Surgical Innovations Group plc
Annual Report and Accounts 2012

Shaping the future of Minimally Invasive Surgery

Company registered number 2298163

Surgical Innovations Group plc specialises in identifying and addressing the "clinical need", with the design and manufacture of creative solutions for minimally invasive surgery.

We listen
Our innovative medical devices are designed to meet the "clinical needs" of surgeons around the world but most importantly, improve patients' quality of life

We innovate
Designed and manufactured in the UK, our medical devices are pioneering, ergonomic, easy to assemble and easy-to-use

We improve
Our expert designers work hand-in-hand with global surgeons, as well as our UK and international Clinical Advisory Board (CAB) to continually improve our devices

We export
We are an export-focused company with over 40 independent distributors selling our pioneering products and solutions in all major markets

Financial highlights

- Revenue of £764 million (2011 £760 million)
- SI branded sales up 12 9% to £5 33 million (2011 £4 73 million) – *representing 68% of total revenue*
- Gross profit up 73% to £3 86 million (2011 £3 60 million)
- Gross margins improved to 50 5% (2011 47 3%)
- Adjusted EBITDA (excluding exceptional items) of £2 89 million (2011 £2.83 million)
- Operating profit reduced to £1 32 million (2011 £1 77 million) – *due to amortisation and exceptional costs*
- Pre-tax profit reduced to £1 23 million (2011 £1 71 million)
- Adjusted earnings per share of 0 35p (2011 0 44p)
- Net cash from operating activities of £612,000 (2011 £1 78 million) – *reflecting increase in working capital as a result of significant sales in December 2012*

Operational highlights

- Strong second half sales with contracted orders in H2 of £5 62 million up 85% on H1 (with c £1 million to be recognised in year ending 31 December 2013)
- US direct sales up 21 9% to £2 15 million (2011 £1 76 million) and are now 28 1% of total revenue (2011 23 2%)
- 33% increase in unit sales of YelloPort+plus™ valves and SwingTop®s
- YelloPort+plus™ cannula sales increased to 10,124 units (2011 5,272 units) – *will drive long-term valve sales*
- RGF grant of up to £5 05 million to fund capital expansion strategy
- FDA approvals and US contracts provide a solid base for development of US strategy
- UK SI branded sales up 34.3% as more NHS hospitals convert to cost-saving Resposable® products
- New areas of MIS progressing well, particularly ultra-MIS (3mm) and hip arthroscopy

Total revenue (£m)

£7.64m +0 5%

12	7 64
11	7 60
10	7 05
09	4.54

Adjusted EBITDA (£m)

£2.89m +2 1%

12	2 89
11	2 83
10	2 55
09	0 94

Group profit before tax (£m)

£1.23m -28%

12	1 23
11	1 71
10	1 55
09	0.26

Review of the year

Our business

Products dedicated to meeting the "clinical needs" of forward-thinking surgeons.

Our pioneering, user-oriented technologies are created through expertise in design and specialist in-house manufacturing The result is creative surgeon-led solutions for MIS

1

Clinical need

Working with members of our Clinical Advisory Board (CAB), we scope the project area for clinical need, intellectual property landscape and new business opportunity

2

Concept

We develop blue-sky ideas according to opportunities identified in the research phase This includes

- Generating working prototypes for Key Opinion Leaders' (KOLs) and CAB feedback
- Evaluating cutting-edge innovations with all users
- Protecting novel ideas through intellectual property patents

3

Design

Our designers are put through the same core skills surgical training exercises as surgeons, allowing them to truly immerse themselves in the role of the end user and understand how prototypes can be improved and refined

4

Manufacture

Our in-house manufacturing facility is made up of a machine shop, assembly, clean room and injection moulding Our state-of-the-art machinery allows us to produce expert precision-engineered products in close collaboration with our design and quality teams

Focusing on delivering high quality products to meet the patient need.

SI's Clinical Advisory Board (CAB) helps to identify clinical need ensuring our continual commitment to meet the "patient need"

SI Brand

We design and manufacture our own successful brand of Resposable® medical devices

2012 revenue
£5.33 million
Percentage of Group revenue
69.8%

OEM

We are proud to be an OEM supplier to several leading international medical device businesses

2012 revenue
£2.20 million
Percentage of Group revenue
28.9%

Industrial

SI's pioneering segment technology is ideally suited to provide industrial solutions for major international companies

2012 revenue
£0.10 million
Percentage of Group revenue
1.3%

Product improvement

With the patient need firmly in mind, product development is a key part of our design and manufacturing process This involves

- Refining the designs using CAD
- Ensuring that products are effectively engineered for manufacture
- Collaborating with our regulatory team so products are compliant with today's international, stringent regulatory standards

Supply

We build and maintain relationships with our distribution network to ensure that SI has a strong reputable global presence SI also licenses its IP over fixed periods and manufactures products on behalf of OEM partners who are committed to minimum value and volume orders

Review of the year
Our progress

A defining year of strengthening our global reach.

2012 was a progressive year for Surgical Innovations (SI)

March
SAGES US – driving the SI brand

This month saw success at US Society of American Gastrointestinal and Endoscopic Surgeons (SAGES) conference and, as the only British company in attendance, SI has truly made an impact on the US market

Meeting international distributors at SAGES

April
Strengthening the Clinical Advisory Board (CAB)

SI was pleased to announce the appointment of two new surgeons to its Clinical Advisory Board (CAB), James Halstead and Chris Sutton The surgeons are both highly experienced in minimally invasive surgery (MIS) and, since joining the CAB, have worked closely with our design team on product testing and feedback

May
Strategic UK partnerships

May saw the signing of a five-year extension to the distribution agreement with UK distributor Elemental Healthcare The agreement, which is based on minimum contracted volumes, will be worth £5 million over the five years and provides Elemental with continued exclusive distribution rights to SI's entire product portfolio within Great Britain under the SI brand

June
Key OEM alliance

An eight-year distribution agreement with CareFusion, a leading, global medical device company, was signed, giving it exclusive rights to sell PretzelFlex® in the US PretzelFlex® has been developed by SI for the effective elevation or retraction of organs and tissue during MIS procedures to provide better access as well as visualisation of surgical sites The device will be marketed under the CareFusion brand and SI will retain the right to manufacture and distribute the device under the SI brand in all other markets

July
SI hosts annual clinical meeting

Some of the best minds in UK surgery came together in July to attend the Company's annual Clinical Advisory Board (CAB) meeting Throughout the two day event, SI's concept designers and product development engineers were given the opportunity to liaise with surgeons to gain clinical feedback on both the innovative Company's existing and planned product portfolio and gain inspiration for new ideas

SI hosts its annual CAB meeting.

November
Launch of new website

SI's new Ltd website was launched The website has been especially designed with a variety of users in mind – including distributors, surgeons, patients and the media It features an Online Distributor Resource Centre where our network of international dealers can access everything they need to promote SI branded products

www surginno com

August
"Ultra" MIS

SI made strong strides into the Paediatric Surgery market after successfully exhibiting at its first paediatric congress The aim of the event was to raise the global profile of SI's new range of 3mm instrumentation for "Ultra" MIS

3mm 5mm

December
Record month of delivery

By working with our Top 10 dealers and establishing them as "strategic partners", SI was delighted to fulfil a record-breaking month of delivery Creating these strategic alliances and working together to drive SI branded products is a key part of our sales strategy and has seen an increase of 51% in revenue from these key dealers

Review of the year

Our opportunities

Responding to clinical need and market opportunities with new technologies.

We are recognised as highly innovative and progressive in the laparoscopic surgery field and our award-winning technologies are ideally suited to be adapted in other areas of MIS

Development

Strategic OEM partnerships

We continue to work with some of the world's leading healthcare companies through OEM partnerships Our speed to market and unique design proposition make SI's design team an effective sales and marketing tool

An example of one of our strategic OEM collaborations is our partnership with Advanced Medical Solutions (AMS) Working with the AIM-listed company, SI has developed an applicator that applies adhesives and sealants internally into the body using minimal invasive techniques SI will develop manufacture and hold the intellectual property rights for the device

Intellectual property portfolio

We will continue to enhance our intellectual property portfolio in the field of MIS with a view to ensuring competitive advantage

24

Cumulative total of UK patents filed since 2009

Innovation

New areas of MIS/surgical techniques

The technologies used in SI's laparoscopic products can be adapted to meet the needs of surgeons in other specialities We are currently working with leading clinicians, academics and other medical companies in these fields to identify emerging areas of surgery, where our skills and expertise can be easily translated

Orthopaedics (hip)

Cardiovascular (heart)

Orthopaedics (spine)

Thoracic surgery (lungs)

Hip arthroscopy

Our concept design team is working on new innovations in hip arthroscopy to improve safety, visualisation and access into the hip joint with assistance from our hip arthroscopy CAB surgeons

"Ultra" Minimally Invasive Surgery (MIS)

To satisfy the continuing clinical trend towards less collateral damage, we have pioneered a 3mm range of instrumentation for "Ultra" MIS that significantly reduces post-operative pain and trauma for patients Making smaller incisions promotes quicker healing and can negate the need for port site closure suturing at the end of procedures

Expansion

United Kingdom

As the NHS continues to reduce costs, SI's cost effective solutions are perfectly placed to support the NHS's cost reduction programme

34%
Increase in UK SI branded sales

7
UK hospitals converted to YelloPort+plus™

How the NHS is changing the UK market

Healthcare systems around the world are expected to make significant savings during this time of austerity In the UK the NHS aims to make savings of up to £20 billion by 2015 SI's Resposable® concept, which combines high quality reusable and disposable components, is ideally positioned to support the NHS and other global healthcare bodies in their cost-saving measures

UK SI branded sales (£m)

£0.88m

12	0 88
11	0 67
10	0 65

United States

Being the biggest medical device market in the world, the United States offers real opportunities for SI

22%
Increase in sales to the US

28.1%
Percentage of total revenue accounted for by US sales

How SI's market is growing in the US

SI continues its focus on the development of US opportunities and has been delighted to further increases revenue streams in this market OEM distribution, direct sales of SI branded products through our master dealer (SI USA Inc) and the use of third party "tray companies" have all contributed to a growing market presence in the US and a 22% increase in sales

Direct US revenue (£m)

£2.15m

12	2 15
11	1 76
10	1 41

See how we will develop opportunities through our strategy on page 11

Review of the year
Chairman's statement

"We remain confident about the future growth prospects of the business as our existing SI branded products continue to gain international clinical recognition."

Doug Liversidge CBE, Chairman

Summary

- The majority of sales continue to come from our higher margin SI branded products which now represent 70% of overall revenues (2011 62%)
- The US remains our largest opportunity and now accounts for 28 1% of total revenue
- Increasing YelloPort+plus™ cannula sales provides the platform for longer term high margin revenues from the disposable elements

Results

We have made good progress throughout the year and the second half was particularly strong, with substantially improved trading across both SI Brand and OEM segments against the first half As a result we saw a considerable increase in contracted orders in the second half of £5 62 million, which represented an 85% improvement on our first half performance (H1 2012 £3 02 million)

However as explained in our February trading update, £1 million of these orders will be recognised as revenue in the first week of the financial year ending 31 December 2013 If the additional orders had have been recognised in the year under review I am confident that we would have seen strong double digit growth in revenues, adjusted EBITDA and pre-tax profits for that period Whilst it is frustrating that the tremendous efforts of the team at the end of the year are not being recognised in this financial year it does mean that we will start the current financial year with a sound platform to build on

As a result of the recognition discussed above, Revenue for the period was £7 64 million (2011 £7 60 million) and Adjusted EBITDA (excluding exceptional items) was ahead of the previous year at £2 89 million (2011 £2 83 million)

The majority of sales continue to come from our higher margin SI branded products where we saw revenues increase by 12 9% to £5 33 million (2011 £4 73 million) Again we experienced particularly strong sales in the final quarter of the year and this growth was driven by our flagship Resposable® products. SI branded products now represent 70% of overall revenues (2011 62%) OEM sales for the year decreased 21 5% to £2 20 million (2011 £2 81 million), reflecting our policy to focus purely on our strategic OEM partners whilst allocating resources to promotion of the SI branded products The Industrial business continues to operate at historic levels with sales of £101,000 (2011 £70,000)

We continue our focus on the development of US opportunities as we further increase revenue streams in this important market Direct sales to the US increased by nearly 22% to £2 15 million (2011 £1 76 million) and now account for 28 1% of total revenue (2011 23 2%)

An important measure of our performance is the growth in sales of the higher margin consumable element of our Resposable® products Total sales of these SI branded consumables increased by 6 7% to £3 17 million (2011 £2 97 million) which now represents 59% of SI Brand sales (2011 63%) There is a clear correlation between long-term valve sales and the number of reusable cannulas in the market I am delighted to report that YelloPort+plus™ cannula sales increased to 10,124 units (2011 5,272 units) and this provides the platform for longer-term high margin revenues from the disposable elements

Gross profit increased by 73% to £3.86 million (2011 £3.60 million) with Gross margins improving to 50.5% (2011 47.3%) Due to the exceptional items and increased amortisation and depreciation costs, operating profit reduced to £1.32 million (2011 £1.77 million) As a result profit before tax was £1.23 million (2011 £1.71 million) Earnings per share adjusted for exceptional items and deferred tax adjustments decreased to 0.35p (2011 0.44p)

Cash flow and investment

The Group generated net cash from operating activities of £612,000 (2011 £1.78 million) which reduced due to an increase in working capital of £1.96 million arising primarily as a result of significant sales in December 2012 As expected, investment in capitalised intangible and tangible assets reduced during the year to £1.98 million (2011 £2.84 million)

At 31 December our net debt stood at £2.63 million (2011 £1.11 million) In addition to existing finance lease facilities, the Group secured a £2 million overdraft facility from HSBC and at 31 December 2012, £1.42 million of this facility was utilised

Dividend

The Board maintains the belief that at this stage in the Group's development it would be more appropriate to continue its focus on strong inward investment and does not intend to pay a dividend for the year ended 31 December 2012

Regional Growth Fund (RGF)

In 2012 we announced Government approval to our final bid for RGF monies of £5.05 million These funds are specifically allocated to our capital expansion strategy comprising a new R&D and training facility within the Leeds City Region We are aware that any capital build programme must be in the best interests of Surgical Innovations and we are in the process of working with our professional advisers on both site location and specification I will be providing further updates over the course of the year as the project progresses

Outlook

Trading in the period since the year end has been encouraging and is in line with our expectations for the first quarter

Our strategy of focused innovation and product development within new growth areas of laparoscopy, fluid delivery and 3mm ultra-MIS, coupled with our move into new therapeutic markets such as hip arthroscopy, ensures that we remain at the forefront of MIS It also provides a solid platform from which we have a growing pipeline of new products to be launched, which will drive additional growth in the coming year and beyond

We remain confident about the future growth prospects of the business as our existing SI branded products continue to gain international clinical recognition The US remains our largest opportunity where we have established multiple routes to market Continued investment in developing these routes will provide quicker and easier access to this key market for both current and future products We expect to see a regular flow of new products throughout the year, which will help to drive future revenues, as well as the development of new and existing relationships with our strategic OEM partners, whilst retaining our primary strategic objective of growing our SI Brand

I would like to thank the Board and staff for their hard work in 2012 and their undoubted contribution to the strong performance of the business, particularly in the second half of the year We start 2013 well positioned to take full advantage of the opportunities that are available to us and I look forward to reporting on the continuing success of the Group over the coming year

Doug Liversidge CBE
Chairman
8 April 2013

Review of the year

Operating review

"We remain confident about the future growth prospects of the business, particularly from our SI branded products which offer an attractive value proposition to both clinicians and procurement managers in these times of austerity."

Graham Bowland, Chief Executive Officer

Summary

- Strong demand for our Resposable® instruments has driven SI branded revenue up 12.9%
- Increased penetration of UK hospital market
- Drive further growth in the business and to capitalise in the US

Operationally, we divide the Group into three segments

SI Brand – our own branded laparoscopic minimally invasive devices These include our port access systems YelloPort® and YelloPort+plus™, our instrument ranges Logi®Range, Logic®Reusable and Quick®Range, as well as our retraction systems FastClamp™ and PretzelFlex® New products are under development to move the business into other areas of MIS beyond laparoscopy

OEM – original equipment manufacturer contracts with third party medical device companies to supply minimally invasive technology products through either own label or co-branding

Industrial – provides minimally invasive technology for industrial applications This remains a non-core element of our business

SI Brand

Revenues from SI branded products increased over the period by 12.9% to £5.33 million (2011 £4.73 million) This growth was driven by SIs flagship Resposable® products YelloPort+plus™ and Logi®Range

We continue to see strong demand for our Resposable® instruments, where some elements are disposable and others reusable. The success of this approach reflects a culture change within the medical device industry and provides cost-saving solutions within an increasingly cost-conscious environment We believe that, whilst the laparoscopic market remains highly competitive, demand for our cost-effective SI Branded products is being driven by the widespread austerity measures now experienced within the general surgery environment

Our "razor/razor blade" model continues to provide us with growing recurring revenues from the on-going sales of consumables In 2012 we saw unit sales of our YelloPort+plus™ valves and SwingTop®s (the higher margin disposable elements) increase by 33%, in direct relation to the increased placing of the cannula units (the reusable element) sold in the previous year In 2012 we sold a total of 10,124 YelloPort+plus™ cannula units, up 92% on the previous year (2011 5,272 units) As a result, we expect to see a consistent pattern of rising consumable revenues in 2013 and beyond

The SI branded products are now sold through a network of specialist laparoscopic distributors across 31 countries As part of our sales strategy we have established strategic alliances with ten key distributors As a consequence we have seen revenues from these particular distributors increase by 51% These alliances will provide improved clinical feedback with links to the International Clinical Advisory Board, greater focus on device solutions for the "clinical need" in each specific market together with enhanced sales and marketing support and attendance at local clinical meetings

In February we received approval from the US Food and Drug Administration (FDA) for our Logic® range of reusable instruments and our US master dealer, SI USA Inc., was awarded a three year contract by the Premier Healthcare Alliance (Premier) for the sale of our Resposable® Logi®Range, and Logic®Reusable range of instruments Importantly this provides SI USA Inc with the opportunity to present our technologies to the 2,800 plus hospitals and

Review of the year

Our strategy and Key Performance Indicators (KPIs)

Driving sustainable growth.

Our strategy

- Delivery of sustained growth of SI Brand revenue
- Promotion of the Resposable® concept
- Continuous expansion into several areas of surgery all encompassed under the umbrella of MIS
- Position SI as a leader in 3mm "Ultra" MIS instrumentation

Objectives

- Leverage the established routes to market in the US
- Continue expansion through organic growth of the reusable cannula platform
- Launch hip arthroscopy products and fluid delivery device in 2013
- Create complete range of viable 3mm instrumentation

Progress

- Focus on increased sales and marketing activity in international key markets
- Growth in sales of the higher margin, consumable element of Resposable® products
- Pre-production hip arthroscopy devices and AMS glue delivery device on track
- New products launched include PretzelFlex® 3mm and the YelloPort+plus™ 3mm range

SI Brand segment revenue (£m)

£5.33m +12.9%

12	5.33
11	4.73
10	3.85
09	2.96

2012 saw continued growth in SI Brand revenues which remains our primary strategic objective

Adjusted EBITDA (£m)

£2.89m +2.1%

12	2.89
11	2.83
10	2.55
09	0.94

Adjusted EBITDA increased by 2.1% reflecting careful cost control

Adjusted earnings per share (p)

0.35p -20.5%

12	0.35
11	0.44
10	0.48
09	0.14

Adjusted earnings per share fell due partly to increased non-cash costs for amortisation and share-based payments

Number of YelloPort+plus™ cannulas

10,124 +92%

12	10,124
11	5,272
10	3,213
09	2,203

YelloPort+plus™ provides a continued platform for growth with a direct colligation between the reusable cannula and the disposable valve

Direct US revenue (£m)

£2.15m +22%

12	2.15
11	1.76
10	1.41
09	0.62

We continue to leverage our established routes to market in the US which remains our largest target market

SI Brand Resposable® product revenue (£m)

£3.18m +7%

12	3.18
11	2.97
10	2.36
09	1.76

Continued growth in SI Brand Resposable® revenues demonstrates the financial benefit of our concept.

Review of the year

Operating review continued

SI Brand continued

90,000 other sites within the Premier Alliance and is a significant benefit to any perspective sub distributor of SI USA Inc We remain committed to driving our US business and with cost saving at the very heart of US procurement thinking, we believe the US will remain our key market in the foreseeable future

Our advanced laparoscopic retractor, PretzelFlex®, was launched in Europe at the end of 2011 We have received positive clinical feedback from surgeons and distributors on the product and it has sold well As a reusable device we will experience revenue growth from new markets, both geographical and clinical, supplemented by new PretzelFlex® line extensions It was pleasing to announce the launch of the new 3mm PretzelFlex® at the end of 2012, this adds value to the range and enhances our move into 3mm surgery

Following the recent five year extension to our distribution agreement with our UK distributor, Elemental Healthcare, we have seen extremely strong growth in UK sales of SI branded products, up 34 3% on the previous year This increase in sales has been driven by a greater penetration of the UK hospital market with a number of hospitals converting to SI branded products In the last year seven UK hospitals converted to using YelloPort+plus™ and eight hospitals converted to using Logi®Cut scissors

With the NHS having to report future annual savings in the region of £20 billion, our cost-effective devices are beginning to make a positive impression with both procurement management and clinicians prepared to support the UK healthcare industry One NHS hospital in West London changed to SI's Resposable® instrumentation and this has brought savings of £250,000 in the first year alone, compared with the previous year's cost of using fully disposable instruments.

Our 3mm instrument range has been developed in response to the continuing trend to less invasive surgery within the MIS space. The benefits of 3mm surgery are identified through smaller incisions thus reducing collateral damage to the abdominal wall, negating the need for port site closure with sutures and ultimately providing near "scarless" surgery SIs objective is to become a leader in 3mm surgery, we are well positioned to do so with our unique offering of 3mm ports, instruments and PretzelFlex®

Our UK Clinical Advisory Board is a key element within our growth strategy By addressing the clinical need" within each area of laparoscopic surgery through our clinical relationships we are able to develop devices that will be widely accepted within the surgical community, both national and international We are proud of our close links with UK clinicians and highly value their feedback and input which has enabled us to launch several new product line extensions over the final quarter of 2012

OEM

Revenues from OEM decreased 21 5% to £2.20 million (2011 £2.81 million) reflecting our focus on strategic OEM partners whilst focussing resources on the promotion of SI branded products

Our OEM contracts business, whereby we license our intellectual property over fixed periods and manufacture the products on our customer's behalf, is very much reliant on our partners driving business on our behalf and it can, on occasion, be unpredictable in terms of initial product launches, supply chain inventory requirements and clinical adoption of new device technology

In the US we sell the PretzelFlex® laparoscopic retractor through an OEM partnership with CareFusion Following FDA 510(k) clearance in March 2012 the first batch of PretzelFlex® devices were shipped under this agreement with a second batch shipped in December In addition we received FDA 510(k) clearance for our reusable 3mm PretzelFlex™ device in January 2013, which will enable CareFusion to address the growing 3mm general surgery market as well as paediatric surgery We have shipped a number of these instruments to CareFusion for evaluation purposes with their key opinion leaders Following the successful conclusion of these evaluations sales to the US have now commenced

2012 also saw the launch of the Vikon branded laparoscopic instrument range for Integrated Medical Systems Inc. (IMS) and we expect to see stronger sales of this product line with a full contribution in 2013, with the opportunity to develop further line extensions thus enhancing the overall Vikon product portfolio

In September 2011 we signed a development agreement with Advanced Medical Solutions Group plc ('AMS') to develop a novel device for internal deployment of their branded adhesive, LiquiBand® This product, described by AMS as their "Hernia Mesh Fixation device", is still on track for a late 2013 launch initially focusing on key European laparoscopic hernia markets

Industrial

Revenues for our non-core Industrial business remain at historic levels at £101,000 (2011 £70,000) These revenues relate to the use of technology in on-wing inspection of jet engines, as well as a feasibility project for a possible bespoke solution for a device delivery system

Product development and new product pipeline

New product development and product enhancement for the SI Brand continues apace and is driven by the R&D team's close working relationship with our Clinical Advisory Boards

We have continued to invest significantly in new products with a total investment of £2.23 million relating to product development (2011 £2 90 million) to generate a regular flow of innovative products to bring to market

The Concept and Development teams have been working on a number of new products which will launch under the SI brand during 2013 Our main focus has been on the development of our 3mm ultra-MIS range, delivery systems – the AMS device being the first for glue deployment, as well as our efforts to diversify our product portfolio from laparoscopy into new clinical areas and in the first instance the hip arthroscopy market We are already working with our Clinical Advisory Board (CAB) members to create a gold standard in 3mm surgery by developing best practices in laparoscopic cholecystectomy (gallbladder removal) and hernia surgery

A dedicated team within our R&D department continues to work with our CAB arthroscopy specialists and having launched pre-production devices for evaluation at the end of 2012 we are confident that will be in a position to have ports and instruments available for clinical use in 2013 It is believed that hip arthroscopy is the fastest growing area within orthopaedic surgery and as surgeon proficiency and patient outcomes improve we look forward to being able to service the increasing demand for the required high quality, cost-effective instrumentation

Review of the year

Case study

What is the Regional Growth Fund?

The RGF is a £2 4 billion fund operating across England to be invested over a three year period The fund supports projects and programmes that lever private sector investment creating economic growth and sustainable employment It aims particularly to help those areas and communities currently dependent on the public sector to make the transition to sustainable private sector-led growth and prosperity As part of the agreement SI will commit to £8 7 million in capital investment by the end of 2015

Deputy Prime Minister Nick Clegg visiting Surgical Innovations to congratulate them on the RGF offer

Regional Growth Fund (RGF)

Surgical Innovations to benefit from £5.05 million RGF grant

"It will allow SI's profile to grow internationally, deliver sustainable jobs and achieve future growth for the Company and the Leeds City Region through establishment of the Leeds Medical Technology Park"

Graham Bowland, Chief Executive Officer

Surgical Innovations Group plc has formally signed the RGF Final Grant Offer Letter, worth up to £5 05 million to SI in Government funding The grant will be used to develop a state of the art research and development facility and clinical training centre, with a reasonable expectation of creating over 300 jobs in the Leeds City region over the next twelve years

The RGF grant will benefit SI by contributing infrastructure funding to implement the Company's long term strategy for growth through enhanced product development in new clinical areas of Minimally Invasive Surgery It will enable the creation of a clinical training centre allowing SI to further the relationships it has with leading clinicians, both UK and international, and will act as a magnet for pioneering surgeons looking to develop new skills and instrumentation in minimal invasive surgery

Review of the year
Operating review continued

Product development and new product pipeline continued

Our product development roadmap has been well documented and we continue to explore possibilities of technology transfer from laparoscopic to other areas of MIS We commenced with hip arthroscopy and this will be followed with moves into thoracic, cardiac and spinal surgery Thoracic MIS techniques centre around video assisted thoracic surgery (VATS) and we have commenced discussions with key opinion leaders on how we can utilise our technologies in this innovative area of surgery

Clinical Advisory Boards

The UK CAB now consists of eight highly-experienced laparoscopic surgeons covering a wide range of specialisms within laparoscopy together with three key opinion leaders in hip arthroscopy and spinal surgery This structure ensures that SI is able to both address the clinical need in all areas of laparoscopy and implement the strategy to transfer our core MIS technology into new areas of the body across a broad range of clinical disciplines

We have also started to develop the International Clinical Advisory Board, (ICAB), a group of key opinion leaders around the world who can offer advice about their local markets and feedback on our products In March this year we announced the appointment to the ICAB of Sean Barnett, a US paediatric and thoracic surgeon specialising in core trauma and bariatric surgery This appointment is significant given the launch of our new 3mm laparoscopic devices which are aimed at all areas of general surgery, but which could be particularly advantageous for minimal invasive surgery in children

Manufacturing

We continue to implement our programme of gross margin improvements throughout the manufacturing process As part of this process we have commenced working with the Manufacturing Advisory Service (MAS) on a long-term lean manufacturing programme This has already provided tangible benefits in 2013 and will be a key driver in our manufacturing objectives for further in-house manufacture of critical, yet currently outsourced components

Following substantial investment in 2011 to ensure the continued growth and optimisation of our manufacturing arm 2012 saw a planned reduction in this investment to £117000 (2011 £1.24 million)

Post period end events

In January 2013 we formally signed the Regional Growth Fund (RGF) Final Grant Offer Letter This provides us with up to £5.05 million in Government funding and will be used to develop a state-of-the-art research and development facility and clinical training centre

We expect that the RGF grant will provide infrastructure funding to implement our long term strategy for growth through enhanced product development in new clinical areas of MIS It will also enable the creation of a clinical training centre which we believe will act as a magnet for pioneering surgeons looking to develop new skills and instrumentation in minimal invasive surgery

Outlook

Our strategy remains firmly in place to become a leading innovator within the laparoscopic surgery field and to continue to focus on product development for our existing markets as well as new therapeutic markets within MIS

We continue to work with our partners to bring our technology to market, be it through OEM agreements with major medical devices companies or through our extensive international distribution network that promotes our own SI branded products

The R&D team continues to work on generating both a wider range of new products and enhancements to existing product lines. We expect to see a regular flow of these in 2013 particularly within the 3mm ultra-MIS range, as well as the launch of our new hip arthroscopy products

We continue to receive interest from global medical device companies to develop innovative laparoscopic products on an exclusive OEM basis. Such enquiries are testament to the high regard in which our design team is held, we assess each enquiry on its merits, taking into consideration the impact on our own SI branded products against the strategic positioning of SI with the potential partner

We expect to see further sales in the US of our PretzelFlex® through our exclusive arrangement with CareFusion, and with the planned 2013 launch of the laparoscopic "Hernia Mesh Fixation" device for Advanced Medical Solutions we should see the commencement of a revenue stream in the final quarter of 2013 and the full benefit in 2014 as the clinical benefits of glue fixation become accepted across the MIS space

We continue to be well placed to drive further growth in the business and to capitalise particularly on the opportunities that are presented to us in the US, which is our largest target market We will continue to promote SI branded products through our master dealer for instruments and through specialist tray companies for our ports It is our intention to allocate resources to support the promotion of our US business, thereby ensuring we fully capitalise on the current opportunities opening up to SI as a result of the economic pressures being applied to the US healthcare system

We remain confident about the future growth prospects of the business, particularly from our SI branded products which offer an attractive value proposition to both clinicians and procurement managers in these times of austerity With the increased placement of cannula units in 2012 we anticipate the benefit of pull through of higher margin consumable sales in 2013 UK sales for SI branded products have started well in 2013 and already in the first quarter nine UK hospitals have converted to using YelloPort+plus™ and a further three hospitals have started using Logi®Cut scissors

The strong performance in the final quarter of the year was a great achievement by the team and I would like to thank my colleagues for their hard work and support in all areas of the business

We remain confident in both our sales and product development strategies There needs to be a fine balance between developing routes to market and the development of new products that ultimately feed into these routes It takes many years to create a robust international sales network capable of promoting our specifically positioned medical devices We believe this balance will be achieved in 2013 as we invest within the US market and I look forward to providing further updates during 2013 as we focus on US revenue generation in the current financial year

Graham Bowland
Chief Executive Officer
8 April 2013

Review of the year
Case study

What is the CAB?

The CAB works closely with SI's design team to offer clinical feedback on its existing product portfolio and also giving inspiration for new ideas The UK and international CAB is made up of prominent Key Opinion Leaders (KOLs) from all areas of MIS, allowing SI to be at the forefront of product development and the continuation of SI's surgeon-led philosophy

UK Consultant Surgeon James Halstead operating with his team at the Nuffield Health Leeds Hospital

Clinical Advisory Board (CAB)

Surgeons and industry working together to identify clinical need

Surgeon-led solutions

20 years ago, a surgeon and engineer came together to address a clinical need This collaboration of engineering and clinical expertise was the secret to our success and, since then, Surgical Innovations (SI) has maintained this surgeon-led focus by creating two CABs – one international and one made up of UK surgeons Consultant surgeon James Halstead is celebrating his first year on the CAB

"It is refreshing to see surgeons and industry working together to identify clinical need and also ensure the right clinical decisions are made in relation to the challenges surgeons face every day. I am proud to work with SI and to be able to contribute to the next generation of instrumentation"

James Halstead, UK Consultant Surgeon

Review of the year

Financial review

"Gross margin from the core MIS business increased to 49 9% (2011· 471%) as a consequence of manufacturing improvements and favourable shifts towards higher margin consumable elements"

Mike Thornton, Chief Financial Officer

Summary

- Reported revenue for 2012 increased 0 5% to £764 million (2011 £760 million)
- Gross margin from the core MIS business increased to 49 9% (2011 471%)
- Adjusted EBITDA increased from £2 83 million to £2 89 million

Revenue

Reported revenue for 2012 increased 0 5% to £764 million (2011 £760 million) A segmental analysis of revenue is provided opposite which illustrates the strong growth performance from the SI brand, offset by a decline in sales of OEM products Further commentary on performance by segment in provided in the Operating review

Gross margin

Gross margin from the core MIS business increased to 49.9% (2011 471%) This improvement is a consequence of manufacturing improvements and favourable shifts towards higher margin consumable elements of the Resposable® range For 2012 SI Brand represented 70% of MIS business (2011 67%)

Operating expenses

Operating expenses increased by £709,000 during the period to £2 54 million (2011 £1.83 million) This increase primarily resulted from exceptional items in the period (£294,000, see below) increased amortisation of product development intangible assets (£150 000) charges for share-based payments (£66,000) and initial investment into new areas of MIS (£123 000) Notwithstanding this increase, the Group continues to rigorously control costs

Exceptional items

During the first half of 2012 we incurred one-off costs of £294,000 (2011 £nil) as a consequence of restructuring various operational areas of the business In order to provide a more accurate picture of the underlying performance of the business the profitability figures quoted below and in the Chairman's statement and Operating review are adjusted to exclude these non-recurring costs

Finance costs

As noted below we utilised an overdraft provided by our bankers for the majority of 2012 and accordingly finance income was negligible Interest payable on the bank overdraft amounted to £31,000 (2011 £15 000)

The majority of the finance cost of £94,000 arose in respect of finance lease obligations where the charge for the year totalled £63 000 (2011 £58 000) Following the major investment of recent years, capital expenditure in 2012 was minimal and this cost is expected to reduce next year

EBITDA and operating profit

We are pleased to report that EBITDA (excluding exceptional items) increased from £2.83 million to £2.89 million in line with the slight increase in revenue which represents a strong signal that we are continuing to carefully manage our costs

We believe EBITDA is the most appropriate measure of profitability for the business as it excludes the impact of significant non-cash charges for depreciation and amortisation which mask underlying performance at operating profit level

Operating profit for the year reduced to £132 million (2011 £177 million) due to the increase in amortisation of product development costs of £150 000 and the exceptional items of £294,000

Revenue (£m)

£7.64m +0 5%
2011 £760m

12	5 33	**SI Brand** +12 9%
11	4 73	
12	2 20	**OEM** -21 5%
11	2 81	
12	0 10	**Industrial** +44 3%
11	0 07	

Taxation

The Group recognised a tax charge of £547,000 (2011 £33,000 credit) reflecting a deferred tax charge of £834 000 offset by a corporation tax credit of £287,000 The effective rate of tax of 44% is distorted by a one-off adjustment to the deferred tax asset in respect of trading losses of £441,000 The underlying effective tax rate is below the headline rate of corporation tax and we expect this to be the case in the future due to the Patent Box and Research and Development regimes

During 2012 the Group submitted enhanced Research and Development claims in respect of 2011 and 2010 and elected to exchange tax losses for a cash refund At 31 December the balance sheet included an asset of £287,000, the majority of which has been received at the date of these financial statements

Earnings per share (EPS)

The Group achieved 0 17p (2011 0 44p) basic EPS in 2012 which is distorted by the exceptional items in the period of £294,000 and the adjustment to deferred tax of £441 000 referred to above Adjusting for these, underlying EPS would be 0.35p

Intangible and tangible assets

As in previous years, we have continued our investment in product development The Board is confident with this investment strategy and accordingly, £1.85 million (2011 £2.50 million) of costs have been capitalised during the year, increasing the total amount of capitalised costs to £8 33 million (2011 £6 48 million)

The amortisation charge against capitalised costs increased significantly to £700 000 (2011 £550,000) reflecting that products developed in recent years are now launched and selling to customers The amortisation charge will undoubtedly continue to increase in future reporting periods, reducing reported profits No impairments have been identified at 31 December 2012 following review by the Board

Capital expenditure during the year was minimal at £183,000 (2011 £1 41 million) following the major investment programme during 2010 and 2011 to implement our strategy of in-house manufacturing.

Foreign currency

During 2012 the Group has continued to generate significant surplus US Dollars through sales to customers These have either been sold into Sterling at spot rates or market risk has been eliminated through the use of forward contracts In respect of the Euro, the Group has largely achieved a natural hedge with Euro denominated receipts being in line with Euro payments The Group will continue to monitor the need for forward contracts depending upon the level of natural hedging achievable and the extent to which surplus currencies are expected to be generated

Cash flow and net debt

Cash flows generated from operations before working capital movements were strong at £2 66 million (2011 £2 83 million) However the significant working capital increase during the year of £1 96 million (see below) reduced cash generated from operations to £706,000 (2011 £1.85 million) As expected, cash used in investment activities reduced during the year to £1 98 million (2011 £2.84 million)

At 31 December net debt, which is defined as cash and cash equivalents less bank overdraft and obligations under finance leases, stood at £2 63 million (2011 £1 11 million) In addition to existing finance lease facilities, the Group secured a £2 million overdraft facility from HSBC for the period through to 30 September 2013 At 31 December 2012, £1 42 million of this facility was utilised

Working capital

Working capital increased by £1.96 million to £6 60 million (2011 £4 64 million) £747,000 of this increase is attributable to inventory levels, however approximately £0 5 million of this increase reversed in the first week of 2013 when the sales referred to in the Chairman's statement were recognised Trade receivables increased by £1 28 million compared to the prior year which reflects the impact of sales of YelloPort+plus™ on extended credit (£637,000) and also the phasing of sales with significant revenue recognised in December 2012

We are committed to improving our manufacturing processes through lean manufacturing, and we believe that this will yield benefits over the course of the year Our distributors operate in many different countries where credit terms and local practices vary significantly Consequently, relatively high trade receivables are a feature of our business that we do not expect to change in the short term

Mike Thornton
Chief Financial Officer
8 April 2013

Review of the year

Principal risks and uncertainties

How we manage risks.

The management of the business and the nature of the Group's strategy are subject to a number of risks which the Directors seek to mitigate wherever possible The principal risks are set out below

Issue	Risk and description	Mitigating actions
Patents and proprietary rights	The Group's success is dependent upon its ability to establish, file and protect intellectual property relating to the development of its proprietary products for eventual sale or license Whilst the Group seeks patent protection where appropriate for its developments, there can be no assurance that patent applications will mature into granted patents or that existing patents will provide the Group with sufficient protection in the case of infringement by third parties, or be successfully challenged or revoked by competitors	The Group has in place an established process for the development of new products Protection of proprietary rights is considered from the genesis of a product through the design process The Concept team has a team member dedicated to patent work, both investigating the Group's ability to protect and also ensuring protection against products available for sale or in more advanced stages of development The Group continues to work with two principal patent attorneys which provides necessary expertise and also familiarity with the Group's product range
Regulatory approval	As an international business a significant proportion of the Group's products require registration from national or federal regulatory bodies prior to being offered for sale With our major product lines now having FDA approval in the US, we are subject to their audit and inspection of our manufacturing facilities There is no guarantee that any product developed by the Group will obtain and maintain national registration or that the Group will always pass regulatory audit of its manufacturing processes Failure to do so could have severe consequences upon the Group's ability to sell products in the relevant country	The Group has a dedicated Quality department which ● assists product development teams with support as required to minimise the risk of regulatory approval not being obtained on new products, and ● ensures that the Group operates processes and procedures necessary to maintain relevant regulatory approvals Whilst there is no guarantee that this will be sufficient, the Group has invested in people with the appropriate experience and skills in this area which mitigates this risk significantly

Issue	Risk and description	Mitigating actions
Product obsolescence	Due to the nature of the market in which the Group operates, products are subject to technological advances and, as a result, obsolescence	The Directors are committed to the research and development of new products, both within Laproscopy and other areas of MIS This should enable the Group to react effectively to developments within the market
Dependence upon reimbursement	The commercial success of the Group's products is partly dependent upon reimbursement levels for laparoscopic procedures set by governments, health authorities, private insurers and other organisations There is no guarantee that changes in reimbursement policy in the Group's main markets will not have an impact on the ability to sell products into those markets	The Group sells its products in the main MIS markets across the globe This mitigates the impact on the Group of changes within an individual territory The Group has a range of cost-effective products, particularly through the Resposable® concept, which means it is well positioned to weather downward changes in reimbursement policy
International trade regulation	The Group operates in a number of territories across the world subject to local laws and regulations, including trading. There is a risk that changes in regulation within an individual territory may have a material impact on the Group's ability to trade and supply product	The Group works closely with distributors and OEM partners to ensure that changes to local legislation are understood, and where possible, addressed Where necessary, the Group works with legal advisors to ensure risks are fully understood and mitigated
Foreign exchange risk	The Group's functional currency is UK Sterling, however it receives significant export income in US Dollars Whilst the Group makes some purchases in this currency, it does not create a natural hedge of the foreign exchange risk Accordingly, the financial position and performance of the business is exposed to movements in US Dollar rates which it is unable to control	The Group monitors currency exposures on an on-going basis and enters into forward currency arrangements where considered appropriate to mitigate the risk of material adverse movements in exchange rates impacting upon the business Euro and US Dollar cash balances are monitored regularly and spot rate sales into sterling are conducted when significant currency deposits have accumulated

Review of the year

Corporate social responsibility

Our community approach.

Corporate Social Responsibility (CSR) lies at the heart of everything we do It is integral to the sustainability of our business and informs all of our actions, all of the time

Highlights

- New scheme to roll out this year, enabling employees to observe CAB members operating
- In 2012 the Board gave employees the opportunity to participate in a share scheme option
- Two of our apprentices were invited to attend a reception hosted by the Deputy Prime Minister Nick Clegg to celebrate apprenticeships

Surgical Innovations (SI) is committed to building a sound Corporate Social Responsibility (CSR) policy and during the last year we have been keen to integrate CSR across the business to help improve performance Our CSR commitments cover the following areas employees apprentices, business ethics, environment, health and safety, and community engagement

Employees

It is important for us to attract and retain the right calibre of people – a vision that we see as the basis for our future success. All employees, regardless of their role in SI, take part in the same core skills surgical training exercises as surgeons, allowing them to truly immerse themselves in the role of the end user
The one-day induction course is carried out by the Chief Executive Officer, and is a valuable training resource for all staff Employees of all levels are also being offered the opportunity to go into local hospitals to observe one of our Clinical Advisory Board (CAB) members operating in theatre It is important that everyone in the Company understands exactly how our instruments are used by surgeons and therefore how critical their own personal role is within this process This is a new scheme which will be rolled out this year

In 2012 the Board, as a thank you to everyone's hard work and dedication, gave employees the opportunity to participate in a share scheme option The scheme gives staff the chance to purchase shares in three years' time at a fixed price and benefit from the future growth and success of the Group

SI staff frequently embark on charitable ventures and we actively encourage employee participation in local fundraising events
SI consistently seeks to financially match employee sponsorship contributions up to a predefined level

Apprentices

SI understands the positive impact the younger generation has to offer the Group and we run a proactive apprenticeship scheme across the organisation to nurture young talent Apprentices are enrolled in an Advanced Mechanical Engineering course at Leeds City College providing them with a sound theoretical knowledge base They are placed on ten-week placements in five different areas of the business including quality, product development engineering, machine shop, assembly and injection moulding, allowing them to gain practical skills in the specialist medical device industry The apprenticeship scheme gives SI the opportunity to train apprentices to our exacting Company standards and help towards combatting the skills shortage throughout the manufacturing industry

Recently two of our apprentices – Louis Ball and James Littlewood – were invited down to London to attend a reception hosted by the Deputy Prime Minister Nick Clegg to celebrate apprenticeships and showcase the contribution they make to the economy

Speaking at the reception Deputy Prime Minister Nick Clegg said "I was delighted to welcome Louis and James to Admiralty House, after being hugely impressed when I visited Surgical Innovations earlier this year It's clear they are making a valuable contribution and their hard work now will no doubt set them up for a bright future"

Business ethics

We strive to play an integral role in society and our core value is to meet the needs of forward-thinking surgeons and clinicians by supplying high-quality cost-effective instrumentation that empowers surgeons and provides patients with an improved quality of life We have also introduced a Resposable® range of instruments, that combine reusable and disposable components, so surgeons can use high-quality instrumentation while also saving their hospitals hundreds of pounds per procedure In a market that is dominated by expensive throw-away devices our Resposable® instruments are seen as a "breath of fresh air" by both surgeons and procurement managers across the globe

Apprentices Louis Ball and James Littlewood at a reception hosted by the Deputy Prime Minister Nick Clegg

Deputy Prime Minister Nick Clegg during his recent visit to Surgical Innovations

Review of the year

Corporate social responsibility continued

UK consultant surgeon James Halstead operating

Designers and CAB members sharing ideas

Business ethics continued

Our Clinical Advisory Board (CAB) consists of renowned surgeons who work in close collaboration with our design team to advise on existing and potential new product lines, ensuring SI's innovations meet the needs of surgeons and patients alike Following the success of our UK CAB we have also started to introduce an International Clinical Advisory Board (ICAB), which will be made up of key surgeons from across the globe Over the coming year we will be working with our international partners to populate this Board and introduce key opinion leaders from around the world

Community engagement

We feel it is vital to support our local community and have actively contributed to the creation of Leeds Health Hub The Hub is made up of medical companies based in Leeds together with representatives from the University of Leeds, Leeds Metropolitan University and Leeds City Council Its aim is to help to place Leeds on the map as a leader in medical innovation

This vision was realised further in January when SI received the final grant offer letter for the Regional Growth Fund (RGF), which is worth up to £5.05 million to SI in Government funding. The grant will be used to develop a state of the art research and development facility and clinical training centre, with a reasonable expectation of creating over 300 jobs in the Leeds City region over the next twelve years The creation of a clinical training centre will allow SI to further the relationships it has with leading clinicians, both UK and international and will act as a magnet for pioneering surgeons looking to develop new skills and instrumentation in minimal invasive surgery

SI is also partnered with universities and hospitals throughout the region including Leeds University and Bradford University and has just completed two Knowledge Transfer Partnerships (KTP), helping us to stimulate innovation in the business improve processes and draw upon the universities' expertise while allowing the universities access to industry The KTP scheme is a partnership between the universities, SI and part-funded by the Government

Environment

Maintaining excellent environmental standards is integral to all organisations and we strive to minimise the effect of our operations on the environment wherever possible We look to review the impact of all of SI's policies and operations covering emissions and fuel efficiency, noise, waste, energy use and recycling We encourage ideas and suggestions from all employees in this regard

Health and safety

SI has an established Health and Safety Committee that is made up of employees from across the organisation The committee meets on a regular basis to discuss any health and safety issues that have been raised from all areas of the business and how we can improve health and safety across SI

Review of the year

Case study

How does the programme work?

It is four year scheme and as part of the course apprentices will participate in ten-week placements in five different areas of the business including quality, product development engineering, machine shop, assembly and injection moulding Within the programme apprentices develop basic engineering skills, knowledge and practical experience by working with machine tools, centre lathes and milling machines

Apprentice James Littlewood in the machine shop at Surgical Innovations

SI's apprenticeship scheme

Combatting the skills shortage throughout the manufacturing industry

Nurturing young talent

At SI we understand the positive impact the younger generation has to offer We run a proactive apprenticeship scheme across the organisation to nurture this young talent The scheme allows us to train apprentices to our exacting Company standards and helps towards combatting the skills shortage throughout the manufacturing industry It has received much praise from many external bodies and was awarded Medium Employer of the Year at the Leeds Apprenticeship Recognition Awards Each year we will be increasing the number of apprentices employed

"I am currently on my second year on the apprentice scheme and I'm finding it really interesting It is a better alternative to higher education because you are learning new, practical skills each and every day. It is exciting to think that the medical devices I help make are used in patients around the world"

James Littlewood, apprentice, 19

Governance
Board of Directors

Name Doug Liversidge CBE
Position Non-executive Chairman
Board committees Remuneration Committee (Chairman), Audit Committee

Experience Doug was educated in Sheffield and graduated with a degree in Metallurgy in 1957 Employed for 21 years at British Steel, Doug attained the position of Chief Quality Manager

After moving to G W Thornton as Managing Director and subsequently appointed Chief Executive, Doug guided the company through its flotation on the London Stock Exchange in March 1987 and was instrumental in the company winning numerous prestigious business awards including the Queen's Award to Industry for Export Achievement and twice the Cutlers Acclaim Award for Corporate Growth In 1991 Doug was awarded South Yorkshire Businessman of the Year Doug was previously Chairman of Medilink Yorkshire and Humber He is proud to have held the office of Master Cutler in Hallamshire from 1998 to 1999

Doug has two honorary degrees from Sheffield University and Sheffield Hallam University and in 2000, was appointed Chairman of the South Yorkshire Learning & Skills Council by Government Office, Leeds

He was awarded the CBE in the 2000 New Year's Honours List for services to industry In 2012 Doug received the coveted Medilink Beacon Award for Outstanding Contribution to Healthcare in recognition of his continued services to the medical device industry

Other appointments Chair of the Leeds Innovation Health Hub and Fusion IP plc

Name Graham Bowland
Position Chief Executive Officer

Experience Graham graduated from Cardiff University with an honours degree in Physics in 1982 He qualified as a Chartered Accountant in 1987 whilst working for a local firm of chartered accountants

After gaining substantial experience in the private sector Graham joined SI in February 1999 as Financial Controller and was promoted in the same year to the Group Board as Finance Director and Company Secretary

Appointed Joint Managing Director of Surgical Innovations Limited in 2000 and made sole Managing Director in 2008, Graham has been instrumental in building upon the Company's reputation within the industry for innovation and in-house manufacturing In 2010, Graham became Group Chief Executive Officer, continuing to build the Company's strategy

Other appointments Until 2012, represented the Leeds city region on its BIG Panel reporting to the Local Enterprise Partnership (LEP) and currently a member of the Leeds Innovation Health Hub

Name Mike Thornton
Position Chief Financial Officer and Company Secretary

Experience Mike is a Fellow of the Institute of Chartered Accountants He joined the Group in December 2011 as Finance Director of the main trading subsidiary and was appointed as Chief Financial Officer of the Group in May 2012 He also acts as Company Secretary

Mike joined the Group from professional services firm PwC Mike trained as a graduate with PwC and then progressed through to Director over a 14-year period, working in offices in Hull, Leeds and London Whilst at PwC he primarily provided audit, due diligence and stock exchange accountancy services to a wide range of clients across the Yorkshire region

Name Colin Glass
Position Non-executive Director
Board committees Audit Committee (Chairman), Remuneration Committee

Experience Colin is a Chartered Accountant and a partner in Winburn Glass Norfolk He is a founder Director of Surgical Innovations Limited and was instrumental in securing early funding and in the reverse takeover of Haemocell plc in 1998, which resulted in the quotation of the Company on AIM

Other appointments Colin is a Non-executive Director of several companies, including Straight PLC and Getech Group plc, which are quoted on AIM He is the Chairman of SI's Audit Committee and a member of SI's Remuneration Committee Using his expertise in financial and corporate advisory matters, Colin has built up a wide range of contacts from various industries and organisations which benefit the companies with which he is involved

Name Ray Simkins
Position Non-executive Director
Board committees Remuneration Committee, Audit Committee

Experience Ray is a mechanical engineer by training and worked for The Getz Group since 1966 spending the majority of his career working within group companies in the USA, Japan, Australia and South East Asia Ray is a member of both the SI's Audit and Remuneration Committees and, with experience in international marketing, logistics and manufacturing in the healthcare field He provides invaluable input into many aspects of the Board's activities

Other appointments Ray is currently President of the Getz Group and continues to focus his activities in the USA and Asia/Pacific region Ray has been a Non-executive Director since 1996 and was instrumental in securing investment from Getz prior to the reverse takeover of Haemocell plc in 1998

Name Professor Mike McMahon
Position Non-executive Clinical Director and Chair of the Clinical Advisory Board

Experience Mike, a founder Director of Surgical Innovations Ltd, became Non-executive Clinical Director in October 2007 He is an Emeritus Prof of Surgery at the University of Leeds, and practices as a Consultant Surgeon at the Nuffield Hospital, Leeds He has carried out research and development of laparoscopic surgery and has demonstrated operative techniques in many countries He is past President of the Association of Laparoscopic Surgeons of Great Britain and Ireland and was also Tutor in MIS at the Royal College of Surgeons and Director of the Leeds Institute for Minimally Invasive Therapy

Other appointments Mike's past roles include President of the Pancreatic Society of Great Britain and Ireland and Chairman of the Education Committee of the European Association of Endoscopic Surgery He is a Non-executive Director of Cipher Surgical Limited

Governance

Clinical Advisory Board

Name Philippe Grange
Speciality. Laparoscopy

Philippe qualified from the Medical School in Nancy and then qualified from Poitiers in general surgery in 1986 and urology in 1989 He is now a Consultant at King's College Hospital in London, Honorary Professor of Urology at The Beijing Hospital and Honorary Consultant Laparoscopist at Guy's Hospital and University College of London Hospital.

His main field of interest lies in pioneering laparoscopic procedures and he has performed over 2,000 major laparoscopic procedures in oncological urology, urogynaecology and abdominal surgery

Philippe has been teaching and mentoring radical prostatectomy in 40 centres for the past three years He is currently a course Director for laparoscopic skills (BAUS, China, RCS, UCLH, ESI) and is an adviser to the Royal College of Surgeons for laparoscopic skills courses He is an adviser on the Board of the International Society of Cryosurgery

Name. Marco Adamo
Speciality Laparoscopy

Marco is a Consultant Surgeon and Bariatric Surgery Lead at the prestigious University College London Hospital (UCLH) where he has worked since 2007 He graduated in 1995 with full marks and honours in Palermo, Italy, and also completed his training in general surgery at the same university He has been living in the United Kingdom since 2000 dedicating his activity to advanced laparoscopic surgery and laparoscopic bariatric (obesity) surgery He was awarded an MD by the University of Leeds for his research on appetite hormones and bariatric surgery

He is a pioneer of single incision bariatric surgery having performed the first single incision laparoscopic sleeve gastrectomy in the UK and often runs advanced training courses for UK and European surgeons in laparoscopic bariatric surgery and laparoscopic hernia surgery

Name James C Halstead
Speciality. Laparoscopy

James graduated from the University of Cambridge with a degree in Medicine in 1996 and is trained in cardiothoracic surgery and general surgery, specialising in bariatric and upper gastrointestinal tract surgery He is now Consultant Surgeon at Leeds Nuffield hospital

James has developed specialist obesity practise utilising the latest advances in laparoscopic surgery for gastric banding, bypass and sleeve gastrectomy In 2009, James was awarded a Clinical Excellence Award in recognition of his work in bariatric surgery

Name Ian Brayshaw
Speciality Laparoscopy

Ian graduated as an Operating Department Practitioner in 1994 He has continued to train in this area and in 2004 completed a Diploma in Advanced Surgical Practice at Huddersfield University and went on to complete The Royal College of Surgeons Basic Skills course He is a surgical first assistant for the Leeds General Infirmary, where he has worked since 1981

Ian specialises in laparoscopic bariatric surgery, upper GI and colorectal surgery He has been the first assistant in over 500 bariatric cases and 50 colorectal pouch procedures in the UK.

Name. Alfred Cutner
Speciality Laparoscopy

Alfred, consultant at University College Hospital London, achieved a distinction in obstetrics and gynaecology in 1985 and went on to obtain his Doctorate in Medicine from the University of London in 1993

Alfred gained his Part II to become a Member of the Royal College of Obstetricians and Gynaecologists in 1993, having obtained Part I in 1987

He has written a book entitled "Basic Urogynaecology" (1993) and has also contributed to many others, including "The Investigation and Management of Urinary Incontinence in Women" (1995) and a more recent chapter in R Kearney A Cutner "Laparoscopic Colposuspension and Paravaginal Repair" Alfred has been a member of several committees and currently holds the position of President of the BSGE

Name. Jon Conroy
Speciality Arthroscopy

Jon is a Consultant Orthopaedic Surgeon specialising in joint replacements and arthroscopic, or "keyhole", surgeries to the hip and knee and is a member of the British Hip Society International Society of Hip Arthroscopy The British Orthopaedic Association and a Fellow of The Royal College of Surgeons of England He also holds a Masters degree in Mechanical Engineering from the University of Leeds and has published research in several medical journals and won the GlaxoSmithKline Orthopaedic Essay Prize in 2005 and the John Fitton Prize for Orthopaedic Specialist Registrars in 2006

Name Siôn Glyn-Jones
Speciality Arthroscopy

Siôn works as a Consultant Hip Surgeon in the Adult Hip and Knee Reconstruction Service at the Nuffield Orthopaedic Centre He undertakes all aspects of adult hip surgery and has a specialist interest in the treatment of hip arthritis in the young patient and revision hip arthroplasty

Siôn studied medicine at Cambridge and later conducted clinical attachment in London Thereafter, he went on to complete his surgical and orthopaedic training in Oxford where he gained a DPhil degree

In conjunction with his colleagues at the OOEC, Siôn is currently investigating the role of mechanics in the initiation of hip osteoarthritis and improving design and outcomes of total hip arthroplasty

Name Chris Sutton
Speciality Laparoscopy

Chris is a Consultant General and Upper Gastrointestinal Surgeon at Spire Leicester Hospital and the Leicester Royal Infirmary studied medicine at the University Of Wales College Of Medicine and qualified in 1993 After undertaking junior surgical training in South Wales, Chris moved to Leicester and completed both senior surgical training and a higher degree in cancer research He also spent a year gaining specialist experience in Upper Gastrointestinal and Obesity Surgery in the University Hospitals of Leeds under the supervision of international experts in these fields

He has been awarded the first British Obesity Surgical Society Bariatric Surgical Fellowship in the UK and holds a certificate in Laparoscopic Obesity Surgery from the European School of Laparoscopic Surgery in Brussels

International Clinical Advisory Board

Name Sean Barnett
Speciality Paediatric
Joined in year. March 2013

Sean is an Assistant Professor of Surgery and Paediatrics at Cincinnati Children's Hospital Medical Center and the University of Cincinnati College of Medicine He is a staff and core trauma surgeon in the Division of Pediatric General & Thoracic Surgery, as well as one of three adolescent bariatric surgeons in the Surgical Weight Loss Program for Teens, all housed within Cincinnati Children's Hospital Medical Center He is currently head of the Operating Room Equipment and Standards Committee Sean is a graduate of Purdue University (BSME), Wright State University (MS in Anatomy), and the Boonshoft School of Medicine (Alpha Omega Alpha). He completed his general surgery training and a fellowship in surgical infectious diseases at the University of Minnesota and a fellowship in paediatric surgery at Cincinnati Children's Hospital Medical Center He is boarded in both general and paediatric surgery, a member of the American College of Surgeons (ACS), the American Pediatric Surgical Association (APSA), the American Association of Pediatrics (AAP) and the International Pediatric Endoscopy Group (IPEG)

Name Jake Timothy
Speciality Orthopaedic Spinal and Neurosurgery
Joined in year December 2012

Jake is a Neurosurgeon based in Leeds He completed the National Spine Fellowship in Leeds in 2001 and 95% of his workload is spine both acute and elective He is the elected UK delegate for the European Association of Neurosurgeons (EANS) training course and the UK representative for the Young Neurosurgeons of the World Federation of Neurosurgeons He is the NICE specialist advisor for XLIF, head injuries, dynamic stabilisation and interspinous process distractors

Last year Jake was awarded the Excellence in Healthcare delivery for the vertebroplasty and kyphoplasty service he developed with his radiology colleague He was also recently appointed as Vice-chair to the regional MSCC committee

Jake has been dedicated to teaching and training around the world and has developed a spinal surgical service in conjunction with orthopaedic surgeons in Bangladesh

Name John Griffith
Speciality Laparoscopy
Joined in year December 2012

John is a Consultant Colorectal and General Surgeon at Bradford Royal Infirmary and the Yorkshire Clinic He specialises in colorectal surgery including inflammatory bowel disease and functional disorders, as well as laparoscopic general surgical procedures including cholecystectomy and hernia operations.

John qualified from Nottingham University in 1985 He moved to Leeds and completed his higher surgical training under the tutelage some of the country's leading laparoscopic surgeons including Professor Mike McMahon and Professor John Monson He also spent a year gaining specialist experience in colorectal surgery at the Singapore General Hospital under the guidance of Professor Francis Seow Chien

He has pioneered laparoscopic colorectal surgery in Bradford and was awarded the status of a National Trainer in laparoscopic colorectal surgery in 2008

Name Bassem Safadi
Speciality Laparoscopy
Joined in year July 2012

Bassem is an Associate Professor of Clinical Surgery at the American University of Beirut in Lebanon Bassem is one of the leaders in laparoscopic and bariatric surgery in Lebanon and the Middle East He is certified by the American Board of Surgery and is a Fellow of the American College of Surgeons and a member of the American Society of Bariatric and Metabolic Surgery Prior to his return to Lebanon in 2005 Bassem was the Director of the Minimally Invasive Surgery Fellowship at Stanford University He completed his surgical training from 1992 until 1999 at the Washington Hospital Center in Washington DC, Case Western Reserve University in Cleveland, Ohio and the University of California San Francisco

Governance
Advisers

Company Secretary and registered office
Mike Thornton
Clayton Wood House
6 Clayton Wood Bank
Leeds LS16 6QZ

Registered number
2298163

Nominated adviser
Panmure Gordon (UK) Limited
One New Change
London EC4M 9AF

Solicitors
Walker Morris
Kings Court
12 King Street
Leeds LS1 2HL

Auditor
Grant Thornton UK LLP
No 1 Whitehall Riverside
Leeds LS1 4BN

Broker
Panmure Gordon (UK) Limited
One New Change
London EC4M 9AF

Registrars
Capita Registrars
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Bankers
HSBC Bank plc
7 Prospect Crescent
Harrogate HG1 1RN

Financial public relations
Walbrook PR Limited
4 Lombard Street
London EC3V 9HD

Governance

Report of the Directors

The Directors present their annual report, together with the audited financial statements, for the year ended 31 December 2012

Principal activities and business review

The Company is the holding company of a Group whose principal activities in the year involved the design, development, manufacture and sale of devices for use in minimally invasive surgery (MIS) and industrial markets In international markets, the Group sells through independent healthcare distributors, through original equipment manufacturer (OEM) and licensing contracts with major suppliers of medical equipment A review of the Group's activities during the year is included within the Chairman's statement on pages 8 and 9, the Operating review on pages 10 to 14 and the Financial review on pages 16 and 17

Results and dividends

The Consolidated statement of comprehensive income for the year is set out on page 36

The Directors believe that at this stage in the Group's development it would be more appropriate to continue its focus on investment and the development of the Group's activities for the longer term and hence do not recommend the payment of a dividend The profit for the period will be transferred to reserves

Research and development

The Group's activities in this area have focused principally on the continuing development of innovative instruments for use in the field of MIS

Employees

The commitment and ability of our employees are key factors in achieving the Group's objectives Employment policies are based on the provision of appropriate training, whilst annual personal appraisals support skill and career development

The Board encourages management feedback at all levels to facilitate the development of the Group's business The Group seeks to keep its employees informed on all matters affecting them by regular management and departmental meetings The Company operates an Enterprise Management Incentive (EMI) share option scheme for all employees

It is the Group's policy to give full and fair consideration to all applications for employment from disabled persons having regard to their particular aptitudes and abilities and to encourage the training and career development of all personnel employed by the Group, including disabled persons Should an employee become disabled, the Group would, where practicable, seek to continue the employment and arrange appropriate training

Directors

The names of the current Directors of the Company and their biographical details are set out on pages 24 and 25 With the exception of M R Thornton, who was appointed to the Board on 23 May 2012 all Directors served throughout the year

Directors' interests

The interests in the share capital of the Company of those Directors in office at the end of the year were as follows

Ordinary shares of 1p each	31 December 2012 Beneficial	1 January 2012 Beneficial
D B Liversidge CBE	**7,171,821**	6,171,821
N G Bowland	**5,028,498**	4,528 498
M R Thornton	—	—
C Glass	**5,881,602**	5,881 602
R Simkins	**7,269,461**	7,269,461
M J McMahon	**17,218,511**	17218511

Apart from the interests disclosed above and the options referred to on page 33, no Directors held interests, at any time during the year, in the share capital of the Company or other Group companies There were no other changes in Directors' interests between the year end and 8 April 2013

Otherwise than as disclosed in note 16, no Director has an interest in any material contract, other than contracts of service and employment, to which the Group was a party

Copies of the Directors' service contracts are available for inspection at the registered office of the Company, Clayton Wood House, 6 Clayton Wood Bank, Leeds LS16 6QZ and will be available at this year's Annual General Meeting (AGM) for 15 minutes prior to and during the whole course of the Meeting

Governance

Report of the Directors continued

Substantial shareholdings

Other than the Directors own holdings, the Board has been notified that as at 15 March 2013, the following shareholders on the Company's share register held interests of 3% or more of the issued ordinary share capital of the Company

	Number of shares (%)
Getz Bros & Co (BVI) Inc	**49,248,810** (12 17%)
R C Greig Nominees Limited	**30,379,054** (7.51%)
Barclayshare Nominees Limited	**28,351,402** (7 01%)
Ferlim Nominees Limited	**24,739,587** (6 12%)
TD Direct Investing Nominees (Europe) Limited	**21,295,417** (5 26%)
HSBC Global Custody Nominee (UK) Limited	**20,633,062** (5.09%)
The Bank of New York (Nominees)	**19,155,616** (4 73%)
HSDL Nominees Limited	**16,619,104** (4 12%)

Share issues

During the year the following ordinary shares of 1p were issued in respect of exercised share options

- 3,500 000 at 15p
- 3,654,546 at 17p and
- 2 234,454 at 3 5p

Creditor payment policy

The Group and Company policy concerning the payment of suppliers is to

- settle the terms of payment with those suppliers when agreeing the terms of each transaction,
- ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts and
- pay in accordance with its contractual and other legal obligations

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

Statement of Directors' responsibilities

The Directors are responsible for preparing the Report of the Directors 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 the Directors have to prepare the Group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs) and have elected to prepare the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP) Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs and profit or loss of the Company and Group for that period In preparing these financial statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent
- ensure applicable IFRSs and UK GAAP 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 adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and Group and enable them to ensure that the financial statements comply with the Companies Act 2006 They are also responsible for safeguarding the assets of the Company and Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

Insofar as each of the Directors is aware

- there is no relevant audit information of which the Company's auditor is 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 auditor is aware of that information

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

Summary of Key Performance Indicators (KPIs)

The Directors have monitored the overall progress of the Group and the individual strategic elements by reference to certain financial and non-financial KPIs as set out below

Financial performance

KPIs are in place to measure revenue by segment, gross margin, operating margin and profit before tax Actual performance, together with relevant commentary is provided within the Chairman's statement on pages 8 and 9, the Operating review on pages 10 to 14 and the Financial review on pages 16 and 17

Employee satisfaction

The Group KPI, which was achieved in 2012, is to ensure all members of staff have a formal annual review in order to measure staff morale, training needs and personal development

Leadership

The performance of Directors and management in conjunction with overall Group strategy and planning is assessed through the use of individual objectives which are set annually

Innovation

KPIs are positioned to measure the creativity and inventiveness of employees to monitor the number of new patents filed and the number of completed projects Commentary is provided in the Operating review on pages 10 to 14

Donations

The Group made a small number of charitable donations during the year, principally to local projects and sponsorship of employees' charitable fundraising events The Group made no political donations

Principal risks and uncertainties

The management of the business and the nature of the Group's strategy are subject to a number of risks which are set out on pages 18 and 19

The Directors are of the opinion that a thorough risk management process is adopted which involves the formal review of all the risks identified Where possible, processes are in place to monitor and mitigate such risks

Financial risk

The Group's activities expose it to a variety of financial risks as set out below Given the size of the Group, the Board of Directors has not delegated the responsibility of monitoring financial risk management to a sub-committee of the Board Instead, policies set by the Group are implemented by the Group's finance department Taking each area of financial risk in turn

a) Market risk The principal market risk exposure relates to exporting goods in US Dollars Further quantitative analysis is provided in note 12 to the Consolidated financial statements

b) Credit risk The Group is exposed to credit risk through offering extended credit terms to those customers operating in markets where extended payment terms are themselves taken by local government and state organisations. The Group is also exposed to credit risk through customer concentration Both of these aspects of credit risk are managed through constant review and personal knowledge of the customer concerned Payment plans are agreed and monitored in all such cases to minimise credit risk

c) Liquidity risk The Group manages its liquidity needs by carefully monitoring all scheduled cash outflows Liquidity needs are monitored in various time bands, on a day-to-day and week-to-week basis, as well as on the basis of a rolling 13 week projection Longer-term needs are monitored as part of the Group's regular rolling monthly re-forecasting process Funding for long-term liquidity is secured by an adequate amount of committed credit both through working capital and asset finance facilities

d) Interest rate cash flow risk The Group has both interest-bearing assets and interest-bearing liabilities Interest-bearing assets include only cash and cash equivalents which are held on deposit at both fixed and floating rates Interest-bearing liabilities include hire-purchase liabilities which are at fixed interest rates

Auditor

Grant Thornton UK LLP has indicated its willingness to continue in office A resolution for their re-appointment as independent auditor will be proposed at the AGM

By order of the Board

M R Thornton
Company Secretary
8 April 2013

Review of the year
Governance
Financial statements
Shareholder information

Governance

Report on remuneration

Remuneration of Executive Directors

The Board recognises that Executive Director remuneration is of legitimate concern to shareholders The Group operates within an innovative and competitive arena that places constant demands on the technical abilities of the Group Its performance depends on the individual contributions of Executive Directors and employees and the Group believes in rewarding all those who have made a positive contribution in the development of the Group Remuneration of Executive Directors is a matter reserved for the Remuneration Committee

Remuneration Committee

The Remuneration Committee, which meets as required, is made up of the following Directors

D B Liversidge CBE (Chairman)

C Glass

R Simkins

Remuneration policy

The principal objective is to develop policies and recommend proposals appropriate to facilitating the recruitment, retention and motivation of the Executive Directors and in so doing to avoid the Group bearing more than a reasonable and necessary cost Where practical and appropriate, the remuneration of the Executive Directors (and other senior management) is aligned with the interests of shareholders

The Remuneration Committee considers that a successful remuneration policy needs to be sufficiently flexible to take account of future changes in the Group's business environment and in remuneration practice Any changes to policy for years after 2013 will be described in future Reports on remuneration

The remuneration of Executive Directors comprises four main elements

- basic salary to remain competitive in the marketplace, reflecting the experience, level of competence of the individual and comparative base salaries elsewhere within the Group,
- annual bonus payment to provide additional short-term remuneration that directly reflects Group and individual performance,
- share options to reward achievements of target and outstanding business performance over the longer term through the regular grant of options and
- pension arrangements to enable Executive Directors to make appropriate provision for retirement

It is Group policy that a significant proportion of the remuneration of Executive Directors should be performance related

Directors' emoluments – information subject to audit

Details of Directors' emoluments for the year are as follows

	Salary and fees 2012 £'000	Benefits 2012 £'000	Total emoluments 2012 £'000	Total emoluments 2011 £'000	Pension contributions 2012 £'000	Pension contributions 2011 £'000
Executive						
N G Bowland[1]	114	17	131	119	10	41
M R Thornton[2]	51	5	56	—	4	—
Non-executive						
D B Liversidge CBE[3]	36	—	36	30	—	—
C Glass[4]	27	—	27	20	—	—
R Simkins[5]	27	—	27	20	—	—
M J McMahon	27	—	27	20	—	—
Total	282	22	304	209	14	41

1 N G Bowlands pension contribution for the prior year included a discretionary bonus of £30 000
2 M R Thornton was appointed as a Director on 23 May 2012
3 D B Liversidges fees are partly paid to Quest Investments Limited, a company of which he is a director
4 C Glass fees are paid to Winburn Glass Norfolk, a firm of which he is a partner
5 R Simkins fees are paid to Getz Bros & Co Inc., a company of which he is vice-president

Benefits received consist of the provision of motor cars and private health insurance

At 31 December 2012 a loan of £12 166 (2011 £13 566) made available to N G Bowland in 2009 was still repayable

Pension contributions represent payments made to defined contribution schemes Non-executive Directors are not entitled to retirement benefits

Remuneration of the Non-executive Directors is determined by the Board

Contracts of service

No Director has a service contract with a notice period in excess of one year

Directors' share options

Details of the share options held by Directors are as follows

	At 1 January 2012	Exercised during the year	Granted during the year	At 31 December 2012	Option price	Date granted
D B Liversidge CBE	1,500,000	—	—	**1,500,000**	170p	November 2007[1]
	1,000,000	(1,000,000)[3]	—	—	150p	January 2009[1]
	400,000	—	—	**400,000**	170p	November 2009[1]
N G Bowland	2,234,454	(2,234,454)[4]	—	—	350p	November 2007[2]
	1454,546	(1 454 546)[4]	—	—	170p	November 2007[1]
	1400 000	(500 000)[3]	—	**900,000**	150p	January 2009[1]
	2 200,000	(2 200 000)[4]	—	—	170p	November 2009[1]
	—	—	2,500 000	**2,500,000**	900p	June 2012[2]
C Glass	1500,000	—	—	**1,500,000**	170p	November 2007[1]
	1,000 000	—	—	**1,000,000**	150p	January 2009[1]
	400,000	—	—	**400,000**	170p	November 2009[1]
M R Thornton	—	—	2,500,000	**2,500,000**	100p	June 2012[2]
M J McMahon	400,000	—	—	**400,000**	170p	November 2009[1]

1 Share options are exercisable between nil and ten years from the date of the grant

2 Share options are exercisable between three and ten years from the date of the grant

3 The market price of the Company's shares at the date of exercise of these options was 6.5p

4 The market price of the Company's shares at the date of exercise of these options was 10.5p

The gain on exercise of share options during the year (calculated based on the market price at exercise) was £503,000 for N G Bowland and £50 000 for D B Liversidge The market price of the Company's shares at the end of the financial year was 7.25p (2011 10.0p) and the range of market prices during the year was between 6 4p (2011 5.3p) and 12 4p (2011 13.5p)

On behalf of the Board

D B Liversidge CBE
Chairman
8 April 2013

Governance

Corporate governance

Principles of good governance

The Board continues to support the principles of good governance The Board has adopted such procedures as it considers practical and appropriate for an AIM listed group of its size

Application of principles

Directors

The Company supports the concept of an effective Board leading and controlling the Group The Board is responsible for approving Group policy and strategy It meets regularly and has a schedule of matters specifically reserved to it for decision Management supplies the Board with appropriate and timely information and the Directors are free to seek any further information they consider necessary All Directors have access to advice from the Company Secretary and independent professionals at the Group's expense Training is available for new Directors and other Directors as necessary

The Board members are

D B Liversidge CBE	–	Non-executive Chairman
N G Bowland	–	Chief Executive Officer
M R Thornton	–	Chief Financial Officer
C Glass	–	Non-executive Director
R Simkins	–	Non-executive Director
M J McMahon	–	Non-executive Director

Accountability and audit

The Board is responsible for maintaining a sound system of internal control to safeguard shareholders' investments and the Company's assets

The Audit Committee comprises C Glass (Chairman), D B Liversidge CBE and R Simkins who are all Non-executive Directors

The Committee considers the appointment and terms of engagement of the external auditor and assesses the independence of the external auditor and reviews the auditor's policy for the rotation of audit partners

The terms of reference of the Committee include reviewing the scope and results of the external audit and its effectiveness

Communication with shareholders

The Board is committed to effective communication between the Group and its shareholders

It regards the AGM as a means of communicating directly with private investors and encourages their participation All Directors normally attend the AGM and private investors have the opportunity to meet the Directors and discuss any issues on an informal basis Separate resolutions are passed on each issue so that they can be given proper consideration and there is a resolution to approve the annual report and accounts

The shareholders can gain access to information on the Group, as well as to the annual report, through the website, www sigroupplc.com

Internal controls

The Board of Directors is ultimately responsible for the Group's management and internal control systems During the financial period and to the date of approval of the financial statements, it has reviewed the operation and effectiveness of the Group's systems of internal control, which can provide only a reasonable but not absolute assurance against material misstatement or loss

The Board discharges its responsibility for internal financial control through the following key procedures

- the establishment of an organisational structure appropriate to the size of the business, with clearly defined levels of authority and division of responsibilities for approval of external payments and receipt and dispatch of goods,
- a comprehensive budgeting and financial reporting system which compares actual performance with budget on a monthly basis, and
- the formulation by the Board of policies and of approval procedures in a number of key areas such as credit control, expenditure authorisation, stock ordering, treasury management and quality assurance

Going concern

On the basis of the budget for 2013, forecasts prepared by the Directors and currently available banking facilities (which comprise hire purchase arrangements for major items of capital expenditure together with a net group overdraft facility of £2 000,000), the Board has a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future For this reason, the Board has concluded that there are no material uncertainties and that the going concern basis should be adopted in preparing these financial statements

On behalf of the Board

D B Liversidge CBE
Chairman
8 April 2013

Financial statements

Independent auditor's report – Group

Independent auditor's report to the members of Surgical Innovations Group plc

We have audited the Group financial statements of Surgical Innovations Group plc for the year ended 31 December 2012 which comprise the Consolidated statement of comprehensive income, the Consolidated balance sheet, the Consolidated cash flow statement, the Consolidated statement of changes in equity and the related notes The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an 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 auditor

As explained more fully in the Statement of Directors' responsibilities set out on page 30, the Directors are responsible for the preparation of the Group financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the Group financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Boards (APB's) Ethical Standards for Auditors

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www frc.org uk/apb/scope/private cfm

Opinion on financial statements

In our opinion the Group financial statements

- give a true and fair view of the state of the Group's affairs as at 31 December 2012 and of its profit for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

- certain disclosures of Directors' remuneration specified by law are not made or
- we have not received all the information and explanations we require for our audit

Other matter

We have reported separately on the parent company financial statements of Surgical Innovations Group plc for the year ended 31 December 2012

Grant Thornton UK LLP

Paul Houghton
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
Leeds
8 April 2013

Financial statements

Consolidated statement of comprehensive income

for the year ended 31 December 2012

	Notes	2012 £'000	2011 £'000
Revenue	2	**7,639**	7,602
Cost of sales		**(3,779)**	(4,005)
Gross profit		**3,860**	3,597
Other operating expenses		**(2,537)**	(1,830)
Adjusted EBITDA*		**2,888**	2,825
Exceptional items		**(294)**	—
Amortisation of intangible assets		**(700)**	(550)
Depreciation of tangible assets		**(571)**	(508)
Operating profit	3	**1,323**	1,767
Finance costs	5	**(94)**	(73)
Finance income		**4**	11
Profit before taxation		**1,233**	1,705
Taxation	6	**(547)**	33
Profit and total comprehensive income for the period attributable to the owners of the parent		**686**	1,738
Earnings per share, total and continuing			
Basic	7	**0.17p**	0.44p
Diluted	7	**0.17p**	0.42p

The Consolidated statement of comprehensive income above relates to continuing operations.

* Adjusted EBITDA means earnings before interest, taxation, depreciation, amortisation and exceptional items.

Financial statements

Consolidated statement of changes in equity

for the year ended 31 December 2012

	Share capital £'000	Share premium £'000	Capital reserve £'000	Retained earnings £'000	Total £'000
Balance as at 1 January 2011	3 815	75	329	6,369	10,588
Employee share-based payment options	—	—	—	*2*	*2*
Exercise of share options	*137*	*151*	—	—	*288*
Total – transactions with owners	137	151	—	2	300
Profit and total comprehensive income for the period	—	—	—	1,738	1,738
Balance as at 31 December 2011	**3,952**	**226**	**329**	**8,109**	**12,616**
Employee share-based payment options	—	—	—	*68*	*68*
Exercise of share options	*94*	*99*	—	—	*193*
Total – transactions with owners	94	99	—	68	261
Profit and total comprehensive income for the period	—	—	—	686	686
Balance as at 31 December 2012	**4,046**	**325**	**329**	**8,863**	**13,563**

Financial statements

Consolidated balance sheet

as at 31 December 2012

	Notes	2012 £'000	2011 £'000
Assets			
Non-current assets			
Property, plant and equipment	8	**2,990**	3,378
Intangible assets	9	**6,393**	5,243
Deferred tax asset	6	**—**	465
Trade receivables	11	**637**	—
		10,020	9,086
Current assets			
Inventories	10	**3,605**	2,858
Trade receivables	11	**3,953**	3,311
Other current assets	11	**679**	511
Cash and cash equivalents		**—**	3,183
		8,237	9,863
Total assets		**18,257**	18 949
Equity and liabilities			
Equity attributable to equity holders of the parent company			
Share capital	13	**4,046**	3,952
Share premium account	14	**325**	226
Capital reserve		**329**	329
Retained earnings		**8,863**	8,109
Total equity		**13,563**	12,616
Non-current liabilities			
Obligations under finance leases	12	**786**	926
Deferred tax liabilities	6	**369**	—
		1,155	926
Current liabilities			
Bank overdraft		**1,419**	2,983
Trade and other payables		**1,475**	1 859
Obligations under finance leases	12	**422**	385
Accruals		**223**	180
		3,539	5,407
Total liabilities		**4,694**	6,333
Total equity and liabilities		**18,257**	18,949

The accompanying accounting policies and notes form part of the financial statements

The financial statements on pages 36 to 59 were approved by the Board of Directors on 8 April 2013 and were signed on its behalf by

D B Liversidge CBE
Director
Company registered number 2298163

Financial statements

Consolidated cash flow statement

for the year ended 31 December 2012

	2012 £'000	2011 £'000
Cash flows from operating activities		
Operating profit	**1,323**	1767
Adjustments for		
Depreciation of property, plant and equipment	**571**	508
Amortisation of intangible assets	**700**	550
Share-based payment charge	**68**	2
Operating cash flows before movement in working capital	**2,662**	2,827
Increase in inventories	**(747)**	(825)
Increase in receivables	**(1,160)**	(1,141)
(Decrease)/increase in payables	**(49)**	987
Cash generated from operations	**706**	1,848
Interest paid	**(94)**	(73)
Net cash generated from operating activities	**612**	1,775
Cash flows from investing activities		
Interest received	**4**	11
Payments to acquire property plant and equipment	**(133)**	(349)
Acquisition of intangible assets	**(1,850)**	(2,498)
Net cash used in investment activities	**(1,979)**	(2,836)
Cash flows from financing activities		
Cash received from issue of shares	**193**	288
Repayment of obligations under finance leases	**(445)**	(472)
Net cash used in financing activities	**(252)**	(184)
Net decrease in cash and cash equivalents	**(1,619)**	(1,245)
Cash and cash equivalents at beginning of period	**200**	1,445
(Net debt)/cash and cash equivalents at end of period	**(1,419)**	200
Cash and cash equivalents	**—**	3,183
Bank overdraft	**(1,419)**	(2,983)
(Net debt)/cash and cash equivalents at end of period	**(1,419)**	200

Financial statements

Notes to the consolidated financial statements

1. Group accounting policies under IFRS

(a) Basis of preparation

These financial statements have been prepared on the basis of the IFRS accounting policies set out below The financial statements have been prepared in accordance with IFRS as adopted for use by the European Union, including IFRIC interpretations, and in line with those provisions of the Companies Act 2006 applicable to companies reporting under IFRS The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates It also requires management to exercise its judgement in the process of applying the Group's accounting policies

The Directors have considered the available cash resources of the Group and its current forecasts and are satisfied that the Group has adequate resources to continue in operational existence and that there are no material uncertainties casting doubt over the going concern status of the Group Accordingly, the financial statements are prepared on a going concern basis Further details of the Directors' assessment are provided in the Corporate governance report on page 34

The financial statements have been prepared under the historical cost convention, are presented in Sterling and are rounded to the nearest thousand

At 31 December 2012 the following standards were in issue but not yet effective

- IFRS 9 Financial Instruments (effective 1 January 2015),
- IFRS 10 Consolidated Financial Statements (effective 1 January 2014),
- IFRS 12 Disclosure of Interests in Other Entities (effective 1 January 2014)
- IFRS 13 Fair Value Measurement (effective 1 January 2013),
- IAS 27 (Revised) Separate Financial Statements (effective 1 January 2013),
- Amendments to IAS 1 Presentation of Items of Other Comprehensive Income (effective 1 July 2012),
- Amendments to IFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities (effective 1 January 2013),
- Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities (effective 1 January 2014),
- Amendments to IFRS 9 and IFRS 7 Mandatory Effective Date and Transition Disclosures (effective 1 January 2015),
- Amendments to IFRS 1 Government Loans (effective 1 January 2013),
- Annual Improvements 2009–2011 Cycle (effective 1 January 2013) and
- Amendments to IFRS 10, IFRS 11 and IFRS 12 Transition Guidance (effective 1 January 2013)

None of these new standards is expected to have a material impact on the financial statements of the Group

(b) Consolidation

Subsidiaries

The Group financial statements consolidate those of the parent company and of its subsidiary undertakings The results of subsidiaries, accounted for under the merger accounting method, are included in the Consolidated statement of comprehensive income as if they had always been part of the Group Intra-group sales and results are eliminated on consolidation and all sales and results relate to external transactions only

(c) Foreign currency translation

Transactions and balances

Foreign currency transactions are translated into the functional currency of Sterling using the exchange rates prevailing at the dates of transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Consolidated statement of comprehensive income

1. Group accounting policies under IFRS continued

(d) Property, plant and equipment

Property, plant and equipment are stated at the cost of acquisition less any provision for depreciation Cost includes expenditure that is directly attributable to the acquisition of the item

The carrying values of plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable

The assets' residual values, useful lives and depreciation methods are reviewed at each financial year end and adjusted where the expected asset utilisation differs significantly from the depreciation method applied

Depreciation is charged so as to write off the cost of property plant and equipment less estimated residual value over their estimated useful economic lives at the following rates

Office and computer equipment	– 10–33% per annum
Plant and machinery	– 10% per annum
Tooling	– 10–20% per annum
Placed equipment	– 33.3% per annum
Leasehold improvements	– Over the remaining term of the lease

Tooling developed for the Group's own products is only depreciated when brought into use

Placed equipment relates to equipment placed in clinical settings to generate a stream of recurring revenue from the single use element of the equipment

(e) Intangible assets

Research and development

Expenditure on research activities is recognised as an expense in the period in which it is incurred

Development expenditure arising from the Group's development activities is capitalised and amortised over the life of the product only if the Group can demonstrate the following

- the technical feasibility of completing the intangible asset so it will be available for use or sale,
- the intention to complete the intangible asset and use or sell it,
- the ability to use or sell the intangible asset,
- that it is probable that the asset created will generate future economic benefits,
- there is the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset, and
- the development cost of the asset can be measured reliably

Where no intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred Capitalised development costs are amortised over the life of the product within cost of sales, which is usually ten years

(f) Impairment of non-financial assets

Impairment reviews are carried out on capitalised development assets on a six-monthly basis and where there is a specific indicator of impairment (see note (p)) An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use

Financial statements

Notes to the consolidated financial statements continued

1. Group accounting policies under IFRS continued

(g) Inventories

Inventories are stated at the lower of cost (using weighted average) and net realisable value

Cost is the purchase cost, including transport, for raw materials, together with a proportion of manufacturing overheads based on normal levels of activity, for finished goods

Net realisable value is based on estimated normal selling price, less further costs expected to be incurred to completion and sale Impairment provisions are made for obsolete, slow moving or defective items where appropriate Such provisions are based upon established future sales and historical experience

(h) Trade receivables

Trade receivables are recognised initially at fair value and thereafter at amortised costs less provision for impairment A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows The amount of the loss is recognised in the Consolidated statement of comprehensive income, as are subsequent recoveries of amounts previously written off

(i) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held on call at banks and bank overdrafts Bank overdrafts are shown within borrowings in current liabilities on the balance sheet

(j) Trade payables

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate

(k) Share capital

Ordinary shares are classified as equity Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from proceeds

(l) Exceptional items

Exceptional items are costs or groups of costs which are non-recurring in nature which the Directors believe should be separately identified in the financial statements to enable the reader to properly understand the underlying trading performance of the business

(m) Income tax

The charge for current tax is based on the results for the period as adjusted for items which are non-assessable or disallowed and any adjustment to tax payable in respect of previous years It is calculated using rates that have been enacted or substantively enacted by the balance sheet date

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax basis used in the computation of taxable profit In principle, deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill (or negative goodwill) or from the initial recognition (other than in business combination) of other assets and liabilities in a transaction which affects neither the taxable profit nor the accounting profit

Tax benefits are not recognised unless the tax positions are probable of being sustained Once considered to be probable, management reviews each material tax benefit to assess whether a deferred tax asset should be recognised, based on the ability under tax statute to recover those tax losses and through the assessment of probable future taxable profits which those tax losses can be recovered

Where the Group is able to control the distribution of reserves from subsidiaries, and there is no intention to distribute the reserves, deferred tax is not recognised for these temporary differences

Deferred tax is calculated at the rates that are enacted or substantively enacted at the balance sheet date Deferred tax is charged or credited in the Consolidated statement of comprehensive income, except when it relates to items credited or charged directly to equity in which case the deferred tax is also dealt with in equity

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis Information as to the calculation of the income tax expense is included in note 6

1. Group accounting policies under IFRS continued

(n) Employee benefits

Pension obligations

The Group provides pension benefits to its employees through contributions to defined contribution Group personal pension policies The amounts charged to the Consolidated statement of comprehensive income are the contributions payable in the period

Share-based compensation

The Group issues equity settled share options to Directors and employees which are measured at fair value and recognised as an expense in the Consolidated statement of comprehensive income with a corresponding increase in profit and loss reserve The fair value of the employee services received in exchange for the grant of the options is treated as remuneration in respect of the individual The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted

The fair values of these payments are measured at the dates of grant and are recognised over the period during which employees become unconditionally entitled to the awards which is usually the vesting period At each balance sheet date, the Group revises its estimate of the number of options that are expected to vest It recognises the impact of the revision to original estimates, if any, in the Consolidated statement of comprehensive income, with a corresponding adjustment to retained earnings

(o) Income recognition

Revenue

Revenue is the total amount receivable by the Group for the supply of goods and services, excluding VAT and trade discounts

(i) Supply of goods

Usually the significant risks and rewards are transferred when title of goods passes and the Group fulfils its contractual obligations Generally, this arises when goods are either despatched to the customer or when the customer is notified that the goods are ready for collection on an ex-works basis

In certain situations the Group recognises revenue on a "bill and hold' basis whereby the related inventory remains at the Groups premises for a period of time Revenue is only recognised on this basis when the customer has taken title to the goods and accepted billing, it is probable that delivery will be made, the goods are on hand and separately identified, the customer acknowledges the deferred delivery and normal payment terms apply

The Group has a branded port access system which comprise a reuseable element ("Capital) and a consumable element In certain situations the Group sells the Capital element to distributors through contractual agreement on significantly extended terms of up to five years In the future, this Capital will either be realised in cash or extinguished through rebates provided on significant additional orders for consumables These Capital sales are recorded at fair value using an appropriate discount rate and are disclosed in the financial statements as non-current trade receivables, reflecting the timing of their contractual maturity

(ii) Supply of services

Design contracts

As soon as the outcome of a design contract can be estimated reliably, contract revenue and expenses are recognised in the Consolidated statement of comprehensive income in proportion to the stage of completion of the contract The stage of completion is assessed by comparing the actual work performed on the contract to the overall estimated work required on the contract. An expected loss on the contract is recognised immediately in the Consolidated statement of comprehensive income

Royalty income

Royalty income is derived from agreements with other parties for them to manufacture and distribute products Such royalty income is included within revenue and recognised in the same period as the licensee makes the related sale

Interest income

Interest income is recognised using the effective interest rate method

Other income

Government grants are recognised in the Consolidated statement of comprehensive income so as to match them with the expenditure towards which they are intended to contribute

Financial statements

Notes to the consolidated financial statements continued

1. Group accounting policies under IFRS continued

(p) Leases

Where the Group enters into a lease which entails taking substantially all the risks and rewards of ownership of an asset, the lease is treated as a finance lease The asset is recorded in the balance sheet at fair value as property, plant and equipment and is depreciated over its estimated useful life or the term of the lease, whichever is the shorter Future instalments under such leases, net of finance charges, are included in liabilities Rentals under operating leases are charged on a straight-line basis over the lease term Lease incentives, comprising rent free periods, are amortised over the period of the lease

(q) Significant management judgement in applying accounting policies

The following are significant management judgements made in applying the accounting policies of the Group that have the most significant effect on the financial statements Critical estimation uncertainties are described in note (r)

Internally generated research and development assets

Management monitors the progress of internal research and development projects using the accounting system and through timesheet records Judgement is required in determining and distinguishing the research phase from the development phase Research costs are incurred by the concept team the cost of which is fully expensed in the period Development costs are captured within the product development teams and are recognised as an asset when all relevant criteria are met Prior to the commencement of the product development phase, it is Group policy that capital expenditure approval is obtained from the appropriate level this enables the Group to ensure that projects are financially viable after taking account of the cost of development

Management performs an impairment review of capitalised development assets on a six-monthly basis The impairment review includes a significant degree of judgement, in particular determining the revenue streams relevant to a particular project Many of the Group's products operate in conjunction with each other, particularly where the Resposable® concept applies Accordingly, management aggregates together certain revenue streams and certain development assets when looking at overall recoverability of the costs held in the consolidated balance sheet Capitalised development costs at 31 December 2012 total £6,393,000 and accordingly any impairment identified in future periods could have a material impact on the Group's results

Deferred tax assets

The assessment of the probability of future taxable income in which deferred tax assets can be utilised is based on the Group's latest approved budgets, adjusted for significant tax impacts Management also assesses the underlying durability of future anticipated taxable profit streams by reference to current and historic financial performance If a positive forecast of taxable income indicates probable use of a deferred tax asset, then the deferred tax asset is usually recognised in full However, where the losses exceed ten years of profit (assessed with reference to current budgets) management restricts the recognition to ten years At 31 December 2012, £15.0 million of losses in a trading subsidiary have not been recognised due to the related trade generating only small profits

Revenue recognition for branded port access system

As explained in note (n) previously, the Group sells a branded port access system which comprises reusable and consumable elements In certain situations the reusable, or (Capital), element is sold on extended credit of up to five years and management have determined that it is appropriate to record this as revenue at fair value of the consideration receivable at the point of sale as there is a contractual obligation to pay for the Capital irrespective of whether the customer makes future purchases of consumables

Future purchases of consumables above a minimum level attract a discount that is applied to extinguish the receivable due for the sale of Capital Given that the full amount of the capital balance will be recoverable in the event that no further purchases of consumables are made, management have taken the judgement that any potential discount offered subsequently is fully attributable to the future purchases of consumables Future receipts for the sale of consumables above the minimum level will therefore be analysed into revenue for the sale of consumables and repayment of the receivable for Capital

1. Group accounting policies under IFRS continued

(r) Estimation uncertainty

When preparing the financial statements management undertakes a number of estimates and assumptions about recognition and measurement of assets, liabilities, income and expenses The actual results may differ from the estimates and assumptions made by the Group and will seldom equal the estimated results Information about significant estimates and assumptions that have the most significant effect on recognition and measurement of assets, liabilities, income and expenses are discussed below

Impairment

As described in note (q) previously, an impairment test is performed every six months to assess the carrying amount of product development assets held in the Group's balance sheet The impairment test performed compares the amount at which the asset is carried with the recoverable amount of the asset – where the recoverable amount is lower than the carrying amount an impairment loss is recognised To determine the recoverable amount, the Group estimates the future revenue stream of the associated product (or group of products) and the associated margin, and discounts this to present value at the Group's weighted average cost of capital (WACC) In the process of estimating future revenue and margin the Group makes assumptions about future operating results and these estimates may vary significantly with actual results This may cause significant adjustments to the Group's assets within future reporting periods

Useful lives of depreciable assets

The Group reviews the useful life of depreciable assets at each reporting date At 31 December 2012 the Directors assess that the useful lives represent the expected utilisation of the assets by the Group Actual results, however may vary due to technical obsolescence or changing customer requirements particularly for plant, machinery and tooling

Inventories

Inventories are measured at the lower of cost and net realisable value The Group benefits from good gross margins and accordingly net realisable value is not considered a material issue However, the Group is exposed to inventory obsolescence caused through changing customer requirements or technological changes Management reviews inventory on a line-by-line basis and makes provision for inventories known to be at risk of obsolescence This involves a degree of estimation based on current circumstances, which may change, and therefore significant inventory adjustments could still arise in future periods At 31 December 2012, the recorded inventory provision of £106,000 represents 4% of gross inventory

Trade receivables

The Group provides in certain agreed situations, products on extended credit terms in order to establish a presence in an export market The Directors constantly review the likelihood of realisation of these receivables and make provision based on their best estimates of when the full value of the receivable will not be recoverable As disclosed in note 11 the top five customers in trade receivables totalled £1,976,000 which highlights that a major customer failing could have a material impact on the Group

(s) Equity

Equity includes the elements listed below

- "Share capital" represents the nominal value of equity shares,
- "Share premium" represents the excess over nominal value of the fair value of consideration received for equity shares, net of expenses of the share issue,
- "Capital reserve" represents the excess over nominal value of the fair value consideration attributed to equity shares issued in part settlement for subsidiary company shares acquired, and
- 'Retained earnings' represents the accumulated profits and losses of the Group

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2. Segmental reporting

Information reported to the Board and for the purpose of assessing performance and making investment decisions is organised into three operating segments The Group's operating segments under IFRS 8 are as follows

SI Brand – the research, development, manufacture and distribution of SI branded minimally invasive devices

OEM – the research, development, manufacture and distribution of minimally invasive devices for third party medical device companies through either own label or co-branding

Industrial – the research, development, manufacture and sale of minimally invasive technology products for industrial application

The measure of profit or loss for each reportable segment is gross margin less amortisation of product development costs

Assets and working capital are monitored on a Group basis, with no separate disclosure of asset by segment made in the management accounts, and hence no separate asset disclosure is provided here

The following segmental analysis has been produced to provide a reconciliation between the information used by the key decision maker within the business and the information as it is presented under IFRS

Year ended 31 December 2012	SI Brand £'000	OEM £'000	Industrial £'000	Total £'000
Revenue	5,334	2,204	101	7,639
Result				
Segment result	2,250	815	95	3,160
Unallocated expenses				(1,837)
Profit from operations				1,323
Finance income				4
Finance costs				(94)
Profit before taxation				1,233
Tax				(547)
Profit for the year				686

Included within the segment/operating results are the following significant non-cash items

Year ended 31 December 2012	SI Brand £'000	OEM £'000	Industrial £'000	Total £'000
Amortisation of intangible assets	530	169	1	700

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2. Segmental reporting continued

Year ended 31 December 2011	SI Brand £'000	OEM £'000	Industrial £'000	Total £'000
Revenue	4 725	2 807	70	7,602
Result				
Segment result	1,950	1,047	49	3,046
Unallocated expenses				(1,279)
Profit from operations				1,767
Finance income				11
Finance costs				(73)
Profit before taxation				1,705
Tax				33
Profit for the year				1,738

Included within the segment/operating results are the following significant non-cash items

Year ended 31 December 2011	SI Brand £'000	OEM £'000	Industrial £'000	Total £'000
Amortisation of intangible assets	386	143	21	550

Unallocated expenses include those costs that cannot be split between segments and which are not separately analysed in the management accounts including concept department, sales and marketing, and head office overheads

Geographical analysis of revenues

	2012 £'000	2011 £000
United Kingdom	**1,777**	1548
Europe	**2,392**	3014
US	**2,149**	1763
Rest of World	**1,321**	1,277
	7,639	7,602

Revenues are allocated geographically on the basis of where revenues were received from and not from the ultimate final destination of use During 2012, £843,000 (11%) of the Group's revenue depended on a single customer in the SI Brand segment (2011 £1050,000 (14%) within the OEM segment) No other single customer accounted for more than 10% of the Group's revenue in either year

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Notes to the consolidated financial statements continued

3. Operating profit

The profit for the year is stated after charging

	2012 £'000	2011 £'000
Depreciation of owned assets	**313**	348
Depreciation of assets held under finance lease	**258**	160
Amortisation of capitalised development costs	**700**	550
Research and development costs – Concept team	**429**	400
Foreign exchange losses	**38**	39
Auditor's remuneration		
– fees payable to the Company's auditor for the audit of the Company's annual financial statements	**8**	7
– fees payable to the Company's auditor for the audit of the subsidiary undertakings	**18**	15
– tax compliance fees	**—**	22
Operating lease rentals		
– land and buildings	**138**	138
Exceptional items	**294**	—

The amortisation of capitalised development costs are accounted for within other operating expenses within the Consolidated statement of comprehensive income Exceptional items of £294,000 comprise restructuring costs incurred during the first half of 2012

4 Employees

The average monthly number of employees (including Executive Directors) employed by the Group during the year was as follows

	2012 Number	2011 Number
Directors	**2**	1
Production	**60**	57
Development	**28**	30
Administration	**17**	16
	107	104

The costs incurred in respect of these employees were

	2012 £'000	2011 £'000
Wages and salaries	**2,400**	2,316
Social security costs	**226**	217
Pension costs	**55**	137
	2,681	2,670

A detailed analysis of Directors' emoluments is shown in the table on page 32

4. Employees continued

Key management including Non-executive Directors

	2012 £'000	2011 £'000
Salaries	**416**	375
Social security costs	**42**	36
Pension costs	**14**	65
Share-based payments	**52**	2
Total	**524**	478

5. Finance costs

	2012 £'000	2011 £'000
On finance leases	**63**	58
On bank overdrafts	**31**	15
	94	73

6. Taxation

Tax on profit

	2012 £'000	2011 £'000
Current tax credit	**(287)**	—
Deferred tax charge/(credit)	**834**	(33)
Total tax charge/(credit)	**547**	(33)

Factors affecting the tax charge for the year

The taxation assessed for the year is lower than the standard rate of Corporation Tax in the UK at 24 5% (2011 27.5%) The differences are explained as follows

	2012 £'000	2011 £'000
Profit on ordinary activities before taxation	**1,233**	1705
Corporation Tax at standard rate of 24 5% (2011 27.5%)	**302**	469
Effects of		
Net impact of research and development enhanced expenditure	**78**	(1,446)
Expenses not tax deductible	**168**	89
Movement on intangible assets	**(319)**	(61)
Deductions on exercise of share options	**(193)**	(181)
Utilisation and recognition of trading losses	**511**	1,097
Total tax charge/(credit) for the year	**547**	(33)

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Notes to the consolidated financial statements continued

6. Taxation continued

Deferred taxation

The movement in the deferred taxation (liability)/asset during the year was

	2012 £'000	2011 £'000
Balance brought forward – asset	**465**	432
Consolidated statement of comprehensive income movement arising during the year	**(834)**	33
Balance carried forward – (liability)/asset	**(369)**	465

The deferred taxation recognised in the financial statements at 23% (2011 26%) is set out below

	2012 £'000	2011 £'000
Trade losses	**821**	1,988
Fixed asset timing differences	**(1,190)**	(1,523)
	(369)	465

The recoverability of the deferred tax asset is dependent on future taxable profits in excess of those arising from the reversal of deferred tax liabilities The recognition of the deferred tax assets is based upon the estimate of future availability of suitable profits Certain deferred tax assets and liabilities have been offset

The following is the analysis of unprovided deferred tax balances

	2012 £'000	2011 £'000
Deferred tax assets	**3,450**	3,340
Deferred tax liabilities	**—**	—
Net unrecognised deferred tax assets	**3,450**	3,340

At the balance sheet date, the Group has unused tax losses of £18 6 million (2011 £21 3 million) available for offset against certain future profits A deferred tax asset of £821,000 (2011 £1,988,000) has been recognised in respect of such losses No deferred tax asset has been recognised in respect of the remaining £15.0 million (2011 £13 4 million) due to the anticipated lack of availability of suitable future trading profits

7 Earnings per ordinary share

Basic earnings per ordinary share

The calculation of basic earnings per ordinary share for the year ended 31 December 2012 was based upon the profit attributable to ordinary shareholders of £686,000 (2011 £1,738,000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2012 of 402 200 875 (2011 392 716 121)

Diluted earnings per ordinary share

The calculation of diluted earnings per ordinary share for the year ended 31 December 2012 was based upon the profit attributable to ordinary shareholders of £686,000 (2011 £1,738 000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2012 of 415,283,787 (2011 410,691,902)

7. Earnings per ordinary share continued

Adjusted earnings per ordinary share

The calculation of adjusted earnings per ordinary share for the year ended 31 December 2012 was based upon the adjusted profit attributable to ordinary shareholders of £1,421,000 (2011 £1,738 000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2012 of 402,200 875 (2011 392,716,121)

Earnings and adjusted earnings	2012 £'000	2011 £'000
Earnings for the purpose of basic and diluted earnings per ordinary share	**686**	1,738
Exceptional items	**294**	—
Deferred tax adjustment	**441**	—
Earnings for the purpose of adjusted earnings per ordinary share	**1,421**	1738

No of shares used in calculation of earnings per ordinary share ('000s)	2012 No of shares	2011 No of shares
Basic earnings per share	**402,201**	392,716
Dilutive effect of unexercised share options	**13,083**	17,976
Diluted earnings per share	**415,284**	410,692

8. Property, plant and equipment

	Tooling £'000	Plant and machinery £'000	Office and computer equipment £'000	Placed equipment £'000	Improvements to leasehold property £'000	Total £'000
Gross carrying amount 31 December 2011	1,538	3,314	857	331	366	6,406
Accumulated depreciation and impairment	(1,119)	(876)	(728)	(195)	(110)	(3,028)
Carrying amount 31 December 2011	419	2 438	129	136	256	3,378
Gross carrying amount 31 December 2012	1 567	3 402	899	355	366	6,589
Accumulated depreciation and impairment	(1 190)	(1 199)	(785)	(255)	(170)	(3,599)
Carrying amount 31 December 2012	**377**	**2,203**	**114**	**100**	**196**	**2,990**

	Tooling £'000	Plant and machinery £'000	Office and computer equipment £'000	Placed equipment £'000	Improvements to leasehold property £'000	Total £'000
Carrying amount 1 January 2011	413	1,527	150	144	243	2,477
Additions – separately acquired	82	1,157	62	54	54	1,409
Depreciation	(76)	(246)	(83)	(62)	(41)	(508)
Carrying amount 31 December 2011	419	2,438	129	136	256	3,378
Additions – separately acquired	29	88	42	24	—	183
Depreciation	(71)	(322)	(57)	(60)	(61)	(571)
Carrying amount 31 December 2012	**377**	**2,204**	**114**	**100**	**195**	**2,990**

Financial statements

Notes to the consolidated financial statements continued

8. Property, plant and equipment continued

Leased plant and equipment

The Group leases plant and machinery under a number of finance lease arrangements The carrying amount and depreciation charge for such assets are disclosed below

	2012 £'000	2011 £'000
Plant and machinery		
Net book value	**1,921**	2,044
Depreciation charge for the year	**258**	160

Security

At 31 December 2012, the assets of the Group are subject to a fixed and floating charge debenture in favour of the Group's banking facilities

9. Intangible assets

	Capitalised development costs 2012 £'000
Cost	
At 1 January 2011	3 984
Additions	2,498
At 1 January 2012	6,482
Additions	1,850
At 31 December 2012	**8,332**
Accumulated amortisation	
At 1 January 2011	689
Charge for the year	550
At 1 January 2012	1 239
Charge for the year	700
At 31 December 2012	**1,939**
Carrying amount	
At 31 December 2012	**6,393**
At 31 December 2011	5,243
At 31 December 2010	3 295

9. Intangible assets continued

The £8 332,000 (2011 £6,482,000) of capitalised development costs represents expenditure that fulfils the requirements of IAS 38 These costs will be amortised over the future commercial life of the product, commencing on the sale of the first commercial item, up to a maximum product life cycle of ten years, and taking account of expected market conditions and penetration

The above costs have been assessed for annual impairment as required by the Group's accounting policies Intangible assets and Impairment of non-financial assets

10. Inventories

	2012 £'000	2011 £'000
Raw materials	**1,971**	1 660
Finished goods	**1,634**	1,198
	3,605	2,858

Included in the analysis above are impairment provisions against inventory amounting to £133,000 (2011 £104 000)

In 2012 a total of £3,743,000 of inventories was included in profit and loss as an expense within cost of sales (2011 £4,339,000) Cost of sales included an amount of £204,000 resulting from the write down of inventories (2011 £24,000)

Inventories are pledged as securities for bank overdrafts

The Group's inventories are comprised of products which are not generally subject to rapid obsolescence on account of technological, deterioration in condition or market trends Consequently management considers that there is little risk of significant adjustments to the Groups inventory assets within the next financial year

11. Trade and other receivables

Falling due in less than one year	2012 £'000	2011 £'000
Trade receivables	**3,953**	3,311
Prepayments and accrued income	**229**	286
Corporation Tax recoverable	**287**	—
Other debtors	**163**	225
	4,632	3,822
Falling due in more than one year		
Trade receivables	**637**	—

The carrying value of trade receivables is considered a reasonable approximation to fair value

Of the trade receivables, £1,976 000 relates to five customers (2011 £2,000,000)

All of the Group's trade and other receivables have been reviewed for indicators of impairment Certain trade receivables were found to be impaired and a provision of £10 000 (2011 £10 000) was recorded

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Notes to the consolidated financial statements continued

11. Trade and other receivables continued

In addition some of the unimpaired trade receivables are past due at the reporting date The age of financial assets past due but not impaired is shown below

	2012 £'000	2011 £'000
Not more than three months	**306**	186
More than three months but not more than six months	**15**	9
More than six months but not more than one year	**—**	20
More than one year	**—**	80

The Group is exposed to credit risk through offering extended credit terms to those customers operating in markets where extended payment terms are themselves taken by local government and state organisations This risk is managed through constant review and personal knowledge of the customer concerned Payment plans are agreed and monitored in all such cases to minimise credit risk

12. Financial instruments

The Group is exposed to market risk through its use of financial instruments The Group's risk management is co-ordinated by the Directors who focus actively on securing the Group's short to medium-term cash flows through regular review of all the operating activities of the business Long-term financial investments are managed to generate lasting returns

The Group does not actively engage in the trading of financial assets for speculative purposes nor does it write options The most significant financial risks to which the Group is exposed are described in the following sections

Foreign currency sensitivity

Exposures to currency exchange rates arise from the Group's overseas sales and purchases, most of which are denominated in Euros and Dollars To mitigate the Group's exposure to foreign currency risk, cash flows in Euros and Dollars are monitored on an ongoing basis Foreign currency denominated financial assets and liabilities are set out below

	2012 €'000	2011 €'000	2012 $'000	2011 $'000
Financial assets	**988**	1,026	**1,606**	765
Financial liabilities	**(100)**	(162)	**(22)**	(280)
Short-term exposure	**888**	864	**1,584**	485

At 31 December 2012, the Group has long-term foreign exchange assets denominated in Dollars of $327000 represented by trade receivables The Group has no other long-term foreign exchange assets or liabilities (2011 £nil)

The Group has significant short-term exposure to the Euro and Dollar at 31 December 2012 An analysis of the effect of a reasonable possible movement in exchange rates shows that a movement of 5% in the exchange rate could result in foreign currency gains or losses of £36 000 (2011 £37000) against the Euro and £49 000 (£16,000) against the Dollar

The Group gives consideration to the use of forward currency contracts to reduce foreign currency exposure

12. Financial instruments continued

Credit risk analysis

The Group's exposure to credit risk is limited to the carrying amount of financial assets recognised at the balance sheet date, which are set out below

	2012 £'000	2011 £'000
Cash and cash equivalents	—	3 183
Trade and other receivables	**5,040**	3,537
	5,040	6,720

The Group continually monitors defaults of customers and other counterparties and incorporates this information into its credit risk controls

Management considers that all of the above financial assets that are not impaired for each of the reporting dates under review are of good credit quality, including those that are past due

In respect of trade and other receivables that are not impaired, the Group does have some credit risk through customer concentration as disclosed in note 11 although this has reduced in 2012 relative to the prior year Significant customers are primarily large multi-national businesses with a demonstrable track record of financial viability As with all customers, rigorous credit control procedures help to mitigate this risk

The credit risk for cash and cash equivalents is considered negligible, as Group policy to only use financial institutions with a high quality external credit rating

Liquidity risk analysis

The Group manages its liquidity needs by carefully monitoring all scheduled cash outflows Liquidity needs are monitored in various time bands, on a day-to-day and week-to-week basis, as well as on the basis of a rolling 13-week projection Longer-term needs are monitored as part of the Group's regular rolling monthly re-forecasting process

Funding for long-term liquidity is additionally secured by an adequate amount of committed credit both through working capital and asset finance facilities

During the year ended 31 December 2012, the Group continued to have access to sufficient funds to meet its business expansion needs The Group negotiated an overdraft facility with HSBC Bank plc providing a total facility of £2.0 million through to annual renewal at 30 September 2013 At 31 December 2012 the Group had drawn down £1,419 000 of this facility

The Group's liabilities have contractual maturities which are summarised below

	Current		**Non-current**
31 December 2012	**Within 6 months £'000**	**Within 6–12 months £'000**	**Over 12 months £'000**
Finance lease obligations	**219**	**203**	**786**
Trade and other payables	**1,475**	**—**	**—**
Bank overdraft	**1,419**	**—**	**—**
	3,113	**203**	**786**

	Current		Non-current
31 December 2011	Within 6 months £'000	Within 6–12 months £'000	Over 12 months £'000
Finance lease obligations	197	188	926
Trade and other payables	1 859	—	—
Bank overdraft	2 983	—	—
	5,039	188	926

Financial statements

Notes to the consolidated financial statements continued

12. Financial instruments continued

Maturity profile of borrowings

	2012 £'000	2011 £'000
Gross lease payments not later than one year	**483**	440
Later than one year but not more than five years	**883**	1,054
Future finance charges	**(159)**	(183)

Summary of financial assets and liabilities by category

	2012 £'000	2011 £'000
Loans and receivables		
Trade and other receivables	**5,040**	3,537
Cash	**—**	3,183
	5,040	6,720

	2012 £'000	2011 £'000
Current liabilities		
Trade payables financial liabilities measured at amortised cost	**1,475**	1,859
Other short-term financial liabilities	**1,419**	2 983
	2,894	4 842
Net financial assets and liabilities	**2,146**	1 878

Management is of the opinion that the carrying value of the above assets and liabilities equates to their fair value

Capital management

The Group's capital management objectives are

- to ensure its ability to continue as a going concern, and
- to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk

The Group manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets In order to maintain or adjust the capital structure the Group may issue new shares or sell assets to reduce debt Historically, the Group has primarily been funded through cash reserves and hire purchase financing and accordingly no target for gearing levels has been set Capital as monitored by the Group for the reporting periods under review is summarised as follows

	2012 £'000	2011 £'000
Total borrowings	**2,627**	4,294
Less cash and cash equivalents	**—**	(3,183)
Net debt	**2,627**	1,111
Total equity	**13,563**	12,616
Total capital	**16,190**	13,727

Fair value

The financial assets of the Group are cash and cash equivalents and trade receivables, and fair value is deemed to be not materially different to the carrying value

13. Share capital

	2012 £'000	2011 £'000
Authorised 600,000,000 (2011 600,000,000) ordinary shares of 1p each	**6,000**	6,000
Allotted, called up and fully paid 404,591,902 (2011 395,202,902) ordinary shares of 1p each	**4,046**	3952

At 31 December 2012 the following share options were outstanding

	Number of shares						Exercise dates	
Scheme and date of grant	At 1 January 2012	Exercised in year	Granted during year	Lapsed	At 31 December 2012	Option price per 1p share	Date from which option may be exercised	Date on which option expires
Non-executive unapproved								
November 2007	3,000,000	—	—	—	**3,000,000**	17p	November 2009	November 2017
January 2009	2,000,000	(1 000 000)	—	—	**1,000,000**	15p	November 2009	January 2019
November 2009	1,200,000	—	—	—	**1,200,000**	17p	November 2009	November 2019
Enterprise management								
November 2007	2,234,454	(2,234,454)	—	—	—	3 5p	November 2010	November 2017
January 2009	2,000,000	(2,000,000)	—	—	—	3 5p	January 2012	January 2019
June 2012	—	—	2,500 000	—	**2,500,000**	1 0p	June 2015	June 2022
June 2012	—	—	2,040,000	(180,000)	**1,860,000**	72p	June 2015	June 2022
June 2012	—	—	4,490,000	(100,000)	**4,390,000**	9 0p	June 2015	June 2022
Executive unapproved								
November 2007	1,454,546	(1,454,546)	—	—	—	17p	November 2009	November 2017
January 2009	1,400,000	(500,000)	—	—	**900,000**	15p	November 2009	January 2019
November 2009	2,200,000	(2,200,000)	—	—	—	17p	November 2009	November 2019

Share-based payments

Share options were granted during 2012 to Executive Directors and employees subject to a minimum period of service The exercise price of the granted options is equal to market price at grant for senior management (with the exception of M R Thornton) and to market price at grant less 20% for all other employees The exercise price for M R Thornton is equal to 1p in accordance with the terms of his recruitment Options are conditional upon completing a three year service period from the date of grant Awards to N G Bowland and the Directors of Surgical Innovations Limited are subject to performance conditions set by the Remuneration Committee and measured over the vesting period

Movements in the number of share options outstanding and their related weighted average exercise price are as follows

	2012		2011	
	Average exercise price pence	**Options '000s**	Average exercise price pence	Options '000s
At 1 January	**1 9**	**15,489**	2 0	29,200
Exercised	**2 1**	**(9,389)**	2 1	(13,711)
Granted	**6 4**	**9,030**	—	—
Lapsed	**7 8**	**(280)**	—	—
At 31 December	**4 4**	**14,850**	1 9	15,489

Out of the 14,850,000 options (2011 15,489,000), 6,100 000 (2010 15,489 000) options were exercisable Options exercised in 2012 resulted in 9,389 000 (2011 13,711 000) shares being issued at a weighted average exercise price of 2 1p (2011 2 1p) The related average weighted share price at the date of exercise was 11.3p (2011 6 9p)

Financial statements

Notes to the consolidated financial statements continued

13. Share capital continued

Share-based payments continued

The weighted average fair value of options granted during the period determined using the Black-Scholes valuation model was 4.5p per option (2011 no options granted) The significant inputs into the model were share price at the date of grant, exercise price as set out above, volatility of 40, an expected option life varying between three and four years and an annual risk-free interest rate of 2.5% Volatility was calculated with reference to statistical analysis of the historic daily share price Accordingly, after taking account of estimated leavers, the total share-based payment charge for the year was £68,000 (2011 £2,000)

14. Share premium

	Share premium £'000
Balance as at 31 December 2011	226
Issue of ordinary share capital	99
Balance as at 31 December 2012	**325**

Share premium comprises the cumulative difference between the net proceeds and nominal value of the Company's issued equity share capital

15. Contingent liabilities and financial commitments

These are as follows

(a) Contingent liabilities

There were no contingent liabilities at 31 December 2012 (2011 £nil)

(b) Operating leases

At 31 December 2012 the Group had future aggregate minimum lease payments under non-cancellable operating leases as follows

	2012 £'000	2011 £'000
Within one year	**219**	225
One to five years	**655**	669
Over five years	**50**	195

(c) Capital commitments

At 31 December 2012 the Group had capital commitments totalling £69,000 (2011 £36,000)

16. Transactions with related parties

A summary of transactions during the year and outstanding amounts at the balance sheet date is as follows

	Amounts invoiced to/(by) the Group 2012 £'000	**Amounts payable/ (receivable) 31 December 2012 £'000**	Amounts invoiced to/(by) the Group 2011 £'000	Amounts payable/ (receivable) 31 December 2011 £'000
Quest Investments Limited[1]	**29**	**10**	30	3
Winburn Glass Norfolk[2]	**25**	**9**	20	2
Getz Bros & Co Inc[3]	**20**	**—**	20	10
N G Bowland[4]	**—**	**12**	—	(14)
ACP[5]	**(205)**	**(358)**	(402)	(330)

Transactions with related parties during the current and prior year were as follows

1 Director's fees for D B Liversidge CBE are paid to Quest Investments Limited, a company of which he is a director
2 Director's fees and advisory fees for C Glass are paid to Winburn Glass Norfolk, a firm of which he is a partner
3 Director s fees and advisory fees for R Simkins are paid to Getz Bros & Co Inc, a company of which he is vice-president
4 At 31 December 2012 £12 166 from a loan of £20,000 made available to N G Bowland in 2009 was still repayable
5 ACP acts as the master distributor for Surgical Innovations in the Far East During the year Surgical Innovations invoiced ACP £205,000 for products and at 31 December 2012 there was an amount owing to Surgical Innovations of £358,000 Getz Bros & Co Inc. is the ultimate beneficial owner of ACP

There is no controlling party of Surgical Innovations Group plc

17. Pensions

The Company currently operates a defined contribution Group personal pension plan for the benefit of employees Company contributions in 2012 were £41,000 (2011 £65,000)

Financial statements

Independent auditor's report – Company

Independent auditor's report to the members of Surgical Innovations Group plc

We have audited the parent company financial statements of Surgical Innovations Group plc for the year ended 31 December 2012 which comprise the parent company balance sheet and the related notes The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice)

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an 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 auditor

As explained more fully in the Statement of Directors responsibilities set out on page 30, the Directors are responsible for the preparation of the parent company financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit and express an opinion on the parent company financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www frc org uk/apb/scope/private cfm

Opinion on financial statements

In our opinion the parent company financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2012,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Report of the Directors for the financial year for which the financial statements are prepared is consistent with the parent company financial statements

Matters on which we are required to report by exception

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

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

Other matter

We have reported separately on the Group financial statements of Surgical Innovations Group plc for the year ended 31 December 2012

Grant Thornton UK LLP

Paul Houghton
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountant
Leeds
8 April 2013

Financial statements

Company balance sheet

as at 31 December 2012

	Notes	2012 £'000	2012 £'000	2011 £'000	2011 £'000
Fixed assets					
Investments	2		**1,018**		1,018
Current assets					
Debtors	3	**2,993**		3,219	
Cash at bank		**3,305**		3,037	
		6,298		6,256	
Creditors amounts falling due within one year	4	**(320)**		(321)	
Net current assets			**5,978**		5 935
Net assets			**6,996**		6 953
Capital and reserves					
Called up share capital	5		**4,046**		3 952
Share premium account	6	**325**		226	
Profit and loss account	6	**2,625**		2 775	
			6,996		3,001
Shareholders' funds	7		**6,996**		6,953

The financial statements on pages 61 to 64 were approved by the Board of Directors on 8 April 2013 and were signed on its behalf by

D B Livesidge CBE
Director
Company registered number 2298163

Financial statements
Notes to the Company financial statements

1. Accounting policies

(a) Basis of preparation

The financial statements have been prepared under the historical cost basis and UK GAAP

(b) Investment in subsidiary undertakings

The Company's investment in subsidiary undertakings is stated at cost less any provision for impairment

(c) Share-based compensation

The Group issues share options to certain employees which are measured at fair value and recognised as an expense in the profit and loss account with a corresponding increase in profit and loss reserve The fair value of the employee services received in exchange for the grant of the options is recognised as an expense The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted

The fair values of these payments are measured at the dates of grant and are recognised over the period during which employees become unconditionally entitled to the awards At each balance sheet date, the Group revises its estimate of the number of options that are expected to vest It recognises the impact of the revision to original estimates, if any, in the profit and loss account, with a corresponding adjustment to retained earnings

2. Investments

Company	£'000
Cost	
At 31 December 2012 and 1 January 2012	**1,018**
Provision for diminution in value	
At 31 December 2012 and 1 January 2012	**—**
Net book value at 31 December 2012 and 1 January 2012	**1,018**

The principal trading subsidiaries of the Group comprise

Company	Description of shares held	Nature of business	Country of incorporation and operation	Proportion held
Surgical Innovations Limited	Ordinary £1 shares	Design and manufacture of minimally invasive devices	Great Britain	100%
Haemocell Limited	Ordinary £1 shares	Design and manufacture of autologous blood products	Great Britain	100%

3. Debtors

	2012 £'000	2011 £'000
Prepayments and accrued income	**17**	68
Other debtors	**70**	31
Amounts due from subsidiary undertakings	**2,906**	3,120
	2,993	3 219

4. Creditors: amounts falling due within one year

	2012 £'000	2011 £'000
Accruals and deferred income	**100**	41
Other creditors	**220**	280
	320	321

5. Share capital

	2012 £'000	2011 £'000
Authorised 600,000,000 (2011 600,000,000) ordinary shares of 1p each	**6,000**	6,000
Allotted, called up and fully paid 404,591,902 (2011 395,202,902) ordinary shares of 1p each	**4,046**	3,952

Details of the share options are contained in note 13 of the consolidated financial statements

During the year the following ordinary shares of 1p were issued in respect of exercised share options for the stated cash consideration

- 3,500,000 at 15p,
- 3,654,546 at 17p, and
- 2,234,454 at 3 5p

A total of 9,389,000 (2011 13,711,000) ordinary shares with a total nominal value of £93,890 (2011 £137,110) were issued for consideration amounting to £193,000 (2011 £288,000)

6. Reserves

	Share premium £000	Accumulated profits/ (losses) £000
At 1 January 2012	226	2,775
Premium on shares issued	99	—
Loss for the year	—	(218)
Employee share-based payments	—	68
At 31 December 2012	**325**	**2,625**

7. Reconciliation of movements in shareholders' funds

	2012 £'000	2011 £'000
Loss for the financial year	**(218)**	(142)
Issue of shares	**193**	288
Employee share-based payments	**68**	2
Net increase in shareholders' funds	**43**	148
Opening shareholders' funds	**6,953**	6,805
Closing shareholders' funds	**6,996**	6,953

Financial statements

Notes to the Company financial statements continued

8. Loss for the financial year of Surgical Innovations Group plc

The loss for the financial year dealt with in the financial statements of the holding company, Surgical Innovations Group plc, was £218,000 (2011 £142,000)

As permitted by Section 408 of the Companies Act 2006 the profit and loss account has not been included in these financial statements

9. Transactions with related parties

A summary of transactions during the year and outstanding amounts at the balance sheet date is as follows

	Amounts invoiced to the Company 2012 £'000	**Amounts payable/ (receivable) 31 December 2012 £'000**	Amounts invoiced to the Company 2011 £'000	Amounts payable/ (receivable) 31 December 2011 £'000
Quest Investments Limited[1]	**29**	**10**	30	3
Winburn Glass Norfolk[2]	**25**	**9**	20	2
Getz Bros & Co Inc[3]	**20**	**—**	20	10
N G Bowland[4]	**—**	**(12)**	—	(14)

As disclosed in the Report on remuneration

1 Director s fees for D B Liversidge CBE are paid to Quest Investments Limited, a company of which he is a director
2 Director s fees and advisory fees for C Glass are paid to Winburn Glass Norfolk, a firm of which he is a partner
3 Director s fees and advisory fees for R Simkins are paid to Getz Bros & Co Inc, a company of which he is vice-president
4 At 31 December 2012 £12 166 from a loan of £20,000 made available to N G Bowland in 2009 was still repayable

The Company has taken advantage of the exemption conferred by FRS 8 Related Party Transactions not to disclose transactions with wholly owned subsidiary undertakings

Financial statements

Five-year summary

	2012 £'000	2011 £'000	2010 £'000	2009 £'000	2008 £'000
Revenue	**7,639**	7,602	7,045	4,541	4,312
Cost of sales	**(3,779)**	(4,005)	(3,526)	(2,647)	(2,032)
Gross profit	**3,860**	3,597	3,519	1,894	2,280
Other operating expenses	**(2,537)**	(1,830)	(1,940)	(1,603)	(1,500)
Adjusted EBITDA	**2,888**	2,825	2,545	937	1,027
Exceptional items	**(294)**	—	—	(200)	—
Amortisation	**(700)**	(550)	(518)	(101)	(60)
Depreciation	**(571)**	(508)	(448)	(345)	(187)
Operating profit	**1,323**	1,767	1,579	291	780
Finance income	**4**	11	9	13	118
Finance costs	**(94)**	(73)	(39)	(40)	(78)
Profit before taxation	**1,233**	1,705	1,549	264	820
Taxation	**(547)**	33	239	261	(190)
Retained profit for the year	**686**	1,738	1,788	525	630
Earnings per ordinary share (basic)	**0 17p**	0 44p	0 48p	0 14p	0 17p
Earnings per ordinary share (diluted)	**0 17p**	0 42p	0 46p	0 14p	0 17p

Shareholder information
Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of the Company will be held at Clayton Wood House, 6 Clayton Wood Bank, Leeds LS16 6QZ on 19 June 2013 at 2 00pm You will be asked to consider the following resolutions

Ordinary business

To consider and, if thought fit, pass the following resolutions which will be proposed as ordinary resolutions

1 To receive and adopt the annual report for the year ended 31 December 2012

2 To elect Mr M R Thornton as a Director of the Company, in accordance with Article 29.2 of the Company's Articles of Association, who offers himself for re-election as a Director

3 To re-elect Mr D B Liversidge CBE as a Director of the Company in accordance with Article 34 of the Company's Articles of Association, who offers himself for re-election as a Director

4 To re-elect Mr M J McMahon as a Director of the Company in accordance with Article 34 of the Company's Articles of Association, who offers himself for re-election as a Director

5 To re-appoint Grant Thornton UK LLP as auditor of the Company to hold office until the conclusion of the next general meeting at which financial statements are laid before the Company and to authorise the Directors to determine the auditor's remuneration

6 To authorise the Board generally and unconditionally pursuant to Section 551 of the Companies Act 2006 (the Act) to exercise all powers of the Company to allot shares in the Company and to grant rights to subscribe for or to convert any security into such shares in the Company (Rights) up to an aggregate nominal amount of £1,348,639 67 (being approximately one-third of the issued share capital of the Company as at the date of this notice) provided that this authority shall expire on the earlier of the date falling six months from the expiry of the Company's current financial year and the date of the next Annual General Meeting of the Company after the passing of this resolution unless varied, revoked or renewed by the Company in general meeting, save that the Board may before the expiry of the authority granted by this resolution make a further offer or agreement which would or might require shares to be allotted or Rights to be granted after such expiry and the Board may allot shares and grant Rights in pursuance of such an offer or agreement as if the authority conferred by this resolution had not expired and the authority granted by this resolution is in substitution for all previous authorities granted to the Directors to allot shares and grant Rights which (to the extent that they remain in force and unexercised) are revoked but without prejudice to any allotment or grant of Rights made or entered into prior to the date of this resolution 6

Special business

To consider, and if thought fit, pass the following resolutions which will be proposed as special resolutions

7 To empower the Board (subject to the passing of the previous resolution) pursuant to Sections 570 and 573 of the Act to allot equity securities (within the meaning of Section 560 of the Act) for cash pursuant to the authority conferred upon them by the previous resolution as if Section 561(1) of the Act did not apply to any such allotment, provided that this power shall be limited to

71 the allotment of equity securities in connection with a rights issue in favour of ordinary shareholders where the equity securities respectively attributable to the interests of all ordinary shareholders are proportionate (as nearly as may be) to the respective numbers of ordinary shares held by them but subject to such exclusions or other arrangements as the Directors may deem necessary or expedient in relation to fractional entitlements, treasury shares, record dates or legal or practical problems under the law of, or the requirements of, any recognised regulatory body or any stock exchange in any territory, and

72 the allotment (otherwise than pursuant to sub-paragraph 71 above) of equity securities up to an aggregate nominal amount of £404,591 90 (being approximately 10% of the issued share capital of the Company at the date of this notice)

and shall expire on the earlier of the date falling six months from the end of the current financial year of the Company and the date of the next Annual General Meeting after the passing of this resolution save that the Company may, before the expiry of any power contained in this resolution, make a further offer or agreement which would or might require equity securities to be allotted after such expiry and the Board may allot equity securities in pursuance of such offer or agreement as if the power conferred by this resolution had not expired

Special business continued

8 To authorise the Company generally and unconditionally for the purpose of Section 701 of the Act to make one or more market purchases (within the meaning of Section 693(4) of the Act) of ordinary shares of 1p each in the capital of the Company (Ordinary Shares) provided that

8 1 the maximum aggregate number of Ordinary Shares authorised by this resolution to be purchased is 40,459,190 shares (representing approximately 10% of the Company's issued share capital as at the date of this notice)

8.2 the minimum price which may be paid for such Ordinary Shares is 1p per share (exclusive of advance corporation tax and expenses),

8 3 the maximum price (exclusive of advance corporation tax and expenses) which may be paid for an Ordinary Share is not more than the higher of 5% above the average of the middle market quotations for an Ordinary Share as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the Ordinary Share is purchased and the amount stipulated by Article 5(1) of the Buy-back and Stabilisation Regulation (Commission Regulation 2273/2003) and

8 4 unless previously revoked or varied the authority conferred by this resolution shall expire on the earlier of the date falling six months from the end of the current financial year of the Company and the date of the next Annual General Meeting of the Company save that the Company may, before such expiry, make a contract or contracts to purchase Ordinary Shares after such expiry as if the power conferred by this resolution had not expired

By order of the Board

M R Thornton
Company Secretary
8 April 2013

Registered office
Clayton Wood House
6 Clayton Wood Bank
Leeds LS16 6QZ

Notes

1 This notice is the formal notification to shareholders of the Company's Annual General Meeting, its date, time and place, and the matters to be considered If you are in doubt as to what action to take you should consult an independent adviser

2 Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001 (as amended) and Section 360B of the Companies Act 2006, only those shareholders registered in the register of members of the Company at 6.00pm on 17 June 2013 as holders of ordinary shares of 1p each in the capital of the Company shall be entitled to attend and vote at the Meeting in respect of the number of shares registered in their name at that time Changes to entries in the register of members of the Company after 6.00pm on 17 June 2013 shall be disregarded in determining the rights of any person to attend and vote at the Meeting.

3 A member entitled to attend speak and vote may appoint a proxy to attend, speak and vote instead of him or her A member may appoint more than one proxy in relation to the Meeting provided that each proxy is appointed to exercise the rights attached to a different share or shares held by that member A proxy need not be a member of the Company A form of proxy is included at the end of this document and contains notes for its completion

To be valid, the form of proxy and any power of attorney or the authority under which it is signed (or a notarially certified copy of it) must be completed and lodged at the Registrars of the Company, Capita Registrars, at PXS, 34, Beckenham Road, Beckenham, Kent BR3 4TU not later than 2.00pm on 17 June 2013

4 Completion and return of a form of proxy does not preclude a member from subsequently attending and voting at the Meeting If a member appoints a proxy or proxies and then decides to attend the Annual General Meeting in person and vote using his poll card, then the vote in person will override the proxy vote(s) If the vote in person is in respect of the member s entire holding, then all proxy votes will be disregarded If, however, the member votes at the Meeting in respect of less than the member's entire holding, then if the member indicates on his polling card that all proxies are to be disregarded, that shall be the case, but if the member does not specifically revoke proxies, then the vote in person will be treated in the same way as if it were the last received proxy and earlier proxies will only be disregarded to the extent that to count them would result in the number of votes being cast exceeding the member's entire holding.

Shareholder information

Notice of Annual General Meeting continued

Notes continued

5 To change your proxy instructions simply submit a new proxy appointment using the methods set out above Note that the cut-off time for receipt of proxy appointments (see note 3 above) also apply in relation to amended instructions, any amended proxy appointment received after the relevant cut-off time will be disregarded

Where you have appointed a proxy using the hard copy proxy form and would like to change the instructions using another hard copy proxy form, please contact Capita Registrars at PXS, 34 Beckenham Road, Beckenham, Kent BR3 4TU

If you submit more than one valid proxy appointment, the appointment received last before the latest time for the receipt of proxies will take precedence

6 In order to revoke a proxy instruction you will need to inform the Company by sending a signed hard copy notice clearly stating your intention to revoke your proxy appointment to Capita Registrars In the case of a member which is a company, the revocation notice must be executed under its common seal or signed on its behalf by an officer of the company or an attorney for the company Any power of attorney or any other authority under which the revocation notice is signed (or a duly certified copy of such power or authority) must be included with the revocation notice

The revocation notice must be received by Capita Registrars at PXS, 34 Beckenham Road, Beckenham Kent BR3 4TU no later than 2.00pm on 17 June 2013 If you attempt to revoke your proxy appointment but the revocation is received after the time specified then, subject to note 5 above, your appointment will remain valid

7 Copies of the following documents will be available for inspection at the registered office of the Company during normal business hours until the date of the Annual General Meeting and on that day, at the place of the Meeting from at least 15 minutes prior to the Meeting until its conclusion

- Directors' service contracts and
- letters of appointment for Non-executive Directors

8 As at 8 April 2013 (being the last practicable business day prior to the publication of this notice) the Company's issued share capital consisted of 404,591,902 ordinary shares of 1p each, with one voting right per share

9 If a corporation is a member of the Company it may by resolution of its directors or other governing body authorise one or more persons to act as its representative or representatives at the Meeting and any such representative or representatives shall be entitled to exercise on behalf of the corporation all the powers that the corporation could exercise if it were an individual member of the Company

Corporate representatives should bring with them either an original or certified copy of the appropriate board resolution or an original letter confirming the appointment, provided it is on the corporation's letterhead, is signed by an authorised signatory and accompanied by evidence of the signatory's authority

10 A member may not use any electronic address (within the meaning of Section 333(4) of the Companies Act 2006) provided in this Notice of Meeting (or in any related or accompanying document (including the form of proxy)) to communicate with the Company for any purposes other than those expressly stated

Shareholder information

Explanatory notes to the Notice of Annual General Meeting

The notes on the following pages give an explanation of the proposed resolutions

Resolutions 1 to 6 are proposed as ordinary resolutions This means that for each of those resolutions to be passed, more than half of the votes cast must be in favour of the resolution

Resolutions 7 to 8 are proposed as special resolutions This means that for each of those resolutions to be passed, at least three-quarters of the votes cast must be in favour of the resolution

Resolution 1 – Annual report

The Directors will present their report, the auditor's report and the audited financial statements for the financial year ended 31 December 2012 to the Meeting as required by law

Resolution 2 – Re-election of Mike Thornton as Director

Mike Thornton was appointed by the Board as a Director on 23 May 2012 In accordance with Article 29.2 of the Articles of Association, Mike holds office only until the AGM, however being eligible, he offers himself for re-election to the Board

Resolutions 3 and 4 – Re-election of Directors

At each general meeting one-third of the Directors for the time being are required to retire (excluding anyone newly appointed in the period) If the number of relevant Directors is not a multiple of three, the number nearest to but not exceeding one-third of Directors should be obliged to retire Directors due to retire by rotation are those longest in office since their last re-election and, as between persons who become or were last re-elected on the same day, those due to retire shall (unless otherwise agreed among themselves) be determined by lot A retiring Director is eligible for re-election In line with past practice two Directors will retire by rotation Doug Liversidge and Mike McMahon retire by rotation and are offering themselves for re-election

Resolution 5 – Re-appointment of auditor

The Company is required to appoint an auditor at each general meeting at which accounts are laid, to hold office until the next general meeting.

The present auditor, Grant Thornton UK LLP, is willing to continue in office for a further year and this resolution proposes its reappointment and, in accordance with standard practice, authorises the Directors to determine the level of the auditor's remuneration

Resolution 6 – Authority to allot shares

The resolution grants the Directors authority to allot relevant securities up to an aggregate nominal amount of £1,348,639 67, being approximately one-third of the Company's ordinary share capital in issue at 8 April 2013 It is not the Directors' current intention to allot relevant securities pursuant to this resolution This authority replaces the existing authority to allot relevant securities but does not affect the ability to allot shares under the share option schemes

Resolution 7 – Disapplication of statutory pre-emption rights

This resolution disapplies the statutory pre-emption rights which would otherwise apply on an issue of shares for cash pursuant to a rights issue where the securities attributable to the interests of all shareholders are proportionate (as nearly as may be) to the number of shares held and generally up to a further £404 591.90, being 10% of the Company's ordinary share capital in issue at 8 April 2013 This replaces the existing authority to disapply pre-emption rights and expires at the conclusion of the next Annual General Meeting of the Company

Shareholder information

Explanatory notes to the Notice of Annual General Meeting continued

Resolution 8 – Purchase of own shares

In certain circumstances it may be advantageous for the Company to purchase its own shares and this resolution seeks authority to do this The Directors would only consider making purchases if they believed that such purchases would be in the best interests of shareholders generally, having regard to the effect on earnings per share and the Company's overall financial position

The resolution gives general authority for the Company to make purchases of up to 40,459,190 ordinary shares (being 10% of the Company's ordinary share capital in issue at 8 April 2013) at a minimum price of 1p and a maximum price being the higher of 5% above the average of the middle market quotations for ordinary shares for the five business days prior to the purchase and the price stipulated by Article 5(1) of the Buy-back and Stabilisation Regulations 2003 (being the higher of the price of the last independent trade and the highest current independent bid on the trading venue where the purchase is carried out)

Companies are permitted to retain any of their own shares which they have purchased as treasury stock with a view to possible re-issue at a future date, rather than cancelling them The Company will consider holding any of its own shares that it purchases pursuant to the authority conferred by this resolution as treasury stock This would give the Company the ability to re-issue treasury shares quickly and cost effectively, and would provide the Company with additional flexibility in the management of its capital base

Shareholder information
Form of proxy
Surgical Innovations Group plc

You may submit your proxy electronically using the Share Portal service at www.capitaregistrars.com/shareholders If not already registered for the Share Portal, you will need your Investor Code

I/We, the undersigned, being (a) member/member(s) of Surgical Innovations Group plc, hereby appoint the Chairman of the Meeting or

Name of proxy ______________________ Number of shares ______________________

(IN BLOCK CAPITALS PLEASE)

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 at Clayton Wood House, 6 Clayton Wood Bank, Leeds LS16 6QZ on 19 June 2013 at 2.00pm and at any adjournment thereof I/We wish my/our proxy to vote as shown below in respect of the resolutions set out in the Notice of the Meeting

Please indicate by ticking the box if this proxy appointment is one of multiple appointments being made ☐

For the appointment of one or more proxy please refer to explanatory note 2 (overleaf)

	For	Against	Vote withheld*
1 To receive and adopt the annual report for the year ended 31 December 2012			
2 To re-elect Mr M R Thornton as Director of the Company			
3 To re-elect Mr D B Liversidge CBE as a Director of the Company			
4 To re-elect Mr M J McMahon as a Director of the Company			
5 To re-appoint Grant Thornton UK LLP as auditor of the Company and to authorise the Directors to determine the auditor's remuneration			
6 To authorise the Board to allot shares in the Company and to grant rights to subscribe for or to convert any security into such shares			
7 To empower the Board to allot equity securities for cash			
8 To authorise the Company to make one or more market purchases of ordinary shares of 1p each in the capital of the Company (Ordinary Shares)			

If you want your proxy to vote in a certain way on the resolutions specified, please place an "X" in the appropriate box If you fail to select any of the given options your proxy can vote as he/she chooses or can decide not to vote at all The proxy can also do this on any other resolution that is put to the Meeting

* The "Vote withheld" option is to enable you to abstain on any particular resolution However it should be noted that a "Vote withheld" is not a vote in law and will not be counted in the calculation of the proportion of the votes "For" and "Against" a resolution

Signed ______________________ Dated this ____________ day of ____________ 2013

Name ______________________

Address ______________________

Review of the year
Governance
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Shareholder information

Form of proxy continued

Surgical Innovations Group plc

Notes

1 Every holder has the right to appoint some other person(s) of their choice who need not be a shareholder as his/her proxy to exercise all or any of his/her rights, to attend, speak and vote on their behalf at the Meeting If you wish to appoint a person other than the Chairman please insert the name of your chosen proxy holder in the space provided (see overleaf) If the proxy is being appointed in relation to less than your full voting entitlement please enter in the box next to the proxy holder's name (see overleaf) the number of shares in relation to which they are authorised to act as your proxy If left blank your proxy will be deemed to be authorised in respect of your full voting entitlement (or if this proxy form has been issued in respect of a designated account for a shareholder, the full voting entitlement for that designated account)

2 To appoint more than one proxy you may photocopy this form Please indicate the proxy holder's name and the number of shares in relation to which they are authorised to act as your proxy (which, in aggregate, should not exceed the number of shares held by you) Please also indicate if the proxy instruction is one of multiple instructions being given

3 The "Vote withheld" option is provided to enable you to abstain on any particular resolution However it should be noted that a "Vote withheld" is not a vote in law and will not be counted in the calculation of the proportion of the votes "For" and Against" a resolution

4 Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, entitlement to attend and vote at the Meeting and the number of votes which may be cast thereat will be determined by reference to the Register of Members of the Company at 2.00pm on the day which is two days before the day of the Meeting or adjourned meeting. Changes to entries on the Register of Members after that time shall be disregarded in determining the rights of any person to attend and vote at the Meeting.

5 To appoint one or more proxies or to give an instruction to a proxy (whether previously appointed or otherwise) via the CREST system, CREST messages must be received by the issuer's agent (ID number RA10) not later than 48 hours before the time appointed for holding the Meeting. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp generated by the CREST system) from which the issuer's agent is able to retrieve the message The Company may treat as invalid a proxy appointment sent by CREST in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001

6 The completion and return of this form will not preclude a member from attending the Meeting and voting in person If you attend the Meeting in person, your proxy appointment will automatically be terminated

7 To be effective, all votes must be lodged not less than 48 hours before the time of the Meeting at the office of the Company's registrars at Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU

Glossary of terms

Clinical Advisory Board (CAB)
UK and US based surgeons who work closely with the design team to develop and test products, bringing together a wealth of experience and expertise in both laparoscopy and arthroscopy

Food and Drug Administration (FDA)
Regulatory body governing the marketing of food, pharmaceuticals and medical devices in the USA

Hip arthroscopy/arthroscopic
Refers to the minimally invasive surgery carried out in the hip joint

Instrumentation
Devices used in surgery to manipulate and dissect tissue or organs

Intellectual Property (IP)
Protection of inventions for commercial advantage over competitors via patent, design registration or trademark

Key Opinion Leaders (KOLs)
KOLs are experts in their field, who influence the behaviour or decision-making of peers

Laparoscopy/laparoscopic
Refers to minimally invasive surgery carried out in the abdominal cavity

Minimally Invasive Surgery (MIS)
Surgery carried out through small incisions (keyholes), thereby minimising wound trauma

Original Equipment Manufacture (OEM)
Manufacture of products supplied to other companies for sale by those companies under their own brand

Port access system
Devices used for gaining access to the abdominal cavity through small incisions

Resposable®
A device or range comprising reusable main elements and disposable accessories

Retraction
Temporary displacement of tissue or organs to increase visualisation during surgical procedures

Trade marks

	UK	EU	US	South Africa	Australia	New Zealand
FrictionFinish	®	®	®	®	TM	TM
Logi	®	®	®	TM	TM	TM
Logic	®	®	®	TM	TM	TM
PretzelFlex	®	®	TM	TM	TM	TM
Resposable	®	®	TM	TM	TM	TM
Surgical Innovations	®	®	®	®	®	®
SwingTop	®	®	®	®	TM	TM
YelloPort	®	®	®	®	TM	TM
YelloPort+plus	TM	TM	TM	TM	TM	TM

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