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PipeHawk plc

Report & Accounts 2006

A pivotal year with profitability for the first time since flotation. Progress on all business fronts, including the successful acquisition of QM Systems Limited in March 2006. All business units have reported excellent results:

- Adien reports record sales and profits again and undertakes the largest single detection and mapping project in the UK in Edinburgh
- Sumo increases sales by 52%, reaches profitability and wins the British Franchising Association's Brand Builder of the year award
- PipeHawk secures future of UK GPR industry with introduction of Ofcom licencing, develops PipeHawk III and continues work on MineHawk
- QM Systems successfully integrated into group

Operating Divisions

Adien — *Providing Nationwide Site Survey Information and Support*

Sumo — Serving the UK for Utility Mark Out Service

PipeHawk Technology Division — Research and development of GPR technology

QM Systems — Test Systems for complex electronic products

"A pivotal year"

This year has marked a turning point in the fortunes of PipeHawk; for the first time since the Company was admitted to trading on AIM in December 2000, the Group is reporting a profit for the year.

I am delighted to report the turnover for the year ended 30 June 2006 was £3,312,000, which is an increase of 124 per cent. on the previous year (2005: £1,477,000), and that the Company achieved a profit after taxation for the year of £141,000 (2005: loss £297,000). These improved results reflect the contribution from QM Systems Limited ("QM Systems"), which was acquired in March 2006. The results for the year include turnover of £1,257,000 and
operating profit of £231,000 relating to QM Systems. Notwithstanding the contribution from QM Systems, turnover attributable to the PipeHawk business increased by £578,000, to £2,047,000, an increase of 39 per cent. over the previous year.

The integration of QM Systems is progressing well and is ahead of management's expectations. Their technology development team is already working with PipeHawk's Technology division on the next generation of PipeHawk GPR equipment.

The trading performances of the Group's four major business areas are set out below;

Adien

Adien, our high definition underground mapping and planning service, has,during the year, both increased its manpower and improved its use of technology to increase the efficiency of its teams.

The change in strategy adopted during 2002, from selling GPR equipment to providing a service to the utilities industry has, after some initial scepticism, been well received. The use of GPR assisted surveys is now more widely specified by the planning authorities; and is increasingly valued by contractors as essential both for the smooth running of the contract and for health and safety reasons.

From September 2006 Adien's service offering has been strengthened following the issue by Ofcom of the first two GPR user licences to PipeHawk and Adien. The licences have been issued following the regulation of the GPR industry after years of negotiations with radio licensing authorities led by our Technical Director, Richard Chignell. All users of GPR equipment operating without a licence from Ofcom are now deemed to be working illegally and can be subject to enforcement action.

The market for Adien's services continues to grow. This growth coupled with the falling price of GPR equipment and increased availability of such equipment has encouraged new entrants imitating the services of Adien to enter the market resulting in some price competition. However, Adien's advantages of many year's GPR experience, Ofcom licences, excellent service delivery and the links to PipeHawk provide a level of protection against these new entrants.

SUMO

SUMO - a 36 per cent. owned joint venture, which provides instant mark out services to its customers.

SUMO has also had a good year. It has increased its turnover to £1,449,000 from £948,000 in 2005 and returned a profit of £2,000 for the year (2005: loss £55,000). During the year it won the British

Franchising Association's Brand Builder of the Year Award. This has resulted in a significant increase in demand for the Company's franchises. To accommodate this growth the Company has moved to new, larger offices and has strengthened its management team.

SUMO received the third licence from Ofcom to operate GPR equipment.

During the year SUMO raised £100,000 from an outside investor for a 9 per cent. holding in the company to finance its expansion. This investment places a value of £1.1 million on SUMO and values PipeHawk's holding at £396,000, compared with £15,000 shown on the Group's balance sheet.

Technology Division

I would like to congratulate Richard Chignell on his contribution to the discussions with Ofcom which has resulted in a regulatory environment for GPR equipment operation which the Board feel is fair and reasonable without being heavy handed on a fledgling industry.

The Technology division has improved the efficiency and effectiveness of Adien both in terms of "normal" subsurface information gathering and designing a GPR system to find large diameter waterpipes buried under fields.

Considerable initial R & D work has been carried out in developing the next generation of GPR equipment from an updated fully Ofcom compliant PipeHawk Mark 3 to the MineHawk, landmine detection vehicle. The Company has sought funding for this landmine detection vehicle by way of an EU grant and the Board anticipate receiving confirmation of this funding during the course of this financial year.

QM Systems

The Company acquired QM Systems on 22 March 2006. QM Systems has a team of able and skilled hardware and software designers, who develop and manufacture innovative and cost effective solutions for clients, particularly in the aerospace industry. They are currently working closely with Lockheed Martin and Smiths Aerospace to develop rigorous testing systems for the power systems in the Joint Strike Fighter Programme. If this initial development work is successful the Board believe this may lead to a long term project.

Strategy and Outlook

Last year I said in my Chairman's Statement that "our strategy is to remain at the forefront of applied GPR and non-invasive testing technologies, delivering high quality value adding services and products which play a vital role in the safety and protection of people worldwide".

2005/6 was a pivotal year in developing this strategy with:

i. achievement of a profit;
ii. obtaining three Ofcom licences; and
iii. the acquisition of QM Systems.

Our ongoing strategy remains as stated above. The current year has started well and we are confident that we can build on the successes of the past year. We now have better critical mass to achieve our aims.

Gordon Watt
Chairman
8 November 2006

"The structures are in place to exploit GPR technology for our shareholders"

Company Information

Directors	**Gordon G Watt** (Executive Chairman) **Dr Richard J Chignell** (Technical Director) **Robert G Tallentire** (Finance Director) **R Randal MacDonnell** (Non Executive)
Secretary	**Robert Tallentire ACA MBA**
Nominated Adviser	**John East & Partners Limited** Crystal Gate 28-30 Worship Street London EC2A 2AH
Brokers	**JM Finn & Co** Salisbury House, London Wall, London EC2M 5TA
Registrars	**Capita IRG Plc** Bourne House 34 Beckenham Road Beckenham Kent BR3 4TU
Registered number	**3995041**
Registered office	Systems House Mill Lane Alton Hampshire GU34 2QG
Auditors	**Menzies Chartered Accountants & Registered Auditors** Neville House 55 Eden Street Kingston Upon Thames London KT1 1BW
Solicitors	**Lawrence Graham** 190 Strand London WC2R 1JN

Principal activities

The directors present the annual report for the year ended 30 June 2006.

Principal activities

The principal activities of the Group during the year were the development, assembly and sale of ground probing radar (GPR) equipment, the provision of GPR based services and the undertaking of complementary Research and Development assignments. On 22 March 2006, the Group acquired QM Systems Limited, a company which designs and manufactures complete software and hardware solutions in an environment which is certified to international quality standards. QM will assist PipeHawk in developing a vehicle capable of detecting and marking landmines with a very low false alarm rate. A review of the operations of the Group is included in the Chairman's statement on page 2.

Results and dividends

The results for the Group for the year are set out in the consolidated profit and loss account on page 12. The directors do not recommend the payment of a dividend for the year (2005: £nil).

Charitable and political contributions

The Group has not made any charitable or political contributions in the year (2005: £nil).

Directors

The present directors of the company are set out on page 4. Mr R MacDonnell was appointed on 28 February 2006. Mr Chambers resigned on 5 February 2006. The directors' beneficial interests in the share capital of the company were as follows:

	8 November 2006		30 June 2006		30 June 2005	
	Ordinary Shares of 1p	% of issued share capital	Ordinary Shares of 1p	% of issued share capital	Ordinary Shares of 1p	% of issued share capital
Dr. R J Chignell	2,204,200	8.2%	2,204,200	8.2%	2,204,200	9.5%
G G Watt	3,646,500	13.6%	3,646,500	13.7%	3,646,500	15.7%
R MacDonnell	729,216	2.7%	729,216	2.7%	-	-
R G Tallentire	-	-	-	-	-	-

The directors are also interested in unissued Ordinary Shares granted to them by the Company under share options held by them pursuant to individual option schemes as set out in note 7 on page 20.

Substantial share interests

Other than directors, the company has been notified of the following persons being interested in more than 3% of the issued share capital of the company at the date of this report.

	Ordinary Shares of 1p	% of issued share capital
J T Twigg	1,054,830	3.99%
N G Wood	1,054,830	3.99%
J Moulton	904,939	3.92%

Suppliers

The Group's policy is, where possible, to pay suppliers in accordance with the terms agreed with them. Where no specific terms have been agreed, the Group's policy is to pay suppliers at the end of the month following that in which the supplier's invoice is received. This policy is made known to staff who handle payments to suppliers and is made known to suppliers on request. For the Group, trade creditors at 30 June 2006 represent 39 days' purchases (2005: 32 days' purchases) and for the company, 43 day's purchases (2005: 48 day's purchases).

Auditors

Menzies' Chartered Accountants reappointment will be proposed at the forthcoming Annual General Meeting, in accordance with section 385 of the Companies Act 1985.

Going concern

After making enquiries, 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 financial statements.

Approval

The report of the directors was approved by the Board on 8 November 2006 and signed on its behalf by:

Robert Tallentire ACA MBA
Secretary

The Company is not subject to the Listing Rules of the Financial Services Authority which require listed companies to disclose how they have applied the principles set out in Section 1 of the Combined Code prepared by the Committee on Corporate Governance and whether they have complied with its provisions throughout the period. The Company considers these principles to be best practice, subject to their appropriateness given the size of the Company and the composition of Board. The following report summarises the current corporate governance processes that are in place.

Directors

The Board currently comprises the executive chairman, two executive directors and one non-executive director.

Executive directors' normal retirement age is 60 and non-executive directors' normal retirement age is 70. Both are subject to periodic reappointment by shareholders. The requirements of the company's articles result in each director being reappointed every three years.

The full Board meets formally six times each year. There is a formal schedule of matters reserved for the Board's decision. All directors have access to the advice and services of the company secretary, who is also responsible for ensuring that Board procedures are followed. There is also a procedure in place for any director to take independent professional advice, if necessary, at the company's expense.

Internal controls

The directors have overall responsibility for ensuring that the Group maintains a system of internal control, and for reviewing its effectiveness, to provide them with reasonable assurance that the assets of the Group are safeguarded and that the shareholders' investments are protected. The system includes internal controls covering financial, operational and compliance areas, and risk management. There are limitations in any system of internal control, which are designed to manage rather than eliminate risk and can provide reasonable but not absolute assurance against material misstatement or loss.

The Board has considered the guidance provided by the Turnbull report and reviewed the system of internal controls in place. An assessment of the major risk areas for the business and methods used to monitor and control them was also undertaken. In addition to financial risk, this covered operational, commercial, marketing and research and development risks. This risk review has become an *ongoing process of identifying, evaluating and managing the significant risks faced by the Company, with regular review by the Board.*

The additional key procedures designed to provide an effective system of internal control are that:

- There is an organisational structure with clearly defined lines of responsibility and delegation of authority.
- Annual budgets are prepared and updated as necessary.
- Management accounts are prepared on a quarterly basis and compared to budgets and forecasts to identify any significant variances.
- The Group appoints staff of the required calibre to fulfil their allotted responsibilities.

The Board has considered it inappropriate to establish an internal audit function. However, this decision will be reviewed as the operations of the Group develop.

Identification of business risk

Regular assessments of ongoing risks facing the business are undertaken as part of the regular Group management meetings in the key areas such as management of working capital, compliance, legal and operational issues. This risk management framework is applied to major initiatives such as acquisitions as well as operational risks within the business including operational health and safety risks.

Financial Instruments

There are no matters concerning financial risk which are material for the assessment of the assets, liabilities, financial position and profit or loss of the company.

Remuneration report

Basic salaries are set having regard to each director's responsibilities and pay levels for comparable positions. In framing its remuneration policy the committee aims to attract and retain directors to run the company successfully without making excessive payments.

Details of individual directors' share options are included in the notes to the financial statements and details of their remuneration including *long term incentive schemes are included in note 7 to the audited financial statements. The notice period in all the directors' service* contracts is one year.

Shareholder relationships

The Board attaches a high priority to communications with shareholders. Presentations are made to shareholders, institutions and analysts once a year to coincide with the announcement of the final results. Additional dialogue with institutional shareholders is entered into as necessary.

The annual general meeting is to be held on 14 December 2006. The resolutions to be proposed at the annual general meeting, together with explanatory notes, appear in the separate Notice of Annual General Meeting on page 33.

Other information about the company is available on the company's web site.

Gordon Watt BA, FCA, FRSA
Chairman (53)

Gordon is a chartered accountant having been a partner at RSM Robson Rhodes and then Finance Director/Deputy Chief Executive of British Bus Plc until it was sold to Arriva Plc. He is non-executive chairman of a number of private companies, he became a non-executive director of the Group in 1998, became finance director in December 2001 and Chairman in January 2003.

Dr Richard Chignell MSc, PhD, C Eng, FIET
Technical Director (59)

Richard founded the business in 1988, having initially worked for GEC-Marconi on advanced antennas for space and defence systems. He obtained his PhD at Imperial College, London producing a solution for air traffic control radars that is still in use. Subsequently he led the UK MoD's Falkland Islands project to detect plastic mines laid by the Argentineans. The project was a success when a trial minefield was searched and every mine found. He has recently stepped down as Chairman of Euro-GPR Association having doubled its membership and negotiated all the European Radio licensing technical standards (ETSI) for GPR through to publication as the final step before full implementation.

Robert Tallentire ACA MBA
Finance Director (47)

Bob joined PipeHawk in 2003 and became Group Finance Director and Managing Director of Adien on 10th December 2004. Bob is a chartered accountant having been a partner at RSM Robson Rhodes and then Managing Director of his own business for 5 years which was successfully sold in 2002. He has extensive consulting and management experience.

R Randal MacDonnell
Non-executive Director (67)

Randal joined the Group in February 2006. He is currently a director of Reverse Takeover Investments plc, having previously been a director of Kleinwort Benson Securities, Laing & Cruickshank Securities and Chase Manhattan Securities Limited. Prior to that he was a partner in stockbrokers Laurie Milbank & Co.

Statement of Directors' Responsibilities for the Annual Report

The directors are responsible for preparing the financial statements in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice.

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 for that year. In preparing those financial statements, the directors are required to:

- Select suitable accounting policies, as described on pages 16 to 17, 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 that disclose with reasonable accuracy at any time the financial *position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. The directors* 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.

In 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 steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

Independent Auditors' Report to the Shareholders of PipeHawk PLC

We have audited the financial statements of the group for the year ended 30 June 2006 on pages 12 to 32, which have been prepared on the basis of the accounting policies set out on pages 16 to 17.

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

As described in the Statement of Directors' Responsibilities the company's directors are responsible for the preparation of the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Our responsibility is to audit the financial statements 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 are properly prepared in accordance with the Companies Act 1985, and whether the information given in the Directors' Report is consistent with the financial statements. We also 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 other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. The other information comprises the Chairman's Statement, Report of the Directors, Corporate Governance Statement, Directors Biographies and the Notice of Annual General Meeting. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the 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. 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 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, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's and group's affairs as at 30 June 2006 and of its profit for the year then ended and 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.

Menzies

Menzies
Chartered Accountants and Registered Auditors

London, England
10 November 2006

Consolidated Profit and Loss Account

For the year ended 30 June 2006

	Note	2006 £'000	2005 £'000
Turnover			
Group and share of joint venture		3,312	1,477
Less: share of joint venture turnover		(529)	(102)
Group turnover – total continuing activities	2	2,783	1,375
Group operating costs	3	(2,690)	(1,689)
Group operating profit/(loss)	3	93	(314)
Share of operating profit/(loss) in joint venture	12	19	(25)
Profit/(loss) on ordinary activities before interest and taxation		112	(339)
Group interest receivable and similar income	4	4	-
Group interest payable and similar charges	4	(44)	(55)
Profit/(loss) on ordinary activities before taxation	5	72	(394)
Tax on profit on ordinary activities	8	69	97
Transfer to reserves	22	141	(297)

	Note	2006 p	2005 p
Earnings per share - Basic	9	0.6	(1.3)
Earnings per share - Diluted	9	0.4	(1.3)

There are no recognised gains or losses other than those reported above.

The group's results for the periods above are entirely from continuing operations.

Consolidated Balance Sheet
at 30 June 2006

	Note		2006 £'000		2005 £'000
Fixed assets					
Intangible assets	10		1,121		241
Tangible assets	11		354		239
Investment in joint venture:	12				
Share of gross assets		70		39	
Share of gross liabilities		(55)		(43)	
		15		(4)	
			15		(4)
			1,490		476
Current assets					
Stocks	14		757		263
Debtors	15		969		469
Cash at bank			221		-
			1,947		732
Creditors: amounts falling due within one year	16		(2,088)		(1,260)
Net current liabilities			(141)		(528)
Total assets less current liabilities			1,349		(52)
Creditors: amounts falling due after more than one year	17		(602)		(111)
Provisions for liabilities and charges	18		-		-
Net assets			747		(163)
Capital and reserves					
Called up share capital	21		267		232
Share premium account	22		4,815		4,081
Profit and loss account	22		(4,335)		(4,476)
Equity shareholders' funds	23		747		(163)

The financial statements were approved by the board on 8 November 2006 and signed on its behalf by:

G Watt

Gordon G Watt
Director

Company Balance Sheet
at 30 June 2006

	Note	2006 £'000	2005 £'000
Fixed assets			
Tangible assets	11	8	20
Investments	13	1,395	597
		1,403	617
Current assets			
Stock	14	195	245
Debtors	15	221	405
		416	650
Creditors: amounts falling due within one year	16	(602)	(1,149)
Net current assets		(186)	(499)
Total assets less current liabilities		1,217	118
***Creditors:** amounts falling due after more than one year*	17	*500*	-
Provisions for liabilities and charges	18	-	-
Net assets		717	118
Capital and reserves			
Called up share capital	21	267	232
Share premium account	22	4,815	4,081
Profit and loss account	22	(4,365)	(4,195)
Equity shareholders' funds		717	118

The financial statements were approved by the board on 8 November 2006 and signed on its behalf by:

G Watt

Gordon G Watt
Director

Consolidated Cash Flow Statement

For the year ended 30 June 2006

	Note	2006 £'000	2005 £'000
Net cash inflow/(outflow) from operating activities	24	133	(126)
Returns on investment and servicing of finance			
Interest received		4	-
Interest element of finance lease rentals		(3)	(3)
Interest paid		(41)	(52)
		93	(181)
Corporation tax received		77	96
Capital expenditure and financial investment			
Payments for tangible fixed assets		(96)	(43)
Acquisitions and disposals			
Cash acquired through purchase of subsidiary		221	-
Costs of acquisition		(51)	-
		170	-
Cash inflow/(outflow) before use of liquid resources and financing		244	(128)
Financing			
New loans		-	216
Repayment of loans		(110)	(15)
Capital element of finance lease and hire purchase payments		(21)	(26)
		(131)	175
Increase in cash	26	113	47

1. Accounting Policies

Basis of accounting
The financial statements are prepared in accordance with applicable accounting standards under the historical cost convention. As permitted by section 230 of the Companies Act 1985, the profit and loss account of the parent company has not been separately presented in the financial statements.

Going concern
The Group is at a relatively early stage in its development and currently has net current liabilities. The directors have reviewed the group's funding requirements for the twelve months following the date of these accounts and are confident that additional funding will be obtainable if required. It is on this basis that the directors consider it appropriate to adopt the going concern basis of preparation within these accounts.

Basis of consolidation
The financial statements consolidate those of PipeHawk plc and of its subsidiary undertakings, which are made up to 30 June 2006.

Goodwill
Positive goodwill arising on acquisitions is capitalised, classified as an asset on the balance sheet and amortised on a straight-line basis over its useful economic life up to a maximum of 20 years. It is reviewed for impairment at the end of the first full financial year following the acquisition and in other periods if events or changes in circumstances indicate that the carrying value may not be recoverable.

Investments in joint ventures
Entities in which the group holds an interest on a long-term basis and are jointly controlled by the group and one or more other venturers under a contractual arrangement are treated as joint ventures. The group's share of the results of joint ventures is included in the consolidated profit and loss account in accordance with Financial Reporting Standard No 9. In the consolidated balance sheet the interest in joint ventures is included at the group's share of the net assets of the joint ventures.

Revenue recognition
Revenue from short-term contracts is recognised upon delivery to the customer, when there are no significant vendor obligations remaining and collection of the resulting income is considered probable. Where a significant vendor obligation exists to meet client requirements, revenue recognition is delayed until the obligation has been satisfied. Long-term contracts are those extending in excess of 12 months and any of a shorter duration, which are material to the activity of the period. Revenue and attributable profit is recognised once the outcome of a long-term contract can be assessed with reasonable certainty. Provision is made for all foreseeable losses if a contract is assessed as unprofitable.

Tangible fixed assets and depreciation
Depreciation is provided evenly on the cost of tangible fixed assets, to write them down to their estimated residual values over their expected useful lives. The carrying values of tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. The principal annual rates used are:

Equipment, fixtures and fittings	10-25%
Motor vehicles	25%
Leasehold improvements	20%

Stocks
Stocks and work in progress are valued at the lower of cost and net realisable value, after making due allowance for obsolete and slow moving items. Costs include all direct expenditure and an appropriate proportion of attributable production overheads.

1. Accounting Policies (continued)

Research and development
Research and development expenditure is written off as incurred, except that development expenditure incurred on an individual project is carried forward when its future recoverability can reasonably be regarded as assured. Any expenditure carried forward is amortised in line with the expected future sales from the related project.

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 against the profit and loss account so as to produce a constant periodic rate of charge on the remaining balance of the obligation for each accounting period.

Operating lease agreements
Rentals applicable to operating leases, where substantially all of the benefits and risk of ownership remain with the lessor, are charged against the profit and loss account on a straight-line basis over the term of the lease.

Pension scheme contributions
Pension contributions are charged to the profit and loss account in the period in which they fall due. All pension costs are in relation to defined contribution schemes.

Foreign currencies
Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at 30 June. Transactions in foreign currencies are recorded at the rates ruling at the date of the transactions.

Deferred Taxation
The payment of taxation is deferred or accelerated because of timing differences between the treatment of certain items for accounting and taxation purposes. Full provision for deferred taxation is made under the liability method, without discounting, on all timing differences that have arisen, but not reversed by the balance sheet date, unless such provision is not permitted by FRS 19. Deferred tax assets are recognised to the extent that it is more likely than not that they will be recovered.

In accordance with FRS 19 deferred tax is not provided for fair value adjustment gains to fixed assets and stock to uplift price of those ruling when an acquisition is made.

2. Segmental Analysis

	2006 £'000	2005 £'000
Turnover by geographical market		
United Kingdom	2,724	1,223
Other EU countries	34	30
USA	9	75
Other	16	47
	2,783	1,375

The Group operates in the United Kingdom and consists of a single business segment.

3. Group Operating Profit/(Loss) from continuing operations

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Turnover	2,783	1,375	252	209
Change in stock and WIP	(92)	(19)	(51)	(29)
Other operating income	5	35	0	28
Raw materials and consumables	(164)	(65)	(33)	(29)
Other external charges	(419)	(186)	(33)	(70)
Staff costs	(1,277)	(1,006)	(349)	(371)
Depreciation and amortisation	(196)	(172)	(13)	(72)
Other operating charges	(547)	(276)	(112)	(120)
Group operating profit (loss)	93	(314)	(339)	(454)

QM Systems contributed £1,257,000 turnover and £231,000 of operating profit during the year.

4. Group Net Interest Payable and Similar Charges

	2006	2005
	£'000	£'000
Bank interest receivable	4	-
Interest payable	(44)	(55)
	(40)	(55)
Interest payable comprises interest on:		
Finance leases	3	3
Bank loans and overdrafts	23	23
Other loans	-	-
Directors' loans	15	24
Other interest	3	5
	44	55

5. Profit/(Loss) on Ordinary Activities before Taxation

This is arrived at after charging for the Group:

	2006 £'000	2005 £'000
Research and development costs	376	398
Amortisation of goodwill	27	14
Depreciation of wholly owned tangible fixed assets	160	169
Depreciation of tangible fixed assets held under finance leases	9	-
Auditors' remuneration		
- audit services	17	13
- *non audit services*	-	-
Operating lease rentals:		
- plant and machinery	-	-
- other including land and buildings	50	43

The company audit fee is £8,500 (2005: £8,000).

6. Employees

	2006 No.	2005 No.
Average monthly number of employees, including directors:		
Production	29	20
Selling and research	7	6
Administration	6	5
	42	31

	2006 £'000	2005 £'000
Staff costs, including directors:		
Wages and salaries	1,112	932
Social security costs	137	74
Other pension costs	16	9
	1,265	1,015

7. Directors' Remuneration

	Salary and fees £'000	Benefits in kind £'000	2006 Total £'000	2005 Total £'000
G G Watt	71	-	71	71
Dr R J Chignell	46	9	55	55
R G Tallentire	47	-	47	30
R MacDonnell	4	-	4	-
Aggregate emoluments	168	9	177	156

Directors' pensions

	2006 No.	2005 No.
The number of directors who are accruing retirement benefits under:		
- defined contributions policies	1	1

Company contributions to directors' defined contribution policies

	2006 £'000	2005 £'000
Dr R J Chignell	9	9

Directors' share options

	No. of options				
	At start of year	Granted during year	At end of year	Exercise price	Date from Which exercisable
G G Watt	250,000	-	250,000	14.5p	10-Dec-05
G G Watt	100,000	-	100,000	20.0p	18-Nov-06
R J Chignell	100,000	-	100,000	20.0p	18-Nov-06
R J Chignell	-	100,000	100,000	13.5p	14-Nov-08
R G Tallentire	40,000	-	40,000	14.5p	20-Dec-05
R G Tallentire	5,000	-	5,000	20.0p	18-Nov-07
R G Tallentire	200,000	-	200,000	12.0p	9-Dec- 07
R G Tallentire	-	100,000	100,000	13.5p	14-Nov-08
R MacDonnell	-	100,000	100,000	24.0p	2-May-09

The Company's share price at 30 June 2006 was 26.0p. The high and low during the period under review were 27.25p and 7.25p respectively.

In addition to the above, in consideration of loans made to the company, G G Watt has warrants over 2,068,965 at an exercise price of 14.5p and 3,703,703 at an exercise price of 13.5p.

8 Taxation

	2006 £'000	2005 £'000
United Kingdom Corporation Tax		
Current taxation	(70)	(80)
Adjustments in respect of prior years	1	(17)
	(69)	(97)
Deferred taxation	-	-
Tax on loss on ordinary activities	(69)	(97)

Current tax reconciliation	2006 £'000	2005 £'000
Profit/(loss) on ordinary activities before taxation	72	(394)
Theoretical tax at UK corporation tax rate 30% (2005: 30%)	21	(117)
Effects of:		
- losses brought forward	(93)	(26)
- joint ventures' losses unrelieved	(6)	8
- R&D tax credit adjustments	15	27
- other expenditure that is not tax deductible	2	4
- adjustments in respect of prior years	12	(17)
- accelerated capital allowances	(3)	24
- losses carried forward	15	-
- short term timing differences	(32)	-
Actual current taxation charge	(69)	(97)

The Group has tax losses amounting to approximately £839,000 (2005: £687,000), available for carry forward to set off against future trading profits.

9. Profit per Share

This has been calculated on profits of £141,000 (2005: loss £297,000) and the number of shares used was 24,245,068 (2005: 23,203,808) being the weighted average number of shares in issue during the year.

10. Intangible Assets

Group

	Goodwill £'000	Trade marks £'000	Total £'000
Cost:			
At 1 July 2005	283	7	290
Additions	907	-	907
At 30 June 2006	1,190	7	1,197
Amortisation			
At 1 July 2005	42	7	49
Charge for the year	27	-	27
At 30 June 2006	69	7	76
Net book value			
At 30 June 2006	1,121	-	1,121
At 30 June 2005	241	-	241

The goodwill on acquisition of Adien Limited and QM Systems Limited is being amortised over 20 years.

11. Tangible Fixed Assets

Group	Equipment, fixtures and fittings £'000	Leasehold improvements £'000	Motor vehicles £'000	Total £'000
Cost				
At 1 July 2005	738	80	90	908
QM Systems Ltd acquisition	87	-	-	87
Additions	192	-	5	197
At 30 June 2006	1,017	80	95	1,192
Depreciation				
At 1 July 2005	543	72	54	669
QM Systems Ltd acquisition	35	-	-	35
Charged in period	103	8	23	169
At 30 June 2006	681	80	77	838
Net book value				
At 30 June 2006	336	-	18	354
At 30 June 2005	223	8	8	239

The net book value of the tangible fixed assets includes £127,292 (2005: £nil) in respect of assets held under hire purchase agreements. Depreciation charged in the period on those assets amounted to £9,408 (2005: £nil).

11. *Tangible Fixed Assets (continued)*

Company

	Equipment, fixtures and fittings £'000	Leasehold improvements £'000	Total £'000
Cost			
At 1 July 2005	195	45	240
Additions	1	-	1
At 30 June 2006	196	45	241
Depreciation			
At 1 July 2005	183	37	220
Charged in period	5	8	13
At 30 June 2006	188	45	233
Net book value			
At 30 June 2006	8	-	8
At 30 June 2005	12	8	20

12. *Investment in Joint Venture*

Group

	Investment in shares £'000
Cost:	
At 1 July 2005 & 30 June 2006	198
Share of profit/losses	
At 1 July 2005	(202)
Share of profit (losses) for the year	19
At 30 June 2006	(183)
Net investment	
At 30 June 2006	15
At 30 June 2005	(4)

The investment in joint venture relates to a 36% shareholding in the ordinary share capital of SUMO Limited. SUMO Limited is engaged in the development of a GPR franchise operation and has a year end of 31 December. For the purpose of preparing this consolidation, financial information has been prepared for the year ended 30 June 2006.

13. Fixed asset investments

Company	Investments in joint ventures £'000 (note 12)	Investments in subsidiaries £'000	Total £'000
Cost			
At 1 July 2005	198	399	597
Additions	-	798	798
At 30 June 2006	198	1,197	1,395
Provisions			
At 1 July 2005 and 30 June 2006	-	-	-
Net book value			
At 30 June 2006	198	1,197	1,395
At 30 June 2005	198	399	597

Principal trading subsidiaries	Parent and group interest in ordinary shares and voting rights	Country of incorporation	Principal activity
Adien Limited	100%	England & Wales	Specialist surveying
QM Systems Limited	100%	England & Wales	Test solutions

QM Systems Limited contributed £250,000 to the group's net operating cash flows, received £2,000 in respect of net returns on investments and servicing of finance, paid £nil in respect of taxation and utilised £nil for capital expenditure and financial investment.

The purchase of QM Systems Limited was achieved through the issue of shares.

13. Fixed asset investments (continued)

On 22 March 2006, the company acquired the entire issued share capital of QM Systems Limited, a company specialising in providing test solutions. No fair value adjustments were made and the company's assets and liabilities at the date of acquisition were:

	£'000
Tangible fixed assets	52
Stock	1,047
Debtors	384
Cash at bank	270
Creditors: amounts falling due within one year	(1,844)
Creditors: amounts falling due after more than one year	(18)
Net assets acquired	(109)
Goodwill	907
Cost of acquisition	798
Consideration: shares	747
Acquisition expenses	51
Cost of acquisition	798

QM Systems Limited – results prior to acquisition	Period from 1 August 2005 to 22 March 2006 £'000	Year to 31 July 2005 £'000
Turnover	572	2,052
Operating profit	(78)	212
Profit before tax	(74)	229
Profit after tax	(74)	227

14. Stocks

	Group		Company	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Raw materials	97	121	95	115
Long term work in progress	520	12	-	-
Short term work in progress	40	-	-	-
Finished goods	100	130	100	130
	757	263	195	245

The replacement cost of the above stocks would not be significantly different from the values stated.

15. Debtors

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Due within one year				
Trade debtors	767	338	59	3
Amounts owed by group undertakings	-	-	-	285
Other debtors	106	89	104	78
Prepayments and accrued income	47	42	9	39
	920	469	172	405

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Due after one year				
Trade debtors	49	-	49	-
	49	-	49	-
Total	969	469	221	405

16. Creditors: Amounts falling due within one year

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Borrowings (note 19)	413	615	226	715
Trade creditors	310	207	149	171
Other taxation and social security	204	121	-	2
Other creditors	49	11	-	-
Payments received on account	926	-	-	-
Accruals	186	306	162	261
Amounts due to group undertakings	-	-	65	-
	2,088	1,260	602	1,149

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

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Borrowings (note 19)	602	111	500	-

18. Provisions for liabilities and charges

Deferred taxation

Group

	Provided		Unprovided	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Fixed asset timing differences	-	-	7	(21)
Other timing differences	-	-	(3)	(21)
Losses or other deductions	-	-	(250)	(164)
	-	-	(246)	(206)

Company

	Provided		Unprovided	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Fixed asset timing differences	-	-	(17)	(21)
Other timing differences	-	-	-	(21)
Losses or other deductions	-	-	(188)	(173)
	-	-	(205)	(215)

19. Borrowing Analysis

	Group		Company	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Due within one year				
Bank overdraft	258	150	218	316
Bank loans	76	66	-	-
Directors' loans	38	349	8	399
Other loans	-	50	-	-
Obligations under finance lease agreements	41	-	-	-
	413	615	226	715
Due after more than one year				
Bank loans	41	111	-	-
Obligations under finance lease agreements	61	-	-	-
Directors' loans	500	-	500	-
	602	111	500	-
Repayable				
Due within 1 year	413	615	226	715
Over 1 but less than 2 years	82	111	-	-
Over 2 but less than 5 years	520	-	500	-
	1,015	726	726	715

Bank loans include loans from Barclays £106,982 (2005: £171,909), Lloyds TSB £nil (2005: £4,999), HSBC £10,223 (2005: £nil).

The Barclays loan is at a rate of 3% over base rate and is repayable in monthly instalments, the final payment being made in September 2007. The HSBC loan was repaid in full in September 2006. The finance lease agreements are with Barclays Asset Finance Limited at a rate of 4.5% over base rate.

Director's loans from G G Watt of £500,000 falls due for repayment in December 2008. Director's loans have also been received from R G Tallentire during the year. Both loans attract interest at 2.15% over Bank of England base rate.

	2005	Repaid in the year	Received in the year	2006
	£'000	£'000	£'000	£'000
G G Watt	349	-	151	500
R G Tallentire	-	-	38	38
	349	-	189	538

20. Financial Instruments

The Group's treasury policy is to control operations centrally by arranging borrowings, investing surplus funds and managing and reducing financial risks. The Group does not use derivative instruments.

Financial Liabilities
All financial liabilities attract interest at floating rates.

Fair Values
There is no material difference between the fair values and book values of the financial assets and liabilities of the Group.

Financial Liabilities: excluding non-debt current liabilities
The interest rate profile at 30 June 2006 was:

	Floating rate £'000	Fixed rate £'000	Total £'000
Sterling	1,015	-	1,015

The interest rate profile at 30 June 2005 was:

	Floating rate £'000	Fixed rate £'000	Total £'000
Sterling	726	-	726

The interest and repayment terms of these financial liabilities are shown in note 18. The floating rate sterling borrowings are linked to the Bank of England base rate.

Maturity analysis of financial liabilities
This is shown in note 19.

Foreign currency
The majority of Group transactions are denominated in sterling, with approximately 5% being denominated in foreign currencies.

Undrawn borrowing facilities
The Group had undrawn borrowing facilities of £2,000 at 30 June 2006 (2005: £50,000). These facilities expired in July 2006 and have been extended and renewed. G G Watt has guaranteed the overdraft.

21. Share Capital

	2006 No	2006 £'000	2005 No	2005 £'000
Authorised				
Ordinary shares of 1p each	40,000,000	400	40,000,000	400
Allotted and fully paid				
Brought forward	23,203,808	232	23,203,808	232
Issued during the year	3,480,000	35	-	-
Carried forward	26,683,808	267	23,203,808	232

21. Share Capital (continued)

On 13 April 2005, JM Finn & Co were issued with a warrant to subscribe for 750,000 Ordinary Shares exercisable at a price of 10.5p per share at any time during the period to 12 April 2010. 230,000 of these warrants were exercised on 18 May 2006 and a further 210,000 were exercised on 17 July 2006.

In addition to the 995,000 share options held by directors, options over ordinary shares have been granted under the Company's share option scheme for staff, such that at 30 June 2006 the following options to subscribe for ordinary shares of 1p each were outstanding.

Date Options Exercisable	Number of Shares	Exercise Price
Between December 2003 and December 2010	15,000	52p
Between December 2004 and December 2011	12,500	43p
Between December 2005 and December 2012	10,000	45p
Between December 2006 and December 2013	142,500	14.5p
Between December 2007 and December 2014	80,000	20p
Between December 2008 and December 2015	122,500	13.5p

22. Reserves

	Share premium *account* £'000	**Profit and loss *account* £'000**
Group		
At 1 July 2005	4,081	(4,476)
Profit for the year	-	141
Share issue	734	-
At 30 June 2006	4,815	(4,335)
Company		
At 1 July 2005	4,081	(4,195)
Loss for the year	-	(170)
Share issue	734	-
At 30 June 2006	4,815	(4,365)

23. Reconciliation of Movements in Shareholders' Funds

	2006 £'000	**2005 £'000**
Group		
Total recognised gains and losses relating to the year	141	(297)
Net proceeds of shares issued	769	-
Increase/(decrease) in shareholders' funds	910	(297)
Opening shareholders' funds	(163)	134
Closing shareholders' funds	747	(163)

24. Reconciliation of Operating Loss to Net Cash Outflow from Operating Activities

	2006 £'000	2005 £'000
Operating profit/(loss)	93	(314)
Amortisation of intangible assets	27	14
Depreciation of tangible fixed assets	169	169
Working capital movements		
Stock and work in progress	65	17
Debtors	(323)	(182)
Creditors	102	170
Net cash inflow/(outflow) from operating activities	133	(126)

25. Reconciliation of Net Cash Flow to Movement of Net Debt

	2006 £'000	2005 £'000
Increase in cash	113	47
Increase in debt and finance lease agreements	(171)	(175)
Decrease/(Increase) in net debt from cash flows	(58)	(128)
Debt acquired with subsidiary	(10)	-
(Increase)/Reduction in net debt	(68)	(128)
Opening net debt	(726)	(598)
Closing net debt	(794)	(726)

26. Analysis of Changes in Net Debt

	1 July 2005 £'000	Cashflow £'000	Acquisition of subsidiary	30 June 2006 £'000
Cash at bank and in hand	-	-	221	221
Bank overdraft	(150)	(108)	-	(258)
Cash	(150)	(108)	221	(37)
Loans	(576)	(69)	(10)	(655)
Finance leases	-	(102)	-	(102)
Borrowings	(576)	(171)	(10)	(757)
Net debt	(726)	(279)	211	(794)

27. Financial Commitments

	2006	2005
Group	**£'000**	**£'000**
Capital commitments		
Capital expenditure commitments contracted for, but not provided in the financial statements were as follows:	-	-

Operating lease commitments
The payments which the company is committed to make in the next year under operating leases are as follows:

	2006	2005
Land and buildings – lease expiring		
- within one year	2	2
- one to five years	28	28
- beyond five years	-	-
	30	30

28. Related Party Transactions

Directors' loan disclosures are given in note 19. The interest payable to directors in respect of their loans during the year was:

G G Watt £22,387 (2005: £20,685)

During the year ended 30 June 2006, there were the following transactions with SUMO Limited and SUMO Services Limited, a subsidiary of the joint venture company SUMO Limited.

	£'000
Sales	62,701

As at 30 June 2006, there was an amount of £53,486 (2005: £3,402) due from SUMO Limited and £54,955 (2005: £76,032) from SUMO Services Limited.