2e2 Group Limited

Report and Financial Statements

31 December 2010

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M McVeigh
N Grossman
S Burt

Secretary
S Burt

Auditors
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Directors' report

The directors' present their report and financial statements for the year ended 31 December 2010

Results and dividends

There was a group operating profit for the year of £14 9m (2009 – £11 2m)

The directors are satisfied with the performance of the group during the year They do not recommend the payment of a dividend (2009 – £nil)

Key performance indicators

The senior management of the group focus on a number of key performance indicators These include sales bookings and billings, the value of contracted annuity revenues, gross margins, cash conversion and staff utilisation These, along with other measures, are monitored regularly with explanations sought for variances against expectations Management have reviewed the key performance indicators during the year and are satisfied with the results

Principal activity and review of the business

The principal activity of the group is the delivery of outsourced computer services, focusing on Unified Communications, Technology Solutions, Managed Services and Business Applications Solutions These services are delivered to customers in the UK and Europe The group continues to expand its activities through a combination of organic growth and acquisitions

The retained loss for the year after taxation amounted to £7 3m (2009 – profit of £2 5m)

Included within operating profit, certain exceptional one-off costs have been highlighted on the face of the profit and loss account to give a better understanding of the underlying performance of the group These costs amount to £5 5m (2009 – £4 5m) and relate to the integration and restructuring of the UK companies, and redundancy and restructuring costs in the Netherlands

During the year the Group started to deliver some of its services through a new partnership with Patni Computer Systems The relationship with Patni will help the Group improve customer service, broaden its offerings, and remain cost effective in a competitive market The implementation of this partnership involved significant reorganisation of our operations, and the costs related to this project have been included within costs of fundamental restructuring in the profit and loss account

In June, the Group acquired the entire share capital of Morse plc for £69 6m plus associated costs Morse provides IT Services and Technology to large customers, principally in the UK, Spain and Ireland The acquisition gives 2e2 significant additional scale and service capability, and has strengthened our position in our core vertical markets

We would like to welcome the customers and employees of Morse to the Group

We completed the integration of the UK business of Morse into the wider 2e2 UK business during the second half of the year The costs of this exercise have been included within costs of fundamental restructuring in the profit and loss account

The acquisition was funded by the issue of £85 0m of new preferred ordinary equity in 2e2 Holdings Limited, the Group's ultimate holding company, to Hutton Collins Capital Partners Limited The excess funding is to be used to provide additional working capital to the Group

The Directors are grateful for the support of the Group's funders, and in particular for the support of our new investor, Hutton Collins Capital Partners, in facilitating the acquisition of Morse

Future developments

In the future the group will continue to investigate suitable acquisition opportunities where it feels these will strengthen its offerings to customers The group is also planning to continue the integration activities in order to maximise the benefits of the increasing scale of the group

Directors' report

Principal risks and uncertainties

Discussed below are the group's major business risks, together with systems and initiatives in place to address them

Market risk

The IT services market is subject to fluctuations of demand by customers These fluctuations are linked to the economic cycle and changes in the spending patterns of customers In addition, the group works with a number of key vendors and it is important to maintain strong relationships and terms of business with these partners

Operational risk

This relates to the risk of financial loss resulting from internal processes, people and systems The group manages this risk through appropriate internal controls and proactive intervention, such as management reporting systems, insurances, business interruption and disaster recovery planning

Liquidity risk

This relates to the risk that the group is unable to fund its requirements because of insufficient banking facilities The group manages liquidity risk via revolving credit facilities and long term debt

Interest rates

This relates to the risk of fluctuations in LIBOR, on which the interest charges for the group's bank facilities are based The group manages interest rate risk by entering into interest rate hedging agreements in relation to the majority of its bank borrowings

Credit risk

This relates to the risk that one party to a financial instrument will cause a financial loss for that other party by failing to discharge an obligation Group policies are aimed at minimising such losses and require that deferred terms are only granted to customers who demonstrate an appropriate payment history and satisfy credit worthiness procedures

Going concern

The directors, after making appropriate enquiries, have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future For this reason, the directors continue to adopt the going concern basis in preparing the financial statements

Directors

The directors who served during the year and to the date of this report were as follows

T Burt
M McVeigh
N Grossman
S Burt

Directors' qualifying third party indemnity provision

The company has granted an indemnity to one or more of its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in Section 234 of the Companies Act 2006 Such qualifying third party indemnity provision remains in force as at the date of approving the directors' report

Employee involvement

The group maintains a practice of keeping employees informed of matters affecting them as employees and the financial and economic factors affecting the performance of the group

Directors' report

Disabled employees

Applications for employment by disabled persons are given full and fair consideration for all vacancies in accordance with their particular aptitudes and abilities In the event of employees becoming disabled, every effort is made to retrain them in order that their employment with the group may continue

It is the policy of the group that training, career development and promotion opportunities be available to all employees

Supplier payment policy

It is the policy of the group to pay all amounts due to suppliers as they fall due As at 31 December 2010, trade creditors of the group were equivalent to 52 days purchases (2009 – 50 days)

Share-based payments

All employee share option plan

Employees may be awarded share options as a reward for past performance or to incentivise future performance The options will vest if the employee remains in service for a period of four years from the date of grant The contractual life of the options is ten years and there are no cash settlement alternatives No options were issued during the year

Corporate governance

The directors recognise the importance of adopting good corporate governance practices in the best interests of shareholders as a whole

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 he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information

Auditors

A resolution to reappoint Ernst & Young LLP as auditors will be put to the members at the Annual General Meeting

On behalf of the Board

Simon Burt
Director

31 March 2011

Statement of directors' responsibilities

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards 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 group and the company and of the profit or loss of the group for that period In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgments and estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, 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 proper accounting records that are sufficient to show and explain the group's and the company's transactions and disclose with reasonable accuracy at any time the financial position of the group and the company and enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the group and company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

Independent auditors' report

to the members of 2e2 Group Limited

We have audited the group and parent undertaking financial statements of 2e2 Group Limited for the year ended 31 December 2010 which comprise the Group Profit and Loss Account, the Group Statement of Total Recognised Gains and Losses, the Group and Company Balance Sheets, the Group Cash Flow Statement and the related notes 1 to 30 The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice)

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

Respective responsibilities of directors and auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) These standards require us to comply with the Auditing Practice's Board's (APB's) Ethical Standards for Auditors

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error This includes as assessment of whether the accounting policies are appropriate to the company's and parent undertaking's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements

Opinion on the financial statements

In our opinion the financial statements

- give a true and fair view of the state of the group's and the parent undertaking's affairs as at 31 December 2010 and of the company's loss for the year then ended
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, 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 by the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements

Independent auditors' report

to the members of 2e2 Group Limited

Matters on which we are required to report by exception

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

- Adequate accounting records have not been kept by the parent undertaking, or returns adequate for our audit have not been received from branches not visited by us, or
- The parent undertaking 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

Ernst + Young LLP

Kevin Harkin (Senior Statutory Auditor)
For and on behalf of Ernst & Young LLP, Statutory Auditor
Reading
31 March 2011

Group profit and loss account

for the year ended 31 December 2010

	Notes	*2010* *£000*	*2009* *£000*
Turnover			
Continuing operations		213,751	200,075
Acquisitions		113,282	–
		327,033	200,075
Discontinued operations		–	731
Group turnover	2	327,033	200,806
Cost of sales		(213,105)	(127,427)
Gross profit		113,928	73,379
Administration expenses		(76,063)	(43,396)
Operating profit before depreciation, amortisation of goodwill and exceptional items*		37,865	29,983
Depreciation (non-rental assets)		(6,620)	(5,661)
Amortisation of goodwill	3	(10,843)	(8,577)
Exceptional administration expenses	3	(5,458)	(4,522)
Operating profit			
Continuing operations		5,048	12,203
Acquisitions	3	9,896	–
		14,944	12,203
Discontinued operations		–	(980)
Group operating profit	3	14,944	11,223
Cost of fundamental restructuring	3	(4,875)	–
Net interest payable	6	(17,718)	(11,466)
Loss on ordinary activities before taxation		(7,649)	(243)
Tax	7	323	2,772
(Loss)/profit for the year attributable to members of the parent undertaking	22	(7,326)	2,529

* Non-statutory disclosure, presented for supplementary understanding of the financial statements

Group statement of total recognised gains and losses
for the year ended 31 December 2010

	2010	2009
	£000	*£000*
(Loss)/profit for the year	(7,326)	2,529
Currency translation differences on foreign currency net investments	646	1,313
Total recognised gains and losses related to the year	(6,680)	3,842

Group balance sheet

at 31 December 2010

	Notes	*2010* *£000*	*2009* *£000*
Fixed assets			
Intangible assets – goodwill	10	203,977	138,290
Tangible assets	11	16,749	17,236
		220,726	155,526
Current assets			
Stocks	13	8,077	3,025
Debtors amounts due within one year	14	156,504	73,554
Debtors amounts due after more than one year	14	6,328	6,328
Cash		18,643	540
		189,552	83,447
Creditors amounts falling due within one year	15	(172,760)	(72,505)
Net current assets		16,792	10,942
Total assets less current liabilities		237,518	166,468
Provisions	16	(6,086)	(1,021)
Creditors amounts falling due after more than one year	17	(152,108)	(160,220)
Net Assets prior to group loans falling due after more than one year*		79,324	5,227
Financed by			
Creditors group loans falling due after more than one year*	18	80,777	–
Capital and reserves			
Called up share capital	21	105	105
Share premium account	22	265	265
Other reserves	22	466	466
Profit and loss account	22	(2,289)	4,391
Shareholders' (Deficit)/Funds and Net (Liabilities)/Assets		(1,453)	5,227
		79,324	5,227

* Non-statutory disclosure, presented for supplementary understanding of the financial statements

Simon Burt

Director

31 March 2011

Company balance sheet

at 31 December 2010

	Notes	2010 £000	2009 £000
Fixed assets			
Tangible assets	11	2	1
Investments	12	222	222
		224	223
Current assets			
Debtors	14	160,159	15,732
		160,159	15,732
Creditors. amounts falling due within one year	15	(23)	(46)
Net current assets		160,136	15,686
Total assets less current assets		160,360	15,909
Creditors amounts falling due after more than one year	17	(73,754)	(9,957)
Net Assets prior to group loans falling due after more than one year*		86,606	5,952
Financed by			
Creditors group loans falling due after more than one year*	18	80,777	–
Capital and reserves			
Called up share capital	21	105	105
Share premium account	22	265	265
Other reserves	22	51	51
Profit and loss account	22	5,408	5,531
Shareholders' Funds and Net Assets		5,829	5,952
		86,606	5,952

* Non-statutory disclosure, presented for supplementary understanding of the financial statements

Simon Burt

Director

31 March 2011

Group statement of cash flows
for the year ended 31 December 2010

	Notes	2010 £000	2009 £000
Net cash inflow from operating activities	23(a)	25,578	14,366
Returns on investments and servicing of finance			
Interest received		66	28
Interest paid		(14,779)	(8,168)
Finance lease interest paid		(100)	(97)
Net cash outflow from returns on investments and servicing of finance		(14,813)	(8,237)
Taxation		455	230
Capital expenditure and financial investment			
Purchase of tangible fixed assets		(6,051)	(5,805)
Net cash outflow from capital expenditure and financial investment		(6,051)	(5,805)
Acquisitions and disposals			
Purchase of subsidiary undertakings		(69,629)	–
Net cash from purchase of subsidiary undertakings		11,435	–
Payments in respect of prior year acquisitions		-	(2,494)
Net cash outflow from acquisitions and disposals		(58,194)	(2,494)
Net cash outflow before financing		(53,025)	(1,940)
Financing			
(Repayment) / receipt of borrowings		(4,561)	2,250
Receipt / (repayment) of loans from parent undertaking		76,351	(3,251)
Finance leases		(662)	(237)
Net cash inflow / (outflow) from financing		71,128	(1,238)
Increase / (decrease) in cash	23(b)	18,103	(3,178)

Notes to the financial statements

at 31 December 2010

1. Accounting policies

Basis of preparation

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards and under the historical cost convention

Basis of consolidation

The group financial statements consolidate those of the company and of its subsidiary undertakings (see note 12), drawn up to 31 December 2010

Subsidiary undertakings

The acquisition method of accounting has been adopted for acquisitions Under this method the results of the subsidiary undertakings acquired or disposed of in the year are included in the profit and loss account from the date of acquisition or up to the date of disposal

In the company's financial statements, investments in subsidiary undertakings are stated at cost less any provisions for diminution in value

In accordance with section 408 of the Companies Act 2006, 2e2 Group Limited is exempt from the requirement to present its own profit and loss account

Goodwill

Goodwill arising on consolidation, representing the excess of the fair value of the consideration given over the fair values of the identifiable net assets acquired, is capitalised and is amortised on a straight line basis over its estimated useful economic life, generally 20 years It is reviewed for impairment at the end of the first full financial year following the acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable

Negative goodwill is written back to the profit and loss account to match the recovery of the non-monetary assets acquired

Turnover

Turnover is the total amount receivable by the group for goods supplied and services provided, excluding VAT and trade discounts Service revenues invoiced in advance are taken to income evenly over the period of delivery of the service

In the case of long-term contracts, turnover reflects the contract activity during the year and represents the proportion of total contract value which costs incurred to date bear to total expected contract costs

Revenue from equipment rentals is recognised over the term of the agreement on a straight line basis Any unrecognised revenue element is shown separately in the balance sheet as deferred income For certain rental equipment arrangements, the company receives a discount against the purchase of products from the suppliers of this rental equipment For these arrangements, revenue is equal to the discount received by the company which is recognised over the term of the rental agreement

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost or valuation, net of depreciation and any provision for impairment

Depreciation is calculated to write down the cost of all tangible fixed assets by equal annual instalments over their estimated useful economic lives or lease term if shorter The rates generally applicable are

Leasehold improvements	–	Term of the lease
Computer equipment	–	3–4 years
Fixtures and fittings	–	4 years
Motor vehicles	–	4 years
Rental assets	–	2 – 3 years

The carrying value of tangible assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable

Notes to the financial statements

at 31 December 2010

1. Accounting policies (continued)

Investments

Investments are included at cost less amounts written off

Stocks

Stocks are stated at the lower of cost and net realisable value Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal

Long-term contracts

The attributable profit on long-term contracts is recognised once their outcome can be assessed with reasonable certainty The profit recognised reflects the proportion of work completed to date on the project

Costs associated with long-term contracts are included in stock to the extent that they cannot be matched with contract work accounted for as turnover Long-term contract balances included in stocks are stated at cost, after provision has been made for any foreseeable losses and the deduction of applicable payments on account

Full provision is made for losses on all contracts in the year in which the loss is first foreseen

Deferred taxation

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or right to pay less or to receive more tax, with the following exceptions

- Provision is made for deferred taxation that would arise on remittance of the retained earnings of subsidiaries, associates and joint ventures only to the extent that, at the balance sheet date, dividends have been accrued as receivable
- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date

Foreign currencies

Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction Monetary assets and liabilities in foreign currencies are translated at the rates of exchange ruling at the balance sheet date The financial statements of foreign subsidiaries are translated at the rate of exchange ruling at the balance sheet date The exchange differences arising from the retranslation of the opening net investment in subsidiaries are taken directly to reserves Where exchange differences result from the translation of foreign currency borrowings raised to acquire foreign assets they are taken to reserves and offset against the differences arising from the translation of those assets All other exchange differences are dealt with through the profit and loss account

Research and development

Research and development expenditure is charged to the profit and loss account in the period in which it is incurred

Notes to the financial statements

at 31 December 2010

1. Accounting policies (continued)

Interest rate swaps

The group's criteria for interest rate swaps are

- The instrument must be related to an asset or liability, and
- It must change the character of the interest rate by converting a variable rate to a fixed rate or vice versa

Interest differentials are recognised by accruing with net interest payable Interest rate swaps are not revalued to fair value or shown on the group balance sheet at the year end If they are terminated early, the gain/loss is spread over the remaining maturity of the original instrument

Interest bearing loans

All interest bearing loans and borrowings are initially recognised at proceeds After initial recognition debt is increased by the finance cost in respect of the reporting period and reduced by repayments made in the period

Finance costs of debt are allocated over the term of the debt at a constant rate on the carrying amount

Costs associated to raising the debt are held on the balance sheet and recognised in the profit and loss account over the term of the corresponding debt

Leasing and hire purchase agreements

Assets held under finance leases and hire purchase contracts are capitalised in the balance sheet and depreciated over their estimated useful economic lives The interest element of leasing payments represents a constant proportion of the capital balance outstanding and is charged to the profit and loss account over the period of the lease All other leases are regarded as operating leases and the payments made under them are charged to the profit and loss account on a straight-line basis over the lease term

Provisions

A provision is recognised when the group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation

Pensions

The group operates a number of defined contribution pension schemes Contributions are charged in the profit and loss account as they become payable

Share options

The group issues equity-settled share-based payments to certain employees and advisers Equity-settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions at the date of grant) The fair value so determined has been expensed on a straight-line basis over the vesting period, based on the group's estimate of the number of shares that will eventually vest, and adjusted for the effect of non-market vesting conditions

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

Fair value is measured using a Black-Scholes-Merton option pricing model The key assumptions used in the model have been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations

Notes to the financial statements

at 31 December 2010

2. Turnover

Turnover is wholly attributable to the provision of Information Technology Solutions An analysis of turnover by geographical market is given below

	2010	*2009*
	£000	*£000*
United Kingdom (including the Channel Islands and the Isle of Man)	231,898	168,985
Europe	89,105	31,821
Rest of world	6,030	–
	327,033	200,806

3. Operating profit

This is stated after charging

		2010	*2009*
		£000	*£000*
Auditors' remuneration – audit services	– UK	375	302
	– Overseas	89	85
	– non-audit services	134	79
Depreciation and amortisation	– goodwill (see note 10)	10,843	8,577
	– tangible fixed assets – owned	6,025	5,328
	– held under finance leases and hire purchase contracts	595	333
FRS 20 share option charges		-	4
Other operating lease rentals		6,422	7,830
Exceptional restructuring and integration costs		5,458	4,522

Exceptional restructuring costs

The restructuring costs relate to the following activities

	2010	*2009*
	£000	*£000*
Restructuring costs and redundancy costs in the UK group	4,096	3,358
Restructuring costs and redundancy costs in the Netherlands group	1,362	1,164
	5,458	4,522

Fundamental restructuring costs

The group incurred costs of £4 9m in relation to a fundamental reorganisation These costs were incurred as a result of the reorganisation of the management and operations within the UK business following the acquisition and subsequent integration of Morse plc The businesses had previously been organised as separately managed corporate entities The reorganisation of the operations included the transfer of certain services to Patni Computer Systems, our new offshore service provider

Notes to the financial statements

at 31 December 2010

3. Operating profit (continued)

The amounts shown within the profit and loss account for the year include the following in respect of acquisitions

	2010 £'000	2009 £'000
Cost of sales	(89,050)	-
Gross profit	24,232	-
Administration expenses	(12,150)	-
Depreciation	(95)	-
Exceptional administration expenses	(2,091)	-
	9,896	-

4. Directors' emoluments

For the current year the group has been charged £300,000 for the services provided by the four directors Further details of the director emoluments are disclosed in the financial statements of 2e2 Holdings Limited

During the year four directors participated in money purchase pension schemes, further details are disclosed in 2e2 Holdings Limited financial statements (2009 – three)

5. Staff costs

Staff costs during the year were as follows

	2010 £000	2009 £000
Wages and salaries	71,574	48,429
Social security costs	8,773	5,705
Other pension costs	1,867	1,340
	82,214	55,474

On the acquisition of Morse plc in June 2010, 2e2 Group assumed the defined benefit pension liabilities which may arise under the South Tyneside & Gateshead ("ST&G") Building Schools for the Future contract A provision of £0 7m was made on acquisition to reflect the estimated liability for a total of 40 employees which were originally expected to transfer to Morse At 31 December 2010, eleven employees were transferred and of these two opted out of the pension scheme At the year end, only nine employees were transferred in and all transfers were made on a fully funded basis

The company plans to carry out an actuarial valuation in 2011 and the provision will be reassessed accordingly in the year ended 31 December 2011

Notes to the financial statements

at 31 December 2010

5. Staff costs (continued)

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

	2010	*2009*
	No	*No*
Management and administration	237	185
Sales and marketing	265	158
Operations	1,115	862
	1,617	1,205

6. Interest payable

	2010	*2009*
	£000	*£000*
Interest payable on bank loans	17,684	11,400
Finance charges in respect of finance leases	100	94
	17,784	11,494
Other interest receivable and similar income	(66)	(28)
	17,718	11,466

7. Tax

(a) Tax on loss on ordinary activities

	2010	*2009*
	£000	*£000*
Current tax		
Overseas taxation	(323)	(178)
Adjustments in respect of prior years	-	91
Total current tax (note 7(b))	(323)	(87)
Origination and reversal of timing differences	-	(2,685)
Total deferred tax	-	(2,685)
Tax on loss on ordinary activities	(323)	(2,772)

Notes to the financial statements

at 31 December 2010

7. Tax (continued)

(b) Factors affecting current tax credit for the year

The tax assessed for the year is higher than the standard rate of corporation tax in the UK of 28% (2009 – 28%) The differences are explained as follows

	2010 *£000*	*2009* *£000*
Loss on ordinary activities before tax	(7,649)	(243)
Loss before tax on ordinary activities multiplied by the standard rate of corporation tax in the UK of 28% (2009 – 28%)	(2,142)	(68)
Effects of		
Expenses not deductible for tax purposes	8,201	2,521
Capital allowances in excess of depreciation	1,191	1,177
Utilisation of tax losses	(7,837)	(2,342)
Adjustments to tax charge in respect of previous years	-	91
Group relief received	(200)	(1,374)
Other short-term timing differences	464	(92)
Current tax for the year (note 7(a))	(323)	(87)

8. Profit for the financial year

The parent undertaking's loss for the year ended 31 December 2010 was £0 1m (2009 – loss of £0 2m)

9. Dividends

No dividends were paid or declared during the year (2009 – £nil)

Notes to the financial statements

at 31 December 2010

10. Intangible fixed assets

Group	*2010* *£000*	*2009* *£000*
Goodwill	203,977	138,290

Group	*Goodwill* *£000*	*Negative Goodwill* *£000*	*Total* *£000*
Cost			
At 1 January 2010	164,142	(2,772)	161,370
Additions (note 24)	76,530	–	76,530
At 31 December 2010	240,672	(2,772)	237,900
Amortisation			
At 1 January 2010	(25,852)	2,772	(23,080)
Provided in year	(10,843)	–	(10,843)
At 31 December 2010	(36,695)	2,772	(33,923)
Net book value			
At 31 December 2010	203,977	–	203,977
At 1 January 2010	138,290	–	138,290

The goodwill that has arisen on all acquisitions is being amortised evenly over the estimate of the useful economic life of 20 years

Notes to the financial statements

at 31 December 2010

11. Tangible fixed assets

	Leasehold Improvements *£000*	*Motor Vehicles* *£000*	*Fixtures, Fittings and Computer Equipment* *£000*	*Total* *£000*
Cost				
At 1 January 2010	3,451	222	23,367	27,040
Acquisitions	–	8	566	574
Additions	26	19	5,700	5,745
Foreign Exchange	7	3	(30)	(20)
Disposals	–	(36)	(675)	(711)
At 31 December 2010	3,484	216	28,928	32,628
Depreciation				
At 1 January 2010	1,664	145	7,995	9,804
Provided in the year	125	53	6,442	6,620
Foreign Exchange	6	2	(3)	5
Disposals	–	(27)	(523)	(550)
At 31 December 2010	1,795	173	13,911	15,879
Net book value				
At 31 December 2010	1,689	43	15,017	16,749
At 1 January 2010	1,787	77	15,372	17,236

The net book value of fixed assets includes £1 0m (2009 – £1 2m) for computer and other equipment in respect of assets held under finance leases and hire purchase contracts

Company	*Computer equipment* *£000*
Cost	
At 1 January 2010	6
Additions	2
At 31 December 2010	8
Depreciation	
At 1 January 2010	5
Provided in the year	1
At 31 December 2010	6
Net book value	
At 31 December 2010	2
At 1 January 2010	1

Notes to the financial statements

at 31 December 2010

12. Investments

Company	*Investment in subsidiary undertakings*
	£000
At 1 January 2010 and 31 December 2010	222

The company owns either directly or indirectly 100% of the ordinary share capital of the following principal subsidiary companies, the principal activities of which are the provision of computer services

Incorporated in the United Kingdom (including the Channel Islands and the Isle of Man)

2e2 Limited
2e2 Offshore Limited
Netstore Limited
Morse Group Limited
Diagonal Solutions Limited
Xayce Limited
2e2 UK Limited
2e2 Property Group Limited
Morse Overseas Holdings Limited
Morse Limited
Diagonal Consulting Limited

Incorporated in the Netherlands

2e2 Tradecom International B V
2e2 Group B V
2e2 Yul Data Security B V
2e2 Dynomic B V
2e2 Motifact Group B V

Incorporated in Spain

Morse Spain SL

Incorporated in Ireland

Morse Computer Group Limited

All subsidiaries are held indirectly with the exception of 2e2 Limited which is held directly

13 Stocks

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Spare parts	2,037	–	1,928	–
Goods for resale	5,966	–	1,028	–
Other stock	74	–	69	–
	8,077	–	3,025	–

Notes to the financial statements

at 31 December 2010

14. Debtors

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Trade debtors	95,832	–	35,685	–
Amounts owed by group undertakings	–	160,159	2,825	15,732
Prepayments and accrued income	60,672	–	35,044	–
Deferred tax asset (see note 20)	6,328	–	6,328	–
	162,832	160,159	79,882	15,732

Included in the above are the following amounts that are due after more than one year

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Deferred tax asset	6,328	–	6,328	–

15. Creditors: amounts falling due within one year

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Bank loans	6,400	–	4,000	–
Trade creditors	75,395	6	21,475	46
Tax and social security	10,717	–	5,263	–
Accruals	45,723	17	16,453	–
Deferred income	34,105	–	24,551	–
Amounts due under finance leases	420	–	763	–
	172,760	23	72,505	46

16. Provisions

	Property £000	*Dilapidations £000*	*Other £000*	*Total £000*
At 1 January 2010	459	562	-	1,021
Acquisition of Morse	3,125	724	1,596	5,445
Arising/(utilised) during the year	(226)	(154)	-	(380)
	3,358	1,132	1,596	6,086
Current 2010	784	126	1,596	2,506
Non-current 2010	2,574	1,006	-	3,580
	3,358	1,132	1,596	6,086

Notes to the financial statements

at 31 December 2010

16. Provisions (contınued)

Property

The property provısıon ıs made up of £3 1m ın 2e2 UK Ltd ın respect of the exıt of two propertıes as part of the Morse ıntegratıon and £0 4m ın 2e2 Property Ltd whereby the sub tenant ıs entıtled to exıt the property before 2e2 Property Ltd's lease expıry date

Dılapidations

The dılapıdatıons provısıon reflects a lıabılıty as at 31st December 2010 for potentıal costs that the busınesses are lıkely to ıncur to brıng all propertıes to the same state as requıred by the lease contract

Other

Other provısıons ınclude £0 5m for potentıal refund claıms on products sold durıng the last five years and £0 3m for potentıal lıabılıtıes that may arıse ın respect of PAYE and employee ıssues

17. Creditors: amounts falling due after more than one year

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Deferred ıncome	1,927	–	1,032	–
Bank loans	149,927	11,898	154,188	9,957
Amounts owed to group undertakıngs	–	61,856	4,426	–
Amounts due under finance leases	254	–	574	–
	152,108	73,754	160,220	9,957

The bank loans are secured by a fixed and floatıng charge over all the assets of the Group The bank loans consıst of the followıng facılıtıes

- Term Loan A – ın the amount of £31 7 mıllıon ıs repayable ın ınstalments A total of £4 mıllıon ıs repayable wıthın one year wıth the balance payable ın ınstalments finıshıng on 30 June 2015 Interest ıs charged at the rate of LIBOR plus 2 25% to 4 50%
- Term Loan B – ın the amount of £37 5 mıllıon ıs repayable ın a sıngle ınstalment on 10 October 2016 Interest ıs charged at the rate of LIBOR plus 3 00% to 5 00%
- Term Loan C – ın the amount of £37 5 mıllıon ıs repayable ın a sıngle ınstalment on 10 October 2017 Interest ıs charged at the rate of LIBOR plus 5 50%
- Revolvıng Facılıty – ın the amount of £15 mıllıon ıs repayable ın a sıngle ınstalment on 30 September 2013 Interest ıs charged at the rate of LIBOR plus 2 25% to 4 50%
- Mezzanıne Facılıty – ın the amount of £35 0 mıllıon ıs repayable ın a sıngle ınstalment on 10 October 2018 Interest ıs payable at the rate of LIBOR plus 16 00% 11 00% of the ınterest ıs not due for payment and rolls up untıl 10 October 2018

Amounts due under finance leases are secured on the assets to whıch they relate

The Company has no bank loans outstandıng

Notes to the financial statements

at 31 December 2010

18. Creditors: group loans falling due after one year

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Amounts due to group undertakings	80,777	80,777	–	–

The directors have included the amounts due to group undertakings separately from other group debt and disclosed it separately on the basis that the debt is not due for payment until 2020 The directors believe that this additional disclosure aids the user in understanding the funding structure of the Group and in helping their understanding of the financial statements

19. Borrowings

Borrowings are repayable as follows

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Within one year				
Bank and other borrowings	6,400	–	4,000	–
Finance leases	420	–	763	–
After one and within two years				
Bank and other borrowings	6,800	–	6,400	–
Finance leases	254	–	573	–
After two years and within five years				
Bank and other borrowings	31,894	–	22,400	–
Finance leases	–	–	–	–
After five years				
Bank and other borrowings	195,471	154,531	133,847	9,957
Less issue costs	(3,461)	–	(4,032)	–
	237,778	154,531	163,951	9,957

Bank and other borrowings repayable after five years comprise

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Bank borrowings	110,000	11,898	127,427	9,957
Accrued interest	4,694	–	1,994	–
Amounts owed to group undertakings	80,777	142,633	4,426	–
	195,471	154,531	133,847	9,957

Notes to the financial statements

at 31 December 2010

19. Borrowings (continued)

On 10 October 2008, the Company entered into a cross guarantee in the amount of £165,000,000, in favour of its bankers in respect of the borrowings of the group

Following the acquisition of Morse plc by 2e2 Ltd on 21 June 2010, the company entered into a cross guarantee on 21 June 2010 for the amount of £85,000,000, in favour of certain investors

Through its Spanish business unit, the group has access to customer specific funding through debt factoring arrangements with a number of financing institutions in Spain Morse Spain SL receives funds from the financing institutions which are then repaid as cash is received from the customer At 31 December 2010 the outstanding borrowings balance was £3,936,000 through the without recourse debt factoring agreement

Interest is charged at different rates depending on the financial institution ranging from EURIBOR + 1 25% to EURIBOR + 4 41%

20. Deferred taxation

Deferred taxation recognised in the financial statements is set out below (see note 14)

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Assets				
Depreciation in excess of capital allowances and other short term timing differences	6,328	-	6,328	–

The movement in deferred tax is as follows

	Group and company £000
At beginning and end of the year	6,328

Unrecognised deferred tax

Unrecognised deferred taxation is set out below

	Group 2010 £000	*Company 2010 £000*	*Group 2009 £000*	*Company 2009 £000*
Assets				
Depreciation in excess of capital allowances	4,105	15	3,770	13
Other short-term timing differences	1,865	-	961	–
Tax losses carried forward	17,429	-	14,040	36
Total tax losses carried forward	23,399	15	18,771	49

Finance Act 2010, which included a reduction in the UK corporate tax rate to 27% was substantially enacted on 21 July 2010 Therefore the deferred tax assets and liabilities of the group have been calculated at this rate

Notes to the financial statements

at 31 December 2010

20. Deferred taxation (continued)

In his budget of 23 March 2011, the Chancellor of the Exchequer announced Budget tax changes, which, if enacted in the proposed manner, will have an effect on the group's future tax position The Budget proposed a decrease in the rate of UK corporation tax from 27% to 26% on April 2011 and by a further 1% each year until 2014 This reduction will affect both the future and current tax charge of the Group The effect of the reduction in the tax rate to 23% would be to reduce the recognised deferred tax asset by £937,526 and reduce the unrecognised deferred tax asset by £3,466,490

The effect on the Company of these proposed changes to the UK tax system will be reflected in the Company's financial statements in future years, as appropriate, once the proposals have been substantively enacted

21. Issued share capital

Group and Company

Allotted, called up and fully paid	*No*	*2010 £000*	*No*	*2009 £000*
Ordinary shares of £0 04 each	2,637,250	105	2,637,250	105

Share option reserve

The group's parent undertaking, 2e2 Holdings Limited operates a share option scheme which is open to all employees of the group at the discretion of the board of 2e2 Holdings Limited The group records a charge in accordance with FRS 20 for options to acquire shares of 2e2 Holdings Limited that are granted to employees of the group In the scheme the options typically vest based on the following pattern, 50% on the second anniversary of the date of grant and a further 25% on the third and fourth anniversary, the options also vest on the listing on a public market or the sale of 2e2 Holdings Limited The options lapse if they remain unexercised after 10 years from the date of grant The options also lapse following the employee leaving the group There were 44,250 share options outstanding at the year end (2009 – 44,250)

The fair values were calculated using a Black-Scholes-Merton model The inputs into the model were as follows

	2010	*2009*
Weighted average share price	£1 00	£1 00
Weighted average exercise price	£1 00	£1 00
Expected volatility	35 5%	35 5%
Risk-free rate	4 25%	4 25%
Expected dividend yield	nil	nil

Expected volatility was determined using as a base the share price movements recorded over the same period as the vesting period (from grant date to vesting date) and taking into account any specific factors impacting during the period The expected life used in the model has been adjusted, based on management's best estimate for the effects of non-transferability, exercise restrictions and behavioural considerations

There were 44,250 outstanding at the year end (2009 – 44,250) No options were issued during the year During the year no options were exercised, cancelled or lapsed For the share options outstanding as at 31 December 2010, the weighted average remaining contractual life is six years (2009 – seven)

The group recognised total charges of £nil related to equity-settled share-based payment transactions during the year (2009 – £3,837)

Notes to the financial statements

at 31 December 2010

22. Reserves

Group

	Share premium account £000	*Other reserves £000*	*Profit and loss account £000*
At 1 January 2010	265	466	4,391
Retained loss for the year	–	–	(7,326)
Currency translation differences on foreign currency net investments	–	–	646
At 31 December 2010	265	466	(2,289)

Company

	Share premium account £000	*Other reserves £000*	*Profit and loss account £000*
At 1 January 2010	265	51	5,531
Retained loss for the year	–	–	(123)
At 31 December 2010	265	51	5,408

23. Notes to the statement of cash flows

(a) Net cash inflow from operating activities

	2010 £000	*2009 £000*
Operating profit	14,944	11,223
Cash impact of fundamental restructuring	(4,875)	–
Amortisation of goodwill	10,843	8,577
Depreciation	6,620	5,661
Increase / (decrease) in stock	(3,209)	2,347
Increase in debtors	(33,845)	(15,104)
Increase in creditors	35,064	1,670
Profit / (loss) on sale of fixed assets	36	(8)
Net cash inflow from operating activities	25,578	14,366

Notes to the financial statements

at 31 December 2010

23. Notes to the statement of cash flows continued

(b) Reconciliation of net cash flow to movement in net debt

	2010 *£000*	*2009* *£000*
Increase in cash in the year	18,103	(3,178)
Cash flow from financing	5,223	(2,012)
Cash flow from amounts due to parent	(76,351)	3,251
Change in net debt resulting from cash flows	(53,025)	(1,939)
Finance leases	-	(238)
Non-cash movements	(2,700)	3,241
	(55,725)	1,064
Net debt at start of year	(163,410)	(164,474)
Net debt at end of year	(219,135)	(163,410)

(c) Analysis of changes in net debt

	At 1 January 2010 *£000*	*Cash flow* *£000*	*Other non-cash movements* *£000*	*At 31 December 2010* *£000*
Cash at bank	540	18,103	-	18,643
Borrowings from parent	(4,426)	(76,351)	-	(80,777)
Long term loans	(158,188)	4,561	(2,700)	(156,327)
Finance leases	(1,336)	662	-	(674)
	(163,410)	(53,025)	(2,700)	(219,135)

Notes to the financial statements

at 31 December 2010

24. Acquisitions

On 21st June 2010 the group acquired the entire share capital of Morse plc for a consideration of £78 8m including acquisition costs An analysis of the acquisition is as follows

	Book value £'000	*Accounting policy alignments £'000*		*Fair value adjustments £'000*		*Provisional fair value £'000*
Tangible fixed assets	657	–		(83)	(a)	574
Stock	2,299	–		(457)	(b)	1,842
Debtors	53,307	(3,586)	(c)	(720)	(d)	49,001
Cash	11,435	–		–		11,435
Creditors	(52,394)	(977)	(e)	(2,072)	(f)	(55,443)
Provisions	(763)	–		(4 419)	(g)	(5,182)
Deferred Tax	527	(527)	(h)	–		–
Total assets	15,068	(5,090)		(7,751)		2,227
Goodwill arising on acquisition						76,530
						78,757
Satisfied by						
Cash						69,554
Costs associated with the acquisition						9,203
						78,757

Notes to the financial statements

at 31 December 2010

24. Acquisitions (continued)

Goodwill arising on the above acquisition has been capitalised The results for Morse plc for the period from 1 July 2009 to 20 June 2010 and for its preceding financial year ended 30 June 2009, on the basis of accounting policies prior to acquisition, are set out below

	Period from 1 July 2009 to 20 June 2010 £'000	*Year ended 30 June 2009 £'000*
Turnover	192,014	211,910
Cost of sales	(154,095)	(167,882)
Gross profit	37,919	44,028
Operating expenses	(29,384)	(35,696)
Exceptional operating expenses	(1,104)	(8,160)
Operating profit	7,431	172
Interest	(56)	(546)
Profit / (loss) before taxation	7,375	(374)
Taxation	(1,441)	1,725
Loss for the period from discontinued operations	(1,150)	(13,442)
Profit / (loss) after taxation	4,784	(12,091)

Statement of recognised gains and losses

	Period from 1 July 2009 to 20 June 2010 £'000	*Year ended 30 June 2009 £'000*
Profit / (loss) for the year	4,784	(12,091)
Foreign currency translation differences	195	1,632
Total recognised gains and losses related to the period	4,979	(10,459)

Adjustments

(a) a reassessment of the carrying value of fixed asset values based on management's expected realisable value
(b) write-down to estimated realisable value
(c) provisions for accrued income and alignment of bad debt provisioning policy
(d) reduction in the carrying value of debtors based on management's expected realisable value
(e) alignment of trading balance release policy
(f) recognition of liabilities not fully reflected in the balance sheet of Morse Plc at acquisition date
(g) recognition of reorganisation and restructuring costs including onerous lease provisions

Notes to the financial statements

at 31 December 2010

24. Acquisitıons (contınued)

(h) reassessment of the recoverabılıty of deferred tax assets ın lıne wıth group accountıng polıcıes

These faır values are provısıonal and wıll be revıewed ın the future to ensure that they remaın reasonable

25. Interest rate swaps

The group purchases ınterest rate swaps to manage the group's exposure to floatıng ınterest rates At the balance sheet date the ınterest rate swaps held by the group were as follows,

Hedged amount at perıod end	£117 0m
Fınal maturıty date	from 8 December 2011 to 30 December 2011
Fıxed rate payable	Between 2 85% and 3 92%
Floatıng rate receıvable	GBP LIBOR BBA

26. Capital commitments

The group had no capıtal commıtments at 31 December 2010 (2009 – £nıl)

27. Contingent liabilitıes

There were no contıngent lıabılıtıes at 31 December 2010 (2009 – £nıl)

28. Leasing commitments – group

Operatıng lease payments amountıng to £2 5m (2009 – £3 0m) are due wıthın one year The leases to whıch these amounts relate expıre as follows

	Land and buıldıngs 2010 £000	*Other 2010 £000*	*Land and buıldıngs 2009 £000*	*Other 2009 £000*
In one year or less	814	1,633	744	2,278
Between one and five years	2,415	2,052	965	2,338
In five years or more	1,449	–	1,387	–
	4,678	3,685	3,096	4,616

29. Related party transactions

The group has taken advantage of the exemptıon avaılable to wholly owned subsıdıary undertakıngs under Fınancıal Reportıng Standard Number 8 ('Related Party Transactıons'), and accordıngly has not provıded detaıls of ıts transactıons wıth entıtıes formıng part of the 2e2 group

Notes to the financial statements

at 31 December 2010

30 Ultimate parent undertaking and controlling party

The company's ultimate parent undertaking is 2e2 Holdings Limited, a company incorporated in the United Kingdom 2e2 Holdings Limited is the only group preparing financial statements which are available from its registered address of The Mansion House, Benham Valence, Newbury, RG20 8LU The company's immediate parent undertaking is 2e2 Investments Limited