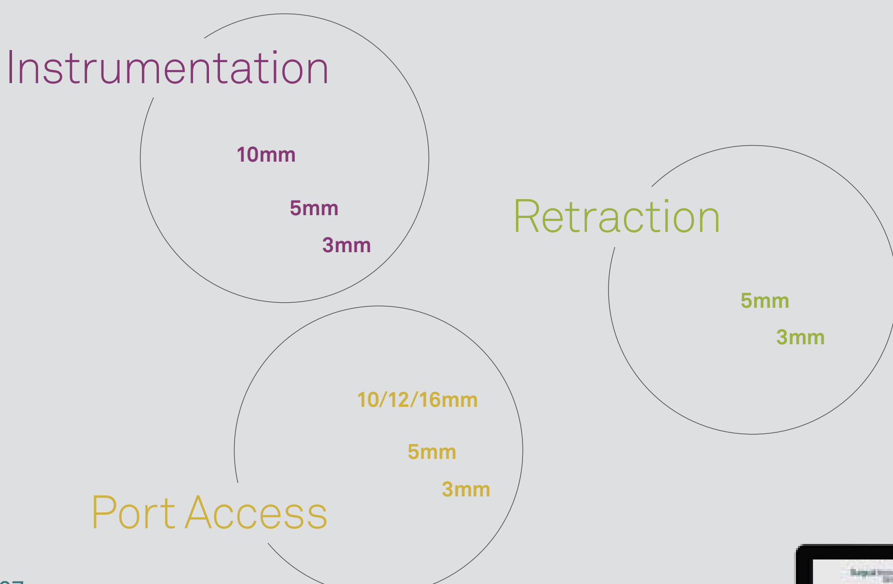
Surgical Innovations Group plc
Annual Report and Accounts 2013

Surgical Innovations

# At the forefront of 3mm "Ultra" Minimally Invasive Surgery

# Surgical Innovations Group plc specialises in identifying and addressing **“the clinical need”**, through the design and manufacture of creative solutions for Minimally Invasive Surgery (MIS).

We listen · We innovate · We improve · We export · **We care...**




**See also** page 07
Our business model

Learn more about
our product range at
**www.sigroupplc.com**

## Retraction

**Ranges**

PretzelFlex™
FastClamp™

## Instrumentation

**Ranges**

Logi™ Range
Logic™
Quick™

## Port Access

**Ranges**

YelloPort+plus™

# Chairman's statement

## Summary

- Demand for Resposable® technology drives SI branded revenues by 22%.
- Recent appointment of Richard Tattersall as Director of Manufacturing proving invaluable to our manufacturing and planning operations.
- New improved production processes have now been introduced.

"Following strategic investment into the Group's revenue channels in the US, there has been an increased exposure to the SI branded product offering, underpinning the overall 12% increase in Group revenue."

**Doug Liversidge CBE** Chairman

## Results and operating review

We are pleased to report that, following strategic investment into the Group's revenue channels in the US, there has been an increased exposure to the SI branded product offering, which has underpinned the overall 12% increase in Group revenue to £8.55 million (2012: £7.64 million). The appointment of Rick Barnett, President of US Sales and Operations, as reported previously, has driven this growth and the Board is encouraged by the further opportunities that this market offers SI. Overall there has been an increase in the demand for the Group's Resposable® technology as SI branded product revenues have grown by 22%. The growth in revenue of consumable elements reflects an important measure of our performance worldwide.

As previously announced, due to the considerable demand for the Group's products and the step change in manufacturing volumes in the final quarter of 2013, the Group experienced difficulties in delivering the quantities required. Significant management time was invested in resolving these issues and the Board is pleased to report that new improved production processes have now been introduced. Following this investment, output capabilities are improving, whilst maintaining the exacting standards required for medical devices. Underpinning this is the recent appointment of Richard Tattersall as Director of Manufacturing. Richard brings with him a wealth of experience and knowledge within large-scale manufacturing that is already proving invaluable to our manufacturing and planning operations.

The Group's profitability was adversely affected by the combined effect of the US Dollar exchange rate in the final quarter of 2013 and the necessary improvements in manufacturing operations designed to streamline and improve process flows of individual product lines, in particular to support the 73% growth in US revenues. As a result, operational capacity was initially reduced, inevitably impacting on manufacturing contribution to profitability, before being re-established at the end of the year to deal with the order backlog. These changes in the product processes initially resulted in higher than anticipated levels of material wastage, but subsequently, following the validation of production lines, substantial improvements are now evident.

The consequence of the above is overall lower Group profitability than expected, with an adjusted EBITDA (excluding exceptional items) for the year ended 31 December 2013 of £2.51 million (2012: £2.89 million). Retained profit for the year was £800,000 (2012: £686,000) and basic earnings per share were 0.20p (2012: 0.17p).

The bank overdraft position at the year end was £2.58 million (2012: £1.41 million). Since the year end, the Board has successfully concluded a refinancing of bank facilities, providing the necessary working capital headroom for the foreseeable future.

## Outlook

The first quarter of 2014 has seen a focus on further improvement in manufacturing operations to ensure the Group is positioned to support the execution and implementation of the Group's clinical and development strategy.

By working towards a unique product offering within a developing area of laparoscopic surgery, the Board looks forward to the future with confidence.

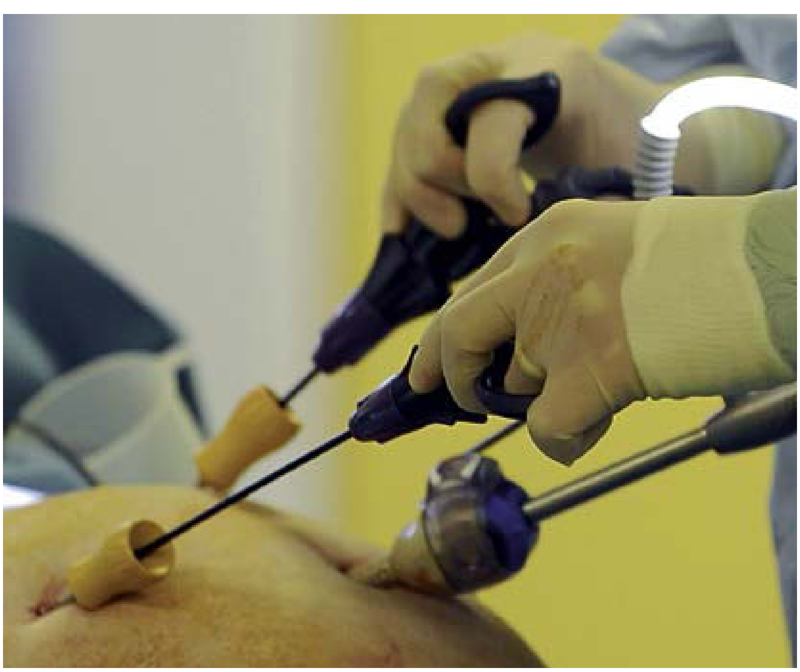
**Doug Liversidge CBE**
Non-executive Chairman
14 April 2014

# Highlights


## Summary

- Revenue of £8.55 million (2012: £7.64 million), a 12% increase against the previous year
- Revenue of SI branded products increased by 22% to £6.50 million (2012: £5.33 million), driven by the demand for the Group's Resposable® technology
- 73% increase in revenue to the US of SI branded products, through multiple new routes to market
- Significant investment in manufacturing and revenue infrastructure to support the US market and related uplift in demand
- Adjusted EBITDA of £2.51 million (2012: £2.89 million) was impacted by the introduction of improved manufacturing processes and currency fluctuations
- Basic earnings per share increased to 0.20p (2012: 0.17p)
- SI continues to be at the forefront of 3mm "Ultra" MIS as it becomes a globally accepted technique
- Further progress on development of world-class clinical training facility underpinned by Regional Growth Fund (RGF) award of £5.05 million

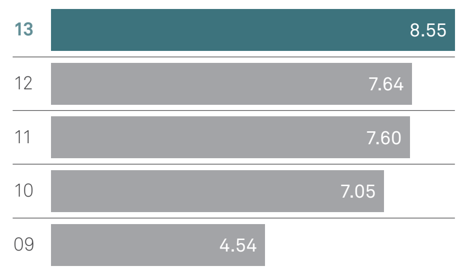

**See also** pages 09 and 12
Operating and Financial reviews



Consultant Surgeon James Halstead using SI's Ultra MIS 3mm range in surgery.

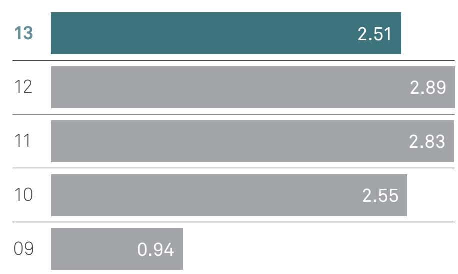
**Total revenue** (£m)

£8.55m +12%




**Adjusted EBITDA** (£m)

£2.51m -13%




**Group profit before tax** (£m)

£0.80m -36%

# Our strategy

## Summary

- The core strategy of the Group is to deliver sustained growth of SI branded products within the Minimally Invasive Surgery (MIS) clinical space.
- The Group's objective is to deliver the overall core strategy by developing a unique and dominant position within 3mm laparoscopic surgery.
- The Group has substantially invested in the creation of a US infrastructure that will support this campaign towards 3mm "Ultra" MIS.

The core strategy of the Group is to deliver sustained growth of SI branded products within the Minimally Invasive Surgery (MIS) clinical space, and, at present, revenues are purely derived from the specific area of laparoscopic surgery. The secondary OEM segment of the business provides a revenue stream from devices again targeted at laparoscopic surgery. Importantly, these instruments, although third party branded, have intellectual property and manufacturing "know-how" under SI ownership and control.

Laparoscopic surgery is the strategic focus of the business, in both the SI Brand and OEM segments. Within this environment SI has traditionally developed and manufactured devices to address access, manipulation and retraction into and within the abdominal cavity. Current surgical techniques command specific diameter instrumentation of 12mm, 10mm and 5mm. There has been a logical progression towards smaller sizes and, being appreciative of Clinical Advisory Board (CAB) input, the Group is committed to the development of 3mm laparoscopic surgery, "Ultra" MIS. In order to convert the vast majority of laparoscopic procedures to this clinical technique, SI intends to promote a complete range of 3mm devices. The Group is now committed to an internal development programme and importantly, a "buying in of technology" approach, through OEM/licence opportunities that will together deliver these surgical requirements.

The Group's objective is to deliver the overall core strategy of growth in SI branded products by developing a unique and dominant position within 3mm laparoscopic surgery.

Our philosophy of providing cost-effective, quality instrumentation remains a key component of our value-added proposition to hospital procurement managers worldwide. Our aim is, wherever possible, the development of Resposable® devices, which consistently provide cost savings against mainstream disposable alternatives.

The Group has substantially invested in the creation of a US infrastructure that will support this campaign towards "Ultra" MIS, and in Europe key distributors have been identified to raise its profile. Clinical endorsement and support will be achieved through the ongoing expansion of our CAB, both in the UK and Internationally, together with attendance at specific clinical congresses.

SI's OEM strategy is now dictated by the added value an OEM agreement will have on both our OEM and SI Brand segments.

SI currently occupies the laparoscopic field within the discipline of MIS. It is an objective of the business to transfer our core competencies into other areas of MIS. Such technology transfers are classified as "blue sky" development projects and are primarily funded through Technology Strategy Board (TSB) awards. Our first project remains focused on hip arthroscopy and associated procedures and is supported by two eminent hip arthroscopy surgeons from our CAB.

The advances towards "Ultra" MIS and the move into new areas of MIS will be supported by the new clinical training centre in Leeds. The project, backed by the Regional Growth Fund (RGF) Award, is progressing well in terms of agreed timescales and budget requirements. The training centre aims to further enhance our global reputation as an innovative medical device company, building and developing our links with both UK and international surgeons. With the training centre located within a new SI design and manufacturing facility, attending surgeons will have the opportunity to make a positive contribution towards all aspects of the design process.

| Objectives | | Progress |
|---|---|---|

## 1 Delivery of sustained growth of SI Brand revenue

| Objectives | Progress |
|---|---|
| Maximise SI Brand exposure in the US, the world's most prominent market | Established key multiple strategic partners across the US |

## 2 Promotion of the Resposable® concept

| Objectives | Progress |
|---|---|
| Organic growth of the reusable modular platform | Achieved approval of this concept within our home and strategic international markets |

## 3 Position SI as a leader in 3mm "Ultra" MIS instrumentation

| Objectives | Progress |
|---|---|
| Develop global, clinical acceptance of 3mm "Ultra" MIS | Engaging with those key opinion leaders (KOLs) promoting the move to 3mm laparoscopic surgery |

## 4 Continued expansion into other areas of MIS

| Objectives | Progress |
|---|---|
| Focus on hip arthroscopy and associated procedures | Good progress enabled through Technology Strategy Board (TSB) investment |

## Our evolution

Opening in 2015, our new international facility is part of our planned growth strategy. This is an important step to providing both training and development in all areas of MIS.

### 1992–2007

- Sub-assembly manufacturing
- Limited design capabilities
- No clinical training

### 2008–2013

- 80% in-house manufacturing
- Substantial investment in R&D
- No clinical training

### 2015–beyond

- 95% in-house manufacturing
- Improved design
- Clinical training

### Clinical training facility

In a drive to become an established world leader in clinical skills and innovation, we are investing in the UK's first purpose-built clinical training facility. The centre will provide a unique platform for surgeons to develop their skills and knowledge, focusing on emerging technology and best practice.

**See also** page 16
Corporate social responsibility

# Our business model

## Applying our **expertise** to new technologies and opportunities in Minimally Invasive Surgery (MIS)

Experts in laparoscopy

Focused on development

Expansion and diversification

### Clinical collaborations

Our experienced design team works closely with our UK and International Clinical Advisory Board surgeons to improve and create medical devices that meet "the clinical need".

### Advanced manufacturing

Designed and manufactured in the UK, our cost-effective medical devices are pioneering, ergonomic, easy to assemble and easy to use.

### IP portfolio

We continue to enhance our intellectual property in the field of MIS to protect the SI brand in international markets.

### Improved technology

We rethink and reinvent to deliver high quality, cost-effective medical device solutions.

### Enhanced revenue per case

We constantly develop our product portfolio to create a total laparoscopic solution.

### Strategic OEM partnerships

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

### Move to "Ultra" 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. This strategy satisfies the growing demand for smaller incisional surgery, which is fast becoming a globally accepted technique.

### Technology transfer

The technologies used in our 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 identity emerging areas of surgery, where our skills and expertise can be easily transferred.

**See also** page 08
Our market opportunities

# Meeting the **"clinical needs"** of forward-thinking surgeons

Our pioneering products are developed in close collaboration with UK and international surgeons (KOLs) to ensure they meet patients' needs and remain at the forefront of innovation.

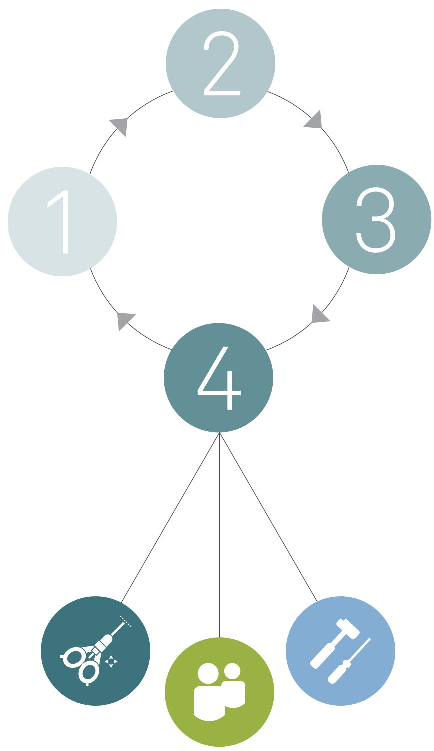
## 1 **Clinical need**

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 CAB feedback;
- evaluating the latest cutting-edge innovations; and
- 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.

### SI Brand

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

### OEM

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

### Industrial

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

Our market opportunities

# Responding to **"clinical need"** and market opportunities

## United Kingdom

SI's Resposable® concept is perfectly placed to support the NHS's cost reduction programme.

**21%**
**increase in sales to UK hospital of SI branded product**

**32%**
**increase in sales to UK hospital YelloPort+plus™**

### The UK market grows from strength to strength

Since the beginning of 2013 our UK dealer, Elemental Healthcare, has converted 21 accounts. This has seen our SI branded sales rise by 63%. It has also seen a 32% increase in YelloPort+plus™ sales, which will have a positive impact on continuous disposable revenue streams over the coming years.

## United States

Being the principal consumer of medical devices in the world, the US offers real opportunities for Surgical Innovations in terms of revenue and brand recognition.

**75%**
**increase in US sales of SI branded products**

**4**
**new stocking dealers introduced covering 15 new states**

### Expansion of the US market

SI continues to focus on the development of US opportunities for our branded products. Through a substantial increase in sales channels to market and resulting brand exposure we have seen a 75% increase in sales of SI branded products.

### "Ultra" MIS

We continue to develop our innovative 3mm "Ultra" MIS products, creating a unique proposition for clinicians worldwide. This strategy satisfies the growing clinical trend towards smaller incisional surgery that reduces post operative pain and trauma for patients enhancing abdominal cosmesis. SI is committed to the development of 3mm laparoscopic surgery "Ultra" MIS.

### Hip arthroscopy

It is our objective to transfer our core competencies into the other area of Minimally Invasive Surgery (MIS). Such technologies transfers are classified as blue sky development projects and are primarily funded through Technology Strategy Board (TSB). Our first project remains focused on hip arthroscopy and associated procedures.

# Operating review

## Summary

- Growth of 22% in SI Brand sales to £6.50 million (2012: £5.33 million) driven by US and UK expansion.
- US revenue growth in SI Brand sales of 73% to £2.49 million (2012: £1.44 million).
- 2014 has started well with sales on track and orders being successfully fulfilled with the three new production lines.

**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.

"The Group has made progress across a number of key areas of the business during the period under review."

**Graham Bowland** Chief Executive Officer

The Group has made progress across a number of key areas of the business during the period under review, despite the issues encountered within the manufacturing processes. The Board is working to refine the Group's strategy; to develop smaller devices for 3mm "Ultra" MIS, to drive growth of SI Brand products with emphasis on the UK and US markets, and to ensure that our innovative R&D projects are fully grant funded. Considerable progress has been made across all of these areas.

## SI Brand

Growth in sales of SI branded products primarily arose from two key markets: the UK and US. It is generally accepted within the SME healthcare sector that access to the NHS is extremely difficult; consequently SI previously focused on developing an export strategy to drive revenue growth. In 2013, as a result of investment in both time and resources, we experienced growth of 63% in UK SI Brand sales, through our exclusive distributor, Elemental Healthcare. The catalyst for this significant increase has been the focused drive to reduce cost and eliminate waste within the NHS. SI has always placed great emphasis on delivering cost-effective, high quality devices, and this philosophy aligns itself perfectly to the needs of the NHS where we are experiencing a substantial number of hospital conversions to our Resposable® technology.

A strong UK presence greatly assists promotion of our technology in export markets, with positive clinical feedback and high usage rates providing comfort to international surgeons previously unaware of SI and Resposable® devices.

Importantly, SI continues to develop the CAB and our ability to attract surgeons to work with us on creative ideas for medical devices sets SI apart from our natural competitors, engendering a loyalty to the brand and our innovative technologies.

In the US, following the appointment of Rick Barnett as President of US Sales and Operations, we were able to develop the distribution infrastructure and exposure to the SI brand. With a dedicated resource, supporting and driving the dealer network, order intake increased in the second half of the year, resulting in US revenue growth of 73% to £2.49 million (2012: £1.44 million). However, as a result of our manufacturing processes unable to withstand the spike in demand in the final months of the year, the US supply chain continues to receive intensive monitoring in order to rebuild customer confidence through our ability to deliver orders on time and in full.

The US remains our key market. Over 50% of the world's medical device spend is within the US and, as with our home market, Resposable® cost-effective solutions are gaining traction with hospital procurement departments as they seek to drive down individual procedure costs.

We are conscious that, as well as offering cost savings, SI has to create an added value proposition to hospitals. Shortened supply chains, easy to use procedure kits and surgeon interaction on product development are all under consideration as part of our investment to continually grow US revenues and market share.

# Operating review
continued

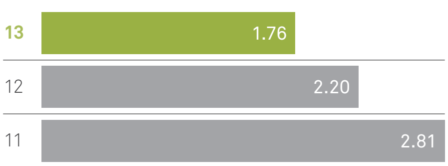
## Key Performance Indicators (KPIs)

**SI Brand segment revenue** (£m)

£6.50m +22%

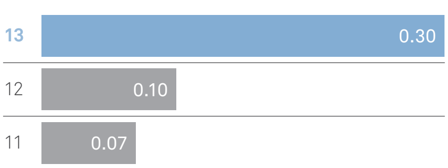

**OEM segment revenue** (£m)

£1.76m -20%




**Industrial segment revenue** (£m)

£0.30m +200%




## SI Brand continued

Within the SI Brand, our port access system, YelloPort+plus™ remains a major revenue generator, contributing revenue of £3.22 million (2012: £2.82 million). In 2013, in order to reinforce and enhance our user base, we committed to a long-term investment plan by assisting in the adoption of the reusable elements of the product offering. Such support has seen a substantial number of cannulas ordered by the dealer network which, over a five-year period, will result in increased revenues from the associated consumable items.

We continue to monitor progress of the programme and have seen positive outcomes already in several important markets.

Our aim is to increase actual revenues per individual procedure, whilst offering cost savings to hospital procurement managers. At present, revenues are generated from individual elements rather than the full range of SI products. By creating unique added-value procedure kits we believe this issue can be addressed, especially as we move to a unique proposition with our Ultra MIS technology.

## OEM

The OEM business continues to provide a contribution to the Group's results; however, given that this is not at a predictable or steady rate, the Board is working to reduce the Group's emphasis on this part of the business. Any decline in this area is being successfully offset by the growth in the SI Brand products, from where the Board sees future growth emanating.

## Industrial

SI Industrial business continues to work through a close relationship with Rolls Royce, our key industry partner in this business segment. During the period we successfully secured a development contract for a new requirement of our flex technology and, since the period end, a further contract has been secured to develop another deployment application. Although this business is not predictable in terms of timing of revenues, from either development contracts or associated device sales, it continues to be an important contribution and further illustrates the potential of the Group's innovative technology.

## Clinical Training Centre

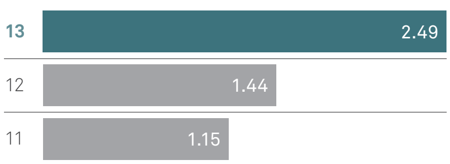
As the Group moves its innovative products into new areas of surgery, largely focused around 3mm surgery, it is evident that there will be considerable requirements for clinical training. The proposed Clinical Training Centre, part of SI's new facility, will not only be used to train surgeons on the Group's own products, but will be a generator of revenue in its own right through multi-channel training courses. The Board anticipates that the Clinical Training Centre will reap rewards in terms of increased sales of the Group's products, as it becomes an integral part of a surgeon's training.

Following granting of planning permission, the Group anticipates that construction will commence in H2 2014, with the facility being completed and operational during Q3 2015. The construction and fit out is being successfully de-risked, with equipment likely to be sponsored by local companies. With specialists being identified to run the centre, the Board is pleased with current progress and excited about the potential for this novel and sophisticated facility and the relationships it will engender between SI and the broader surgical community.

## Key Performance Indicators (KPIs)

**SI Brand – US sales** (£m)

£2.49m +73%

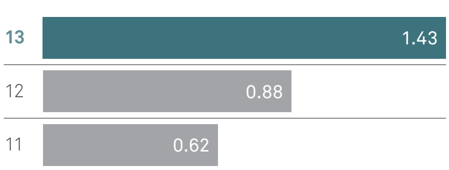



**SI Brand Resposable® product revenue** (£m)

£4.03m +27%


**SI Brand – UK sales** (£m)

£1.43m +63%




## Research and development

The Board believes that there is considerable scope for the transferability of the Group's technology and is currently working to explore other areas with current focus on Hip Arthroscopy. This is being funded on a case-by-case basis through grant applications, such as those from the Technology Strategy Board. The Group has appointed an experienced Executive in order to focus on all of these grant applications and projects. Surgical Innovations has a strong track record for securing regulatory approval and patent protection of the Group's products, with a dedicated quality department and concept team. There is significant opportunity in a number of new areas of MIS, and the Board's approach is to be cautious and to de-risk the R&D by awaiting grant funding before progressing any of the product development projects.

## Team

SI has experienced major challenges in the year and is addressing them by a programme of continual improvement. This programme includes investment in people and training, increasing knowledge, expertise and skills across the organisation. The SI team has been particularly strengthened in the areas of manufacturing and process engineering to ensure SI has the ability to deliver total customer satisfaction.

SI is proud of the efforts that it puts into its apprenticeship scheme and internal training of staff. There is considerable emphasis on succession planning and investing in the future of the business. The apprenticeship scheme has been particularly successful, especially in the manufacturing part of the business, and the Board intends to extend this scheme to other areas of the business once the new facility is operational.

## Outlook

The Group's strategy is to drive the SI Brand through new innovative devices coupled with enhanced routes to market. The Board sees the future growth of the Group from a suite of products that create a unique clinical solution within a growing area of surgery, Ultra MIS, driving further penetration in the UK and US markets, and over the long-term exploitation of our core technology in other areas of MIS. These areas of focus, alongside the construction and commencement of operations at the Clinical Training Centre, have considerable potential for further development and the Board intends to drive forward all of these initiatives over the coming months.

The Board is exploring innovative ways of increasing the Group's revenue per case and adding value to each procedure; further updates on this will be made in due course.

# Financial review

## Summary

- Reported revenue for 2013 increased 12% to £8.55 million (2012: £7.64 million).
- Gross margin reduced to 44.3% (2012: 50.5%), reflecting the manufacturing difficulties experienced in the second half.
- Gross margin was also adversely impacted by the strengthening of the US Dollar in the second half.

"We were delighted to conclude a refinancing of the Group's banking facilities in April 2014 with Yorkshire Bank providing a committed three year revolving credit facility of £3m."

**Mike Thornton** Chief Financial Officer

## Revenue

Reported revenue for 2013 increased 12% to £8.55 million (2012: £7.64 million). A segmental analysis of revenue is provided below which illustrates the strong growth performance from the SI brand, offset by a decline in sales of OEM products and a significant contribution from the Industrial segment. Further commentary on performance by segment is provided in the Operating review.

## Gross margin

Gross margin reduced to 44.3% (2012: 50.5%), reflecting the manufacturing difficulties experienced in the second half of the year when manufacturing volumes were increased in anticipation of the strong US-led sales demand. Gross margins were also adversely impacted by the strengthening of the US Dollar in the second half, which increased from 1.55 at the end of August to 1.65 at the end of the year.

## Operating expenses

Excluding exceptional items, operating expenses increased by £466,000 during the period to £2.709 million (2012: £2.243 million). This increase primarily resulted from increased amortisation of product development intangible assets (£206,000), charges for share-based payments (£82,000) and recurring costs arising in connection with the establishment of the enhanced US distribution model (£196,000). Notwithstanding this increase, the Group continues to rigorously control costs.

## Exceptional items

During 2013 we incurred exceptional costs of £196,000 (2012: £294,000) related entirely to the settlement of old income tax liabilities. The prior year exceptional item of £294,000 related to the restructuring of 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 2013, resulting in interest payable of £57,000 (2012: £31,000). We also incurred £62,000 (2012: £63,000) of finance charges in respect of finance lease obligations. Finance costs will increase in future years, primarily as a result of the new building project which will be funded in part by a bank mortgage alongside the RGF grant.

| | **2013 £'000** | 2012 £'000 | % change |
|---|---|---|---|
| SI Brand | **6,500** | 5,334 | +21.9% |
| OEM | **1,757** | 2,204 | -20.3% |
| Industrial | **296** | 101 | +193.1% |
| Total | **8,553** | 7,639 | +12.0% |

## EBITDA and operating profit

EBITDA (excluding exceptional items) reduced from £2.888 million to £2.514 million, primarily reflecting the marked reduction in gross margin, but also the increase in operating expenses.

We continue to believe that 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.

## Taxation

The Group recognised a small tax credit of £4,000 (2012: £547,000 charge) reflecting a deferred tax charge of £193,000 offset by a corporation tax credit of £197,000. The effective rate of tax of nil% is partially distorted by remeasurement of deferred tax at 20% (2012: 23%) reflecting the continuing reduction in UK corporation tax rates.

The low rate of corporation tax, the patent box regime and the research and development rules create a very favourable tax position for the Group and during 2013 the Group submitted enhanced research and development claims in respect of 2012 elected to exchange tax losses for a cash refund of £197,000 (2012: £287,000) which was received after the year end.

## Earnings per share (EPS)

Basic and diluted earnings per share increased to 0.20p (2012: 0.17p). Adjusted earnings per share (which exclude exceptional items and a prior year deferred tax correction) reduced to 0.25p (2012: 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, £1.854 million (2012: £1.850 million) of costs have been capitalised during the year, increasing the total amount of capitalised costs to £7.341 million (2012: £6.393 million).

Consistent with expectations, the amortisation charge against capitalised costs increased significantly to £906,000 (2012: £700,000), 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 2013 following review by the Board.

Capital expenditure on tangible assets during the year was relatively low at £326,000 (2012: £183,000) and included £90,000 of costs incurred in respect of the new facility. Capital expenditure in 2014 and 2015 is expected to be significant given the new building project.

## Foreign currency

During 2013 the Group has continued to generate significant surplus US Dollars through sales to customers and this is likely to continue given the strong progress made in developing this market. These have either been sold into Sterling at spot rates or market risk has been eliminated through the use of forward contracts. The strengthening of Sterling against the Dollar at the end of 2013 was against most consensus forecasts, and consequently the Group did not have sufficient forward contract cover for the strong Dollar denominated sales in the second half of 2013. 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 £2.449 million (2012: £2.662 million). However, the significant working capital increase during the year of £1.278 million (2012: £1.956 million) (see below) reduced cash generated from operations to £1.171 million (2012: £0.706 million).

As expected, cash used in investment activities was consistent with prior year at £2.043 million (2012: £1.979 million).

At 31 December, net debt, which is defined as cash and cash equivalents less bank overdraft and obligations under finance leases, stood at £3.488 million (2012: £2.627 million). In addition to existing finance lease facilities, the Group operated using a £2.8 million overdraft facility from HSBC and at 31 December 2013, £2.584 million of this facility was utilised.

We were delighted to conclude a refinancing of the Group's banking facilities in April 2014 with Yorkshire Bank providing a committed three year revolving credit facility of £3m which provides much greater certainty than the previous overdraft. The commitment of the revolving credit facility is subject to compliance with financial covenants which measure profitability and debt service starting quarterly from June 2014 and September 2014 respectively.

## Working capital

Working capital increased by £1.278 million (2012: £1.96 million) to £7.878 million (2012: £6.60 million). Long-term trade receivables increased by £1.487 million compared to the prior year reflecting further investment in the YelloPort+plus™ sales model. Excluding this item, short-term working capital was closely monitored and reduced by £209,000 compared to prior year.

Looking forwards, we are committed to improving our manufacturing processes which should improve our ability to offer customers high levels of on time in full (OTIF) performance and, in time, enable stock turn to reduce. Our distributors operate in many different countries where credit terms and local practices vary significantly and consequently relatively high trade receivables are a feature of our business that we do not expect to change in the short term.

# 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 the Directors seek to mitigate wherever possible. The principal risks are set out below.

| Risk and description | Mitigating actions | Change |
|---|---|---|
| **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 who provide necessary expertise and also familiarity with the Group's product range. | No change |
| **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 that:<br>• assists product development teams with support as required to minimise the risk of regulatory approval not being obtained on new products; and<br>• ensures that the Group operates processes and procedures necessary to maintain relevant regulatory approvals.<br>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. | No change |
| **Liquidity** | | |
| Due to the continued reinvestment in research and development, the Group does not currently generate free cash flow and the current committed banking facility of £3 million is committed subject to ongoing compliance with covenants. Failure to meet these covenants may have a severe impact upon the business. | Liquidity and covenant compliance is monitored carefully across varying time horizons to facilitate short-term management and also strategic planning. This monitoring enables the management team to consider and to take appropriate actions within suitable timeframes. | Increased risk for 2014 |

| Risk and description | Mitigating actions | Change |
|---|---|---|
| **Customer concentration** | | |
| The Group exports to over 30 countries and distributors around the world, but certain distributors are material to the financial performance and position of the Group. As disclosed in note 2 to the financial statements, two customers individually accounted for more than 10% of revenue in 2013 (together, 30%) and the loss, failure or actions of one of these customers could have a severe impact on the Group. | The majority of distributors, including the most significant, are well established and their relationships with the Group spans many years. Credit levels and cash collection are closely monitored by management, and issues are quickly elevated both within the Group and with the distributor. | No change |
| **Foreign exchange** | | |
| 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 ongoing 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. | Increased risk for 2014 |

# Corporate social responsibility

### Our approach:

Surgical Innovations (SI) is keen to incorporate corporate social responsibility (CSR) polices across all areas of the business to help improve performance. Our CSR commitments cover a number of areas including:

- Employees
- Investing in the young
- Business ethics
- Clinical training
- Community engagement
- Health and safety and environment

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.

## 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.

Last year SI took part in a number of fundraising activities such as arranging a cake sale to support breast cancer awareness and cooking a big breakfast for all SI employees to raise the profile of prostate cancer and supporting the "Movember" campaign. We also held a Christmas raffle to raise money for the National Blind Children's Society. This summer a number of SI's employees are taking part in a 120 mile cycling challenge around Yorkshire to raise money for the Sick Children's Trust.

## Investing in the young

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.

Last year first-year apprentice student James Nicholson was presented with the prestigious "Apprentice of the Year Award" at Leeds City College, making him the only first-year student to ever win the award.

## 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.

Working with clinicians we have also introduced a pioneering range of "Ultra" MIS technologies that takes MIS to the next generation by significantly reducing post-operative pain and trauma for patients. Smaller incisions promote quicker healing and can negate the need for port site closure suturing at the end of procedures, saving the patient the discomfort of stitch removal.

Many of our product lines use Resposable® technology, a combination of reusable and disposable elements, which offers hospitals worldwide high quality instrumentation with cost-saving advantages. 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. They can help healthcare organisations reduce their costs per procedure by up to two-thirds and also reduce the amount of clinical waste they have.


First year apprentice James Nicholson receiving his award.


SI visiting Tong High School.

## Clinical training

The advances towards "Ultra" MIS and the move into new areas of MIS will be supported by the creation of a new state-of-the-art clinical training centre in Leeds.

The surgical training facility aims to provide a unique platform for surgeons from around the world to develop their technical skills and knowledge. It will provide high-quality laparoscopic and arthroscopic skills training with a focus on training clinicians on new procedures, emerging technologies and best clinical practice. The centre will use a variety of teaching methods, including high-level simulation. For SI it will help further enhance our global reputation as an innovative medical device company whilst contributing to society by improving levels of patient care.

## Community engagement

Throughout the year we have been delighted to visit a number of schools in the region to talk to schoolchildren about the types of opportunities that are available to them after school within the medical device industry. Recently Joshua Sheard, an SI Development Engineer, visited Tong High School to talk about SI's successful apprenticeship scheme and how students could get involved. We have also been working with a number of head teachers from the region in a unique scheme that will see schools and industry working closer together in the future.

SI was also asked to showcase its manufacturing excellence as part of the Yorkshire Manufacturing Excellence Showcase held at the Department for Business, Innovation & Skills (BIS). The exhibition aimed to raise the profile of Yorkshire and showcase the varied and innovative nature of Yorkshire's manufacturing. SI is committed to bringing manufacturing home to Yorkshire and over the years we have invested substantially in manufacturing facilities to ensure that our philosophy is realised.

## Health and safety and environment

SI has an established Health and Safety Committee. 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.

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 encourage ideas and suggestions from all employees in this regard and over the last few months have run a proactive green campaign to encourage staff to think about how their actions can reduce the Company's carbon footprint.

**Graham Bowland**
Chief Executive Officer
14 April 2014

# Board of Directors

## Doug Liversidge CBE
**Non-executive Chairman**

**Board committees** R A

**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** Doug is also a Non-executive Director of IP Group Plc.

## Graham Bowland
**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.

## Mike Thornton
**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.

## Colin Glass
**Non-executive Director**

**Board committees** R A

**Experience** Colin is a Chartered Accountant and a partner in Winburn Glass Norfolk. He is a founding 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.

## Ray Simkins
**Non-executive Director**

**Board committees** R A

**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.

## Professor Mike McMahon
**Non-executive Director and Chair of the Clinical Advisory Board**

**Board committees**

**Experience** Mike, a founder Director of Surgical Innovations Ltd, became Non-executive 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.

**Board committees**

- R Remuneration Committee
- A Audit Committee
- R Chairman of Remuneration Committee
- A Chairman of Audit Committee

# Advisory boards

SI's UK and international **Clinical Advisory Boards (CABs)** helps to identify clinical need and is key in all aspects of the product design cycle.

Read more about our
UK and international CABs
**www.surginno.com/cab**

## Philippe Grange

**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 and Honorary Professor of Urology at The Beijing Hospital.

## Alfred Cutner

**Laparoscopy**

Alfred is consultant at University College Hospital, London, past president of The British Society for Gynaecological Endoscopy and current Vice-chair of the British Society of Urogynaecology.

## Jon Conroy

**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 and The British Orthopaedic Association and a Fellow of The Royal College of Surgeons of England.

## Siôn Glyn-Jones

**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.

## Jake Timothy

**Neurosurgery**

Jake is a neurosurgeon based in Leeds. He completed the National Spine Fellowship in Leeds in 2001 and 95% of his workload in spine both acute and elective. He is the elected UK delegate for the European Association of Neurosurgeons (EANS) training course.

## Marco Scarci

**Video-assisted thoracoscopic surgery**

Marco is a Consultant Thoracic Surgeon specialising in video-assisted thoracoscopic surgery (VATS) at Papworth Hospital NHS Foundation Trust. Marco undertook his specialist training in Italy, Malta, Essex Cardiothoracic Centre and Guy's and St Thomas'.

## Henrik Steinbrecher

**Paediatric**

Henrik is a consultant at Southampton University Hospital NHS Trust where he has been a consultant since 1998. Henrik has been an executive member of the Royal College of Paediatrics (RCPCH) Clinical Directors Group from April 2004 to June 2006 and has been an advisor on Simulation Training for Specialist Advisory Committee (SAC) in Paediatric Surgery.

The **International Clinical Advisory Board (ICAB)** is a group of key opinion leaders around the world who are on hand to offer advice about their market and feedback on our products.

## Sean Barnett

**Paediatric**

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 and Thoracic Surgery.

## Bernhard Dauser

**Laparoscopy**

Bernhard is a Consultant General Surgeon at the St John of God Hospital in Vienna, Austria. He graduated in 2003 from the Medical University of Vienna and completed his surgical training in 2010. In 2011 the Austrian Medical Chamber appointed him as emergency physician and two years later as visceral surgeon.

## Marco Adamo
**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 is a council member of British Obesity and Metabolic Surgery Society (BOMSS).

## James Halstead
**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.

## Chris Sutton
**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.

## Ian Brayshaw
**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.

## John Griffith
**Laparoscopic colorectal surgery**

John is a Consultant Colorectal and General Surgeon at Bradford Royal Infirmary. He specialises in laparoscopic colorectal surgery for cancer, inflammatory bowel disease and functional disorders. He also performs laparoscopic general surgical procedures.

## Romain Pizzi
**Veterinary**

Romain is the only veterinary surgeon in the UK to specialise in minimally invasive keyhole surgery for wildlife and has had strong links with SI for many years helping drive awareness of Surgical's MIS products.

# 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 Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

**Bankers**
Yorkshire Bank
20 Merrion Way
Leeds LS2 8NZ

**Financial public relations**
Abchurch Communications Limited
125 Old Broad Street
London EC2N 1AR

## Jody Valk
**Laparoscopy, thoracoscopy**

Jody graduated from the University of Utrecht in the Netherlands in medicine in 1998. He is trained in thoracic and general surgery, specialising in upper gastrointestinal tract surgery and lung surgery. Since 2006 he has worked at the Stuivenberg Hospital in Antwerp, Belgium.

## Bassem Safadi
**Laparoscopy**

Bassem is an Associate Professor of Clinical Surgery at the American University of Beirut in Lebanon. He is one of the leaders in laparoscopic and bariatric surgery in Lebanon and the Middle East.

## Denis Pitot
**Laparoscopy**

A specialist in bariatric surgery, Denis performs both laparoscopy and SILS (Single Incision Laparoscopic Surgery). He is part of the BeSOMS board (Belgian section of Obesity and Metabolic Surgery) and is a member of IFSO (International Federation for the Surgery of Obesity).

# Directors' report

The Directors present their annual report, together with the audited financial statements, for the year ended 31 December 2013.

## Principal activities

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.

## Results and dividends

The Consolidated statement of comprehensive income for the year is set out on page 28.

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 who all served throughout the year and their biographical details are set out on pages 18 and 19.

## 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 2013 Beneficial** | 1 January 2013 Beneficial |
|---|---|---|
| D B Liversidge CBE | **7,171,821** | 7,171,821 |
| N G Bowland | **5,168,498** | 5,028,498 |
| 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** | 17,218,511 |

Apart from the interests disclosed below and the options referred to on page 25, 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 14 April 2014.

Other than as disclosed in note 17, 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.

## Substantial shareholdings

Other than the Directors' own holdings, the Board has been notified that, as at 31 March 2014, 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%) |
| Mr C W N John | **37,907,124** (9.37%) |
| TD Direct Investing | **24,197,138** (5.98%) |
| Investec Wealth & Investment | **20,164,087** (4.98%) |
| Barclays Wealth Mgt (UK) | **19,679,326** (4.86%) |
| Unicorn Asset Management | **19,135,116** (4.73%) |
| Hargreaves Lansdown Asset Management | **18,899,948** (4.67%) |
| Halifax Share Dealing | **17,286,558** (4.27%) |

## Share issues

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

- 140,000 at 1.5p.

## Directors' responsibilities statement

The Directors are responsible for preparing the Strategic report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law 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.

The Directors confirm that:

- so far as each Director 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 as Directors 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.

## 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 13 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
14 April 2014

# 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 2014 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 2013 £'000** | **Benefits 2013 £'000** | **Total emoluments 2013 £'000** | Total emoluments 2012 £'000 | **Pension contributions 2013 £'000** | Pension contributions 2012 £'000 |
|---|---|---|---|---|---|---|
| Executive | | | | | | |
| N G Bowland | **117** | **14** | **131** | 131 | **9** | 10 |
| M R Thornton[1] | **81** | **10** | **91** | 56 | **7** | 4 |
| Non-executive | | | | | | |
| D B Liversidge CBE[2] | **40** | **—** | **40** | 36 | **—** | — |
| C Glass[3] | **30** | **—** | **30** | 27 | **—** | — |
| R Simkins[4] | **30** | **—** | **30** | 27 | **—** | — |
| M J McMahon | **30** | **—** | **30** | 27 | **—** | — |
| Total | **328** | **24** | **352** | 304 | **16** | 14 |

1. M R Thornton was appointed as a Director in the prior year on 23 May 2012.
2. D B Liversidge's fees are partly paid to Quest Investments Limited, a company of which he is a director.
3. C Glass' fees are paid to Winburn Glass Norfolk, a firm of which he is a partner.
4. 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 2013 a loan of £12,166 (2012: £12,166) made available to N G Bowland in 2009 was still repayable. Also at 31 December 2013, £17,478 and £9,800 was owed by N G Bowland and M J McMahon for taxes arising in connection with share option exercises made in prior years.

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 2013 | Exercised during the year | Granted during the year | **At 31 December 2013** | Option price | Date granted |
|---|---|---|---|---|---|---|
| D B Liversidge CBE | 1,500,000 | — | — | **1,500,000** | 1.70p | November 2007[1] |
| | 400,000 | — | — | **400,000** | 1.70p | November 2009[1] |
| N G Bowland | 900,000 | (140,000) | — | **760,000** | 1.50p | January 2009[1,3] |
| | 2,500,000 | — | — | **2,500,000** | 9.00p | June 2012[2] |
| C Glass | 1,500,000 | — | — | **1,500,000** | 1.70p | November 2007[1] |
| | 1,000,000 | — | — | **1,000,000** | 1.50p | January 2009[1] |
| | 400,000 | — | — | **400,000** | 1.70p | November 2009[1] |
| M J McMahon | 400,000 | — | — | **400,000** | 1.70p | November 2009[1] |
| M R Thornton | 2,500,000 | — | — | **2,500,000** | 1.00p | June 2012[2] |

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 7p.

The gain on exercise of share options during the year (calculated based on the market price at exercise) was £7,700 for N G Bowland. The market price of the Company's shares at the end of the financial year was 6.00p (2012: 7.25p) and the range of market prices during the year was between 4.4p (2012: 6.4p) and 7.8p (2012: 12.4p).

On behalf of the Board

**D B Liversidge CBE**
Chairman
14 April 2014

# 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.

## 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, 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

The Directors have prepared forecasts for the period to December 2015 which assess the ability of the Group to remain compliant with current banking facilities. These facilities comprise a committed £3 million revolving credit facility and hire purchase liabilities. The commitment of the revolving credit facility is subject to compliance with financial covenants which measure profitability and debt service with measurement starting quarterly from June 2014 and September 2014 respectively.

Based on the forecasts, the Board has a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. The Board has also 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
14 April 2014

## 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 |

# 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 2013 which comprise the Consolidated statement of comprehensive income, the Consolidated statement of changes in equity, the Consolidated balance sheet, the Consolidated cash flow statement 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 Directors' responsibilities statement set out on page 23, 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 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 Financial Reporting Council'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 2013 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 Strategic report and the Directors' report 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:

Under the Companies Act 2006 we are required 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 2013.

**Paul Houghton**
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
Leeds
14 April 2014

# Consolidated statement of comprehensive income

## for the year ended 31 December 2013

| | Notes | 2013 £'000 | 2012 £'000 |
|---|---|---|---|
| Revenue | 2 | **8,553** | 7,639 |
| Cost of sales | | **(4,763)** | (3,779) |
| Gross profit | | **3,790** | 3,860 |
| Other operating expenses | | **(2,905)** | (2,537) |
| Adjusted EBITDA* | | **2,514** | 2,888 |
| Exceptional items | 3 | **(196)** | (294) |
| Amortisation of intangible assets | 10 | **(906)** | (700) |
| Depreciation of tangible assets | 9 | **(527)** | (571) |
| Operating profit | 3 | **885** | 1,323 |
| Finance costs | 5 | **(119)** | (94) |
| Finance income | 6 | **30** | 4 |
| Profit before taxation | | **796** | 1,233 |
| Taxation credit/(charge) | 7 | **4** | (547) |
| Profit and total comprehensive income for the period attributable to the owners of the parent | | **800** | 686 |
| Earnings per share, total and continuing | | | |
| Basic | 8 | **0.20p** | 0.17p |
| Diluted | 8 | **0.20p** | 0.17p |

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

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

# Consolidated statement of changes in equity
## for the year ended 31 December 2013

| | Share capital £'000 | Share premium £'000 | Capital reserve £'000 | Retained earnings £'000 | Total £'000 |
|---|---|---|---|---|---|
| Balance as at 1 January 2012 | 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** |
| *Employee share-based payment options* | *—* | *—* | *—* | *150* | *150* |
| *Exercise of share options* | *1* | *1* | *—* | *—* | *2* |
| Total – transactions with owners | 1 | 1 | — | 150 | 152 |
| Profit and total comprehensive income for the period | — | — | — | 800 | 800 |
| **Balance as at 31 December 2013** | **4,047** | **326** | **329** | **9,813** | **14,515** |

# Consolidated balance sheet
## at 31 December 2013

| | Notes | 2013 £'000 | 2012 £'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 9 | **2,788** | 2,990 |
| Intangible assets | 10 | **7,341** | 6,393 |
| Trade receivables | 12 | **2,124** | 637 |
| | | **12,253** | 10,020 |
| **Current assets** | | | |
| Inventories | 11 | **3,120** | 3,605 |
| Trade receivables | 12 | **4,464** | 3,953 |
| Other current assets | 12 | **810** | 679 |
| | | **8,394** | 8,237 |
| **Total assets** | | **20,647** | 18,257 |
| **Equity and liabilities** | | | |
| **Equity attributable to equity holders of the parent company** | | | |
| Share capital | 14 | **4,047** | 4,046 |
| Share premium account | 15 | **326** | 325 |
| Capital reserve | | **329** | 329 |
| Retained earnings | | **9,813** | 8,863 |
| **Total equity** | | **14,515** | 13,563 |
| **Non-current liabilities** | | | |
| Obligations under finance leases | 13 | **505** | 786 |
| Deferred income – government grant | | **100** | — |
| Deferred tax liabilities | 6 | **562** | 369 |
| | | **1,167** | 1,155 |
| **Current liabilities** | | | |
| Bank overdraft | | **2,584** | 1,419 |
| Trade and other payables | | **1,605** | 1,475 |
| Obligations under finance leases | 13 | **399** | 422 |
| Accruals | | **377** | 223 |
| | | **4,965** | 3,539 |
| **Total liabilities** | | **6,132** | 4,694 |
| **Total equity and liabilities** | | **20,647** | 18,257 |

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

The financial statements on pages 28 to 50 were approved by the Board of Directors on 14 April 2014 and were signed on its behalf by:

**D B Liversidge CBE**
Director
Company registered number: 2298163

# Consolidated cash flow statement

## for the year ended 31 December 2013

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Operating profit | **885** | 1,323 |
| Adjustments for: | | |
| Depreciation of property, plant and equipment | **527** | 571 |
| Amortisation of intangible assets | **906** | 700 |
| Share-based payment charge | **150** | 68 |
| Grant income | **(20)** | — |
| Loss on disposal of fixed assets | **1** | — |
| **Operating cash flows before movement in working capital** | **2,449** | 2,662 |
| Decrease/(increase) in inventories | **485** | (747) |
| Increase in non-current trade receivables | **(1,457)** | (637) |
| Increase in current receivables | **(590)** | (523) |
| Increase/(decrease) in payables | **284** | (49) |
| **Cash generated from operations** | **1,171** | 706 |
| Taxation received | **216** | — |
| Interest paid | **(119)** | (94) |
| **Net cash generated from operating activities** | **1,268** | 612 |
| **Cash flows from investing activities** | | |
| Interest received | **—** | 4 |
| Payments to acquire property, plant and equipment | **(189)** | (133) |
| Acquisition of intangible assets | **(1,854)** | (1,850) |
| **Net cash used in investment activities** | **(2,043)** | (1,979) |
| **Cash flows from financing activities** | | |
| Cash received from issue of shares | **2** | 193 |
| Cash received from government grant | **49** | — |
| Repayment of obligations under finance leases | **(441)** | (445) |
| **Net cash used in financing activities** | **(390)** | (252) |
| **Net decrease in cash and cash equivalents** | **(1,165)** | (1,619) |
| (Net debt)/cash and cash equivalents at beginning of period | **(1,419)** | 200 |
| **Net debt at end of period – bank overdraft** | **(2,584)** | (1,419) |

# 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 26.

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 2013, the following standards were in issue but not yet effective:

- IFRS 10 Consolidated Financial Statements (EU effective date 1 January 2014);
- IFRS 11 Joint Arrangements (EU effective date 1 January 2014);
- IFRS 12 Disclosure of Interests in Other Entities (EU effective date 1 January 2014);
- IAS 27 (Revised) Separate Financial Statements (EU effective date 1 January 2014);
- IAS 28 (Revised) Investments in Associates and Joint Ventures (EU effective date 1 January 2014);
- Transition Guidance – Amendments to IFRS 10, IFRS 11 and IFRS 12 (EU effective date 1 January 2014);
- Investment Entities – Amendments to IFRS 10, IFRS 12 and IAS 27 (effective 1 January 2014);
- Offsetting Financial Assets and Financial Liabilities – Amendments to IAS 32 (effective 1 January 2014);
- Recoverable Amount Disclosures for Non-Financial Assets (Amendments to IAS 36) (effective 1 January 2014); and
- Novation of Derivatives and Continuation of Hedge Accounting (Amendments to IAS 39) (effective 1 January 2014).

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.

### (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.

# Notes to the consolidated financial statements
continued

## 1. Group accounting policies under IFRS continued

### (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 against 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 7.

## 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 Group's 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 reusable 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 hours performed on the contract to the overall estimated hours 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.

# 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 2013 total £7,341,000 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 2013, £14.9 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 (o) 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 has 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 2013 the Directors assessed 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 2013, the recorded inventory provision of £484,000 represented 14% 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 12, the top five customers in trade receivables totalled £3,449,000 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.

# Notes to the consolidated financial statements
continued

## 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 2013 | SI Brand £'000 | OEM £'000 | Industrial £'000 | Total £'000 |
|---|---|---|---|---|
| Revenue | 6,500 | 1,757 | 296 | 8,553 |
| Result | | | | |
| Segment result | 2,229 | 395 | 260 | 2,884 |
| Unallocated expenses | | | | (1,999) |
| Profit from operations | | | | 885 |
| Finance income | | | | 30 |
| Finance costs | | | | (119) |
| Profit before taxation | | | | 796 |
| Tax credit | | | | 4 |
| Profit for the year | | | | 800 |

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

| Year ended 31 December 2013 | SI Brand £'000 | OEM £'000 | Industrial £'000 | Total £'000 |
|---|---|---|---|---|
| Amortisation of intangible assets | 708 | 196 | 2 | 906 |

Unallocated expenses for 2013 include sales and marketing costs (£643,000), research and development costs (£369,000) and central overheads (£701,000).

| 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 |

## 2. Segmental reporting continued

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 |

Unallocated expenses for 2012 include sales and marketing costs (£441,000), research and development costs (£429,000) and central overheads (£748,000).

### Geographical analysis of revenues

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| United Kingdom | **2,341** | 1,777 |
| Europe | **2,392** | 2,392 |
| US | **2,871** | 2,149 |
| Rest of World | **949** | 1,321 |
| | **8,553** | 7,639 |

Revenues are allocated geographically on the basis of where revenues were received from and not from the ultimate final destination of use. During 2013, £1,290,000 (15%) and £1,277,000 (15%) of the Group's revenue depended on two customers in the SI Brand segment (2012: £843,000 (11%) one customer within the SI Brand segment). No other single customer accounted for more than 10% of the Group's revenue in either year. Revenues to Europe included £710,000 (2012: £318,000) to Belgium and £697,000 (2012: £704,000) to France.

## 3. Operating profit

The profit for the year is stated after charging:

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Depreciation of owned assets | **268** | 313 |
| Depreciation of assets held under finance lease | **259** | 258 |
| Amortisation of capitalised development costs | **906** | 700 |
| Research and development costs – Concept team | **369** | 429 |
| Foreign exchange losses | **36** | 38 |
| Auditor's remuneration: | | |
| – fees payable to the Company's auditor for the audit of the Company's annual financial statements | **8** | 8 |
| – fees payable to the Company's auditor for the audit of the subsidiary undertakings | **19** | 18 |
| Operating lease rentals: | | |
| – land and buildings | **138** | 138 |
| Exceptional items | **196** | 294 |

The amortisation of capitalised development costs are accounted for within other operating expenses within the Consolidated statement of comprehensive income. Exceptional items of £196,000 relate to the settlement of old PAYE liabilities arising in connection with share option schemes operated by the Group. Prior year exceptional items of £294,000 comprise restructuring costs incurred during the first half of 2012.

# Notes to the consolidated financial statements
continued

## 4. Employees

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

| | 2013 Number | 2012 Number |
|---|---|---|
| Directors | **2** | 2 |
| Production | **54** | 60 |
| Development | **21** | 28 |
| Administration | **16** | 17 |
| | **93** | 107 |

The costs incurred in respect of these employees were:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Wages and salaries | **2,224** | 2,400 |
| Social security costs | **203** | 226 |
| Pension costs | **47** | 55 |
| | **2,474** | 2,681 |

A detailed analysis of Directors' emoluments is shown in the table on page 24.

Key management including Non-executive Directors:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Salaries | **431** | 416 |
| Social security costs | **43** | 42 |
| Pension costs | **23** | 14 |
| Share-based payments | **97** | 52 |
| Total | **594** | 524 |

## 5. Finance costs

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| On finance leases | **62** | 63 |
| On bank overdrafts | **57** | 31 |
| | **119** | 94 |

## 6. Finance income

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Unwinding of discount on non-current trade receivables | **30** | — |
| | **30** | — |

## 7. Taxation

### Tax on profit

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Current tax credit | **(197)** | (287) |
| Deferred tax charge | **193** | 834 |
| Total tax (credit)/charge | **(4)** | 547 |

## 7. Taxation continued

### 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 23.25% (2012: 24.50%). The differences are explained as follows:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Profit on ordinary activities before taxation | **796** | 1,233 |
| Corporation Tax at standard rate of 23.25% (2012: 24.50%) | **185** | 302 |
| Effects of: | | |
| Net impact of research and development enhanced expenditure | **(653)** | 78 |
| Expenses not tax deductible | **146** | 168 |
| Movement on intangible assets | **260** | (319) |
| Deductions on exercise of share options | **33** | (193) |
| Utilisation and recognition of trading losses | **25** | 511 |
| Total tax charge for the year | **(4)** | 547 |

### Deferred taxation

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

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Balance brought forward – (liability)/asset | **(369)** | 465 |
| Consolidated statement of comprehensive income movement arising during the year | **(193)** | (834) |
| Balance carried forward – liability | **(562)** | (369) |

The deferred taxation recognised in the financial statements at 20% (2012: 23%) is set out below:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Trade losses | **648** | 821 |
| Fixed asset timing differences | **(1,210)** | (1,190) |
| | **(562)** | (369) |

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:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Deferred tax assets | **2,971** | 3,450 |
| Deferred tax liabilities | **—** | — |
| Net unrecognised deferred tax assets | **2,971** | 3,450 |

At the balance sheet date, the Group has unused tax losses of £18.1 million (2012: £18.6 million) available for offset against certain future profits. A deferred tax asset of £640,000 (2012: £821,000) has been recognised in respect of such losses. No deferred tax asset has been recognised in respect of the remaining £14.9 million (2012: £15.0 million) due to the anticipated lack of availability of suitable future trading profits.

## 8. Earnings per ordinary share

### Basic earnings per ordinary share

The calculation of basic earnings per ordinary share for the year ended 31 December 2013 was based upon the profit attributable to ordinary shareholders of £800,000 (2012: £686,000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2013 of 404,591,902 (2012: 402,200,875).

# Notes to the consolidated financial statements
continued

## 8. Earnings per ordinary share continued

### Diluted earnings per ordinary share

The calculation of diluted earnings per ordinary share for the year ended 31 December 2013 was based upon the profit attributable to ordinary shareholders of £800,000 (2012: £686,000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2013 of 409,062,516 (2012: 415,283,787).

### Adjusted earnings per ordinary share

The calculation of adjusted earnings per ordinary share for the year ended 31 December 2013 was based upon the adjusted profit attributable to ordinary shareholders of £996,000 (2012: £1,421,000) and a weighted average number of ordinary shares outstanding for the year ended 31 December 2013 of 404,591,902 (2012: 402,200,875).

| Earnings and adjusted earnings | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Earnings for the purpose of basic and diluted earnings per ordinary share | **800** | 686 |
| Exceptional items | **196** | 294 |
| Deferred tax adjustment | **—** | 441 |
| Earnings for the purpose of adjusted earnings per ordinary share | **996** | 1,421 |

| Number of shares used in calculation of earnings per ordinary share ('000s) | **2013 No. of shares** | 2012 No. of shares |
|---|---|---|
| Basic earnings per share | **404,592** | 402,201 |
| Dilutive effect of unexercised share options | **4,471** | 13,083 |
| Diluted earnings per share | **409,063** | 415,284 |

## 9. Property, plant and equipment

| | Tooling £'000 | Plant and machinery £'000 | Office and computer equipment £'000 | Placed equipment £'000 | Improvements to leasehold property £'000 | Assets under construction £'000 | Total £'000 |
|---|---|---|---|---|---|---|---|
| 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 |
| Gross carrying amount 31 December 2013 | 1,241 | 3,487 | 928 | 380 | 366 | 90 | 6,492 |
| Accumulated depreciation and impairment | (847) | (1,501) | (842) | (315) | (199) | — | (3,704) |
| **Carrying amount 31 December 2013** | **394** | **1,986** | **86** | **65** | **167** | **90** | **2,788** |

| | Tooling £'000 | Plant and machinery £'000 | Office and computer equipment £'000 | Placed equipment £'000 | Improvements to leasehold property £'000 | Assets under construction £'000 | Total £'000 |
|---|---|---|---|---|---|---|---|
| Carrying amount 1 January 2012 | 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 |
| Additions – separately acquired | 84 | 95 | 32 | 25 | — | 90 | 326 |
| Depreciation | (67) | (312) | (59) | (60) | (29) | — | (527) |
| Loss on disposal | — | — | (1) | — | — | — | (1) |
| **Carrying amount 31 December 2013** | **394** | **1,986** | **86** | **65** | **167** | **90** | **2,788** |

## 9. 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:

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Plant and machinery | | |
| Net book value | **1,826** | 1,921 |
| Depreciation charge for the year | **259** | 258 |

### Security

At 31 December 2013, the assets of the Group were subject to a fixed and floating charge debenture in favour of the Group's banking facilities.

## 10. Intangible assets

| | Capitalised development costs 2013 £'000 |
|---|---|
| Cost | |
| At 1 January 2012 | 6,482 |
| Additions | 1,850 |
| At 1 January 2013 | 8,332 |
| Additions | 1,854 |
| At 31 December 2013 | **10,186** |
| Accumulated amortisation | |
| At 1 January 2012 | 1,239 |
| Charge for the year | 700 |
| At 1 January 2013 | 1,939 |
| Charge for the year | 906 |
| At 31 December 2013 | **2,845** |
| Carrying amount | |
| At 31 December 2013 | **7,341** |
| At 31 December 2012 | 6,393 |
| At 31 December 2011 | 5,243 |

The £10,186,000 (2012: £8,332,000) 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 shown in notes 1(e) and 1(f) on page 33.

# Notes to the consolidated financial statements
continued

## 11. Inventories

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Raw materials | **1,873** | 1,971 |
| Finished goods | **1,247** | 1,634 |
| | **3,120** | 3,605 |

Included in the analysis above are impairment provisions against inventory amounting to £260,000 (2012: £133,000).

In 2013 a total of £4,682,000 of inventories was included in profit and loss as an expense within cost of sales (2012: £3,743,000). Cost of sales included an amount of £152,000 resulting from the write down of inventories (2012: £204,000).

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 or market trends. Consequently, management considers that there is little risk of significant adjustments to the Group's inventory assets within the next financial year.

## 12. Trade and other receivables

| Falling due in less than one year | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Trade receivables | **4,464** | 3,953 |
| Prepayments and accrued income | **321** | 229 |
| Corporation Tax recoverable | **268** | 287 |
| Other debtors | **221** | 163 |
| | **5,274** | 4,632 |

| Falling due in more than one year | | |
|---|---|---|
| Trade receivables | **2,124** | 637 |

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

Of the current and non-current trade receivables, £3,449,000 relates to five customers (2012: £1,976,000).

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 £14,000 (2012: £10,000) was recorded.

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:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Not more than three months | **427** | 306 |
| More than three months but not more than six months | **121** | 15 |
| More than six months but not more than one year | **110** | — |
| More than one year | **12** | — |

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.

## 13. 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:

| | **2013 €'000** | 2012 €'000 | **2013 $'000** | 2012 $'000 |
|---|---|---|---|---|
| Financial assets | **962** | 988 | **2,661** | 1,606 |
| Financial liabilities | **(56)** | (100) | **(9)** | (22) |
| Short-term exposure | **906** | 888 | **2,652** | 1,584 |

At 31 December 2013, the Group has long-term foreign exchange assets denominated in Dollars of $1,040,000 (2012: $327,000) represented by trade receivables. The Group has no other long-term foreign exchange assets or liabilities (2012: £nil).

The Group has significant exposure to the Euro and Dollar at 31 December 2013. 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 £37,000 (2012: £36,000) against the Euro and £85,000 (2012: £49,000) against the Dollar.

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

### 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:

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Trade and other receivables | **7,077** | 5,040 |
| | **7,077** | 5,040 |

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 12.

# Notes to the consolidated financial statements
continued

## 13. Financial instruments continued

### 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 2013, the Group continued to have access to sufficient funds to meet its business expansion needs and in April 2014 the Group entered into a committed three-year revolving credit facility with Yorkshire Bank. The commitment of the revolving credit facility is subject to compliance with financial covenants which measure profitability and debt service with measurement starting quarterly from June 2014 and September 2014 respectively.

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

| | **Current** | | **Non-current** |
|---|---|---|---|
| **31 December 2013** | **Within 6 months £'000** | **Within 6–12 months £'000** | **Over 12 months £'000** |
| Finance lease obligations | **210** | **189** | **505** |
| Trade and other payables | **1,605** | **—** | **—** |
| Bank overdraft | **2,584** | **—** | **—** |
| | **4,399** | **189** | **505** |

| | 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 |

### Maturity profile of borrowings

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Gross lease payments not later than one year | **452** | 483 |
| Later than one year but not more than five years | **565** | 883 |
| Future finance charges | **(113)** | (159) |

## 13. Financial instruments continued

### Summary of financial assets and liabilities by category

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| **Loans and receivables** | | |
| Trade and other receivables | **7,077** | 5,040 |
| | **7,077** | 5,040 |

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| **Current liabilities** | | |
| Trade payables: financial liabilities measured at amortised cost | **1,605** | 1,475 |
| Other short-term financial liabilities measured at amortised cost | **2,983** | 1,841 |
| | **4,588** | 3,316 |
| **Net financial assets and liabilities** | **2,665** | 1,724 |

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:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Total borrowings | **3,488** | 2,627 |
| Less: cash and cash equivalents | **—** | — |
| Net debt | **3,488** | 2,627 |
| Total equity | **14,515** | 13,563 |
| Total capital | **18,003** | 16,190 |

### 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.

# Notes to the consolidated financial statements
continued

## 14. Share capital

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Authorised 600,000,000 (2012: 600,000,000) ordinary shares of 1p each | **6,000** | 6,000 |
| Allotted, called up and fully paid 404,731,902 (2012: 404,591,902) ordinary shares of 1p each | **4,047** | 4,046 |

At 31 December 2013, the following share options were outstanding:

| | Number of shares | | | | | | Exercise dates | |
|---|---|---|---|---|---|---|---|---|
| Scheme and date of grant | At 1 January 2013 | Exercised during year | Granted during year | Lapsed during year | **At 31 December 2013** | 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** | 1.7p | November 2009 | November 2017 |
| January 2009 | 1,000,000 | — | — | — | **1,000,000** | 1.5p | November 2009 | January 2019 |
| November 2009 | 1,200,000 | — | — | — | **1,200,000** | 1.7p | November 2009 | November 2019 |
| **Enterprise management** | | | | | | | | |
| June 2012 | 2,500,000 | — | — | — | **2,500,000** | 1.0p | June 2015 | June 2022 |
| June 2012 | 1,860,000 | — | — | (280,000) | **1,580,000** | 7.2p | June 2015 | June 2022 |
| June 2012 | 4,390,000 | — | — | (300,000) | **4,090,000** | 9.0p | June 2015 | June 2022 |
| June 2013 | — | — | 3,150,000 | — | **3,150,000** | 5.1p | June 2016 | June 2023 |
| **Executive unapproved** | | | | | | | | |
| January 2009 | 900,000 | (140,000) | — | — | **760,000** | 1.5p | November 2009 | January 2019 |
| **Other option awards** | | | | | | | | |
| January 2013 | — | — | 4,999,998 | — | **4,999,998** | 6.9p | January 2018 | January 2023 |
| June 2013 | — | — | 1,000,000 | — | **1,000,000** | 5.1p | June 2016 | June 2023 |

### Share-based payments

Share options were granted during 2013 to certain employees, distributors and members of the Clinical Advisory Board. The exercise price of the granted options is equal to market price at grant. For employees, options are conditional upon completing a three-year service period from the date of grant. For distributors and members of the Clinical Advisory Board, options are conditional on the completion of appropriate objectives.

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

| | **2013** | | 2012 | |
|---|---|---|---|---|
| | **Average exercise price pence** | **Options '000s** | Average exercise price pence | Options '000s |
| At 1 January | **4.4** | **14,850** | 1.9 | 15,489 |
| Exercised | **1.5** | **(140)** | 2.1 | (9,389) |
| Granted | **6.1** | **9,150** | 6.4 | 9,030 |
| Lapsed | **8.1** | **(580)** | 7.8 | (280) |
| At 31 December | **5.0** | **23,280** | 4.4 | 14,850 |

## 14. Share capital continued

### Share-based payments continued

Out of the 23,279,998 options (2012: 14,850,000), 5,960,000 (2012: 6,100,000) options were exercisable at an average exercise price of 5.0p (2012: 4.4p). Options exercised in 2013 resulted in 140,000 (2012: 9,389,000) shares being issued at a weighted average exercise price of 1.5p (2012: 2.1p). The related average weighted share price at the date of exercise was 7.0p (2012: 11.3p).

The weighted average fair value of options granted during the period determined using the Black-Scholes valuation model was 2.15p per option (2012: 4.50p). 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 five 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 £150,000 (2012: £68,000).

## 15. Share premium

| | Share premium £'000 |
|---|---|
| Balance as at 31 December 2012 | 325 |
| Issue of ordinary share capital | 1 |
| **Balance as at 31 December 2013** | **326** |

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

## 16. Contingent liabilities and financial commitments

These are as follows:

### (a) Contingent liabilities

There were no contingent liabilities at 31 December 2013 (2012: £nil).

### (b) Operating leases

At 31 December 2013 the Group had future aggregate minimum lease payments under non-cancellable operating leases as follows:

| | **2013 £'000** | 2012 £'000 |
|---|---|---|
| Within one year | **224** | 219 |
| One to five years | **575** | 655 |
| Over five years | **—** | 50 |

### (c) Capital commitments

At 31 December 2013 the Group had capital commitments totalling £nil (2012: £69,000).

# Notes to the consolidated financial statements
continued

## 17. 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 2013 £'000** | **Amounts payable/ (receivable) 31 December 2013 £'000** | Amounts invoiced to/(by) the Group 2012 £'000 | Amounts payable/ (receivable) 31 December 2012 £'000 |
|---|---|---|---|---|
| Quest Investments Limited[1] | **39** | **12** | 29 | 10 |
| Winburn Glass Norfolk[2] | **30** | **9** | 25 | 9 |
| Getz Bros. & Co. Inc.[3] | **30** | **30** | 20 | — |
| ACP[4] | **(239)** | **(135)** | (205) | (358) |

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. ACP acts as the master distributor for Surgical Innovations in the Far East. During the year Surgical Innovations invoiced ACP £239,000 for products and at 31 December 2013 there was an amount owing to Surgical Innovations of £135,000. Getz Bros. & Co. Inc. is the ultimate beneficial owner of ACP.
5. Details of loans to Directors are disclosed in the Remuneration report on page 24.

There is no controlling party of Surgical Innovations Group plc.

## 18. Pensions

The Company currently operates a defined contribution Group personal pension plan for the benefit of employees. Company contributions in 2013 were £47,000 (2012: £41,000).

# 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 2013 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 Directors' responsibilities statement set out on page 23, 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 Financial Reporting Council'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 2013;
- 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 Strategic report and the Directors' report 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 2013.

**Paul Houghton**
Senior Statutory Auditor
for and on behalf of Grant Thornton UK LLP
Statutory Auditor, Chartered Accountants
Leeds
14 April 2014

# Company balance sheet
## at 31 December 2013

| | Notes | 2013 £'000 | 2013 £'000 | 2012 £'000 | 2012 £'000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| Investments | 2 | | **1,018** | | 1,018 |
| **Current assets** | | | | | |
| Debtors | 3 | **6,054** | | 2,993 | |
| Cash at bank | | **119** | | 3,305 | |
| | | **6,173** | | 6,298 | |
| **Creditors:** amounts falling due within one year | 4 | **(526)** | | (320) | |
| **Net current assets** | | | **5,647** | | 5,978 |
| **Net assets** | | | **6,665** | | 6,996 |
| **Capital and reserves** | | | | | |
| Called up share capital | 5 | | **4,047** | | 4,046 |
| Share premium account | 6 | **326** | | 325 | |
| Profit and loss account | 6 | **2,292** | | 2,625 | |
| | | | **2,618** | | 2,950 |
| **Shareholders' funds** | 7 | | **6,665** | | 6,996 |

The financial statements on pages 52 to 55 were approved by the Board of Directors on 14 April 2014 and were signed on its behalf by:

**D B Liversidge CBE**
Director
Company registered number: 2298163

# 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<br>At 31 December 2013 and 1 January 2013 | **1,018** |
| Provision for diminution in value<br>At 31 December 2013 and 1 January 2013 | **—** |
| Net book value at 31 December 2013 and 1 January 2013 | **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

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Prepayments and accrued income | **2** | 17 |
| Other debtors | **94** | 70 |
| Amounts due from subsidiary undertakings | **5,958** | 2,906 |
| | **6,054** | 2,993 |

## 4. Creditors: amounts falling due within one year

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Accruals and deferred income | **126** | 100 |
| Other creditors | **400** | 220 |
| | **526** | 320 |

# Notes to the Company financial statements
continued

## 5. Share capital

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Authorised 600,000,000 (2012: 600,000,000) ordinary shares of 1p each | **6,000** | 6,000 |
| Allotted, called up and fully paid 404,731,902 (2012: 404,591,902) ordinary shares of 1p each | **4,047** | 4,046 |

Details of the share options are contained in note 14 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:

- 140,000 at 1.5p.

A total of 140,000 (2012: 9,389,000) ordinary shares with a total nominal value of £1,400 (2012: £93,890) were issued for consideration amounting to £2,100 (2012: £193,000).

## 6. Reserves

| | Share premium £'000 | Accumulated profits/ (losses) £'000 |
|---|---|---|
| At 1 January 2013 | 325 | 2,625 |
| Premium on shares issued | 1 | — |
| Loss for the year | — | (483) |
| Employee share-based payments | — | 150 |
| At 31 December 2013 | **326** | **2,292** |

## 7. Reconciliation of movements in shareholders' funds

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Loss for the financial year | **(483)** | (218) |
| Issue of shares | **2** | 193 |
| Employee share-based payments | **150** | 68 |
| Net (reduction)/increase in shareholders' funds | **(331)** | 43 |
| Opening shareholders' funds | **6,996** | 6,953 |
| Closing shareholders' funds | **6,665** | 6,996 |

## 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 £483,000 (2012: £218,000).

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 2013 £'000** | **Amounts payable 31 December 2013 £'000** | Amounts invoiced to the Company 2012 £'000 | Amounts payable 31 December 2012 £'000 |
|---|---|---|---|---|
| Quest Investments Limited[1] | **39** | **12** | 29 | 10 |
| Winburn Glass Norfolk[2] | **30** | **9** | 25 | 9 |
| Getz Bros. & Co. Inc.[3] | **30** | **30** | 20 | — |

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. Details of loans to Directors are disclosed in the Remuneration report on page 24.

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

# Five-year summary

| | 2013 £'000 | 2012 £'000 | 2011 £'000 | 2010 £'000 | 2009 £'000 |
|---|---|---|---|---|---|
| Revenue | **8,553** | 7,639 | 7,602 | 7,045 | 4,541 |
| Cost of sales | **(4,763)** | (3,779) | (4,005) | (3,526) | (2,647) |
| Gross profit | **3,790** | 3,860 | 3,597 | 3,519 | 1,894 |
| Other operating expenses | **(2,905)** | (2,537) | (1,830) | (1,940) | (1,603) |
| Adjusted EBITDA | **2,514** | 2,888 | 2,825 | 2,545 | 937 |
| Exceptional items | **(196)** | (294) | — | — | (200) |
| Amortisation | **(906)** | (700) | (550) | (518) | (101) |
| Depreciation | **(527)** | (571) | (508) | (448) | (345) |
| Operating profit | **885** | 1,323 | 1,767 | 1,579 | 291 |
| Finance income | **30** | 4 | 11 | 9 | 13 |
| Finance costs | **(119)** | (94) | (73) | (39) | (40) |
| Profit before taxation | **796** | 1,233 | 1,705 | 1,549 | 264 |
| Taxation | **4** | (547) | 33 | 239 | 261 |
| Retained profit for the year | **800** | 686 | 1,738 | 1,788 | 525 |
| Earnings per ordinary share (basic) | **0.20p** | 0.17p | 0.44p | 0.48p | 0.14p |
| Earnings per ordinary share (diluted) | **0.20p** | 0.17p | 0.42p | 0.46p | 0.14p |

# 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 24 June 2014 at 2 pm. 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 2013.
2. To re-elect Mr N G Bowland 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.
3. To re-elect Mr R Simkins 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-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.
5. 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 £1,349,106.34 (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 5.

## Special business

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

6. 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:

    6.1. 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

    6.2. the allotment (otherwise than pursuant to sub-paragraph 6.1 above) of equity securities up to an aggregate nominal amount of £404,731.90 (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.

By order of the Board

**M R Thornton**
Company Secretary
14 April 2014

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

# Notice of Annual General Meeting
continued

## 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 20 June 2014 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 20 June 2014 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 Asset Services, at PXS, 34, Beckenham Road, Beckenham, Kent BR3 4ZF not later than 2.00pm on 20 June 2014.

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.

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 Asset Services at PXS, 34 Beckenham Road, Beckenham, Kent BR3 4ZF.

   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 Asset Services. 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 Asset Services at PXS, 34 Beckenham Road, Beckenham, Kent BR3 4ZF no later than 2.00pm on 20 June 2014. 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.

## Notes continued

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 15 April 2014 (being the last practicable business day prior to the publication of this notice) the Company's issued share capital consisted of 404,731,902 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 is 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.

# 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 5 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 6 is proposed as a special resolution. This means that for this resolution 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 2013 to the Meeting as required by law.

## Resolutions 2 and 3 – 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. Graham Bowland and Ray Simkins retire by rotation and are offering themselves for re-election.

## Resolution 4 – 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 re-appointment and, in accordance with standard practice, authorises the Directors to determine the level of the auditor's remuneration.

## Resolution 5 – Authority to allot shares

The resolution grants the Directors authority to allot relevant securities up to an aggregate nominal amount of 1,349,106.34, being approximately one-third of the Company's ordinary share capital in issue at 15 April 2014. 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 6 – 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 £404,731.90, being 10% of the Company's ordinary share capital in issue at 15 April 2014. This replaces the existing authority to disapply pre-emption rights and expires at the conclusion of the next Annual General Meeting of the Company.

THE QUEEN'S AWARDS
FOR ENTERPRISE:
INNOVATION
2010

Surgical Innovations Group Plc

**Surgical Innovations Group plc**
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