The basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders for the year by the weighted average number of ordinary shares in issue during the year less the weighted average number of Matching Shares held by the Epistem SIP which are not yet vested.

The diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares in relation to share options and share warrants. The number of share options has been adjusted to take into account the issue price and the fair value, consistent with IAS 33 Earnings per share.

	2010 £'000	2009 £'000
Profit/(loss) for the year after taxation	290	83
	2010 No.	2009 No.
Weighted average number of ordinary shares in issue	7,649,732	7,201,928
Dilutive ordinary shares from options and warrants in issue	1,075,938	739,372
Dilutive weighted average number of ordinary shares	8,725,670	7,941,300
Earnings per share		
– basic	3.8p	1.1p
– diluted	3.3p	1.0p

Notes to the Financial Statements

(continued)

10. Intangible assets

	Patents £'000	Intellectual property £'000	Total £'000
Cost			
At 1 July 2009	88	77	165
Additions	–	–	–
At 30 June 2010	88	77	165
Amortisation			
At 1 July 2009	–	26	26
Charge for the year	–	4	4
At 30 June 2010	–	30	30
Net book value			
At 30 June 2009	88	51	139
At 30 June 2010	88	47	135
Cost			
At 1 July 2008	–	77	77
Additions	88	–	88
At 30 June 2009	88	77	165
Amortisation			
At 1 July 2008	–	22	22
Charge for the year	–	4	4
At 30 June 2009	–	26	26
Net book value			
At 30 June 2008	–	55	55
At 30 June 2009	88	51	139

During the year to 30 June 2010, the cost of the Company's Patents assessed as not having been brought into economic use amounted to £88k (2009: £88k).

11. Plant and equipment

	Lab equipment £'000	Fixtures & fittings £'000	Other equipment £'000	Total £'000
Cost				
At 1 July 2009	885	19	110	1,014
Additions	269	11	28	308
At 30 June 2010	1,154	30	138	1,322
Depreciation				
At 1 July 2009	482	12	55	549
Charge for the year	143	4	18	165
At 30 June 2010	625	16	73	714
Net book value				
At 30 June 2009	403	7	55	465
At 30 June 2010	529	14	65	608

	Lab equipment £'000	Fixtures & fittings £'000	Other equipment £'000	Total £'000
Cost				
At 1 July 2008	684	19	71	774
Additions	201	–	39	240
At 30 June 2009	885	19	110	1,014
Depreciation				
At 1 July 2008	372	9	41	422
Charge for the year	110	3	14	127
At 30 June 2009	482	12	55	549
Net book value				
At 30 June 2008	312	10	30	352
At 30 June 2009	403	7	55	465

Obligations under finance leases

Included within the net book value of lab equipment is £67k (2009: £89k) relating to assets held under finance lease agreements. The depreciation charged to the Financial Statements in the year in respect of such assets amounted to £22k (2009: £30k).

Capital commitments

	2010 £'000	2009 £'000
Contracted but not provided for in the Financial Statements	–	120

12. Deferred taxation

Recognised

	2010 £'000	2009 £'000
Tax losses carried forward	490	497
Excess of tax allowances over depreciation	(124)	(75)
Share-based payment transactions	170	172
	536	594

Deferred tax assets are recognised to the extent that the Directors, having reviewed expectations of future profitability, consider it is probable that there will be sufficient profit available against which the deferred tax asset may be utilised.

The Group did not recognise deferred tax assets in respect of share-based payment transactions of £2,963k (2009: £2,765k).

13. Trade and other receivables

	2010 £'000	2009 £'000
Trade receivables	662	474
Other receivables	114	71
Prepayments	46	106
Accrued income	189	169
	1,011	820

Notes to the Financial Statements

(continued)

13. Trade and other receivables (continued)

Analysis of trade receivables

	2010 £'000	2009 £'000
Neither impaired nor past due	611	461
Past due but not impaired	51	13
Trade receivables	662	474

Ageing of past due but not impaired trade receivables

There is no other class of financial assets that is past due but not impaired except for trade receivables. The Group's credit period generally ranges up to 60 days. The age analysis of the trade receivables have been considered from the date of the invoice and, net of allowances that are past due, is given below:

	2010 £'000	2009 £'000
Not later than one month	15	–
Later than one month but not later than three months	36	13

14. Cash and cash equivalents

	2010 £'000	2009 £'000
Cash at bank and in hand	371	484
Short-term bank deposits	5,000	3,264
	5,371	3,748

Cash and cash equivalents comprise current accounts held by the Group with immediate access and short-term bank deposits with a maturity of three months or less. Market rates of interest are earned on such deposits. The credit risk on such funds is limited because the counter parties are banks with high credit ratings assigned by international credit rating agencies.

15. Deferred income

The items recorded as Deferred income are to be recognised over future periods as follows:

	2010 £'000	2009 £'000
Amounts to be recognised within one year	974	1,380
Amounts to be recognised within two to five years	–	920
	974	2,300

16. Trade and other payables

	2010 £'000	2009 £'000
Trade payables	457	349
Other payables	213	147
Accruals	344	225
	1,014	721

17. Obligations under finance leases

Future commitments under finance lease agreements are as follows:

	2010 £'000	2009 £'000
Due within one year	41	49
Due within two to five years	–	40
	41	89
– less future finance charges	(4)	(6)
Present value of finance lease obligations	37	83
Current obligations	37	46
Non-current obligations	–	37
Obligations under finance leases	37	83

18. Share-based payments

(a) Share options outstanding at 30 June 2010

Prior to 28 November 2007, the Company operated a number of HMR&C approved and unapproved share option schemes for employees (including Directors). The original options were granted by Epistem Limited but, following the acquisition by Epistem Holdings Plc, these were released in exchange for equivalent options over the ordinary shares of Epistem Holdings Plc. On 28 November 2007 the Company established the 2007 Epistem Share Option Scheme.

Share options

Award	Number of awards	Exercise price	Period within which options are exercisable	Fair value per option	Fair value £
EMI – Approved	88,800	£0.50	07 Jan 2002 to 06 Jan 2012	See note below	
EMI – Approved	11,200	£0.75	31 Mar 2003 to 30 Mar 2013	28.2p	3,158
EMI – Approved	9,000	£0.75	07 Apr 2003 to 06 Apr 2013	28.2p	2,538
EMI – Approved	10,200	£0.75	21 Jul 2004 to 20 Jul 2014	26.6p	2,713
Share Warrants (Note 22)	198,554	£1.61	18 Mar 2005 to 17 Mar 2015	56.1p	111,389
EMI – Unapproved	78,000	£1.29	31 Mar 2005 to 30 Mar 2015	44.9p	35,022
EMI – Approved	31,824	£1.20	25 Nov 2005 to 24 Nov 2015	42.6p	13,557
EMI – Unapproved	472,153	£1.20	10 Jan 2006 to 09 Jan 2016	42.6p	201,137
EMI – Approved	197,722	£1.20	10 Jan 2006 to 09 Jan 2016	42.6p	84,230
EMI – Approved	9,400	£1.20	29 Sept 2006 to 28 Sept 2016	41.6p	3,910
EMI – Approved	80,644	£1.24	28 Mar 2007 to 27 Mar 2017	42.6p	34,354
EMI – Unapproved	177,653	£1.24	28 Mar 2007 to 27 Mar 2017	42.6p	75,680
EMI – Approved	25,903	£1.67	27 Jul 2007 to 26 Jul 2017	38.9p	10,076
EMI – Unapproved	57,727	£1.60	15 Oct 2007 to 14 Oct 2017	36.0p	20,782
2007 Epistem Share Option Scheme	71,918	£1.53	03 Mar 2011 to 02 Mar 2018	36.0p	25,890
2007 Epistem Share Option Scheme	65,800	£1.77	31 Jul 2011 to 30 Jul 2018	37.0p	24,346

Notes to the Financial Statements

(continued)

18. Share-based payments (continued)

Option valuations

The options were valued using the Black-Scholes option-pricing model. Where appropriate, performance conditions were included in the fair value calculations. The fair value per option granted and the assumptions used in the calculations are in the table below. The Group's effective date for IFRS 2 (Share-based payments) implementation is 1 July 2006 and the IFRS has been applied to all options granted after 7 November 2002 which have not been vested by this effective date.

Award	Grant date	Expected term (Note a)	Expected dividend yield % (Note b)	Expected volatility % (Note c)	Risk free rate (Note d)	Performance condition
EMI – Approved	31 Mar 2003	5 years	0	60	3.75	None
EMI – Approved	07 Apr 2003	5 years	0	60	3.75	None
EMI – Approved	21 Jul 2004	5 years	0	60	4.50	None
Share Warrants	18 Mar 2005	5 years	0	60	4.75	None
EMI – Unapproved	31 Mar 2005	5 years	0	60	4.75	None
EMI – Approved	25 Nov 2005	5 years	0	60	4.50	None
EMI – Unapproved	10 Jan 2006	5 years	0	60	4.50	See Note (e)
EMI – Approved	10 Jan 2006	5 years	0	60	4.50	None
EMI – Approved	29 Sept 2006	5 years	0	60	4.50	None
EMI – Approved	28 Mar 2007	5 years	0	60	5.25	See Note (f)
EMI – Unapproved	28 Mar 2007	5 years	0	60	5.25	See Note (f)
EMI – Approved	27 Jul 2007	5 years	0	45	5.50	None
EMI – Unapproved	15 Oct 2007	5 years	0	45	5.75	Note (g)
2007 Epistem Share Option Scheme	03 Mar 2008	5 years	0	45	5.25	Note (h)
2007 Epistem Share Option Scheme	31 Jul 2008	5 years	0	40	5.00	Note (h)

- (a) The expected term used in the model is five years and is based upon the Directors' best estimates for the effects of exercise restrictions and behavioural considerations;
- (b) The dividend yield of 0% reflects the absence of a history of paying dividends and a clear dividend policy at the relevant grant dates;
- (c) The expected volatility at the date of grant was estimated by the Directors after inspection of the Financial Statements of comparable businesses in the same business sector as the Group;
- (d) The risk free rate used is based upon the prevailing UK bank base rate at the date of the grant;
- (e) These options vest on dates dependant on anniversaries of commencing employment with the Group which commenced 1 September 2005 with the final tranche vesting on 1 September 2008;
- (f) The main conditions for these options to vest are the later of (i) when the audited accounts for the year ended 30 June 2010 become available and (ii) when the earnings per share of the financial year are a positive figure;
- (g) These options are subject to performance criteria which are appropriate to the option holders' role within the Company and which are assessed by the Remuneration Committee.
- (h) These options may be exercised following the third anniversary of grant and are subject to performance criteria which are appropriate to the option holders' role within the Company and which are assessed by the Remuneration Committee.

The number of options and their weighted average exercise prices are as follows:

Group	Number		Weighted average exercise price		Weighted average remaining contracted life – years	
	2010	2009	2010	2009	2010	2009
Outstanding as at 1 July	1,590,148	1,583,298	£1.28	£1.26		
Granted during the year	–	68,050	–	£1.77		
Exercised during the year	(2,900)	(19,200)	£1.21	£1.27		
Lapsed during the year	(750)	(42,000)	£1.76	£1.53		
Outstanding as at 30 June	1,586,498	1,590,148	£1.28	£1.28	5.62	6.62
Options exercisable at 30 June	1,190,483	1,193,383	£1.24	£1.24	5.11	6.11

The weighted average share price at the exercise dates was £3.23 (2009: £2.57).

(b) Share Investment Plan

During the year, the Company introduced the Epistem Share Investment Plan, SIP, which is open to Directors and employees in accordance with HMRC approved rules. Under the terms of the SIP, Directors and employees may invest up to £125 per month to be invested in ordinary shares (Partnership Shares) in the Company at the prevailing market price. At the same time as each monthly subscription, a maximum of two Matching Shares for each Partnership Share will be acquired on behalf of the SIP's participants. Both the Partnership and the Matching Shares are purchased on behalf of the scheme's participants by Epistem SIP Trustee Limited, a wholly owned subsidiary of the Company. Participants, who must be employed by the Company, may withdraw their Matching Shares once their associated Partnership Shares have been held for three years. The cost of the Matching Shares is expensed as and when this vesting condition is met.

	2010	2009
Capital SIP Shares		
Partnership Shares held at 30 June	5,852	N/A
Matching Shares held at 30 June	11,694	N/A
Unamortised cost of Matching Shares (comprising Employee SIP reserve)	£43k	–

19. Financial risk management objectives and policies

The Group holds or issues financial instruments in order to achieve three main objectives, being:

- (a) to finance its operations; and
- (b) to manage its exposure to interest and currency risks arising from its operations and from its sources of finance.

In addition, various financial instruments (e.g. trade receivables, trade payables, accruals and prepayments) arise directly from the Group's and the Company's operations.

Transactions in financial instruments result in the Group assuming or transferring to another party one or more of the financial risks described below.

Interest rate risk

The Group currently finances its operations through reserves of cash and liquid resources and does not have a borrowing requirement. Surplus cash at bank is placed on deposits at variable rates. The Board monitors the financial markets and the Group's own requirements to ensure that the policies are exercised in the Group's best interests.

The following table demonstrates the sensitivity to a possible change in interest rates on the Group's profit before tax through the impact of floating rate cash balances.

	Decrease in the basis points	Effect on loss before tax and equity £'000
2010		
Cash and cash equivalents	25	5
2009		
Cash and cash equivalents	25	5

An increase in 25 basis points would have a similar opposite effect.

Credit risk

The Group monitors credit risk closely and considers that its current policies of credit checks meet its objectives of managing exposure to credit risk.

The Group has no significant concentrations of credit risk. Amounts shown in the balance sheet best represent the maximum credit risk exposure in the event that other parties fail to perform their obligations under financial instruments.

Liquidity risk

The Board's policy aims to ensure that sufficient funds are held on a short-term basis in order to meet operational needs.

Notes to the Financial Statements

(continued)

19. Financial risk management objectives and policies (continued)

Currency risk

The Group's functional currency is sterling. The exposure to currency risk relates to licence income and those short-term trade receivables which are not invoiced in sterling. There are no significant costs incurred that involve payments in foreign currency.

The Group has no forward contracts at the year end (2009: nil) to manage foreign currency risk.

Balances which are denominated in US dollars are detailed below:

	2010 £'000	2009 £'000
Trade and other receivables	325	121
Cash and cash equivalents	340	479
	665	600

The following table demonstrates the sensitivity to a possible change in currency rates on the Group's loss before tax through the impact of sterling weakening against the US dollar.

	Decrease in the currency rate	Effect on loss before tax and equity £'000
2010		
Trade and other receivables	5%	16
Cash and cash equivalents	5%	17
2009		
Trade and other receivables	5%	6
Cash and cash equivalents	5%	24

An increase in currency rate of 5% would have a similar opposite effect.

Fair values of financial assets and liabilities

There is no material difference between the book value and the fair value of the Group's financial assets or liabilities.

20. Commitments under operating leases

At 30 June 2010 the Group had annual commitments under non-cancellable operating leases as set out below.

	Land and buildings	
	2010 £'000	2009 £'000
Operating leases which expire		
Within one year	148	143

The operating leases are in respect of the company's office and laboratories which are held under short-term leases.

21. Related party transactions

At the balance sheet date, the amounts owed to the following Directors, Prof. C Potten and D Evans were £3k and £8k respectively (2009: £7k and £3k). The transactions during the year with these related parties relate entirely to Directors' remuneration for the year and the amounts for each are detailed in the Directors' Remuneration Report.

22. Share capital

On 25 November 2009, the Company adopted new Articles of Association which removed the requirement for the shareholders to proscribe a level of Authorised share capital. Prior to 25 November 2009, the Authorised share capital had been set at 10,000,000 shares (£150k.)

Allotted and called up share capital:

	2010 No.	2010 £'000	2009 No.	2009 £'000
At 1 July	7,211,083	108	7,191,883	108
Private placing	720,000	10	–	–
Exercise of options	2,900	1	19,200	–
Ordinary shares of £0.015 each	7,933,983	119	7,211,083	108

On 16 March 2007, the Company entered into a warrant instrument in respect of the subscription for up to 198,554 ordinary shares of £0.015 each in Epistem Holdings Plc. This warrant instrument replaced a previous warrant instrument created by Epistem Limited on 18 March 2005. Each warrant confers the right to subscribe for one ordinary share at a subscription price of £1.61 per ordinary share. The subscription rights under the warrants may be exercised up to 21 September 2015.

23. Reserves

	Share premium account £'000	Employee share incentive plan reserve £'000	Share options reserve £'000	Reverse acquisition reserve £'000	Retained earnings £'000
Balance as at 1 July 2008	8,437	–	547	(2,484)	(4,026)
Total Comprehensive Income for the year	–	–	–	–	83
Allotment of ordinary shares	24	–	–	–	–
Exercise of options	6	–	(6)	–	–
Lapse of options	–	–	(6)	–	6
Recognition of equity-settled share-based payments in the year	–	–	71	–	–
Balance at 30 June 2009	8,467	–	606	(2,484)	(3,937)
Balance as at 1 July 2009	8,467	–	606	(2,484)	(3,937)
Total Comprehensive Income for the year	–	–	–	–	290
Allotment of ordinary shares	2,873	–	–	–	–
Share issue costs	(135)	–	–	–	–
Unamortised cost of Matching Shares	–	(43)	–	–	–
Exercise of options	1	–	(1)	–	–
Recognition of equity-settled share-based payments in the year	–	–	28	–	–
Balance at 30 June 2010	11,206	(43)	633	(2,484)	(3,647)

The reverse acquisition reserve arises as a difference on consolidation under merger accounting principles and is solely in respect of the merger of the Company and Epistem Limited.

The employee share incentive plan reserve represents 11,694 shares in Epistem Holdings Plc (2009: nil shares) all of which are held by Epistem SIP Trustee Limited. These shares are listed on the Alternative Investment Market and their market value at 30 June 2010 was £38k (2009: £nil). The nominal value held at 30 June 2010 was £175 (2009: £nil).

Company Balance Sheet

As at 30 June 2010

	Notes	2010 £'000	2009 £'000
Non-current assets			
Investments	a	5,663	5,635
Current assets			
Amounts receivable from Group undertakings		1,492	735
Cash and cash equivalents	b	5,001	3,001
		6,493	3,736
Current liabilities			
Trade and other payables		(2)	–
Net current assets		6,491	3,736
Total assets less current liabilities		12,154	9,371
Capital and reserves			
Called-up equity share capital	22	119	108
Share premium account	23	11,206	8,467
Share options reserve	23	633	606
Retained earnings		196	190
Total shareholders' equity		12,154	9,371

These Financial Statements were approved by the Directors and authorised for issue on 5 October 2010 and are signed on their behalf by:

D Evans
Non-executive Chairman

H Rylands
Company Secretary

Company Statement of Changes in Equity

For the year ended 30 June 2010

	Share capital £'000	Share premium account £'000	Share options reserve £'000	Retained earnings £'000	Total equity £'000
At 1 July 2008	108	8,437	547	150	9,242
Allotment of ordinary shares	–	24	–	–	24
Recognition of equity settled share-based payments	–	–	71	–	71
Exercise of options	–	6	(6)	–	–
Lapse of options	–	–	(6)	6	–
Profit for the year	–	–	–	34	34
At 30 June 2009	108	8,467	606	190	9,371
Balance at 1 July 2009	108	8,467	606	190	9,371
Allotment of ordinary shares	11	2,873	–	–	2,884
Share issue costs	–	(135)	–	–	(135)
Recognition of equity settled share-based payments	–	–	28	–	28
Exercise of options	–	1	(1)	–	–
Profit for the year	–	–	–	6	6
At 30 June 2010	119	11,206	633	196	12,154

Company Statement of Cash Flows

For the year ended 30 June 2010

	2010 £'000	2009 £'000
Cash flows from operating activities		
Profit for the year	–	–
Operating profit before changes in working capital and provisions	–	–
(Increase)/decrease in trade and other receivables	(757)	961
Increase in trade and other payables	–	(19)
Cash (outflow)/inflow from operations	(757)	942
Interest received	8	34
Tax (paid)/received	–	–
	8	34
Net cash outflow from operating activities	(749)	976
Cash flows from financing activities		
Proceeds from issue of share capital	2,884	24
Expenses of share issue	(135)	–
Net cash inflow from financing activities	2,749	24
Net increase in cash equivalents	2,000	1,000
Cash and cash equivalents at beginning of year	3,001	2,001
Cash and cash equivalents at end of year	5,001	3,001
Analysis of net funds		
Cash at bank and in hand	5,001	3,001
Bank overdrafts	–	–
Net funds	5,001	3,001

Notes to the Company Financial Statements

For the year ended 30 June 2010

a. Investments

The Company is the holding company of the Group.

The Company owns 100% of the issued share capital of Epistem Limited and Epistem SIP Trustees Limited, companies both registered in England and Wales. The issued share capital is fully paid and is included in the consolidated Financial Statements of the Group. The principal activity of Epistem Limited is the provision of services to the biotechnology and pharmaceutical industries. The principal activity of Epistem SIP Trustees Limited is to act as trustee to the Epistem Share Incentive Plan. On 29th August 2009 Epistem Holdings Plc subscribed for 100% of the share capital of Epistem Inc., a company that was incorporated in United States of America. The principal activity of Epistem Inc. is the provision of services to the biotechnology and pharmaceutical industries.

	Investment in subsidiary £'000
Cost	
At 1 July 2009	5,635
Additions	28
At 30 June 2010	5,663

Net book value	
At 30 June 2009	5,635
At 30 June 2010	5,663

	Investment in subsidiaries £'000
Cost	
At 1 July 2008	5,564
Additions	71
At 30 June 2009	5,635

Net book value	
At 30 June 2008	5,564
At 30 June 2009	5,635

Additions in the year ended 30 June 2010 comprised the fair value of the share options issued to employees of the subsidiary undertaking during the year of £28k. Additions in the year ended 30 June 2009 comprised the fair value of the share options issued to employees of the subsidiary undertaking during the year of £71k. Full details of the share options issued are set out in Note 18 to the consolidated Financial Statements.

b. Cash and cash equivalents

Company	2010 £'000	2009 £'000
Cash at bank and in hand	1	1
Short-term bank deposits	5,000	3,000
	5,001	3,001

Cash and cash equivalents comprise current accounts held by the Group with immediate access and short-term bank deposits with a maturity of three months or less. Market rates of interest are earned on such deposits. The credit risk on such funds is limited because the counter parties are banks with high credit ratings assigned by international credit rating agencies.

c. Related party transactions

During the course of the year, Epistem SIP Trustee acquired 11,694 (2009: nil) shares in Epistem Holdings Plc on behalf of the Epistem Share Investment Plan at a cost of £43k (2009: nil).

Notes

Directors, Secretary and Advisers

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Matthew Walls
Chris Potten
Catherine Booth
Gerard Brady
Roger Lloyd
Jeffrey Moore
Robert Nolan
John Rylands

Company Secretary

John Rylands

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