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Chroma Therapeutics Limited
Report and Consolidated financial statements

Year ended 31 December 2007

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Company information

Company number	4066289 (England & Wales)
Directors	P V Allen (Chairman) T J Haines Dr J Hemberger I J Nicholson (Chief Executive Officer) Dr P T Vainio Dr K Veitinger Prof P Workman
Secretary	R E Bungay
Registered office	93 Milton Park Abingdon OX14 4RY
Auditors	Ernst & Young LLP Apex Plaza Reading RG1 1YE

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Directors' report

for the year ended 31 December 2007

The directors present their report and consolidated financial statements for Chroma Therapeutics Ltd ('the Company') and its subsidiaries ('the Group') for the year ended 31 December 2007

Principal activities and review of the business

The principal activity of the Group continues to be the research and development of novel therapeutic agents for the treatment of cancer and inflammatory disorders

During the financial year, the Group's research and development pipeline progressed in line with its expectations The Group's lead development candidate, CHR-2797, completed initial Phase I clinical studies and was entered into Phase II clinical development The Group also continued to progress two novel agents, CHR-3996 and CHR-2845, through preclinical development and to prepare for the anticipated entry of these agents into clinical development during 2008 The Group has also continued to develop its esterase-sensitive motif (ESM) technology platform and has broadened its portfolio of intellectual property during 2007 Reflecting the growth in the Group's clinical development activities, a number of new appointments were made in this area during 2007 This substantial growth in the Group's preclinical and clinical development activities, along with other factors such as the introduction of a new management bonus scheme, resulted in an increase in its research and development expenditure of 48% compared to the previous financial year General and administrative expenses increased by 37% compared to the previous financial year, primarily due to increased business development activities and the introduction of a new management bonus scheme

The Group does not have regular sources of revenue other than interest earned on its cash and short term deposits and the UK R&D tax credit scheme, which enables the Group to surrender a proportion of its tax losses relating to research and development in each financial year in return for a cash receipt Finance revenue increased substantially compared to the previous financial year as a result of higher average cash balances during the year along with higher base interest rates in the UK The Group also receives income from an EU research grant, as detailed in Note 4

The Group's income and expenses during the year were in line with its expectations

As is typical for biotechnology companies at a similar stage of development, the Group anticipates its operations will continue to absorb cash for the foreseeable future and anticipates financing these activities through a combination of equity issuance, debt financing and from income derived from licensing activities During 2008 the Group finalised the terms of a £7 5 million debt financing facility that, upon draw down, is expected to extend its cash reserves to the second half of 2009 (see Note 18 'Subsequent events') The Group is also pursuing a number of opportunities related to the application of its ESM technology platform and anticipates generating signature fees, milestone payments and research funding from one or more such deals during 2008, which will further extend its cash resources

Principal risks and uncertainties

The Group operates in a high-risk sector, which is reflected in the Group's investor base, comprising primarily specialist venture capital organisations The key risks facing the Group are as follows

Product risk

The development of a new therapeutic agent carries substantial risks, including difficulties in the design and execution of studies to evaluate the efficacy and safety of the agent or the results from such studies being inconsistent with those from earlier studies In addition, the pharmaceutical sector is highly competitive with many companies pursuing similar therapeutic approaches There is substantial risk that competitors' agents may reach the market ahead of those of the Group or have a superior profile to the Group's agents, or that the Group's patent filings may be found to infringe the rights of others or be declared invalid

Financing risk

Until it has sustainable revenues from marketed products, the Group is highly dependent upon raising new equity finance to execute its long term business plan Such finance may not be available on acceptable terms or at all The Group is seeking to raise further funds through product licensing arrangements Such licensing arrangements may not be executable on mutually acceptable terms or at all The Group currently receives finance income from its cash and short-term deposits and R&D tax credit payments A substantial reduction in base interest rates or a substantial reduction in scope or withdrawal of the R&D tax credit scheme will have an adverse effect on the Group's financial position

Directors' report (continued)

Regulatory risk
The pharmaceutical sector is regulated by relevant authorities in the EU, US and the rest of the world There is substantial risk that the Group may not be able to agree study designs with regulatory authorities that are mutually acceptable or that regulatory requirements may change during the course of a study, rendering the results of the study unusable

Future developments
The Group intends to progress its pipeline of novel therapeutic agents during 2008 and expects that research and development expenditure will increase modestly, reflecting the anticipated progression of its novel agents CHR-3996 and CHR-2845 from preclinical to clinical development

Share capital
During the year, 3,676,471 C convertible preferred ordinary shares were issued fully paid for cash and 40,000 C ordinary shares were issued at the nominal value of £0 001 per share Further details can be found in Note 12 to the financial statements

Results and dividends
The Group made a loss for the year of £11,662,080 (year ended 31 December 2006 loss of £7,623,820) The directors do not recommend the payment of a dividend Expenditure on tangible fixed assets during the year was £143,096 (year ended 31 December 2006 £343,617)

Directors and their interests
The directors who held office during the year and their interests in the share capital of the Company, as recorded in the register of directors' interests, of those serving at the year end, were as follows

	Options over ordinary shares of £0 001 each		Ordinary shares of £0 001 each	
	At 31 December 2007	**At 31 December 2006**	**At 31 December 2007**	**At 31 December 2006**
J F Abell (resigned 23/2/07)	-	-	-	-
P V Allen	-	-	80,000	80,000
Dr J Eskay-Eagle (resigned 20/3/07)	-	-	-	-
T J Haines (appointed 23/2/07)	-	-	-	-
Dr J Hemberger	-	-	40,000	40,000
I J Nicholson	650,000	450,000	450,000	450,000
Dr S J Powell (resigned 20/3/07)	-	-	-	-
Dr P T Vainio	-		40,000	40,000
Dr K Veitinger (appointed 1/4/07)	-	-	40,000	-
Prof P Workman	-	-	140,000	140,000

Ordinary shares issued to directors and employees are subject to a vesting period of between 13 months and 59 months from the date of issue Vesting conditions for share options are detailed in Note 11 to the financial statements

Financial risk management
During the year ended 31 December 2007, the Group initiated a number of preclinical and clinical studies in the US, resulting in a material exposure to the US dollar The Group managed this exposure by purchasing US dollars at a rate which was favourable to its budgeted exchange rate, and holding these balances to settle its US dollar-denominated obligations The Group continually reviews its exposure to different foreign currencies and will enter into the most appropriate hedging arrangements to minimise the impact of adverse exchange rate movements where necessary To the extent that cash reserves are not required to meet immediate operational requirements, excess reserves are invested in fixed interest investment grade bank deposits The impact of a reduction in base interest rates is not considered to represent a material exposure for the Group, hence the Group does not enter into any interest rate hedging arrangements The Group does not have any material exposure to credit risk

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Directors' report (continued)

Directors' qualifying third party indemnity provisions
The Company has granted an indemnity to its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies Act 1985 Such qualifying third party indemnity provision remains in force as at the date of approving the directors' report

Charitable and political donations
The Group did not make any charitable or political donations during the year

Payment of creditors
The Group's policy with respect to the payment of its suppliers is to either use standard payment terms or to agree payment terms when entering into a transaction and to abide by those terms Trade payables as at 31 December 2007 represented 38 days as a proportion of the total purchases during the financial year

Disclosure of information to the auditors
So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware Having made enquiries of fellow directors and the Group's auditor, each director has taken all the steps that they are obliged to take as a director in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information

Re-appointment of auditors
A resolution to reappoint Ernst & Young LLP as auditors and to authorise the directors to fix their remuneration will be proposed at the forthcoming Annual General Meeting

Statement of directors' responsibilities in respect of the consolidated financial statements
Company Law requires that the directors are responsible for preparing the Annual Report and the consolidated financial statements in accordance with applicable United Kingdom law and have elected to prepare consolidated financial statements in accordance with those International Financial Reporting Standards as adopted by the European Union Company law requires the directors to prepare consolidated financial statements for each financial period which give a true and fair view of the state of affairs of the Group and the Company of the income statement of the group for that period In preparing those consolidated financial statements, the directors are required to

- select suitable accounting policies in accordance with IAS8 Accounting Policies, Changes in Accounting Estimates and Errors, and apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state that the group has compiled with IFRSs, subject to any material departures disclosed and explained in the financial statements, and
- prepare the consolidated financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the consolidated financial statements comply with the Companies Act 1985 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

Events after the balance sheet date
Events after the balance sheet date are detailed in Note 18 'Events after the balance sheet date'

This report was approved by the Board on 23 May 2008 and has been prepared in accordance with the Companies Act 1985

By order of the Board

R E Bungay
Secretary

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Independent auditors' report to the shareholders of Chroma Therapeutics Limited

We have audited the Group and parent company financial statements ("financial statements") of Chroma Therapeutics Limited for the year ended 31 December 2007 which comprise the consolidated income statement, the consolidated and parent company balance sheets, the consolidated and parent company statement of changes in equity, the consolidated and parent company cash flow statement, and the related notes 1 to 19 These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985 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

The directors' responsibilities for preparing the financial statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We also report to you whether the information given in the Directors' Report is consistent with the financial statements

In addition, we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements

Opinion

In our opinion

- the group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 December 2007 and of its loss for the year then ended,
- the parent company financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union as applied in accordance with the provisions of the Companies Act 1985, of the state of the parent company's affairs as at 31 December 2007,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the directors' report is consistent with the financial statements

Ernst & Young LLP

Ernst & Young LLP
Registered auditor
Reading
Date 23 May 2008

Chroma THERAPEUTICS

Consolidated income statement
for the year ended 31 December 2007

	Note	Year ended 31 December 2007 £	Year ended 31 December 2006 £
Revenue		59,757	-
Research and development costs	4	(12,259,858)	(8,304,824)
Administrative expenses	4	(1,841,883)	(1,347,921)
Loss before financing items		(14,041,984)	(9,652,745)
Finance revenue	10	1,190,847	954,680
Loss before taxation		(12,851,137)	(8,698,065)
Tax credit	7	1,189,057	1,074,245
Loss for the year		(11,662,080)	(7,623,820)

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Consolidated balance sheet
as at 31 December 2007

	Note	31 December 2007 £	31 December 2006 £
ASSETS			
Non current assets			
Property, plant and equipment	8	402,258	548,729
Current assets			
Trade and other receivables		613,423	651,876
R&D tax credit receivable	7	1,189,057	1,073,995
Prepayments		324,377	273,149
Cash and short term deposits	10	16,276,472	22,027,655
		18,403,329	24,026,675
TOTAL ASSETS		18,805,587	24,575,404
EQUITY AND LIABILITIES			
Equity			
Issued capital	12	41,428	37,711
Share premium	12	48,666,004	43,656,991
Warrants	13	118,934	121,507
Other reserves	12	187,316	66,503
Retained earnings		(32,724,538)	(21,062,458)
Total equity		16,289,144	22,820,254
Current liabilities			
Trade and other payables	14	2,516,443	1,755,150
TOTAL EQUITY AND LIABILITIES		18,805,587	24,575,404

Approved by the Board on 23 May 2008 and signed on its behalf by

I J Nicholson
Director

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Company balance sheet
as at 31 December 2007

	Note	31 December 2007 £	31 December 2006 £
ASSETS			
Non current assets			
Property, plant and equipment	8	402,258	548,729
Investment in subsidiary companies	9	2	-
		402,260	548,729
Current assets			
Trade and other receivables		613,423	651,876
R&D tax credit receivable	7	1,189,057	1,073,995
Prepayments		324,377	273,149
Cash and short term deposits	10	16,276,472	22,027,655
		18,403,329	24,026,675
TOTAL ASSETS		18,805,589	24,575,404
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TOTAL EQUITY AND LIABILITIES		18,805,589	24,575,404

Approved by the Board on 23 May 2008 and signed on its behalf by

I J Nicholson
Director

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Consolidated and company statement of changes in equity

for the year ended 31 December 2007

	Issued capital £	Share premium £	Warrants £	Other reserves £	Retained earnings £	Total equity £
At 1 January 2006	19,249	18,815,485	-	8,927	(13,317,131)	5,526,530
Issue of C preferred ordinary shares for cash (Note 12)	18,382	24,981,617	-	-	-	24,999,999
Issue of warrants (Note 13)	-	-	121,507	-	(121,507)	-
Issue of ordinary shares for cash (Note 12)	80	31,920	-	-	-	32,000
Expenses of issuing new equity (Note 12)	-	(172,031)	-	-	-	(172,031)
Expense of share options issued to employees (Note 11)	-	-	-	57,576	-	57,576
Loss for the year	-	-	-	-	(7,623,820)	(7,623,820)
At 31 December 2006	37,711	43,656,991	121,507	66,503	(21,062,458)	22,820,254
Issue of C preferred ordinary shares for cash (Note 12)	3,677	4,996,323	-	-	-	5,000,000
Issue of ordinary shares for cash (Note 12)	40	15,960	-	-	-	16,000
Expenses of issuing new equity (Note 12)	-	(3,270)	-	-	-	(3,270)
Expense of share options issued to employees (Note 11)	-	-	-	120,813	-	120,813
Adjustment to the fair value of warrants	-	-	(2,573)	-	-	(2,573)
Loss for the year	-	-	-	-	(11,662,080)	(11,662,080)
At 31 December 2007	41,428	48,666,004	118,934	187,316	(32,724,538)	16,289,144

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Consolidated and company cash flow statement

for the year ended 31 December 2007

	Note	Year ended 31 December 2007 £	Year ended 31 December 2006 £
Cash flows from operating activities			
Loss before financing items		(14,041,984)	(9,652,745)
Adjustments to reconcile loss before tax to net cash flows			
Non-cash items			
• Expense of share options issued to employees		120,813	57,576
• Shares issued to directors at nominal value	12	15,960	31,920
• Depreciation and impairment	8	289,567	271,658
Working capital adjustments			
• Income tax received		1,073,995	806,267
• Increase in payables		761,293	580,658
• Increase in receivables		(97,154)	(266,662)
Net cash flows used in operating activities		(11,877,510)	(8,171,328)
Cash flows from investing activities			
Purchase of property, plant and equipment	8	(143,096)	(343,617)
Net cash flows used in investing activities		(143,096)	(343,617)
Cash flows from financing activities			
Interest received		1,272,653	657,381
Proceeds from issue of shares	12	5,000,040	25,000,079
Transaction costs of issue of shares	12	(3,270)	(172,031)
Net cash flows from financing activities		6,269,423	25,485,429
Net (decrease)/increase in cash and cash equivalents		(5,751,183)	16,970,484
Cash and cash equivalents at start of period		22,027,655	5,057,171
Cash and cash equivalents at end of period	10	16,276,472	22,027,655

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Notes to the consolidated financial statements

for the year ended 31 December 2007

1 CORPORATE INFORMATION

The group and company financial statements of Chroma Therapeutics Limited for the year ended 31 December 2007 ("financial statements") were authorised for issue in accordance with a resolution of the directors on 2 May 2008 Chroma Therapeutics Limited is a limited company incorporated in England & Wales and domiciled in the United Kingdom

2 BASIS OF PREPARATION

The consolidated financial statements have been prepared on a historical cost basis, except for employee share options, warrants and items settled by issue of shares, which have been measured at fair value The financial statements are presented in sterling and all values are rounded to the nearest pound

Going concern

The consolidated financial statements have been prepared on a going concern basis In common with other companies in the biotechnology sector, the Group is dependent upon raising new finance to support its research and development operations until such time as it has sustainable revenues from marketed products Per Note 18 'Events after the balance sheet date', at the date of signing the financial statements the Group had entered into a £7 5 million debt financing facility that is expected to extend available cash resources to meet the Group's current cash flow projections until the second half of 2009 The Group also continues to review future financing options, including revenue from licensing activities and equity financing Accordingly, the directors believe that it is appropriate to continue to prepare the financial statements on a going concern basis

Basis of consolidation

The consolidated financial statements comprise the financial statements of Chroma Therapeutics Limited and its subsidiary as at 31 December each year Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases The financial statements of the subsidiaries are prepared with the same accounting reference date of 31 December, using consistent accounting policies All intra-group transactions are eliminated in full

Statement of compliance

The financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and in accordance with the Companies Act 1985

Changes in accounting policies

The accounting policies adopted by the Group are consistent with the previous financial year except as follows

The Group has adopted the following new and amended IFRSs and IFRIC interpretations with effect from 1 January 2007

- IFRIC 9 *Reassessment of Embedded Derivatives*

The Group has also early-adopted the following IFRIC interpretation relevant to the Group during the year

- IFRIC 11 *IFRS2 – Group and Treasury Share Transactions*

The principal effect of these changes was as follows

IFRIC 9 *Reassessment of Embedded Derivatives*

IFRIC 9 states that the date to assess the existence of an embedded derivative is the date that an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows As the Group has no embedded derivative requiring separation from the host contract, the Interpretation had no impact on the financial position or performance of the Group

Notes to the consolidated financial statements
for the year ended 31 December 2007

2 BASIS OF PREPARATION (continued)

IFRIC 11 *IFRS2 – Group and Treasury Share Transactions*
The Group has elected to adopt IFRIC Interpretation 11 as of 1 January 2007 This Interpretation requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme, even if the entity buys the instruments from another party, or the shareholders provide the equity instruments needed The Group has determined that the accounting treatment of share options issued to employees is unchanged by the Interpretation, consequently the Interpretation had no impact on its financial position or performance

New standards and interpretations not applied
During the year and up to the date of signing the 2007 financial statements, the IASB and IFRIC have issued the following amendments of standards and new interpretations relevant to the Group with an effective date after the date of these financial statements and which the Group has not applied in its 2007 financial statements

Amendment to IFRS2 *Share-based Payment – Vesting Conditions and Cancellations*
This amendment to IFRS2 *Share-based Payment* was published in January 2008 and becomes effective for financial years beginning on or after 1 January 2009 The Standard restricts the definition of "vesting conditions" to a condition that includes an explicit or implicit requirement to provide services Any other conditions are non-vesting conditions, which have to be taken into account to determine the fair value of the equity instruments granted In the case that the award does not vest as a result of a failure to meet a non-vesting condition that is within the control of either the entity or the counterparty, this must be accounted for as a cancellation As detailed in Note 11, share options issued by the Company expire after 10 years from their commencement date, and are only exercisable in the event of an initial public offering of the Company's shares or trade sale of the Company Since the options outstanding at 31 December 2007 had a weighted average remaining contractual life of 8 2 years, the Group does not anticipate the adoption of the revised Standard will have any impact on its financial position or performance

IFRS 3R *Business Combinations and IAS 27R Consolidated and Separate Financial Statements*
These revised Standards were issued in January 2008 and become effective for financial years beginning on or after 1 July 2009 IFRS 3R introduces a number of changes in the accounting for business combinations that will impact the amount of goodwill recognised, the reported results in the period that an acquisition occurs, and future reported results IAS 27R requires that a change in the ownership interest of a subsidiary is accounted for as an equity transaction Therefore, such a change will have no impact on goodwill, nor will it give rise to a gain or loss Furthermore, the amended Standard changes the accounting for losses incurred by the subsidiary, as well as the loss of control of a subsidiary The changes introduced by IFRS 3R and IAS 27R must be applied prospectively and will affect future acquisitions and transactions with minority interest The revised standards have not yet been adopted by the EU

Amendments to IAS 1 'Presentation of Financial Statements' – *A Revised Presentation*
The revised IAS 1 *Presentation of Financial Statements* was issued in September 2007 and becomes effective for financial years beginning on or after 1 January 2009 The Standard separates owner and non-owner changes in equity The statement of changes in equity will include only details of transactions with owners, with all non-owner changes in equity presented as a single line In addition, the Standard introduces the statement of comprehensive income, which represents all items of income and expense recognised in profit and loss, together with all other items of recognised income and expense, either in one single statement, or in two linked statements There will be no impact on the Group's reported income or net assets This amendment has not yet been adopted by the EU

Notes to the consolidated financial statements
for the year ended 31 December 2007

2 BASIS OF PREPARATION (continued)

Amendments to IAS 32 'Financial Instruments Presentation' and IAS 1 'Presentation of Financial Statements' *Puttable Financial Instruments and Obligations Arising on Liquidation*
Amendments to IAS 32 'Financial Instruments Presentation' and IAS 1 were issued in February 2008 and become effective for financial years beginning on or after 1 January 2009 The amendment to IAS 32 requires certain puttable financial instruments and obligations arising on liquidation to be classified as equity if certain criteria are met The amendment to IAS 1 requires disclosure of certain information relating to puttable instruments classified as equity The Group does not expect these amendments to impact its financial statements The revised standards have not yet been adopted by the EU

Significant accounting judgements, estimates and assumptions
The Group has not applied any judgements (other than estimations) having a significant effect on any amounts recognised in the financial statements The Group has not identified any assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Property, plant and equipment
Plant and equipment is stated at cost, excluding the costs of routine servicing, less accumulated depreciation and accumulated impairment in value Such cost includes the cost of replacing part of such plant and equipment when that cost is incurred, if the recognition criteria are met Depreciation is calculated on a straight line basis over the useful life of the assets The carrying value of plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable

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

The asset's residual values, useful lives and methods are reviewed, and adjusted if appropriate, at each financial year end

Intangible assets
Intangible assets are measured on initial recognition at cost Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is expensed as incurred The useful lives of intangible assets are assessed to be either finite or indefinite Intangible assets with finite lives are amortised over the useful economic life and are assessed for impairment whenever there is indication that the intangible asset may be impaired The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible asset

Intangible assets with indefinite useful lives are tested for impairment annually Such intangibles are not amortised The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis

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Notes to the consolidated financial statements
for the year ended 31 December 2007

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets (continued)

Research and development costs
The principal business activity of the Group is the research and development of human therapeutic agents In order to achieve authorisation from the appropriate regulatory authorities to sell human therapeutic agents, multiple studies and clinical trials must be successfully completed Such activities require the application of substantial resources and skilled individuals, which may not be available to the Group on a timely basis or at all The risks associated with the successful completion of a registration programme for a therapeutic agent are substantial In many cases the Group may choose to license its therapeutic programmes to a third party with substantially greater resources, however the risks associated with successful completion of a registration programme remain high

Research costs are expensed as incurred Reflecting the risks highlighted above, the Group capitalises internal development costs only to the extent that it is more likely than not that the associated therapeutic agent will obtain authorisation from regulatory authorities The threshold for such recognition will normally be the successful completion of the final human clinical studies required to complete a registration package for a therapeutic agent The value of such an intangible asset is calculated with reference to the useful economic life of, and the projected revenues from, the therapeutic agent

Likewise, the Group may from time to time acquire rights to use the intellectual property of a third party in the conduct of its research and development programmes The ability to generate future economic benefits from such rights are subject to the successful registration of the programmes using such intellectual property, and therefore the same risks as noted above Consequently, intangible assets arising from acquired intellectual property rights are subject to the same recognition criteria as internal development costs, as noted above

The Group has not incurred any costs meeting the recognition criteria detailed above to date

Impairment of assets
The Group assesses at each reporting date whether there is an indication that an asset may be impaired If any such indication exists, or where annual impairment testing for an asset is required, the Group makes an estimate of the assets recoverable amount An assets recoverable amount is the higher of an assets fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets Where the carrying value of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount 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 Impairment losses of continuing operations are recognised in the income statement in those expense categories consistent with the function of the impaired asset

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased If such indication exists, the recoverable amount is estimated A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised If that is the case the carrying amount of the asset is increased to its recoverable amount That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years Such reversal is recognised in the income statement unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase After such a reversal the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and short-term deposits
Cash and short-term deposits in the balance sheet comprise cash at banks net of outstanding bank overdrafts, cash in hand and treasury deposits All treasury deposits are held to meet operational needs, have an original maturity of twelve months or less, are readily tradable and are recorded in the balance sheet at their open market value Consequently, all treasury deposits are classified as cash and cash equivalents

Leases
The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent upon the use of a specific asset or assets or the arrangement conveys a right to use the asset A reassessment is made after the inception of the lease only if one of the following applies

a There is a change in contractual terms, other than a renewal or extension of the arrangement,
b A renewal option is exercised or extension granted, unless the term of the renewal or extension was initially included in the lease term,
c There is a change of the determination of whether fulfilment is dependent upon a specified asset, or
d There is a substantial change to the asset

When a reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gave rise to the reassessment for scenarios a, c and d and at the date of renewal or extension for scenario b

Company as lessee
Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term

Pensions and other post-employment benefits
The Company operates a defined contribution pension scheme and pension contributions are charged to the income statement as incurred

Share-based payment transactions
From time-to-time the Company issues shares as consideration for rights granted under technology licence agreements and grants share options to employees of the Group Both types of share-based payment are equity settled transactions as detailed below

Equity-settled transactions
The cost of equity-settled technology rights transactions is measured by reference to fair value of the equity issued at the date on which the relevant technology rights are granted to the Group The cost is expensed to the income statement immediately on obtaining such rights

The cost of equity-settled transactions with employees and directors is measured by reference to the fair value at the date at which they are granted (after approval by the directors) and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees and directors become fully entitled to the award Fair value is determined using the Black-Scholes pricing model In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the Company (market conditions) No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied

Notes to the consolidated financial statements
for the year ended 31 December 2007

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Share-based payment transactions (continued)
At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions, number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above The movement in cumulative expense since the previous balance sheet date is recognised in the income statement, with a corresponding entry in equity

Where the terms of an equity-settled award are modified or a new award is designated as replacing a cancelled or settled award, the cost based on the original award terms continues to be recognised over the original vesting period In addition, an expense is recognised over the remainder of the new vesting period for the incremental fair value of any modification, based on the difference between the fair value of the original award and the fair value of the modified award, both as measured on the date of the modification No reduction is recognised if this difference is negative Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any cost not yet recognised in the income statement for the award is expensed immediately Any compensation paid up to the fair value of the award at the cancellation or settlement date is deducted from equity, with any excess over fair value being treated as an expense in the income statement

Warrants
Warrants to subscribe to the Company's C convertible preferred ordinary shares are measured at the date of issue using the Black-Scholes pricing model taking into account the terms and conditions upon which the instruments were granted (see Note 13) Whilst the number of shares issueable under the warrants or the warrant's exercise price is floating, the warrants are treated as a derivative liability, with the fair value of warrants being remeasured at each balance sheet date and any movement in the fair value recognised through the income statement The fair value of the warrants at the date of issue is ordinarily recognised as a liability in the balance sheet with the corresponding debit being deducted from the retained earnings account, until such point as the number of shares issueable under the warrants and the exercise price become fixed, at which time the fair value of the liability is reclassified as equity

Revenue recognition
Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured The following specific recognition criteria must also be met before revenue is recognised

Interest income
Revenue is recognised as interest accrues using the effective interest rate method

Government grants
Government grants are recognised where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with Where the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate Where the grant relates to an asset it is recognised as income over the expected useful life of the relevant asset on a straight line basis

Taxation

Current tax
Current tax assets for the current and prior periods are measured at the amount expected to be recovered from the taxation authorities The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date

Notes to the consolidated financial statements
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3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxation (continued)
The amount recorded in the financial statements as research and development tax credit receivable by the Group for the financial year ended 31 December 2007 is an estimated amount and has not yet been agreed with HM Revenue & Customs

Deferred tax
Deferred income tax is provided using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax credits and unused tax losses can be utilised The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised Unrecognised deferred income tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered

Deferred tax assets and liabilities are measured on an undiscounted basis at the tax rates that are expected to apply to the year when the asset is realised, based on tax rates (and tax laws) enacted or substantively enacted at the balance sheet date

Foreign currency translation
Monetary assets and liabilities in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date Transactions in foreign currencies are translated into sterling at the rate ruling on the date of the transaction All exchange differences arising in the normal course of business are taken to the income statement as they arise

4 OTHER REVENUE AND EXPENSES

(a) Government grants
During the year ended 31 December 2006, a consortium of which the Group is a member was awarded an EU grant for a long-term collaborative research project Under the terms of the consortium agreement, the Group will provide drug discovery and lead optimisation services to the consortium and, as consideration, may receive up to €753,750 in grant income dependent upon achieving pre-agreed milestones Should the Group breach its obligations under the consortium agreement, the consortium may request the Group repays some or all of the grant income it has received Grant income is recognised only to the extent that the Group has achieved its pre-agreed milestones to the satisfaction of the consortium The revenue recognised in the income statement is calculated by comparing the cumulative expenditure at the end of each financial period with the total estimated costs to complete the Group's obligations, and matching the grant income accordingly

During the year ended 31 December 2007, the Group received an initial grant payment of €320,267 (£215,175 at the exchange rate ruling on the date of receipt) from the consortium, of which £59,757 has been recognised in the income statement and £155,418 has been classified as deferred income

Notes to the consolidated financial statements
for the year ended 31 December 2007

4 OTHER REVENUE AND EXPENSES (continued)

(b) Depreciation and amortisation included in the income statement

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Included in research and development costs		
Depreciation and impairment	261,541	253,359
Operating lease expense	303,247	284,788
Included in administrative expenses		
Depreciation and impairment	28,026	18,299
Operating lease expense	91,241	85,686
Net foreign exchange differences	65,872	1,335

(c) Employee benefits expense

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Wages and salaries	3,095,073	2,438,902
Social security costs	369,392	288,553
Pension costs	272,775	231,817
Expense of share options issued to employees	120,813	57,576
	3,858,053	3,016,848
Of which		
Included in research and development costs	2,642,252	2,088,885
Included in administrative expenses	1,215,801	927,963
	3,858,053	3,016,848

(d) Fees paid to auditors
Administrative Expenses include fees paid to the auditors for audit services of £20,000 (year ended 31 December 2006 £15,900), for other services relating to taxation of £18,450 (year ended 31 December 2006 £1,950) and other accounting services of £nil (year ended 31 December 2006 nil)

5 EMPLOYEES

The average number of employees of the Group during the year was as follows

	Year ended 31 Dec 2007	Year ended 31 Dec 2006
Research and development	44	40
Administration	10	8
	54	48

Notes to the consolidated financial statements
for the year ended 31 December 2007

6 DIRECTORS' REMUNERATION

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Total emoluments	369,979	271,342
Employers contributions paid to money purchase pension schemes	20,000	20,000

As at 31 December 2007, one director (31 December 2006 one director) was accruing benefits under defined contribution pension schemes

The amounts in respect of the highest paid director are as follows

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Total emoluments	266,229	201,342
Employers contributions paid to money purchase pension schemes	20,000	20,000

7 TAXATION

(a) Current income tax

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
UK corporation tax	-	-
R&D tax credit receivable – draft claim for financial year	1,189,057	1,073,995
R&D tax credit receivable – adjustment in financial year relating to claims for prior periods	-	250
	1,189,057	1,074,245

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Notes to the consolidated financial statements
for the year ended 31 December 2007

7 TAXATION (continued)

(b) Factors affecting the tax credit for the year

The tax assessed on the loss for the year is lower than the standard rate of UK corporation tax The differences are explained below

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Loss before tax	(12,851,137)	(8,698,065)
Loss before tax multiplied by standard rate of corporation tax in the UK of 30% (year ended 31 December 2006 30%)	(3,855,341)	(2,609,420)
Effect of		
Disallowed expenses and non-taxable income	53,184	30,568
50% enhanced deduction – R&D relief	(1,163,546)	(841,651)
Timing differences between capital allowances and depreciation charges	46,514	19,761
Adjustment relating to prior years	-	(250)
Other timing differences	25,314	(89,190)
Losses surrendered for R&D tax credit at 16% (year ended 31 December 2006 16%)	1,040,425	939,746
Unrelieved tax losses	2,664,393	1,476,191
Current tax credit for the period	(1,189,057)	(1,074,245)

(c) Deferred income tax

The deferred tax asset not recognised in the financial statements is as follows

	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Capital allowances in advance of depreciation	(60,588)	(100,291)
Other temporary differences	(71,959)	(97,273)
Tax losses available	7,178,469	4,514,076
	7,045,922	4,316,512

The deferred tax asset has not been recognised as there is uncertainty regarding when suitable future profits against which to offset the accumulated tax losses will arise There is no expiration date for the accumulated tax losses

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Notes to the consolidated financial statements

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8 PROPERTY, PLANT AND EQUIPMENT

31 December 2007

	Group and Company		
	Leasehold improvements £	**Plant and equipment £**	**Total £**
At 1 January 2007, net of accumulated depreciation and impairment	169,481	379,248	548,729
Additions	35,149	107,947	143,096
Depreciation charge for the year	(19,455)	(270,112)	(289,567)
At 31 December 2007, net of accumulated depreciation and impairment	185,175	217,083	402,258
At 1 January 2007			
Cost	183,496	938,848	1,122,344
Accumulated depreciation and impairment	(14,015)	(559,600)	(573,615)
Net carrying amount	169,481	379,248	548,729
At 31 December 2007			
Cost	218,645	1,033,677	1,252,322
Accumulated depreciation and impairment	(33,470)	(816,594)	(850,064)
Net carrying amount	185,175	217,083	402,258

During the year ended 31 December 2007 the Group disposed of assets with an original cost of £13,118 that had been fully written down through depreciation and impairment charges in prior financial periods

As at 31 December 2007, fully depreciated assets with an original cost of £443,073 were still in use (31 December 2006 £68,673)

Notes to the consolidated financial statements
for the year ended 31 December 2007

8 PROPERTY, PLANT AND EQUIPMENT (continued)

31 December 2006

	Group and Company		
	Leasehold improvements £	Plant and equipment £	Total £
At 1 January 2006, net of accumulated depreciation and impairment	26,188	450,582	476,770
Additions	155,739	187,878	343,617
Depreciation charge for the year	(12,446)	(259,212)	(271,658)
At 31 December 2006, net of accumulated depreciation and impairment	169,481	379,248	548,729
At 1 January 2006			
Cost	27,757	750,970	778,727
Accumulated depreciation and impairment	(1,569)	(300,388)	(301,957)
Net carrying amount	26,188	450,582	476,770
At 31 December 2006			
Cost	183,496	938,848	1,122,344
Accumulated depreciation and impairment	(14,015)	(559,600)	(573,615)
Net carrying amount	169,481	379,248	548,729

During the year ended 31 December 2006 the Group did not dispose of any assets

The useful life of the assets is estimated as follows

Leasehold improvements	The shorter of 20 years or the lease term
Plant and equipment	3 to 5 years

9 INVESTMENTS

	Company	
	31 Dec 2007 £	31 Dec 2006 £
Investment in subsidiary company	2	-

On 19 December 2007 the Company acquired 100% of a new, wholly-owned subsidiary company, MacroTarg Limited ('MacroTarg'), with an issued share capital of 200 ordinary shares with a nominal value of £0 01 each, for consideration of £2 MacroTarg did not have any trading activities during the year ended 31 December 2007 Subsequent to the year end, the Company transferred certain intellectual property to MacroTarg in return for a further issue of shares, details of which are contained in Note 18 'Events after the balance sheet date'

Notes to the consolidated financial statements
for the year ended 31 December 2007

10 CASH AND SHORT TERM DEPOSITS

	Group and Company	
	31 Dec 2007	31 Dec 2006
	£	£
Cash at bank and in hand	172,354	176,785
Short term deposits	16,104,118	21,850,870
	16,276,472	22,027,655

Cash at bank earns interest at floating rates based on daily bank deposit rates Short term deposits are made for periods between one day and twelve months depending upon the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates Finance revenue comprises the following

	31 Dec 2007	31 Dec 2006
	£	£
Interest receivable on cash at bank and short term deposits	1,188,274	954,680
Gain on remeasurement of warrants (Note 13)	2,573	-
	1,190,847	954,680

11 SHARE-BASED PAYMENT PLANS

Enterprise Management Incentive ('EMI') scheme
All employees of the Group participate in the Company's EMI share option scheme Options granted under this scheme vest over a period of four years from the commencement date and, to the extent they have vested, are only exercisable in the event of an initial public offering of the Company's shares or trade sale of the Company The exercise price of the options is the market value of the Company's ordinary shares at the date of grant of the option The options expire after 10 years from their commencement date The following table illustrates the number and weighted average exercise price (WAEP) of, and movements in, share options during the year

	Year ended 31 Dec 2007		Year ended 31 Dec 2006	
	Number	WAEP	Number	WAEP
Outstanding at the beginning of the period	2,288,800	£0 14	672,500	£0 12
Granted during the period	710,000	£0 40	1,623,800	£0 14
Forfeited during the period	(4,500)	£0 13	(7,500)	£0 12
Outstanding at the end of the period	2,994,300	£0 20	2,288,800	£0 14
Exercisable at the end of the period	-	-	-	-

Notes to the consolidated financial statements
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11 SHARE-BASED PAYMENT PLANS (continued)

The options outstanding at 31 December 2007 had a weighted average remaining contractual life of 8 2 years (31 December 2006 8 8 years) and have exercise prices in the range £0 12 to £0 40 per share (31 December 2006 £0 12 to £0 14 per share) Included within the outstanding options are 102,500 options issued to an employee of the Group and 40,000 options issued to a former director of the Company on an unapproved basis under the rules of the EMI scheme

The fair value of options is measured at the date of grant using the Black-Scholes pricing model, taking into account the terms and conditions upon which the options were granted The following table lists the inputs to the model used for the current and prior financial years

	Year ended 31 Dec 2007	Year ended 31 Dec 2006
Expected volatility (%)	40 0	40 0
Risk-free interest rate (%)	5 5	4 5
Expected life of options (years)	5 0 or 7 0	5 0 or 7 0
Weighted average share price (£)	0 40	0 14

The Group does not have any historic data relating to the expected period to exercise of the options and therefore has estimated this based upon industry experience, with a 7 year period assumed for senior management and a 5 year period assumed for all other employees The expected volatility has been estimated based upon historic data from companies with a similar profile in the biotechnology sector The risk free interest rate represents the Bank of England base interest rate at the date of grant of the option The weighted average share price is determined by performing a share valuation at the date of grant of the options The expense calculation includes an allowance for forfeiture of 15% of the total share options granted other than to senior management, for which the forfeiture rate is estimated as 0% The fair value calculation does not include any allowance for dividends as the Company has no available profits for distribution

The charge to the income statement relating to options during the year is detailed in Note 4

During January 2008, the company issued 38,400 options over ordinary shares to employees of the Group at an exercise price of £0 40 per share

12 ISSUED CAPITAL AND RESERVES

Authorised capital

	31 Dec 2007 Number	31 Dec 2006 Number	31 Dec 2007 £	31 Dec 2006 £
Ordinary shares of £0 001 each	6,900,000	6,900,000	6,900	6,900
Convertible preferred ordinary shares of £0 001 each	13,000,000	13,000,000	13,000	13,000
B-1 convertible preferred ordinary shares of £0 001 each	3,875,969	3,875,969	3,876	3,876
C convertible preferred ordinary shares of £0 001 each	22,426,470	22,426,470	22,426	22,426
			46,202	46,202

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12 ISSUED CAPITAL AND RESERVES (continued)

Issued capital

	31 Dec 2007 Number	31 Dec 2006 Number	31 Dec 2007 £	31 Dec 2006 £
Issued and fully paid				
Ordinary shares of £0 001 each	1,557,200	1,557,200	1,557	1,557
A ordinary shares of £0 001 each	700,000	700,000	700	700
B ordinary shares of £0 001 each	450,000	450,000	450	450
C ordinary shares of £0 001 each	200,000	160,000	200	160
E ordinary shares of £0 001 each	190,000	190,000	190	190
A convertible preferred ordinary shares of £0 001 each	1,766,874	1,766,874	1,767	1,767
B convertible preferred ordinary shares of £0 001 each	10,629,340	10,629,340	10,629	10,629
B-1 convertible preferred ordinary shares of £0 001 each	3,875,969	3,875,969	3,876	3,876
C convertible preferred ordinary shares of £0 001 each	22,058,823	18,382,352	22,059	18,382
			41,428	37,711

Ordinary shares
The Articles of Association allow for the sub-categorisation of the Company's ordinary shares into A, B, C, D, or E ordinary shares These sub-classes have rights identical to the ordinary shares other than being subject to a vesting period of between 13 months and 59 months from the vesting commencement date As at 31 December 2007 191,216 ordinary shares with a total subscription price of £1,012 had not yet vested (31 December 2006 213,510 ordinary shares with a total subscription price of £2,117) The shares issued subject to vesting can be repurchased by the Company at the original subscription price if the employee leaves employment prior to vesting Although such an arrangement has the characteristics of an early-exercised share option, no compensation charge on such share arrangements has been recorded as it is immaterial over the vesting period The unvested shares have been reflected as issued share capital in the balance sheet and not included in the share option data disclosed in Note 11

During the year ended 31 December 2007, the Company issued 40,000 C ordinary shares to a director of the Company and during the year ended 31 December 2006 the Company issued 80,000 shares to certain directors of the Company as part of their remuneration package These shares were issued for cash at the nominal value per share of £0 001 The market value of the ordinary shares at the date of issue has been determined as £0 40 per share The difference of £0 399 between the market value and nominal value per share has been charged to the income statement as an administrative expense and the corresponding amount was credited to the share premium account in the relevant accounting periods

The Company has reserved 3,130,000 ordinary shares (2006 3,250,000 ordinary shares) for issue under options (see Note 11), of which 2,994,300 options were issued and outstanding at 31 December 2007 (31 December 2006 2,288,800)

Notes to the consolidated financial statements
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12 ISSUED CAPITAL AND RESERVES (continued)

Convertible preferred ordinary shares
The convertible preferred ordinary shares carry the right to receive a fixed non-cumulative dividend payable semi-annually, to the extent that the Company has distributable reserves, at the rate of 7% per annum on the subscription price for the A convertible preferred ordinary shares and 8% per annum on the subscription price for the B, B-1 and C convertible preferred ordinary shares Each convertible preferred ordinary share can be converted to one ordinary share automatically upon the flotation or initial listing of the Company on a stock exchange Upon a liquidation or sale of the Company where the proceeds are below the subscription price of the convertible preferred ordinary shareholders, those shares become participating shares in that the distribution of any proceeds after settling arrears of dividends will be applied firstly in returning the capital subscribed by the convertible preferred ordinary shareholders, with the balance being distributed amongst the ordinary and convertible preferred ordinary shareholders as if conversion to ordinary shares had taken place In the event that new shares are issued for consideration less than their respective subscription prices, the B, B-1 and C convertible preferred ordinary shareholders are entitled to a bonus issue of shares In all other respects the ordinary and convertible preferred ordinary shares rank pari passu

During the financial year ended 31 December 2006 the Company issued 18,382,352 new C convertible preferred ordinary shares for total consideration of £24,999,999 to a syndicate of investors ("Series C Investors") The expenses associated with the issue of these shares of £172,031 have been deducted from the Share Premium Reserve The Series C Investors undertook to subscribe to a further 3,676,471 C convertible preferred ordinary shares at £1 36 per share at the call of a majority of non-investor directors of the Company on or before 20 November 2007 (the £5 million "Facility") As consideration for providing the Facility, the Series C Investors were issued with warrants to subscribe to additional C convertible preferred ordinary shares (see Note 13)

During the financial year ended 31 December 2007 the Company issued 3,676,471 new C convertible preferred ordinary shares for total consideration of £5,000,000 following the decision of the Company to call the Facility on 20 March 2007 The expenses associated with the issue of these shares of £3,270 have been deducted from the Share Premium Reserve

Nature and purpose of other reserves
'Other reserves' comprises the cumulative charge for share options issued under the Company's EMI share option scheme (see Note 11)

13 WARRANTS

As detailed in Note 12, the Company issued warrants to the Series C Investors entitling them to subscribe for a predetermined number of C convertible preferred ordinary shares (or, in the event the Company undertakes a flotation or initial listing on a stock exchange, ordinary shares) at a price of £1 36 per share The maximum number of shares issueable to the warrant holders was 367,647, this was reduced to 183,823 shares if the Company called the Facility (see Note 12) by 20 March 2007 or 294,118 shares if the Company called the Facility between 21 March 2007 and 20 June 2007 The Facility was called by the Company on 20 March 2007, fixing the maximum shares issuable to warrant holders at 183,823 The warrants expire on 20 March 2012

Notes to the consolidated financial statements
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13 WARRANTS (continued)

The fair value of warrants is measured at the date of issue using the Black-Scholes pricing model, taking into account the terms and conditions upon which the warrants were granted Following their issue the warrants are treated as a derivative financial instrument since the number of shares issueable under the warrants varies depending upon the date the Facility is called The number of shares issuable under the warrants was fixed at 183,923 on 20 March 2007, consequently as at 31 December 2007 and 31 December 2006 the warrants are classified as equity

While the warrants are treated as derivative financial instruments, their fair value is remeasured at each balance sheet date based upon an assessment of the value of a holding of the underlying C convertible preferred ordinary shares, with any gains or losses being recorded in the income statement As at 31 December 2006 it was determined that all fair value assumptions remained unchanged since the warrants were issued, hence no gain or loss was recorded in the income statement for the year ended 31 December 2006 As at 20 March 2007 (the date at which the warrants ceased to be treated as a derivative financial instrument and became an equity instrument) their fair value was remeasured and fixed It was determined that fair value assumptions relating to expected volatility and weighted average share price had not changed, however, at this date the risk-free interest rate had increased to 5 25% and the expected life of the warrants, estimated as 80 months from the completion of the Series C financing, the maximum term of warrants, was reduced to 6 0 years from the date of remeasurement of fair value As a consequence, a gain of £2,573 was recorded in the income statement for the year ended 31 December 2007

The following table lists the inputs to the Black-Scholes model at fair value measurement dates during 2007 and 2006

	20 Mar 2007 and 31 Dec 2007	**21 Mar 2006 and 31 Dec 2006**
Expected volatility (%)	40 0	40 0
Risk-free interest rate (%)	5 25	4 5
Expected life of warrants (years)	6 0	6 7
Weighted average share price (£)	1 36	1 36

The expected volatility is consistent with that used in the valuation of employee ordinary share options (see Note 11) since the shares underlying both the warrants and employee share options are impacted by the same factors The weighted average share price is the contractual exercise price as the directors have not changed their estimate of the fair value of C convertible preferred ordinary shares since the Series C financing The fair value calculation does not include any allowance for dividends as the Company has no available profits for distribution

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14 TRADE AND OTHER PAYABLES

	Group 31 Dec 2007 £	Company 31 Dec 2007 £	Group and Company 31 Dec 2006 £
Trade payables	1,110,867	1,110,867	1,023,529
Taxation and social security	281,510	281,510	92,256
Deferred income	155,418	155,418	-
Amount payable to subsidiary company	-	2	-
Other payables and accruals	968,648	968,648	639,365
	2,516,443	2,516,445	1,755,150

Other payables and accruals include outstanding contributions payable to the defined contribution pension scheme of £34,542 (31 December 2006 £29,923)

The terms and conditions of the above financial liabilities are as follows

- Trade payables are non-interest bearing and are settled based upon pre-agreed credit terms, typically within 30 days from the date of the invoice
- Taxation and social security creditors and contributions payable to the defined contribution pension scheme are non-interest bearing and are due during the month following payment of the salaries to which they relate
- Other payables are non-interest bearing and primarily comprise accruals for liabilities incurred but not yet invoiced

15 OTHER FINANCIAL COMMITMENTS

Operating leases – Group as lessee
The future minimum rental payable under the operating lease for the Group's premises at 93 Milton Park, reflecting contractual break clauses, is as follows

	Land and buildings 31 Dec 2007 £	Land and buildings 31 Dec 2006 £
Not later than one year	431,891	394,742
After one year but not more than five years	1,430,533	90,845
	1,862,424	485,587

The minimum payments above do not reflect any increase that may arise from the contractual rent review scheduled for 25 March 2008

The Group does not have any operating leases other than that for its premises

Finance leases – Group as lessee
The Group did not have any leasing arrangements classifying as finance leases at 31 December 2007 or 31 December 2006

Capital commitments
Contracted for capital commitments as at 31 December 2007 amounted to £nil (31 December 2006 £22,523)

Notes to the consolidated financial statements

for the year ended 31 December 2007

16 RELATED PARTY DISCLOSURES

Funds managed by Abingworth Management Limited ("Abingworth") held shares in the Company as at 31 December 2007 T J Haines is a director of Abingworth and has a financial interest in Abingworth's funds

Funds managed by Essex Woodlands Health Ventures ("Essex") held shares in the Company as at 31 December 2007 P T Vainio is a director of Essex and has a financial interest in Essex's funds

Compensation of key management personnel of the Company is detailed in Note 6 Director's interests in employee share option schemes are detailed in the Directors' Report

17 TRANSACTIONS WITH DIRECTORS AND OFFICERS

During the period the Group paid consultancy fees to Prof P Workman totalling £32,000 (year ended 31 December 2006 £32,000)

18 EVENTS AFTER THE BALANCE SHEET DATE

Following the year end, the Company issued 38,400 options over ordinary shares to employees of the Group at an exercise price of £0 40 The options vest over a period of 48 months and are only exercisable upon a flotation or trade sale of the Company

As highlighted in Note 9 'Investments', the Company incorporated a new, wholly-owned subsidiary company, MacroTarg Limited ('MacroTarg') on 19 December 2007 On 1 January 2008 the Company assigned certain intellectual property rights to MacroTarg and licensed back rights to use certain elements of these intellectual property rights Contemporaneously with this transfer of intellectual property, the Company entered into agreements under which MacroTarg will reimburse the Company for its provision of certain research and development and administrative services The net transfer of intellectual property rights to MacroTarg was valued at £5 million, which was satisfied by the issue of 5 million ordinary shares of MacroTarg to the Company at a value of £1 per share

As highlighted in Note 2, at the date of signing the financial statements the Group had entered into a £7 5 million debt financing facility ('Facility') that is expected to extend available cash resources to meet the Group's current cash flow projections until the second half of 2009 The Facility has a fixed rate of interest and is repayable over 36 months from the date of drawing down the Facility

19 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICY

In line with similar companies in the biotechnology sector, the Group derives long-term financing through the issue of new equity The Group's principal financial instruments comprise trade payables, operating leases and government grants which arise directly from its operations and are not designed as a means of raising finance for the Group's operations The Group has various financial assets such as receivables and cash and short-term deposits, which arise directly from its operations The Group does not consider that its financial instruments gave rise to any material financial risks during the financial years ended 31 December 2007 and 31 December 2006 An overview of areas of potential risk are summarised below

Interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to finance income from its cash at bank and short-term deposits (see Note 10) The change in the Group's profit or loss before tax arising from a change in the Bank of England base interest rates will depend on the remaining duration of any specific treasury deposits placed at that time and the average cash and cash equivalents for the remainder of the financial year following the change The exposure to changes in base interest rates is not considered to be material The interest rate profile of the Group's financial assets is as follows

Notes to the consolidated financial statements

for the year ended 31 December 2007

19 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICY (continued)

Interest rate risk (continued)

	31 Dec 2007			31 Dec 2006		
	Floating	Fixed	Total	Floating	Fixed	Total
	£	£	£	£	£	£
Cash and short term deposits	759,011	15,517,461	16,276,472	236,784	21,790,871	22,027,655

Foreign currency risk

The Group does not have any overseas operations and therefore does not have any exposure to the retranslation of the assets and liabilities of overseas operations The Group purchases goods and services from a number of international suppliers and therefore has transactional currency exposures During the financial year ended 31 December 2006 these exposures were not significant, consequently the Group did not enter into any currency hedging arrangements during that financial year During the financial year ended 31 December 2007, the Group initiated a number of preclinical and clinical studies in the US, resulting in a material exposure to the US dollar The Group managed this exposure by purchasing US dollars at a rate which was favourable to its budgeted exchange rate and holding these balances to settle its US dollar-denominated obligations The Group intends to continue using currency hedging arrangements to mitigate exposure to movements in the US dollar, either by way of forward purchase contracts relating to scheduled contractual payments or by holding part of its cash and short term deposits as US dollars It is the Group's policy to not enter into any forward purchase contracts until the underlying supply agreements have been executed The aggregate carrying amount of foreign currency denominated monetary assets and liabilities held by the Group and company, which are not denominated in functional currency, as at the reporting date are as follows

	31 Dec 2007		31 Dec 2006	
	Assets	Liabilities	Assets	Liabilities
	£	£	£	£
US dollar ($)	667,182	184,415	27,742	30,546
Euro (€)	586	376,660	191	161,382
Swiss Franc (CHF)	85	77,408	17	17,430
	667,853	638,483	27,950	209,358

The following table illustrates the sensitivity to a reasonably possible change in the currencies above, compared to sterling, of the Group's loss before tax due to the changes in the fair value of monetary assets and liabilities A positive value indicates a decrease in the Group's loss before tax

	Change in rate	31 Dec 2007 £	31 Dec 2006 £
US dollar	+5%	(22,989)	133
	-5%	25,409	(148)
Euro	+5%	17,908	7,676
	-5%	(19,794)	(8,484)
Swiss Franc	+5%	3,682	829
	-5%	(4,070)	(916)

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Notes to the consolidated financial statements

for the year ended 31 December 2007

19 FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICY (continued)

Credit risk

The sole revenues of the Group during the financial year ended 31 December 2007 (31 December 2006 £nil) were recognition of amounts earned under a research grant paid by the EU (see Note 4), consequently the Group did not have any exposure to trade credit risk during this financial year With respect to credit risk arising from the other financial assets of the Group, which primarily comprise cash and short-term deposits, the exposure to credit risk arises from the default of the counterparty, with a maximum exposure equal to the carrying amount of these investments The Group has in place investment guidelines outlining authorised counterparties in order to minimise such risk

Liquidity risk

The Group monitors its funding requirements through preparation of short,-term, mid-term and long-term forecasts All short-term deposits are immediately convertible to liquid funds without penalty and are recorded in the balance sheet at their open market value

Capital management

In line with similar companies in the biotechnology sector at a similar stage of development, the Group is loss-making and does not have any significant trading revenues Reflecting this, the Group funds its operations through a combination of equity issuance, debt financing, government grants and also through funds generated by technology or product licensing activities In light of its ongoing funding requirements, the Group does not have a policy of paying dividends to shareholders except for potential payments to holders of the Company's convertible preferred ordinary shares as permitted in its Articles of Association (Note 12)