Controlling life-long tissue renewal

A year of significant progress and growth

Epistem Holdings Plc
Annual Report and Accounts 2007

Epistem is a biotechnology company commercialising its expertise in epithelial stem cells in the areas of oncology, gastrointestinal diseases and dermatology.

Epistem has become recognised as a specialist in epithelial tissue and stem cell analyses. Our heritage is based on expert science and know-how in the field of epithelial tissue and adult stem cell biology.

Epistem provides specialised preclinical efficacy testing, biomarker services and the development of novel therapies for partner companies across the biotechnology and pharmaceutical drug development industries.

Founded in 2000, the Company was originally part of the Paterson Institute for Cancer Research, UK. The founders and management are international experts in epithelial tissue and stem cell control and lead a team of scientific staff with specialist skills in the field.

Stem cell research and discovery is a sophisticated and growing area of therapeutic focus where Epistem has amassed significant background expertise, know-how, and intellectual property, enabling the Company to build a sizeable barrier to technical entry.

Our innovations, discoveries and developments are focused on targeting unmet medical needs primarily in cancer and gastrointestinal diseases where the world market for these therapeutic areas was estimated to be over $35.0bn in 2006.

Located in purpose-built office and laboratory facilities adjacent to The University of Manchester, UK, Epistem maintains close links with drug development companies, clinicians and academics in the field, ensuring that the Company remains at the forefront of stem cell science and technology development.

Epistem does not conduct research into embryonic stem cells or stem cell transplantation.

Business Overview

Review of the year

Governance

Accounts

What we do

Life-long tissue renewal explained

Epithelial stem cells
Epithelial stem cells are rare cells which represent the 'building blocks' of tissue growth and renewal. Stem cells are essential for tissue repair, wound healing and tissue renewal since they are responsible for all cell replacement.

Expertise
Epistem is applying its know-how and expertise to identify controlling genes and proteins, their activities and responses to external factors in order to develop drugs to treat cancer and other epithelial diseases.

Innovative therapeutics, clinical biomarkers and contract research services to drug development companies

Novel Therapies

Epistem is discovering key regulators of adult epithelial stem cells and developing therapeutics to control cell production, initially in the area of oncology. With over 80% of adult cancers arising from epithelial tissues, the Company believes that its understanding of the behaviour of stem cells will identify new targets and pathways for drug development.

The Novel Therapies division is focused on developing its own proprietary therapeutics based on its discovery of key regulators of epithelial cell production. The team has identified 250 potential protein regulators which are being evaluated in the Company's preclinical efficacy models. Lead candidates are now starting to emerge.

Biomarker

Epistem is developing an innovative, non-invasive test for pharmaceutical companies developing new drugs, initially in the area of oncology. The test is designed to identify changes in gene expression that result from treatment with a new targeted oncology drug. The Company is currently working with several top-tier pharmaceutical companies and anticipates applying its test to the treatment of cancer patients in the near term.

This proprietary new biomarker technology leverages the Company's knowledge of the behaviour of epithelial stem cells and high resolution gene expression to measure drug effects during treatment.

Epithelial tissue and the importance of adult stem cells:
All body surfaces and cavities such as the skin, gastrointestinal tract, the lining of the mouth, genital cavities and breast ducts are lined by epithelial tissue, providing a protective barrier. Under normal conditions this barrier is maintained by an active process where cell loss is balanced by cell production throughout our entire lives.

The importance of stem cell analyses:
The study of epithelial stem cells, their regulatory genes and their responses to external factors is important when developing novel drugs to treat epithelial diseases – in order to determine the clinical applications of a candidate drug and its potential side effects at the earliest possible stage of drug development.

Vision

Epistem's vision is to control stem cells with its emerging novel protein therapeutics to provide a new biological approach to prevent, treat or cure health and life-threatening diseases.

Contract Research Services

Contract Research Services provides specialised preclinical efficacy testing primarily for drug development companies on a fee for service basis. The division is growing strongly and is cash generative and profitable on a stand-alone basis. Our Contract Research Services group has an established five-year track record of providing testing services to over 80 client companies primarily in Europe and the United States, including most major pharmaceutical companies.

We assist companies with the preclinical development of their drug therapies to treat epithelial proliferative diseases including:

- Cancers
- Mucositis (cancer supportive care)
- Inflammatory bowel disease
- UV-induced skin damage
- Wound healing
- Dermatology

Stem cell models:
Adult stem cells are not the easiest of cells to study since they are rare and cell markers are generally unavailable. However, Epistem has developed small and large intestinal stem cell assays which provide well-proven biological models for studying stem cell behaviour.

Genetic and molecular analysis of adult stem cells:
Epistem's in-house single cell molecular analysis techniques, coupled with its extensive knowledge of gut epithelial tissue and efficacy models, enable the Company to undertake powerful molecular analysis of adult stem cells. This technical and biological advantage underpins the Company's drug development and partnership programmes.

Our business and strategy

A robust business model with a strategy for future growth

Epistem has an unrivalled knowledge of epithelial tissue behaviour and an extensive array of stem cell assays, which is becoming a key consideration in the development of new epithelial drugs.

Future Strategy

Preclinical

Contract Research Services

Specialised efficacy testing in:

- Oncology
- Mucositis
- Inflammatory bowel disease
- Dermatology

Novel Therapies

Discovery leads and characterisation

Biomarkers

Preclinical and clinical development programmes. Fee for service and licensing opportunities

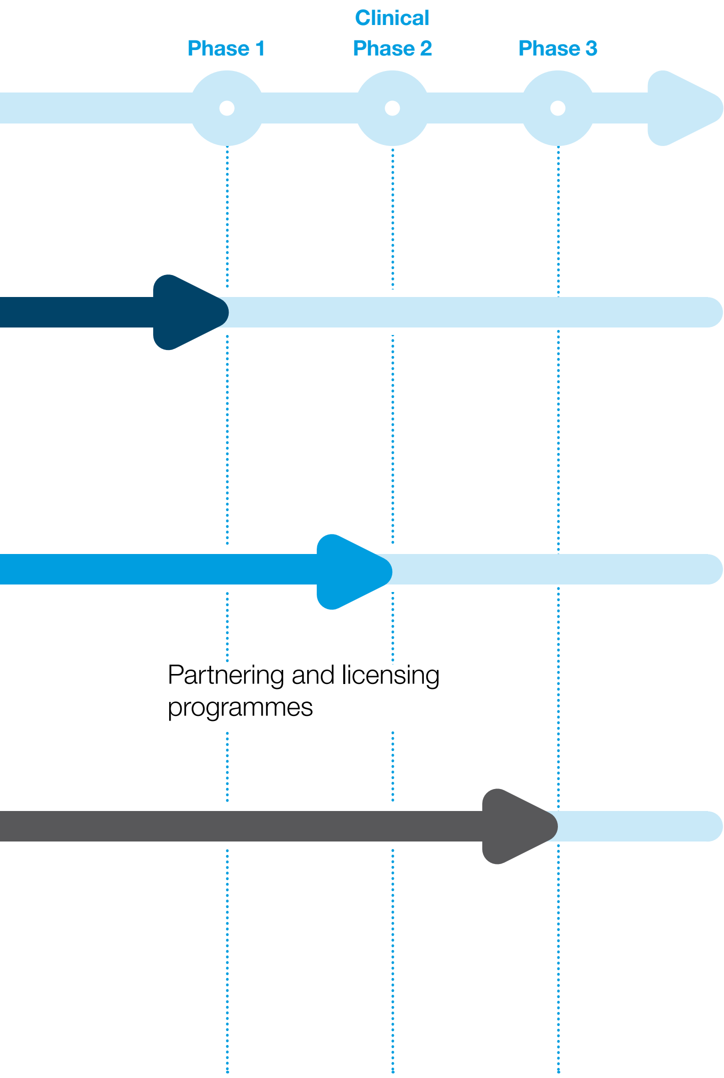
Strategic goals:

Growth: Epistem expects to deliver impressive and sustainable turnover growth and increased visibility over the forthcoming year. Advancing our critical mass and increasing awareness of our leading edge technology and commercial developments will underpin this growth position.

Technical: Our stem cell core expertise and industry recognition is anticipated to grow considerably over the next year, based on an increased number of collaborations and licensing programmes in stem cell testing and drug development. We expect to supplement where necessary our technical groups with industry leading expertise.

Financial: Turnover over the forthcoming year is forecast to maintain the past year's growth trend, with the first commercial advances in our biomarker programme forecast towards the end of the year. We will continue to support and nurture our combined business model which we believe strengthens our company financial offering whilst allowing us to invest in developing our Novel Therapies business.

Investor: The product of Epistem's growth and the technical and financial forecasts provides an increasingly attractive investment opportunity for investor groups. The UK biotechnology industry often provides a volatile environment for small technology growth companies, but the combined business model coupled with the Company's developments in the field of stem cells marks Epistem as a highly exciting stock with significant future opportunity.



Combined business model

Epistem's approach is a balanced risk model which combines its profitable and growing Contract Research Services division with the discovery and early development of novel therapeutics.
The Contract Research Services business has already established robust relationships with pharmaceutical and biotechnology leaders worldwide. These relationships and our wide ranging stem cell services provide the basis of the future partnering strategy for Epistem's emerging novel therapeutics and biomarker business.

Active partnering programme

The Company licensed its first drug candidate to a clinical development company in February 2007. This is a powerful validation of the underlying platform of the Novel Therapies division, while providing potential revenue-generating opportunities over the longer term.

Further licensing opportunities

The depth of the platform underpinning the Company's Novel Therapies is reflected by the 250 potential drug candidates which the Company has identified to date.

A number of these candidates are now undergoing further development as stem cell regulators, which will drive Epistem's drug development pipeline.

Feasibility studies are under way with several drug development companies using Epistem's clinical biomarker technology.

A year of progress

The 2006/07 financial year saw Epistem transition from a biotechnology start-up to an AIM-listed public company with outstanding opportunities in its chosen field. The maiden results for the Company were also impressive, with year-on-year turnover up 50%. Epistem's shares were well received in the market with the stock post-flotation showing a 20% premium on the admission price.

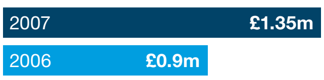
A strong turnover that positions us well for the future

Year highlights

- Epistem admitted to AIM; £3.0m funds raised – 2.5m of new ordinary shares issued at £1.24
- Epistem Holdings Plc announces biomarker studies for new drug development programme with AstraZeneca plc
- Epistem's radiation damage models for intestinal stem cells chosen for the US National Institute of Health bio-defence programme
- Epistem contracts with Eden Biodesign for the manufacture of 250 candidate therapeutic proteins
- Epistem Novel Therapies division enters its first out-licensing agreement
- Epistem announces the successful completion of the initial series of tests for the US National Institute of Health bio-defence programme and the commissioning of follow-on studies
- Epistem develops a comprehensive protocol for plucking human hair for use as a non-invasive biomarker

Key performance indicators

Turnover



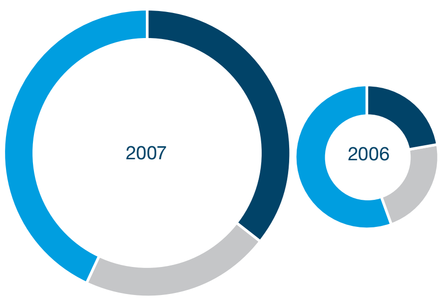
+50%

Our business split by turnover

United Kingdom
£0.6m
(2006: £0.5m)

United States
£0.5m
(2006: £0.2m)

Europe and Asia
£0.3m
(2006: £0.2m)



Biotechnology drug market dynamics

Growth in the biotechnology industry is projected to account for approximately 25% of the total drugs on the market by 2010. In 2006, the top selling biotechnology drugs accounted for $56.4bn in revenue, compared to a total of $44.2bn in 2005, representing a 27% increase. Additionally 25% of the 100 top selling drugs on the market in 2006 were biotechnology drugs. 25% of 102 drugs on the market that had revenues of $1bn or more were biotechnology-derived drugs. New biotechnology drug development remains most prominent in the development of cancer and gastrointestinal disease therapeutics.

Strategic Progress in 2007

The combination of a revenue-generating and profitable Contract Research Services group coupled with an investment-driven Novel Therapies division continued to provide a balanced risk profile for our development throughout the year. The year saw Epistem extend the growth of its Contract Research Services model alongside acceleration of its Novel Therapies drug discovery programme. The ongoing successful validation, growth and commercialisation of the Company's proprietary technology underpins the Company's core strategy for 2008.

Technology platform

At the heart of Epistem's strategy is the Novel Therapy drug discovery programme targeting identification of the key proteins which control cell production. Knowledge of the behaviour and regulation of tumour-maintaining cells and stem cells is increasingly being developed and integrated into oncology companies as part of their drug development strategies. This is an area of key expertise for Epistem, with the Company well placed to participate in the discovery and validation of new targets.

Biomarkers

Recent commercial advances in our development of single plucked hairs to provide a surrogate biomarker for the development of cancer therapeutics will be an important and valuable adjunct to Epistem's core technology position. During the course of 2007, the Company has entered into a series of feasibility studies to validate the use of plucked hairs as drug development biomarkers to determine the gene signature (correlation with genes of interest) for new cancer drugs in development. The Company hopes to establish a new division to market and deliver this biomarker service to drug development companies primarily in the field of cancer therapeutics.

Integrated business model

A key feature of Epistem's business model is the ability to test its emerging Novel Therapeutics in the Contract Research division's range of leading stem cell assays. This integrated approach to drug discovery and lead candidate characterisation provides a powerful means of identifying and benchmarking new drug discoveries and their activities. Equally strong is the link between our biomarker for drug development and the extension of the customer collaborations for our Contract Research Services. During the course of 2007, the breadth and depth of our Contract Research Services client base broadened appreciably as clients have taken an interest in Epistem's core technology platform.

Bio-defence

The position of Epistem's mucositis assays as the "gold standard" in testing the efficacy of new bio-defence therapeutics (based on treating mucositis) has been underscored by the selection of Epistem by the US National Institute for Health in its programme to discover new treatments for the effects of radiation fallout. The success of the programme has led to a substantial increase in the turnover of the Contract Research Services division.

Novel Therapies drug discovery programme

Investment

2007	£1.0m
2006	£0.8m

+£0.2m

Operating loss

2007	£1.2m
2006	£1.0m

Cash resources

2007	£2.3m
2006	£0.7m

The Company is satisfied that it has sufficient resources to enable it to undertake its investment plans.

Chairman's Statement

The forecast outlook for 2007/08 maintains strong advances in our revenue. This forecast is based on the pharmaceutical and biotechnology industry's demand and interest in our stem cell technology products and services, our recognised expertise and management team, and the increased number of commercial opportunities now beginning to emerge. This confluence of activities will define Epistem globally as one of the most forward and exciting companies in the biotechnology sector.

Dear Shareholder,

I am delighted to present the maiden annual report for the Company following its admission to AIM on 4 April 2007.

The overall report has been designed to provide a summary of the year's progress and to explain the background and opportunity behind our scientific and commercial plans for the exploitation of our unparalleled knowledge of adult epithelial stem cells.

The financial results for the Group as presented in this report are prepared using merger accounting, thus reflecting the results for the Group's sole subsidiary for the year to 30 June 2007 and for the comparative period to 30 June 2006.

A year of progress

Fuller details of the results for the period are covered in the CEO's review but, operationally and financially, the year to 30 June 2007 saw the Company generate revenues of £1.4m (2006: £0.9m). With a net CRO contribution of £0.25m (2006: £0.2m), and research and other operating costs of £1.5m (2006: £1.2m), the after tax loss reported for the year was £1.0m (2006: £0.9m).

Cash held in the Company at the end of June 2007 was £2.3m.

During the year, the Group made significant progress on a number of key fronts:

- Contract Research revenues grew by 50% to £1.4m (2006: £0.9m) underpinned by a three-year contract signed with the University of Maryland as part of a US government bio-defence initiative.
- The first biomarker contracts were signed with both a large pharma and an emerging US biotech company. The rate of commercial progress has been rapid and the key risks lie in the technical execution and the validation of the underlying hypothesis that mRNA analysis of the plucked hair is a surrogate for what is happening to epithelial stem cells in the small intestine.
- The first commercial contract for the exploitation of one of Epistem's identified proteins was signed with an early stage UK biotechnology company. Whilst the initial sums of money are not significant, it has demonstrated initial proof of principle, that even for a new use for a well known drug, Epistem can commercialise its output from its Novel Therapies division. This augurs well for the future.
- Management was significantly strengthened through the appointment of Matthew Walls as CEO, who brings a welcome blend of experience, energy and commitment to the Group.
- In April, Epistem achieved a successful flotation on the LSE AIM Market, one of the few biotech companies to do this during 2007 in the UK, and this was achieved through a dedicated team effort. Allied to the move to AIM, the Company strengthened its Board in July 2007 with the appointment of Dr Roger Lloyd as a non-executive director. Roger's wealth of experience as Head of Licensing at Astra Zeneca will be invaluable to the Group as it moves forward its discussions with large pharma for the commercial exploitation of its protein therapeutic targets.

Current trading

Trading in the first three months of the new financial year has been buoyant and is at least 30% ahead of the comparative period last year.

Outlook

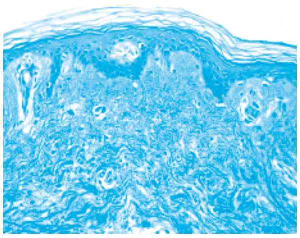
The outlook for Epistem is very positive, although we remain vigilant of the key challenges ahead. This positive outlook is driven, in particular, by the progress made with the biomarker programme and the substantial level of interest now being generated. The biomarker interest has also created a complementary platform to help support discussions around our Novel Therapies development programme. The Board recognises that the development of its novel protein therapies will require the support and participation of like-minded drug development companies to partner closely with Epistem to achieve our therapeutic goals.

Finally I would like to thank both the Group's employees for their passion and commitment in ensuring Epistem's continued progress and you, as shareholders whose support has underpinned a year of marked achievement.

David Evans
Chairman
10 October 2007

October 2006
Epistem contracts with Eden Biodesign for the manufacture of 250 candidate therapeutic proteins

November 2006
Epistem's radiation damage models for intestinal stem cells chosen for the US National Institute of Health bio-defence programme



Chief Executive's Review

Our achievements over the past year pave the way for significant future growth.

Over the past year, Epistem has taken significant technical and commercial steps in developing itself as a globally-recognised drug discovery and early-stage development company, focused in the areas of cancer, gastrointestinal (GI) and other epithelial diseases.

There have been a number of notable milestones in 2007, including a 50% year-on-year growth in company revenues, the commencement of our bio-defence collaboration with the US government, feasibility studies for a new proprietary plucked hair biomarker, signed heads of terms for the out-licensing of our first proprietary therapeutic and our recent well-received admission to AIM and £3.0m fundraising.

Each of the Company's divisions has developed strongly over the past year and I am pleased to report that these developments have met fully with our 2007 business plan.

February 2007
Epistem Novel Therapies division enters its first out-licensing agreement

Combined business model
Epistem operates a combined business model that offers significant out-licensing opportunities from its drug and biomarker developments (Novel Therapies division), in addition to lower-risk activities providing drug testing services for third parties (Contract Research Services division).

This combined business model also enables the Company to integrate its divisional expertise to produce a drug discovery and testing house for its own, proprietary novel protein therapeutics.

Financial review
The Company reports turnover of £1.4m (2006: £0.9m) for the year ended 30 June 2007. This revenue figure is drawn almost entirely from the Contract Research Services division where increased demand for the Company's efficacy testing assays was the prime driver for the year-on-year growth.

Revenues for the Company were mainly generated across the UK and US markets, with mainland Europe beginning to generate revenues resulting from new dedicated business development support for this territory.

On a stand-alone basis, Contract Research Services' contribution increased year-on-year by 28% to £0.25m. Investment in our Novel Therapies (including Biomarkers) and central administration increased year on year by £0.3m, to £1.5m, due to increased headcount in senior management and production cost investment in our protein therapeutics. The loss reported for the financial year (net of a £0.2m R&D tax credit) was £1.0m (2006: £0.9m). Headcount in the Company is now 30 (2006: 29).

The Company was admitted to the LSE: Alternative Investment Market (AIM) on 4 April 2007 raising £3.0m (£2.5m net of listing expenses) at an issue price of £1.24 per share. Demand for the Company's stock has remained firm and the stock has subsequently out-performed the market indices. Cash balances at the June 2007 financial year end were £2.3m.

The Company's annual audit was completed in October 2007 by HW, Chartered Accountants, and their Audit report is included in the annual accounts.

Operating review
Contract Research Services
The Contract Research Services division provides specialist epithelial testing for companies wishing to evaluate their cancer, GI and dermatological drugs against a wide range of both normal and diseased epithelial tissues including lung, colon, breast, prostate and skin, all of which have been well characterised, over many years, by the Company.

The Contract Research Services team has built an enviable record of working with major international pharmaceutical and biotechnology companies.

During 2007, the Contract Research Services team saw the initiation of the Company's first major contract with the US National Institute of Health (NIH) to test treatments for radiation sickness following a nuclear terrorist attack. Epistem is the major provider of these services, which identify novel drugs that can improve the repair of the GI tract following exposure to irradiation. There are currently no medications approved by the FDA to treat this condition. Epistem is an established provider of similar GI services for oncology supportive care. The contract with the US NIH is expected to develop further over the forthcoming year.

April 2007
Epistem Holdings Plc admitted to AIM; £3.0m funds raised – 2.5m of new ordinary shares issued at £1.24

May 2007
Epistem Holdings Plc announces biomarker studies for new drug development programme with AstraZeneca plc

Chief Executive's Review (continued)

During 2007, the Company entered its first out-licence agreement, including milestone payments for a small molecule in the area of gastrointestinal and oncology supportive care.

Operating review (continued)

Contract Research Services (continued)

The tests performed by Epistem are also likely to identify agents with oncology supportive care applications. These agents will reduce mucositis – severe ulceration and diarrhoea experienced by patients during radio- and chemotherapy.

Product development remains a vital part of our specialist assay service and the Company is currently developing novel stem cell services for drug efficacy testing. The division is also extending its Inflammatory Bowel Disease portfolio of assays to meet with increased customer demand.

The 2007 year saw greater visibility and awareness of the Company's assays and services, which resulted in an increase in the number of contractual service agreements with our pharmaceutical and biotechnology partner companies. Increased awareness of the Company's core expertise and know-how is still unfolding and customer numbers are set to grow further in 2008.

Biomarkers

The Company's biomarker technology is based on gene expression profiles which measure how a single plucked hair can provide a means of evaluating how effectively a drug is targeting a particular gene or set of genes in a signal pathway. Epistem's biomarker technology is at the forefront of cancer drug development and provides an innovative approach to quickly assessing cell and tissue exposure to a drug. Epistem commenced its first biomarker feasibility studies during 2007 with a number of pharmaceutical partners. Biomarker demand continues to build and this has been further buoyed by the US FDA's efforts to find effective biomarkers for cancer therapeutic development.

There are inevitable risks in the development of this technology as it is positioned to measure the effectiveness of cancer therapeutic agents, but we are confident, based on recent developments, that we will pioneer a new approach to help guide oncology-based drug development. We expect to see the first preclinical and clinical results of our efforts in the fourth quarter 2007.

We also forecast an increased revenue contribution for the forthcoming financial year arising from our developments and collaborations in this new business area.

Novel Therapies

Epistem is focused on the discovery of novel protein therapeutics to control the production of epithelial cells. The Company has focused its high resolution gene expression technology on the discovery and development of novel therapeutics which regulate cell production, including inhibition. The development of these protein cell regulators will initially target the disease areas of oncology, oncology supportive care (mucositis), GI and other epithelial disorders such as wound healing.

During the year, the Company identified and selected a core group of 250 proteins from which to find those responsible for controlling cell production. These proteins have advanced through development and the initial subset has now been selected for testing through the Company's established disease efficacy models. Over the next few months, the Company expects to identify a number of emerging lead candidates with activity and efficacy relevant to our targeted disease areas. It is expected that these leads, the Company's discovery programme and our high resolution gene expression platform will form part of a partnership collaboration to identify and develop protein therapeutics targeting cancer stem cells.

There are risks associated with our therapeutic discovery programme, primarily in relation to an extended timescale for the identification of robust protein therapeutic activities. To mitigate these risks, the Company has undertaken to identify and develop the 250 proteins via a number of routes to maximise the probability of its success. It will also seek to minimise any development timescale exposure by identifying complementary pharmaceutical or biotechnology partners to co-develop its protein regulators and other elements of its novel therapeutic programme.

Epistem's protein therapeutic discovery strategy is to develop its protein leads to late stage preclinical validation and then licence and/or co-develop these novel therapeutics with its pharmaceutical and biotechnology partner companies.

During 2007, the Company entered its first out-licensing agreement, including milestone payments, for a small molecule in the area of GI and oncology supportive care.

Intellectual property

Traditionally, Epistem has provided its know-how and expertise on a fee-for-service basis.

The biomarker technology is proprietary to the Company and any intellectual property emerging in relation to this technology will be secured, as appropriate, by the Company. Provision for control over biomarker intellectual property arising out of biomarker commercial contracts will also be secured by the Company.

With a pipeline of novel proteins now emerging, the Company will also secure its valuable intellectual property rights in relation to these proteins as they advance through development on a case-by-case basis. The company's protection of normal mucosal tissues patent in relation to its first out-licence is currently undergoing patent examination.

Outlook

Epistem is developing its technology, lead therapies and contract services whilst rapidly growing its revenues and expertise. This requires a careful management approach, good communication and a close relationship with our investor base. We have a globally recognised and experienced management team with strengthening commercial expertise. We are confident that the year ahead will see a substantial increase in our forecast revenues, supported by our Contract Research Services and Biomarker growth alongside our Novel Therapies' emerging lead candidates.

The Company will also consider other complementary technology acquisitions and in-licensing where appropriate to underpin its growth ambitions.

Finally, I would like to thank the Board, management and employees for their continued commitment in building the success of Epistem, as well as both our established and new investors for their continued close support of our exciting company. It has been my privilege to join the Board of Epistem and it is our ambition to significantly build shareholder value by providing the next generation of cancer and GI therapies, by exploiting our know-how and expertise in epithelial stem cells.

Matthew H Walls
Chief Executive Officer
10 October 2007

June 2007
Epistem develops a comprehensive protocol for plucking human hair for use as a non-invasive biomarker

September 2007
Epistem announces the successful completion of the initial series of tests for the US National Institute of Health bio-defence programme and the commissioning of follow-on studies

Board of Directors

1. David Evans (aged 47)
Chairman
David joined Epistem as a Non-executive Director in June 2005 and became Executive Chairman in March 2006 until the flotation in April 2007, when he reverted to a non-executive position. David, a qualified accountant, has many years' experience both as an executive and as a non-executive of publicly listed diagnostic and life science companies. In addition to his chairmanship of Epistem, he is currently Non-executive Chairman of the following AIM listed companies: BBI Holdings plc, Immunodiagnostic System Holdings plc and Omega Diagnostics Group plc.

2. Matthew Walls (aged 43)
Chief Executive Officer
Matthew joined Epistem in February 2007 as Chief Executive Officer. He is an experienced CEO, most recently with Oxford Biosignals Limited, where he led the strategic collaboration with Rolls Royce Plc and Covance Inc. Matthew spent the early part of his career with ICI Plc, progressing through to AstraZeneca Plc prior to its plant crop biotechnology group merger with Novartis to form Syngenta Plc. Matthew has led the growth of several technology and biotechnology companies as CEO, including Internexus Limited and Zylepsis Limited. He holds a non-executive post at Riyada Oxford Investments Limited and is a chartered accountant and a member of CIMA.

3. John Rylands (aged 52)
Financial Director
John originally joined Epistem as an investor and Non-executive Director, and in 2005, he took over his current role. John provided corporate finance advice to private companies before joining Epistem. Until 1999 he was an investor in and consultant to the SDS group of companies. John holds a degree in Economics and Accountancy from Manchester University and is a member of ICAEW.

4. Jeffrey Moore, Ph.D. (aged 47)
Managing Director, Novel Therapies
Jeffrey joined Epistem in 2005 in his current role. Prior to joining Epistem he had been at Phylogix, a US biotechnology company which he founded in 1998. Jeff has held two postdoctoral fellowships at different research institutes, DNAX Research Institute of Molecular and Cellular Biology Inc and the Walter and Eliza Hall Institute of Medical Research, following which he joined Imclone Systems Inc. Throughout his career, Jeffrey has kept a strong interest in stem cell regulation and the potential commercial application of these factors and he holds a Ph.D. from George Washington University.

5. Prof. Chris Potten, Ph.D. (aged 66)
Chief Scientific Adviser
Chris is a co-founder of Epistem and the Company capitalises on the results of the research that was produced by him and his team at the Paterson Institute over the past three decades. While not involved in the day-to-day management of the Company, Chris keeps a strong interest in the progress and success of the Company and prior to Epistem's AIM listing, was its biggest individual shareholder.

6. Catherine Booth, Ph.D. (aged 42)
Managing Director, Contract Research Services
Catherine is a co-founder of Epistem and prior to starting Epistem she worked for 10 years with Prof. Chris Potten at the Paterson Institute. Whilst at the Paterson Institute she developed many pre-clinical assays. This knowledge is at the core of the Epistem Contract Research Service. Catherine received her Ph.D. from Emmanuel College, University of Cambridge.

7. Gerard Brady, Ph.D. (aged 51)
Research Director, Novel Therapies
Gerard joined Epistem shortly after its inception from Manchester University, where he was a lecturer, and was previously a Zeneca Fellow. He brought with him important technological expertise gained through working on blood stem cells. Of particular importance to Epistem is his expertise in single cell gene analysis, which enables the examination of rare cells such as stem cells. Gerard previously held scientific positions in Canada and at EMBL, Heidelberg.

8. Robert Nolan, Ph.D. (aged 64)
Non-executive Director
Robert has been a Non-executive Director of the Company since 2004. He brings with him a wealth of expertise in partnering and licensing negotiations both with small biotechnology and large pharmaceutical companies. Prior to his retirement he was Director, Global Licensing at AstraZeneca. He is also a Non-executive Director of f2g Ltd.

9. Roger Lloyd, Ph.D. (aged 59)
Non-executive Director
Roger joined the Board as a Non-executive Director on 1 July 2007, having only recently stood down as Executive Director, Global Licensing, at AstraZeneca plc. In this capacity, he headed up the deal-making team responsible for the acquisitions by AstraZeneca of Cambridge Antibody Technologies plc and KuDOS Pharmaceuticals Limited, as well as other strategically important transactions.

Directors' Report

For the year ended 30 June 2007

The Directors present their first report for Epistem Holdings Plc ("the Company") and its subsidiary (together "Epistem" or "the Group") for the period ended 30 June 2007. Notwithstanding that Epistem Holdings Plc was incorporated part way during the year, this Report and the attached Accounts seek to reflect, where appropriate, the activities of the Group for the full year from 1 July 2006 to 30 June 2007.

Principal activities and review of the business

The principal activity of the Group during the period was the provision of services to the biotechnology and pharmaceutical industries, covering preclinical testing and gene biomarker services and the development of novel therapeutics for partner companies. A detailed overview of the activities of the Group is outlined in the Business Overview on pages 2-5 of this report.

A review of the business during the period which summarises overall progress, research and development and key performance, risks and developments is detailed in the Review of the year on pages 6-13 of this report.

Results and dividends

The trading results for the period and the Group's financial position at the end of the financial period are shown in the financial statements on pages 22-42 of this report.

The statements have been prepared under International Financial Reporting Standards ("IFRS"). The adoption of IFRS 2 relating to the issue of share options has given rise to a fair value adjustment, which is detailed in Note 18 to the Accounts.

The Directors do not recommend payment of a final dividend.

Going concern

After due consideration, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Directors and their interests in shares

Directors' interests in the share capital of the Company, including family and pension scheme trust interests, were as follows:

	Date of appointment	1 July 2006	16 March 2007	30 June 2007
David Evans	15 February 2007	–	**–**	80,645
Chris Potten	28 March 2007	1,020,000	**1,020,000**	919,320
Catherine Booth	28 March 2007	980,000	**980,000**	980,000
Gerard Brady	28 March 2007	–	**–**	–
Roger Lloyd	11 July 2007	–	**–**	–
Jeffrey Moore	15 February 2007	–	**–**	14,500
Robert Nolan	28 March 2007	–	**–**	8,065
John Rylands	15 February 2007	177,800	**177,800**	189,898
Matthew Walls	26 February 2007	–	**–**	5,645

Significant shareholdings

As of 30 September 2007, in addition to the Directors' holdings, the Company had been advised of the following interests of over 3% of the issued ordinary shares:

	Ordinary shares	Percentage holding
Managed by Calculus Capital Ltd	928,475	14.20%
Helium Special Situations Fund	385,600	6.04%
North West Business Investment Scheme	294,780	4.51%
Jonathan Moulton	235,925	3.61%
Rensburg Client Nominees Ltd	235,925	3.61%
Thomas Bloxham	204,870	3.13%

Policy on payments to suppliers
It is the policy of the Company in respect of all of its suppliers, where reasonably practicable, to settle the terms of payment with those suppliers when agreeing the terms of each transaction, to ensure that those suppliers are made aware of the terms of payment, and to abide by those terms. The Group has complied with this policy during the year. The average number of creditor days for the Group and the Company for the year ended 30 June 2007 was 66 days (2006: 38 days).

Statement of Directors' responsibilities
The Directors are responsible for preparing the Annual Report, the Directors' Remuneration Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

The Directors are responsible for preparing financial statements for each financial year which give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of affairs of the Company and the Group and of profit or loss of the Group for that period.

In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make suitable judgements and estimates that are reasonable and prudent;
- state whether the financial statements comply with IFRSs as adopted by the European Union;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors confirm that they have complied with the above requirements in preparing 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 the Group and to enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 1985 and Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Principal risks
We consider that the summary headed risk factors detailed in the AIM Admission document remains an appropriate assessment of the principal risks facing the business. In addition, the Group's policies regarding financial risks are disclosed in Note 19 to the financial statements.

Provision of information to auditors
So far as the Directors are aware, there is no relevant audit information of which the Company's auditors are unaware and the Directors have taken all the steps that ought to have been taken as Directors in order to make themselves aware of any audit information and to establish that the Company's auditors are aware of that information.

Auditors
HW, Chartered Accountants have expressed their willingness to continue as auditors. A resolution to reappoint HW, Chartered Accountants will be proposed at the Annual General Meeting.

Approved by the Board

H J J Rylands
Company Secretary
10 October 2007

Directors' Remuneration Report

For the year ended 30 June 2007

Introduction

This report has been prepared in accordance with the requirements of Schedule 7A to the Companies Act 1985 ("The Schedule") and also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the Principles of Good Governance relating to Directors' Remuneration. In accordance with Section 241A of the Companies Act 1985 ("The Act"), a resolution to approve the report will be proposed at the Annual General Meeting of the Company at which the Financial Statements are to be approved.

Section 235 of the Act requires the auditors to report to the Company's members on the "auditable part" of the Directors' Remuneration Report and to state whether, in their opinion, that part of the report has been properly prepared in accordance with Part 3 of the Schedule. This report has therefore been divided into separate sections for audited and unaudited information.

Unaudited information

Remuneration policy

Executive remuneration packages are prudently designed to attract, motivate and retain Directors of the necessary calibre and to reward them for enhancing value to shareholders. The performance measurement of the executive directors and key members of senior management and the determination of their annual remuneration package is undertaken by the Remuneration Committee. The remuneration of the non-executive directors is determined by the Board within limits set out in the Articles of Association.

Executive directors are entitled to accept appointments outside the Company providing the Board's permission is sought.

Non-executive directors' terms of engagement

The non-executive directors have specific terms of engagement. Their remuneration is determined by the Board and as set out in the Admission Document. In the event that a Non-executive undertakes additional assignments for the Company, the Non-executive's fee will be agreed by the Company in respect of each assignment.

Audited information

Aggregate directors' remuneration

The directors who served during the year and their remuneration was as follows:

	Fee/basic salary £	Payments related to listing £	Total £
David Evans	15,000	119,107	134,107
Chris Potten	69,972	–	69,972
Catherine Booth	75,000	–	75,000
Gerard Brady	75,000	–	75,000
Roger Lloyd*	–	–	–
Jeffrey Moore	80,000	10,000	90,000
Robert Nolan	15,000	–	15,000
John Rylands	52,500	10,000	62,500
Matthew Walls**	58,333	–	58,333
	440,805	**139,107**	**579,912**

* Appointed 1 July 2007
** Appointed 28 March 2007

Directors' share options

Details of the options for directors who served during the year are as follows:

		As at 1 July 2006	Options granted	As at 30 June 2007	Exercise price	Earliest exercise date	Expiry date
David Evans	(1)	62,112	–	**62,112**	£1.20	04/04/2007	09/01/2016
Chris Potten	(2)	15,528	–	**15,528**	£1.20	Exit	09/01/2016
Catherine Booth	(2)	15,528	–	**15,528**	£1.20	Exit	09/01/2016
Gerard Brady	(2)	88,800	–	**88,800**	£0.50	Exit	06/01/2012
Gerard Brady	(2)	3,200	–	**3,200**	£0.75	Exit	30/03/2013
Gerard Brady	(2)	2,200	–	**2,200**	£0.75	Exit	20/07/2014
Gerard Brady	(2)	1,800	–	**1,800**	£0.75	Exit	24/11/2015
Gerard Brady	(2)	24,224	–	**24,224**	£1.20	Exit	09/01/2016
Jeffrey Moore	(3)	83,000	–	**83,000**	£1.20	04/04/2007	09/01/2016
Jeffrey Moore	(1)	100,000	–	**100,000**	£1.20	04/04/2007	09/01/2016
Jeffrey Moore	(1)	83,000	–	**83,000**	£1.20	01/09/2007	09/01/2016
Jeffrey Moore	(1)	83,000	–	**83,000**	£1.20	01/09/2008	09/01/2016
Robert Nolan	(1)	78,000	–	**78,000**	£1.29	31/05/2005	30/03/2015
Robert Nolan	(1)	15,528	–	**15,528**	£1.20	10/01/2006	09/01/2016
John Rylands	(3)	83,000	–	**83,000**	£1.20	04/04/2007	09/01/2016
John Rylands	(1)	127,847	–	**127,847**	£1.20	04/04/2007	09/01/2016
Matthew Walls	(4)	–	258,297	**258,297**	£1.24	31/10/2010	27/03/2017

1. Unapproved stand-alone agreement, no performance criteria
2. EMI Company scheme, no performance criteria
3. EMI stand-alone scheme, no performance criteria
4. EMI and Unapproved stand-alone scheme, with performance criteria

Approved by the Board

D E Evans
Chairman
10 October 2007

Corporate Governance Report

For the year ended 30 June 2007

The Group is subject to the continuing requirements of the AIM Rules and is committed to adhering to corporate governance standards appropriate for a company of its size. The Group follows the Quoted Companies Alliance guidelines and has Remuneration, Audit and Nomination committees with written terms of reference and a schedule of matters reserved for the Board.

On 16 March 2007, the Board established an Audit Committee, a Remuneration Committee and a Nomination Committee. The membership of these committees presently comprises David Evans (Non-executive Chairman) and Robert Nolan (Non-executive Director).

Remuneration Committee

The Remuneration Committee will review the scale and structure of the Executive Directors' and senior management's remuneration and the terms of their service contracts. The remuneration and terms of appointment of the Non-executive Directors will be set by the Board. The Remuneration Committee will also approve the issue of share options under schemes approved by the Board.

None of the Committee have any personal financial interest (other than as shareholders), conflicts of interest arising from cross-directorships, or day-to-day involvement in the running of the business. No Director plays a part in any discussion about his or her own remuneration.

Audit Committee

The Audit Committee has responsibility for receiving accounts and reviewing reports from the management and the Company's auditors, relating to Annual and Interim Accounts and the accounting and internal controls in place throughout the Group. The Audit Committee meets at least three times each year.

Nomination Committee

The Nomination Committee has responsibility for reviewing the size, structure and composition of the Board, as well as retirements and appointments of replacement and additional Directors, and for making appropriate recommendations to the Board.

Relations with shareholders

The Group recognises the importance of communicating with its shareholders to ensure that its strategy and performance is understood and that it remains accountable to shareholders. The Board as a whole is responsible for ensuring that a satisfactory dialogue with shareholders takes place, while the Chairman and Chief Executive ensure that the views of the shareholders are communicated to the Board as a whole. The Board ensures that the Group's strategic plans have been carefully reviewed in terms of their ability to deliver long-term shareholder value.

Internal controls

The Board acknowledges its responsibility for establishing and maintaining the Group's system of internal controls and will continue to ensure that management keeps these processes under regular review and improves them where appropriate. The system of internal controls is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss.

Social, environmental and ethical matters

The Board recognises the growing awareness of social, environmental and ethical matters and it endeavours to take into account the interests of the Group's stakeholders, including its investors, employees, suppliers and business partners, when operating the business.

Employment

At a subsidiary level the individual company has established policies which address key corporate objectives in the management of employee relations, communications and employee involvement, training and personal development and equal opportunities.

Health, safety and environmental issues

The Board recognises its legal responsibilities to ensure the well-being, safety and welfare of its employees and to maintain a safe and healthy working environment for them and for its visitors and sub-contractors. Health and Safety is on the agenda for regularly scheduled Board meetings.

By their nature, the Group's regular operations are judged to have a low environmental impact and are not expected to give rise to any significant, inherent environmental risks over the next 12 months.

The Group is committed to maintaining high standards in implementing appropriate health, safety and environmental protection policies. The Group has an excellent health and safety record. Waste materials are recycled where possible, and hazardous waste is catalogued and handled by licenced, specialist disposal companies.

Independent Auditors' Report to the Members of Epistem Holdings Plc

For the year ended 30 June 2007

We have audited the Group and Parent Company Financial Statements (the "Financial Statements") of Epistem Holdings Plc for the year ended 30 June 2007 which comprise the Group Income Statement, the Group and Parent Company Balance Sheets, the Group and Parent Company Cash Flow Statements, the Group and Parent Company Statements of Changes in Equity and the related notes. These Financial Statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditor's Report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

The Directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the Financial Statements in accordance with United Kingdom law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the Financial Statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Financial Statements give a true and fair view and whether the Financial Statements and the part of the Directors' Remuneration report that is described as having been audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Financial Statements. The information given in the Directors' Report includes specific information that is presented elsewhere in the Annual Report that is cross referred from the Business Review section of the Directors' Report.

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

We read the other information contained in the Annual Report and consider whether it is consistent with the audited Financial Statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Financial Statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Financial Statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion:

- the Financial Statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's and the Parent Company's affairs as at 30 June 2007 and of the Group's loss and the Parent Company's profit for the year then ended;
- the Financial Statements and the Directors' Remuneration report that is described as having been audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the Financial Statements.

Bridge House
157 Ashley Road
Hale
Altrincham
Cheshire
WA14 2UT

HW
Chartered Accountants
& Registered Auditors

1. The maintenance and integrity of the Epistem Holdings Plc website is the responsibility of the Directors; the audit does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
2. Legislation in the United Kingdom governing the preparation and dissemination of the financial statements differs from legislation in other jurisdictions.

Consolidated Income Account

For the year ended 30 June 2007

	Notes	2007 £	2006 £
Revenue	2	**1,357,444**	901,161
Contract research costs		**(1,112,093)**	(711,466)
Discovery and development costs		**(1,034,053)**	(822,792)
General administrative costs		**(452,708)**	(409,491)
Operating loss	3	**(1,241,410)**	(1,042,588)
Interest receivable		**49,793**	49,853
Interest payable and similar charges	6	**(5,276)**	(5,643)
Loss on ordinary activities before taxation		**(1,196,893)**	(998,378)
Tax credit on loss on ordinary activities	7	**(160,358)**	(130,527)
Loss for the financial year	24	**(1,036,535)**	**(867,851)**
Earnings per share (pence)	10	**(22)p**	(22)p

All of the activities of the Group are classed as continuing.

The Company has taken advantage of section 230 of the Companies Act 1985 not to publish its own Income Account.

The accompanying notes form part of the consolidated financial statements.

Consolidated Statement of Changes in Equity

For the year ended 30 June 2007

	Share capital £	Share premium account £	Share options reserve £	Reverse acquisitions reserve £	Profit and loss account (restated) £	Total £
Balance at 1 July 2005	199	2,445,207	–	–	(811,681)	1,633,725
Prior year adjustment	–	–	156,432	–	(156,432)	–
Restated balance at 1 July 2005	199	2,445,207	156,432	–	(968,113)	1,633,725
Allotment of ordinary shares	3	119,996	–	–	–	119,999
Share issue costs	–	(33,235)	–	–	–	(33,235)
Loss for the year as originally reported	–	–	–	–	(625,471)	(625,471)
Recognition of equity settled share based payments in the year (prior year adjustment)	–	–	242,380	–	(242,380)	–
Restated balance at 30 June 2006	202	2,531,968	398,812	–	(1,835,964)	1,095,018
Restated balance at 1 July 2006	202	2,531,968	398,812	–	(1,835,964)	1,095,018
IFRS 3 reverse acquisition conversion	60,482	2,423,924	–	(2,484,406)	–	–
Allotment of ordinary shares	37,387	3,053,250	–	–	–	3,090,637
Share issue costs	–	(607,542)	–	–	–	(607,542)
Recognition of equity settled share based payments	–	–	55,120	–	–	55,120
Loss for the year	–	–	–	–	(1,036,535)	(1,036,535)
At 30 June 2007	**98,071**	**7,401,600**	**453,932**	**(2,484,406)**	**(2,872,499)**	**2,596,698**

The accompanying notes form part of the consolidated financial statements.

Consolidated Balance Sheet

As at 30 June 2007

	Notes	2007 £	2007 £	2006 £	2006 £
Non-current assets					
Intangible assets	12		**58,826**		62,690
Plant and equipment	13		**368,099**		292,307
			426,925		354,997
Current assets					
Trade and other receivables	14	**357,089**		323,363	
Tax receivables		**160,358**		130,527	
Cash and cash equivalents	15	**2,394,456**		680,960	
		2,911,903		1,134,850	
Liabilities					
Current liabilities					
Trade and other payables	16	**394,994**		214,038	
Obligations under finance leases	17	**81,317**		62,497	
Bank overdrafts and loans		**128,884**		5,089	
		605,195		281,624	
Net current assets			**2,306,708**		853,226
Total assets less current liabilities			**2,733,633**		1,208,223
Non-current liabilities					
Obligations under finance leases	17		**(136,935)**		(113,205)
Net assets			**2,596,698**		**1,095,018**
Capital and reserves					
Called-up equity share capital	23		**98,071**		202
Share premium account	24		**7,401,600**		2,531,968
Share options reserve	24		**453,932**		398,812
Reverse acquisition reserve	24		**(2,484,406)**		–
Profit and loss account	24		**(2,872,499)**		(1,835,964)
Total shareholders' equity			**2,596,698**		**1,095,018**

These financial statements were approved by the Directors and authorised for issue on 10 October and are signed on their behalf by:

D E Evans
Chairman

H J J Rylands
Company Secretary

The accompanying notes form part of the consolidated financial statements.

Consolidated Statement of Cash Flows

For the year ended 30 June 2007

	2007 £	2007 £	2006 £	2006 £
Cash flows from operating activities				
Loss for the year		**(1,241,410)**		(1,042,588)
Depreciation, amortisation and impairment		**109,264**		73,635
Share based payment expense		**55,120**		242,380
Operating profit before changes in working capital and provisions		**(1,077,026)**		(726,573)
(Increase)/decrease in trade and other receivables		**(33,726)**		6,872
Increase/(decrease) in trade and other payables		**180,956**		(155,068)
Net cash outflow from operations		**(929,796)**		(874,769)
Interest paid	**(5,276)**		(5,643)	
Interest received	**49,793**		49,853	
Tax received	**130,527**		8,011	
		175,044		52,221
Net cash outflow from operating activities		**(754,752)**		(822,548)
Cash flows from investing activities				
Acquisition of fixed assets, net of lease finance	**(63,192)**		(82,131)	
Net cash outflow from investing activities		**(63,192)**		(82,131)
Cash flows from financing activities				
Proceeds from issue of share capital	**3,090,637**		119,999	
Expenses of share issue	**(607,542)**		(33,235)	
Repayment of borrowings	**(75,450)**		(23,480)	
Net cash inflow from financing activities		**2,407,645**		63,284
Net increase/(decrease) in cash equivalents		**1,589,701**		(841,395)
Cash and cash equivalents at beginning of period		**675,871**		1,517,266
Cash and cash equivalents at end of period		**2,265,572**		**675,871**
Analysis of net funds				
Cash at bank and in hand		**2,394,456**		680,960
Bank overdrafts		**(128,884)**		(5,089)
Net funds		**2,265,572**		**675,871**

The accompanying notes form part of the consolidated financial statements.

Notes to the Financial Statements

For the year ended 30 June 2007

1. Accounting policies

Basis of accounting

The financial statements have been prepared under the historical cost convention, modified to include the revaluation of financial instruments and in accordance with applicable accounting standards.

Epistem Holdings Plc is a company incorporated in the UK.

The consolidated financial statements consolidate those of the Company and its subsidiary (together referred to as the "Group").

The consolidated financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs").

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

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Basis of consolidation

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Transactions between Group companies are eliminated on consolidation.

On 16 March 2007, Epistem Holdings Plc merged with Epistem Limited, and on that date the shareholders of Epistem Limited exchanged their shares for equivalent shares in Epistem Holdings Plc. As Epistem Holdings Plc was newly incorporated at the time of the transaction under the terms of IFRS 3 'Business Combinations', this transaction has been accounted for as a reverse acquisition, on the basis that the shareholders of Epistem Limited gained a controlling interest in the Group. The financial statements therefore represent a continuation of the financial statements of Epistem Limited.

Impact of IFRS 2 – share based payments

The Group has adopted IFRS 2 from 1 July 2006 whereby the value of share options based upon fair value at their grant date is calculated. As a result of the adoption of IFRS 2 the results for the year ended 30 June 2006 have been restated to reflect the fair value of share options and share warrants issued but not vested at 1 July 2005. The impact of the transition to IFRS 2 is set out in Note 18.

Turnover

The turnover shown in the consolidated income account represents the amount invoiced during the year, exclusive of Value Added Tax.

Revenue recognition

The Company generally invoices and reports as sales 50% of the value of a new contract on signature. This policy is designed to recognise that, in negotiating contracts for new studies, the Company performs specific pre-contract work to establish the parameters of the study work. When the final report is issued to the client the remainder of the contract is invoiced and recognised as income, at that date. In other cases where the contract does not provide for income recognition on signature, revenue is recognised as the work is invoiced.

Segment reporting

A segment is a group of assets, liabilities and operations engaged in providing products or services that are subject to risks and returns that are different from those of other parts of the business. The Group's primary format for segment reporting is based on business segments.

Research and development

Research and development expenditure is written off in the year in which it is incurred.

Intangible fixed assets – other

Other intangible fixed assets are stated at cost less accumulated amortisation and any accumulated impairment losses.

Amortisation
Amortisation 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:

Intellectual property	–	5% straight line basis

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:

Plant & machinery	–	25% reducing balance
Fixtures & fittings	–	25% reducing balance
Equipment	–	25% reducing balance

Finance lease agreements
Assets held under finance lease agreements are capitalised and disclosed under tangible fixed assets at their fair value. The capital element of the future payments is treated as a liability and the interest is charged to the consolidated income account on a straight line basis.

Operating lease agreements
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.

Foreign currencies
Transactions in foreign currencies are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date. Non-monetary items carried at fair value and denominated in foreign currencies are retranslated at the rates prevailing on the date when fair value is determined.

Exchange differences arising on the settlement of monetary items and on the retranslation of monetary items are taken to the income account. Exchange differences arising on non-monetary items, carried at fair value, are included in the income account, except for such non-monetary items in respect of which gains and losses are recorded in equity.

Share-based payments
The group issues equity-settled and cash-settled share-based payments to certain employees (including Directors). Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight line basis over the vesting period, together with a corresponding increase in equity, based upon the Group's estimate of the shares that will eventually vest.

Fair value is measured using the Black-Scholes pricing model. 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.

Where the terms of an equity-settled transaction are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled transaction is cancelled, it is treated as if it had vested on the date of the cancellation, and any expense not yet recognised for the transaction is recognised immediately. However, if a new transaction is substituted for the cancelled transaction, and designated as a replacement transaction on the date that it is granted, the cancelled and new transactions are treated as if they were a modification of the original transaction, as described in the previous paragraph.

Financial instruments
Financial instruments are classified and accounted for, according to the substance of the contractual arrangement, as either financial assets, financial liabilities or equity instruments. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Trade and other debtors
Trade and other debtors are recognised and carried forward at invoiced amounts less provisions for any doubtful debts. Bad debts are written off when identified.

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

1. Accounting policies (continued)

Cash and cash equivalents
Cash and cash equivalents are included in the balance sheet at cost. Cash and cash equivalents comprise cash at bank and in hand and short term deposits with an original maturity of three months or less.

Interest-bearing loans and borrowings
All loans and borrowings are recognised initially at cost, which is the fair value of the consideration received, net of issue costs associated with the borrowing.

After initial recognition, interest-bearing loans and borrowings are measured at amortised cost using the effective interest method. Gains or losses are recognised in the consolidated income account when liabilities are derecognised or impaired, as well as through the amortisation process.

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

Deferred tax is recognised in respect of all temporary differences identified at the balance sheet date, except to the extent that the deferred tax arises from the initial recognition of goodwill (if amortisation of goodwill is not deductible for tax purposes) or the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting profit nor taxable profit and loss. Temporary differences are differences between the carrying amount of the Group's assets and liabilities and their tax base.

Deferred tax liabilities may be offset against deferred tax assets within the same taxable entity. Any remaining deferred tax asset is recognised only when, on the basis of all available evidence, it can be regarded as probable that there will be suitable taxation profits, within the same jurisdiction, in the foreseeable future against which the deductible temporary difference can be utilised.

Deferred tax is provided on temporary differences arising in subsidiaries, jointly controlled entities and associates, except where the timing of reversal of the temporary difference will not reverse in the foreseeable future. Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the asset is realised or liability settled, based on tax rates and laws that have been enacted or substantially enacted by the balance sheet date. Measurement of deferred tax liabilities and assets reflects the tax consequence expected to fall from the manner in which the asset or liability is recovered or settled.

Standards, amendments and interpretations effective in 2007
The following standards, amendments and interpretations to published standards are mandatory for accounting periods beginning on or after 1 January 2006 but they are not relevant to the Group's operations:

IAS 21 (amendment), net investment in a foreign operation;
IAS 30 (amendment), cash flow hedger accounting of forecast intragroup transactions;
IAS 39 (amendment), the fair value option;
IAS 39 and IFRS 4 (amendment), financial guarantee contracts;
IFRS 6 (amendment), exploration for and evaluation of mineral resources;
IFRIC 4 determining whether an arrangement contains a lease;
IFRIC 5 rights to interests arising from decommissioning, restoration and environmental rehabilitation funds;
IFRIC 6 liabilities arising from participation in a specific market – waste electrical and electronic equipment;
IFRIC 7 applying the restatement approach under IAS 29 financial reporting in hyperinflationary economies;
IFRIC 9 re-assessment of embedded derivatives;
IFRIC 10 interim financial reporting and impairment.

The following standards and interpretations to published standards have been issued, but do not take effect until 2008 and 2009 financial years and are not expected to have a significant impact on the consolidated financial statements.

IFRS 8 operating segments;
IFRIC 11 group and treasury share transactions;
IFRIC 12 service concession arrangements;
IFRIC 13 customer loyalty programmes;
IFRIC 14 the limit on a defined benefit asset.

2. Turnover and segmental analysis

Segment information

The Group's primary reporting format is business segments and the secondary format is geographical segments.

Business segments

	Contract Research Services		Novel Therapies Division		Total	
	£	£	£	£	£	£
Revenue	1,357,444	901,161	–	–	**1,357,444**	901,161
Segment result	245,351	189,695	(1,034,053)	(822,792)	**(788,702)**	(633,097)
Unallocated expenses					**(452,708)**	(409,491)
Operating loss					**(1,241,410)**	**(1,042,588)**
Segment assets	433,585	484,235	249,806	156,060	**683,391**	640,295
Unallocated assets					**2,655,437**	849,552
Total assets					**3,338,828**	**1,489,847**
Segment liabilities	280,127	181,814	238,711	116,326	**518,838**	298,140
Unallocated liabilities					**223,292**	96,689
Total liabilities					**742,130**	**394,829**
Segment capital expenditure	13,148	99,216	155,312	162,423	**168,460**	261,639
Unallocated capital expenditure					**12,732**	16,532
Total capital expenditure					**181,192**	**278,171**
Segment depreciation	28,400	12,871	68,600	49,800	**97,000**	62,671
Unallocated depreciation					**8,400**	7,100
					105,400	**69,771**

Geographical segments

The Group's operations are located in the United Kingdom. The following table provides an analysis of the Group's sales by geographical market:

	2007 £	2006 £
United Kingdom	**553,220**	555,455
Europe	**258,677**	109,092
United States of America	**545,547**	172,988
Asia	**–**	63,626
	1,357,444	**901,161**

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

3. Operating loss

Operating loss is stated after charging:

	2007 £	2006 £
Research and development expenditure written off	**989,678**	719,975
Amortisation	**3,864**	3,864
Depreciation of owned fixed assets	**32,899**	30,965
Depreciation of assets held under finance lease agreements	**72,501**	38,806
Auditor's remuneration		
– as auditor	**10,000**	2,000
– for other services	**–**	3,575
Operating lease costs – property rent	**107,434**	**187,600**

4. Particulars of employees

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

	2007 No	2006 No
Contract research	**17**	12
Research and development	**8**	6
Administrative	**4**	4
	29	**22**

The aggregate payroll costs of the above were:

	2007 £	2006 £
Wages and salaries	**1,087,876**	735,649
Social security costs	**105,381**	80,805
Equity-settled share-based payments	**55,120**	242,380
	1,248,377	**1,058,834**

5. Directors' emoluments

	2007 £	2006 £
Salaries	**440,805**	344,677
Equity-settled share-based payments	**55,120**	233,562
	495,925	**578,239**

Full details of the Directors' remuneration and Directors' options are contained in the Directors' Remuneration Report. In addition to the above, bonuses totalling £139,107 have been written off to the share premium account as part of the cost of issuing shares on AIM.

6. Interest payable and similar charges

	2007 £	2006 £
Interest payable on bank borrowing	**356**	203
Finance charges	**4,920**	5,440
	5,276	**5,643**

7. Taxation on ordinary activities

(a) Recognised in the income statement

	2007 £	2006 £
Current tax:		
Research and development tax credits	**(160,358)**	(130,527)
Total current tax	**(160,358)**	**(130,527)**

(b) Reconciliation of total tax charges

	2007 £	2006 £
Loss before taxation	**(1,196,893)**	**(998,378)**
Tax using the UK corporation tax rate of 16% (2006: 16%)	**(191,503)**	(184,770)
Capital allowances claimed in excess of depreciation charges	**(2,642)**	(10,082)
Expenditure not allowed for tax purposes	**8,820**	41,130
Adjustments in respect of research and development tax credits	**(55,048)**	(27,193)
Tax loss for the year carried forward by rate of tax	**80,015**	50,388
Total tax in income statement	**(160,358)**	**(130,527)**

No liability to UK corporation tax arose during the year. The Group had losses, as computed for tax purposes, of approximately £1,072,000 available to carry forward to future periods.

In accordance with the provisions of the Finance Act 2000 in respect of research and development allowances, the Group is entitled to claim tax credits for certain research and development expenditure. The amount included in the financial statements in respect of the year ended 30 June 2007 is £160,358 (2006: £130,527).

8. Profit attributable to members of the parent company

The profit dealt with in the accounts of the parent company was £29,903 (2006: £Nil).

9. Prior year adjustment

The prior year adjustment relates to the notional value of the cost of share based payments in respect of share options granted in earlier years following the adoption of IFRS 2.

Notes to the Financial Statements (continued)

For the year ended 30 June 2007

10. Loss per share

The basic loss per share is calculated by dividing the earnings attributable to ordinary shareholders for the year by the weighted average number of ordinary shares in issue during the year.

For diluted loss per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. Since the Group is loss-making there is no dilutive impact.

	2007 £	2006 £
Loss for the year after taxation	**1,036,535**	**867,851**
Weighted average number of shares in issue	**4,635,934**	**4,028,883**
Loss per share (basic and diluted)	**22p**	**22p**

11. Investments

Company

The Company is the holding company of the Group. The Company owns 100% of the issued share capital of Epistem Limited, a company registered in England and Wales. The issued share capital is fully paid and is included in the consolidated financial statements of the Group.

	Investment in subsidiary £
Cost	
Additions	5,016,576
At 30 June 2007	**5,016,576**
Net book value	
At 30 June 2007	**5,016,576**

12. Intangible fixed assets

Group	Intellectual property £
Cost	
At 1 July 2006 and 30 June 2007	**77,175**
Amortisation	
At 1 July 2006	14,485
Charge for the year	3,864
At 30 June 2007	**18,349**
Net book value	
At 30 June 2006	62,690
At 30 June 2007	**58,826**
Cost	
At 1 July 2005 and 30 June 2006	**77,175**
Amortisation	
At 1 July 2005	10,621
Charge for the year	3,864
At 30 June 2006	**14,485**
Net book value	
At 30 June 2005	66,554
At 30 June 2006	**62,690**

13. Tangible fixed assets

	Lab equipment £	Fixtures & fittings £	Equipment £	Total £
Cost				
At 1 July 2006	454,278	8,509	44,577	507,364
Additions	168,460	7,009	5,723	181,192
At 30 June 2007	**622,738**	**15,518**	**50,300**	**688,556**
Depreciation				
At 1 July 2006	187,547	4,227	23,283	215,057
Charge for the year	97,000	2,400	6,000	105,400
At 30 June 2007	**284,547**	**6,627**	**29,283**	**320,457**
Net book value				
At 30 June 2006	266,731	4,282	21,294	292,307
At 30 June 2007	**338,191**	**8,891**	**21,017**	**368,099**

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

13. Tangible fixed assets (continued)

	Lab equipment £	Fixtures & fittings £	Equipment £	Total £
Cost				
At 1 July 2005	192,639	8,509	28,045	229,193
Additions	261,639	–	16,532	278,171
At 30 June 2006	**454,278**	**8,509**	**44,577**	**507,364**
Depreciation				
At 1 July 2005	124,876	2,727	17,683	145,286
Charge for the year	62,671	1,500	5,600	69,771
At 30 June 2006	**187,547**	**4,227**	**23,283**	**215,057**
Net book value				
At 30 June 2005	67,763	5,782	10,362	83,907
At 30 June 2006	**266,731**	**4,282**	**21,294**	**292,307**

Obligations under finance leases

Included within the net book value of £368,099 is £247,003 (2006: £201,503) relating to assets held under finance lease agreements. The depreciation charged to the financial statements in the year in respect of such assets amounted to £72,501 (2006: £38,806).

Capital commitments

	2007 £	2006 £
Contracted but not provided for in the financial statements	**–**	**118,000**

14. Trade and other receivables

Group	2007 £	2006 £
Trade debtors	**259,340**	205,638
Other debtors	**97,749**	105,673
Prepayments and accrued income	**–**	12,052
	357,089	**323,363**

Company	2007 £	2006 £
Amounts receivable from Group undertakings	**499,847**	–
	499,847	**–**

15. Cash and cash equivalents

Group	2007 £	2006 £
Cash at bank and in hand	**394,456**	40,728
Short term bank deposits	**2,000,000**	640,232
	2,394,456	**680,960**

Company	2007 £	2006 £
Cash at bank and in hand	**13,151**	–
Short term bank deposits	**2,000,000**	–
	2,013,151	**–**

Cash and cash equivalents comprise current accounts held by the Group with immediate access and short term bank deposits with a maturity of three months or less. Market rates of interest are earned on such deposits. The credit risk on such funds is limited because the counter parties are banks with high credit ratings assigned by international credit rating agencies.

16. Trade and other payables

	2007 £	2006 £
Trade creditors	**236,637**	133,732
Other creditors	**49,926**	32,057
Accruals and deferred income	**108,431**	48,249
	394,994	**214,038**

17. Obligations under finance leases

Future commitments under finance lease agreements are as follows:

	2007 £	2006 £
Amounts payable within 1 year	**99,617**	71,297
Amounts payable between 2 to 5 years	**147,362**	127,817
	246,979	199,114
Less: interest and finance charges relating to future periods	**28,727**	23,412
	218,252	**175,702**
Hire purchase agreements are analysed as follows:		
Current obligations	**81,317**	62,497
Non-current obligations	**136,935**	113,205
	218,252	**175,702**

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

18. Share-based payments

The Company operates a number of approved and unapproved share option schemes for employees (including Directors). The original options were granted by Epistem Limited but, following the acquisition by Epistem Holdings Plc, these were released in exchange for equivalent options over the ordinary shares of Epistem Holdings Plc.

Share Options

Award	Number of awards	Exercise price	Period within which options are exercisable	Fair value per option	Fair value £
EMI – Approved	88,800	£0.50	7 Jan 2002 to 6 Jan 2012	See note below	
EMI – Approved	13,600	£0.75	31 Mar 2003 to 30 Mar 2013	28.2p	3,835
EMI – Approved	10,600	£0.75	7 Apr 2003 to 6 Apr 2013	28.2p	2,989
EMI – Approved	12,200	£0.75	21 Jul 2004 to 20 Jul 2014	26.6p	3,196
Share Warrants	198,554	£1.61	18 Mar 2005 to 17 Mar 2015	56.1p	111,389
EMI – Unapproved	78,000	£1.29	31 Mar 2005 to 30 Mar 2015	44.9p	35,022
EMI – Approved	33,824	£1.20	25 Nov 2005 to 24 Nov 2015	42.6p	14,409
EMI – Unapproved	472,153	£1.20	10 Jan 2006 to 9 Jan 2016	42.6p	201,137
EMI – Approved	197,722	£1.20	10 Jan 2006 to 9 Jan 2016	42.6p	84,230
EMI – Approved	11,100	£1.20	29 Sept 2006 to 28 Sept 2016	41.6p	4,729
EMI – Unapproved	258,297	£1.24	28 Mar 2007 to 27 Mar 2017	42.6p	107,452

Option valuations

The options were valued using the Black-Scholes option-pricing model. Where appropriate, performance conditions were included in the fair value calculations. The fair value per option granted and the assumptions used in the calculations are in the table below. The Group's effective date for IFRS 2, 'Share Based Payments' implementation is 1 July 2006 and the IFRS has been applied to all options granted after 7 November 2002 which have not been vested by this effective date.

Award	Grant date	Expected term	Expected dividend yield %	Expected volatility %	Risk % rate	Performance condition
EMI – Approved	31 Mar 2003	5 years	0	60	3.75	None
EMI – Approved	7 Apr 2003	5 years	0	60	3.75	None
EMI – Approved	21 Jul 2004	5 years	0	60	4.50	None
Share Warrants	18 Mar 2005	5 years	0	60	4.75	None
EMI – Unapproved	31 Mar 2005	5 years	0	60	4.75	None
EMI – Approved	25 Nov 2005	5 years	0	60	4.50	None
EMI – Unapproved	10 Jan 2006	5 years	0	60	4.50	See Note (e)
EMI – Approved	10 Jan 2006	5 years	0	60	4.50	None
EMI – Approved	29 Sept 2006	5 years	0	60	4.50	None
EMI – Unapproved	28 Mar 2007	5 years	0	60	5.25	See Note (f)

a) The expected life used in the model is five years and is based upon the Directors' best estimates for the effects of exercise restrictions and behavioural considerations;

b) The dividend yield of 0% reflects the absence of a history of paying dividends and a clear dividend policy at the relevant grant dates;

c) The Group's shares were not on any market on the dates covered by the options granted and for this reason the expected volatility has been estimated by the Directors after inspection of the financial statements of comparable businesses in the same business sector as the Group;

d) The risk free rate used is based upon the prevailing UK bank base rate at the date of the grant;

e) These options vest on dates dependant on anniversaries of commencing employment with the Group which commenced 1 September 2005 with the final tranche vesting on 1 September 2008;

f) The main conditions for these options to vest are the later of (i) when the audited accounts for the year ended 30 June 2010 become available and (ii) the earnings per share of the financial year are a positive figure.

The number of options and their weighted average exercise prices are as follows:

	Number	Weighted average exercise price	Weighted average remaining contractual life years
EMI approved schemes			
Number of options outstanding at 1 July 2005	128,000	£0.56	
Granted in the year ended 30 June 2006	231,546	£1.20	
Lapsed in the year ended 30 June 2006	(2,800)	£0.75	
Outstanding at 30 June 2006	356,746	£0.98	8.29
Granted in the year ended 30 June 2007	11,100	£1.20	
Outstanding at 30 June 2007	**367,846**	**£0.99**	**7.34**
EMI unapproved schemes			
Number of options outstanding at 1 July 2005	78,000	£1.29	
Granted in the year ended 30 June 2006	472,153	£1.20	
Outstanding at 30 June 2006	550,153	£1.21	9.42
Granted in the year ended 30 June 2007	258,297	£1.24	
Outstanding at 30 June 2007	**808,450**	**£1.22**	**8.85**
Share warrants			
Number outstanding at 1 July 2005 and 30 June 2006	198,554	£1.61	8.72
Number outstanding at 30 June 2007	**198,554**	**£1.61**	**7.72**

The result of adopting IFRS 2, share-based payments, has been a charge to the profit and loss account of £55,120 in respect of share options granted in the period. A prior year adjustment has been made to the result for the year ended 30 June 2006 increasing the costs for the year by £242,380 and an equal credit to the share options reserve in the balance sheet with no impact on net assets at 1 July 2006. A similar adjustment has also been made for the year ended 30 June 2005 amounting to £156,432.

19. Financial risk management objectives and policies

The Group holds or issues financial instruments in order to achieve three main objectives, being:

(a) to finance its operations;

(b) to manage its exposure to interest and currency risks arising from its operations and from its sources of finance; and

(c) for trading purposes.

In addition, various financial instruments (e.g. trade debtors, trade creditors, accruals and prepayments) arise directly from the Group's operations.

In addition, various financial instruments (e.g. trade debtors, trade creditors, accruals and prepayments) arise directly from the Company's operations.

Transactions in financial instruments result in the Company assuming or transferring to another party one or more of the financial risks described below.

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

19. Financial risk management objectives and policies (continued)

Interest rate risk
The Group currently finances its operations through reserves of cash and liquid resources and does not have a borrowing requirement. Surplus cash at bank is placed on deposits at variable rates. The Board monitors the financial markets and the Group's own requirements to ensure that the policies are exercised in the Group's best interests.

Credit risk
The Group monitors credit risk closely and considers that its current policies of credit checks meets its objectives of managing exposure to credit risk.

The Group has no significant concentrations of credit risk. Amounts shown in the balance sheet best represent the maximum credit risk exposure in the event other parties fail to perform their obligations under financial instruments.

Liquidity risk
The Board's policy is to ensure that sufficient funds are held on a short term basis in order to meet operational needs without the use of an overdraft facility.

Currency risk
The Group's functional currency is sterling. The exposure to currency risk is very limited because almost all customers are invoiced in sterling and settle the debt in sterling. There are no costs incurred that involve payments in foreign currency.

Fair values of financial assets and liabilities
There is no material difference between the book value and the fair value of the Group's financial assets or liabilities.

20. Commitments under operating leases

At 30 June 2007 the Group had annual commitments under non-cancellable operating leases as set out below.

	Land and buildings 2007 £	Land and buildings 2006 £
Operating leases which expire:		
Within 1 year	**53,697**	**50,127**

21. Related party transactions

During the period the Company purchased consultancy services to Directors as follows – Prof. C. Potten – £69,972, D Evans – £134,107 and Dr. R Nolan – £11,400. These were on a normal trading basis and are included within Non-executive Directors' fees.

At the balance sheet date the amounts owed to D Evans and R Nolan were £14,896 and £9,686 respectively.

No other transactions with related parties were undertaken such as are required to be disclosed under Financial Reporting Standard 8.

22. Deferred taxation (unrecognised)

	2007 £	2006 £
Tax effect of timing differences:		
Losses	**214,513**	108,770
Excess of tax allowances over depreciation	**(19,898)**	(15,032)
Potential deferred tax asset	**194,615**	**93,738**

There was no potential liability to deferred tax at 30 June 2007 nor 30 June 2006.

In view of the uncertainty of the recoverability of the Group's tax losses carried forward, no deferred tax asset in respect of the available tax losses is recognised. Note 7 gives details of the tax losses available to carry forward by the Group.

23. Share capital

Authorised share capital:

	2007 £	2006 £
10,000,000 ordinary shares of £0.015 each	**150,000**	–
20,000,000 ordinary shares of £0.0005 each	**–**	1,000

Allotted and called up:

	2007 No	2007 £	2006 No	2006 £
At 1 July	**4,045,628**	**202**	3,971,094	199
Allotted as consideration for Epistem Limited	**–**	**60,684**	–	–
IFRS 3 reverse acquisition conversion	**–**	**(202)**	–	–
Placing on AIM	**2,492,447**	**37,387**	–	–
Private placing	**–**	**–**	74,534	3
Ordinary shares of £0.015 each	**6,538,075**	**98,071**	**4,045,628**	**202**

At an Extraordinary General Meeting of Epistem Holdings Plc held on 28 March 2007 a special resolution was passed to increase the authorised share capital from £77,433 to £150,000.

During the period the Company issued 4,045,626 ordinary £0.015 shares for the acquisition of the entire issued share capital of Epistem Limited. These shares were issued as fully paid at a value of £1.24 each, giving rise to a consideration of £5,016,576. In addition, the Company issued a further 2,492,447 ordinary £0.015 shares at the placing price of £1.24 each, giving a total consideration of £3,090,637.

On 16 March 2007 the Company entered into a warrant instrument in respect of the subscription for up to 198,554 ordinary shares of £0.015 each in Epistem Holdings Plc. This warrant instrument replaced a previous warrant instrument created by Epistem Limited on 18 March 2005. Each warrant confers the right to subscribe for one ordinary share at a subscription price of £1.61 per ordinary share. The subscription rights under the warrants may be exercised up to 21 September 2015.

Notes to the Financial Statements (continued)
For the year ended 30 June 2007

24. Reserves

	Share premium account £	Share options reserve £	Reverse acquisition reserve £	Profit and loss account (restated) £
Balance at 1 July 2005	2,445,207	–	–	(811,681)
Prior year adjustment (Note 9)	–	156,432	–	(156,432)
Restated balance as at 1 July 2005	2,445,207	156,432	–	(968,113)
Loss for the year as originally reported	–	–	–	(625,471)
Premium on issue of shares	119,996	–	–	–
Share issue costs	(33,235)	–	–	–
Transfers	–	–	–	–
Recognition of equity-settled share-based payments in the year (prior year adjustment)	–	242,380	–	(242,380)
Balance at 30 June 2006	**2,531,968**	**398,812**	**–**	**(1,835,964)**
Restated balance as at 1 July 2006	2,531,968	398,812	–	(1,835,964)
Loss for the year	–	–	–	(1,036,535)
Premium on issue of shares	3,053,250	–	–	–
Share issue costs	(607,542)	–	–	–
IFRS 3 reverse acquisition conversion	2,423,924	–	(2,484,406)	–
Recognition of equity-settled share-based payments in the year	–	55,120	–	–
Balance at 30 June 2007	**7,401,600**	**453,932**	**(2,484,406)**	**(2,872,499)**

The reverse acquisition reserve arises as a difference on consolidation under merger accounting principles and is solely in respect of the merger of the Company and Epistem Limited.

Company Balance Sheet
As at 30 June 2007

	Notes	2007 £	£
Non-current assets			
Investments	11		5,016,576
Current assets			
Trade and other receivables	14	**499,847**	
Cash and cash equivalents	15	**2,013,151**	
			2,532,998
Total assets			**7,529,574**
Capital and reserves			
Called-up equity share capital	23		98,071
Share premium account	24		7,401,600
Profit and loss account	8		29,903
Total shareholders' funds equity			**7,529,574**

These financial statements were approved by the Directors and authorised for issue on 10 October 2007 and are signed on their behalf by:

D E Evans
Chairman

H J J Rylands
Company Secretary

Company Statement of Changes in Equity
For the year ended 30 June 2007

	Share capital £	Share premium account £	Profit and loss account £	Total £
Issue of share capital	98,071	7,401,600	–	7,499,671
Profit for the year	–	–	29,903	29,903
At 30 June 2007	**98,071**	**7,401,600**	**29,903**	**7,529,574**

Company Statement of Cash Flows

For the year ended 30 June 2007

	2007 £	2007 £
Cash flows from operating activities		
Profit for the year		–
Operating profit before changes in working capital and provisions		–
Increase in trade and other receivables		(499,847)
Cash outflow from operations		(499,847)
Interest received	29,903	
Tax (paid)/received	–	
		29,903
Net cash outflow from operating activities		**(469,944)**
Cash flows from financing activities		
Proceeds from issue of share capital	3,090,637	
Expenses of share issue	(607,542)	
Net cash inflow from financing activities		2,483,095
Net increase in cash equivalents		2,013,151
Cash and cash equivalents at beginning of period		–
Cash and cash equivalents at end of period		**2,013,151**
Analysis of net funds		
Cash at bank and in hand		2,013,151
Bank overdrafts		–
Net funds		**2,013,151**

Notes

Notes

Directors, Secretary and Advisers

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David Evans
Matthew Walls
Chris Potten
Cath Booth
Gerard Brady
Roger Lloyd
Jeffrey Moore
Robert Nolan
John Rylands

Company Secretary
John Rylands

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