Rackspace Limited

Directors' report and financial statements

Registered number 3897010

31 December 2009

Contents

Directors' report

The directors present their directors' report and financial statements for the year ended 31 December 2009

Principal activities

The principal activity of the company is the provision of data hosting solutions

As a hosting solutions provider Rackspace Limited (the Company) owns and is responsible for the date centre, network, device operating system and application infrastructure components of the service In addition, the Company is responsible for providing a stable operating environment for the applications it hosts

The Company has a portfolio of hosting services including Managed hosting, Cloud hosting and Cloud applications Managed hosting continues to be the Company's core service offering

Business review

Turnover for the year amounted to £99,991,749 (2008 £79,959 887) representing a growth rate of 25% for the year This growth primarily resulted from an increase in the volume of services provided both to new customers and incremental services provided to existing customers Profit after tax for the year amounted to £19,913,637 (2008 £3 067 243) Included in the net income for the year is a net foreign currency gain of £3 608 536 (2008 loss £7 938 025)

The key objective of management is to provide world-class customer support In order to maintain the Company's position in the market, the singular focus remains on Fanatical Support through the recruiting, training and development of employees

The Company also recognises the importance for operational controls and the need for this to evolve with the growth of the Company In line with this internal audit and internal control functions have been established to ensure that the business realises operational efficiencies and at the same time demonstrates proper controls in its operations The Company implemented processes and procedures to seek compliance with Sarbanes Oxley, with which it is required to comply as the ultimate parent company, Rackspace Hosting Inc is listed on the New York Stock Exchange

Management continues to focus on the growth within the UK market both in terms of existing and new products whilst at the same time continuing to explore opportunities for expansion

Principal risks and uncertainties

Management consider the biggest risk to stem from the current economic condition and also recognise this as having a key impact on the potential performance of the business Management continue to monitor the markets and how this impacts the company s business

Key performance indicators

Key performance indicators used by management are structured around growth profitability, capital efficiency, infrastructure capacity and utilisation and include install base growth, customer churn, adjusted EBITDA, return on capital and technical space utilisation All key performance indicators were met during the year

Proposed dividend

The directors do not recommend the payment of a dividend *(2008 £nil)*

Subsequent events

On the 25th February 2010 and 17th June 2010 Rackspace Limited declared and paid a dividend of £6 million and £8 million, respectively to its immediate parent company Rackspace Benelux BV

Policy and practice on payment of creditors

The company's policy is to settle terms of payment with suppliers when agreeing the terms of each transaction ensure suppliers are made aware of the terms of payment and abide by the terms of payment The number of days' purchases outstanding at 31 December 2009 was 24 days (2008 23 days)

Directors' report *(continued)*

Directors

The directors who held office during the year were as follows

A Napier

G Weston

B Thomson

Employees

The company places considerable value on the involvement of its employees and has continued to keep them informed on matters affecting them as employees and on various factors affecting the performance of the company This is achieved through formal and informal meetings the company magazine and other methods of communication Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests

Disabled employees

In considering applications for employment from disabled people in the UK, the company seeks to ensure that full and fair consideration is given to the abilities and aptitudes of the applicant against the requirements of the jobs for which he or she has applied Employees who become temporarily or permanently disabled are given individual consideration and where possible equal opportunities for training career development and promotions are given to disabled persons

Within the bounds of commercial confidentiality, information is disseminated to all levels of staff about matters that affect the progress of the company and are of interest and concern to them as employees The company also encourages employees, where relevant, to meet on a regular basis to discuss matters affecting them

Political and charitable contributions

During the year the Company made charitable donations of £nil *(2008 £500)* The Company did not make any political donations during the year *(2008 £nil)*

Disclosure of information to auditors

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the company's auditors are unaware, and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information

Auditors

Pursuant to Section 487 of the Companies Act 2006, the auditors will be deemed to be reappointed and KPMG LLP will therefore continue in office

By order of the board

Brian Thomson
Director

4 The Square
Stockley Park
Uxbridge
Middlesex
UB11 1ET
7th July 2010

Statement of directors' responsibilities in respect of the directors' report and the financial statements

The directors are responsible for preparing the Directors' 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 they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable law

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period In preparing these financial statements, the directors are required to

• select suitable accounting policies and then apply them consistently

• make judgments and estimates that are reasonable and prudent,

• state whether they have been prepared in accordance with IFRSs as adopted by the EU, and

• prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006 They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities

KPMG

KPMG LLP
8 Salisbury Square
London
EC4Y 8BB

Independent auditors' report to the members of Rackspace Limited

We have audited the financial statements of Rackspace Limited for the year ended 31 December 2009 set out on pages 5 to 31 The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU

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 Directors' Responsibilities Statement set out on page 3, 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) Those 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

A description of the scope of an audit of financial statements is provided on the APB's web-site at www frc org uk/apb/scope/UKNP

Opinion

In our opinion the financial statements
- give a true and fair view of the state of the company's affairs as at 31 December 2009 and of its profit for the year then ended
- have been properly prepared in accordance with IFRSs as adopted by the EU, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if in our opinion
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us or
- the financial statements are not in agreement with the accounting records and returns, or
- certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit

Avtar Jalif (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor

12 July 2010

Chartered Accountants

Registered Auditor

Income Statement
for year ended 31 December 2009

	Note	2009 £	2008 £
Revenue	1 2	**99,991,749**	79 959,887
Cost of sales		**(29,022,493)**	(26,109 035)
Gross profit		**70,969,256**	53,850,852
Other operating income	3	**125,409**	117,532
Administrative expenses		**(46,893,201)**	(40,650,810)
Operating profit		**24,201,464**	13,317,574
Financial income	7	**3,648,889**	149,130
Financial expenses	7	**(1,372,937)**	(8 998,322)
Net financing income/(expense)		**2,275,952**	(8,849,192)
Profit before tax		**26,477,416**	4,468,382
Taxation	8	**(6,563,779)**	(1,401 139)
Profit for the year		**19,913,637**	3,067,243

The notes on pages 10 to 31 are an integral part of these financial statements

Statement of Comprehensive Income

for year ended 31 December 2009

	Note	2009	2008
		£	£
Profit for the period	17	**19,913,637**	3,067,243
Other comprehensive income			
Deferred tax recognised in equity	17	**203,987**	-
Other comprehensive income for the period, net of income tax		**203,987**	-
Total comprehensive income for the period		**20,117,624**	3 067,243

Registered number 3897010

Statement of Financial position
at 31 December 2009

	Note	2009 £	2008 £
Non-current assets			
Property, plant and equipment	9	**52,285,898**	42,370,460
Intangible assets	10	**178,642**	7,925
Trade and other receivables	11	**801,912**	780,787
		53,266,452	43,159,172
Current assets			
Trade and other receivables	11	**9,664,694**	7,493,572
Deferred tax assets	12	**1,152,958**	282,091
Cash and cash equivalents	13	**6,895,509**	7,501,774
		17,713,161	15,277,437
Total assets		70,979,613	58 436 609
Current liabilities			
Other interest-bearing loans and borrowings	14	**17,326,825**	33 510 151
Trade and other payables	15	**14,307,953**	9,657,455
Tax payable		**3,922,909**	130 487
		35,557,687	43,298,093
Non-current liabilities			
Other interest-bearing loans and borrowings	14	**4,745,186**	3 652,254
Trade and other payables	15	**610,709**	1,324 357
Deferred tax liabilities	12	-	213,498
		5,355,895	5 190,109
Total liabilities		**40,913,582**	48,488 202
Net assets		**30,066,031**	9 948,407
Equity			
Share capital	17	**1,000**	1,000
Retained earnings	17	**30,065,031**	9,947,407
Total equity		**30,066,031**	9 948,407

These financial statements were approved by the board of directors on 7th July 2010 and were signed on its behalf by

Brian Thomson

Director

Statement of changes in equity
for year ended 31 December 2009

	Note	Share capital £	Retained earnings £	Total equity £
Balance at 1 January 2008		1,000	6 880 164	6,881,164
Total comprehensive income for the period				
Profit for the year		-	3,067 243	3 067 243
Balance at 31 December 2008	17	**1,000**	**9,947,407**	**9,948,407**
Balance at 1 January 2009		1,000	9,947,407	9,948,407
Total comprehensive income for the period				
Profit for the year		-	19,913,637	19 913,637
Deferred tax recognised in equity		-	203 987	203 987
Balance at 31 December 2009	17	**1,000**	**30,065,031**	**30,066,031**

Statement of Cash Flows

for year ended 31 December 2009

	Note	2009 £	2008 £
Cash flows from operating activities			
Profit for the year		**19,913,637**	3 067 243
Adjustments for			
Depreciation, amortisation and impairment		**12,832,511**	10,213,751
Interest income		**(40,353)**	(149 130)
Interest expense		**1,372,937**	1,060,297
Foreign exchange gain / loss		**(5,593,531)**	7,780,010
Loss on sale of plant and equipment		**411,010**	380,239
Taxation		**6,563,779**	1,401,139
Cash flow from operations before change in working capital and tax		**35,459,990**	23,753,549
(Increase) in trade and other receivables		**(2,349,625)**	(2,729 732)
Increase/(Decrease) in trade and other payables		**3,888,934**	(948 139)
Cash flow from operations before tax		**36,999,299**	20,075 678
Tax paid		**(3,651,736)**	(784 689)
Net cash flow from operating activities		**33,347,563**	19,290,989
Cash flows from investing activities			
Proceeds from sale of plant and equipment		**14,414**	4,850
Interest received		**40,353**	123 548
Acquisition of plant and equipment		**(17,548,272)**	(27,744 783)
Acquisition of other intangible assets	10	**(237,676)**	(8 646)
Loan to group undertaking		**157,378**	(808 305)
Net cash from investing activities		**(17,573,803)**	(28,433 336)
Cash flows from financing activities			
Proceeds from new loan		**-**	13,734 859
Additional borrowings on loans		**1,296,387**	-
Repayment of loan		**(12,746,819)**	-
Interest paid		**(1,372,937)**	(1,060,297)
Payment of finance lease liabilities		**(3,556,656)**	(1,057,948)
Net cash from financing activities		**(16,380,025)**	11,616,614
Net (decrease)/increase in cash and cash equivalents		**(606,265)**	2,474,267
Cash and cash equivalents at 1 January 2009		**7,501,774**	5,027 507
Cash and cash equivalents at 31 December 2009	13	**6,895,509**	7 501 774

Notes

(forming part of the financial statements)

1 Accounting policies

Rackspace Limited (the 'Company') is a company incorporated and domiciled in the UK

The company's financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRSs')

The accounting policies set out below have unless otherwise stated, been applied consistently to all periods presented in these financial statements

Judgements made by the directors in the application of these accounting policies that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 23

Measurement convention

The financial statements are prepared on the historical cost basis Non-current assets and disposal groups held for sale are stated at the lower of previous carrying amount and fair value less costs to sell

Foreign currency

Transactions in foreign currencies are translated to the Company's functional currencies at the exchange rate ruling at the date of the transaction Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are re-translated to the functional currency at the exchange rate ruling at that date Foreign exchange differences arising on translation are recognised in the income statement Non-monetary assets and liabilities denominated in foreign currencies that are recognised at historical cost are translated using the exchange rate at the date of the transaction Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are retranslated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined

Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables

Trade and other receivables

Trade and other receivables are recognised initially at fair value Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses

Trade and other payables

Trade and other payables are recognised initially at fair value Subsequent to initial recognition they are measured at amortised cost using the effective interest method

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits Bank overdrafts that are repayable on demand and form an integral part of the Company's cash management are included as a component of cash and cash equivalents for the purpose only of the cash flow statement

Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method, less any impairment losses

Notes (continued)

1 Accounting policies *(continued)*

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment

Leases in which the Company assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases Where land and buildings are held under leases the accounting treatment of the land is considered separately from that of the buildings Leased assets acquired by way of finance lease are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease less accumulated depreciation and less accumulated impairment losses Lease payments are accounted for as described below

Depreciation is charged to the income statement on a straight-line basis over the estimated useful economic lives of each part of an item of property plant and equipment Land is not depreciated The estimated useful lives are as follows

- Assets under construction - Nil
- Leasehold property - over the life of the lease or useful economic life, if shorter
- Plant and machinery - between 20% and 33 3%
- Fixtures and fittings - between 14 3% and 20%

Depreciation methods, useful lives and residual values are reviewed at each balance sheet date

Other intangible assets

Other intangible assets that are acquired by the Company are stated at cost less accumulated amortisation and less accumulated impairment losses

Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite Intangible assets with an indefinite useful life are systematically tested for impairment at each balance sheet date Other intangible assets are amortised from the date they are available for use The estimated useful lives are as follows

- Software - 3 years

Impairment excluding deferred tax assets

The carrying amounts of the Company's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment, a financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset If any such indication exists, the asset's recoverable amount is estimated

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount Impairment losses are recognised in the income statement

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit on a pro rata basis A cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets

Calculation of recoverable amount

The recoverable amount of other assets is the greater of their fair value less costs to sell and value in use In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs

Reversals of impairment

In respect of other assets an impairment loss is reversed when there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation if no impairment loss had been recognised

Notes (continued)

1 Accounting policies *(continued)*

Employee benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably

Share-based payment transactions

The share option programme allows employees to acquire shares of Rackspace Hosting Inc The fair value of options granted after 7 November 2002 and those not yet vested as at 1 January 2005 are recognised as an employee expense with a corresponding increase in amounts owed to group undertakings The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options The fair value of the options granted is measured using an option pricing model, taking into account the terms and conditions upon which the options were granted The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is only due to share prices not achieving the threshold for vesting

Provisions

A provision is recognised in the balance sheet when the Company has a present legal or constructive obligation as a result of a past event, that can be reliably measured and it is probable that an outflow of economic benefits will be required to settle the obligation Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects risks specific to the liability

Revenue

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for services provided in the normal course of business, net of discounts, Value Added Tax and other sales taxes

Revenue consists primarily of recurring monthly fees from hosting services which is recognised as the services are provided Hosting service contracts range from one month to 5 years Payments received and billings in advance of providing services are deferred until the services are provided Unbilled revenues for services provided are accrued at the end of each period

Set up fees are non refundable and are recognised on a straight line basis over the expected average customer economic life at the time of sale Set up costs consist primarily of labour by technical support personnel to configure the customer's server and to activate the new service When customers terminate services with the Company, any unamortised set up fees are recognised in income

Usage based fees are recognised as the service is provided

Service credits are provided on a case by case basis in accordance with the master services agreement and the service level agreement These credits are determined and accounted for at the time the service failure becomes evident

Revenue includes services rendered wholly within the United Kingdom, together with a share of income arising from the sale of hosting services on the Parent Company's servers and the sale by the parent company of hosting services on the Company's servers

Notes (continued)

1 Accounting policies *(continued)*

Expenses

Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease Lease incentives received are recognised in the income statement as an integral part of the total lease expense

Finance lease payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability

Financing income and expenses

Financing expenses comprise interest payable, finance charges on finance leases, and net foreign exchange losses that are recognised in the income statement (see foreign currency accounting policy) Financing income comprises interest receivable on funds invested and net foreign exchange gains

Interest income and interest payable is recognised in profit or loss as it accrues, using the effective interest method Foreign currency gains and losses are reported on a net basis

Taxation

Tax on the profit or loss for the year comprises current and deferred tax Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity in which case it is recognised in equity

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes The following temporary differences are not provided for the initial recognition of goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised

Adopted IFRS not yet applied

The following Adopted IFRSs and IASs were available for early application but have not been applied by the Company in these financial statements Their adoption is not expected to have a material effect on the financial statements unless otherwise indicated

Revised IAS 24 Related Party Disclosures is mandatory for the year commencing 1 January 2011 The definition of a related party was simplified, clarifying its intended meaning and eliminating inconsistencies from the definition The company will be applying this amendment for the year commencing 1 January 2011

Notes (continued)

2 Revenue

Revenue is attributable to the one principal activity of the company being hosting services

3 Other operating income

	2009 £	2008 £
Management charge to group undertakings	**120,000**	96,927
Other income	**5,409**	20,605
	125,409	117,532

4 Expenses and auditors' remuneration

Profit before tax is stated after charging

	2009 £	2008 £
Depreciation of property, plant and equipment		
-owned	**9,749,621**	9,041,408
-held under finance leases and hire purchase contracts	**3,015,931**	1,171,622
Amortisation of intangible assets	**66,959**	721
Loss on disposal of fixed assets	**411,010**	380,239
Operating lease costs		
-land and buildings	**4,927,124**	6,418 378
-plant and machinery	**32,462**	46,859
Royalties and management fees	**4,766,128**	3,955,648

Auditors' remuneration

	2009 £	2008 £
Audit of these financial statements	**92,043**	106,029

Notes (continued)

5 Staff numbers and costs

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

	Number of employees 2009	2008
Technical	**268**	247
Sales	**101**	98
Administration	**107**	102
	476	447

The aggregate payroll costs of these persons were as follows

	2009 £	2008 £
Wages and salaries	**23,490,060**	21 152,563
Social security costs	**4,363,472**	2,528,155
Contributions to defined contribution plans	**774,792**	553 413
	28,628,324	24,234,131

6 Directors' remuneration

	2009 £	2008 £
Directors' emoluments	**308,194**	430 890
Company contributions to money purchase pension plans	**14,200**	31,148
	322,394	462 038

The aggregate of emoluments and amounts receivable under long term incentive schemes of the highest paid director was £308 194 *(2008 £387 040)* and company pension contributions of £14 200 *(2008 £21,217)* were made to a money purchase scheme on his behalf

	Number of directors 2009	2008
Retirement benefits are accruing to the following number of directors under Money purchase schemes	**1**	1

Notes (continued)

7 Finance income and expense

	2009 £	2008 £
Finance income		
Interest income on short term bank deposits	**8,693**	113,768
Other interest	**31,660**	35,362
Net foreign exchange gain	**3,608,536**	-
Total finance income	**3,648,889**	149 130

	2009 £	2008 £
Finance expense		
Finance charges as obligations under finance lease	**548,391**	321,122
Interest payable on amounts due to parent undertakings	**824,546**	739,175
Net foreign exchange loss	**-**	7 938,025
Total finance expense	**1,372,937**	8,998 322

Notes (continued)

8 Taxation

	2009	2008
	£	£
Current tax expense		
UK corporation tax	**7,444,157**	1,518,370
Adjustments for prior years	**-**	(120,412)
Current tax expense	**7,444,157**	1,397,958
Deferred tax expense	**(880,378)**	3,181
Total tax expense in income statement	**6,563,779**	1,401,139

Reconciliation of effective tax rate

	2009	2008
	£	£
Profit before tax	26,477,416	4,468,382
Tax at the UK corporation tax rate of 28% (2008 28%/30%)	7,413,677	1,273,366
Non-deductible expenses	62,370	68,986
Stock option costs	(912,268)	-
Prior year adjustment	-	55,715
Tax rate change differences	-	3,072
Total tax expense	6,563,779	1,401,139

Notes (continued)

9 Property, plant and equipment

	Assets under construction £	Leasehold property £	Plant and Machinery £	Fixtures and fittings £	Total £
Cost					
At beginning of year	4,625,738	19 082,381	40,439,754	1,459,356	65,607,229
Additions	-	9,323,875	13,101 346	681,194	23,106,415
Disposals	-	(625,568)	(1,447,461)	(3,612)	(2,076,641)
Transfer between asset classes	(3 467,553)	3,467,553	-	-	-
At end of year	1,158,185	31,248,241	52,093,639	2,136,938	86,637,003
Depreciation and impairment					
At beginning of year	-	1,845,401	20,905,919	485,449	23,236,769
Depreciation charge for the year	-	1,856,651	10,655,107	253,794	12,765,552
Disposals	-	(625,568)	(1,024,612)	(1,036)	(1,651,216)
At end of year	-	3,076,484	30,536,414	738,207	34,351,105
Net book value					
At 31 December 2009	**1,158,185**	**28,171,757**	**21,557,225**	**1,398,731**	**52,285,898**
At 31 December 2008	4,625,738	17,236,980	19,533,835	973,907	42,370,460

Leased plant and machinery

At 31 December 2009 the net carrying amount of plant and machinery includes £9,423,725 *(2008 £6,275,592)* in respect of assets held under finance lease The leased equipment is provided as security to the lessor under these lease arrangements (see note 14)

Notes (continued)

10 Intangible assets

	Software licenses £
Cost	
At beginning of year	8,646
Additions	237,676
At end of year	246,322
Amortisation and impairment	
At beginning of year	721
Amortisation for the year	66,959
At end of year	67,680
Net book value	
At 31 December 2009	**178,642**
At 31 December 2008	7,925

Amortisation charge

The amortisation charge is recognised in the following line item in the income statement

	2009 £	2008 £
Administrative expenses	**66,959**	721

11 Trade and other receivables

	2009 £	2008 £
Current assets		
Trade receivables due from group undertakings	**890,118**	1,047,496
Other trade receivables	**7,448,746**	5,633,189
Prepayments	**917,879**	765,643
Other receivables	**407,951**	47,244
	9,664,694	7,493,572
Non-current assets		
Prepayments	**434,185**	110 686
Other receivables	**367,727**	670 101
	801,912	780,787

Notes (continued)

12 Deferred tax assets and liabilities

Recognised deferred tax assets and liabilities

Deferred tax (assets) and liabilities are attributable to the following

	Assets 2009 £	2008 £	Liabilities 2009 £	2008 £	Net 2009 £	2008 £
Property, plant and equipment	**(20,604)**	-	-	213 498	**(20,604)**	213,498
Allowance for doubtful accounts	**(38,534)**	(44 149)	-	-	**(38,534)**	(44,149)
Share-based payments	**(862,602)**	(223,703)	-	-	**(862,602)**	(223,703)
Employee benefits	**(231,218)**	(14,239)	-	-	**(231,218)**	(14 239)
Tax (assets) / liabilities	**(1,152,958)**	(282 091)	-	213 498	**(1,152,958)**	(68,593)
Net of tax liabilities / (assets)	-	213 498	-	(213,498)	-	-
Tax (assets) / liabilities	**(1,152,958)**	(68,593)	-	-	**(1,152,958)**	(68,593)

Movement in deferred tax during the year

	1 January 2009 £	Recognised in reserves £	Recognised in income £	31 December 2009 £
Property, plant and equipment	**213,498**	-	**(234,102)**	**(20,604)**
Allowance for doubtful accounts	**(44,149)**	-	**5,615**	**(38,534)**
Share-based payments	**(223,703)**	**(203,987)**	**(434,912)**	**(862,602)**
Employee benefits	**(14,239)**	-	**(216,979)**	**(231,218)**
	(68,593)	**(203,987)**	**(880,378)**	**(1,152,958)**

Movement in deferred tax during the prior year

	1 January 2008 £	Recognised in reserves £	Recognised in income £	31 December 2008 £
Property, plant and equipment	333,222	-	(119,724)	213,498
Allowance for doubtful accounts	(26,250)	-	(17 899)	(44,149)
Share-based payments	(335,698)	-	111,995	(223,703)
Employee benefits	(13,754)	-	(485)	(14,239)
Other	(29,294)	-	29,294	-
	(71,774)	-	3,181	(68,593)

Notes (continued)

13 Cash and cash equivalents

	2009 £	2008 £
Cash and cash equivalents per Statement of Financial position	**6,895,509**	7,501,774
Cash and cash equivalents per Statement of Cash Flows	**6,895,509**	7,501,774

14 Other interest-bearing loans and borrowings

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings, which are measured at amortised cost For more information about the Company s exposure to interest rate and foreign currency risk, see note 18

	2009 £	2008 £
Current liabilities		
Current portion of finance lease liabilities	**4,539,090**	3,630,536
Loans from group undertakings	**12,787,735**	29,879,615
	17,326,825	33,510,151
Non-current liabilities		
Finance lease liabilities	**4,745,186**	3,652,254

Loans due to group undertakings relate to the revolving credit agreement from Rackspace Benelux BV of £12,787,735 (2008 £nil) It bears interest at three months LIBOR plus 1%, which is determined on a quarterly basis and is payable in arrears 15 days after the quarter The loan is repayable on demand and has been classified as current The revolving credit facility cannot exceed £75,000,000, and is available for a one year period, which will automatically roll over into further one year revolving credit agreements, if no notice has been given

During 2009 loans due to group undertakings of £29,878 815 with Rackspace Hosting Inc were settled through a combination of cash settlement (£8 746 819), foreign exchange movements (£5 593,531), additional charges £1,248 470 and a transfer of the remaining loan balance of £16,787,735 to Rackspace Benelux BV

Finance lease liabilities

Finance lease liabilities are payable as follows

	Minimum lease payments 2009 £	**Interest 2009 £**	**Principal 2009 £**	Minimum lease payments 2008 £	Interest 2008 £	Principal 2008 £
Less than one year	**4,973,790**	**434,700**	**4,539,090**	4,075,507	444,971	3,630,536
Between one and five years	**4,972,452**	**227,266**	**4,745,186**	3,836,929	184,675	3,652,254
	9,946,242	**661,966**	**9,284,276**	7,912,436	629,646	7,282,790

Notes (continued)

15 Trade and other payables

	2009	2008
	£	£
Current		
Trade payables due to group undertakings	**527,856**	479,939
Other trade payables	**2,404,692**	1,982,739
Non-trade payables	**6,489,740**	2,089,706
Accrued expenses	**1,681,446**	3,083,415
Deferred income	**3,204,219**	2,021 656
	14,307,953	9,657,455
Non-current		
Non-trade payables	**-**	483,336
Deferred income	**610,709**	841,021
	610,709	1,324,357

16 Employee benefits

Pension plans

Defined contribution plans

The Company operates a number of defined contribution pension plans

The total expense relating to these plans in the current year was £774,792 *(2008 £553,413)*

Notes (continued)

16 Employee benefits (continued)

Share-based payments

Share options over the shares of Rackspace Hosting Inc, the ultimate parent entity are granted to certain employees and executives of the company

All share-based payments schemes are treated as equity-settled This is on the basis that there is neither mandatory redemption nor a buy-back arrangement in place for these share-based payments and there is no intention or obligation by the ultimate parent company to settle these schemes in cash

The fair value of options and units granted is recognised as an expense with a corresponding increase in amounts owed to group undertakings The total expense recognised in respect of these schemes was £1,251,011 for the year ended 31 December 2009 *(2008 £869,919)*

Under the share option plans, the ultimate parent company may grant options to directors and employees of the Company to purchase Ordinary shares Options typically vest either rateably over the requisite service period or at the end of three years The term of the options may not exceed ten years Share options are granted under a service condition There are no market conditions associated with the share option grants

The number and weighted average exercise prices of share options in are as follows

	2009 Weighted average exercise price	**2009 Number of options**	2008 Weighted average exercise price	2008 Number of options
Outstanding at the beginning of the year	**$6 29**	**1,492,150**	$4 44	1,817,500
Granted during the year	**$5 63**	**501,700**	$10 18	653,150
Forfeited during the year	**$8 07**	**(220,075)**	$6 58	(754,750)
Exercised during the year	**$2 95**	**(365,350)**	$1 61	(223,750)
Outstanding at the end of the year	**$6.64**	**1,408,425**	$6 29	1,492,150
Exercisable at the end of the year	**$3 42**	**258,013**	$2 56	505,250

The weighted average share price at the date of exercise of share options exercised during the year was $16 27 *(2008 $10 83)*

The options outstanding at the year-end have an exercise price in the range of $1 25 to $17 95 and a weighted average contractual life of 8 05 years

For valuation prior to our Initial Public Offering (IPO), the fair value of our common stock was determined using both a market and discounted cash flow approach The aggregate equity valuation was allocated between our various securities using the treasury stock method Subsequent to the IPO, the end of day market price on the grant date was used to determine fair value

The estimate of the fair value of the services received is measured based on a Black Scholes option pricing model with the following assumptions

	2009	2008
Fair value at measurement date	**$3.27**	$8 15
Share price (range)	**$5 09-$17.95**	$6 69-$15 59
Exercise price (range)	**$5 09-$17 95**	$6 69-$15 59
Expected volatility (weighted average volatility)	**56 6%-60.9%**	60%-65%
Option life (expected weighted average life)	**6.25 years**	6 25-6 50 years
Expected dividends	**0.00%**	0 00%
Risk free interest rate (range)	**2 24%-3 03%**	2 71%-3 45%

Management estimates volatility for option grants by evaluating the average historical volatility of a peer group, as well as the volatility of the company's stock since the IPO Management believes historical volatility of the identified peer group (while incorporating the company's historical volatility) to be the best estimate of future volatility

Notes (continued)

17 Capital and reserves

Reconciliation of movement in capital and reserves

	Share Capital £	Retained earnings £	Total equity £
Balance at 1 January 2008	1,000	6,880,164	6,881,164
Total recognised income and expense	-	3,067,243	3 067,243
Balance at 31 December 2008	1,000	9,947,407	9,948,407
Balance at 1 January 2009	1,000	9,947,407	9,948,407
Deferred tax recognised in equity	-	203,987	203,987
Total recognised income and expense	-	19,913,637	19,913,637
Balance at 31 December 2009	**1,000**	**30,065,031**	**30,066,031**

Share capital

	Ordinary shares	
	2009	2008
On issue at 1 January and 31 December 2009 – fully paid	**1,000**	1 000

	2009 £	2008 £
Authorised		
Ordinary shares of £1 each	**100,000**	100,000
Allotted, called up and fully paid		
Ordinary shares of £1 each	**1,000**	1,000

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company

Notes (continued)

18 Financial instruments

18 (a) Fair values of financial instruments

Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows discounted at the market rate of interest at the balance sheet date if the effect is material

Trade and other payables

The fair value of trade and other payables is estimated as the present value of future cash flows, discounted at the market rate of interest at the balance sheet date if the effect is material

Cash and cash equivalents

The fair value of cash and cash equivalents is estimated as its carrying amount where the cash is repayable on demand

Interest-bearing borrowings

Fair value, which after initial recognition is determined for disclosure purposes only, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the balance sheet date For finance leases the market rate of interest is determined by reference to similar lease agreements

18 (b) Credit risk

Financial risk management

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers and investment securities

The company's credit risk is primarily attributable to its trade receivables The amounts presented in the balance sheet are net of allowance for doubtful receivables An allowance for impairment is made where there is an identified loss event which based on previous experience, is evidence of a reduction in the recoverability of the cash flows

The company performs credit checks on all customers and takes steps to mitigate the risk of non-payment by securing upfront payment where deemed appropriate

There is no significant concentration of credit risk with the exposure spread over a large number of counterparties and customers

Credit quality of financial assets and impairment losses

The aging of trade receivables at the balance sheet date was

	Gross 2009 £	**Provision 2009 £**	Gross 2008 £	Provision 2008 £
Not past due	**6,343,450**	**-**	4,472,976	-
Past due (0-30 days)	**961,251**	**30,069**	1,181,824	76,149
Past due (31-120 days)	**210,171**	**42,562**	85,749	31,211
More than 120 days	**409,122**	**402,617**	179,686	179,686
	7,923,994	**475,248**	5,920,235	287,046

The movement in the allowance for impairment in respect of trade receivables during the year was as follows

	2009 £	2008 £
Balance at 1 January	**287,046**	165,137
Increase in provision	**188,202**	121,909
Balance at 31 December	**475,248**	287,046

Notes (continued)

18 Financial instruments *(continued)*

18 (c) Liquidity risk

Financial risk management

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due

The company's use of financial instruments is confined to a bank account finance leases and loan funding from Rackspace Benelux BV

The company's exposure to liquidity risk is determined by the ability of Rackspace Inc the ultimate parent company and Rackspace Benelux BV, the immediate parent company to continue to provide the company support The contractual maturities of the Company's financial liabilities, excluding estimated interest payments are as follows

	2009 £	2008 £
Less than one year	28,430,559	41,145,950
Between one and five years	4,745,186	3,652,254
More than five years	-	-
	33,175,745	44,798,204

18 (d) Market risk

Financial risk management

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices, will affect the Company's income or the value of its holdings of financial instruments

The majority of customers are invoiced, and substantially all of the Company's expenses are paid in the functional currency, however some customers are invoiced in currencies other than the applicable functional currency which could result in foreign currency losses based on the changes in exchange rates between the date of the invoice and the date of collection

Market risk – Foreign currency risk

In 2009 other interest bearing loans and borrowings which were denominated in USD were either repaid or transferred into GBP denominated loan balances with Rackspace Benelux BV This removes the Company's exposure to foreign currency risk on these balances To date the company has not entered into any hedging contracts

The Company's exposure to foreign currency risk is as follows This is based on the carrying amount for monetary financial instruments except derivatives when it is based on notional amounts

31 December 2009

	Sterling £	Euro £	US Dollar £	Other £	Total £
Cash and cash equivalents	4,164,075	2,414,019	317,415	-	6,895,509
Trade receivables (current)	8,128,112	142,017	476,686	-	8,746,815
Trade receivables (non-current)	367,727	-	-	-	367,727
Other interest-bearing loans and borrowings	(12,787,735)	-	-	-	(12,787,735)
Finance leases	(9,284,276)	-	-	-	(9,284,276)
Trade payables (current)	(11,059,313)	(10,767)	(24,516)	(9,138)	(11,103,734)
Exposure	(20,471,410)	2,545,269	769,585	(9,138)	(17,165,694)

Notes (continued)

18 Financial instruments *(continued)*

18 (d) Market risk (continued)

31 December 2008

	Sterling £	Euro £	US Dollar £	Other £	Total £
Cash and cash equivalents	7,036,815	436,544	28,415	-	7,501,774
Trade receivables (current)	6,572,756	155,173	-	-	6,727 929
Trade receivables (non-current)	670,101	-	-	-	670,101
Other interest-bearing loans and borrowings	-	-	(29,879,615)	-	(29,879,615)
Finance leases	(7,282,790)	-	-	-	(7,282,790)
Trade payables (current)	(7 564,875)	(29,268)	(26,087)	(15,569)	(7,635,799)
Trade payables (non-current)	(483 336)	-	-	-	(483 336)
Exposure	(1,051,329)	562 449	(29,877 287)	(15,569)	(30,381 736)

Sensitivity analysis

A 5% weakening of the following currencies against pound sterling at 31 December would have decreased profit by the amounts shown below This calculation assumes that the change occurred at the balance sheet date and had been applied to risk exposures existing at that date

This analysis assumes that all other variables, in particular other exchange rates and interest rates, remain constant The analysis is performed on the same basis for 2008

	Profit or (Loss) 2009 £	2008 £
€	**(127,263)**	(28,122)
$	**(38,479)**	1,493,864

A 5% strengthening of the above currencies against pound sterling at 31 December would have had an equal but opposite effect on the above currencies by the amounts shown above, on the basis that all other variables remain constant

Market risk – Interest rate risk

Interest is charged from Rackspace Benelux BV to the company in relation to a revolving credit agreement In 2008 two separate agreements were held with Rackspace Hosting Inc

The loan agreement bears interest at 3 months EURO LIBOR plus 1% This market rate of interest is fluctuating and exposes our interest expense to risk

Other than borrowings from Rackspace Benelux BV no other financial assets or financial liabilities are subject to interest rate exposure

Notes (continued)

22 Ultimate parent company and parent company

The Company is a subsidiary undertaking of Rackspace Benelux BV The ultimate controlling party is Rackspace Hosting Inc

The smallest and largest group in which the results of the Company are consolidated is that headed by Rackspace Hosting Inc, incorporated in the United States of America No other group financial statements include the results of the Company The consolidated financial statements of these groups are available to the public and may be obtained from www rackspace com

23 Accounting estimates and judgments

The company prepares its financial statements in accordance with IFRS In some cases, the accounting treatment of a particular transaction is specifically dictated by IFRS and does not require management's judgment in its application, while in other cases, significant judgment is required in making estimates, and selecting among available alternative accounting standards that allow different accounting treatment for similar transactions These judgments and estimates affect the reported amounts of assets, liabilities, revenue, costs and expenses and related disclosures

The company reviews its estimates and judgments on an ongoing basis, including those related to revenue recognition, service credits, allowance for doubtful accounts, property and equipment, intangibles, and taxation

Notes (continued)

18 Financial instruments *(continued)*

18 (d) Market risk (continued)

Market risk – Interest rate risk (continued)

Profile

At the balance sheet date the interest rate profile of the Company's interest-bearing financial instruments was

	2009 £	2008 £
Fixed rate instruments		
Financial liabilities	**9,284,276**	7 282,790
Variable rate instruments		
Financial liabilities	**12,787,735**	29 879,615

Sensitivity analysis

An increase (2008 reduction) of 100 basis points in interest rates at the balance sheet date would have decreased profit by the amounts shown below This calculation assumes that the change occurred at the start of the accounting period and had been applied to risk exposures existing at the end of the accounting period

This analysis assumes that all other variables, in particular foreign currency rates, remain constant and considers the effect of financial instruments with variable interest rates, financial instrument at fair value through profit or loss or available for sale with fixed interest rates and the fixed rate element of interest rate swaps The analysis is performed on the same basis for 2008

	2009 £	2008 £
Profit or loss		
Increase	-	175,559
Decrease	**24,646**	-

18 (e) Capital management

The Company funds day to day working capital requirements largely through cash generated from operations Additional funding requirements are met through draw downs on the Company's revolving credit facility with Rackspace Benelux BV as disclosed in Note 14

Notes (continued)

19 Operating leases

Non-cancellable operating lease rentals are payable as follows

	2009	2008
	£	£
Less than one year	**2,856,147**	4,817 330
Between one and five years	**8,848,899**	9,434,046
More than five years	**7,399,129**	9,142,460
	19,104,175	23,393,836

The company leases a number of office facilities to provide a working environment for staff that provide a wide range of functions The company also leases warehouse space which has been adapted to accommodate servers which are used to provide hosting services to customers

During the year £4,959,586 was recognised as an expense in the income statement in respect of operating leases (2008 £6,465,237)

20 Contingencies

The company will accrue for contingent obligations including estimated legal costs when the obligation is probable and the amount is reasonably estimable As facts concerning contingencies become known, the company reassesses the position and makes appropriate adjustments to the financial statements Estimates that are particularly sensitive to future changes include those related to tax, legal, and other regulatory matters, changes in the interpretation and enforcement of international laws, and the impact of local economic conditions and practices which are all subject to change as events evolve and as additional information becomes available during the administrative and litigation process

Notes (continued)

21 Related parties

Identity of related parties with which the Company has transacted

The Company has transactions with Rackspace Benelux BV, which is the immediate parent undertaking, and, Rackspace Hosting Inc, which is considered the ultimate parent undertaking by virtue of its 100% shareholding in Rackspace Benelux BV

Transactions with key management personnel

The compensation of key management personnel (including the directors) is as follows

	2009 £	2008 £
Key management emoluments including social security costs	**1,695,033**	1,303,995
Company contributions to money purchase pension plans	**53,380**	64,515
	1,748,413	1,368,510

Other related party transactions

The following inter-company transactions are included within the Company's results

	2009 £	2008 £
Revenue from Rackspace Hosting Inc	**7,074,529**	7,158,099
Revenue from Rackspace BV	**487,743**	36 023
Cost of sales recharged from Rackspace Hosting Inc	**1,992,991**	1 768,801
Administrative expense-Royalties and management charges from Rackspace Hosting Inc	**4,766,128**	3,955,649
Administrative expense-Royalties and management charges to Rackspace BV	**120,000**	96,927
Interest charges from Rackspace Hosting Inc	**793,598**	739 174
Interest charges from Rackspace Benelux BV	**30,948**	-

	Receivables outstanding 2009 £	2008 £	Payables outstanding 2009 £	2008 £
Rackspace Hosting Inc	**848,972**	-	**527,856**	30,359,554
Rackspace BV	**41,147**	1,047,496	**12,787,735**	-
	890,119	1,047,496	**13,315,591**	30,359 554