Surface Transforms plc

Annual Report and Financial Statements
Registered number 3769702
31 May 2008

Contents

Highlights

- Revenue increased by 90% to £508,111 *(2007 £266,789)*
- Losses after taxation improved by 8% to £594,065 *(2007 £646,422)*
- Cash position as at 31 May 2008 of £1,112 719 *(2007 £878,971)*
- Order Book of £302,124 (as at 31 May 2008)
- Receipt of a 4 year, £300 000 to £400,000 per annum initial contract with a leading, global, brake systems group for the supply of carbon fibre brake discs
- Mov'it has signed a further supply agreement with the Company to purchase between £300,000 to £400,000 of brake discs per annum
- Award of a £150 000 3 year development contract with MBDA a world leading missile manufacturer jointly owned by BAE Systems EADS and Finmeccanica
- Unit costs of ceramic brake discs are now 20%lower than levels in May 2007
- The commencement of a development contract with a new, US based aircraft brake system supplier which currently supplies both commercial and defence aircraft
- Fundraising amounting to £897 000 net of expenses by the issue of new ordinary shares at 20 pence per share as announced in July 2007

Chairman's statement

In the 12 months to 31 May, 2008 the Company has achieved its financial targets for the year and has also met a number of the strategic and operating milestones that the management had set themselves

The Company started the 2008/09 financial year with a record order book, four automotive brake systems clients that are ordering brake discs on a regular basis and improved prospects for further growth in the business The key achievements for the period under review were

- Receipt of a 4 year, £300,000 to £400,000 p a initial contract with a leading, global, brake systems group for the supply of carbon fibre brake discs
- Award of a £150,000, 3 year development contract with MBDA, a world leading missile manufacturer jointly owned by BAE Systems, EADS and Finmeccanica
- Unit costs of ceramic brake discs are now 20% lower than levels in May 2007
- The commencement of a development contract with a new, US based aircraft brake system supplier which currently supplies both commercial and defence aircraft
- Fundraising amounting to £897,000 net of expenses by the issue of new ordinary shares at 20 pence per share as announced in July 2007

FINANCIAL REVIEW

In the 12 months to 31 May 2008 revenue was £508,111 *(2007 £266,789)* This represents a 90% increase on the same period in 2007 Increased automotive brake disc revenues account for most of the increase and now represents over 80% of the Company's revenue

At 31 May 2008 the outstanding order book was £302,124 *(2007 £126,097)*

Losses after taxation for the 12 months period were £594 065 *(2007 £646,422)*

Earnings per share was a loss of 3 33 pence per share *(2007 4 61pence per share)*

During the year the Company raised £897 000 by way of an issue of ordinary shares at 20 pence per share Shareholder funds at 31 May 2008 were £1,722,839 *(2007 £1,413,058)* and this included cash deposits of £1,112 719 *(2007 £878,971)*

Capital expenditure during the year amounted to £142,599 *(2007 £193,382)*

The Company has no borrowings

DEVELOPMENTS

At present, the Company is currently in advanced discussions regarding a supply contract with a leading European supplier of braking systems to the after-market industry A further announcement regarding this will be made in due course

In addition, in April 2008, the Company signed a four year supply agreement to supply carbon fibre brake discs to a global automotive brake system supplier

The directors believe, based on forecasts prepared by the brakes system supplier, that this contract could generate additional revenues of approximately £300,000 to £400,000 per annum over the life of the agreement and that the Company has sufficient manufacturing capacity to meet this demand This agreement demonstrates that Surface Transforms has the expertise in advanced carbon fibres and industrial fabrics which can provide a competitive

Chairman's statement *(Continued)*

DEVELOPMENTS (Continued)

edge in composite brake technology and takes the Company's leading-edge products into the forefront of the international automotive performance brake market

PEOPLE

The Board would like to thank management and staff who have all contributed to the progress the Company has made during the year We continue to incentivise executives with share options as we wish to align their rewards with those of shareholders

OUTLOOK

We envisage further progress during the coming year

The Board believes that Surface Transforms has established itself as an industry operator with world class technology The commercial and development contracts which have been signed in the past year underline this reputation

In spite of the widely reported slowdown in world consumer and industrial markets, the Company continues to improve its order book The Board anticipates that the revenue growth experienced in 2008/09 will continue

Kevin D'Silva
Chairman

23 September 2008

Chief executive's report

The Company has completed its first year of operations at the new Ellesmere Port site and the relocation which consolidated the activities of two previous sites has delivered measurable improvements in productivity and management team coordination

Over the year the business has gained more stability in its revenues and over 80% of revenues derived from automotive applications In addition 69% of the revenue produced in the year has arisen from Continental European markets

The business in 2008 had 11 OEM and after market automotives clients 3 in aircraft brake systems and 3 in rocket components

AUTOMOTIVE BRAKE SYSTEMS

The Company's SystemST brake disc product is now on 28 car platforms to date and such cars are typically priced in excess of €90,000 The main car platforms using SystemST in 2008 were

Koenigsegg Automotive (*www Koenigsegg sw*)
SystemST brake discs are now on over 40 supercars and current production is between 24 – 30 cars per year

Mov'it Gmbh (*www movit de*)
Mov'it is a leading European after market brake system supplier Sales of SystemST have exceeded expectations this year On 22 September 2008 Mov'it signed a further supply agreement with the Company to purchase a minimum of £300,000 to £400,000 brake discs per annum

Weber Sport (*www Weber sw*)
Weber now has an established distributor network and will commence production this Autumn, targeting to build between five and eight of the €1,000,000 price tagged supercars in the first year

Tramontana (*www Tramontana sp*)
Tramontana, the Spanish supercar manufacturer build just 12 cars per annum and purchased six ceramic brake car systems last year

MM Industries Avocet
The MMI Avocet is a newly built British sports car, launched to great interest on the ST Stand at Autosport 2008 at the NEC Birmingham in January, the 225hp Spyder version will be fitted with SystemST as standard Final production volume forecasts have not yet been released by MMI

In April 2008, the Company signed a four year supply agreement to supply carbon fibre brake discs to a global automotive brake system supplier

The directors believe, based on forecasts prepared by the brakes system supplier, that this contract could generate additional revenues of approximately £300 000 to £400,000 per annum over the life of the agreement and that the Company has sufficient manufacturing capacity to meet this demand This agreement demonstrates that Surface Transforms has the expertise in advanced carbon fibres and industrial fabrics which can provide a competitive edge in composite brake technology, and takes the Company's leading-edge products into the forefront of the international automotive performance brake market

Chief executive's report *(continued)*

On 22 September 2008 Mov'it Gmbh already an established customer of the Company, signed a new Supply and Purchase contract to purchase annually, ceramic brake discs at a much higher level of volumes than had been experienced in the previous year The Board believes that this will amount to revenues in excess of between £300 000 and £400,000 per annum

AEROSPACE

Aircraft Brake Systems

Revenues from aircraft brake systems are principally from paid development contracts Revenues in 2008 in this area have reduced in value from the previous year One of our clients Dunlop Braking Systems a subsidiary of Meggitt plc has now merged with a key US competitor and the combined operations now trade under Meggitt Aircraft Braking Systems (MABS)

MABS has been and remains a key partner of the £1 34 million, three year collaborative R&D project funded by the UK Technology Strategy Board (formerly the DTI) This project is being led by Surface Transforms

In recent months, development work has commenced with a second US brake system supplier that supplies both commercial and military aircraft principally in US markets

Rocket Components

Surface Transforms proprietary technology is uniquely positioned to deliver high performance (in terms of extended life time and reduced mass) affordable ceramic rocket propulsion components

The award of a £150 000 3 year development contract with MBDA, a world leading missile manufacturer jointly owned by BAE Systems EADS and Finmeccanica recognises the potential for Surface Transform's material technology

In addition interest from other defence contractors has been shown and the Board believe progress during this financial year will lead to further development agreements

PRODUCTION & NEW TECHNOLOGY PROJECTS

The development of CVIST the carbon vapour infiltration process plant has taken longer than had been expected Technical challenges have arisen with the process plant capabilities and this has prolonged final commissioning We now believe we are in the final stages of commissioning and expect production parts to be manufactured during the second half of the current financial year

Improved machining and finishing operations in the manufacture of brake discs has contributed to the reduction in the unit cost of a ceramic brake disc Cost levels currently are 20 per cent below levels of May 2007 and the CVIST process will contribute further to lowering unit costs

PEOPLE

The Company has a strong senior management team who have now worked together for over two years

This year we have taken the opportunity to appoint two new senior engineers, Geoff Whitfield BSc MSc, and Martin Bell BEng (Hons) MIET to the management organisation

The blend of skills, experience and commitment has allowed the Company to build solid foundations and the team are well equipped to continue the good progress made to date

We have continued to incentivise our management and staff with share options as we wish to align their rewards with those of shareholders

I would like to thank all my colleagues for their dedication over the past year

Dr Kevin Johnson
Chief Executive

23 September 2008

Directors' report

The directors present their annual report and the audited financial statements for the year ended 31 May 2008

Principal activity

The principal activity of the Company during the year was the development and manufacture of carbon fibre reinforced ceramic products (CFRC) for aircraft brake automotive brake and rocket component applications

Business review

A review of the Company's activities during the year is dealt with in the financial review section of the Chairman's statement

Key risks and uncertainties

The principal risk faced by the Company is unchanged from last year and relates to the speed at which our customers and potential customers adopt the new ceramic disc technology Indications in the automotive area are that the technology continues to be well received and is being adopted over an increasing number of vehicles This risk is constantly assessed by monitoring the level of enquiries and orders for both the Company and industry wide

Key performance indicators

The Directors continue to monitor the business internally with a number of performance indicators order intake sales output profitability and manufacturing cost of automotive discs The Company has met its performance targets in each of these areas as evidenced below

- Turnover £508,111 *(2007 £266,789)*
- Losses after taxation £594,065 *(2007 £646,422)*
- Order Book of £302,124 (as at 31 May 2008)
- Manufacturing cost of automotive discs as at July 2008, 20% below levels of May 2007

The Company produces an annual business plan and full monthly forecasts detailing sales, profitability and cash flow to help monitor business performance going forward

Future developments

The Board aims to continue with its corporate strategy which is to exploit its technologies in carbon fibre reinforced ceramics by

- establishing contract development opportunities and collaborations with national and multi-national customers in the aerospace and automotive industries and
- expanding commercial sales of CFRC products

Research and development

The majority of the Company's staff are employed in research and development activities which are concentrated on the ongoing development of carbon fibre reinforced ceramic friction and non-friction materials for new products and applications

Proposed dividend and transfer to reserves

The loss for the year after taxation amounted to £594,065 *(2007 £646,422)* The directors do not recommend the payment of a dividend

Policy and practice on payment of payables

It is the Company's policy that payments to suppliers are made in accordance with the terms and conditions agreed between the Company and its suppliers, providing that all trading terms and conditions have been complied with The Company does not follow any code or standard on payment practice

At the year end there were 53 days *(2007 74 days)* purchases in trade payables

Directors' report *(continued)*

Political and charitable donations

The Company made no political or charitable donations during the year *(2007 £nil)*

Directors and directors' interests

The directors who held office during the year were as follows

K D'Silva* (Chairman)
Dr K Johnson (Managing Director)
JJ Faria*
Professor DT Clark*
Dr G Gould
KM Baker*

* denotes non-executive Director

JJ Faria resigned as an executive director on 30 November 2007 and was immediately appointed as a non-executive director

The directors retiring by rotation are K D'Silva and JJ Faria who, being eligible, offer themselves for re-election

The directors who held office at the end of the financial year had the following interests in the ordinary shares of the Company according to the register of directors' interests

	% of issued share capital at end of year	Number of £0.01 ordinary shares Interest at end of year	Interest at start of year
JJ Faria	9 71	1,848,089	1,848,089
Professor DT Clark	5 15	979,661	979,661
K D'Silva	1.35	256,986	156,986
Dr K Johnson	0 42	79,750	79,750
KM Baker	0.47	90,000	40,000
Dr G Gould	0.02	4,350	4,350

According to the register of directors' interests, no rights to subscribe for shares in or debentures of the Company were granted to any of the directors or their immediate families, or exercised by them during the financial year, except as disclosed in the report on directors' remuneration on pages 10 and 11

The directors benefited from qualifying third party indemnity provisions in place during the financial year and at the date of this report

Substantial shareholders

In addition to the directors' interests noted above, the directors are aware of the following who were interested in 3% or more of the Company's equity as of 5 September 2008

Registered holding	Number of ordinary shares	% of issued share capital
JM Finn Nominees Limited	3,983,860	20 93%
Pershing Nominees Limited	1,675,000	8 80%
Octopus Investments Nominees	1,006,292	5 29%
HSBC Global Custody (Nominee) Ltd	807,143	4 24%
Sinjul Nominees Ltd	730,000	3 84%

Directors' report *(continued)*

Corporate governance

Surface Transforms plc is committed to maintaining high standards of corporate governance The Company complies with the Combined Code as modified by the recommendations of the Quoted Companies Alliance to the extent the directors consider appropriate, given the size of the Company, its current stage of development and the constitution of the Board

The Board has appointed an Audit Committee whose primary role is to review the Company's interim and annual financial statements before submission to the Board for approval The Board has also appointed a Remuneration Committee, which is responsible for reviewing executive remuneration and performance The Remuneration and Audit Committees are made up of four non-executive directors, David Clark, Julio Faria, Kevin D'Silva and Ken Baker Details of the Remuneration Committee are disclosed in the report on directors' remuneration on pages 10 and 11

International Financial Reporting Standards ('IFRS') as adopted by the EU

The Company has successfully applied IFRS as adopted by the EU, and a restatement report is included in these financial statements

Disclosure of information to auditors

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

Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of KPMG Audit Plc as auditors of the Company is proposed at the forthcoming Annual General Meeting

Post balance sheet event

On 22 September 2008 Mov'it Gmbh, already an established customer of the Company, signed a new Supply and Purchase contract to purchase annually, ceramic brake discs at a much higher level of volumes than had been experienced in the previous year The Board believes that this will amount to revenues in excess of between £300,000 and £400,000 per annum

ANNUAL GENERAL MEETING

The notice convening the Annual General Meeting to be held at 11 30am on 28 October 2008 at the offices of Halliwells LLP, 3 Hardman Square, Spinningfields, Manchester M3 3EB is set out on pages 40 to 44

SPECIAL BUSINESS AT THE ANNUAL GENERAL MEETING

Under resolution 6, it is proposed in accordance with section 80 of the Companies Act 1985, to renew the directors' authority to allot shares in the Company up to a nominal amount of £63,436, representing approximately 33% of the issued share capital of the Company

Resolution 7 seeks to renew, in accordance with section 89 of the Companies Act 1985, the directors' authority to allot further shares for cash without first offering them to existing shareholders under the statutory pre-emption procedure This authority is limited to the issue of equity securities in connection with rights issues and otherwise up to a nominal amount of £19,031, representing approximately 10% of the Company's present issued share capital

Directors' report *(continued)*

SPECIAL BUSINESS AT THE ANNUAL GENERAL MEETING *(Continued)*

The authorities contained in resolutions 6 and 7 will both expire at the conclusion of the annual general meeting of the Company to be held in 2008 or 15 months after the passing of such resolutions (whichever is the earlier)

The directors consider that it is appropriate for these authorities to be granted It is not the directors' present intention to allot any ordinary shares except to satisfy options that may be exercised under the Company's share option schemes

By order of the Board

K D'Silva
Chairman

23 September 2008

Unit 4
Olympic Park
Poole Hall Road
Ellesmere Port
Cheshire
CH66 1ST

Report on directors' remuneration

Policy on executive directors' remuneration

The Remuneration Committee comprises of Kevin D'Silva, Julio Faria, David Clark and Ken Baker

The Remuneration Committee is responsible for reviewing and determining the Company's policy on executive remuneration (including the grant of options under the Share Option Scheme) and ensuring compliance with and implementation by the Company, as far as reasonably practicable, the recommendations and guidelines of the Combined Code Executive remuneration packages are designed to ensure the Company's executive directors and senior executives are fairly rewarded for their individual contributions to the Company

Fees for non-executive directors

The fees for non-executive directors are determined by the Board The non-executive directors are not involved in the decisions about their own remuneration

Directors' remuneration

Set out below is a summary of the fees and emoluments received by all directors for the year or, where applicable, period of office

	2008	2007
	£	£
Executive directors		
Dr K Johnson	84,399	74,886
JJ Faria*	30,049	57,966
Dr G Gould	53,943	52,890
	168,391	185,742
Non-executive directors		
K D'Silva	18,000	18,000
Professor DT Clark	18,253	20,854
JJ Faria*	9,000	-
KM Baker	18,000	13,500
	63,253	52,354
	231,644	238,096

With the exception of Kevin Johnson, none of the directors received pension contributions in respect of their office In addition to the emoluments received, as stated above, Kevin Johnson received £3,898 (*2007 £3,600*) in respect of pension contributions

*JJ Faria resigned as an executive director on 30 November 2007 and was immediately appointed as a non-executive director

Directors' interests

Details of any contracts in which a director has a material interest are disclosed in note 18

None of the directors received any remuneration or benefits under long term incentive schemes

Report on directors' remuneration *(continued)*

Share options

The Company operates a share incentive scheme All options are granted at the discretion of the Board The options granted, date of grant, exercise price and exercise periods under the scheme are set out below No options were granted during the year

None of the directors exercised options during the year Directors' options outstanding and the options which were granted and expired during the year are as follows

Enterprise Management Incentive Scheme

Director	Date of Grant	Number of Share options granted	Number of Share options expired	Exercise Price	Exercise Period	Expiry Date
JJ Faria	19/12/02	64,286	-	£0 70	19/12/05-19/12/12	19/12/12
Dr G Gould	19/12/02	64,286	-	£0 70	19/12/05-19/12/12	19/12/12
Dr G Gould	08/12/03	34,091	-	£0 88	08/12/06-08/12/13	08/12/13
Dr G Gould	08/03/04	20,000	-	£0 665	08/03/07-08/03/14	08/03/14
Dr G Gould	14/09/05	29,000	-	£0 40	14/09/08-14/09/15	14/09/15
Dr G Gould	18/04/07	50,000	-	£0 21	18/04/10-18/04/17	18/04/17
Dr K Johnson	04/04/05	50,000	-	£0 50	04/04/08-04/04/15	04/04/15
Dr K Johnson	14/09/05	180,000	-	£0 40	14/09/08-14/09/15	14/09/15
Dr K Johnson	18/04/07	100,000	-	£0 21	18/04/10-18/04/17	18/04/17
Prof DT Clark	18/04/07	15,000	-	£0 21	18/04/10-18/04/17	18/04/17
KA D'Silva	18/04/07	50,000	-	£0 21	18/04/10-18/04/17	18/04/17
KM Baker	18/04/07	15,000	-	£0 21	18/04/10-18/04/17	18/04/17
		671,663				

The market price of the shares at 31 May 2008 was £0 1475 and during the year varied from £0 225 to £0 105

By order of the Board

K D'Silva
Chairman

23 September 2008

Unit 4
Olympic Park
Poole Hall Road
Ellesmere Port
Cheshire
CH66 1ST

Statement of directors' responsibilities in respect of the annual report and the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year Under that law they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable laws

The financial statements are required by law to present fairly the financial position and the performance of the Company, the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation

In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgments and estimates that are reasonable and prudent
- state whether they have been prepared in accordance with IFRSs as adopted by the EU, 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 enable them to ensure that its financial statements comply with the Companies Act 1985 They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities

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

KPMG Audit Plc
St James' Square
Manchester M2 6DS
United Kingdom

Independent auditors' report to the members of Surface Transforms plc

We have audited the financial statements of Surface Transforms plc for the year ended 31 May 2008 which comprise the Income Statement, the Statement of Changes in Equity, the Balance Sheet, the Cash Flow Statement and the related notes These financial statements have been prepared under the accounting policies set out therein

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

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 12

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 whether the financial statements have been properly prepared in accordance with the Companies Act 1985 We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements The information given in the Directors' Report includes that specific information presented in the Chairman's Statement that is cross referred from the Business Review section of the Directors' Report

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

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the 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 judgments 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

Independent auditors' report to the members of Surface Transforms plc
(continued)

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 IFRSs as adopted by the EU, of the state of the Company's affairs as at 31 May 2008 and of its loss for the year then ended,
- the financial statements 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

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor

23 September 2008

Income Statement
for the year ended 31 May 2008

	Note	2008	2007
		£	£
Revenue	2	**508,111**	266,789
Cost of sales		**(252,874)**	(138,955)
Gross profit		**255,237**	127,834
Administrative expenses			
Before research costs		**(678,078)**	(586,643)
Research costs		**(615,617)**	(560,005)
Total administrative expenses		**(1,293,695)**	(1,146,648)
Other operating income	3	**220,652**	176,530
Operating loss		**(817,806)**	(842,284)
Financial income	6	**67,347**	59,845
Loss before tax		**(750,459)**	(782,439)
Taxation	7	**156,394**	136,017
Loss for the year	15	**(594,065)**	(646,422)
Loss per ordinary share			
Basic and diluted	19	**(3 33p)**	**(4 61p)**

All amounts relate to continuing activities

Statement of Changes in Equity
as at 31 May 2008

2007	Share Capital	Share premium account	Capital reserve	Profit and loss account	Total
	£	£	£	£	£
Credit in relation to share based payments	-	-	-	62,375	62,375
Net income recognised directly to equity	-	-	-	62,375	62,375
Loss for the year	-	-	-	(646,422)	(646,422)
Total recognised income and expense	-	-	-	(584,047)	(584,047)
Opening shareholders funds at 1 June 2006	140,308	4,902,715	463,885	(3,509,803)	1,997,105
Closing shareholders funds at 31 May 2007	140,308	4,902,715	463,885	(4,093,850)	1,413,058

2008	Share Capital	Share premium account	Capital reserve	Profit and loss account	Total
	£	£	£	£	£
Credit in relation to share based payments	-	-	-	56,609	56,609
Net income recognised directly to equity	-	-	-	56,609	56,609
Loss for the year	-	-	-	(594,065)	(594,065)
Issue of new shares	50,000	847,237	-	-	897,237
Total recognised income and expense	50,000	847,237	-	(537,456)	359,781
Opening shareholders funds at 1 June 2007	140,308	4,902,715	463,885	(4,093,850)	1,413,058
Closing shareholders funds at 31 May 2008	190,308	5,749,952	463,885	(4,631,306)	1,772,839

Balance sheet
at 31 May 2008

	Note	2008		2007	
		£	£	£	£
Non-current assets					
Intangible assets	8		-		1,886
Property, plant and equipment	9		382,975		289,455
			382,975		291,341
Current assets					
Inventories	10	258,874		212,181	
Trade and other receivables	11	292,923		289,576	
Cash and cash equivalents		1,112,719		878,971	
Total Assets			1,664,516		1,380,728
			2,047,491		1,672,069
Current Liabilities					
Trade and other payables	12	(274,652)		(259,011)	
Total Liabilities			(274,652)		(259,011)
Net assets			1,772,839		1,413,058
Equity					
Share capital	14		190,308		140,308
Share premium	15		5,749,952		4,902,715
Capital reserve	15		463,885		463,885
Retained earnings	15		(4,631,306)		(4,093,850)
Total equity attributable to equity shareholders of the Company			1,772,839		1,413,058

These financial statements were approved by the Board of directors on 23 September 2008 and were signed on its behalf by

K D'Silva
Director

Dr K Johnson
Director

Cash flow statement
for the year ended 31 May 2008

	Note	2008	2007
		£	£
Cash flows from operating activities			
Loss for the year		**(594,065)**	(646,422)
Adjusted for			
Depreciation charge		**49,079**	74,083
Amortisation charge		**1,886**	2,218
Equity settled share-based payment expenses		**56,609**	62,375
Financial income		**(67,347)**	(59,845)
Taxation		**(156,394)**	(136,017)
		(710,232)	(703,608)
Changes in working capital			
Increase in inventories		**(46,693)**	(87,846)
Increase in trade and other receivables		**(3,347)**	(205,441)
Increase in trade and other payables		**15,641**	129,997
		(744,631)	(866,898)
Finance income received	*17*	**67,347**	59,845
Taxation received		**156,394**	136,017
Net cash used in operating activities		**(520,890)**	(671,036)
Cash flows from investing activities			
Acquisition of property, plant and equipment	*17*	**(142,599)**	(193,382)
Net cash used in investing activities		**(142,599)**	(193,382)
Cash flows from financing activities			
Proceeds from issue of share capital		**897,237**	-
Net cash from financing activities		**897,237**	-
Net increase/(decrease) in cash and cash equivalents		**233,748**	(864,418)
Cash and cash equivalents at the beginning of the period		**878,971**	1,743,389
Cash and cash equivalents at the end of the period		**1,112,719**	878,971

Notes

(forming part of the financial statements)

1 Accounting policies

Surface Transforms plc (the Company") is a Company incorporated and domiciled in the UK

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules modified to include revaluation to fair value of certain financial instruments described below

The accounting policies set out below have, unless otherwise stated been applied consistently to all periods presented in these financial statements and in preparing an opening IFRS balance sheet at 1 June 2006 for the purposes of the transition to Adopted IFRSs

Going concern

The financial statements have been prepared on a going concern basis which the directors believe to be appropriate The Company incurred a net loss of £594,065 during the year however the directors are satisfied, based on detailed cash flow projections that sufficient cash is available to meet the Company's needs as they fall due for at least 12 months from the date of signing the accounts In addition revenues are expected to continue to increase in the coming years resulting in the Company becoming profitable in due course

Transition to Adopted IFRSs

The Company is preparing its financial statements in accordance with Adopted IFRS for the first time and consequently has applied IFRS 1 An explanation of how the transition to Adopted IFRSs has affected the reported financial position, financial performance and cash flows of the Company is provided in note 24

IFRS 1 grants certain exemptions from the full requirements of Adopted IFRSs in the transition period The following exemptions have been taken in these financial statements

Share based payments – IFRS 2 is being applied to equity instruments that were granted after 7 November 2002 and that had not vested by 1 June 2006

Share based payments

The share option programme allows employees to acquire shares of the Company The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options The fair value of the options granted is measured using an option pricing model, taking into account the terms and conditions upon which the options were granted The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is only due to share prices not achieving the threshold for vesting

Intangible assets and amortisation

Expenditure on patents is capitalised and amortised to nil by equal annual instalments over the useful economic life of seven and a half years

Property, plant and equipment

Depreciation is provided to write off the cost less the estimated residual value of property, plant and equipment by equal instalments over their estimated useful economic lives as follows

Plant and machinery	-	12 5% - 20% per annum
Fixtures and fittings	-	25% per annum
Motor vehicles	-	25% per annum
Leasehold Improvements	-	Over life of lease

Notes *(continued)*

1 Accounting policies *(continued)*

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency at the foreign exchange rate ruling at the balance sheet date and the gains or losses on translation are included in the income statement

Leases

Operating lease rentals are charged to the profit and loss account on a straight line basis over the period of the lease

Government grants

Revenue grants are credited to the profit and loss account, and included within other operating income, so as to match them with expenditure to which they relate

Post retirement benefits

The Company does not operate a pension scheme, but does contribute to specific employees' personal pension schemes The amount charged to the profit and loss account represents the contributions payable to employees personal pension schemes during the accounting year

Research and development expenditure

Expenditure on research activities is recognised in the income statement as an expense as incurred

Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the Company intends and has the technical ability and sufficient resources to complete development, future economic benefits are probable and if the Company can measure reliably the expenditure attributable to the intangible asset during its development No research costs met the criteria for capitalisation in the current or preceding years

Inventories

Inventories are stated at the lower of cost and net realisable value In determining the cost of raw materials and consumables the purchase price is used For work in progress, cost is taken as production cost, which includes an appropriate proportion of attributable overheads

Taxation

The charge for taxation is based on the loss for the year and takes into account taxation deferred or accelerated arising from temporary differences between the carrying amounts of certain items for taxation and for accounting purposes

Deferred taxation is provided for in full at the tax rate which is expected to apply to the period when the deferred taxation is expected to be realised, including on tax losses carried forward

Deferred taxation assets are recognised only to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised

Research and development tax credits are recognised on a cash received basis as a reduction in the current tax payable as this is when the tax credit is considered recoverable

Cash and cash equivalents

Cash and cash equivalents, for the purpose of the cash flow statement, comprises cash in hand and deposits repayable on demand

Notes *(continued)*

1 Accounting policies *(continued)*

New standards and interpretations that have been endorsed, but which are not yet effective and not early adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 May 2008, and have not been applied in preparing these financial statements

IFRS 8 'Operating Segments' introduces the management approach" to segment reporting IFRS 8, which becomes mandatory for the Company's 2010 financial statements will require the disclosure of segment information based on the internal reports regularly reviewed by the Company's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them Currently the Company presents primary segment information in respect of its business segments (see Note 2)

New standards and interpretations that have not yet been endorsed.

Amendment to IAS 1 'Presentation of Financial Statements A Revised Presentation' If endorsed by the EU this will be applicable to the Company's 2010 financial statements

Amendment to IFRS 2 Share Based Payment Vesting Conditions and Cancellations' If endorsed by the EU this will be applicable to the Company's 2010 financial statements

Revised IAS 23 Borrowing Costs' removes the option to expense borrowing costs and requires that an entity capitalise borrowing costs directly attributable to the acquisition construction or production of a qualifying asset as part of the cost of that asset If endorsed the revised IAS 23 will become mandatory for the Company's 2010 financial statements and will constitute a change in accounting policy for the Company In accordance with the transitional provisions the Company will apply the revised IAS 23 to qualifying assets for which capitalisation of borrowing costs commences on or after the effective date

Amendment to IAS 32 and IAS 1 Puttable Financial Instruments and Obligations Existing on Liquidation' If endorsed by the EU this will be applicable to the Company's 2010 financial statements

Revenue

Revenue comprises income derived from research the supply of carbon fibre structures and carbon fibre reinforced ceramic products Revenue is recognised on transfer to the customer of significant risks and rewards of ownership, generally this will be when goods are despatched to the customer Turnover excludes value added taxes

Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities trade and other receivables cash and cash equivalents, loans and borrowings, and trade and other payables

Trade and other receivables

Trade and other receivables are recognised initially at fair value Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses

Trade and other payables

Trade and other payables are recognised initially at fair value Subsequent to initial recognition they are measured at amortised cost using the effective interest method

Interest rate risk

The Company finances its operations through cash Cash resources are invested to attract the highest rates for periods that do not limit access to these resources

Notes *(continued)*

1 Accounting policies *(continued)*

Liquidity risk

With regard to liquidity, the Company's policy has throughout the year been to ensure that the Company is able at all times to meet its financial liabilities as and when they fall due

Critical accounting estimates

The preparation of financial statements in conformity with adopted IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities income and expenses The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances , the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not already apparent from other sources Actual results may differ from these estimates The estimates and assumptions which have a significant risk of causing a material adjustment to carrying amount of assets and liabilities within the next financial year are discussed below

Impairment of property, plant and equipment
Property, plant and equipment are reviewed for impairment if events or changes in circumstances indicate that the carrying amount of an asset is not recoverable

Provision to write inventories down to net realisable value
The Company makes provisions for obsolescence based on historical experiences and management estimates of future events Actual outcome could vary significantly from these estimates

2 Analysis of turnover and loss on ordinary activities before taxation

Revenue and loss on ordinary activities before taxation is wholly attributable to the principal activity of the Company

Primary reporting format – business segments

Revenue by business segment is analysed as follows

	2008	2007
	£	£
Automotive	**424,413**	216,065
Aerospace	**83,698**	50,724
	508,111	266,789

All business segments are serviced by a single production facility As such, net assets, liabilities, additions to property, plant and equipment, loss before tax and depreciation cannot be attributed to specific business segments

Notes *(continued)*

2 Analysis of turnover and loss on ordinary activities before taxation *(continued)*

Secondary reporting format – Geographical segments

Revenue by destination is analysed as follows

	2008	2007
	£	£
By geographical market:		
United Kingdom	**138,074**	93,270
Rest of Europe	**353,964**	129,522
United States of America	**16,073**	42,897
Rest of World	**-**	1,100
	508,111	266,789

Revenue by origin, net assets and profit before interest and tax all relate to the UK

3 Expenses and auditors remuneration

	2008	2007
	£	£
Operating loss before taxation is stated		
after charging		
Depreciation of owned tangible fixed assets	**49,079**	74,083
Research and development expensed as incurred	**615,617**	560,005
Amortisation of patents and licences	**1,886**	2,218
Rents payable under operating leases – land and buildings	**50,251**	36,463
Exchange losses	**2,294**	412
after crediting		
Exchange gains	**2,164**	988
Government grants	**220,652**	176,530

Notes *(continued)*

3 Expenses and auditors remuneration *(continued)*

Audit of these financial statements	**2008** **£**	2007 £
Amounts receivable by auditors and their associates in respect of		
Audit of financial statements pursuant to legislation	**17,450**	18,725
Other services relating to taxation	**7,242**	7,875

Government grants

Grants received comprise revenue grants from DTI and North West Development Agency

These are subject to making expenditure as stipulated in the grant applications and to audit of the claims There are no unfulfilled conditions or contingencies associated with government assistance received

North West Development Agency grants have been received in full

4 Remuneration of directors

The Company considers key management personnel as defined in IAS 24 "Related party disclosures" to be the directors of the Company The aggregate amount of emoluments paid to directors in respect of qualifying services during the year was £231,644 *(2007 £238,096)* Of this, £84,299 *(2007 £74,886)* was made to the highest paid director and Company pension contributions of £3,898 *(2007 £3,600)* were made to a money purchase scheme on his behalf

Full disclosure of directors' emoluments, share options and directors' pension entitlements which form part of the package as well as remuneration and transactions is given in the Report on directors' remuneration on pages 10 and 11

Notes *(continued)*

5 Staff numbers and costs

The average number of persons employed by the Company (including directors) during the year, analysed by category, was as follows

	Number of employees	
	2008	2007
Directors	**6**	6
Other employees	**14**	11
	20	17

The aggregate payroll costs of these persons were as follows

	2008	2007
	£	£
Wages and salaries	**624,013**	492,217
Social security costs	**61,685**	52,334
Other pension costs (see note 16)	**19,497**	12,568
	705,195	557,119

6 Financial income

	2008	2007
	£	£
Bank interest receivable	**67,347**	59,845

Notes *(continued)*

7 Taxation

Analysis of credit in year

	2008	2007
	£	£
UK corporation tax		
Research and development tax repayment	**(156,394)**	(136,017)
Income tax credit	**(156,394)**	(136,017)

Details of the unrecognised deferred tax asset are included in note 13

Factors affecting the tax credit for the current period

The current tax credit for the year is lower *(2007 lower)* than the standard rate of corporation tax in the UK of 28% *(2007 30%)* The differences are explained below

	2008	2007
Reconciliation of effective tax rate	£	£
Loss for the year	**(594,065)**	(646,422)
Total income tax credit	**(156,394)**	(136,017)
Loss excluding income tax	**(750,459)**	(782,439)
Current tax at average rate of 29 67% *(2007 30%)*	**(222,661)**	(234,732)
Effects of		
Non-deductible expenses	**632**	3,118
Reduction in tax rate	**38,861**	-
Change in unrecognised timing differences	**4,976**	(41,302)
Current year losses for which no deferred tax recognised	**178,192**	272,916
Tax incentives	**(156,394)**	(136,017)
Income tax credit (see above)	**(156,394)**	(136,017)

The corporation tax rate applicable to the Company has changed from 30% to 28% with effect from 1 April 2008

Factors that may affect future tax charges

The effective tax rate in future years is expected to be below the standard rate of corporation tax in the UK due principally to historical losses which have been carried forward

Notes *(continued)*

8 Intangible assets

	Patents and licences £
Cost	
At 1 June 2006, 31 May 2007 and 31 May 2008	16,637
Amortisation	
At 1 June 2006	12,533
Charge for year	2,218
At 31 May 2007	14,751
Charge for year	1,886
At 31 May 2008	16,637
Net book value	
At 1 June 2006	4,104
At 31 May 2007	1,886
At 31 May 2008	-

Notes *(continued)*

9 Property, plant and equipment

	Assets in the course of construction £	Leasehold improvements £	Plant and machinery £	Fixtures and fittings £	Motor vehicles £	Total £
Cost						
At 1 June 2006	44,216	-	320,966	10,470	28,660	404,312
Additions	-	47,315	127,092	18,975	-	193,382
At 31 May 2007	44,216	47,315	448,058	29,445	28,660	597,694
Additions	-	16,453	118,687	7,459	-	142,599
Disposals and write offs	-	-	(203,290)	(7,335)	-	(210,625)
At 31 May 2008	44,216	63,768	363,455	29,569	28,660	529,668
Depreciation						
At 1 June 2006	-	-	215,386	9,452	9,318	234,156
Charge for year	44,216	1,454	18,198	3,050	7,165	74,083
At 31 May 2007	44,216	1,454	233,584	12,502	16,483	308,239
Disposals and write offs	-	-	(203,290)	(7,335)	-	(210,625)
Charge for year	-	5,557	31,582	4,775	7,165	49,079
At 31 May 2008	44,216	7,011	61,876	9,942	23,648	146,693
Net book value						
At 1 June 2006	44,216	-	105,580	1,018	19,342	170,156
At 31 May 2007	-	45,861	214,474	16,943	12,177	289,455
At 31 May 2008	-	**56,757**	**301,579**	**19,627**	**5,012**	**382,975**

10 Inventories

	2008 **£**	2007 £
Raw materials and consumables	**28,059**	96,838
Work in progress	**230,815**	115,343
	258,874	212,181

Raw materials, consumables and changes in finished goods and work in progress recognised as cost of sales in the year amounted to £252,874 *(2007 £138,955)*

Notes *(continued)*

11 Trade and other receivables

	2008 £	2007 £
Trade receivables	**160,954**	114,706
Other receivables	**86,475**	129,786
Prepayments and accrued income	**45,494**	45,084
	292,923	289,576

All receivables fall due within one year

12 Trade and other payables. amounts falling due within one year

	2008 £	2007 £
Trade payables	**171,620**	200,495
Taxation and social security	**19,723**	17,575
Accruals and deferred income	**83,309**	40,941
	274,652	259,011

13 Deferred tax

The elements of deferred taxation are as follows

	2008 £	2007 £
Difference between accumulated depreciation and amortisation and capital allowances	**17,810**	(5,866)
Other short term timing differences	**(2,572)**	(1,296)
Tax losses	**(566,180)**	(538,737)
Unrecognised deferred tax asset	**(550,942)**	(545,899)

The Company has an unrecognised deferred tax asset at 31 May 2008 of £550,942 *(2007 £545,899)* relating principally to tax losses which the Company can offset against future taxable profits from the same trade

The deferred tax asset has not been recognised in the accounts because it is not possible to assess whether there will be suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted

Notes *(continued)*

14 Called up share capital

	2008	2007
	£	£
Authorised		
20,000,000 ordinary shares of £0 01 each	**200,000**	200,000
Allotted, called up and fully paid		
19,030,748 shares *(2007 14,030,748)* of £0 01 each	**190,308**	140,308

Enterprise Management Incentive Scheme

The Company operates a share incentive scheme for the benefit of the directors and certain employees All options are granted at the discretion of the Board The scheme grants options to purchase ordinary shares of £0 01 each No options were exercised in the period

The options granted to directors, date of grant and exercise price and exercise periods under the scheme are set out in the report on directors' remuneration on pages 10 and 11 In addition to the directors' share options, certain employees have been granted the following options

Date of grant	Number of unexpired share options at year end	Exercise price	Exercise period
19/12/02	30,301	£0 70	19/12/05-19/12/12
08/03/04	40,000	£0 665	08/03/07-08/03/14
04/04/05	35,000	£0 50	04/04/08-04/04/15
14/09/05	215,000	£0 40	14/09/08-14/09/15
18/04/07	195,000	£0 21	18/04/10-18/04/17

There are a total of 515,301 unexpired options held by employees and a total of 671,663 unexpired options held by directors

15 Share premium and reserves

	Share premium account	Capital reserve	Profit and loss account
	£	£	£
At 1 June 2006	4,902,715	463,885	(3,509,803)
Retained loss for the year	-	-	(646,422)
Reversal of charge in relation to share based payments	-	-	62,375
At beginning of year	4,902,715	463,885	(4,093,850)
Retained loss for the year	-	-	(594,065)
Share Issue	847,237	-	-
Reversal of charge in relation to share based payments	-	-	56,609
At end of year	5,749,952	463,885	(4,631,306)

Notes *(continued)*

16 Pension scheme

The Company contributes to specific employees' personal pension schemes The pension cost charge for the year represents contributions payable by the Company to the scheme and amounted to £19,497 *(2007 £12,568)*

There were outstanding contributions of £nil (*2007 £nil)* at the end of the financial year

17 Analysis of cash flows

	2008 £	2007 £
Returns on investments and servicing of finance		
Interest received	**67,347**	59,845
Capital expenditure and financial investment		
Purchase of tangible fixed assets	**(142,599)**	(193,382)

18 Related party disclosures

The results of the Company include the following transactions with related parties

Company/entity	Relationship	Purchase	2008 £	2007 £
April Training Executive Ltd	JJ Faria is a director and has a controlling interest	Administrative services	-	1,174

All purchases from related parties are conducted on an arms length basis under normal commercial trading terms

19 Loss on ordinary shares

The calculation of basic loss per ordinary share is based on the loss for the financial year divided by the weighted average number of shares in issue during the year

Losses and number of shares used in the calculations of loss per ordinary share are set out below

Basic

	2008 £	2007 £
Loss after tax	**(594,065)**	(646,422)
Weighted average number of shares	**17,828,562**	14,030,748
Loss per share	**(3 33p)**	(4 61p)

Notes *(continued)*

19 Loss on ordinary shares *(continued)*

The calculation of diluted loss per ordinary share is identical to that used for the basic loss per ordinary share This is because the exercise of options would have the effect of reducing the loss per ordinary share from continuing operations and is therefore not dilutive under the terms of IAS33

20 Derivatives and other financial instruments

The Company's policies with regard to financial instruments are set out within the accounting policies note The risks arising from the Company's financial assets and liabilities are set out below with the policies for their respective management

Currency Risk

The Company transacts business in foreign currencies and therefore incurs some transaction risk

The Company had no open foreign exchange contracts at the Balance Sheet date

The Company's exposure to foreign currency risk was as follows, this is based on the carrying amount for monetary financial instruments

	31 May 2008			31 May 2007		
	US Dollar	**Euro**	**Sterling**	US Dollar	Euro	Sterling
	£	**£**	**£**	£	£	£
Cash and cash equivalents	-	-	1,112,719	-	-	878,971
Trade Receivables	-	56,803	104,151	13,407	3,698	97,601
Trade Payables	(19,531)	-	(152,089)	(3,365)	(4,686)	(192,444)
Net Exposure	(19,531)	56,803	1,064,781	10,042	(988)	784,128

	Average Rate		**Reporting Date Spot Rate**	
	2008	**2007**	**2008**	**2007**
US Dollar	2 006	1 921	1 976	1 978
Euro	1 385	1 479	1 273	1 472

Sensitivity Analysis

A one percent strengthening of the pound against the US Dollar and the Euro at 31 May 2008 would have (decreased)/increased profit by the amounts below This analysis assumes that all other variables, in particular interest rates, remain constant The analysis is performed on the same basis for 2007

	US Dollar	**Euro**
	£	**£**
31 May 2008	(178)	516
31 May 2007	91	(9)

A one percent weakening of the pound against the US Dollar and the Euro at 31st May 2008 would have an equal and opposite effect to the amounts shown above, on the basis all other variables remain constant

Notes *(continued)*

20 Derivatives and other financial instruments *(continued)*

Price Risk

The Company aims to minimise its exposure to supplier price increases and customer price decreases by offsetting reciprocal supplier and customer arrangements

Credit Risk

The Company operates a closely monitored collection policy

The ageing of trade receivables at the reporting date was

	31 May 2008			31 May 2007		
	Gross	**Impairment**	**Net**	**Net**	**Impairment**	**Net**
	£	**£**	**£**	**£**	**£**	**£**
Not past due	151,381	-	151,381	99,532	-	99,532
Past due 0 to 30 days	9,264	-	9,264	12,219	-	12,219
Past due 31 to 90 days	5,105	(4,796)	309	12,454	(9,499)	2,955
	165,750	(4,796)	160,954	124,205	(9,499)	114,706

The movement in the allowance for impairment in respect of trade receivables was as follows

	Impairment Allowance
	£
Balance 1 June 2006	12,439
Impairment loss recognised	(10,428)
Increase in impairment allowance	7,488
Balance 31 May 2007	9,499
Impairment loss recognised	(4,703)
Balance 31 May 2008	4,796

Liquidity Risk

The Company's objective is to maintain a balance between continuity and flexibility of funding through the use of short term deposits

Interest Rate Risk

The Company has cash deposits of £1,039,603 (*2007 £750,000*) These funds are placed on deposit at rates which track and exceed bank base rate These deposits are reviewed at least every 30 days These funds are available on demand At the year end, the weighted average interest rate for the floating rate cash deposits was the HBOS base rate of 5 49% (*2007 4 90% Barclays*)

The Company has no borrowings at 31 May 2008 (*2007 £nil*) The Company does not undertake hedging of interest rates

Financial assets

The Company has £1,112,719 (*2007 £878,971*) held in cash and deposits as financial assets as well as short term debtors These cash deposits are placed on the money market and are available on demand

Financial liabilities

The Company has no financial liabilities except for short term creditors

Notes *(continued)*

20 Derivatives and other financial instruments *(continued)*

Fair values of the Company's financial assets and liabilities

The fair value of financial assets and liabilities, together with the carrying amounts shown in the balance sheet are as follows

	2008 Carrying value £	2008 Fair value £	2007 Carrying value £	2007 Fair value £
Financial assets				
Cash and cash equivalents	1,112,719	1,112,719	878,971	878,971
Loans and receivables				
Trade receivables	160,954	160,954	114,706	114,706
Total financial assets	1,273,673	1,273,673	993,677	993,677
Financial liabilities at amortised cost				
Trade payables	(171,620)	(171,620)	(200,495)	(200,495)
Other payables (current)	(19,723)	(19,723)	(17,575)	(17,575)
Accruals	(83,309)	(83,309)	(40,941)	(40,941)
Total financial liabilities	(274,652)	(274,652)	(259,011)	(259,011)

21 Commitments

Total future minimum commitments under non-cancellable operating leases are as follows

	Land and buildings 2008 £	Land and buildings 2007 £
Operating leases which expire		
Within one year	-	-
In the second to fifth years inclusive	**183,509**	233,557
	183,509	233,557

Notes *(continued)*

22 Share based payments

Share Options

The number of options outstanding under the Company's share option scheme is as follows

Number of Share Options - Ordinary Shares at 1p

Note	At 31 May-07	Granted	Exercised	Lapsed	At 31 May-08	Exercise price	Date from which exercisable	Expiry date
(a)	171,016	-	-	(12,143)	158,873	70p	19/12/2005	19/12/2012
(a)	34,091	-	-	-	34,091	88p	08/12/2006	08/12/2013
(a)	80,000	-	-	(20,000)	60,000	66 5p	08/03/2007	08/03/2014
(a)	85,000	-	-	-	85,000	50p	04/04/2008	04/04/2015
(a)	444,000	-	-	(20,000)	424,000	40p	14/09/2008	14/09/2015
(a)	334,125	-	-	(20,000)	314,125	21p	18/04/2010	18/04/2017
(b)	110,875	-	-	-	110,875	21p	18/04/2010	18/04/2017
	1,259,107	-	-	(72,143)	1,186,964			

(a) These options have been granted under the EMI approved scheme There have been no variations to the terms and conditions or performance criteria attached to these share options during the financial year There are no performance conditions attached to these shares other than continued employment by the Company

(b) These options have been granted under the unapproved scheme There have been no variations to the terms and conditions or performance criteria attached to these share options during the financial year There are no performance conditions attached to these shares other than continued employment by the Company

There was no cost payable by the employees on the grant of any of the above options

The option holder may only exercise his options during employment with the Company

The movements of the EMI and unapproved share options outstanding are shown overleaf

Notes *(continued)*

22 Share based payments *(continued)*

	EMI Scheme		Unapproved Scheme	
	Number of awards	**Weighted Average Exercise Price £**	**Number of awards**	**Weighted Average Exercise Price £**
Outstanding at 1 June 2005	445,965	0 66	-	-
Granted	504,000	0 40	-	-
Forfeited	(55,858)	0 58	-	-
Outstanding at 31 May 2006	894,107	0 52	-	-
Granted	334,125	0 21	110,875	0 21
Forfeited	(80,000)	0 53	-	-
Outstanding at 31 May 2007	1,148,232	0 43	110,875	0 21
Forfeited	(72,143)	0 47	-	-
Outstanding at 31 May 2008	1,076,089	0 41	110,875	0 21
Exercisable at 31 May 2008	337,964	0 66	-	-
Range of exercise prices	0 21 to 0 88			0 21
Weighted average remaining contractual life	7 years 3 months		8 years 11 months	

Included within the EMI share options balance are options over 205,107 (*2007 205,107*) shares that have not been recognised in accordance with IFRS2 because either they were granted on or before 7 November 2002 or that they had vested prior to the effective date on 1 June 2006 These options have not been subsequently modified and therefore do not need to be accounted for in accordance with IFRS 2

There were no share options exercised during the year *(2007 nil)*

A charge of £56,609 *(2007 £62,375)* has been made in the profit and loss account to spread the fair value of the options over the 3 year service obligations of those incentives

Assumptions used in the valuation of share based options

In calculating the fair value of the share based payment arrangements the Company has used the Black Scholes method The fair value of the share options granted in 2007 and the assumptions used of their fair value on the date of grant were as follows

Weighted Average Assumptions	**2008**	2007
Fair Value per share option	**N/a***	15 9p
Share price on date of grant	**N/a***	20p
Exercise Price	**N/a***	21p
Share options granted in the year EMI	**N/a***	334,125
Share options granted in the year Unapproved	**N/a***	110,875
Expected Volatility	**N/a***	100%
Exercise Pattern (years)	**N/a***	3-10 years uniformly
Expected dividend yields	**N/a***	0%
Risk free rate of return	**N/a***	4 50%

* No share options were granted in the year to 31 May 2008

Notes *(continued)*

22 Share based payments *(continued)*

The fair value of the share options is applied to the number of options that are expected to vest which takes into account the expected and actual forfeitures over the vesting period as a result of cessation of employment

Expected volatility was determined by assessing the Company's historic data and the market the Company operates in

23 Capital management

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business The Board of directors monitors the return on capital, defined as net operating income divided by total shareholders' equity

At present employees and directors hold 21% of the share capital, assuming all outstanding share options are exercised

Shares issued in the year totalled £897,237 There were no changes in the Company's approach to capital management in the year

24 IFRS Restatement Information

The Company's financial statements for the year ended 31 May 2008 are the Company's first annual statements in compliance with adopted IFRSs

There are no material differences between the figures previously presented under UK GAAP and their restatement to adopted IFRSs

Company information and advisers

Websites	www surface-transforms com and www systemsST com
Registered Number	03769702
Directors	Kevin D'Silva *(Non-executive Chairman)* Dr Kevin Johnson *(Managing Director)* Julio Joseph Faria *(Non-executive Director)* Geoffrey Gould *(Sales and Marketing Director)* Professor David Thomas Clark *(Non-executive Director)* Kenneth Michael Baker *(Non-executive Director)*
Address	Unit 4 Olympic Park Poole Hall Road Ellesmere Port Cheshire CH66 1ST Tel 0151 356 2141
Nominated adviser	John East & Partners Limited 10 Finsbury Square London EC2A 1AD
Brokers	John East & Partners Limited 10 Finsbury Square London EC2A 1AD Redmayne Bentley 1 Skipton Road Ilkley LS29 9EH
Auditors	KPMG Audit Plc St James' Square Manchester M2 6DS
Solicitors to the Company	Halliwells LLP 3 Hardman Square, Spinningfields, Manchester M3 3EB
Bankers	Barclays Bank plc 125 Main Street Frodsham Cheshire WA6 7AD Bank of Scotland Plc The Mound Edinburgh EH1 1YZ

Registrars	Capita IRG plc Bourne House 34 Beckenham Road Beckenham Kent BR3 4TU

Company Number 3769702

NOTICE OF ANNUAL GENERAL MEETING
SURFACE TRANSFORMS PLC

NOTICE IS HEREBY GIVEN that the annual general meeting of the Company will be held at the offices of Halliwells LLP 3 Hardman Square, Spinningfields, Manchester M3 3EB on 28 October 2008 at 11 30am The business of the meeting will be

ORDINARY BUSINESS

- To receive consider and adopt the audited accounts for the year ended 31 May 2008 and the reports of the directors and auditors thereon

- To re-elect Julio Faria, who is retiring by rotation in accordance with article 113, as a director of the Company

- To re-elect Kevin D'Silva, who is retiring by rotation in accordance with article 113, as a director of the Company

- To re-appoint KPMG Audit Plc as auditors of the Company and to authorise the directors to fix their remuneration

- To approve the Directors' Remuneration report

SPECIAL BUSINESS

To consider and, if though fit to pass the following resolutions which will be proposed as to resolution 6 as an ordinary resolution and as to resolution 7 as a special resolution

- **THAT**, in substitution for all existing and unexercised authorities and powers, the Directors of the Company be and they are hereby generally and unconditionally authorised for the purpose of section 80 of the Companies Act 1985 (the "**Act**") to exercise all or any of the powers of the Company to allot relevant securities (within the meaning of section 80(2) of the Act) up to a maximum nominal amount of £63 436 to such persons at such times and generally on such terms and conditions as the directors may determine (subject always to the articles of association of the Company) provided that this authority and power shall unless previously renewed, varied or revoked by the Company in general meeting, expire at the conclusion of the next annual general meeting or 15 months after the passing of this resolution (if earlier) and provided further that the directors of the Company may before the expiry of such period make an offer or agreement which would or might require relevant securities to be allotted after the expiry of such period and the Directors of the Company may allot relevant securities in pursuance of such offer or agreement as if the authority conferred hereby had not expired

- **THAT**, subject to and conditional upon the passing of resolution 6 and in substitution for all existing and unexercised authorities and powers, the Directors of the Company be and are hereby empowered pursuant to section 95 of the Act to allot equity securities (as defined in section 94 of the Act) pursuant to the authority conferred upon them by resolution 6 as if section 89(1) of the Act did not apply to any such allotment provided that this authority and power shall be limited to

  (a) the allotment of equity securities in connection with a rights issue or similar offer in favour of ordinary shareholders where the equity securities respectively attributable to the interest of all ordinary shareholders are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them subject only to such exclusions or other arrangements as the Directors of the Company may consider appropriate to deal with fractional entitlements or legal and practical difficulties under the laws of, or the requirements of any recognised regulatory body in, any territory, and

(b) to the allotment (otherwise than pursuant to sub-paragraph (a) above) of equity securities up to an aggregate nominal amount of £19,031 representing approximately 10% of the current issued share capital of the Company

and shall expire on the date of the next annual general meeting of the Company or (if earlier) 15 months from the date of the passing of this resolution save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Directors of the Company may allot equity securities in pursuance of such offer or agreement as if the power conferred hereby had not expired

BY ORDER OF THE BOARD

G V Hall

Company Secretary

Dated 2008

Registered Office

Unit 4
Olympic Park
Poole Hall Road
Ellesmere Port
Cheshire
CH66 1ST

Notes:

1 A person entitled to attend and vote at this meeting is entitled to appoint one or more proxies to attend and on a poll, vote in his/her stead A proxy need not be a member of the Company Appointment of proxies does not preclude members from attending and voting at the meeting should they wish to do so

2 To be valid the instrument appointing a proxy must be deposited at the office of the Company's registrars Capita Registrars, Proxy Department The Registry, 34 Beckenham Street, Beckenham, Kent BR3 4TU not less than 48 hours before the time of the meeting

3 Copies of the Directors' contracts of service with the Company will be available for inspection during normal business hours on any week day at the registered office of the Company from the date of this notice until the annual general meeting and on the day of the annual general meeting at the place of the meeting from 15 minutes prior to its commencement until its conclusion

4 As permitted by Regulation 41 of the Uncertificated Securities Regulations 2001, the Company specifies that only those shareholders of the Company on the register at close of business on 26 October 2008 shall be entitled to attend or vote at the meeting in respect of the number of shares registered in their name at the time Changes to the register of members after 26 October 2008 shall be disregarded in determining the rights of any person to attend or vote at the meeting

5 CREST members who wish to appoint a proxy or proxies by utilising the CREST electronic proxy appointment service may do so by utilising the procedures described in the CREST Manual CREST Personal Members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s) who will be able to take the appropriate action on their behalf

In order for a proxy appointment made by means of CREST to be valid, the appropriate CREST message must be transmitted so as to be received by the Company's agent, Capita Registrars (whose CREST ID is RA10) by the specified latest time(s) for receipt of proxy appointments For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by the CREST Applications Host) from which the Company's agent is able to retrieve the message by enquiry to CREST in the manner prescribed

The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001

SURFACE TRANSFORMS PLC
FORM OF PROXY

Form of proxy for use at the Annual General Meeting of Surface Transforms plc to be held at 11 30am on 28 October 2008 at the offices of Halliwells LLP, 3 Hardman Square, Spinningfields, Manchester M3 3EB

I/We ______________________________

Please insert full name(s) in BLOCK CAPITALS

of ______________________________

being (a) Member(s) of Surface Transforms plc hereby appoint the Chairman of the Meeting or

____

(note 2) as my/our proxy to vote for me/us and on my/our behalf at the Annual General Meeting of the Company to be held on 28 October 2008 and at any adjournment thereof as directed by a mark in the spaces below

ORDINARY BUSINESS	FOR	AGAINST	ABSTAIN/ WITHHELD
1 To receive and adopt the audited accounts for the year ended 31 May 2008			
2 To re-elect Julio Faria as a director			
3 To re-elect Kevin D'Silva as a director			
4 To reappoint KPMG Audit Plc as auditors of the Company and to authorise the directors to fix their remuneration			
5 To approve the Directors' Remuneration Report			
SPECIAL BUSINESS			
6 To grant the directors authority to allot shares			
7 To disapply the statutory pre-emption rights			

Signature   Date

/see notes overleaf

NOTES

1 To be valid, completed form(s) of proxy must be deposited with Capita Registrars, Proxy Department, The Registry, 34 Beckenham Street, Beckenham, Kent BR3 4TU not less than 48 hours before the time for holding the meeting together with the power of attorney or other authority (if any) under which it is signed, or a notarially or otherwise certified copy of such power or authority or in the case of CREST members, by using the CREST electronic proxy appointment service CREST members should refer to note 5 in the notice of annual general meeting enclosed with this form of proxy in relation to the submission of a proxy appointment via CREST

2 This form may be used for the appointment of any other person as proxy by deleting the words "Chairman of the Meeting or" and inserting the name and address of the person whom it is desired to appoint A proxy need not be a member of the Company

3 Any alterations made to this form of proxy should be initialled

4 In the case of a corporation this proxy should be given under its common seal or under the hand of an officer or attorney duly authorised in writing

5 Please indicate how you wish your votes to be cast by placing "X" in the relevant box On receipt of this form duly signed, but without any specific direction as to how you wish your votes to be cast, you will be deemed to have authorised your proxy to vote, or to abstain from voting, as they think fit

6 In the case of joint holders the vote of the senior who tenders a vote, whether in person or by proxy, will be accepted to the exclusion of the votes of the other joint holders For this purpose seniority is determined by the order in which the names stand in the Register of Members in respect of the joint holding

7 Return of the completed form of proxy will not preclude a member from attending and voting in person at the meeting