

KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

DIRECTORS' REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2011

COMPANY NUMBER 212159

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KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

COMPANY INFORMATION

Chairman	Maxwell C B Ward, MA (resigned 29 th September 2011) John Olcay, BA, MBA (appointed as a Director 25 th May 2011, appointed Chairman 29 th September 2011)
Directors	Andrew N R Fleming, BA (Chief Executive) Christophe C Ferrand, DESCF, MaBa (Ceased to be director 7 th July 2011) Philip J G Smith, MA, CA Martin J Harris, BSc Sarah Russell, MAF Arnab K Banerji, MA, BM, BCh (Appointed 29 th September 2011) David K Watson, BSc, ACA (Appointed 29 th November 2011)
Secretary	Alison Talbot LLB
Company Number	212159
Registered Office	3 Lochside Avenue Edinburgh Park Edinburgh EH12 9SA
Auditors	Ernst & Young LLP Ten George Street Edinburgh EH2 2DZ

**KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)**

**DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2011**

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**KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)**

**DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2011**

The Directors present their report and the audited financial statements for the year ended 31 December 2011.

Structure of these accounts

The Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union as they apply to the financial statements of the Company for the year ended 31 December 2011 and applied in accordance with the Companies Act 2006.

Principal and ongoing activity

The principal activity is the provision of asset management services. The Company is incorporated and domiciled in Scotland.

Results and dividends

The results for the period are set out on page 9.

The Company delivered profits after tax but before dividends of £2,216k (2010: £4,154k). The Company paid dividends of £3.0m during the year (2010: £8.5m). This was equivalent to 300p per share (2010 : 850p). The Board of Directors consider the results to be satisfactory.

Net assets at the end of the year were £4,429k (2010: £5,213k). This was in line with Directors' expectations based on expected current year profits offset by dividend payments to the parent company.

The Directors do not recommend payment of a final dividend.

Review of business and future developments

On 1st September 2011 the name of the company was changed from AEGON Investment Management UK Limited to Kames Capital Management Limited.

Development and Performance of the Business

The following review covers the results of Kames Capital Management Limited (formerly known as AEGON Investment Management UK Ltd) and, where appropriate, its parent Kames Capital Plc (formerly known as AEGON Asset Management UK Plc).

The Board of the Company monitors key management information on a quarterly basis to track business performance. This information includes investment performance, assets under management, revenues, expenses, headcount and capital position. Combined assets under management increased by 0.4% during 2011 (2010: increase of 18%) with strong growth in our Retail book offset by the run-off of insured assets. Revenues have increased (10%) due to the increase in the proportion of retail assets within our portfolio. Administrative expenses have increased by 14% (2010: increase of 8%). This is largely attributable to payroll and additional costs incurred for Marketing relating to the rebranding to the new Kames brand. The increase in payroll is due to a combination of inflation and bonus; bonus increased as a result of improved investment and business performance this year. The combined total average number of employees during the year increased by 4% (2010: 8%) from 243 FTEs to 253 FTEs.

Directors and their Interests

The Directors who held office at the date of this report are shown on page 1. On 29th September Maxwell Ward resigned as a Director and as Chairman. On 25th May 2011 John Olcay was appointed as a non-Executive Director. On 29th September 2011 John Olcay was appointed Chairman of the Board. On 29th September 2011 Arnab Banerji was appointed as a non-Executive Director. On 29th November 2011 David Watson was appointed as a non-Executive Director. Christophe Ferrand ceased to be an Executive Director on 7th July

**KAMES CAPITAL MANAGEMENT LIMITED
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**DIRECTORS' REPORT
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2011. All other Directors served throughout the year. The Directors have declared that they had no interest in the share capital of the Company in the year to 31 December 2011.

Each of the Directors has been granted a qualifying third party indemnity by the Company, in terms of the sections of the Companies Act 2006.

Creditor payment policy

The objective is to treat our suppliers fairly and in accordance with good commercial practice. Suppliers' invoices are settled in accordance with agreed contractual terms or, if no terms are scheduled, generally within 30 days of the appropriate invoice date.

Corporate governance, capital management and financial instruments

During the year, the Company was subject to global AEGON Asset Management governance. AEGON Asset Management has established a governance framework for monitoring and overseeing strategy, conduct of business standards and operations of the business across the group that includes a clearly stated corporate organisational structure, appropriate delegated authorities and independent internal audit and risk management functions. Risk management for the Company operated within this governance framework.

The Company's objective in managing its capital is to ensure that there are adequate resources to meet the Company's liabilities as they fall due, and to allocate capital efficiently to support growth and repatriate excess capital where appropriate. The Company's capital is managed in conjunction with that of other Companies in the group. The Company manages its capital by measuring its resources and cash available on a regular basis. The Company's capital position and the movement in this from the prior year are disclosed within the Statement of Changes in Equity.

The Company is a wholly owned subsidiary of Kames Capital Plc (formerly known as AEGON Asset Management UK Plc), an entity regulated by the Financial Services Authority. The Company does not have individual capital requirements, but is included within the scope of consolidated capital supervision.

The Company is not exposed to significant financial instrument risk. Credit risk is significantly reduced as assets are primarily cash and short term deposits, which are placed with major banks of acceptable credit standing, and inter-company receivables from AEGON companies.

Risk and Capital Management and Financial Instruments

The Company has a very simple Balance Sheet consisting largely of cash and short-term assets and liabilities.

Credit Risk

The Company offers standard industry credit terms to clients and has an appetite for limited credit risk for this purpose. Aged items exceeding these terms are monitored against set thresholds for acceptable overdue debts. Action is taken to recover such debts (through deduction from client assets if appropriate). The Company's main sources of non-client related credit risk are other AEGON Group companies. These are considered inherent in the business activities of the Company.

No restrictions are imposed on the size of such debts, but there is an aim to collect these in a timely way. The Company has no appetite for on-balance sheet trading activity that might create excessive counterparty risk.

KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2011

The Company has no appetite for direct market risk and is subject to indirect market risk through market impacts on fee income. The Company considers this risk to be uncontrollable; it is inherent in the business of asset management. This risk is mitigated where possible through diversification of asset types. Potential market risk is monitored through scenario analysis.

Liquidity Risk

The Company has a low tolerance for liquidity risk. It operates a liquidity risk management policy setting out minimum threshold levels. Its liquidity position is reported to key management personnel on a monthly basis as part of our regular reporting. The Company's assets are in cash or short term deposits and invoices are settled as they fall due without the need to realise illiquid assets.

Market Risk

Revenues can be impacted by market risk as they are dependant upon the value of assets under management. (Note 12).

Interest Rate Risk

Interest Rate Risk is significant only in that the impact of interest rate movements upon the Company's assets under management affects fee income. The Company considers this risk uncontrollable, as it is inherent in the business of asset management. (Note 12).

Going Concern

The Directors have considered the performance of the Company in 2011, its Statement of Financial Position on 31 December 2011, its future plan and its approach to capital and risk management. The Directors consider that the Company has adequate resources to continue to operate for the foreseeable future. Accordingly, they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

Auditors

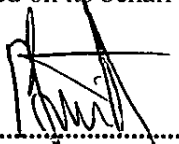
An elective resolution was passed on 10 August 2001 to dispense with (a) the requirement to lay the Report and Accounts before the Company in a general meeting, (b) the holding of an Annual General Meeting for 2001 and subsequent years, and (c) the obligation to appoint auditors annually.

Disclosure of information to auditors

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

This report was approved by the Board of Directors and authorised for issue on 10th April 2012

Signed on its behalf by



.....
Philip J G Smith, MA, CA
Director

**KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)**

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the Annual Report and the Company financial statements in accordance with applicable United Kingdom law and those International Financial Reporting Standards as adopted by the European Union,

Under Company Law the directors must not approve the Company financial statements unless they are satisfied that they present fairly the financial position, financial performance and cash flows of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies in accordance with IAS 8: *Accounting Policies, Changes in Accounting Estimates and Errors* and then apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance; and
- state that the Company has complied with IFRSs, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the Company financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF KAMES CAPITAL MANAGEMENT LIMITED (FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

We have audited the financial statements of Kames Capital Management Limited (formerly known as AEGON Investment Management UK Ltd) for the year ended 31 December 2011 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Cash Flow Statement and the related notes 1 to 15. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company'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. In addition, we read all the financial and non-financial information in the Directors' Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2011 and of its profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

**KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)**

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF KAMES CAPITAL MANAGEMENT
LIMITED (FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)**

Opinion on other matters prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Susan Dawe

Susan Dawe (Senior statutory auditor)

for and on behalf of Ernst & Young LLP, Statutory Auditor

Edinburgh

Date : 10th April 2012

KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2011

	Notes	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Revenue			
Revenue from rendering of services	2	54,575	53,909
Cost of sales	3	<u>(5,407)</u>	<u>(4,920)</u>
Gross profit		49,168	48,989
Administrative expenses	4	<u>(46,294)</u>	<u>(43,371)</u>
Operating profit		2,874	5,618
Finance revenue	5	<u>109</u>	<u>194</u>
Profit before tax		2,983	5,812
Tax charge	6	<u>(767)</u>	<u>(1,658)</u>
Profit for the year		2,216	4,154
Other Comprehensive Income			
Other comprehensive income for the year net of income tax		<u>-</u>	<u>-</u>
Total comprehensive income for the year		<u>2,216</u>	<u>4,154</u>

The result for the year relates wholly to continuing activities.

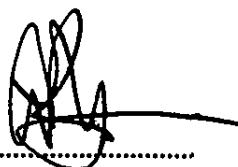
The profit for the year is attributable to the equity shareholders of the Company.

KAMES CAPITAL MANAGEMENT LIMITED
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STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2011
COMPANY NUMBER 212159

	<u>Notes</u>	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Non-current assets			
Deferred tax	7	1,851	1,748
Trade and other receivables	8	-	18
		<u>1,851</u>	<u>1,766</u>
Current assets			
Trade and other receivables	8	3,218	5,541
Cash and short term deposits	9	17,306	16,349
		<u>20,524</u>	<u>21,890</u>
Total assets		<u>22,375</u>	<u>23,656</u>
Current liabilities			
Tax payables		1,261	780
Trade and other payables	10	16,326	13,407
		<u>17,587</u>	<u>14,187</u>
Non-current liabilities			
Trade and other payables	10	359	4,256
Total liabilities		<u>17,946</u>	<u>18,443</u>
Net assets		<u>4,429</u>	<u>5,213</u>
Capital and reserves			
Issued capital	11	1,000	1,000
Retained earnings		3,429	4,213
Total equity		<u>4,429</u>	<u>5,213</u>

The financial statements were approved for issue by the Board on 10th April 2012 and signed on its behalf by



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Andrew N R Fleming, BA
Chief Executive

KAMES CAPITAL MANAGEMENT LIMITED
(FORMERLY KNOWN AS AEGON INVESTMENT MANAGEMENT UK LTD)

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2011

	<u>Issued capital £000's</u>	<u>Retained earnings £000's</u>	<u>Total £000's</u>
At 1 January 2011	1,000	4,213	5,213
Profit for the year	-	2,216	2,216
Dividends paid	-	(3,000)	(3,000)
At 31 December 2011	<u>1,000</u>	<u>3,429</u>	<u>4,429</u>

FOR THE YEAR ENDED 31 DECEMBER 2010

	<u>Issued capital £000's</u>	<u>Retained earnings £000's</u>	<u>Total £000's</u>
At 1 January 2010	1,000	8,559	9,559
Profit for the year	-	4,154	4,154
Dividends paid	-	(8,500)	(8,500)
At 31 December 2010	<u>1,000</u>	<u>4,213</u>	<u>5,213</u>

All equity is attributable to equity shareholders of the Company.

The Company did not recognise any income or expense directly in equity (2010 - £nil).

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CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2011

	Note	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Operating activities			
Profit before interest and tax		2,874	5,618
<i>Adjustment to reconcile profit before tax to net cash inflow from operating activities:</i>			
Decrease/(Increase) in trade and other receivables		2,341	(4,128)
(Decrease)/Increase in trade and other payables		(978)	7,704
Income tax paid		(389)	(1,120)
Interest received	5	109	194
Net cash flow from operating activities		<u>3,957</u>	<u>8,268</u>
Financing activities			
Dividends paid	14	(3,000)	(8,500)
Shares Issued		-	-
Net cash flow used in financing activities		<u>(3,000)</u>	<u>(8,500)</u>
Net Increase/(Decrease) in cash and cash equivalents		957	(232)
Cash and cash equivalents at 1 January		<u>16,349</u>	<u>16,581</u>
Cash and cash equivalents at 31 December	9	<u>17,306</u>	<u>16,349</u>

The cash flow statement is prepared according to the indirect method.

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**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011**

1. Accounting Policies

1.1. Basis of preparation

The Company's financial statements have been prepared on a going concern basis and in accordance with International Financial Reporting Standards as adopted by the European Union as they apply to the financial statements of the Company for the year ended 31 December 2011 and applied in accordance with the Companies Act 2006.

The financial statements of Kames Capital Management Limited (formerly known as AEGON Investment Management UK Ltd) were authorised for issue in accordance with a resolution of the directors on 10th April 2012.

The functional currency of the company is pounds sterling (GBP). Amounts displayed within these accounts are rounded into thousands (£000s).

1.1.1. Adoption of new IFRS accounting standards

New standards become effective on the date specified by IFRS, but may allow companies to opt for an earlier adoption date. In 2011, the following new standards issued by the IASB and Interpretations issued by the IFRS Interpretations Committee (formerly known as the IFRIC) became mandatory:

- Improvements to IFRS (May 2010).

Improvements to IFRS (May 2010)

The IASB issued, in May 2010, a number of minor amendments to 7 different standards and interpretations. These amendments, which are effective from January 1 2011, deal with minor changes to the wordings used in the individual standards and seek to remove editorial and other inconsistencies in the literature. The company adopted all the relevant changes from the improvements project to its accounting policies. The improvements project did not result in any changes to the classification, measurement or presentation of any items in the financial statements.

In addition, the following new standards, amendments to existing standards and interpretations are mandatory for the first time for the financial year beginning January 1 2011 but are not currently relevant for the Group:

- IAS 24 (revised) Related Party Disclosures;
- IFRIC 14 (Amendment) Prepayment of a minimum funding requirement;
- IFRIC 19 Extinguishing financial liabilities with equity instrument;
- IFRS 1 (amendment) First Time Adoption – Limited Exemption from Comparative IFRS 7 Disclosures for First Time Adopters;
- IFRS 1 (amendment) First Time Adoption – Severe Hyperinflation and Removal of Fixed Dates for First Time Adopters
- Amendment to IAS 32 Classification of Rights Issues.

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**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011**

1.1.2. Future adoption of new IFRS accounting standards

The following standards, amendments to existing standards and interpretations, published prior to January 1 2012, were not early adopted by the Group and will be applied in future years:

- IFRS 7 Financial Instruments: Disclosures – Enhanced Derecognition Disclosure Requirements; ¹
- IFRS 9 Financial Instruments; ¹
- IFRS 10 Consolidated Financial Statements; ¹
- IFRS 11 Joint Arrangements; ¹
- IFRS 12 Disclosure of Interests in Other Entities; ¹
- IFRS 13 Fair Value Measurement; ¹
- IAS 1 Financial Statement Presentation – Presentation of Items of Other Comprehensive Income; ¹
- IAS 12 Income Taxes – Recovery of Tax Assets; ¹
- IAS 19 Employee Benefits; ¹
- IAS 27 Separate Financial Statements ¹
- IAS 28 Investments in Associates and Joint Ventures ¹
- Improvements to IFRS (2011). ¹

IFRS 7 Financial Instruments: Disclosures – Enhanced Derecognition Disclosure Requirements

The amendments to IFRS 7 are effective for annual periods beginning on or after July 1 2011 and will improve the understanding of transfer transactions of financial assets including understanding the possible effects of any risks that may remain with the entity that transferred the assets.

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments addresses classification and measurement of financial assets, is available for early adoption immediately, but mandatory only for accounting periods beginning on or after January 1 2013. IFRS 9 replaces the multiple classification and measurement models in IAS 39 with a single model that has only two classification categories: amortized cost and fair value. IFRS 9 represents the first stage in the IASB's planned replacement of IAS 39.

IFRS 10 Consolidated Financial Statements

The standard applies to financial years beginning on or after January 1 2013, and identifies the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess.

IFRS 11 Joint Arrangements

The standard applies to financial years beginning on or after January 1 2013, and provides a reflection of joint arrangements by focusing on the rights and obligations of the arrangement rather than its legal form. The standard requires a single method to account for interests in jointly controlled entities.

¹ Not yet endorsed by the European Union.

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IFRS 12 Disclosure of Interests in Other Entities

The standard applies to financial years beginning on or after January 1 2013, and provides disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, structured entities and other off balance sheet vehicles.

IFRS 13 Fair Value Measurement

The standard applies to financial years beginning on or after January 1 2013, and provides a definition of fair value and a single source of fair value measurement, and disclosure requirements for use across IFRSs.

IAS 1 Financial Statement Presentation – Presentation of Items of Other Comprehensive Income

The amendments apply to financial years beginning on or after July 1 2012. The amendments require the grouping together of items within other comprehensive income that may be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that items in other comprehensive income and profit or loss should be presented as either a single statement or two consecutive statements.

IAS 12 Income Taxes

The amended standard is effective for annual periods beginning on or after January 1 2012. The amendment provides a practical solution to the difficult and subjective assessment whether recovery will be through use or through sale when the asset is measured using the fair value model in IAS 40 Investment Property, by introducing a presumption that recovery of the carrying amount will, normally be through sale.

IAS 19 Employee benefits

The amended standard applies to financial years beginning on or after January 1 2013. The amendments eliminate the option to defer the recognition of gains and losses, known as the 'corridor method'. The amendments streamline the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in other comprehensive income. And furthermore, they enhance the disclosure requirements for defined benefit plans, providing information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

IAS 27 Separate Financial Statements (as revised in 2011)

As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. The amendment becomes effective for annual periods beginning on or after January 1 2013.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. The amendment becomes effective for annual periods beginning on or after January 1 2013.

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Improvements to IFRS (2011)

This set of improvements to IFRS issued by the IASB in June 2011, which applies to financial years beginning on or after January 1 2013, makes a number of minor amendments to 5 different standards and interpretations.

None of the above changes is expected to have a significant impact upon the results of the company.

1.2. Significant accounting judgements, estimates and assumptions

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the Statement of Financial Position date and the amounts reported for revenues and expenses during the year. However, the nature of estimation means that actual outcomes could differ from those estimates.

Taxes

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future profits together with future tax planning strategies.

Deferred tax assets also exist in respect of timing differences relating to the payment of LTIP and DCIP incentives to employees.

The company has deferred tax balances amounting to £1,851k (2010:£1,748k).

1.3. Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding VAT. The following specific recognition criteria must also be met before revenue is recognised:

Rendering of services

Fees are recognised as revenue over the period in which related services are provided.

Interest income

Revenue is recognised on interest on an accrual basis.

1.4 Cost of sales

Cost of sales represents Loyalty Bonus payments made to customers of the Scottish Equitable Pooled Funds. Such payments are recognised over the period in which the related services are provided.

1.5. Deferred transaction costs

Incremental costs, such as initial commission, that are directly attributable to securing future investment management services are recognised as an asset if they can be identified separately and measured

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**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011**

reliably and if it is probable that they will be recovered. This is reported within prepayments and accrued income.

The deferred transaction costs are amortised in line with fee income, unless there is evidence that another method better represents the provision of services under the contract.

1.6. Deferred revenue

Initial fees, margins and front-end loadings paid by clients, for future investment management services, are deferred and recognised as revenue when the related services are rendered. This is reported within accruals and deferred revenue.

The deferred revenue is amortised over a period of four years in line with fee income, unless there is evidence that another method better represents the provision of services under the contract.

1.7. Taxation

Current income tax

Current income tax assets and liabilities for the current period and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities, or paid to or recovered from other group companies in respect of group relief surrendered or received. The tax rates and laws used to compute the amount are those that are enacted or substantively enacted by the Statement of Financial Position date.

Current income tax relating to items recognised directly in equity is recognised in equity and not in the statement of comprehensive income.

Deferred income tax

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

Deferred income tax liabilities are recognised for all taxable temporary differences except:

- When the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss, and
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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 except:

- When the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination

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and, at the time of the transaction, affects neither the accounting profit nor the taxable profit or loss; and

- In respect of deductible temporary differences associated with investments in subsidiaries, associates and interest in joint ventures, deferred income tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each Statement of Financial Position 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 tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each Statement of Financial Position 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 income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the Statement of Financial Position date.

Deferred income tax relating to items recognised directly in equity is recognised directly in equity and not in the statement of comprehensive income.

Deferred income tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred income tax relates to the same taxable entity and the same taxation authority.

1.8. Trade and other receivables

Trade receivables, which generally have 30 day terms, are recognised and carried at the lower of their original invoices value and recoverable amount. Where the time value of money is material, receivables are carried at amortised cost. Provision is made when there is objective evidence that the Company will not be able to recover balances in full. Balances are written off when the probability of recovery is assessed as being remote.

1.9. Cash and cash equivalents

Cash and short-term deposits in the Statement of Financial Position comprise cash at banks and in hand and short-term deposits with an original maturity of three months or less.

For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above.

1.10. Long term Incentive Plan (LTIP)

The LTIP meets the definition of employee benefits as defined in IAS 19. It is a defined contribution plan and the contributions are payable by the Company based on achievement of targets in specified calendar years. The cost of the scheme is recognised as an expense and liability upon achievement of the targets. The Company pays the set amount to an independent employee benefits trust in the year following recognition of the contribution. Once the contribution has been made, the Company has no ability to recover any amount paid to the trust.

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1.11. Deferred Cash Incentive Plan (DCIP)

The DCIP (which operated in prior years) is a deferred bonus scheme which is classified as an other long-term employee benefit under IAS 19. It falls under the definition of a defined benefit plan with contributions to the scheme spread over the term of service provision. Contributions are based on achievement of targets over the period of the plan. The cost of the scheme is recognised as an expense and liability based on the measurement of that liability in a given year. This is re-assessed over the period of the plan, increasing or decreasing the liability as required until vesting.

2. Revenue from rendering of services

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Management Fees	52,298	53,027
Performance Fees	1,353	250
Security Lending Fees	924	632
Fees	<u>54,575</u>	<u>53,909</u>

Revenue represents fees receivable from other AEGON NV subsidiary companies in respect of the provision of investment management services by the Company.

For terms and conditions relating to related party transactions, refer to note 13.

3. Cost of sales

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Loyalty Bonus	5,407	4,920
Cost of Sales	<u>5,407</u>	<u>4,920</u>

Cost of sales relates to Loyalty Bonuses paid to customers of the Scottish Equitable Pooled Funds.

4. Administrative expenses

Administrative expenses include £44,827,110 (2010: £40,988,008) relating to recharges to the Company by AEGON UK Corporate Services Limited, a fellow subsidiary of AEGON NV. For terms and conditions relating to related party transactions, refer to note 13.

AEGON UK Corporate Services Limited, a fellow subsidiary of AEGON NV, employs all staff whose costs are included in administrative expenses.

Details of Directors' emoluments for the year ended 31 December 2011 can be found in the parent company accounts of Kames Capital Plc (formerly known as AEGON Asset Management UK Plc).

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5. Finance revenue

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Cash and short term deposits income	95	171
Interest income on loan to Parent company	14	23
	<u>109</u>	<u>194</u>

Interest income on the loan to the Parent company is calculated at LIBOR plus 0.51%.

6. Taxation

(a) Current year tax charge

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
<u>UK current tax</u>		
Corporation tax for the year	(723)	(1,477)
Adjustments in respect of prior years	(147)	23
Total current tax charge	<u>(870)</u>	<u>(1,454)</u>
<u>UK deferred tax</u>		
Origination of temporary differences	(55)	(134)
Adjustments in respect of prior years	302	-
Change in deferred tax rate	(144)	(70)
Total deferred tax charge	<u>103</u>	<u>(204)</u>
Total tax charge reported in the statement of comprehensive income	<u>(767)</u>	<u>(1,658)</u>

The 2012 Budget announced a number of changes to the corporation tax rate. These included :-

- A reduction in the UK corporation tax rate from 25% to 24% (the 25% rate was enacted by Finance Act 2011 to be effective from 1 April 2012).
- A further reduction in the UK corporation tax rate to 23% effective from 1 April 2013.
- Proposed further changes to reduce the rate of UK corporation tax to 22% by April 2014.

The rate reduction to 24%, effective from 1 April 2012 was substantively enacted on 26 March 2012. The rate reduction to 23%, effective from 1st April 2013 and other proposals included within the Finance Bill have yet to be substantively enacted.

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(b) Reconciliation of tax charge

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Accounting profit before tax	<u>2,983</u>	<u>5,812</u>
Accounting profit multiplied by the UK standard rate of corporation tax of 26.5% (2010: 28%)	(791)	(1,627)
Non tax deductible expenses	13	11
Change in tax rate	(144)	(65)
Adjustments in respect of prior years	<u>155</u>	<u>23</u>
Total tax charge reported in the statement of comprehensive income	<u>(767)</u>	<u>(1,658)</u>

7. Deferred Taxation

Recognised deferred tax

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when income taxes relate to the same fiscal authority. The amounts are as follows:

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Deferred tax assets comprise		
Incentive plans	<u>1,851</u>	<u>1,748</u>
	<u>1,851</u>	<u>1,748</u>
	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Deferred tax assets		
At 1 January	1,748	1,952
Prior Year Adjustments	302	-
Change in deferred tax rate	(144)	(70)
Amounts recorded in statement of comprehensive income	<u>(55)</u>	<u>(134)</u>
At 31 December	<u>1,851</u>	<u>1,748</u>

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8. Trade and other receivables

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Non-current trade and other receivables		
Prepayments and accrued income	-	18
Current trade and other receivables		
Amounts owed by fellow AEGON NV subsidiary undertakings	3,216	3,117
Loan provided to Kames Capital Holding Limited	-	2,400
Prepayments and accrued income	2	24
	<u>3,218</u>	<u>5,541</u>
	<u>3,218</u>	<u>5,559</u>

For terms and conditions relating to related party transactions, refer to note 13.

9. Cash and short term deposits

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Short term deposits	<u>17,306</u>	<u>16,349</u>
	<u>17,306</u>	<u>16,349</u>

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short term deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Company, and earn interest at the respective short-term deposit rates. The fair value of cash and short term deposits is £17,306,565 (2010: £16,349,200).

The Company only deposits cash surpluses with major banks of acceptable credit standing.

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10. Trade and other payables

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Current trade and other payables		
Payables to fellow AEGON NV subsidiary undertakings	11,772	10,075
DCIP accrual	2,757	3,132
LTIP Payable to employee trust	1,764	-
Accruals and deferred income	33	200
	<u>16,326</u>	<u>13,407</u>
Non-current trade and other payables		
Accruals and deferred income	359	391
LTIP Payable to employee trust	-	2,626
DCIP accrual	-	1,239
	<u>359</u>	<u>4,256</u>
	<u>16,685</u>	<u>17,663</u>

Terms and conditions of the above financial liabilities:

- For terms and conditions relating to related parties, refer to note 13.
- Trade payables are non-interest bearing and are normally settled in 30 days.
- The LTIP payable is non-interest bearing and normally settled 3 months after the year end.
- The DCIP accrual (which operated in prior years) payable is non-interest bearing and normally settled within 1 month of the vesting date.

11. Capital and reserves

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Authorised share capital		
10,000,002 Ordinary shares of £1 each	<u>10,000</u>	<u>10,000</u>
Allotted, called up and fully paid		
1,000,002 Ordinary shares of £1 each	<u>1,000</u>	<u>1,000</u>

Information on capital management and risk management is included in the Directors' Report under 'Corporate governance, capital management and financial instruments'.

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12. Risk Management

General

The Company is exposed to financial risks. The main financial risks are credit risk, liquidity risk and market risk, with the principal elements of market risk being interest rate risk and price risk. The Company is not exposed to significant currency risk other than through exposure to the funds it manages, and this risk is managed as for Market risk. The Risk and Capital Management and Financial Instruments section of the Report of the Directors describes the Company's general approach to risk management and the management of financial risks.

Credit Risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company. The carrying amounts of financial assets best represents the maximum credit risk exposure at the balance sheet date.

At the reporting date the Company's financial assets exposed to credit risk amounted to the following :

	<u>2011</u> <u>£000s</u>	<u>2010</u> <u>£000s</u>
Cash and cash equivalents	17,306	16,349
Interest, dividends and other receivables	3,218	5,541

The Company is exposed to credit risk on standard industry credit available to clients and has an appetite for limited credit risk for this purpose. Aged items exceeding these terms are monitored against set thresholds for acceptable overdue debts. Action is taken to recover such debts (through deduction from client assets if appropriate). The Company's main sources of non-client related credit risk are HMRC, or other AEGON Group companies. These are considered inherent in the business activities of the Company. The Company does not hold financial instruments which give rise to concentrations of risk. Details of these balances are listed under note 8.

The company's cash balances are currently held by a number of counterparties. Bankruptcy or insolvency of any of these counterparties may cause the company's rights with respect to the cash balances to be delayed or limited. The Company monitors the credit quality of the relevant counterparties and should the credit quality or the financial position of these counterparties deteriorate significantly the Company would move the cash holdings over to another bank.

Liquidity Risk

The Company has only limited exposure to liquidity risk as balances are held in cash and short term deposits. It operates a liquidity risk management policy setting out minimum threshold levels. Amounts due are settled without the need to realise illiquid assets. Details of these balances are listed under note 9.

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The table below summarises the maturity profile of the Company's financial liabilities at 31 December 2011 and 2010 based on contractual undiscounted payments.

Maturity Analysis

FOR THE YEAR ENDED 31 December 2011

	<u>On</u> <u>Demand</u> <u>£000</u>	<u>Less</u> <u>than 3</u> <u>months</u> <u>£000</u>	<u>3 to 12</u> <u>months</u> <u>£000</u>	<u>1 to 5 yrs</u> <u>years</u> <u>£000</u>	<u>>5 yrs</u> <u>years</u> <u>£000</u>	<u>Total</u> <u>£000</u>
Non Derivative Financial Liabilities						
Trade and other payables	-	11,813	4,513	359	-	16,685

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	<u>On</u> <u>Demand</u> <u>£000</u>	<u>Less</u> <u>than 3</u> <u>months</u> <u>£000</u>	<u>3 to 12</u> <u>months</u> <u>£000</u>	<u>1 to 5 yrs</u> <u>years</u> <u>£000</u>	<u>>5 yrs</u> <u>years</u> <u>£000</u>	<u>Total</u> <u>£000</u>
Non Derivative Financial Liabilities						
Trade and other payables	-	13,384	23	4,256	-	17,663

Market Risk

Results of the Company's sensitivity analyses are presented throughout this section to show the estimated sensitivity of Profit for the year and Shareholder's Equity to various scenarios. For interest rate risk and equity market risk, the analysis shows how these measures would have been affected by changes in the relevant risk variables that were reasonably possible at the reporting date. In performing the analyses and determining the impact for the financial year, the assumption is made that the financial instrument exposures at the Statement of Financial Position date were in existence for a full year. For each sensitivity test the impact of a reasonably possible change in a single factor is shown.

The sensitivities do not reflect what the results for the period would have been if risk variables had been different, because, for financial instruments, the analysis is based on the exposures in existence at the reporting date rather than on those that actually occurred during the year. The analysis does not take into account the impact of future new business, which is an important component of the Company's future earnings. It also does not consider all instruments available to management to respond to changes in the financial environment. Furthermore, the results of the analyses cannot be extrapolated for wider variations since effects are not always linear. No risk management process can clearly predict future results.

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Interest Rate Risk

The sensitivity analysis in the table below shows an estimate of the effect of a parallel shift in the yield curve on Profit for the year and Shareholders' Equity. The effect of an increase in the yield curve would be to reduce the overall asset valuations thereby reducing fee income earned. The converse applies for a reduction in yield. Because assets are not held within the Statement of Financial Position of the Company the only equity impact of this change is on Fee Income earned and is carried directly through the Statement of Comprehensive Income to impact Retained Profits.

	<u>Impact on</u> <u>profit for</u> <u>the year</u> <u>2011</u> <u>£000's</u>	<u>Impact on</u> <u>equity</u> <u>2011</u> <u>£000's</u>
Immediate change		
Shift up 100 basis points	(547)	(547)
Shift down 100 basis points	547	547

	<u>Impact on</u> <u>profit for</u> <u>the year</u> <u>2010</u> <u>£000's</u>	<u>Impact on</u> <u>equity</u> <u>2010</u> <u>£000's</u>
Immediate change		
Shift up 100 basis points	(1,349)	(1,349)
Shift down 100 basis points	1,349	1,349

Equity price risk

The sensitivity analysis of Profit for the year and Shareholders' Equity to changes in equity prices is presented in the table below. The sensitivity of Profit for the year and Shareholders' Equity primarily reflects changes in the value of Assets under Management leading to corresponding increases or decreases in fee income and therefore profits.

	<u>Impact on</u> <u>profit for</u> <u>the year</u> <u>2011</u> <u>£000's</u>	<u>Impact on</u> <u>equity</u> <u>2011</u> <u>£000's</u>
Immediate change		
Equity increase 10%	1,124	1,124
Equity decrease 10%	(1,124)	(1,124)

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	<u>Impact on</u> <u>profit for</u> <u>the year</u> <u>2010</u> <u>£000's</u>	<u>Impact on</u> <u>equity</u> <u>2010</u> <u>£000's</u>
Immediate change		
Equity increase 10%	1,422	1,422
Equity decrease 10%	(1,422)	(1,422)

13. Related party transactions

(a) Immediate parent undertaking

The immediate parent company is Kames Capital Plc (formerly known as AEGON Asset Management UK Plc) which, is registered in Scotland. Copies of Kames Capital Plc accounts are available from the Company Secretary, Kames Capital Plc, Edinburgh Park, Edinburgh, EH12 9SE.

(b) Ultimate parent undertaking

The ultimate parent company is AEGON NV, which is incorporated in the Netherlands. The group accounts of AEGON NV are available from the Company Secretary, Kames Capital Plc, Edinburgh Park, Edinburgh, EH12 9SE.

(c) Year end balances and transactions with related parties

The Company provides investment management services to other members of the AEGON UK Plc Group at prices which are agreed from time to time between the Company and the recipients of the service, taking into account the size and nature of the service (see note 2 for total amount of such transactions). Income for these services is derived from Management Fees, Performance Fees and Security Lending Fees. For further detail of these transactions refer to Note 2.

Administrative expenses are recharged to the Company at cost plus a 5% mark-up by AEGON UK Corporate Services Limited, a fellow subsidiary of AEGON NV (see note 4 for total amount of such transactions).

The Company also provides and receives shared services from other members of the AEGON Asset Management Group. Expenses relating to these shared services are recharged at cost plus a 5% mark up.

Outstanding balances are unsecured, interest free and cash settlement is generally expected within 30 days of invoice. The Company has not provided or benefited from any guarantees for any related party receivables or payables. During the year ended 31 December 2011 the Company has not made any provision for doubtful debt relating to amounts owed by related parties (2010: nil).

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During the year a loan of £2,400,000 which the company had made to Kames Capital Holdings Ltd (formerly known as AEGON Asset Management UK Holding Ltd) was repaid in full.

Year end balances for related party transactions are detailed in notes 8 and 10.

(d) Compensation of key management personnel (including directors)

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Short term employee benefits	1,346	1,188
Post employment employee benefits	110	114
Other long term benefits	826	773
	<u>2,282</u>	<u>2,075</u>

14. Dividends paid and proposed

	<u>2011</u> <u>£000's</u>	<u>2010</u> <u>£000's</u>
Declared and paid during the year		
Equity dividend on ordinary shares		
Final dividend for 2011 – 300p (2010 : 850p)	<u>3,000</u>	<u>8,500</u>
 Proposed for approval by shareholders		
Final dividend for 2011 – nil (2010 300p)	<u>-</u>	<u>3,000</u>

15. Post balance sheet events

There were no significant events in the period from 1st January 2012 to the date of signing of the financial statements.