

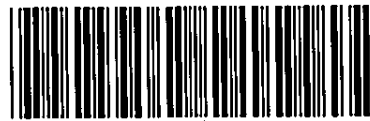
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COMPANY REGISTRATION NUMBER 3533689 (DELAWARE)

PHORM UK, INC.
ANNUAL REPORT AND FINANCIAL STATEMENTS
31 DECEMBER 2007

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PHORM UK, INC.

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YEAR ENDED 31 DECEMBER 2007

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PHORM UK, INC.

OFFICERS AND PROFESSIONAL ADVISERS

YEAR ENDED 31 DECEMBER 2007

THE BOARD OF DIRECTORS

H Drayton
L Millar

REGISTERED OFFICE

2711 Centerville Road
Suite 400
City of Wilmington 19808
County of New Castle
Delaware
USA

BANKERS

HSBC Group plc
70 Pall Mall
St James
London
SW1Y 5EZ

SOLICITORS

Nabarro LLP
Lacon House
Theobald's Road
London
WC1X 8RW

PHORM UK, INC.

DIRECTORS' REPORT

YEAR ENDED 31 DECEMBER 2007

The Directors present their annual report and the unaudited financial statements of the company for the year ended 31 December 2007. The company is a Delaware corporation, however as the company's shares are quoted on the Alternative Investment Market in London, the financial statements have been prepared using United Kingdom Generally Accepted Accounting Principles.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The principal activity of the parent company and of the Group during the year was to develop a platform for the delivery and management of targeted, contextual and behavioural online advertising campaigns on behalf of its clients.

PRINCIPAL RISKS AND UNCERTAINTIES

The Directors recognise that within the business there are a number of risks, which may affect the performance of the Group. These risks are subjected to regular review and where appropriate processes are established to minimise the level of exposure.

ISP Risk

The Group's plan to deploy its service using the network of numerous ISPs is wholly dependent on reaching arrangements with such ISPs. There can be no assurance that we will be able to reach satisfactory agreements with said ISPs.

Financial Risks

The Group's financial instruments comprise cash and other items, including trade debtors and trade creditors that arise directly from its operations. The Group seeks to reduce or eliminate financial risk and to invest cash assets safely and profitably. The Group has transactional currency exposure as it deals in multi-currencies however the Directors do seek to limit this risk as much as possible.

People

One of the key assets of the Group is the commitment and skill of its staff. The retention of these people is therefore key to the success of the business. The Group monitors closely the satisfaction of its employees and that their remuneration packages match both contribution and the wider employment market. In addition the Group has a share option scheme which allows employees to participate in the success of the Group as a whole.

Technology and market changes

Phorm UK, Inc. operates at the forefront of the digital advertising technology marketplace. The Directors acknowledge that this is a rapidly evolving environment and the Group monitors closely how changes will impact the Group. During 2006 the Directors made a strategic decision to redirect the focus of the Group towards the ISP marketplace. The Group has needed to expend considerable capital in pursuing its strategy with the global ISP community prior to obtaining any significant revenues from this business.

Competition

The Group continuously monitors new product offerings into the market place and the Directors believe Phorm's technical team have a strong track record in maintaining competitive advantage.

RESEARCH AND DEVELOPMENT

Research and development is undertaken on an ongoing basis in order to further develop and enhance the Group's software products.

PHORM UK, INC.

DIRECTORS' REPORT

YEAR ENDED 31 DECEMBER 2007

THE DIRECTORS AND THEIR INTERESTS

The Directors at the end of the year were as follows

Lynne Millar (resigned on 16 June 2009)
Hugo Drayton (resigned on 16 June 2009)

None of the directors who served during the year had any beneficial interests in the share capital of the company

Andrew Croxson and Nan Richards were appointed as directors of the company on 16 June 2009

EMPLOYEE CONSULTATION

The policy of informing and consulting with employees is maintained by means of regular team briefs, conference calls and meetings. Employees are encouraged to present their views and suggestions in respect of the Group's performance.

CREDITOR PAYMENT POLICY

The Group's current policy concerning the payment of trade creditors is to

- (i) settle the terms of payment with suppliers when agreeing the terms of each transaction
- (ii) ensure that suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts
- (iii) pay in accordance with the Group's contractual or other legal obligations

The average trade creditor days for the year were 13 days



PHORM UK, INC.

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). The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgments and estimates that are reasonable and prudent,

state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements,

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

PHORM UK, INC.

COMPANY PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 2007

		2007	2006 Restated
	Notes	\$	\$
Turnover	2	-	1,272,254
Cost of Sales		(294,098)	(403,306)
Gross Profit/(Loss)		(294,098)	868,948
Sales and Administrative Expenses			
- General		(23,426,796)	(10,937,288)
- Share Based Payments		(6,752,372)	(1,533,134)
Operating Loss	3	(30,473,266)	(11,601,474)
Interest receivable	6	688,843	82,312
Interest Payable and similar Charges	7	(8,816)	(16,186)
Loss on Ordinary Activities Before Taxation		(29,793,239)	(11,535,348)
Taxation on Loss on Ordinary Activities	8	(3,941)	(12,705)
Loss on Ordinary Activities After Taxation		(29,797,180)	(11,548,053)

All activities of the Company are classed as continuing

PHORM UK, INC.

STATEMENT OF TOTAL RECOGNIZED GAINS AND LOSSES FOR THE YEAR ENDED 31 DECEMBER 2007

	Notes	2007 \$	2006 Restated \$
Loss for the financial year		(29,797,180)	(11,548,053)
Share option charge taken to option reserve		6,752,372	1,533,133
Currency translation difference on overseas divisions		(48,310)	(106,675)
Total recognized gains and losses relating to the year		(23,093,118)	(10,121,595)
Prior year adjustments	9	-	(101,306)
Total gains and losses recognized since last annual report		(23,093,118)	(10,222,901)

PHORM UK, INC.

COMPANY BALANCE SHEET

AS AT 31 DECEMBER 2007

		2007	2006 Restated
	Notes	\$	\$
Fixed Assets			
Tangible assets	10	661,172	128,614
		<u>661,172</u>	<u>128,614</u>
Current Assets			
Debtors	11	1,374,688	594,063
Cash at bank and in hand		16,557,681	3,804,771
		<u>17,932,369</u>	<u>4,398,834</u>
Creditors Amounts Falling Due Within One Year	12	<u>(33,023,541)</u>	<u>(1,267,411)</u>
Net Current Assets		<u>(15,091,172)</u>	<u>3,131,423</u>
Total Assets Less Current Liabilities		<u>(14,430,000)</u>	<u>3,260,037</u>
Creditors Amounts Falling Due After One Year	13	<u>(401,464)</u>	<u>(35,548)</u>
Net Assets		<u><u>(14,831,464)</u></u>	<u><u>3,224,489</u></u>
Capital and Reserves			
Called Up Share Capital	14	-	11,217
Share Premium Account	15	-	18,706,233
Foreign Exchange Reserve	15	(329,206)	(280,896)
Warrants	15	-	300,300
Profit and Loss Account	15	<u>(14,502,258)</u>	<u>(15,512,365)</u>
Shareholders' Funds		<u><u>(14,831,464)</u></u>	<u><u>3,224,489</u></u>

The financial statements of Phorm UK, Inc., registered number 3533689 (Delaware), were approved by the Board of Directors and authorised for issue on 13th May 2010

Signed on behalf of the Board of Directors



A Croxson
Director



Nan Richards
Director

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

1. ACCOUNTING POLICIES

The financial statements are prepared in accordance with applicable United Kingdom law and accounting standards. The particular accounting policies adopted are described below, and have been applied consistently in the current and preceding year.

Basis of preparation

These financial statements present information about the company as an individual undertaking and not about its group. The accounts have been prepared on an historical cost basis.

The company is exempt from the obligation to prepare and deliver group accounts under Sections 228(2) of the Companies Act 1985 as it is a wholly-owned subsidiary of Phorm Inc (see note 22).

Basis of going concern

These financial statements have been prepared on a going concern basis which assumes that the company will continue to be supported by its parent, Phorm, Inc.

Turnover

Turnover represents amounts receivable for services net of VAT and trade discounts.

Research and development

In accordance with best practice in the software industry, research and development expenditure is expensed to the profit and loss accounts as incurred.

Tangible fixed assets

All tangible fixed assets are initially recorded at cost, and then stated at cost less depreciation.

Depreciation

Depreciation is calculated so as to write off the cost of an asset, less its estimated residual value, over the useful economic life of that asset as follows:

Computer hardware & machinery	- 50% on cost
Fixtures and fittings	- 33% on cost
Software development costs	- 50% on cost

Fixed asset investments

Fixed asset investments are stated at cost less provision for impairment in value.

Leasing and hire purchase commitments

Assets held under finance leases and hire purchase contracts are treated as if they had been purchased outright at the present value of the rentals payable, less finance charges, over the primary period of the agreements. The corresponding obligations under these agreements are included in creditors. The finance element of the rentals payable is charged to the profit and loss account so as to produce a constant rate of charge on the outstanding balance in each period.

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

Contribution to pension funds

The company contributes to individual defined contribution pension plans for the benefit of certain employees and directors. The assets of the scheme are administered by trustees in a fund independent from those of the company.

The pension costs charged against profits represent the amount of the contributions payable to the scheme in respect of the accounting period.

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

ACCOUNTING POLICIES *(Continued)*

Share based payments

The Group issues equity-settled share-based payments to certain employees and has applied Financial Reporting Standard No 20 'Share-based payments'

The cost of employee share-based compensation awards is recognised as an expense. The total amount to be expensed rateably over the vesting period is determined by reference to the fair value of the options determined at the grant date, excluding the impact of non-market vesting conditions (for example, profitability and sales targets). Non-market vesting conditions are included in the assumptions about the number of options that will eventually vest. This estimate is revised at each reporting date and an adjustment is made to the profit and loss account. Fair value is measured by using the Black-Scholes pricing model, except for options with market based vesting conditions, where a binomial model is used.

Employer's taxes on share options

Employers' national insurance contributions in the UK, are calculated using the market value of the company's shares at the reporting date, and pro-rated over the vesting period of the options.

Deferred taxation

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

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the accounts. Deferred tax is not provided on timing differences arising from the revaluation of fixed assets where there is no commitment to sell the assets. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Foreign currencies

Monetary assets and liabilities in foreign currencies are translated into US dollars at the closing rates of exchange ruling at the balance sheet date. Transactions in foreign currencies are translated into US dollar at the rate of exchange ruling at the date of the transaction. All differences are taken to the profit and loss account.

The results of overseas branches are translated into US dollars at the average rates for the year. The net assets/(liabilities) of overseas branches are translated at year-end exchange rates. The exchange differences arising on translation of the opening net assets/(liabilities) and results of overseas operations are taken to reserves.

Functional currency

The financial statements have been prepared in US dollars as the majority of the Company's trade occurs in this currency.

Cash flow statement

The company has taken advantage of the exemption available under Financial Reporting Standard No 1 'Cash flow statements (Revised 1996)' not to prepare a statement of cash flows as it is a wholly-owned subsidiary undertaking. Phorm UK, Inc. cash flows are included in the consolidated accounts of Phorm, Inc, which are publicly available.

Segmental reporting

The company has taken advantage of the exemption available under Statement of Standard Accounting Practice 25 'Segmental reporting', paragraph (41) not to provide additional segmental reporting disclosures as it is a wholly owned subsidiary undertaking. Phorm UK, Inc. segmental reporting disclosures are included in the consolidated accounts of Phorm Inc, which are publicly available.

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

ACCOUNTING POLICIES (Continued)

Prior year restatement

In accordance with FRS 3 'Reporting Financial Performance', the directors have restated the 31 December 2006 figures for three errors identified which in their view are fundamental. Please refer to note 9.

2 TURNOVER

The turnover and loss before tax are attributable to the one principal activity of the Company.

The geographical analysis of turnover is given below.

	2007 \$	2006 \$
North America	-	995,184
Europe	-	277,070
	<u>-</u>	<u>1,272,254</u>

During 2006 the Directors made a strategic decision to cease the sale and marketing of the desktop software business (Pagesense Desktop), and focus the company's resources on the online behavioural and contextual advertising market through arrangements with global ISPs.

3 OPERATING LOSS BEFORE TAX

Operating loss is stated after charging/(crediting)

	2007 \$	2006 \$
Research and development expenditure written off	3,799,037	638,636
Operating lease rentals		
- Other assets	161,467	152,070
Share Based Payments		
- Charge under FRS 20	6,752,372	1,533,133
- Employer's NIC	1,036,918	497,290
Depreciation of owned fixed assets	186,546	133,041
Depreciation of tangible fixed assets held under finance lease and hire purchase contracts	15,023	50,000
Auditors' remuneration		
Fees payable to the Company's auditors for the audit of the company's annual accounts	83,732	46,400
Fees payable to the Company's auditors for other services	227,764	62,669
Net loss/(profit) on foreign currency translation	<u>(216,015)</u>	<u>169,860</u>

Fees payable to the company's auditors for non-audit services to the company are not required to be disclosed because the consolidated financial statements are required to disclose such fees on a consolidated basis.

4 STAFF COSTS

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

	2007 No	2006 No
Research and development	4	2
Sales and administration	58	34
	<u>62</u>	<u>36</u>

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

4 STAFF COSTS (Continued)

The aggregate payroll costs of the above were

	2007 \$	2006 \$
Wages and salaries	18,178,445	5,112,747
Social security costs	1,726,898	713,789
Other pension costs	264,739	16,852
	<u>20,170,082</u>	<u>5,843,388</u>

5 DIRECTORS' EMOLUMENT

The Directors' aggregate emoluments in respect of qualifying services were

	2007 \$	2006 \$
Emoluments receivable	<u>708,090</u>	<u>763,981</u>

Emoluments of highest paid director

	2007 \$	2006 \$
Total emoluments (excluding pension contributions)	<u>477,500</u>	<u>343,320</u>

The highest paid director did not exercise any share options in the year

The company has not made pension contributions under defined contribution schemes in respect of any directors (2006 nil)

6 INTEREST RECEIVABLE

	2007 \$	2006 \$
Bank interest receivable	<u>688,843</u>	<u>82,312</u>
	<u>688,843</u>	<u>82,312</u>

7 INTEREST PAYABLE AND SIMILAR CHARGES

	2007 \$	2006 \$
Interest payable on Finance lease and hire purchase contracts	<u>8,816</u>	<u>16,186</u>
	<u>8,816</u>	<u>16,186</u>

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

8 TAXATION ON ORDINARY ACTIVITIES

	2007 \$	2006 \$
Current tax		
Delaware state tax	3,941	12,705
Total current tax	<u>3,941</u>	<u>12,705</u>
Factors affecting the tax charge for the period		
Loss on ordinary activities before taxation	(29,793,239)	(11,535,348)
Profit on ordinary activities before taxation multiplied by standard rate of UK corporation tax of 30% (2006 30%)	(8,937,972)	(3,460,604)
Effects of		
Expenses not deductible for tax purposes	24,315	26,810
Capital allowances for the period in excess of depreciation	(63,863)	70,465
Other tax adjustments	3,941	12,705
Movement on tax losses	8,977,522	3,363,329
Current Tax charge	<u>3,941</u>	<u>12,705</u>

Deferred tax assets have not been recognised as they may not be utilised until suitable profits arise and it is not yet sufficiently probable that such profits will be available in the future

9. PRIOR YEAR ADJUSTMENT

In accordance with FRS 3 'Reporting Financial Performance', the directors have restated the 31 December 2006 figures for three errors identified which in their view are fundamental. The effects of those three errors are summarised below

	At 31 December 2006 \$
Shareholders' equity as previously reported	3,325,795
Fundamental errors identified	
Website development costs (note (i))	(48,827)
Software development costs (note (ii))	(256,243)
Share options NI (note (iii))	<u>203,764</u>
Restated shareholders' equity	<u>3,224,489</u>

Further information is provided below in respect of these items

- (i) As at 31 December 2006, the Group had recorded an intangible fixed asset for capitalised website costs with a net book value of \$48,827 (1 January 2006 - \$nil). Such costs are capitalisable under UK GAAP where the conditions set out in UITF Abstract 29 "Website Development Costs" are met. This requires, amongst other conditions, that the website will generate sales or other revenues directly. As the Company's website did not have the capacity to generate revenue, management has reversed this amount as an error and expensed the costs in the period in which they arose, being the six months ended 31 December 2006.

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

9. PRIOR YEAR ADJUSTMENT (Continued)

- (ii) As at 31 December 2006, the Group had recorded an intangible fixed asset for capitalised software development costs with a net book value of \$256,243 (1 January 2006 - \$324,889). Such costs were capitalisable under UK GAAP where the conditions set out in SSAP 13 "Accounting for Research and Development" are met. This requires, amongst other conditions, that technological feasibility and commercial viability has been established for the products under development and that recovery of costs is reasonably assured. The Directors have not been able to satisfy themselves that all of these conditions had been achieved by the historic reporting dates. Consequently, amounts previously capitalised have been expensed in the period in which they were incurred as an error.
- (iii) As required, under UK GAAP, the Company adopted FRS 20 "Share-based payment" in the year ended 31 December 2006, resulting in the recognition of the cost of share options at fair value. Management, having taken independent expert advice, have subsequently determined that the assumptions applied in determining the fair value of the options contained errors, relating to the expected life assumption, where the contractual term had been applied rather than the expected option term, and with respect to the expected volatility. Management have revised the fair value of options granted, and have adjusted the share option expense to reflect these revised fair values. As a consequence the fair value charge on options has been understated by \$279,068 in the year ended 31 December 2006 and the accrual for employers NIC was overstated by \$203,764 at 31 December 2006, as a result of the inclusion in error of National Insurance on options held by non UK employees and an under-accrual due to incorrect vesting assumptions.

10. TANGIBLE FIXED ASSETS

	Computer Hardware & Machinery \$	Fixtures & Fittings \$	Software Development \$	Total \$
COST				
At 1 January 2007	566,813	68,397	1,129,124	1,764,334
Prior year adjustment (note 9)	(412,974)	-	(1,129,124)	(1,129,124)
Adjusted 1 January 2007	153,839	68,397	-	222,236
Additions	728,566	5,561	-	734,127
At 31 December 2007	882,405	73,958	-	956,343
DEPRECIATION				
At 1 January 2007	482,427	24,169	872,881	1,379,477
Prior year adjustment (note 9)	(412,974)	-	(872,881)	(872,881)
Adjusted 1 January 2007	69,453	24,169	-	93,622
Charge for the year	178,616	22,953	-	201,569
At 31 December 2007	248,069	47,122	-	295,191
NET BOOK VALUE				
At 31 December 2007	634,336	26,836	-	661,172
At 31 December 2006	84,386	44,228	256,243	384,857
Adjusted 31 December 2006	84,386	44,228	-	128,614

Finance Leases and Hire Purchase Contracts

The net book value of tangible fixed assets includes an amount of \$9,266 (2006 \$12,500) in respect of assets held under finance lease or hire purchase contracts. The depreciation charge for the year was \$3,234 (2006 \$50,000).

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

11. DEBTORS

	2007	2006
	\$	\$
Amounts owed by Group undertakings	24,453	-
Rent deposit	282,894	218,735
VAT recoverable	466,555	211,397
Other debtors	69,292	46,893
Prepayments and accrued income	531,494	117,038
	<u>1,374,688</u>	<u>594,063</u>

12 CREDITORS Amounts falling due within one year

	2007	2006
	\$	\$
Net obligations under finance leases and hire purchase contracts	15,104	39,077
Amounts owed to Group undertakings	29,961,683	-
Trade creditors	529,370	156,736
Other taxation and social security	953,578	55,956
Other creditors	44,081	11,445
Accruals and deferred income	1,519,725	1,004,197
	<u>33,023,541</u>	<u>1,267,411</u>

The intercompany balance due to the parent company represents the sterling fund raising on the UK equity market. The parent company has confirmed that this loan is of an equity nature and it is not envisaged that this loan will be repaid.

13 CREDITORS: Amounts falling due after one year

	2007	2006
	\$	\$
Provisions for social taxes on share based payments	-	24,245
Net obligations under finance leases and hire purchase contracts	5,486	11,303
	<u>5,486</u>	<u>35,548</u>

Net obligations under finance leases and hire purchase contracts

Repayable within one year	15,104	39,077
Repayable between one and five years	5,486	11,303
	<u>20,590</u>	<u>50,380</u>
Included in liabilities falling due within one year	(15,104)	(39,077)
	<u>5,486</u>	<u>11,303</u>

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

14 SHARE CAPITAL

Authorised share capital

	2007 \$	2006 \$
100 Common shares of \$0.001 each	0.1	13,000

Allotted, called up and fully paid

	2007 No	\$	2006 No	\$
Common shares of \$0.001 each	100	0.1	11,216,642	11,217

On 3 May 2007, an Agreement and Plan of Merger was entered into as part of a group restructuring. In accordance with the laws of the State of Delaware, the company's share capital was reduced from 11,393,000 shares with nominal value of \$0.01 per share as at 3 May 2007 to 100 shares with nominal value of \$0.01. This was approved by the shareholders at a general meeting on 26 April 2007.

15 RESERVES

	Share capital \$	Additional paid in capital \$	Warrants \$	Translation reserve \$	Accumulated Deficit \$	Total \$
At 1 January 2006 as previously reported	8,190	6,734,601	584,572	(174,221)	(5,181,906)	1,971,236
Prior year adjustment (note 9)	-	-	-	-	(315,539)	(315,539)
At 1 January 2006 - restated	8,190	6,734,601	584,572	(174,221)	(5,497,445)	1,655,697
Loss for the year	-	-	-	-	(11,548,053)	(11,548,053)
Share-based payment charge	-	-	-	-	1,533,133	1,533,133
Issue of new stock	3,027	11,687,360	-	-	-	11,690,387
Exchange differences on translation of overseas operations	-	-	-	(106,675)	-	(106,675)
Transfer on exercise of warrants	-	284,272	(284,272)	-	-	-
At 1 January 2007	11,217	18,706,233	300,300	(280,896)	(15,512,365)	3,224,489
Loss for the year	-	-	-	-	(29,797,180)	(29,797,180)
Share-based payment charge	-	-	-	-	6,752,372	6,752,372
Issue of new stock	176	5,036,989	-	-	-	5,037,165
Transfer of stock	(11,393)	(24,043,522)	-	-	(24,054,915)	-
Exchange differences on translation of overseas operations	-	-	-	(48,310)	-	(48,310)
Transfer on exercise of warrants	-	300,300	(300,300)	-	-	-
At 31 December 2007	-	-	-	(329,206)	(14,502,258)	(14,831,464)

16 WARRANTS

No warrants (2006: 31,473) remain outstanding at the balance sheet date.

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

17 SHARE BASED PAYMENTS

The group has a share scheme whereby options over the common shares of the company are granted to employees, consultants and directors. Options are granted at the mid market price on close of the day of grant and must be exercised within 10 years of grant unless the employment is terminated in which case options generally must be exercised within 90 days of termination.

The reconciliation of option movements during the year ended 31 December 2007 is shown below:

	Number	2007 Weighted average exercise price £	Number	2006 Weighted average exercise price £
Outstanding at beginning of period	2,532,240	£3 68	1,825,801	£1 26
Granted during the year	895,964	£19 01	1,756,000	£4 99
Lapsed	(115,350)	£5 68	(325,639)	£3 66
Exercised	(284,301)	£1 61	(723,922)	£0 74
Outstanding at end of period	3,028,553	£8 32	2,532,240	£3 68
Exercisable at end of period	719,319	3 91	519,012	£1 38

The following options over ordinary shares were in existence at 31 December 2007:

Range of exercise Price £	Number	Weighted average exercise price £	2007 Weighted average remaining life (years)	Number	Weighted average exercise price £	2006 Weighted average remaining life (years)
£0 01 - £2 49	1,224,561	1 66	7 54	1,591,546	1 65	8 58
£2 50 - £4 99	121,778	4 64	8 48	130,694	4 59	9 40
£5 00 - £9 99	800,750	7 09	8 70	650,000	6 43	9 53
£10 00-£15 00	160,000	11 90	8 58	160,000	11 90	9 56
£15 00-£20 00	375,000	18 05	10 00	-	-	-
£20 00-£25 00	205,550	21 45	9 93	-	-	-
£25 00-£30 00	140,914	27 30	9 58	-	-	-
Total	3,028,553	8 32	8 50	2,532,240	3 68	8 93

The fair value of the options granted during the year was calculated using the following assumptions:

2007 grants

Grant date	14 Feb 2007	14 Feb 2007	6 Mar 2007	26 Jul 2007	1 Oct 2007
Pricing model	Monte Carlo	Black Scholes	Black Scholes	Black Scholes	Black Scholes
Share price at grant	£9 95	£9 95	£13 83	£27 30	£23 20
Exercise price	£9 95	£9 95	£13 83	£27 30	£23 20
Vesting criteria	(1)	(2)	(3)	(2)	(4)
Expected volatility	46 29%	46 3%	49 4%	51 2%	50 6%
Expected life (years)	n/a	5 6	5 3	4 7	6 03
Risk free rate	5 45%	5 12%	5 11%	5 33%	4 94%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture rate p a	5%	12%	5%	12%	12%
Probability non-market based performance criteria is met	N/A	N/A	N/A	N/A	N/A
Fair value per option	£4 94	£4 98	£7 03	£13 41	£12 64

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

17 SHARE BASED PAYMENTS (Continued)

2007 grants

Grant date	1 Oct 2007	6 Nov 2007	11 Dec 2007	19 Dec 2007	19 Dec 2007
Pricing model	Black Scholes	Black Scholes	Black Scholes	Black Scholes	Black Scholes
Share price at grant	£23 20	£21 00	£20 38	£18 05	£18 05
Exercise price	£23 20	£21 00	£20 38	£18 05	£18 05
Vesting criteria	(2)	(2)	(2)	(5)	(6)
Expected volatility	50 6%	50 7%	50 3%	50 3%	50 3%
Expected life (years)	6 25	6 03	6 03	5 00	5 00
Risk free rate	4 95%	4 84%	4 58%	4 55%	4 55%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture rate p a	12%	12%	12%	5%	0%
Probability non-market based performance criteria is met	N/A	N/A	N/A	100%	N/A
Fair value per option	£12 84	£11 42	£10 94	£8 87	£8 87

2006 grants

Grant date	28 Feb 2006	28 Feb 2006	23 Mar 2006	19 Apr 2006	27 Apr 2006
Pricing model	BlackScholes	BlackScholes	BlackScholes	BlackScholes	BlackScholes
Share price at grant	£1 540	£1 540	£2 000	£2 130	£2 800
Exercise price	£1 540	£1 540	£2 065	£2 120	£3 000
Vesting criteria	(1)	(2)	(1)	(2)	(1)
Expected volatility	26 2%	26 2%	26 8%	35 8%	35 8%
Expected life	10 Years	10 Years	10 Years	10 Years	10 Years
Risk free rate	4 50%	4 50%	4 50%	4 50%	4 50%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture	30%	30%	30%	30%	30%
Probability criteria is met	1	0 50	1	0 50	1
Fair value per option	£0 735	£0 735	£0 942	£1 160	£1 498

Grant date	1 Jun 2006	1 Jun 2006	7 Jun 2006	24 July 2006	26 July 2006
Pricing model	BlackScholes	BlackScholes	Binomial	BlackScholes	BlackScholes
Share price at grant	£4 824	£4 824	£5 233	£11 050	£12 030
Exercise price	£4 850	£4 850	£5 40	£11 575	£12 450
Vesting criteria	(1)	(2)	(3)	(6)	(4)
Expected volatility	42 5%	42 5%	42 5%	51 5%	51 5%
Expected life	10 Years	10 Years	10 Years	10 Years	10 Years
Risk free rate	4 50%	4 50%	4 50%	4 50%	4 50%
Dividend yield	0%	0%	0%	0%	0%
Estimated forfeiture	30%	30%	0%	30%	30%
Probability criteria is met	1	0 5	1	1	1
Fair value per option	£2 923	£2 923	£2 171	£5 852	£6 850

Grant date	1 Nov 2006	1 Nov 2006
Pricing model	BlackScholes	Binomial
Share price at grant	£9 550	£9 550
Exercise price	£9 875	£9 875
Vesting criteria	(4)	(5)
Expected volatility	55 1%	55 1%
Expected life	10 Years	10 Years
Risk free rate	4 75%	4 75%
Dividend yield	0%	0%
Estimated forfeiture	30%	30%
Probability criteria is met	1	1
Fair value per option	£5 361	£5 200

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

17 SHARE BASED PAYMENTS (Continued)

2007 grants

Vesting criteria

- (1) At the rate of 1/6th after 6 months, and 1/36th subsequently, for a total vesting period of 36 months
- (2) Conditional upon achieving average monthly net revenues of \$3m over a period of 6 months consecutive. It is estimated this will be met within 3 years from date of grant
- (3) At the rate of 1/5th for achieving each incremental increase of £100 in the share price up to a maximum of £500. It is estimated this will be met within 5 years from date of grant
- (4) At the rate of 1/8th after 6 months, and 1/48th subsequently, for a total vesting period of 48 months
- (5) Conditional that 5-day average share price is not above £50.00 prior to 11 July 2007. If so, 25% vests immediately and remainder over 36 months. If condition is not met, options are cancelled
- (6) At the rate of 1% for each 1% of targeted number subscribers becoming subject to qualifying agreements

The expected volatility was based upon historical volatility of the company's share price from IPO to date of grant. The expected life is the expected period to exercise.

At the year end the company has accrued \$1,017,092 (2006 \$516,986) in respect of potential employers' National Insurance Contribution arising on exercise of the options by United Kingdom employees, calculated in line with the FRS 20 charge. This is included in accruals in creditors falling due within less than one year.

18 RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

	2007	2006
	\$	\$
Loss for the financial year	(29,797,180)	(11,548,053)
New share capital subscribed	5,037,165	11,690,387
Other recognized gains and losses	6,704,062	1,426,458
Net addition/(reduction) to shareholders' funds	(18,055,953)	1,568,792
Opening shareholders' funds	3,224,489	1,655,697
Closing shareholders' funds	(14,831,464)	3,224,489

19 PENSIONS

Defined Contribution

The Company operates a defined contribution pension scheme. The assets of the scheme are held separately from those of the Company in an independently administered fund. The pension cost charge represents contributions payable by the Company to the fund and amounted to \$264,739 (2006 \$16,852). At the year end a creditor of \$30,951 (2006 \$10,775) was owed in respect of unpaid contributions.

PHORM UK, INC.

NOTES TO THE FINANCIAL STATEMENTS

YEAR ENDED 31 DECEMBER 2007

20 FINANCIAL COMMITMENTS

Capital commitments

At 31 December 2007, no capital commitments (2006 none) had been authorised or contracted for by the directors

Operating lease commitments

At 31 December 2007, the Company had annual commitments under non-cancellable operating leases as set out below -

	Land and buildings	
	2007	2006
	\$	\$
Operating leases which expire		
Within 2 to 5 years	166,400	-
More than 5 years	-	175,016
	<u>166,400</u>	<u>175,016</u>

21 RELATED PARTY TRANSACTIONS

Transactions with the directors of the company are disclosed in note 5

The company has taken advantage (where applicable) of the exemptions in paragraph 3(c) of Financial Reporting Standard 8 'Related party disclosures' and has not disclosed details of transactions with fellow group companies

There are no other related party transactions during the year

22 ULTIMATE CONTROLLING PARTY

Phorm Inc is the immediate and ultimate parent company and controlling party of the smallest and largest group that prepares group accounts which are publicly available. The Group's annual report and accounts are available from www.phorm.com