



FUTURA
M E D I C A L

ANNUAL REPORT
2005

Company Profile

Futura Medical plc ("Futura") is a pharmaceutical drug and medical device group that develops innovative products for sexual health. Our products under development are focused on the sexual wellbeing of healthy men and women and the treatment of sexual dysfunction. Our primary focus is on non-prescription products with particular appeal to men and women who are reluctant to discuss potentially embarrassing sexual matters with their doctors. A summary of our main products under development is set out below.

CSD500 – Condom Safety Device

CSD500 will be a condom to be used by healthy men. It incorporates an erectogenic compound in the tip of the condom to help maintain a full erection throughout intercourse in order to reduce condom slippage. The gel is to be licensed under the trademark Zanifil™.

Market research has identified that 22 per cent of healthy men have experienced a partial loss of penile rigidity before or during intercourse as a result of wearing a condom. This not only discourages the use of condoms but also increases the risk of the condom slipping completely off the penis during intercourse.

It has been estimated that approximately two percent of condoms slip off during intercourse and that global condom usage in 2004 exceeded 14 billion. This implies that incidences of "slippage" may occur up to 280 million times a year, with the resultant risk of both unwanted pregnancies and the transference of sexually transmitted infections. The Directors believe that by making condom use more acceptable CSD500 will considerably extend the market as well as reduce the risk of condom slippage.

Discussions with EU regulatory authorities have confirmed that the product will be classified within the EU as a Class III medical device with an ancillary medicinal substance. This classification will allow the product to be sold throughout Europe in the same way as conventional condoms.

Futura has a global distribution agreement for CSD500 with the world's largest branded condom manufacturer and distributor, SSL International plc ("SSL" - makers of the Durex™ condom range) for the lifetime of the patents.

On 28 November 2005, the regulatory dossier for CSD500 was submitted to the relevant Notified Body and Competent Authority seeking marketing authorisation in the European Union.

FLD500 – Female Lubrication Device

FLD500 is a "sister" product to CSD500. However, the erectogenic compound will be applied to the outside of a condom, thereby coming into direct contact with the vagina during sexual intercourse.

A survey conducted on behalf of Futura in the UK showed that about 40 per cent of condoms are purchased by women. A further survey conducted amongst women on behalf of Futura showed there was a high level of appeal for FLD500, which was perceived to be a unique product providing a competitive advantage for better and safer sex.

FLD500 is aimed at helping healthy women maintain lubrication during intercourse, reducing the risk of condom failure. The product is intended to be classified within the EU as a Class III medical device with an ancillary medicinal substance.

During sexual penetration a pharmacological dose will be delivered to the clitoral and peri-clitoral regions. This will result in improved local blood flow which in turn should lead to increased vaginal lubrication. By reducing friction during intercourse, this should reduce the risk of condom slippage or breakage. As well as improving safety, the Directors believe this may facilitate an enhanced overall sexual experience for both partners.

Futura also has a global distribution licence for FLD500 with the world's largest branded condom manufacturer and distributor, SSL for the lifetime of the patents.

MED2002* – Male Erectile Dysfunction Treatment

MED2002 will be a 'rub-on' gel applied directly to the penis for the treatment of male erectile dysfunction. The Directors believe this will become the first pharmaceutical treatment for erectile dysfunction which will be available without the need of a doctor's prescription.

It is estimated that 50 per cent of men aged 45 or over have some degree of erectile dysfunction. The British Journal of Urology expects the number of men with erectile dysfunction to double from its current level of 152 million worldwide to 302 million by 2025.

The Futura product is based on glyceryl trinitrate, a potent vasodilator, which has been used for the treatment of angina and associated cardio-vascular defects for more than 40 years and has been determined to be a safe and effective drug with a known side-effect profile.

Futura is in the final stage of formal approval with a major global pharmaceutical group for the worldwide development and commercialisation of MED2002.

Website

More information regarding Futura Medical plc can be found on our website www.futuramedical.co.uk

Notes

*MED2002 describes all Futura's different gel formulations applied directly to the penis for the treatment of male erectile dysfunction. Futura may code certain formulations, for identification purposes, by altering the final digit, e.g. MED2001 or MED2004.

Contents

1	Highlights
2	Chairman and Chief Executive Joint Review
4	Financial Review
5	Directors
6	Directors' Report
8	Remuneration Report
11	Corporate Governance
14	Independent Auditor's Report
15	Consolidated Profit and Loss Account
16	Balance Sheets
17	Consolidated Cash Flow Statement
18	Notes to the Consolidated Cash Flow Statement
19	Notes to the Financial Statements

Futura Medical plc is a pharmaceutical drug and medical device group that develops innovative products for sexual health

Highlights

- **CSD500 – regulatory dossier submitted to the relevant Notified Body and Competent Authority seeking marketing approval within the European Union**
- **FLD500 – Durex™ exercises its option for global distribution and marketing rights**
- **MED2002 – in final stage of formal approval for worldwide development and commercialisation with a major global pharmaceutical group**
- **Pre-tax loss of £2.2 million for year ended 31 December 2005 (year ended 31 December 2004: £1.4 million)**
- **Cash balances of £1.8 million at 31 December 2005 (31 December 2004: £3.7 million)**

Chairman and Chief Executive Joint Review

All too often the announcements we make about achieving intermediate milestones fail to convey the full impact of the progress we have made. It therefore gives us enormous pleasure to advise our shareholders on some major milestones Futura has achieved in the past year.

Product Development

CSD500 – Zanifil™ **Condom safety device**

In April 2005, we announced that satisfactory pilot stability and compatibility results had enabled SSL, the consumer healthcare brands company and manufacturer and distributor of Durex™ the world's biggest-selling branded condom, to commence manufacturing trials and additional stability studies to meet regulatory requirements.

In November 2005, SSL submitted the regulatory dossier for CSD500 to the relevant Notified Body and Competent Authority seeking marketing authorisation in the European Union. The initial response from the Notified Body and Competent Authority has been positive and, in line with expectations, additional information has been requested which is a normal part of the approval process. We anticipate a further response from the Notified Body and Competent Authority during the summer of 2006 and at that point will again update our shareholders. The regulatory approval of CSD500 will be a major milestone achievement for Futura which will lead to our generating revenues from the first of our three key products.

CSD500 will be marketed by our global distribution partner, SSL. CSD500 contains an active compound which will help healthy men maintain an erection during sexual intercourse, thereby helping to reduce condom slippage. Both Futura and SSL believe CSD500 could be an exciting leading product within the Durex™ range that will help to improve the sex lives of Durex™ customers.

FLD500 **Female lubrication device**

We have also made significant progress with FLD500.

In July 2005, SSL exercised its option for the rights to market and distribute FLD500 globally. FLD500 will be marketed as a Durex™ condom targeted at women, who currently purchase 40 per cent of condoms sold within the UK and are therefore an important sector of the market.

In August 2005, we also concluded, following a complete review of all our clinical trials, that we had sufficient clinical data to support a regulatory dossier submission to a Notified Body and Competent Authority seeking marketing authorisation in the European Union thereby avoiding the need of further expensive and time consuming clinical trials.

Although there is considerable technical overlap with CSD500, FLD500 is based on significantly different design resulting in many new technical and manufacturing challenges. Significant progress has been made since the interim statement last September and we expect to make a further announcement shortly to shareholders on this development once the current technical evaluation studies have been completed.

MED2002 – Eroxon™ **Treatment for erectile dysfunction**

We have been in exclusive discussions with a major global pharmaceutical group ("MGPG") on a proposed agreement for the worldwide development and commercialisation of MED2002 for well over 12 months.

During this period, considerable resources have been committed by both parties to the joint development of MED2002. MGPG has conducted work to confirm the optimum regulatory strategy for MED2002 in the key consumer markets and evaluate the size of the market opportunity for MED2002.

In November 2005, we announced the results of our *in vivo* trials on healthy subjects in respect of our revised formulation of MED2002. In the first of the trials, we observed an excellent safety profile with a dose-related occurrence of adverse events which allowed us to define the maximum tolerated dose. The side effects were entirely predictable, being predominantly mild headaches which resolved spontaneously and did not require treatment. No serious side effects were recorded. Further, the absorption profile was consistent with the intended use of the product in treating erectile dysfunction, suggesting a rapid onset of action within a few minutes of product application.

The second of the trials also confirmed an excellent safety profile. In addition, and despite the lack of sexual stimulation, subjects displayed increases in blood flow into the penis which were consistent with those seen during sexual arousal and are an encouraging indicator of the potential efficacy of MED2002 in the treatment of erectile dysfunction.

With these studies completed the agreement of the commercial terms will facilitate a full commitment by both parties to the joint development programme for MED2002. As part of this, the exclusivity period with MGPG has been extended and we are now advised that the formal approval process is in its final stage within MGPG.

Futura expect MED2002 to become the world's first non-prescription pharmaceutical treatment for men with erectile dysfunction. By being available from pharmacies without the need for a doctor's prescription, MED2002 will be aimed at satisfying a large unmet demand from men with erectile dysfunction.

Chairman and Chief Executive Joint Review (*continued*)

Finance

Our overall loss after tax for the year ended 31 December 2005 was £1.9 million. The loss was in line with our expectations and our costs continue to be in line with our internal budgets. Cash at the end of December 2005 was £1.8 million.

Outlook

We believe we are close to having signed agreements for all three products with, in our view, the best possible partners for the products in their respective markets. Moreover we anticipate that no further clinical trials will be required for either of the condom products prior to regulatory approvals.

Futura's management team has been seeking new product opportunities and we expect to update shareholders on our progress following the conclusion of an agreement for MED2002. Nevertheless, our efforts over the past year have been committed to our three key products and will remain so.

Conclusion

The past twelve months have been pivotal for us and the momentum continues to gain pace. Once more we want to thank our incredible small team of hard working professionals who drive Futura forward and hope that our shareholders remain as excited about the future as we are.

Dr W D Potter, Executive Chairman

J H Barder, Chief Executive

Financial Review

The Financial Review should be read in conjunction with the financial statements and the notes to the financial statements set out on pages 15 to 27.

Turnover

The Group's turnover for the year to 31 December 2005 was £1,660 (year ended 31 December 2004: £129,863). This derived from the settlement of an intellectual property dispute in 2004 and the major part of this royalty stream was sold in July 2004 for £125,000.

Losses

The Group retained loss for the year ended 31 December 2005 was £1.9 million (year ended 31 December 2004: £1.2 million). The Group operating loss for the year ended 31 December 2005 was £2.3 million (year ended 31 December 2004: £1.6 million) and the operating loss of the sole subsidiary, Futura Medical Developments Limited, for the year ended 31 December 2005 was £2.2 million (year ended 31 December 2004: £1.5 million).

Losses per share for the year ended 31 December 2005 were 3.9 pence (year ended 31 December 2004: 2.6 pence).

Group research and development costs

The Group continues to focus on balancing the most cost effective and ethical research and development against the commercial applications of such research and development and time to bring products to market.

Research and development costs for the year were £1,535,240 (year ended 31 December 2004: £960,141). The main focus of this expenditure related to significant expansion of development work and clinical trials in respect of MED2002 in anticipation of entering into an agreement with MGPG and studies in respect of CSD500 leading to regulatory dossier submission in November 2005.

Other administrative costs

The Group continues to maintain a focus on tight control of expenditure. Other administrative costs for the year ended 31 December 2005 were £791,004 (year ended 31 December 2004: £745,806). The principal reasons for the increase relate to enhanced investor relations and other professional adviser and service costs arising from our being quoted on the Alternative Investment Market ("AIM"), the addition of one administrative staff member and ongoing licence negotiations.

Taxation

A research and development tax credit of £286,973 (31 December 2004: £170,086) in respect of research and development expenditure incurred is recognised in the financial statements.

Capital structure and funding

At 31 December 2005, the Group had shareholders' funds of £2.0 million (31 December 2004: £3.7 million) including cash balances of £1.8 million (31 December 2004: £3.7 million). The Group did not have any bank borrowings at 31 December 2005 (31 December 2004: £nil).

The Group is principally funded by equity capital. However, it does continue to receive research and development tax credits under the inland revenue scheme and also received a final tranche from the research grant awarded in 2003 from the DTI.

During the year ended 31 December 2005, in addition to turnover the Group's cash inflows included net proceeds from the issue of shares (pursuant to the exercise of share options) of £135,800 (year ended 31 December 2004: £2.6 million from placings and the exercise of warrants), research and development tax credit receipts of £167,858 (year ended 31 December 2004: £108,436) and the final tranche of the research grant from the DTI totalling £11,250 (year ended 31 December 2004: £48,750).

Net cash outflow from operating activities during the year ended 31 December 2005 was £2.3 million (year ended 31 December 2004: £1.6 million).

Treasury and financial risk management policy

It is Group policy not to enter into speculative positions using complex financial instruments. The Group's primary treasury objective is to minimise exposure to potential capital losses whilst at the same time securing favourable market rates of interest on Group cash deposits using money market deposits with banks.

In respect of foreign exchange exposure, the Group primarily enters into supplier contracts which are to be settled in sterling. However, some contracts involve other major world currencies including the US Dollar and the Euro. Where large supplier contracts of more than £100,000 total value are to be settled in foreign currencies, it is operating policy for the sums to be paid through conversion of sterling deposits to the appropriate foreign currency holdings at the outset of the contract to minimise the risk of adverse currency fluctuations. For contracts with smaller values the foreign currency risk is not considered sufficient to require the establishment of foreign currency bank accounts unless specific circumstances are identified which warrant this. Forward and option contracts are not used.

During the year ended 31 December 2005, costs in respect of supplier contracts settled in foreign currencies represented 0.3 per cent of total administrative expenses (year ended 31 December 2004: 2.8 per cent). In addition, the Group was exposed to the US Dollar as a result of holding residual dollar balances (of less than £13,000 throughout the year) and the US dollar account was closed during August 2005.

A L Clayden, Finance Director

Directors



Dr William Duncan Potter, PhD
Executive Chairman (59)

Dr Potter became Chairman in June 2001. He is a member of the Nominations Committee and an adviser to the Remuneration Committee. He provides advice and expertise on product development matters bringing to bear his considerable experience. He has spent 34 years in research and development including 26 years bringing new products to market involving a wide range of medical devices. He has extensive knowledge of world-wide regulatory procedures, intellectual property issues and licensing. Dr Potter previously worked at London International Group, including 7 years as Group Scientific Affairs Director, and at Smith & Nephew plc.



James Henry Barder
Chief Executive (46)

Mr Barder joined the Company as Chief Executive in June 2001. He assists the Remuneration and the Nominations Committees (but is not a member of and does not vote on either). He has overall responsibility for all activities of the Group, is a principal contact for all shareholder and investor relations matters and leads licensing and distribution negotiations and new product development activities. He first became involved with the Group as an investor in 1997 and has been a Director of the subsidiary since 1998. Prior to becoming Chief Executive, he was Managing Director of Aon Capital Markets Limited. Mr Barder has predominantly worked in the field of insurance and finance including firms he founded and co-owned. Mr Barder is also a Non-Executive Director of Lorega Ltd and Creon Corporation plc.



Anthony Louis Clayden, BSc (Hons), FCA, MSI
Finance Director and Company Secretary (39)

Mr Clayden joined the Company as Finance Director and Company Secretary in October 2001. He assists the Audit and the Nominations Committees (but is not a member of and does not vote on either). As well as managing financial and compliance matters, he has driven the governance and risk management initiatives and supports the corporate finance and investor relations activities. Mr Clayden's previous Finance Director roles were with privately-owned businesses involved in information technology data storage services and solutions and in consulting and business services. Previously, he worked in corporate finance, mainly focused on technology and services businesses, at PricewaterhouseCoopers and KPMG. He qualified as a Chartered Accountant with BDO Stoy Hayward LLP.



David Bryn Davies, BSc (Hons), MBA
Product Development Director (43)

Mr Davies has been a Director of the Company since September 2001. He is responsible for all product development programmes for the Group, and has extensive experience in the pharmaceutical industry. Prior to joining the Company, Mr Davies was Director of Project Management at Clintrials Research Limited. He has 22 years experience of pharmaceutical and healthcare product development, within pharmaceutical companies and global contract clinical research organisations. Previous employers also include Porton Down, Glaxo Group Research, Wellcome Research Limited, Zambon Limited and PPD Pharmaco Limited.



Jonathan David Freeman, BA (Hons), MBA
Senior Independent Non-Executive Director and Chairman of Remuneration Committee and Audit Committee (41)

Mr Freeman joined the Board in July 2003 and was appointed Senior Independent Non-Executive Director in November 2003. As well as chairing the Audit and the Remuneration Committees, he is also a member of the Nominations Committee. He provides guidance on city regulatory matters, corporate finance and investor relations. He provides over ten years of corporate finance experience including as a Partner at Gambit Corporate Finance, as a Director of Beeson Gregory and involvement in the creation of EASDAQ. Mr Freeman is also an Executive Director of Creon Corporation plc and a Non-Executive Director of AIM-quoted Cobra Capital Limited, Equity Pre-IPO Investments Limited and Syndicate Asset Management plc.



Andrew Slater, BA (Hons)
Independent Non-Executive Director and Chairman of Nominations Committee (58)

Mr Slater joined the Board in July 2003. As well as chairing the Nominations Committee, he is also a member of the Remuneration and the Audit Committees. He provides insight into the marketing and consumer aspects of bringing new products to market. He has over 30 years worldwide marketing expertise mainly in healthcare and pharmaceuticals and was a Director of SSL International plc having spent 17 years with London International Group plc. Mr Slater's experience includes all aspects of the promotion and marketing of SSL International plc's products including family planning products and he was the Managing Director of both the Americas and Europe.

Directors' Report

The Directors present their report and the audited financial statements for the year ended 31 December 2005.

Principal activities

The principal activity of the Group is the research and development of pharmaceutical products and medical devices and their commercial exploitation. The Chairman and Chief Executive Joint Review on pages 2 to 3 and Financial Review on page 4 report in more detail on the Group's activities during the year and anticipated future developments.

Research and development activities

The main area of research and development continues to be in the field of medical products for sexual health and sexual well-being.

Business review and future developments

During the year, the subsidiary Futura Medical Developments Limited has continued to incur research and development expenditure which has been written off as incurred.

As well as continuing its existing research and development program, the Group continues to seek new opportunities for potential products to add to its portfolio.

Results and Dividends

The results of the Group for the year are set out on pages 15 to 27 and show a loss after tax of £1,904,144 (year ended 31 December 2004: £1,228,951). No dividends are paid or proposed (year ended 31 December 2004: £Nil).

Directors and their interests

The Directors of the Company during the year were:

Dr W D Potter	D B Davies
J H Barder	J D Freeman
A L Clayden	A Slater

The Directors who held office at the end of the financial year had the following interests in the shares of the Company:

	Ordinary shares of 0.2 pence each			
	31 December 2005		1 January 2005	
	Beneficial Interests	Other interests	Beneficial interests	Other interests
J H Barder	236,997	314,500	236,997	314,500
D B Davies	15,152	–	15,152	–

Other than shown in the table above, no Director had any interest in the shares of the Company or any other Group companies at 31 December 2005.

The share options held by the Directors at 31 December 2005 are set out below:

	Number of options over shares	
	At 31 December 2005	At 1 January 2005
J H Barder	350,000	250,000
D B Davies	1,250,000	1,150,000
A L Clayden	775,000	675,000
W D Potter	425,000	375,000

None of the share options held by the Directors have been exercised or have lapsed.

Employees

At 31 December 2005, the Group employees comprise two Non-Executive Directors, four Executive Directors and five full time staff all of whom are employed by the subsidiary. The Chairman moved from a non-executive to executive role during the course of the year.

In this context the Executive Directors keep staff informed of the progress and development of the Group regularly through formal and informal meetings and employee feedback is encouraged. The Company has a policy of offering share options to all eligible employees, subject to availability under the option plan rules and with due consideration to the level of dilution of shareholders.

The Group does not discriminate between employees and prospective employees on grounds of race, religion or gender. Every effort is made to provide the same opportunities to disabled persons as to others.

Directors' Report (*continued*)

Supplier payment policy

The Group's policy concerning the payment of its trade creditors is to pay on the basis of the agreed terms of payment established with each supplier, providing that all terms and conditions have been complied with and in accordance with the Group's financial control procedures.

The average credit period (expressed as creditor days) during the year ended 31 December 2005 was 20 days (year ended 31 December 2004: 20 days) for the Group. At the year end the Company had trade creditors totalling £6,571 (31 December 2004: £598) giving rise to the average credit period for the year ended 31 December 2005 of 8 days (year ended 31 December 2004: 1 day).

Charitable and political contributions

No charitable donations were made during the year (year ended 31 December 2004: £6,000). No political donations were made during the year (year ended 31 December 2004: £nil).

Substantial shareholdings

At 11 May 2006, the issued share capital of the Company was 49,668,601 ordinary shares of 0.2 pence each and the following shareholders were listed in the shareholder register as holding 3 per cent or more of the Company's share capital:

	Number of ordinary shares	Percentage of issued ordinary share capital
Ferlim Nominees Limited Pooled Acct	5,179,627	10.4%
The Bank of New York (Nominees) Limited Cor Acct	3,372,000	6.8%
WT Lamb Investments Limited	3,000,000	6.0%
Christopher John Crabtree	2,498,030	5.0%
R C Greig Nominees Limited	2,440,840	4.9%
HSBC Global Custody Nominee (UK) Limited 934567 Acct	1,862,915	3.8%
HSBC Global Custody Nominee (UK) Limited 741812 Acct	1,776,600	3.6%
Willbro Nominees Limited	1,515,449	3.1%

Directors' responsibilities

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and Group and of the profit or loss of the Group for that year. In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985. In addition the Directors are responsible for ensuring that the annual report includes information required by the listing rules of AIM. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Financial statements are published on the Company's website in accordance with legislation in the United Kingdom governing the preparation and dissemination of financial statements, which may vary from legislation in other jurisdictions. The maintenance and integrity of the Company's website is the responsibility of the Directors. The Directors' responsibility also extends to the ongoing integrity of the financial statements contained therein.

Auditors

A resolution to reappoint BDO Stoy Hayward LLP as auditors will be proposed at the next Annual General Meeting.

By order of the Board

A L Clayden, Secretary
19 May 2006

Remuneration Report

Composition and Terms of Reference

The Group's Remuneration Committee during the year ended 31 December 2005 comprised the independent Non-Executive Directors, A Slater and J D Freeman, and was chaired by J D Freeman. Dr W D Potter, as Executive Chairman, acted as an adviser to the Remuneration Committee because of his knowledge of the industry. However, by virtue of his executive role he was not considered to be independent and was excluded from voting.

The purpose of the Remuneration Committee is to ensure that the Executive Directors and other Senior Executives are fairly rewarded for their individual contribution to the overall performance of the Company. The Committee considers and recommends to the Board the remuneration of the Executive Directors and is kept informed of the remuneration packages of senior staff and invited to comment on these.

The Board retains responsibility for overall remuneration policy. The Remuneration Committee operates within agreed terms of reference which are published on the Group's website. There were no changes to the terms of reference nor to the composition of the Remuneration Committee during the year ended 31 December 2005.

Policy on Executive Directors' remuneration

Executive remuneration packages are designed to attract and retain executives of the necessary skill and calibre to run the Company successfully but avoiding paying more than is necessary. Direct benchmarking of remuneration is not possible given the specialised nature and size of the Company. The Remuneration Committee recommends to the Board remuneration packages by reference to individual performance and uses the knowledge and experience of the Non-Executive Directors and the Executive Chairman and published surveys relating to AIM Directors, the pharmaceutical industry and market changes generally. The Remuneration Committee has responsibility for recommending any long term incentive schemes.

The full Board determine whether or not Executive Directors are permitted to serve in roles with other companies. Such permission is only granted where a role is on a strictly limited basis, where there are no conflicts of interest or competing activities and providing there is not an adverse impact on the commitments required to the Group. Earnings from such roles are not disclosed nor paid to the Group.

There are potentially four main elements of the remuneration package for Executive Directors and senior employees.

(i) Basic salaries and benefits in kind

Basic salaries are recommended to the Board by the Remuneration Committee, taking into account the performance of the individual and the rates for similar positions in comparable companies. Benefits in kind include car allowance (no company cars are provided), death in service insurance, permanent health insurance and private medical insurance. Salary alternatives are available instead of the benefits in kind. Car allowance and benefits in kind are not pensionable.

(ii) Share option schemes

The Company operates approved and unapproved share option schemes for the Chairman, Executive Directors, employees and consultants to motivate those individuals through equity participation in the Company. Exercise of options under the schemes is subject to specified exercise periods.

The schemes are overseen by the Remuneration Committee which recommends to the Board the grant of share options to senior management and Executive Directors based on personal performance and specifying the terms under which eligible individuals may be invited to participate.

The Combined Code refers to the requirement for the performance-related elements of remuneration to form a significant proportion of the total remuneration package of Executive Directors and should be designed to align their interests with those of shareholders. In the development phase of the Group and during the early stages of revenue generation, the Remuneration Committee currently considers that the best alignment of these interests is through continued incentivisation of performance through the award of share options.

(iii) Bonus Scheme

Currently, the Company does not operate a bonus scheme.

(iv) Pensions

The Group pays a defined contribution to the pension scheme of Executive Directors and employees or offers a cash alternative. The individual pension schemes are private and their assets are held separately from those of the Group.

Salaries and benefits were reviewed in January 2006 to cover the year from 1 February 2006 to 31 January 2007. Future reviews will continue to be on an annual basis in the month following the Company's financial year to enable the Group's performance to be considered.

Remuneration Report (*continued*)

Service contracts

All Executive Directors except the Chairman are employed under service contracts requiring six months notice by either party. All Non-Executive Directors and the Chairman receive payments under appointment letters which are terminable by three months notice from either party. In addition, the Chairman has a consulting contract with the subsidiary requiring one month's notice by either party.

All Directors are directors of the subsidiary.

Policy on Non-Executive Directors' remuneration

The Non-Executive Directors and the Chairman each receive a fee for their services, which is approved by the Board, mindful of the time commitment and responsibilities of their roles and of current market rates for comparable organisations and appointments. Non-Executive Directors and the Chairman receive travelling expenses and other minor reimbursements of costs incurred.

The Chairman received options prior to the Group joining AIM and is receiving further grants of options in the future in accordance with Group policy. Since this has been the basis of his original appointment and he is not considered independent by the Board, it is not the intention to seek shareholder approval specifically for any future grants of options to the Chairman nor to require any shares acquired by virtue of the exercise of the options to be held by the Chairman for at least one year after leaving the Board.

However, to maintain independence the independent Non-Executive Directors do not participate in any incentive or share option arrangements.

Directors' remuneration

The emoluments of the individual Directors for the year were as follows:

	Year ended 31 December 2005				Total £	Year ended 31 December 2004		
	Salary or Fees £	Benefits in Kind £	Aggregate emoluments £	Pension £		Aggregate emoluments £	Pension £	Total £
Executive Directors								
W D Potter	22,500	–	22,500	–	22,500	21,283	–	21,283
J H Barder	139,375	3,773	143,148	12,838	155,986	134,668	12,078	146,746
D B Davies	117,607	2,369	119,976	8,021	127,997	110,793	9,791	120,584
A L Clayden	106,167	981	107,148	–	107,148	100,958	–	100,958
Non-Executive Directors								
A Slater	20,008	–	20,008	–	20,008	18,917	–	18,917
J D Freeman	20,008	–	20,008	–	20,008	18,917	–	18,917

W D Potter moved from a non-executive role to become Executive Chairman during 2005. His emoluments for 2004 were in a non-executive capacity and they were previously shown together with the Non-Executive Directors. In addition to the above emoluments, W D Potter provides consulting services to Futura Medical Developments Limited, the wholly owned subsidiary, through his consulting company Stapleford Scientific Services Limited. These comprised consultancy fees of £58,000 plus reimbursed expenditure of £2,416 (year ended 31 December 2004: consultancy fees of £40,000 plus reimbursed expenditure of £1,953).

All of the above fees and emoluments do not include reimbursed expenditure incurred in the conduct of Group business.

Directors' interests in share options

The Board uses share options to align employees interests with shareholders in order to incentivise and reward employees relative to improvements in Company performance.

After due consideration by the Remuneration Committee and the Board in consultation with our Nominated Advisor, the expiry date for the options exercisable until 31 January 2006 was extended to 31 January 2007 in order to enable the orderly exercise of the options outside of a close period. This was a result of the company being in multiple, extended close periods for most of the original exercise period (particularly as a result of the anonymity of MGPG during discussions and the exclusivity period for negotiations).

Remuneration Report (*continued*)

Directors' interests in share options (*continued*)

The share options of the Directors under the Futura Medical plc Enterprise Management Incentive Scheme are set out below:

	Grant Date	Awarded Number	Exercise Price/Share	Earliest Exercise Date	Expiry Date
J H Barder	5 March 2002	250,000	53p	1 August 2004	31 January 2007
	22 March 2005	100,000	76p	1 April 2007	31 March 2009
D B Davies	5 March 2002	1,000,000	33p	1 August 2004	31 January 2007
	8 July 2003	150,000	70p	1 August 2005	31 July 2007
	22 March 2005	100,000	76p	1 April 2007	31 March 2009
A L Clayden	5 March 2002	500,000	33p	1 August 2004	31 January 2007
	8 July 2003	175,000	70p	1 August 2005	31 July 2007
	22 March 2005	100,000	76p	1 April 2007	31 March 2009

The share options under the Futura Medical plc Unapproved Share Option Scheme (formerly the Futura Medical plc Pre-IPO Share Option Scheme) of the Directors who served during the year are set out below:

	Grant Date	Awarded Number	Exercise Price/Share	Earliest Exercise Date	Expiry Date
W D Potter	21 March 2002	250,000	33p	1 August 2004	31 January 2007
	21 March 2002	125,000	53p	1 August 2004	31 January 2007
	22 March 2005	50,000	76p	1 April 2007	31 July 2009

All options have been granted with an exercise price at or above market value. The two independent Non-Executive Directors will not receive share options in order to maintain their independence under the Combined Code.

There were no further options granted to Directors during the year and none of the Directors' options have been exercised or have lapsed during the year.

J D Freeman, Chairman of the Remuneration Committee

Corporate Governance

Introduction

As an AIM quoted company, compliance with the Combined Code has not been mandatory for the Group. However, the Board is committed to maintaining appropriate standards of Corporate Governance. The Group accepts the principles of good Corporate Governance as embodied in the Combined Code.

Significant aspects of the 1998 Combined Code were adopted by the Group in advance of joining AIM in July 2003 and in 2004 further changes were made in respect of the July 2003 Combined Code. It is Group policy to undertake an annual review of Corporate Governance and this was most recently completed in December 2005.

In assessing the appropriate standards of Corporate Governance, the Board is mindful of the nature and small size of the Group and has given due consideration to the Quoted Companies Alliance ("QCA") Guidelines published in 2005. The QCA Guidelines represent a simple set of guidelines for corporate governance for AIM companies and are a benchmark for Combined Code compliance.

This report includes any changes made to our Corporate Governance and our compliance with the Combined Code and QCA Guidelines following our annual review.

Statement of compliance

At the start of 2005, substantially the whole of the 2005 Combined Code had already been considered and formalised where appropriate in the procedures of the Group. The only changes of significance during 2005 were the Chairman moving from a non-executive to executive role, his consequent stepping down from the Audit Committee to be replaced by an Independent Non-Executive Director and the establishment of the Nominations Committee.

The 2005 annual review determined that the Group's practice and procedures comply with the QCA Guidelines in all respects except that the Audit Committee report is included within this Corporate Governance section rather than forming a separate report.

The Board considers that given the size and nature of its activities it does not intend to comply with the Combined Code in respect of certain items listed below. None of these items is required by the QCA Guidelines. This is considered by the Board to be reasonable and does not compromise the overall principles of Corporate Governance which the Board strongly supports:

- There will be no preclusion of the Chief Executive becoming Chairman although there is no current intention for this succession.
- The Remuneration Committee in deciding on remuneration at its annual review each January takes into account the performance of the Group as a whole and the individual Directors. However, the nature of this performance evaluation is not specified in the annual report.
- Where the Board permits the Executive Directors to serve in roles with other companies as long as they do not compromise the individual's ability to perform his services to the Group, the earnings from such roles are not disclosed to the Board nor paid to the Group.

The Board considers that the remuneration of Executive Directors does include a performance-related element but this is not associated with a cash bonus scheme. Instead it is based on the award of share options as recommended by the Remuneration Committee and details are set out in the Remuneration Report on pages 8 to 10. The Remuneration Committee is considering the introduction of a cash bonus incentive as part of the overall performance-related reward as the Company moves towards revenue generation.

Board of Directors

The Board of Directors has overall responsibility for the Group. The composition and biographies are set out on page 5.

The Board comprises an Executive Chairman, two independent Non-Executive Directors and three further Executive Directors. The Chairman provides consulting services to the subsidiary, Futura Medical Developments Limited, and has share options in the Company. The two independent Non-Executive Directors do not have shareholdings or options in the Company and solely receive fees as Non-Executive Directors. The Board is satisfied that it has an appropriate mix of independence and experience in its Non-Executive Directors.

The roles of Chairman and Chief Executive are and will remain separate and it is not permissible for the same individual to be appointed to both roles simultaneously. The Company does not formally preclude a Chief Executive being appointed as Chairman upon resignation as a Chief Executive but there are no plans for this to occur.

The Chairman provides strategic and operational guidance bringing to bear extensive experience of the medical device and pharmaceutical industries. He also oversees the duties performed by the Chief Executive and ensures that they are in line with Board expectations with a particular emphasis on monitoring product development. The Chief Executive manages the day-to-day running and strategic direction of the Company in line with policy decisions given by the Board and shareholder expectations with particular emphasis on the commercial direction of the Company.

The Board retains full control of the Group with day-to-day operational control delegated by the Board to the Executive Directors. The full Board meets bi-monthly and on any other occasions it considers necessary. During 2005, the Board had 9 full Board meetings and 3 further sub-committee meetings. In respect of attendance, of the 9 full Board meetings held, A Slater and D B Davies missed one meeting each but they were otherwise fully attended as were all committee meetings by their constituent Directors.

Corporate Governance (*continued*)

Board of Directors (*continued*)

The Board is responsible for approving interim and annual financial statements, formulating and monitoring Group strategy and approving financial plans and reviewing performance, as well as complying with legal, regulatory and corporate governance matters. There is a schedule of matters reserved for the Board. Board papers are circulated in advance of each Board meeting.

Audit Committee

The Audit Committee comprises the Non-Executive Directors J D Freeman and A Slater (replacing W D Potter who moved from a non-executive to an executive role during 2005) and is chaired by J D Freeman as Senior Independent Non-Executive Director. It meets as required and specifically to review the Interim Report and Annual Report and to consider the suitability and monitor the effectiveness of the internal control processes. There were 3 Audit Committee meetings during 2005. The Audit Committee reviews the findings of the external auditors and reviews accounting policies and material accounting judgments. The Group does not have an internal audit function and this is still considered appropriate given the size and nature of the Group and its operations.

The independence of the auditors is considered by the Audit Committee. The Audit Committee (without any Executive Director present) meets at least once a year with the auditors to discuss their objectivity and independence, the Annual Report, audit issues arising (if any), internal control processes and any other appropriate matters. As well as providing audit related services, the auditors provide taxation advice and undertake work in relation to the Interim Report and the DTI grant. The fees in respect of the non-audit services provided is approximately half the fees for the audit services. Further, the overall fees paid to the auditors are not deemed to be of such significance to them to impair their independence. The Audit Committee considers that the objectivity and independence of the auditors is safeguarded.

Despite the small size and transparent nature of the Group, the Audit Committee has followed good Corporate Governance practice by establishing formal "whistleblowing" procedures. These enable staff to confidentially raise concerns about possible improprieties and to enable proportionate and independent investigation of such matters and appropriate follow up action.

During 2005, the Audit Committee reviewed and made recommendations to the Board regarding updating its terms of reference. The majority of these changes related to formalising existing practice. These recommendations were approved by the Board. The current terms of reference of the Audit Committee are set out in the governance pages on the Group's website (www.futuramedical.co.uk).

Internal control

The Directors are responsible for establishing and maintaining the Group's system of internal control and for reviewing its effectiveness. The system of internal control is designed to manage, rather than eliminate, the risk of failure to the achievement of business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The Audit Committee continues to monitor and review the effectiveness of the system of internal control and report to the Board when appropriate with recommendations. There have been no significant changes to the system of internal control throughout the year.

The Audit Committee continues to consider annually the requirement for an internal audit function. Although activity levels had increased, the annual review of internal control and financial reporting procedures did not highlight any issues warranting the introduction of an internal audit function. It was concluded, given the current size and transparency of the operations of the Group, that an internal audit function was still not required.

The main features of the internal control system are outlined below:

- A control environment exists through the close management of the business by the Executive Directors. The Group has a defined organisational structure with delineated approval limits. Controls are implemented and monitored by the Executive Directors.
- The Board has a schedule of matters expressly reserved for its consideration and this schedule includes acquisitions and disposals, major capital projects, treasury and risk management policies and approval of budgets.
- The Group utilises a detailed budgeting and forecasting system. Detailed budgets are prepared annually by the Executive Directors before submission to the Board for approval. Forecasts are regularly updated at least quarterly to reflect changes in the business and are monitored by the Board including future cash flow projections. Actual results are monitored against annual budgets in detail on a six monthly basis, with variances highlighted for the Board.
- Financial risks are identified and evaluated for each major transaction for consideration by the Board and senior management.
- Standard financial control procedures operate throughout the Group to ensure that the assets of the Group are safeguarded and that proper accounting records are maintained.
- A risk review process is in operation whereby the Chief Executive and Finance Director report to the Board twice each year on the key business risks.

Corporate Governance (*continued*)

International Financial Reporting Standards

IFRS will apply to AIM quoted companies for financial years commencing on or after 1 January 2007. Therefore, Futura Medical plc will be required to report its year ending 31 December 2007 financial statements applying IFRS with comparatives for 31 December 2006. No early adoption of IFRS is planned.

Going concern

The Directors have a reasonable expectation that the Group and the Company will continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Group's financial statements.

Nominations Committee

A Nominations Committee was established comprising the two Non-Executive Directors and the Chairman and was chaired by A Slater, an independent Non-Executive Director. Terms of reference were established in March 2005. The Nominations Committee has been established to monitor the requirements of the Group in respect of Board composition as the Group evolves and succession planning when any such issues should arise. There were 2 Nominations Committee meetings during 2005. There are no matters outstanding to date.

The terms of reference of the Nominations Committee are set out in the governance pages on the Group's website (www.futuramedical.co.uk).

Remuneration Committee

The details of the Remuneration Committee are not included here as their activities are set out in the Remuneration Report on pages 8 to 10. There was one Remuneration Committee meeting during 2005. The terms of reference of the Remuneration Committee are set out in the governance pages on the Group's website (www.futuramedical.co.uk).

Relationship with shareholders

The Directors seek to build a mutual understanding of objectives between the Company and its shareholders. The Group reports formally to shareholders in its interim and annual reports setting out details of its activities. In addition, the Group keeps shareholders informed of events and progress through the issue of press releases. The Executive Directors meet with institutional shareholders following interim and final results. The Company also maintains investor relations pages on its website (www.futuramedical.co.uk).

Where possible the Annual Report is sent to shareholders at least 20 working days before the Annual General Meeting. Directors are required to attend Annual General Meetings of the Company unless unable to do so for personal reasons or due to pressing commercial commitments. Shareholders are given the opportunity to vote on each separate issue. The Company counts all proxy votes and will indicate the level of proxies lodged on each resolution, after it has been dealt with by a show of hands.

A L Clayden, Secretary

Independent Auditor's Report

To the shareholders of Futura Medical plc

We have audited the financial statements of Futura Medical plc for the year ended 31 December 2005 which comprise of the Consolidated Profit and Loss Account, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement and the related notes. These financial statements have been prepared under the accounting policies set out on pages 19 and 20.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the annual report and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Group has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We read other information contained in the annual report and consider whether it is consistent with the audited financial statements. The other information comprises only the Company Profile, Highlights, Chairman and Chief Executive Joint Review, the Financial Review, the Corporate Governance Statement, the Remuneration Report and the Directors' Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of affairs of the Company and the Group as at 31 December 2005 and of the loss of the Group for the year then ended and the financial statements have been properly prepared in accordance with the Companies Act 1985.

BDO STOY HAYWARD LLP

*Chartered Accountants
and Registered Auditors*
Reading

19 May 2006

Consolidated Profit and Loss Account
For the year ended 31 December 2005

	Notes	Year ended 31 December 2005 £	Year ended 31 December 2004 £
Turnover		1,660	129,863
Research and development costs		(1,535,240)	(960,141)
Other administrative costs		(791,004)	(745,806)
Administrative expenses		(2,326,244)	(1,705,947)
Operating loss	2	(2,324,584)	(1,576,084)
Other interest receivable and similar income	5	133,467	177,047
Loss on ordinary activities before taxation		(2,191,117)	(1,399,037)
Tax on loss on ordinary activities	6	286,973	170,086
Loss on ordinary activities after taxation and retained loss for the year	16	(1,904,144)	(1,228,951)
Basic and diluted loss per share (pence)	7	(3.9p)	(2.6p)

All amounts relate to continuing activities.

There were no recognised gains and losses in the year, or in the prior period, other than those passing through the profit and loss account above and therefore no separate statement of total recognised gains and losses has been presented.

The notes on pages 19 to 27 form part of these financial statements.

Balance Sheets
At 31 December 2005

	Notes	Group 31 December 2005 £	Group 31 December 2004 £	Company 31 December 2005 £	Company 31 December 2004 £
Fixed Assets					
Tangible assets	8	25,370	28,120	–	–
Investments	9	–	–	60,724	60,724
		25,370	28,120	60,724	60,724
Current Assets					
Stock	10	31,956	14,812	–	–
Debtors – due within one year	11	351,079	258,211	17,203	18,094
Debtors – due after more than one year	11	–	–	6,654,596	4,742,780
Total debtors		351,079	258,211	6,671,799	4,760,874
Cash at bank and in hand		1,808,913	3,672,647	1,732,998	3,512,964
		2,191,948	3,945,670	8,404,797	8,273,838
Creditors: amounts falling due within one year	12	(237,147)	(225,275)	(35,913)	(26,584)
Net current assets		1,954,801	3,720,395	8,368,884	8,247,254
Total net assets		1,980,171	3,748,515	8,429,608	8,307,978
Capital and reserves					
Called up share capital	14	97,877	97,357	97,877	97,357
Share premium account	16	8,560,987	8,425,707	8,560,987	8,425,707
Other reserves	16	1,152,165	1,152,165	–	–
Profit and loss account	16	(7,830,858)	(5,926,714)	(229,256)	(215,086)
Equity shareholders' funds	17	1,980,171	3,748,515	8,429,608	8,307,978

The financial statements on pages 15 to 27 were approved and authorised for issue by the Board on 19 May 2006 and were signed on its behalf by

J H Barder, Director

The notes on pages 19 to 27 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2005

	Notes	Year ended 31 December 2005 £	Year ended 31 December 2005 £	Year ended 31 December 2004 £	Year ended 31 December 2004 £
Net cash outflow from operating activities	A		(2,292,863)		(1,559,590)
Returns on investments and servicing of finance					
Interest received		139,306		175,141	
Net cash inflow from returns on Investments and servicing of finance			139,306		175,141
Corporation Tax					
Research and development tax credit received		167,858		108,436	
Capital expenditure					
Payments to acquire tangible fixed assets		(13,835)		(21,648)	
Proceeds on disposal of fixed assets		–		170	
Net cash outflow from capital expenditure			(13,835)		(21,478)
Net cash outflow before use of liquid resources and financing			(1,999,534)		(1,297,491)
Management of liquid resources					
Decrease/(Increase) in short term deposits			(1,787,913)		(1,160,993)
Financing					
Issue of ordinary shares		135,800		2,644,550	
Expenses paid in connection with share issues		–		(76,120)	
Net cash inflow from financing			135,800		2,568,430
(Decrease)/Increase in net cash	B		(75,821)		109,946

The notes on page 18 form part of this cash flow statement.

Notes to the Consolidated Cash Flow Statement

For the year ended 31 December 2005

A Reconciliation of operating loss to net cash outflow from operating activities

	Year ended 31 December 2005 £	Year ended 31 December 2004 £
Operating loss	(2,324,584)	(1,576,084)
Depreciation	13,203	15,414
Loss on sale of fixed assets	–	3,897
(Increase)/Decrease in stocks	(17,114)	2,467
Decrease/(Increase) in debtors	20,408	(46,463)
Increase in creditors	15,254	41,179
Net cash outflow from operating activities	<u>(2,292,863)</u>	<u>(1,559,590)</u>

B Analysis of net cash

	At 1 January 2005 £	Cash flow £	At 31 December 2005 £
Cash at bank and in hand	164,734	(75,821)	88,913
Other liquid resources	3,507,913	(1,787,913)	1,720,000
	<u>3,672,647</u>	<u>(1,863,734)</u>	<u>1,808,913</u>

C Reconciliation of net cash flow to movement in net funds

	Year ended 31 December 2005 £	Year ended 31 December 2004 £
(Decrease)/Increase in cash in the year	(75,821)	109,946
Cash (outflow)/inflow from changes in liquid resources	(1,787,913)	1,160,993
Movement in net funds in the year	(1,863,734)	1,270,939
Net funds at start of year	3,672,647	2,401,708
Net funds at end of year	<u>1,808,913</u>	<u>3,672,647</u>

Notes to the Financial Statements

For the year ended 31 December 2005

1 Accounting policies

1.1 Basis of preparation

The financial statements have been prepared under the historical cost accounting rules and in accordance with applicable UK accounting standards. The following principle accounting policies have been applied.

1.2 Basis of consolidation

The consolidated financial statements include the results of the Company and its subsidiary, Futura Medical Developments Limited, for the year ended 31 December 2005.

Under the provisions of Financial Reporting Standard 6, Acquisitions and Mergers, these consolidated financial statements are prepared using merger accounting.

The investment is recorded in the Company's balance sheet at the nominal value of the shares issued together with the fair value of any additional consideration paid.

In the Group financial statements, merged subsidiary undertakings are treated as if they had always been a member of the Group. The results of such a subsidiary are included for the whole period in the year it joins the Group. The corresponding figures for the previous year include its results for that period, the assets and liabilities at the previous balance sheet date and the shares issued by the Company as consideration as if they had always been in issue. Any difference between the nominal value of the shares acquired by the Company and those issued by the Company to acquire them is taken to reserves.

As permitted by Section 230 of the Companies Act 1985, the holding Company's profit and loss account has not been included in these financial statements. The Company made a loss after tax of £14,170 for the year (year ended 31 December 2004: profit after tax of £53,519).

1.3 Turnover

Turnover comprises royalty fees and the sale of rights to future royalty fees and excludes value added tax.

Royalty fees that are receivable are recognised as turnover in the year to which they relate. Sales of the rights to future royalty fees are recognised as turnover on the date on which they become receivable.

1.4 Research and development

Research and development expenditure is charged to the profit and loss account in the year in which it is incurred.

1.5 Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less depreciation. Depreciation is provided at rates calculated to write off the cost less estimated residual value of each asset over its expected useful life, as follows:

Plant and machinery	25% Straight line
Fixtures, fittings & equipment	25% Straight line

1.6 Deferred taxation

Deferred tax balances are recognised in respect of all timing differences that have originated but not reversed by the balance sheet date, except that the recognition of deferred tax assets is limited to the extent that the Company anticipates making sufficient taxable profits in the future to absorb the reversal of the underlying timing differences. Deferred tax balances are not discounted.

1.7 Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date. Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. All differences are taken to profit and loss account.

1.8 Pension costs

The Group provides retirement benefits to all employees and Executive Directors who wish to participate by defined contribution pension schemes. The assets of these schemes are held separately from those of the Group in independently administered funds. Contributions made by the Group are charged to the profit and loss account in the year in which they become payable.

Notes to the Financial Statements

For the year ended 31 December 2005

1 Accounting policies (continued)

1.9 Leased assets

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

1.10 Share based employee remuneration

When shares and share options are granted to employees a charge is made to the Group profit and loss account and a reserve created in capital and reserves to record the fair value of the awards in accordance with UITF Abstract 17 "Employee Share Schemes". No charge has been made to date as the exercise price of all share options granted has been equal to the Company's share price at the date of award. Prior to becoming quoted on AIM, the Company's share price was considered to be the price of the placing preceding the particular grant of options.

1.11 National insurance on share options

Where possible, all employee option holders enter into an Inland Revenue joint election to transfer the employers' national insurance contribution potential liability to the employee. To the extent that such an election has not been entered into and where the share price at the balance sheet date is greater than the exercise price on options granted after 19 May 2000, provision for any employers' national insurance contribution has been made based on the prevailing rate of national insurance. However, under the terms of all option rules any liability which may arise is recoverable from each option holder and a corresponding debtor is also included.

1.12 Stocks

Stocks are stated at the lower of cost and net realisable value using the FIFO method. Cost includes all direct expenditure in bringing the stock to its current location and condition.

1.13 Government grants

Government grants relating to research and development expenditure are credited to the profit and loss account as the related expenditure is incurred.

1.14 Liquid resources

For the purpose of the cash flow statement liquid resources are defined as short term money market deposits and notice accounts.

2 Operating loss

	Year ended 31 December 2005	Year ended 31 December 2004
	£	£
Operating loss is stated after charging:		
Depreciation of tangible assets	13,203	15,414
Loss on sale of fixed assets	–	3,897
Hire of other assets – operating leases	70,752	70,752
Auditors' remuneration		
– Audit services	28,620	24,650
– Tax services	10,700	9,450
– Other services	4,500	2,500
	<u> </u>	<u> </u>
Operating loss is stated after crediting:		
Government grants	–	54,587
	<u> </u>	<u> </u>

The audit services relating to the Company for the year ended 31 December 2005 amount to £23,120 (31 December 2004: £18,150).

Notes to the Financial Statements

For the year ended 31 December 2005

3 Wages and salaries

The average monthly number of persons (including all Directors) employed by the Group during the year and their aggregate emoluments are shown below:

	Year ended 31 December 2005	Year ended 31 December 2004
	No.	No.
Management and administration	11	9
The costs incurred in respect of those employed were:		
	£	£
Wages and salaries	615,557	508,820
Social security costs	76,363	62,606
Other pension and insurance benefits costs	47,841	40,394
	<u>739,761</u>	<u>611,820</u>

4 Directors' emoluments

	Year ended 31 December 2005	Year ended 31 December 2004
	£	£
Directors		
Aggregate emoluments	432,789	405,536
Company pension contributions	20,858	21,869

Emoluments disclosed above include the following amounts paid to the highest Director:

	Year ended 31 December 2005	Year ended 31 December 2004
	£	£
Aggregate emoluments	143,148	134,668
Company pension contributions to money purchase scheme	12,838	12,078

During the year, two Directors (year ended 31 December 2004: one Director) participated in a private money purchase pension scheme and no Director (year ended 31 December 2004: one Director) accrued a sum to be allocated to a private money purchase scheme once it has been established.

5 Other interest receivable and similar income

	Year ended 31 December 2005	Year ended 31 December 2004
	£	£
Bank interest receivable	133,467	177,047

Notes to the Financial Statements

For the year ended 31 December 2005

6 Taxation

	Year ended 31 December 2005 £	Year ended 31 December 2004 £
<i>Current tax</i>		
UK corporation tax on loss for the year	(281,536)	(162,421)
Underprovision in prior year	(5,437)	(7,665)
	<u>(286,973)</u>	<u>(170,086)</u>

The tax assessed for the year is different from the standard rate of corporation tax in the UK. The differences are explained below:

	Year ended 31 December 2005 £	Year ended 31 December 2004 £
Loss on ordinary activities before tax	(2,191,118)	(1,399,037)
Loss on ordinary activities at the standard rate of corporation tax in the UK of 19 per cent (31 December 2004: 19%)	(416,312)	(265,817)
Expenses not deductible for tax purposes	1,751	2,480
Difference between depreciation and capital allowances	602	376
Other short-term timing differences	(6,019)	2,331
Unutilised tax losses	220,604	137,409
Additional relief attaching to R&D tax claim	(82,162)	(39,200)
Underprovision in current year	(5,437)	(7,665)
Current tax credit for the year	<u>(286,973)</u>	<u>(170,086)</u>

The Group has tax losses of approximately £5,152,600 (31 December 2004: £3,950,000) available for offset against future taxable profits.

Deferred tax assets amounting to £978,201 (31 December 2004: £755,282) have not been recognised on the basis that their future economic benefit is not certain. Assuming a prevailing tax rate of 19 per cent when the timing differences reverse, the deferred tax asset comprises:

	Year ended 31 December 2005 £	Year ended 31 December 2004 £
Accelerated capital allowances	(1,202)	(943)
Other short term timing differences	404	6,331
Unutilised tax losses	978,999	749,894
	<u>978,201</u>	<u>755,282</u>

7 Loss per ordinary share

Basic loss per share has been calculated in accordance with FRS22. Basic loss per share has been calculated by dividing the loss on continuing ordinary activities after taxation by the weighted average number of ordinary shares in issue during the year. The weighted average number of equity shares in issue was 48,686,327 (year ended 31 December 2004: 48,069,839 shares) and the loss for the year was £1,904,144 (year ended 31 December 2004: £1,228,951). The effect of all potential ordinary shares is antidilutive.

Notes to the Financial Statements
For the year ended 31 December 2005

8 Tangible fixed assets

Cost	Plant and machinery £	Fixtures fittings, and equipment £	Total £
At 1 January 2005	23,806	39,286	63,092
Additions	7,386	3,067	10,453
At 31 December 2005	<u>31,192</u>	<u>42,353</u>	<u>73,545</u>
Depreciation			
At 1 January 2005	6,168	28,804	34,972
Charge for year	7,107	6,096	13,203
At 31 December 2005	<u>13,275</u>	<u>34,900</u>	<u>48,175</u>
Net book value			
At 31 December 2005	<u>17,917</u>	<u>7,453</u>	<u>25,370</u>
At 31 December 2004	<u>17,638</u>	<u>10,482</u>	<u>28,120</u>

There were no disposals during the year ended 31 December 2005. All fixed assets of the Group are held in Futura Medical Developments Limited.

9 Fixed asset investments

Company	Shares in subsidiary undertakings £
Cost and net book value at 1 January 2005 and 31 December 2005	<u>60,724</u>
Interests in group undertakings	
Subsidiary undertaking	Description of shares held
	Proportion of nominal value of issued shares held and voting rights
Futura Medical Developments Limited	Ordinary £1 shares 100%

The above Company is incorporated in England and Wales, and is included in the consolidated financial statements. Futura Medical Developments Limited undertakes research, development, production and sale of pharmaceutical products.

10 Stock

	Group	Company
	31 December 2005	31 December 2004
	£	£
Raw materials and consumables	<u>31,956</u>	<u>14,812</u>
	<u>–</u>	<u>–</u>

There is no material difference between the replacement cost of stocks and the amounts stated above.

Notes to the Financial Statements

For the year ended 31 December 2005

11 Debtors

	Group		Company	
	31 December 2005	31 December 2004	31 December 2005	31 December 2004
	£	£	£	£
Amounts receivable within one year:				
Corporation tax repayable	281,536	162,421	–	–
Other debtors	27,847	40,901	–	–
Prepayments and accrued income	41,696	54,889	17,203	18,094
	<u>351,079</u>	<u>258,211</u>	<u>17,203</u>	<u>18,094</u>
Amounts receivable after more than one year:				
Amounts owed by subsidiary	–	–	6,654,596	4,742,780
	<u>–</u>	<u>–</u>	<u>6,654,596</u>	<u>4,742,780</u>

12 Creditors: amounts falling due within one year

	Group		Company	
	31 December 2005	31 December 2004	31 December 2005	31 December 2004
	£	£	£	£
Trade creditors	114,586	79,310	6,571	598
Taxation and social security	30,780	21,777	–	–
Accruals and deferred income	91,781	124,188	29,342	25,986
	<u>237,147</u>	<u>225,275</u>	<u>35,913</u>	<u>26,584</u>

13 Financial Instruments

The Group holds or issues financial instruments to finance its operations and to manage the interest rate risks arising from its operations and from its sources of finance. The Financial Review on page 4 sets out the Group's treasury and financial risk management policy. Trade creditors and trade debtors are the only other financial instruments that arise directly from the Group's operations.

In the year, the Group's financial instruments comprised financial assets details of which are as follows:

Financial assets

The Group's financial assets at 31 December 2005 were cash at bank and in hand, made up as follows:

	31 December 2005	31 December 2004
	£	£
Currency		
Sterling	1,808,913	3,661,133
US Dollar	–	11,514
	<u>1,808,913</u>	<u>3,672,647</u>

The Group's financial assets comprise money held in bank current accounts, which are instant access, and sterling cash deposits on the money market at monthly rates.

Interest rates and currency of financial assets

Fixed rate financial assets of £1,720,000 (31 December 2004: £3,507,913) were held in sterling cash deposits at the year end. The weighted average period to maturity for sterling cash deposits held at the year end is 34 days (31 December 2004: 32 days), with a weighted average interest rate of 4.51 per cent per annum (31 December 2004: 4.75 per cent per annum). Deposits are held with Butterfield Private Bank and Anglo Irish Bank. In addition, cash of £88,913 (31 December 2004: £164,734) was held on current accounts at Butterfield Private Bank, earning nominal amounts of interest. The US dollar account was closed during the year (31 December 2004: £11,514).

This money is used to provide the necessary finance for the Group's operations.

Notes to the Financial Statements

For the year ended 31 December 2005

13 Financial Instruments (continued)

Currency exposures

The Group enters into some contracts with suppliers which are paid in US Dollars, Euros, or Swiss Francs. To mitigate the risk of any exposure to foreign currency fluctuations where the supplier contract value is more than £100,000, once a price for a contract has been agreed, funds are transferred to the relevant foreign currency bank account established for the purpose, and so are translated at the exchange rate at the date of agreement. The Group will therefore not be exposed to the risks of changing exchange rates, but they will also not benefit from any exchange rate gains. For contracts with smaller values the foreign currency risk is not considered sufficient by the Group to require the establishment of foreign currency bank accounts unless specific circumstances are identified which warrant this. Forward and option contracts are not used.

Foreign exchange creditors at 31 December 2005 totalled £nil (31 December 2004: £2,606).

14 Share capital

	31 December 2005		Authorised		31 December 2004	
	No.	£	No.	£	No.	£
Ordinary shares of 0.2 pence each	500,000,000		500,000,000	1,000,000		1,000,000
	31 December 2005		Allotted, called up and fully paid		31 December 2004	
	No.	£	No.	£	No.	£
Ordinary shares of 0.2 pence each	48,938,601		48,678,601	97,877		97,357

In November 2005, the Company issued 10,000 ordinary shares of 0.2 pence each for the total consideration of £3,300 pursuant to the exercise of share options.

In December 2005, the Company issued 250,000 ordinary shares of 0.2 pence each for the total consideration of £132,500 pursuant to the exercise of share options.

15 Share options

At 31 December 2005, the number of ordinary shares of 0.2 pence each subject to options granted under the Share Option Schemes were:

Exercisable from 1 August 2004 to 31 January 2006 (since extended to 31 January 2007)						
Date of grant	Exercise price per share	At 1 January 2005	Grants	Options exercised	Options waived	At 31 December 2005
5 March 2002	33 pence	1,500,000	–	–	–	1,500,000
5 March 2002	53 pence	250,000	–	–	–	250,000
21 March 2002	33 pence	530,000	–	(10,000)	–	520,000
21 March 2002	53 pence	1,000,000	–	(250,000)	–	750,000
29 July 2002	50 pence	10,000	–	–	–	10,000
25 October 2002	50 pence	110,000	–	–	–	110,000
		3,400,000	–	(260,000)	–	3,140,000

After due consideration by the Remuneration Committee and the Board in consultation with our Nominated Advisor, the expiry date for the options exercisable until 31 January 2006 was extended to 31 January 2007 in order to enable the orderly exercise of the options outside of a close period. This was a result of the company being in multiple, extended close periods for most of the original exercise period (particularly as a result of the anonymity of MGPG during discussions and the exclusivity period for negotiations).

Notes to the Financial Statements

For the year ended 31 December 2005

15 Share options (continued)

Exercisable from 1 August 2005 to 31 July 2007						
Date of grant	Exercise price per share	At 1 January 2005	Grants	Options exercised	Options waived	At 31 December 2005
8 July 2003	70 pence	410,000	–	–	–	410,000
Exercisable from 1 October 2006 to 30 September 2008						
Date of grant	Exercise price per share	At 1 January 2005	Grants	Options exercised	Options waived	At 31 December 2005
1 December 2004	70 pence	150,000	–	–	–	150,000
Exercisable from 1 April 2007 to 31 March 2009						
Date of grant	Exercise price per share	At 1 January 2005	Grants	Options exercised	Options waived	At 31 December 2005
22 March 2005	76 pence	–	425,000	–	–	425,000
Totals for all exercise periods						
Totals for all exercise periods		At 1 January 2005	Grants	Options exercised	Options waived	At 31 December 2005
		3,960,000	425,000	(260,000)	–	4,125,000

16 Reserves

	Share premium account £	Other reserves £	Profit and loss account £
Group			
At 1 January 2005	8,425,707	1,152,165	(5,926,714)
Retained loss for the year	–	–	(1,904,144)
Shares issued during the year	135,280	–	–
Cost of share issues	–	–	–
At 31 December 2005	8,560,987	1,152,165	(7,830,858)
Company			
At 1 January 2005	8,425,707	–	(215,086)
Retained profit for the year	–	–	(14,170)
Shares issued during the year	135,280	–	–
Cost of share issues	–	–	–
At 31 December 2005	8,560,987	–	(229,256)

Other reserves represents the reserve arising on the acquisition of Futura Medical Developments Limited on 6 June 2001 via a share for share exchange accounted for as a Group reconstruction using merger accounting.

Notes to the Financial Statements

For the year ended 31 December 2005

17 Reconciliation of movements in shareholders' funds

	Group		Company	
	31 December 2005	31 December 2004	31 December 2005	31 December 2004
	£	£	£	£
(Loss)/profit for the financial year	(1,904,144)	(1,228,951)	(14,170)	53,519
Net proceeds from issue of shares	135,800	2,568,430	135,800	2,568,430
Net (reduction)/addition to shareholders' funds	(1,768,344)	1,339,479	121,630	2,621,949
Opening shareholders' funds	3,748,515	2,409,036	8,307,978	5,686,029
Closing shareholders' funds	1,980,171	3,748,515	8,429,608	8,307,978

18 Pension costs

The pension charge represents contributions payable by the Group to independently administered funds and during the year amounted to £35,647 (year ended 31 December 2004: £31,535). Pension contributions payable but not yet paid at 31 December 2005 totalled £nil in respect of pension contribution entitlements where employees had not yet provided details of the funds to which the contributions should be made (31 December 2004: £33,604) and are included in creditors.

19 Related party transactions

W D Potter, a Director of the Company, provides consulting services to Futura Medical Developments Limited, the wholly owned subsidiary, through Stapleford Scientific Services Limited. Of the total fees and expenses invoiced during the year by Stapleford Scientific Services Limited of £60,416 plus VAT (year ended 31 December 2004: £41,953 plus VAT), the amount outstanding at 31 December 2005 to Stapleford Scientific Services Limited was £7,826 (31 December 2004: £4,254).

Company Information

Company Number

04206001

Secretary and registered office

Anthony L Clayden
Futura Medical plc
Surrey Technology Centre
40 Occam Road
Guildford
Surrey
GU2 7YG

Nominated advisor and joint broker

Canaccord Adams Limited
Brook House
27 Upper Brook Street
London
W1K 7QF

Principal Solicitors

Memery Crystal
44 Southampton Buildings
London
WC2A 1AP

Auditors

BDO Stoy Hayward LLP
Kings Wharf
20-30 Kings Road
Reading
Berkshire
RG1 3EX

Joint broker

Collins Stewart Limited
9th Floor
88 Wood Street
London
EC2V 7QR

Patent Attorneys

Withers and Rogers
1 Redcliff Street
Bristol
BS1 6NP

Registrars

Capita Registrars
The Registry
Beckenham
Kent
BR3 4TU

Public Relations Advisers

Buchanan Communications Limited
45 Moorfields
London
EC2Y 9AE

Principal Bankers

Butterfield Private Bank
99 Gresham Street
London
EC2V 7NG

Futura Medical plc
Surrey Technology Centre 40 Occam Road The Surrey Research Park Guildford Surrey GU2 7YG
Tel: 01483 685670 Fax: 01483 685671
mail@futuramedical.co.uk www.futuramedical.co.uk