Phytopharm plc

Annual Report

for the year ended 31 August 1996

Registered no: 3131723

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COMPANIES HOUSE 06/03/97

Annual report
for the year ended 31 August 1996

Directors' report for the year ended 31 August 1996

The directors present their report and the audited financial statements for the year ended 31 August 1996.

Principal activities

The principal activities of the group are unchanged from last year, and are the investigation and development of medicines derived from plant origins.

Review of the business

The consolidated profit and loss account for the year is set out on page 13.

The directors remain satisfied with the progress of the group and are particularly pleased to report the successful flotation of the company on the London Stock Exchange in April and the submission of the product licence application to the Medicines Control Agency in July for Zemaphyte™, the group's treatment for severe eczema.

On 21 March 1996 Phytotech Limited (formerly Phytopharm Limited) acquired the entire share capital of Phytodevelopments Limited by way of share exchange. The assets and liabilities of Phytodevelopments Limited were transferred to Phytotech Limited (formerly Phytopharm Limited) at book value.

On 3 April 1996 the group structure was reorganised and a new holding company, Phytopharm plc, was established. Holders of shares in Phytotech Limited (formerly Phytopharm Limited) exchanged their shares in Phytotech Limited for fully paid up shares in Phytopharm plc in the ratio 1 for 12.

On 19 April 1996 the company published its prospectus for a full listing on the London Stock Exchange. The company issued 7,428,571 shares (representing 24% of its issued share capital) at £1.75 per share, raising £11,842,470 net of expenses. Trading in the shares commenced on 25 April 1996.

Dividends

The directors do not recommend a dividend for the year ended 31 August 1996. The loss for the year will be transferred to the group's reserves.

Group research and development activities

The group is heavily committed to research and development activities in order to continue its work in the field of plant based prescription medicines. Such development costs are written off as they are incurred.

Directors

All of the directors of the company were appointed during the year on the following dates:

	Date of appointment	Date of resignation
Dr R P Dixey	5 February 1996	
Dr S C Loach	5 February 1996	
Dr I D Rubin	26 February 1996	
Dr B A Whittle	26 February 1996	
Dr G W Guy	26 February 1996	
Mr K Hebben	26 February 1996	1 April 1996
Mr B Ingham	26 February 1996	1 April 1996
Dr P M Whitney	1 April 1996	
Dr T H Flanagan	1 April 1996	

Biographical details of the non-executive directors are shown below:

Dr G W Guy
Non Executive Chairman Dr. Geoffrey Guy (aged 41) gained a BSc in pharmacology from the University of London in 1976, an MB BS at St. Bartholomew's Hospital in 1979, an MRCS Eng. and LRCP London in 1979, an LMSSA Society of Apothecaries in 1979 and a Diploma of Pharmaceutical Medicine from the Royal Colleges of Physicians in 1984. He has been non-executive chairman of Phytopharm since he co-founded it in 1990 and is the chairman and chief executive of Ethical Holdings plc, a company listed on NASDAQ which he founded in 1985. He served as director of clinical developments at Napp Laboratories from 1983 to 1985 and as international clinical research co-ordinator at Laboratories Pierre Fabre from 1981 to 1983.

Dr P M Whitney
Non-Executive Deputy Chairman Dr. Paul Whitney (aged 48) has a BSc (Hons) in chemistry (Aston, 1969), a PhD in physical chemistry (Aston, 1972) and an MBA (Cranfield, 1980). From 1993 to 1996 he was chief executive of NatWest Investment Management Limited and Managing Director of NatWest Asset Managers Limited. Prior to that he was chief executive of CIN Management Limited. He is currently chief executive of Sunlife Asset Management Limited. He was appointed as non-executive deputy chairman of the Company on 1 April 1996.

Dr T H Flanagan
Non-Executive Director Dr. Trevor Flanagan (aged 58) has a BSc (Hons) in biochemistry (Cardiff, 1960) and a PhD in biochemistry (Cardiff, 1963). From 1963 to 1978 he worked at ICI Pharmaceuticals Limited in research project management and as a licensing manager. From 1978 to 1986 he worked for Synthelabo and was responsible for international project management and global regulatory affairs. In 1986 he joined Wellcome Foundation where he was strategic business manager for all therapeutic areas except anti-infectives. In 1995 he established his own Pharmaceutical Consultancy. He was appointed a non-executive director of the Company on 1 April 1996.

There were no contracts of significance with the company or any of its subsidiaries subsisting during or at the end of the financial year in which a director of the company was materially interested.

The interests of directors in the shares of the company and other group companies at 31 August 1996 are disclosed in the report of the remuneration committee on pages 4 to 7.

Substantial shareholdings

The directors have been advised of the following substantial holdings in the company's issued share capital as at 28 November 1996:

Name of shareholder	% holding
Ethiphyte Ltd	28.5
Chakra Ltd	25.7
Brian Whittle Associates Ltd	7.8
CAL International Ltd	5.6
Prudential Corporation Group	4.4
James W Lewis	3.9
Robert Fleming Holdings Ltd	3.6

Creditor payment policy

The group's current policy concerning the payment of the majority of its trade creditors is to follow the CBI's Prompt Payers Code (copies are available from the CBI, Centre Point, 103 New Oxford Street, London WC1A 1DU). For other suppliers, the group's policy is to:

a) settle the terms of payment with those suppliers when agreeing the terms of each transaction;

b) ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and

c) pay in accordance with its contractual and other legal obligations.

The payment policy applies to all payments to creditors for revenue and capital supplies of goods and services without exception.

Auditors

A resolution to reappoint the auditors, Coopers & Lybrand, will be proposed at the annual general meeting.

By order of the board

S. Loach

Dr S C Loach
Secretary

Report of the remuneration committee

The remuneration committee is comprised exclusively of non-executive directors. They are as follows:

Dr P M Whitney (chairman)
Dr T H Flanagan

The company has complied since its incorporation with section A of the best practice provisions for directors' remuneration annexed to the London Stock Exchange's Listing Rules, which concerns the membership and operation of the remuneration committee.

The company's remuneration committee decides the remuneration policy that applies to executive directors and the group's other senior management. In determining that policy it has given full consideration to section B of the best practice provisions for directors' remuneration annexed to the London Stock Exchange's Listing Rules. In setting the policy it considers a number of factors including:

a) The basic salaries and benefits available to executive directors of comparable companies;

b) The need to attract and retain directors of an appropriate calibre;

c) The need to ensure executive directors' commitment to the continued success of the company by means of incentive schemes.

Remuneration of non-executive directors

The non-executive directors each receive a fee for their services, which is agreed by the board following recommendation by the chairman with the assistance of independent advice concerning comparable organisations and appointments.

The company pays Ethical Holdings plc a fee equal to that of the other non-executive directors for the services of Dr G W Guy, the non executive chairman.

Neither the chairman nor the other non-executive directors receive any pension or other benefits from the company. Apart from Dr G W Guy, who has been granted 300,000 share options, the non executive directors do not participate in any of the bonus or incentive schemes or share option schemes. Dr G W Guy was granted the share options in recognition of his services as non-executive chairman of Phytotech Limited (formerly Phytopharm Limited) from its incorporation.

The chairman and the other non-executive directors have service agreements with the company. They can only be removed from office by the shareholders at general meetings.

Remuneration policy for executive directors

The company's remuneration policy for executive directors is to:

a) Have regard to the directors' experience and the nature and complexity of their work and due regard to directors' remuneration in comparable companies in order to pay a competitive salary that attracts and retains management of the highest quality;

b) Link individual remuneration packages to the group's long-term performance through the award of share options and incentive schemes;

c) Provide post retirement benefits through the group's pension schemes;

d) Provide employment related benefits including the provision of a company car, life assurance, insurance relating to the director's duties and medical insurance.

Salaries and benefits

The remuneration committee meets at least twice a year in order to consider and set the annual salaries for executive directors, having regard to personal performance and independently compiled salary survey information.

Pensions

All the executive directors have money purchase pension schemes to which the company contributes 8% of basic salary.

Contracts of service

All of the executive directors have contracts of service which can be terminated by the company with a notice period of one year in the case of Dr R P Dixey and Dr I D Rubin and six months in the case of Dr B A Whittle and Dr S C Loach, such notice to expire not before two years from 1 April 1996. The notice period was set at two years from the date of the flotation to ensure that there was continuity of management in the period following the flotation. In addition, one third of the directors are required under the Articles of Association to resign and offer themselves for re-election at each annual general meeting.

Directors' detailed emoluments

Details of individual directors' emoluments for the year are as follows:

	1996				1995		1996
	Salary & Fees	**Benefits**	**Pension contributions**	**Total**	Total	Pension contributions	**Current annual salary & fees**
Executive	**£**	**£**	**£**	**£**	£	£	**£**
Dr R P Dixey	**95,833**	**5,692**	**4,025**	**105,550**	40,681	2,348	**115,000**
Dr I D Rubin	**47,865**	**4,835**	**3,821**	**56,521**	-	-	**95,000**
Dr S C Loach	**33,320**	**3,820**	**2,657**	**39,797**	-	-	**65,000**
Dr B A Whittle	**86,539**	**3,039**	**3,821**	**93,399**	68,810	-	**115,000**
	263,557	**17,386**	**14,324**	**295,267**	109,491	2,348	**390,000**
Non-executive							
Dr G W Guy	-	-	-	-	-	-	-
Dr P M Whitney	**6,250**	-	-	**6,250**	-	-	**15,000**
Dr T H Flanagan	**7,450**	-	-	**7,450**	-	-	**15,000**
	13,700	-	-	**13,700**	-	-	**30,000**
Total	**277,257**	**17,386**	**14,324**	**308,967**	109,491	2,348	**420,000**

The company paid Ethical Holdings plc, of which Dr G W Guy is chief executive, a fee of £6,250 (1995: £nil) for Dr Guy's services as non executive chairman.

Included in the above is £38,622 (1995; £68,810) paid to Brian Whittle Associates Limited, a company controlled by Dr Whittle, in respect of services provided by Dr Whittle prior to the company's flotation.

Dr Flanagan's fees of £7,450 includes a consultancy fee of £1,200 in addition to his director's fees of £6,750.

No director waived emoluments in respect of the year ended 31 August 1996 (1995: £nil).

Directors' interests in shares

The interests of the directors in the shares of the company at 31 August 1996 were:

	Ordinary shares of 1 pence	
	31 August 1996	31 August 1995
R P Dixey	**7,932,000**	-
I D Rubin	-	-
B A Whittle	**2,400,000**	-
S C Loach	-	-
G W Guy	-	-
P M Whitney	-	-
T H Flanagan	-	-

Dr R P Dixey's interest arises as he is the beneficial owner of 50% of the issued share capital of Chakra Limited, which owns 7,932,000 shares in Phytopharm plc.

Dr B A Whittle's interest arises as he is the beneficial owner of the entire share capital of Brian Whittle Associates Limited, which owns 2,400,000 shares in Phytopharm plc.

Apart from the interests disclosed above no directors were interested at any time in the year in the share capital of the company or other group companies.

There has been no change in the interests set out above between 31 August 1996 and 28 November 1996.

Interests in share options

Details of options held by directors are set out below:

	Number of options				Date from	
	Granted in the year	At 31 August 1996	Note*	Exercise price	which exercisable	Expiry Date
G W Guy	300,000	300,000	1	26.25p	17 April 1999	16 April 2003
R P Dixey	540,000	540,000	1	26.25p	17 April 1999	16 April 2003
	58,700	58,700	2b	£1.925	24 April 1999	23 April 2003
	52,800	52,800	3b	£1.925	24 April 1999	23 April 2003
	126,600	126,600	4	£1.925	24 April 1999	23 April 2003
	778,100	778,100				
I D Rubin	204,000	204,000	1	26.25p	17 April 1999	16 April 2003
	17,000	17,000	2a	£1.925	24 April 1999	23 April 2006
	29,900	29,900	2b	£1.925	24 April 1999	23 April 2003
	42,200	42,200	3b	£1.925	24 April 1999	23 April 2003
	117,300	117,300	4	£1.925	24 April 1999	23 April 2003
	410,400	410,400				
S C Loach	180,000	180,000	1	26.25p	17 April 1999	16 April 2003
	17,000	17,000	2a	£1.925	24 April 1999	23 April 2006
	18,200	18,200	2b	£1.925	24 April 1999	23 April 2003
	39,900	39,900	3b	£1.925	24 April 1999	23 April 2003
	107,900	107,900	4	£1.925	24 April 1999	23 April 2003
	363,000	363,000				
B A Whittle	180,000	180,000	1	26.25p	17 April 1999	16 April 2003
	46,900	46,900	2b	£1.925	24 April 1999	23 April 2003
	52,600	52,600	3b	£1.925	24 April 1999	23 April 2003
	279,500	279,500				
Total	**2,131,000**	**2,131,000**				

There were no options outstanding at the beginning of the year and no options were exercised during the year.

* Further details of the terms of the share option schemes are contained in note 20 to the Financial Statements under the note reference in the above table.

The market price of the company's shares at the end of the financial year was 190.5 pence and the range of market prices during the year was between 175 pence and 295 pence.

Corporate governance

The board supports the highest standards in corporate governance and is pleased to confirm that the company has complied from the commencement of trading with the Code of Best Practice published by the Committee on the Financial Aspects of Corporate Governance (the 'Cadbury Committee'). Prior to that the group was comprised of small private companies .

Board composition

The group board comprises four executive and three non-executive directors. It is chaired by Dr G W Guy and meets for regular business six times a year. In addition, further meetings are held as circumstances require. The board is responsible for the overall direction and strategy of the group and for securing the optimum performance from group assets. Our non-executive directors have a breadth of successful commercial and professional experience.

Board committees

The audit committee comprises Dr P M Whitney and Dr T H Flanagan and is chaired by Dr P M Whitney. It meets at least twice a year and assists the board in ensuring that the Group's published financial statements give a true and fair view and in securing reliable internal financial information for decision making. It also reviews the suitability and effectiveness of the group's internal controls. The committee reviews the findings of the external auditors and reviews key accounting policies and judgements.

The remuneration committee comprises Dr P M Whitney and Dr T H Flanagan and is chaired by Dr P M Whitney. It meets at least twice a year and is responsible for making recommendations to the board on remuneration policy for senior executives and all directors and for setting salaries, incentive payments and share options granted.

Going concern

After making appropriate enquiries, the directors have a reasonable expectation that the group and the company have 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 group's financial statements.

Internal financial controls

Your board of directors is responsible for the group's system of internal financial controls. It should be recognised that such a system can provide only reasonable and not absolute assurance against material misstatement or loss. The key features of the system which have been established are as follows:

Control environment

The group's control environment is the responsibility of the group's directors and managers at all levels. The group's organisational structure has clear lines of responsibility, and senior management meet monthly to review progress against plan.

Identification of business risks

A specific exercise has been undertaken to review and assess the risks facing the group's business and to enhance the systems which manage the key risks identified.

Major corporate information systems

The group operates a comprehensive budgeting and financial reporting system which, as a matter of routine, compares actual out-turn to budget. Management accounts are compiled on a monthly basis. Variances from plan are thoroughly investigated and revisions to forecasts are made as appropriate. Cash flow statements are prepared quarterly following project reviews and cover a period of three years to ensure that the group has adequate funds and resources for the foreseeable future.

Main control procedures

Standard financial control procedures operate throughout the group to ensure the integrity of the group's financial statements. The board has established procedures for authorisation of all expenditure, including capital expenditure and the appointment of staff, whether on a temporary or permanent basis.

Monitoring system used by the board

The board reviews and approves budgets and monitors the group's performance against those budgets. Variances from the expected outcome are investigated fully. The group's cash flow is also monitored and compared to forecast. The board has reviewed the effectiveness of the system of internal financial control for the period.

The audit committee also reviews the findings of external auditors.

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and the group and of the profit or loss of the company and 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 judgements and estimates that are reasonable and prudent;

- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and

- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

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

By order of the board

S. Loach

Dr S C Loach
Secretary

Report of the auditors to the members of Phytopharm plc

We have audited the financial statements on pages 13 to 27.

Respective responsibilities of directors and auditors

As described on page 10 the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the company and the group at 31 August 1996 and of the loss, total recognised losses and cash flows of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Coopers & Lybrand

Coopers & Lybrand
Chartered Accountants and Registered Auditors
Cambridge

28 November 1996

Report of the auditors to Phytopharm plc on corporate governance matters

In addition to our audit of the financial statements we have reviewed the directors' statement on pages 8 and 9 on the company's compliance with the paragraphs of the Code of Best Practice specified for our review by the London Stock Exchange. The objective of our review is to draw attention to non-compliance with those paragraphs of the Code which is not disclosed.

Basis of opinion

We carried out our review in accordance with bulletin 1995/1 'Disclosures relating to corporate governance' issued by the Auditing Practices Board. That Bulletin does not require us to perform the additional work necessary to, and we do not, express any opinion on the effectiveness of either the group's system of internal financial control or its corporate governance procedures, nor on the ability of the group or company to continue in operational existence.

Opinion

With respect to the directors' statements on internal financial control on pages 8 and 9 and going concern on page 8, in our opinion the directors have provided the disclosures required by paragraphs 4.5 and 4.6 of the Code (as supplemented by the related guidance for directors) and such statements are consistent with the information of which we are aware from our audit work on the financial statements.

Based on enquiry of certain directors and officers of the company and examination of relevant documents, in our opinion the directors' statement on page 8 appropriately reflects the company's compliance with the other paragraphs of the Code specified for our review.

Coopers & Lybrand
Chartered Accountants
Cambridge

Consolidated profit and loss account for the year ended 31 August 1996

	Notes	1996 £	1995 £
Turnover	2	**933,886**	1,114,106
Cost of sales	3	**84,410**	60,118
Gross profit		**849,476**	1,053,988
Other operating expenses	3	**1,534,516**	700,682
Operating (loss)/profit		**(685,040)**	353,306
Interest receivable and similar income		**219,432**	311
Interest payable and similar charges	6	**(99,301)**	(164,429)
(Loss)/profit on ordinary activities before and after taxation	7	**(564,909)**	189,188
Retained (loss)/profit for the year	22	**(564,909)**	189,188
(Loss)/earnings per ordinary share (pence)	10	**(2.54)**	1.10
IIMR (loss)/earnings per share (pence)	10	**(2.54)**	1.11

All revenues and expenses shown above were generated from continuing operations.

The group has no recognised gains or losses other than those included in the losses above, and therefore no separate statement of total recognised gains and losses has been presented.

There is no difference between the loss on ordinary activities before taxation and the retained loss for the year stated above, and historical cost equivalents.

Reconciliation of movements in shareholders' funds

Reconciliation of movements in shareholders' funds

	1996 £	1995 £
(Loss)/profit for the financial year	**(564,909)**	189,188
New share capital issued	**13,785,237**	-
Expenses of share issue	**(1,157,530)**	-
Net addition to shareholders' funds	**12,062,798**	189,188
Opening shareholders' funds	**(2,520,239)**	(2,709,427)
	9,542,559	(2,520,239)

Balance sheets at 31 August 1996

		Group		Company	
	Notes	1996	1995	1996	1995
		£	£	£	£
Fixed assets					
Tangible assets	11	**231,432**	79,753	-	-
Investments	12	-	-	**205,800**	-
		231,432	79,753	**205,800**	-
Current assets					
Stocks	13	**16,967**	33,784	-	-
Debtors: amounts falling due after one year	14	-	-	**3,602,364**	-
Debtors: amonts falling due within one year	14	**421,198**	225,748	**25,900**	-
Cash at bank and in hand		**9,264,641**	530	**9,235,292**	
		9,702,806	260,062	**12,863,556**	-
Creditors: amounts falling due within one year	15	**354,153**	258,949	**65,694**	-
Net current assets		**9,348,653**	1,113	**12,797,862**	-
Total assets less current liabilities		**9,580,085**	80,866	**13,003,662**	-
Creditors: amounts falling due after more than one year	16	**37,526**	2,601,105	-	-
Net assets/(liabilities)		**9,542,559**	(2,520,239)	**13,003,662**	-
Capital and reserves					
Called up share capital	19	**308,886**	1,715	**308,886**	-
Share premium account	22	**13,020,028**	495,407	**12,524,621**	-
Merger reserve	22	**(204,211)**	(126)	-	-
Profit and loss account	22	**(3,582,144)**	(3,017,235)	**170,155**	-
Equity shareholders' funds/(deficit)		**9,542,559**	(2,520,239)	**13,003,662**	-

The financial statements on pages 13 to 27 were approved by the board of directors on 28 November 1996 and were signed on its behalf by:

S. Loach

Dr S C Loach
Finance Director

Consolidated cash flow statement for the year ended 31 August 1996

	Notes	1996 £	1995 £
Net cash (outflow)/inflow from operating activities		(740,576)	340,559
Returns on investments and servicing of finance			
Interest received		219,432	311
Interest paid on loans and overdraft		(460)	(143)
Interest paid on finance leases		(3,865)	(922)
Other interest paid	6	(171,340)	-
Net cash inflow/(outflow) from returns on investment and servicing of finance		43,767	(754)
Taxation			
UK corporation tax paid		-	-
Investing activities			
Purchase of tangible fixed assets		(144,396)	(30,141)
Proceeds on sale of tangible fixed assets		1,223	7,445
Net cash outflow from investing activities		(143,173)	(22,696)
Net cash (outflow)/inflow before financing		(839,982)	317,109
Financing			
Proceeds from exercise of options		785,237	-
Proceeds from issue of share capital		11,842,470	-
Repayment of loan from related party		(2,499,777)	(316,192)
Repayment of principal under finance leases		(19,423)	(18,570)
Net cash inflow/(outflow) from financing		10,108,507	(334,762)
Increase/(decrease) in cash and cash equivalents	24	9,268,525	(17,653)

Reconciliation of operating (loss)/profit to net cash (outflow)/inflow from operating activities

	1996 £	1995 £
Operating (loss)/profit	(685,040)	353,306
Depreciation on tangible fixed assets	55,552	35,996
(Profit)/loss on disposal of fixed assets	(161)	1,288
Decrease in stocks	16,817	1,614
(Increase) in trade debtors	(156,163)	(202,434)
(Increase)/decrease in other debtors	(646)	9,974
(Increase)/decrease in prepayments and accrued income	(38,641)	4,109
Increase/(decrease) in trade creditors	55,984	(15,492)
(Decrease)/increase in other taxation and social security	(107,811)	158,338
Increase/(decrease) in accruals and deferred income	119,533	(6,140)
Net cash (outflow)/inflow from continuing operations	(740,576)	340,559

Notes to the financial statements for the year ended 31 August 1996

1 Principal accounting policies

The financial statements have been prepared in accordance with applicable Accounting Standards in the United Kingdom. A summary of the more important accounting policies, which have been applied consistently, is set out below.

Basis of accounting

The financial statements are prepared in accordance with the historical cost convention.

Basis of consolidation

On 3 April 1996 the group structure was reorganised and a new holding company established by way of a share exchange. This has been accounted for as a merger in the consolidated accounts, and all transactions within the group have been eliminated.

The acquisition by the company's subsidiary, Phytotech Limited (formerly Phytopharm Limited), of Phytodevelopments Limited on 21 March 1996 has been accounted for as a merger in the consolidated financial statements, and all transactions between the two companies have been eliminated.

Tangible fixed assets

The cost of tangible fixed assets is their purchase cost, together with any incidental expenses of acquisition.

Depreciation is calculated so as to write off the cost of tangible fixed assets, less their estimated residual values, on a straight line basis over the expected useful economic lives of the assets concerned. The principal rates used for this purpose are:

Plant and machinery	20%
Computer equipment	33⅓%
Fixtures and fittings	20%
Motor vehicles	25%

Leasehold improvements are amortised over the length of the lease.

Research and development expenditure

Expenditure on research and development is written off as incurred.

Finance and operating leases

Costs in respect of operating leases are charged on a straight line basis over the lease term. Where fixed assets are financed by leasing agreements, which transfer to the company substantially all the benefits and risks of ownership, the assets are treated as if they had been purchased outright and included in tangible fixed assets. The capital element of the leasing commitments is shown as obligations under finance leases. The lease rentals are treated as consisting of capital and interest elements. The capital element is applied to reduce the outstanding obligations and the interest element is charged against profit in proportion to the reducing capital element outstanding. Assets held under finance leases are depreciated over the shorter of the lease term and the useful lives of equivalent owned assets.

Stock and work in progress

Stock and work in progress is stated at the lower of cost and net realisable value. Work in progress includes contract work carried out as part of on-going work to obtain licences for the sale of specific medicines. Expenditure on stock purchased exclusively for research and development purposes, which is not reimbursable under a licence and development agreement, is written off as incurred.

Foreign currencies

Assets and liabilities expressed in foreign currencies are translated into sterling at rates of exchange ruling at the end of the financial year. Foreign exchange differences are taken to the profit and loss account in the year in which they arise.

Turnover

Turnover, which excludes value added tax, represents the invoiced value of goods and services supplied. Income under licence agreements is taken to profit according to invoice date unless it relates to costs not yet incurred.

Deferred taxation

Tax deferred or accelerated is accounted for in respect of all material timing differences to the extent that it is probable that a liability or asset will crystallise.

Pension costs

The company contributes a set proportion of employees' gross salary costs to defined contribution money purchase schemes. Employees may opt out of the State scheme if they wish. The pension costs charged against profit represent the amount of contributions payable to the pension schemes in respect of the accounting period.

The company provides no other post retirement benefits to its employees.

2 Segmental analysis by class of business

	1996	1995
	£	£
By business activity		
Licensing and development	**800,000**	1,015,000
Product sales	**133,886**	99,106
	933,886	1,114,106

By geographical area

All of the group's turnover, loss before taxation and net assets arose in the United Kingdom

3 Cost of sales and other operating income and expenses

	1996 £	1995 £
Cost of sales	**84,410**	60,118
Gross profit	**849,476**	1,053,988
Research and development	**1,176,152**	473,905
Administrative expenses	**321,614**	146,777
Administrative expenses from related party	**36,750**	80,000
Operating expenses	**1,534,516**	700,682
Operating (loss)/profit	**(685,040)**	353,306

The administrative expenses from related party comprise management charges from Ethical Holdings plc to the company's subsidiary, Phytotech Limited, prior to the formation and flotation of the company.

4 Directors' emoluments

Detailed disclosures of directors' individual remuneration and share options are given in the report of the remuneration committee on pages 4 to 7.

	1996 £	1995 £
Fees	**13,700**	-
Salary payments (including benefits in kind and pension contributions)	**295,267**	109,491
	308,967	109,491
Consideration paid to Ethical Holdings plc for the services of Dr Guy	**6,250**	-
	315,217	109,491

Fees and other emoluments (excluding pension contributions) payable to the chairman and the highest paid director are as follows:

	1996 £	1995 £
Chairman	-	-
Highest paid director	**101,525**	38,333

The number of directors (including the chairman and the highest paid director) who received fees and other emoluments (excluding pension contributions) in the following ranges was:

	1996 Number	1995 Number
£1 - £5,000	**1**	4
£5,001 - £10,000	**2**	-
£35,001 - £40,000	**1**	1
£50,001 - £55,000	**2**	-
£85,001 - £90,000	**1**	-
£100,001 - £105,000	**1**	-

5 Employee information

At 31 August the group employed 19 persons (including executive directors). The average weekly number of persons (including executive directors) employed during the year was:

	1996 Number	1995 Number
Administration	8	2
Research and development	4	5
	12	7

	1996 £	1995 £
Staff costs (for the above persons):		
Wages and salaries	429,754	139,668
Social security costs	42,055	13,990
Other pension costs	16,278	5,384
	488,087	159,042

6 Interest payable and similar charges

	1996 £	1995 £
On bank loans, overdrafts and other loans repayable within 5 years, not by instalments	428	143
On finance leases and hire purchase contracts	3,865	922
Other interest payable	95,008	163,364
	99,301	164,429

Other interest payable comprises interest due on a loan from Ethical Holdings plc. The loan was repaid from the proceeds of the flotation. Interest was charged at the Lloyds Bank Base Rate plus 2%.

7 (Loss)/profit on ordinary activities before taxation

	1996 £	1995 £
(Loss)/profit on ordinary activities before taxation is stated after charging:		
Depreciation charge for the year:		
Tangible owned fixed assets	30,540	15,688
Tangible assets held under finance leases	25,012	20,308
Auditors' remuneration for audit (company £10,000)	14,000	5,000
Auditors' remuneration for non-audit work	106,614	4,400
Operating lease charges:		
Plant and machinery	2,188	1,462
Other assets	10,000	10,000

Included within auditors' remuneration for non-audit work is £97,964 (1995: £nil) which related to the company's flotation on the London Stock Exchange. This has been charged against the share premium account as expenses of issue.

8 Tax on (loss)/profit on ordinary activities

There is no corporation tax charge because of the incidence of tax losses (1995: £nil).

9 Profit for the financial year

As permitted by section 230 of the Companies Act 1985, the parent company's profit and loss account has not been included in these financial statements. The parent company's profit for the period from incorporation to 31 August 1996 was £170,155.

10 (Loss)/earnings per ordinary share

The calculation of earnings per share on the net basis is based on the loss on ordinary activities after taxation, namely £(564,909) (1995:profit £218,926) and on 22,233,577 (1995: 17,148,000) ordinary shares, being the weighted average number of ordinary shares in issue and ranking for dividend during the year.

A further measure of earnings per share has been recommended by the Institute of Investment Management and Research (the 'IIMR') for adoption by financial analysts. This measure, known as headline earnings, adjusts standard earnings per share to eliminate capital items only, rather than all exceptional items. IIMR headline loss per share amounted to (2.54)p (1995: earnings 1.11p) as set out
below:

	1996 pence per share	1995 pence per share
Earnings per share	**(2.54)**	1.10
IIMR adjustments		
Gain on sale of tangible fixed assets	-	0.01
IIMR earnings per share	**(2.54)**	1.11

11 Tangible fixed assets

Group

	Short Leasehold	**Computer equipment**	**Motor vehicles**	**Plant and machinery**	**Fixtures and fittings**	**Total**
	£	**£**	**£**	**£**	**£**	**£**
Cost						
At 1 September 1995	20,492	15,032	40,545	102,925	3,309	182,303
Additions	-	69,505	98,888	14,898	25,002	208,293
Disposals	-	(814)	(1,595)	-	-	(2,409)
At 31 August 1996	**20,492**	**83,723**	**137,838**	**117,823**	**28,311**	**388,187**
Depreciation						
At 1 September 1995	3,668	8,577	15,728	71,994	2,583	102,550
Charge for year	4,098	11,158	22,346	16,501	1,449	55,552
Disposals	-	(90)	(1,257)	-	-	(1,347)
At 31 August 1996	**7,766**	**19,645**	**36,817**	**88,495**	**4,032**	**156,755**
Net book value						
At 31 August 1996	**12,726**	**64,078**	**101,021**	**29,328**	**24,279**	**231,432**
Net book value						
At 31 August 1995	16,824	6,455	24,817	30,931	726	79,753

The net book values of tangible fixed assets held under finance leases and hire purchase contracts included in the above figures are as follows:

	Group		Company	
	1996	1995	1996	1995
	£	£	£	£
Motor vehicles	**78,811**	24,313	-	-
Plant and machinery	**600**	7,698	-	-
	79,411	32,011	-	-

Company

The Company has no tangible fixed assets.

12 Fixed asset investments

Company

Interests in Group Undertakings

	£
At 1 September 1995	-
Additions	205,800
At 31 August 1996	205,800

Interests in group undertakings

Name of undertaking	Country of incorporation	Description of shares held	Proportion of nominal value of issued shares held by Group %	Company %
Phytotech Limited	England and Wales	Ordinary 10 pence shares	100	100
Phytodevelopments Limited	England and Wales	Ordinary £1 shares	100	-

Both the above companies have been included in these financial statements and operated principally in their country of incorporation or registration.

The principal business activities of these subsidiary undertakings are:

Phytotech Limited - research and development of plant based medicines
Phytodevelopments Limited - non trading

On 21 March the company's subsidiary Phytotech Limited (formerly Phytopharm Limited) acquired the entire share capital of Phytodevelopments Limited by issuing 2,860 10 pence ordinary shares in exchange for the entire share capital of Phytodevelopments Limited. Phytodevelopments Limited held the rights to certain plant based remedies but had ceased trading at the time of the acquisition. Net liabilities acquired of £1,900 comprised an amount due to Phytotech Limited.

13 Stocks

	Group 1996 £	Group 1995 £	Company 1996 £	Company 1995 £
Raw materials and consumables	**11,981**	24,069	**-**	-
Finished goods and goods for resale	**4,986**	9,715	**-**	-
	16,967	33,784	**-**	-

14 Debtors

	Group 1996 £	Group 1995 £	Company 1996 £	Company 1995 £
Amounts falling due after one year				
Amounts owed from group undertakings	**-**	-	**3,602,364**	-
Amounts falling due within one year				
Trade debtors	**371,040**	214,877	**-**	-
Other debtors	**825**	179	**-**	-
Prepayments and accrued income	**49,333**	10,692	**25,900**	-
	421,198	225,748	**25,900**	-
	421,198	225,748	**3,628,264**	-

Included in trade debtors is an amount of £340,522 (1995: £175,000) due from the group's licensee under the terms of the Licence and Development Agreement for Zemaphyte™. This was received after the year end.

15 Creditors: amounts falling due within one year

	Group 1996 £	Group 1995 £	Company 1996 £	Company 1995 £
Bank overdraft	**-**	4,414	**-**	-
Obligations under finance leases	**26,065**	12,913	**-**	-
Trade creditors	**104,472**	48,488	**18,275**	-
Amounts owed to related undertakings	**18,760**	-	**-**	-
Accruals and deferred income	**151,831**	32,298	**37,500**	-
Other creditors including taxation and social security	**53,025**	160,836	**9,919**	-
	354,153	258,949	**65,694**	-

16 Creditors: amounts falling due after more than one year

	Group 1996 £	Group 1995 £	Company 1996 £	Company 1995 £
Amounts owed to related undertakings	**-**	2,594,901	**-**	-
Obligations under finance leases	**37,526**	6,204	**-**	-
	37,526	2,601,105	**-**	-

Finance leases

The net finance lease obligations to which the group is committed are:

	Group		Company	
	1996	1995	1996	1995
	£	£	£	£
In one year or less	**31,427**	14,658	-	-
Between one and two years	**28,043**	5,076	-	-
Between two and five years	**12,345**	1,692	-	-
	71,815	21,426	-	-
Less: interest	**8,224**	2,309	-	-
	63,591	19,117	-	-

17 Deferred taxation

There is no provision or amount unprovided for deferred tax at 31 August 1996 due to the incidence of tax trading losses (1995: £nil).

18 Pension and similar obligations

The group operates a number of defined contribution pension schemes for employees. The assets of the schemes are held separately from those of the group in independently administered funds. The pension cost charged represents contributions paid and payable by the company to the funds and amounted to £16,278 (1994: £5,384).

19 Called-up share capital

	1996	1995
	£	£
Authorised		
50,000,000 ordinary shares of 1p each (1995: 1,715 ordinary shares of £1 each)	**500,000**	1,715
Allotted, called-up and fully paid		
30,888,571 ordinary shares of 1p each (1995: 1,715 ordinary shares of £1 each)	**308,886**	1,715

The authorised and called up fully paid share capital disclosed for 1995 is that of Phytotech Limited (formerly Phytopharm Limited) which, in accordance with merger accounting provisions, has been increased by £286 to reflect the issue of shares on 21 March 1996 to acquire Phytodevelopments Limited.

On 3 April 1996 the company issued 205,800 £1 ordinary shares in exchange for the entire share capital of Phytotech Limited (formerly Phytopharm Limited) such that the shareholders of Phytotech Limited became shareholders in Phytopharm plc.

On 18 April 1996 the company resolved by special resolution to subdivide each ordinary share of £1 nominal value into 100 ordinary shares of 1 pence par value.

On 19 April 1996 the company published its prospectus for a full listing on the London Stock Exchange. The company issued 7,428,571 1 pence ordinary shares at £1.75 each raising £13,000,000 gross. Expenses of issue were £1,157,530. Shares commenced trading on 25 April 1996. The company is using the proceeds to finance such additional work as may be required by the Medicines Control Agency for the registration in the UK of the company's lead product Zemaphyte™, to fund research and development of the company's other products, and to facilitate the production of Zemaphyte™ in commercial volumes through the provision of manufacturing facilities and purchase of raw materials.

20 Options in shares of Phytopharm plc

Options have been granted for 1p ordinary shares as follows:

Number of share options outstanding	Note	Date option granted	Subscription price per share
1,836,000	1	17 April 1996	26.25p
67,000	2a	24 April 1996	£1.925
153,700	2b	24 April 1996	£1.925
33,000	3a	24 April 1996	£1.925
187,000	3b	24 April 1996	£1.925
429,800	4	24 April 1996	£1.925
2,706,500			

Note

1 These options vest in tranches of one third on each of the first, second and third anniversaries of the date of grant. The options are exercisable between three and seven years from the date of grant.

2a These options vest in tranches of one third on each of the first, second and third anniversaries of the date of grant, and have been granted under a scheme approved by the Inland Revenue. The option is subject to the following condition which must be satisfied before it can be exercised, namely that the increase between an amount equal to 91% of the option price and the middle market quotation of a share on a date falling no earlier than the third anniversary of the date of grant of that option shall be at least one and a half times the increase over the period from the date of grant to such date in the FT Actuaries All Share Index. The options remain exercisable for ten years from the date of grant.

2b These options vest and must satisfy the same conditions as under Note 2a above. However, these options remain exercisable for seven years from the date of grant and have not been submitted to the Inland Revenue for approval.

3a These options vest in tranches of one third on each of the first, second and third anniversaries of the date of grant and have been granted under a scheme approved by the Inland Revenue. The option is subject to the following condition which must be satisfied before it can be exercised, namely that the increase between an amount equal to 91% of the option price and the middle market quotation of a share on a date falling no earlier than the third anniversary of the date of grant of that option shall be at least two times the increase over the period from the date of grant to such date in the FT Actuaries All Share Index.. The options remain exercisable for ten years from the date of grant.

3b These options vest and must satisfy the same conditions as under Note 3a above. However, these options remain exercisable for seven years from the date of grant and have not been submitted to the Inland Revenue for approval.

4 These options vest in tranches of one fifth on each of the first, second, third, fourth and fifth anniversaries of the date of grant. The option is subject to the following condition which must be satisfied before it can be exercised, namely that the increase between an amount equal to 91% of the option price and the middle market quotation of a share on a date falling no earlier than the third anniversary of the date of grant of that option shall be at least one and a half times the increase over the period from the date of grant to such date in the Pharmaceuticals Index as published by the Financial Times as a constituent part of the FT Actuaries All Share Index. The options remain exercisable for seven years from the date of grant.

21 Mergers

On.21 March 1996 Phytotech Limited (formerly Phytopharm Limited) acquired the entire share capital of Phytodevelopments Limited by way of a share exchange. The consideration was satisfied by the issue of 2,860 10 pence ordinary shares in Phytotech Limited credited as fully paid in accordance with an agreement dated 11 April 1994. Phytodevelopments Limited held the rights to certain plant based remedies but had ceased trading at the time of the acquisition. The fair value of the consideration at the issue price is £6,006,000. As the two companies were under common control this transaction has been treated as a group reconstruction and accounted for as a merger. The results of Phytodevelopments Limited up to 21 March 1996 are disclosed below after eliminating all transactions between the two companies. No adjustments were required as a result of applying Phytotech Limited's accounting policies to Phytodevelopments Limited.

	Period to 31 March 1996 £	Year to 31 August 1995 £
Retained profit/(loss)	**9,263**	(29,738)
Net liabilities	**(1,900)**	(11,163)

On 3 April 1996 the group structure was reorganised and a new holding company, Phytopharm plc, was established by way of a share exchange. The transaction has been treated as a group reconstruction and accounted for as a merger. Phytopharm plc had not traded prior to 3 April 1996 and it adopted the accounting policies and year end of Phytotech Limited.

22 Share premium account and reserves

Group

	Share premium account £	Merger reserve £	Profit and loss account £
At 1 September 1995	495,407	(126)	(3,017,235)
Premium on new share issue	13,682,151	-	-
Expenses of share issue	(1,157,530)	-	-
Merger reserve arising	-	(204,085)	-
Retained loss for the year	-	-	(564,909)
At 31 August 1996	**13,020,028**	**(204,211)**	**(3,582,144)**

Company

	Share premium account £	Profit and loss account £
At 1 September 1995	-	-
Premium on new share issue	13,682,151	-
Expenses of share issue	(1,157,530)	-
Retained loss for the year	-	170,155
At 31 August 1996	**12,524,621**	**170,155**

23 Analysis of changes in financing during the year

	1996		1995	
	Share capital including premium and merger reserve	**Loans and finance lease obligations**	Share capital including premium and merger reserve	Loans and finance lease obligations
	£	**£**	£	£
At 1 September 1995	**496,996**	**19,117**	496,996	26,055
Proceeds from options exercised	**785,237**	-	-	-
Proceeds from issue of shares	**13,000,286**	-	-	-
Expenses of issue	**(1,157,530)**	-	-	-
Inception of finance lease contracts	-	**63,897**	-	11,632
Repayment of principal on finance leases	-	**(19,423)**	-	(18,570)
At 31 August 1996	**13,124,989**	**63,591**	**496,996**	**19,117**

24 Cash and cash equivalents

	1996	1995
	£	£
Changes during the year		
At 1 September 1995	(3,884)	13,769
Net cash inflow	9,268,525	(17,653)
At 31 August 1996	**9,264,641**	**(3,884)**

	1996	1996 Change in year	1995	1995 Change in year	1994
	£	£	£	£	£
Analysis of balances					
Cash at bank and in hand	9,264,641	9,264,111	530	(31,115)	31,645
Bank overdrafts	-	4,414	(4,414)	13,462	(17,876)
	9,264,641	**9,268,525**	**(3,884)**	**(17,653)**	**13,769**

25 Major non-cash transactions

During the year the company entered into finance lease arrangements in respect of fixed assets with a total capital value at the inception of the leases of £63,897 (1995: £11,632).

26 Capital commitments

There were no capital commitments for fixed assets authorised by the directors or contracted for at 31 August 1996 (1995: £nil)..

27 Contingent liabilities

There were no contingent liabilities at 31 August 1996 (1995: £nil).