

Avecia Group plc

Directors' report and consolidated
financial statements

Registered number 3768265

31 December 2005

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Directors' report

The directors present their annual report and the audited financial statements for the year ended 31 December 2005 for Avecia Group plc (the "company" or the "parent company") and its subsidiary undertakings (the "group").

Principal activities

The group now operates two main businesses within the Biotechnology segment, having disposed of its remaining specialty chemicals business segments during 2004, 2005 and 2006. These two businesses provide contract manufacturing and development services to drug development companies.

The Biologics business is based in Billingham in the North East of England and manufactures medicines based on recombinant proteins using microbial fermentation processes.

The DNA Medicines business is based in Milford, Massachusetts, USA and makes oligonucleotide based medicines using solid-phase synthesis. These medicines are effectively short strands of DNA or RNA.

Both businesses develop and carry out the manufacturing processes on behalf of customers who own the intellectual property to the compounds. The businesses are currently making a number of medicines which are in late stages of clinical trials. It is hoped that the customers will get regulatory approval of their drugs in the next few years.

The Biologics business is also developing defence vaccines, specifically for anthrax and plague, funded by the US and UK Governments. These vaccines, in respect of which Avecia has intellectual property rights, are based on Avecia's core technology in microbially derived recombinant proteins and, if successful, Avecia may seek to obtain regulatory approval for their use.

Business review

Turnover for the year to 31 December 2005 from continuing operations increased in comparison to 2004 due to higher levels of activity in the Biotechnology segment, which led to a significant improvement in operating profits, before the costs of closure of one of the manufacturing assets for the segment. During the year, the group completed the disposal of the NeoResins business to Koninklijke DSM NV for a consideration of £356.7m generating a profit of £120.5m, the Covion business to Merck KgaA for a consideration of £33.7m, generating a profit of £12.9m, the Fine Chemicals business to Kemfine Oy for a consideration of £15.5m generating a profit of £7.1m, and the Pharmaceutical Intermediates business to Nicholas Piramal India Limited for £2.8m generating a loss of £14.6m.

During 2006, the group has disposed of the Inkjet Printing Materials and Electrophotography businesses and its share of the Image Polymers joint venture. Following these disposals the group utilised £76m of the proceeds to redeem all of the outstanding high yield bonds, including accrued interest and the premium due on redemption. The group also made a one-off contribution of £25m to the UK pension scheme on 3 April 2006, reducing the pension deficit by the same amount.

On 5 July 2006 the company redeemed 1,822,489 of its Redeemable preference shares at a total cost of US\$48.1 million, leaving 1,200,000 of the Redeemable preference shares in issue, with a principal value of US\$30 million.

For more information on these matters, see note 27 Post Balance Sheet Events.

The directors expect sales growth across the continuing business segments during 2006. Operating profit growth from continuing business segments will be primarily dependant on sales growth, improving manufacturing efficiencies and the level of increase in the cost base.

The directors have considered the appropriateness of the going concern concept in relation to the preparation of the financial statements and more detail in respect of this can be found in note 1 to the accounts.

Results and proposed dividend

During the year the group made a profit of £40.0 million (2004: £31.6 million). The directors do not recommend the payment of an equity dividend (2004: £Nil).

Directors' report (*continued*)

Research and development

The group's research, development and process technology activities for its Biotechnology business are located with its manufacturing facilities at Teeside, UK, and Milford, Massachusetts, USA. Its research, development and process technology efforts are driven by the specific requirements of customers and market trends.

Policy and practice on payment of creditors

Given the international nature of the group's operations, there is no group standard in respect of payments to suppliers. Local operational management are responsible for agreeing terms and conditions for their business transactions when orders for goods and services are placed, ensuring that suppliers are aware of the payment terms and including the relevant terms in contracts where appropriate. These arrangements are adhered to when making payments, subject to the terms and conditions being met by the supplier.

Creditor days have not been calculated for the company as the company had no trade creditors at 31 December 2005, nor 2004. At the year end there were 69 days (*2004: 67 days*) purchases in trade creditors for the group.

Directors and directors' interests

The directors who held office during the year were as follows:

DC Greensmith	
DA Nicholson	
JP Scudamore	
A Buckmaster	(Appointed 3 October 2005)
KP Cox	(Appointed 3 October 2005)
D McLellan	(Appointed 3 October 2005)

No director had any interest in the ordinary shares of the company. The interests of the directors who held office at the end of the financial year in Avecia Holdings plc are disclosed in the financial statements of that company. Mr Greensmith resigned on 17 February 2006. Mr Scudamore and Mr Nicholson resigned on 22 March 2006.

Directors' report *(continued)*

Employees

Employee involvement

The group adopts an approach of being honest and open with employees about matters affecting the business. The group is fully committed to keeping employees informed about the performance, progress and issues relating to their business or work unit, and about wider business issues. Certain formal national and local employee consultation arrangements previously operated by the group have ceased to have application having regard to the reduced business segments, number of locations and employees in the group but the group maintains employee communications through line managers and informal processes, as well as formal structures and processes as required by applicable laws.

Equal opportunities

The group believes that every employee should be treated with the same respect and dignity. It values the rich diversity and creative potential of people with differing backgrounds and abilities, and encourages a culture of equal opportunities in which personal success depends on personal merit and performance. It is group policy that there should be no discrimination against any person for any reason that is not relevant to the effective performance of their job. All judgements about people for the purposes of recruitment, development and promotion will be made solely on the basis of their ability and potential in relation to the needs of the job. Every manager is responsible for implementing this policy.

Employment of people with disabilities

It is group policy that people with disabilities should have the same consideration as others with respect to recruitment, retention and personal development. Depending on their skills and abilities, they enjoy the same career prospects as other employees and the same scope for realising potential. The group also takes all reasonable steps to ensure that its working environments can accommodate special needs. The group also makes every effort to continue to employ staff who may become disabled while employed, providing appropriate training and adapting facilities to allow them to continue working wherever possible.

Political and charitable contributions

The group made no political contributions during the year. Donations to UK charities amounted to £45,000 (2004: £35,000).

Auditors

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

By order of the board

[A P CREE]

AP Cree
Secretary

Hexagon Tower
Blackley
Manchester
M9 8ZS

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

The directors are responsible for preparing the Directors' Report and the group and parent company financial statements, in accordance with applicable law and regulations.

Company law requires the directors to prepare group and parent company financial statements for each financial year. Under that law the directors are required to prepare the group financial statements in accordance with IFRSs as adopted by the EU and have elected to prepare the parent company financial statements in accordance with UK Accounting Standards.

The group financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the group; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

The parent company financial statements are required by law to give a true and fair view of the state of affairs of the parent company.

In preparing each of the group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- for the group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and the parent company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

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

KPMG Audit Plc

St James' Square
Manchester
M2 6DS
United Kingdom

Report of the independent auditors to the members of Avecia Group plc

We have audited the group and parent company financial statements (the "financial statements") of Avecia Group plc for the year ended 31 December 2005 which comprise the group income statement, the group and parent company balance sheets, the group cash flow statement, the group statement of recognised income and expense and the related notes. These financial statements have been prepared under the accounting policies set out therein.

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

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Directors' Report and the group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU, and for preparing the parent company financial statements in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 3.

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

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985 and, as regards, the group financial statements, Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and company'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 group financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the group's affairs as at 31 December 2005 and of its profit for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and as regards the group financial statements, Article 4 of the IAS Regulation;
- the parent company financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the parent company's affairs as at 31 December 2005.

[KPMG AUDIT PLC 13 JULY 2006]

KPMG Audit Plc
Chartered Accountants
Registered Auditor

Consolidated Income Statement
for the year ended 31 December 2005

	<i>Note</i>	2005 £m	2004 £m
Continuing Operations			
Group revenue	2	67.0	60.8
Operating costs (excluding restructuring costs)	3	(100.4)	(80.7)
Restructuring costs	3	(7.8)	(14.6)
		(108.2)	(95.3)
Other operating income	3	2.5	5.2
		(38.7)	(29.3)
Operating loss			
Finance income	8	14.7	47.1
Finance costs	9	(69.4)	(76.9)
		(93.4)	(59.1)
Loss before tax			
Taxation	10	(1.6)	(1.9)
		(95.0)	(61.0)
Loss after tax from continuing operations			
Profit from discontinued operations and gain on disposal of discontinued operations, net of tax		135.0	92.6
		40.0	31.6
Retained profit for the year		40.0	31.6
Attributable to equity holders of the parent		40.0	31.6
Discontinued operations is broken down as follows:			
Group revenue	2	146.7	346.4
Operating costs	3	(140.5)	(324.0)
Onerous contracts		-	(1.7)
Impairment of non-current assets		-	(22.2)
		(140.5)	(347.9)
Other operating income	3	2.5	3.9
		8.7	2.4
Profit from discontinued operations			
Share of loss of joint ventures		(3.7)	(6.9)
Gain on disposal of discontinued operations	4	130.0	97.1
		135.0	92.6
Profit from discontinued operations & gain on disposal of discontinued operations		135.0	92.6

Consolidated balance sheet

as at 31 December 2005

	<i>Note</i>	2005 £m	2004 £m
ASSETS			
Non-current assets			
Property, plant and equipment	<i>12</i>	71.8	146.1
Goodwill	<i>11</i>	20.6	40.2
Intangible assets	<i>11</i>	0.3	0.5
Investment in joint controlled entities	<i>13</i>	-	7.9
Amounts due from parent undertakings		42.7	15.0
Total non current assets		135.4	209.7
Current assets			
Inventories	<i>14</i>	7.2	33.3
Trade and other receivables	<i>15</i>	17.6	35.9
Cash and cash equivalents		49.1	22.7
Assets classified as held for sale	<i>4</i>	71.7	291.9
Total current assets		145.6	383.8
Total assets		281.0	593.5
LIABILITIES			
Current liabilities			
Trade and other creditors	<i>16</i>	34.9	57.3
Financial liabilities	<i>18</i>	3.5	76.8
Current tax liabilities		0.1	0.6
Provisions	<i>20</i>	8.8	9.9
Liabilities classified as held for sale	<i>4</i>	12.9	53.1
		60.2	197.7
Non-current liabilities			
Financial liabilities	<i>18</i>	109.3	310.7
Other creditors	<i>17</i>	0.2	1.6
Deferred tax liabilities	<i>21</i>	0.2	2.1
Pension liabilities	<i>26</i>	48.4	82.1
		158.1	396.5
Total liabilities		218.3	594.2
Net assets/(liabilities)		62.7	(0.7)
Equity			
Called up share capital	<i>22</i>	329.1	329.1
Retained earnings	<i>23</i>	(251.0)	(309.9)
Other reserves	<i>23</i>	(15.4)	(19.9)
Equity attributable to equity holders of parent		62.7	(0.7)
Total equity and liabilities		281.0	593.5

These financial statements were approved by the board of directors on 10 July 2006 and were signed on its behalf by:

[D MCLELLAN]

D McLellan
Director

Consolidated cash flow statement
for the year ended 31 December 2005

	2005	2004
	£m	£m
Cash flows from operating activities		
Profit for the period	40.0	31.6
<i>Adjustments for:</i>		
Depreciation, amortisation and impairment charges	23.7	50.4
Finance income	(14.7)	(47.1)
Finance costs	69.4	76.9
Share of loss of associates	3.7	6.9
Gain on disposal of discontinued operations	(130.0)	(97.1)
Tax expense	1.6	1.9
	<hr/>	<hr/>
Operating loss / (profit) before changes in working capital and provisions	(6.3)	23.5
Non cash items	(0.7)	(0.8)
Decrease in provision for pensions and similar obligations	(4.5)	(1.1)
Increase in other provisions	2.4	8.4
Profit on sale of fixed assets	(2.2)	(1.8)
(Increase)/decrease in stocks	(2.7)	1.7
Decrease/(increase) in debtors	7.1	(16.8)
Decrease in creditors	(5.8)	(1.9)
	<hr/>	<hr/>
Cash generated from operations	(12.7)	11.2
Taxation paid	(1.4)	(0.2)
Interest paid	(46.0)	(39.2)
Finance lease interest paid	(0.1)	(0.3)
	<hr/>	<hr/>
Net cash outflow from operating activities	(60.2)	(28.5)
	<hr/>	<hr/>
Cash flows from investing activities		
Dividends from joint ventures	0.3	2.5
Interest received	1.6	1.1
Purchase of tangible fixed assets	(8.5)	(17.4)
Purchase of intangible fixed assets	-	(1.1)
Sale of tangible fixed assets	2.7	5.2
Net cash disposed with subsidiary	(4.8)	(0.2)
Acquisition of fixed asset investment	(1.5)	-
Disposal of subsidiary undertaking	393.8	187.1
	<hr/>	<hr/>
Net cash inflow from investing activities	383.6	177.2
	<hr/>	<hr/>
Cash flows from financing activities		
Loan repayable in current year	6.0	117.5
Loan repayments	(302.7)	(250.5)
Finance lease capital repayments	(0.5)	(0.8)
	<hr/>	<hr/>
Net cash outflow from financing activities	(297.2)	(133.8)
	<hr/>	<hr/>
Net increase in cash and cash equivalents	26.2	14.9
Cash and cash equivalents brought forward	22.7	8.0
Effect of exchange rate fluctuations on cash held	0.2	(0.2)
	<hr/>	<hr/>
Cash and cash equivalents carried forward	49.1	22.7
	<hr/> <hr/>	<hr/> <hr/>

Consolidated statement of recognised income and expense
for the year ended 31 December 2005

	2005	2004
	£m	£m
Foreign exchange translation differences	(6.8)	6.3
Net gain/(loss) on hedge of net investment in foreign subsidiary	6.1	(10.4)
Exchange gains recycled through income statement	5.6	0.3
Actuarial loss relating to pension liability	(8.1)	(10.5)
	<hr/>	<hr/>
Net expense recognised directly in equity	(3.2)	(14.3)
Profit for the year	40.0	31.6
	<hr/>	<hr/>
Total recognised income and expense for the period attributable to equity holders of the parent	36.8	17.3
	<hr/> <hr/>	<hr/> <hr/>

Notes

(forming part of the financial statements)

1 Significant accounting policies

Avecia Group Plc (the "company") is a company incorporated in Great Britain.

The group financial statements consolidate those of the company and its subsidiaries (together referred to as the "group") and equity account the group's interest in jointly controlled entities. The parent company financial statements present information about the company as a separate entity and not about its group (see note 32).

Statement of compliance

The group financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs"). The company has elected to prepare its parent company financial statements in accordance with UK GAAP; these are presented on pages 63 to 70.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these group financial statements and in preparing an opening IFRS balance sheet at 1 January 2004 for the purposes of the transition to Adopted IFRSs.

In applying these accounting policies management makes certain judgements and estimations. Areas where judgements made by the directors have a significant effect on the financial statements are described in the accounting policy description.

Transition to Adopted IFRSs

The group is preparing its financial statements in accordance with Adopted IFRSs for the first time and consequently has applied IFRS 1. An explanation of how the transition to Adopted IFRSs has affected the reported financial position, financial performance and cash flows of the group is provided in note 29.

IFRS 1 grants certain exemptions from the full requirements of IFRSs in the transition period. The following exemption has been taken in these financial statements:

- Business combinations – Business combinations that took place prior to 1 January 2004 have not been restated.

The group has adopted IAS 39 as at the date of transition. The group has not retrospectively applied the derecognition criteria of IAS 39.

Measurement convention

The financial statements are prepared on the historical cost basis except for derivative financial instruments which are stated at their fair value. Non-current assets and disposal groups held for sale are stated at the lower of previous carrying amount and fair value less costs to sell.

Basis of consolidation

Subsidiaries are entities controlled by the group. Control exists when the group has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Jointly controlled entities are those entities over whose activities the group has joint control, established by contractual agreement. The consolidated financial statements include the group's share of the total recognised gains and losses of jointly controlled entities on an equity accounted basis, from the date that joint control commences until the date that joint control ceases.

Notes (continued)

1 Significant accounting policies (continued)

Going Concern

The financial statements have been prepared on the assumption that the Group remains a going concern. The following paragraphs summarise the issues and basis on which the directors have reached their conclusion.

At 31 December 2005 the Group had High Yield Bonds outstanding of \$125m due for repayment in 2009, and \$75m of redeemable preference shares due for repayment in 2010.

Following the successful disposal of its Inkjet Printing Materials and Electrophotography businesses after 31 December 2005, the group used the proceeds of these disposals to repay all of the High Yield Bonds remaining in issue, and to make a contribution to the Avecia Limited pension fund of £25 million. In addition the group retained circa. £50 million of the net proceeds after transaction costs, to be utilised to manage liquidity, re-invest in the group or make repayments of Redeemable preference shares. On 5 July 2006 the company redeemed 1,822,489 of the Redeemable preference shares at a total cost of US\$ 48,056,048, leaving 1,200,000 of the Redeemable preference shares in issue.

The directors have reviewed the group's budget for the current year and outline projections for the subsequent year, including cash flows and forecasts of liquidity available. Following this review, the directors have formed a judgement that, at the time of approval of the financial statements, the Group has sufficient resources to continue operating for the foreseeable future. For these reasons the directors continue to prepare the financial statements on a going concern basis.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Where parts of an item of property, plant and equipment have different useful lives they are accounted for as separate property, plant and equipment.

The cost of each item of property, plant and equipment is written off evenly over its estimated remaining life. Reviews are made periodically of the estimated remaining lives of individual productive assets, taking account of commercial and technological obsolescence as well as normal wear and tear. Depreciation is charged to the income statement on a straight line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. The total asset lives approximate to 15 years for buildings and 10 years for plant and equipment.

Intangible assets and goodwill

Subject to the transitional relief in IFRS 1, all business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries and Jointly Controlled Entities. Identifiable intangibles are those which can be sold separately or which arise from legal rights regardless of whether those rights are separable.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but is tested annually for impairment.

In respect of acquisitions prior to 1 January 2004, goodwill is included at 1 January 2004 on the basis of its deemed cost, which represents the amount recorded under UK GAAP. On transition amortisation of goodwill has ceased as required by IFRS 1. Negative goodwill arising on an acquisition is recognised in the income statement.

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

Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the group has sufficient resources to complete development. The expenditure capitalised includes the cost of materials, direct labour and an appropriate proportion of overheads. Other development expenditure is recognised in the income statement as an expense as incurred.

Expenditure on internally generated goodwill and brands is recognised in the income statement as an expense as incurred.

Intangible assets acquired, including patents and intellectual property rights are capitalised and amortised on a straight line basis over their estimated useful lives. Internally developed intangible assets are not capitalised.

Notes (continued)

1 Significant accounting policies (continued)

Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate the risks specific to the liability.

Classification of financial instruments issued by the Group

Following the adoption of IAS 32, financial instruments issued by the Group are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

- (a) they include no contractual obligations upon the group to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the group; and
- (b) where the instrument will or may be settled in the company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the company's own equity instruments or is a derivative that will be settled by the company's exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of finance expenses. Finance payments associated with financial instruments that are classified in equity are dividends and are recorded directly in equity.

Derivative financial instruments and hedging

Derivative financial instruments

Derivative financial instruments are recognised at fair value. The gain or loss on remeasurement to fair value is recognised immediately in the income statement.

Hedge of net investment in a foreign operation

The portion of the gain or loss on an instrument used to hedge a net investment in a foreign operation that is determined to be an effective hedge is recognised directly in equity. The ineffective portion is recognised immediately in the income statement.

There were no hedge transactions during the year ended 31 December 2005.

Loans and preference shares

Loans and preference shares in kind are stated at amortised cost less impairment.

Foreign currency

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated at foreign exchange rates ruling at the dates the fair value was determined.

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated at an average rate for the period where this rate approximates to the foreign exchange rates ruling at the dates of the transactions.

Notes (continued)

1 Significant accounting policies (continued)

Foreign currency (continued)

Exchange differences arising from this translation of foreign operations, and of related qualifying hedges are taken directly to the hedging reserve. They are released into the income statement upon disposal.

Government grants

Government grants made as a contribution towards revenue expenditure, or for an objective with an associated revenue cost (such as job creation) are included on the balance sheet as deferred income and released to the income statement in line with the costs being incurred.

Capital based government grants are included within accruals and deferred income in the balance sheet and credited to the income statement over the estimated useful economic lives of the assets to which they relate.

Where grants comprise both capital and revenue elements, these elements are split out on a reasonable basis and each element is treated as described above.

Leases

Leases in which the group assumes substantially all the risks and rewards are classified as finance leases. Assets held under finance leases are capitalised and included in property, plant and equipment at the lower of their fair value and the present value of the minimum lease payments at the inception of the lease, less accumulated depreciation and impairment losses. Each asset is depreciated over the shorter of the lease term or its useful life. The obligations related to finance leases, net of finance charges in respect of future periods, are included as appropriate under creditors due within, or creditors due after, one year. The interest element of the rental obligation is allocated to accounting periods during the lease term to reflect a constant rate of interest on the remaining balance of the obligation for each accounting period.

Rentals under operating leases are charged to the income statement on a straight-line basis over the lease term. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

Net financing costs

Net financing costs comprise interest payable, finance charges on shares classified as liabilities and finance leases, interest receivable on funds invested, dividend income, foreign exchange gains and losses and gains and losses on hedging instruments that are recognised in the income statement (see financial instruments accounting policy) and finance charges with respect to the group's defined benefit pension schemes.

Interest income and interest payable are recognised in the income statement as they accrue, using the effective interest method. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established.

Post-retirement benefits

Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value, and the fair value of any plan assets (at bid price) is deducted. The liability discount rate is the yield at the balance sheet date on AA credit rated bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified actuary using the projected unit credit method.

All actuarial gains and losses as at 1 January 2004, the date of transition to Adopted IFRSs, were recognised. In respect of actuarial gains and losses that arise subsequent to 1 January 2004 the Group recognises them in the period they occur directly into equity through the statement of recognised income and expense.

Current service costs and finance charges are recognised in the income statement.

Notes (continued)

1 Significant Accounting policies (continued)

Non-current assets held for sale and discontinued operations

A non-current asset or a group of assets containing a non-current asset (a disposal group) is classified as held for sale if its carrying amount will be recovered principally through sale rather than through continuing use, it is available for immediate sale and sale is highly probable within one year.

On initial classification as held for sale, non-current assets and disposal groups are measured at the lower of previous carrying amount and fair value less costs to sell with any adjustments taken to the income statement. The same applies to gains and losses on subsequent remeasurement. A discontinued operation is a component of the group's business that represents a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to resale, that has been disposed of, has been abandoned or that meets the criteria to be classified as held for sale.

Discontinued operations are presented on a single line in the income statement (including the comparative period).

Inventories

Inventories are stated at the lower of cost and net realisable value. The first in, first out or an average method of valuation is used. In determining cost, depreciation is included but selling expenses and certain overhead expenses (principally central administration costs) are excluded. Net realisable value is determined as selling price less costs of disposal.

Trade and other receivables

Trade and other receivables are stated at amortised cost less impairment losses.

Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill; the initial recognition of assets or liabilities that affect neither accounting nor taxable profit other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Revenue

The company generates revenue through sales of specialty chemicals in the open market, through raw material conversion and supply and development contracts. Revenue excludes inter-segment revenue and value added taxes.

Revenue is recognised when services have been rendered and significant risks and rewards in respect of ownership of the products are passed to the customer. Where multiple-element sales arrangements exist, this entails the company recognizing revenue on individual contract elements for work performed or services rendered during the period.

Cash and cash equivalents

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

Notes (continued)

1 Significant Accounting policies (continued)

Impairment

The carrying amounts of the group's assets other than, inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit on a pro rata basis. A cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

Goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use were tested for impairment as at 1 January 2004, the date of transition to Adopted IFRSs.

Calculation of recoverable amount

The recoverable amount of the group's investments in held-to-maturity securities and receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e. the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted.

The recoverable amount of other assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Reversals of impairment

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed when there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between the initial value and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

Adopted IFRS not yet applied

The following adopted IFRSs were available for early application but have not been applied by the group in these financial statements :

IFRS 7 'Financial Instruments : Disclosure' applicable for years commencing on or after 1 January 2007.

The application of IFRS 7 in 2005 would not have affected the balance sheet or income statement as the standard is only concerned with disclosure. The Group plans to adopt it in 2007.

Notes (continued)

2 Segmental information

Classes of business

The group now operates through two main businesses within the Biotechnology segment which report to the central management team. Inter segment sales are minimal. The group's businesses which were disposed of in 2004 or 2005, or since 1 January 2006 are described below under *Discontinued Operations*.

The following is a brief description of each business segment:

Biotechnology – manufacturing and process development services for advanced medicines;

Discontinued Operations – comprises of i. the entire Specialty Products business segment (the final parts of the segment, the Additives and Biocides businesses, having been sold in January and April 2004 respectively), ii. the NeoResins business (supplier of water-borne resins used as binders and additives in the paint, coating, adhesives and printing ink industries) having been sold in January 2005, iii. Chemicals the Fine Chemicals and Pharmaceutical businesses having being sold in September and December 2005 respectively and iv. Electronic Materials, with the Displays and Organic Semiconductor business unit being sold in February 2005 and the Inkjet, Electrophotography and Image Polymers business units having been sold post year end (see note 27, Post Balance Sheet Events).

The following tables analyse certain income statement and net asset items by business segment. No segment allocation has been shown for interest and taxation as they have not been allocated to these businesses. The accounting policies for each segment are the same as those for the consolidated/combined business. Central costs and overheads are not allocated to individual segments. The group's policy is to transfer products internally at external market prices.

Notes *(continued)*

2 Segmental information *(continued)*

Year ended 31 December 2005	Continuing Operations			Discontinued Operations			Total
	Biotechnology	Central and other	Electronic Materials	Chemicals	NeoResins	Specialty Products	
	£m	£m	£m	£m	£m	£m	£m
Revenue							
Total revenue	62.2	4.8	80.5	56.2	17.3	-	221.0
Jointly controlled entities revenue	-	-	(7.3)	-	-	-	(7.3)
Revenue to third parties	62.2	4.8	73.2	56.2	17.3	-	213.7
Segment operating (loss)/profit before:	(13.8)	(24.9)	12.7	(7.4)	3.4	-	(30.0)
Share of loss in jointly controlled entities	-	-	(3.7)	-	-	-	(3.7)
Profit on disposal of business	-	-	12.9	(7.5)	120.5	4.1	130.0
Segment (loss)/profit before interest and taxation	(13.8)	(24.9)	21.9	(14.9)	123.9	4.1	96.3
Total assets as at 31 December 2005	79.4	143.8	57.8	-	-	-	281.0
Total liabilities at 31 December 2005	16.7	196.5	5.1	-	-	-	218.3
Capital expenditure	2.3	1.1	3.7	0.6	0.4	-	8.1
Depreciation & amortisation	16.0	2.0	1.6	3.6	0.5	-	23.7

Biotechnology operating loss includes a charge of £7.8m relating to accelerated depreciation arising on closure of one of the business's manufacturing operations.

Within the discontinued capital expenditure line above is £0.4 million of expenditure relating to the NeoResins business whose assets are classified as held for sale at 31 December 2004.

Notes *(continued)*

Segmental information *(continued)*

Year ended 31 December 2004	Continuing Operations		Discontinued Operations				Total
	Biotechnology	Central and other	Electronic Materials	Chemicals	NeoResins	Specialty Products	
	£m	£m	£m	£m	£m	£m	£m
Revenue							
Total revenue	55.7	5.1	70.2	77.9	181.0	26.1	416.0
Jointly controlled entities revenue	-	-	(8.8)	-	-	-	(8.8)
Revenue to third parties	55.7	5.1	61.4	77.9	181.0	26.1	407.2
Segment operating (loss)/profit before:	(9.6)	(19.7)	1.2	(49.8)	45.4	5.6	(26.9)
Share of loss in jointly controlled entities	-	-	(6.9)	-	-	-	(6.9)
Profit on disposal of business	-	-	-	-	-	97.1	97.1
Segment (loss)/profit before interest and taxation	(9.6)	(19.7)	(5.7)	(49.8)	45.4	102.7	63.3
Total assets as at 31 December 2004	98.6	263.5	75.4	54.8	101.2	-	593.5
Total liabilities at 31 December 2004	18.1	521.1	10.7	17.4	26.9	-	594.2
Capital expenditure	4.7	0.8	2.4	1.8	5.2	0.3	15.2
Depreciation & amortisation	6.5	1.9	6.4	28.8	6.1	0.8	50.5

The fixed asset impairment charge in 2005 was £Nil. Included in the year ended 31 December 2004 is £22.2 million of fixed asset impairment charge in discontinued operations.

Notes (continued)

2 Segmental information (continued)

Year ended 31 December 2005	UK £m	Continental Europe £m	The Americas £m	Asia, Africa and Australia £m	Total £m
<i>Revenue by destination</i>					
Revenue to third parties	33.3	44.4	90.1	45.9	213.7
<i>Revenue by origin</i>					
Revenue to third parties	110.4	14.4	75.2	13.7	213.7
Total assets as at 31 December 2005	232.1	-	47.1	1.8	281.0
Capital expenditure	6.7	0.4	1.0	-	8.1
Year ended 31 December 2004	UK £m	Continental Europe £m	The Americas £m	Asia, Africa and Australia £m	Total £m
<i>Revenue by destination</i>					
Revenue to third parties	49.5	156.0	141.4	60.3	407.2
<i>Revenue by origin</i>					
Revenue to third parties	115.9	133.6	123.3	34.4	407.2
Total assets as at 31 December 2004	405.2	104.2	78.1	6.0	593.5
Capital expenditure	7.0	4.7	3.5	-	15.2

Notes (continued)

3 Group operating loss

	2005	2005	2005	2004	2004	2004
	Continuing	Discontinued	Total	Continuing	Discontinued	Total
	operations	operations	£m	operations	operations	£m
	£m	£m		£m	£m	£m
Operating costs						
Cost of sales	(41.6)	(114.4)	(156.0)	(41.7)	(228.4)	(270.1)
Distribution costs	(0.7)	(1.5)	(2.2)	(2.6)	(19.6)	(22.2)
Research and development	(10.5)	(15.8)	(26.3)	(11.1)	(34.3)	(45.4)
Selling, general and administrative expenses	(55.4)	(8.8)	(64.2)	(39.9)	(65.6)	(105.5)
	<u>(108.2)</u>	<u>(140.5)</u>	<u>(248.7)</u>	<u>(95.3)</u>	<u>(347.9)</u>	<u>(443.2)</u>
	<u><u>(108.2)</u></u>	<u><u>(140.5)</u></u>	<u><u>(248.7)</u></u>	<u><u>(95.3)</u></u>	<u><u>(347.9)</u></u>	<u><u>(443.2)</u></u>
The following are included within selling, general and administrative expenses :						
Restructuring and site closure	(7.8)	-	(7.8)	(14.6)	-	(14.6)
Impairment of goodwill, intangible & tangible assets	-	-	-	-	(22.2)	(22.2)
Onerous contract	-	-	-	-	(1.7)	(1.7)
	<u>(7.8)</u>	<u>-</u>	<u>(7.8)</u>	<u>(14.6)</u>	<u>(23.9)</u>	<u>(38.5)</u>
	<u><u>(7.8)</u></u>	<u><u>-</u></u>	<u><u>(7.8)</u></u>	<u><u>(14.6)</u></u>	<u><u>(23.9)</u></u>	<u><u>(38.5)</u></u>
Other operating income						
Government grant and licence income	2.5	2.5	5.0	5.2	3.9	9.1
	<u>2.5</u>	<u>2.5</u>	<u>5.0</u>	<u>5.2</u>	<u>3.9</u>	<u>9.1</u>
	<u><u>2.5</u></u>	<u><u>2.5</u></u>	<u><u>5.0</u></u>	<u><u>5.2</u></u>	<u><u>3.9</u></u>	<u><u>9.1</u></u>
Total charge for depreciation and amortisation included above	<u>(18.0)</u>	<u>(5.7)</u>	<u>(23.7)</u>	<u>(8.4)</u>	<u>(42.1)</u>	<u>(50.5)</u>
	<u><u>(18.0)</u></u>	<u><u>(5.7)</u></u>	<u><u>(23.7)</u></u>	<u><u>(8.4)</u></u>	<u><u>(42.1)</u></u>	<u><u>(50.5)</u></u>

Notes (continued)

4 Non-current assets held for sale and discontinued operations

On 2 February 2005 the group completed the sale of the NeoResins business to Koninklijke DSM N.V. for a consideration of EUR 515m. The business's principal manufacturing assets at Waalwijk (Netherlands), Parets des Villes (Spain), Willmington MA and Frankfort IN (United States) were included in the sale. Approximately 635 employees transferred to DSM upon completion. The assets and liabilities of the NeoResins business are classified as held for sale at 31 December 2004 and have been treated as discontinued operations.

On 28 February 2005 the group completed the sale of its Displays and Organic Semiconductor businesses to Merck KgaA of Darmstadt for EUR 50million. The sale included its polymer research and development activities based in Manchester, UK. Approximately 74 employees transferred to Merck KgaA upon completion. The assets and liabilities of these businesses are classified as held for sale at 31 December 2004 and have been treated as discontinued operations.

On 19 September 2005 the group completed the sale of its Fine Chemicals business to KemFine OY, Finland for net proceeds of £15.5 million and has been treated as discontinued operations. The sale included all Avecia Fine Chemicals' assets and operations on the 65 hectare site at Grangemouth in Scotland. Approximately 310 Avecia Fine Chemicals' employees transferred to KemFine upon completion.

On 2 December 2005 the group completed the sale of its Pharmaceutical (custom synthesis) business to Nicholas Piramal India Limited for £2.8 million and has been treated as discontinued operations. The sale included all Avecia Pharmaceuticals' assets and operations at its principal UK site in Huddersfield, England, a large scale fermentation asset at Billingham, England, a High Potency Substance (HPS) facility at Grangemouth in Scotland and its North American operation - Torcan Chemicals in Aurora, Canada. Approximately 350 employees transferred to Nicholas Piramal upon completion.

The principal effects on the reported results are as follows:

	NeoResins	Displays & OSC	Fine Chemicals	Pharma- ceuticals	Other	Total
	£m	£m	£m	£m	£m	£m
Cash flow						
Cash disposed	(4.6)	(0.1)	-	(0.1)	-	(4.8)
Sale of business	356.7	33.7	15.5	2.8	1.6	410.3
Profit on disposal						
Goodwill written off on disposal	(170.5)	(9.2)	-	-	-	(179.7)
Net assets disposed excluding cash (net of pension fund curtailment gain)	(74.7)	(10.9)	(21.8)	(24.0)	-	(131.4)
Pension fund curtailment gain	23.6	0.4	17.6	7.7	2.8	52.1
Disposal costs	(10.0)	(1.0)	(4.2)	(1.0)	(0.3)	(16.5)
Profit on disposal	<u>120.5</u>	<u>12.9</u>	<u>7.1</u>	<u>(14.6)</u>	<u>4.1</u>	<u>130.0</u>
Consideration: Cash	358.5	34.5	15.6	2.8	1.6	413.0
Working capital settlement	(1.8)	(0.8)	(0.1)	-	-	(2.7)
	<u>356.7</u>	<u>33.7</u>	<u>15.5</u>	<u>2.8</u>	<u>1.6</u>	<u>410.3</u>
Impact on cashflows during the period :						
Cash generated from operations	3.8	(0.9)	(0.2)	(5.7)	-	(3.0)
Cashflows from investing activities	(0.5)	-	(0.4)	(0.7)	-	(1.6)
Cashflows from financing activities	-	-	-	-	-	-

Other above includes further sales proceeds in respect of the Biocides business of 1.6m, a pension fund curtailment gain of £2.8m in respect of the Additives business disposal and associated disposal costs of £0.3m. The group has tax losses which can be used to offset the gain from discontinued operations.

Notes *(continued)*

4 Non-current assets held for sale and discontinued operations *(continued)*

On 26 December 2005 the group announced that Fuji Photo Film Co. Ltd ("Fujifilm") was to acquire Avecia's Inkjet and Electrophotography businesses for £143.0 million. The transaction was completed on 17 February 2006. The sale included all Avecia Inkjet and EP development and manufacturing assets in Manchester, England, Grangemouth, Scotland and New Castle, Delaware, USA. 340 employees transferred with the business on completion.

On 31 March 2006 the group sold its interest in the Image Polymer business, a jointly controlled entity to Mitsui.

The assets and liabilities of the Inkjet, Electrophotography and Image Polymers businesses have therefore been classified as held for sale at 31 December 2005. At 31 December 2004 the assets of the NeoResins and Displays and Organic Semiconductors businesses were similarly classified as held for sale.

Assets classified as held for sale	2005	2004
	£m	£m
Disposal group held for sale		
Goodwill	17.7	180.4
Property, plant and equipment	26.8	60.5
Stocks	15.9	16.9
Trade and other receivables	6.9	34.1
Investment in jointly controlled entities	4.4	-
	<hr/> 71.7 <hr/>	<hr/> 291.9 <hr/>

Liabilities classified as held for sale	2005	2004
	£m	£m
Disposal group held for sale		
Trade and other creditors	7.0	24.5
Provisions	0.2	0.8
Other creditors	-	0.6
Deferred taxation	-	3.6
Pension liabilities	5.7	23.6
	<hr/> 12.9 <hr/>	<hr/> 53.1 <hr/>

Notes *(continued)*

5 Profit for the year

	2005	2004
	£m	£m
<i>Profit for the year (excluding interest and taxation) is stated after charging:</i>		
Auditors' remuneration:		
Group - audit	0.4	0.4
- fees paid to the auditors and their associates in respect of other services	0.6	0.6
Depreciation and other amounts written off tangible fixed assets		
Owned	23.4	25.6
Leased	-	1.1
Impairment of tangible and intangible fixed assets	-	22.2
Impairment of investment in joint controlled entities	3.6	7.2
Amortisation of intellectual property rights	0.3	1.5
Operating leases		
Land and buildings	0.5	0.3
Research and development expenditure	26.3	45.4
<i>after crediting:</i>		
Exchange gains	-	32.1
Government grants	0.3	1.2
	0.3	32.1

Notes (continued)

6 Remuneration of directors

	2005	2004
	£000	£000
Directors' emoluments	1,435	1,179

The aggregate emoluments of the highest paid director were £551,182 for the year ended 31 December 2005 (2004: £522,313) and company pension contributions of £12,672 (2004: £12,240) were made to a money purchase scheme on his behalf.

	Number of directors	
	2005	2004
Retirement benefits are accruing to the following number of directors under:		
Money purchase schemes	2	2
Defined benefit schemes	3	1
	2005	2004
	£000	£000
Compensation to directors for loss of office	1,980	-

7 Staff numbers and costs

The average number of persons employed by the company (including directors) during the year, analysed by business segment, was as follows:

	Number of employees	
	2005	2004
Biotechnology	525	562
Discontinued	335	1,825
Other	36	140
	896	2,527

The aggregate payroll costs of these persons were as follows:

	2005	2004
	£m	£m
Wages and salaries	52.2	89.6
Social security costs	4.1	9.4
Other pension costs	7.7	11.2
	64.0	110.2
Other employment costs		
Severance costs	10.4	10.1
Post retirement costs	0.6	0.8
	11.0	10.9
	75.0	121.1

Notes *(continued)*

8 Finance income

	2005 £m	2004 £m
Exchange gains	0.3	32.1
On bank deposits	1.8	0.7
Other	-	0.1
Income from parent company	0.6	-
Income from current asset investment	-	0.2
Pension income	12.0	14.0
	14.7	47.1
	14.7	47.1

9 Finance costs

	2005 £m	2004 £m
Exchange losses	12.6	1.9
On bank loans and overdrafts	0.6	6.8
On all other loans	26.7	34.2
Amortisation of finance fees	9.1	10.2
Finance charges in respect of pensions	13.0	16.1
Finance charges in respect of provisions	0.5	0.8
Finance charges payable in respect of finance leases and hire purchase contracts	0.1	0.3
Dividends on redeemable preference shares	6.8	6.6
	69.4	76.9
	69.4	76.9

Notes (continued)

10 Taxation

Analysis of charge in year

	2005	2004
	£m	£m
<i>UK corporation tax</i>		
Current tax on income for the year	-	-
Adjustments in respect of prior years	-	-
	<hr/>	<hr/>
	-	-
Overseas taxation	2.9	1.3
	<hr/>	<hr/>
Total current tax charge	2.9	1.3
Deferred taxation	(1.3)	0.6
	<hr/>	<hr/>
Tax on profit on ordinary activities	1.6	1.9
	<hr/> <hr/>	<hr/> <hr/>

The total tax expense differs from the amount computed by applying the UK rate of 30% to income before tax as a result of the following:

	2005	2004
	£m	£m
<i>Current tax reconciliation</i>		
Profit on ordinary activities before tax (including £135.0m of discontinued profit (2004: £92.6m))	41.6	33.5
	<hr/>	<hr/>
Taxation charge at United Kingdom corporation tax rate of 30% for the year ended 31 December 2005 (2004: 30%)	12.5	10.1
Overseas tax rates	0.3	3.2
Other	(11.2)	(11.4)
	<hr/>	<hr/>
Taxes on income from ordinary activities	1.6	1.9
	<hr/> <hr/>	<hr/> <hr/>

At 31 December 2005 there were £133.3 million of UK tax losses to be carried forward with no expiration date (2004: £86.9 million). In addition, at that date, the group had US\$ 28.0million of US federal tax net operating losses which expire in years 2019 to 2022 (2004: \$30.7 million). No deferred tax asset was recognised in respect of these losses which results in the lower effective tax rate for the group.

Notes (continued)

10 Taxation (continued)

Factors affecting the tax charge for the current year

The current tax charge for the period is lower (2004 : lower) than the standard rate of corporation tax in the UK 30%, (2004: 30%). The differences are explained below.

	2005	2004
	£m	£m
<i>Current tax reconciliation</i>		
Profit on ordinary activities before tax	41.6	33.5
	<hr/>	<hr/>
Current tax at 30% (2004: 30%)	12.5	10.1
<i>Effects of:</i>		
Expenses not deductible for tax:		
Depreciation for the period in excess of capital allowances	2.3	1.6
Disallowable items	4.6	-
Non taxable income	-	(2.9)
Generation of additional tax losses in the year	0.2	2.9
Higher rates on overseas earnings	0.3	3.2
Tax losses utilised	(19.9)	(9.9)
State taxes	0.1	0.2
Profit in inventory	0.4	(1.8)
Previous year adjustment	-	(2.2)
Prior period taxation relating to Stahl Iberica, see note 24	2.5	-
R&D tax credits	(0.1)	(0.3)
Dividends not taxable	-	0.4
	<hr/>	<hr/>
Total current tax charge (see above)	2.9	1.3
Deferred tax (credit)/charge for the period	(1.3)	0.6
	<hr/> <hr/>	<hr/> <hr/>
Deferred taxation		
Profit in inventory	(0.2)	0.2
Unremitted earnings	(0.6)	0.6
Other timing differences	(0.5)	(0.2)
	<hr/> <hr/>	<hr/> <hr/>
Total deferred taxes	(1.3)	0.6
	<hr/> <hr/>	<hr/> <hr/>
Taxes on income from ordinary activities	1.6	1.9
	<hr/> <hr/>	<hr/> <hr/>

All current and deferred income tax expense for the year is attributable to foreign operations.

Analysis of loss on ordinary activities before taxation:

	2005	2004
	£m	£m
UK activities	37.0	11.1
Non UK activities	4.6	22.4
	<hr/>	<hr/>
	41.6	33.5
	<hr/> <hr/>	<hr/> <hr/>

Notes *(continued)*

11 Intangible fixed assets

Group

	Goodwill	Intellectual	Total
	£m	Property rights	£m
		£m	
<i>Cost</i>			
Balance at 1 January 2004	341.6	16.7	358.3
Additions	-	0.1	0.1
Disposals	(4.7)	(0.1)	(4.8)
Transfers to assets held for sale	(260.1)	(13.2)	(273.3)
Translation adjustments	(6.3)	(0.2)	(6.5)
Balance at 31 December 2004	70.5	3.3	73.8
Balance at 1 January 2005	70.5	3.3	73.8
Additions	-	-	-
Disposals	(12.8)	(2.1)	(14.9)
Transfers to assets held for sale	(28.7)	-	(28.7)
Translation adjustments	(0.6)	0.2	(0.4)
Balance at 31 December 2005	28.4	1.4	29.8
<i>Amortisation</i>			
Balance at 1 January 2004	113.4	6.6	120.0
Charge for year	-	1.5	1.5
Impairment	-	0.1	0.1
Disposals	(1.7)	-	(1.7)
Transfers to assets held for sale	(79.7)	(5.2)	(84.9)
Translation adjustments	(1.7)	(0.2)	(1.9)
Balance at 31 December 2004	30.3	2.8	33.1
Balance at 1 January 2005	30.3	2.8	33.1
Charge for year	-	0.3	0.3
Transfers to assets held for sale	(11.0)	-	(11.0)
Disposals	(12.8)	(2.0)	(14.8)
Translation adjustments	1.3	-	1.3
Balance at 31 December 2005	7.8	1.1	8.9
<i>Carrying amounts</i>			
At 1 January 2004	228.2	10.1	238.3
At 31 December 2004	40.2	0.5	40.7
At 1 January 2005	40.2	0.5	40.7
At 31 December 2005	20.6	0.3	20.9

Notes *(continued)*

11 Intangible fixed assets *(continued)*

The following units have significant carrying amounts of goodwill :

	31 December 2005 £m	31 December 2004 £m
Biotechnology	20.6	21.6
Inkjet	-	18.6
	<u>20.6</u>	<u>40.2</u>

The following goodwill amounts are included in "Assets held for Sale"

	31 December 2005 £m	31 December 2004 £m
Inkjet	17.7	-
OSC	-	8.9
NeoResins	-	154.0

The goodwill has been tested for impairment by comparing carrying values to the recoverable amounts. In 2005 the sales prices for the above units have been used as a basis for determining the recoverable amounts. The recoverable amounts exceeded the carrying value of the units.

In 2004, the recoverable amounts of the units were determined using value in use calculation. The calculation used cashflow projections based upon actual operating results and the five year business plan. Cashflows were discounted at a rate of 16%. Following the review, goodwill of £17.4m and £4.8m was written off with respect to the Fine Chemicals and Pharmaceuticals businesses.

Notes (continued)

12 Property, plant and equipment

	Land and buildings	Plant and equipment	Assets in the course of construction	Total
	£m	£m	£m	£m
<i>Cost or valuation</i>				
At 1 January 2004	54.8	315.8	59.9	430.5
Additions	0.1	3.0	12.1	15.2
Disposals	(3.6)	(31.7)	(0.6)	(35.9)
Transfers	2.6	50.1	(52.7)	-
Transfers to assets held for sale	(32.7)	(53.7)	(10.7)	(97.1)
Translation adjustments	(2.4)	(5.8)	(0.8)	(9.0)
At 31 December 2004	18.8	277.7	7.2	303.7
At 1 January 2005	18.8	277.7	7.2	303.7
Additions	-	0.3	7.4	7.7
Disposals	(12.5)	(101.3)	(0.3)	(114.1)
Transfers	0.2	6.5	(6.7)	-
Transfers to assets held for sale	(2.6)	(25.4)	(4.7)	(32.7)
Translation adjustments	2.2	5.3	0.1	7.6
At 31 December 2005	6.1	163.1	3.0	172.2
<i>Depreciation and impairment losses</i>				
At 1 January 2004	7.8	159.5	-	167.3
Charge for year	2.8	23.9	-	26.7
Impairment	1.1	21.1	-	22.2
Disposals	(0.2)	(9.2)	-	(9.4)
Transfers to assets held for sale	(10.3)	(34.3)	-	(44.6)
Translation adjustments	(1.0)	(3.6)	-	(4.6)
At 31 December 2004	0.2	157.4	-	157.6
At 1 January 2005	0.2	157.4	-	157.6
Charge for year	0.3	23.1	-	23.4
Disposals	-	(78.0)	-	(78.0)
Transfers to assets held for sale	-	(6.0)	-	(6.0)
Translation adjustments	0.1	3.3	-	3.4
At 31 December 2005	0.6	99.8	-	100.4
<i>Carrying amounts</i>				
At 1 January 2004	47.0	156.3	59.9	263.2
At 31 December 2004	18.6	120.3	7.2	146.1
At 1 January 2005	18.6	120.3	7.2	146.1
At 31 December 2005	5.5	63.3	3.0	71.8

Notes *(continued)*

12 Property, plant and equipment (continued)

The carrying amounts of land and buildings comprises:

	2005	2004
	£m	£m
Freehold	4.0	17.2
Long leasehold	1.5	1.4
	<hr/> 5.5 <hr/>	<hr/> 18.6 <hr/>

The cost of land and buildings include £5.9 million of depreciable assets at 31 December 2005 (*2004: £17.2 million*).

Included in the total net book value of land and buildings is £Nil in respect of assets held under finance leases at 31 December 2005 (*2004: £0.7 million*). Depreciation for the year ended 31 December 2005 on these assets was £Nil (*2004: £0.1 million*). In respect of plant and equipment the net book value of assets held under finance leases is £Nil (*2004: £3.9 million*). Depreciation on these assets was £0.3 million (*2004: £3.9 million*).

Depreciation was not charged on land with a cost of £0.2 million included in land and buildings during the year ended 31 December 2005 (*2004: £1.4 million*).

Notes (continued)

13 Investment in jointly controlled entities

Group

	2005 £m	2004 £m
<i>Cost</i>		
At beginning of year		
Goodwill	12.9	14.1
Exchange movements on goodwill	-	(1.3)
Share of net assets	9.1	9.8
Translation adjustments	0.3	(0.3)
Capital contributions	(0.1)	(0.3)
Transfer to assets held for sale	(22.2)	-
	-	22.0
At end of year	-	22.0
<i>Share of post acquisition reserves</i>		
At beginning of year	(1.2)	(0.3)
Retained profit less losses	(0.1)	1.1
Dividends received	(0.1)	(2.0)
Transfer to assets held for sale	1.4	-
	-	(1.2)
At end of year	-	(1.2)
<i>Amortisation</i>		
At beginning of year	(12.9)	(4.8)
Charged for year	-	(0.9)
Impairment	(3.6)	(7.2)
Transfer to assets held for sale	16.5	-
	-	(12.9)
At end of year	-	(12.9)
<i>Net book value</i>		
At 31 December	-	7.9

Net book value of £7.9 million comprised of assets of £7.9 million and goodwill of £Nil in 2004.

The value of the investment in joint ventures has been tested for impairment by comparing carrying values to the recoverable amounts. In 2005 the sales prices for the investment has been used as a basis for determining the recoverable amount. An impairment of £3.6m was taken in 2005.

In 2004, the recoverable amount was determined using value in use calculation. The calculation used cashflow projections based upon actual operating results and the five year business plan. Cashflows were discounted at a rate of 16%. Following the review, an impairment of £7.2m was taken against the value of the investment.

Notes (continued)

13 Investment in jointly controlled entities (continued)

Joint controlled entities	Country of incorporation	Principal activity	Percentage of equity owned %
Image Polymers Europe	UK	Chemical manufacture	50*
Image Polymers Company	USA	Chemical manufacture	50*

* all ordinary shares held

Image Polymers Europe and Image Polymers Company were partnerships with the Mitsui Chemicals group and the group held a 50% interest in each of these partnerships. On 31st March 2006, the group sold these partnership interests to the Mitsui Chemicals group and thereby ceased to have any further interest in the partnerships.

Joint controlled entities

The following information is relevant to an undertaking of the investments in joint controlled entities.

The amounts included in respect of joint controlled entities comprise the following:

	Assets £m	Liabilities £m	Equity £m	Revenues £m	(Loss)/Profit £m
2005					
Image Polymers Europe	5.5	(0.5)	5.0	2.7	(0.1)
Image Polymers Company	4.1	(1.1)	3.0	4.6	0.0
	9.6	(1.6)	8.0	7.3	(0.1)
	9.6	(1.6)	8.0	7.3	(0.1)
2004					
Image Polymers Europe	5.7	(0.6)	5.1	3.6	0.4
Image Polymers Company	3.9	(1.1)	2.8	5.3	0.7
	9.6	(1.7)	7.9	8.9	1.1
	9.6	(1.7)	7.9	8.9	1.1

An impairment loss amounting to £3.6m in respect of Image Polymers Europe and Image Polymers Company was recognised during the year owing to expected future returns falling below the carrying value of the investments.

Notes *(continued)*

14 Inventories

	2005	2004
	£m	£m
Raw materials and consumables	4.0	21.0
Work in progress	1.2	6.7
Finished goods and goods for resale	2.0	5.6
	<u>7.2</u>	<u>33.3</u>
	<u>1.9</u>	<u>1.1</u>
Inventories stated at fair values less costs to sell		

Notes *(continued)*

15 Trade and other receivables

	2005 £m	2004 £m
Trade receivables	10.1	28.2
Other receivables	5.6	3.6
Prepayments and accrued income	1.8	3.7
Amounts receivable from joint ventures	0.1	0.4
	17.6	35.9
	17.6	35.9

16 Trade and other payables

	2005 £m	2004 £m
Trade payables	20.6	31.7
Other taxation and social security	0.9	5.1
Other payables	1.9	2.2
Accruals and deferred income	11.5	18.3
	34.9	57.3
	34.9	57.3

17 Other payables

	2005 £m	2004 £m
Other payables	0.2	0.4
Accruals and deferred income	-	1.2
	0.2	1.6
	0.2	1.6

18 Financial liabilities

	2005 £m	2004 £m
Current liabilities :		
Redeemable preference share dividend	3.5	3.2
Bank loans and overdrafts	-	72.9
Finance lease liabilities	-	0.7
	3.5	76.8
Non-current liabilities :		
High yield bonds	70.3	272.6
Redeemable preference shares <i>(see note 22)</i>	39.0	34.4
Finance lease liabilities	-	3.7
	109.3	310.7
Total financial liabilities (see note 19)	112.8	387.5

Notes (continued)

18 Financial liabilities (continued)

The above figures include preference shares, the redemption of which is mandatory on 1 July 2010. They may, however, be redeemed at the option of the company on or after 1 January, 2006 or earlier on certain public equity offerings at a redemption value equal to the liquidation preference value (\$25 per share) plus all accumulated and unpaid dividends to the date of redemption. On 5 July 2006 the company redeemed 1,822,489 of the Redeemable preference shares at a total cost of US\$ 48,056,048, leaving 1,200,000 of the Redeemable preference shares in issue.

High yield bond

In 1999, the company had issued high yield bonds repayable in 2009 and with interest fixed at 11%. The difference between net and gross repayable is unamortised fees. The high yield bond was guaranteed by Avecia Corporation Limited. Payments under the guarantee were subordinated to the guarantor's payment of its obligations under the term loan agreements. Under the terms of the bond, Avecia Group plc and certain of its subsidiaries were subject to restrictions over the sale of assets unless certain, specified conditions are met.

All of the outstanding high yield bonds were repaid by the company on 23 March 2006.

The above liability is net of unamortised fees of £2.0m (2004 £6.2m).

Bank loans and overdrafts

The group has repaid its outstanding term loans during the course of the year. Under the conditions of the term loans entered into by the group, Avecia Corporation Limited, a wholly owned subsidiary of the company, and certain of its subsidiaries had guaranteed the obligations of each other. In addition, the various obligations under the credit agreement were secured by security interests created over certain of the assets of Avecia Corporation Limited and its subsidiaries.

The agreement entered into by Avecia Corporation Limited and Avecia Investments Limited with the lenders of the term loans contained customary events of default and various restrictive covenants. These covenants placed restriction on the actions of Avecia Investments Limited and its subsidiaries, in particular in relation to the payment of dividends and other specified payments to Avecia Corporation Limited or any of its holding companies, other than in certain specific circumstances. The credit agreement also contained financial covenants, including maintenance of financial ratios, including among others:

- A ratio of consolidated EBITDA to consolidated net interest charges
- A ratio of adjusted cash flow to relevant expenditure
- A ratio of net senior debt to consolidated EBITDA
- A maximum limitation on capital expenditure

These obligations ceased on repayment of the outstanding term loans.

Notes (continued)

18 Financial liabilities (continued)

Finance lease liabilities

The maturity of obligations under finance leases and hire purchase contracts is as follows:

	2005	2004
	£m	£m
Within one year	-	1.0
Between one and two years	-	0.9
Between two and three years	-	0.8
Between three and four years	-	0.8
Between four and five years	-	0.8
Over five years	-	1.2
	<hr/>	<hr/>
	-	5.5
Less: future finance charges	-	(1.0)
	<hr/>	<hr/>
	-	4.5
	<hr/> <hr/>	<hr/> <hr/>

The finance leases held by the group were disposed of as part of the sale of the Fine Chemicals business during 2005. At 31 December 2005, £Nil (2004: £nil) of borrowings falling due after more than one year were secured on assets of the group.

Borrowing facilities

The group had no committed borrowing facilities available to it at 31 December 2005. The undrawn committed facilities available at 31 December 2004 were as follows:

	2005	2004
	£m	£m
Expiring in one year or less	-	71.8
Expiring in more than one year but not more than two years	-	-
Expiring in more than two years	-	-
	<hr/>	<hr/>
	-	71.8
	<hr/> <hr/>	<hr/> <hr/>

Notes (continued)

19 Borrowings, financial instruments and risk management

The group's treasury department manages the group's funding, liquidity and exposure to interest rates and foreign exchange rate risks.

The group holds or issues financial instruments for two main purposes:

- to finance its operations;
- to manage the interest rate and currency risks arising from its operations and from its sources of finances.

In addition, various financial instruments – for example, trade debtors, trade creditors, accruals and prepayments – arise directly from the group's operations.

The group financed its operations by a mixture of bank borrowings, high yield bonds and redeemable preference shares. The group's long term loans were raised centrally by group finance companies which funded operating subsidiaries, on commercial terms, all of which are included in the consolidated financial statements. During 2005 and the first three months of 2006 the group has repaid all bank borrowings and the high yield bonds from proceeds arising on the disposal of businesses.

The group now finances its operations by a combination of redeemable preference shares and cash retained from proceeds arising on the disposal of businesses.

All derivatives previously used for interest rate management have matured.

The main risks arising from the group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and market price risk. The board reviews and agrees policies for managing each of these risks and they are summarised below. These policies have remained unchanged since incorporation.

Liquidity risk

Group policy is to match currency cash expenditure with currency cash income subject to the existence of a free market for that currency's debt and differences in funding costs between markets. Group borrowings comprise bank debt of £Nil million (2004: £72.9 million) and a High Yield Bond of £70.3 million (2004: £271.2 million) due in 2009, both shown net of unamortised fees, 3% (2004: 25%) of the group's total borrowings at the year end will become due in the next 12 months, 97% (2004: 75%) in more than two years and 0% (2004: 0%) will become due in more than five years.

At 31 December 2005, the group had no undrawn committed borrowing facilities (2004: £71.8 million). Commitment fees are paid on the undrawn portion of these facilities. In March 2006 the group redeemed all the outstanding High Yield Bonds.

Finance and interest rate risk

Having repaid all variable rate debt, the group is no longer exposed to interest rate fluctuations on borrowings. At the year end, after taking account of interest rate swaps, the proportion of the group's borrowings at fixed rates was 100% (2004: 100%).

Notes *(continued)*

19 Borrowings, financial instruments and risk management *(continued)*

Effective interest rate and repricing analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and periods in which they reprice.

	Effective Interest Rate	Total	2005				
			6 months or less	6-12 months	1-2 years	2-5 years	More than 5 years
Cash and cash equivalents	4.3%	49.1	49.1	-	-	-	-
Unsecured bond issues	11%	(70.3)	-	-	-	(70.3)	-
Redeemable preference shares	16%	(42.5)	-	-	-	(42.5)	-
Finance lease liabilities		-	-	-	-	-	-
		<u>(63.7)</u>	<u>49.1</u>	<u>-</u>	<u>-</u>	<u>(112.8)</u>	<u>-</u>

	Effective Interest Rate	Total	2004				
			6 months or less	6-12 months	1-2 years	2-5 years	More than 5 years
Cash and cash equivalents		22.7	22.7	-	-	-	-
Secured Bank loans	-	(72.9)	-	(72.9)	-	-	-
Unsecured bond issues	11%	(272.6)	-	-	-	-	(272.6)
Redeemable preference shares	16%	(37.6)	-	-	-	-	(37.6)
Finance lease liabilities	7.8%	(3.7)	-	-	-	-	(3.7)
		<u>(364.1)</u>	<u>22.7</u>	<u>(72.9)</u>	<u>-</u>	<u>-</u>	<u>(313.9)</u>

Included within liabilities classified as held for sale in 2004 were finance liabilities of £0.7 million with an effective interest rate of 7.8% due after more than five years.

Notes (continued)

19 Borrowings, financial instruments and risk management (continued)

Currency risk

The group publishes its financial statements in pounds sterling and conducts businesses in many foreign currencies. As a result, it is subject to foreign currency exchange risk due to exchange rate movements which will affect the group's transaction costs and revenues, and the translation of the results and underlying net assets of its subsidiaries. By holding borrowings in foreign currencies, the group hedges a substantial portion of its exposure to fluctuations on the translation into pounds sterling of its foreign currency net assets.

The group hedges, on a rolling 12 month basis, the translation of a proportion of its forecast future net cash flow denominated in US Dollars (50%), Euro (50%) and Japanese Yen (75%) with forward foreign currency contracts. This limits in part the transactional exposure of the group's net cash flow to movements in exchange rates. The fair value of forward contracts is recognised on the balance sheet and the gain or loss on the hedge is recognised at the same time as the underlying transaction.

At 31 December 2005 the group had £3.3 million of outstanding gross foreign exchange contracts as a result of the transaction exposure cover outlined above; all were to sell Japanese Yen. All outstanding foreign exchange contracts at the end of 2005 matured during 2006. No further foreign exchange contracts have been entered into.

At 31 December 2004 the group had £16.2 million of outstanding gross foreign exchange contracts as a result of the transaction exposure cover outlined above. Of the total £2.0 million were to sell US dollars, £9.9 million were to sell Japanese Yen, £4.3 million were to buy US dollars.

Notes *(continued)*

19 Borrowings, financial instruments and risk management *(continued)*

Currency exposures

At 31 December 2005 the net monetary assets and liabilities denominated in currencies other than the functional currencies of the group companies (other than certain non sterling borrowings treated as hedges of net investments in overseas operations) were as follows:

Functional currency of group operation	Sterling	US dollar	Euro	Japanese yen	Other	Total
	£m	£m	£m	£m	£m	£m
Sterling	-	(30.3)	-	1.0	-	(29.3)
US dollar	-	71.1	-	-	-	71.1
Euro	-	-	-	-	-	-
	-	40.8	-	1.0	-	41.8
	-	40.8	-	1.0	-	41.8

At 31 December 2004, the net monetary assets and liabilities denominated in currencies other than the functional currencies of the group companies (other than certain non sterling borrowings treated as hedges of net investments in overseas operations) were as follows:

Functional currency of group operation	Sterling	US dollar	Euro	Japanese yen	Other	Total
	£m	£m	£m	£m	£m	£m
Sterling	-	(236.1)	1.3	0.3	2.8	(231.7)
US dollar	-	64.9	-	-	-	64.9
Euro	-	-	23.0	-	-	23.0
	-	(171.2)	24.3	0.3	2.8	(143.8)
	-	(171.2)	24.3	0.3	2.8	(143.8)

Credit risk and market risk

The above financial instruments are subject to credit and market risk. Avecia contains credit risk by ongoing review procedures. All financial instruments are transacted with commercial banks. The notional principal values of balance sheet financial instruments do not represent amounts exchanged by the parties and are not a measure of the credit risk to the group of these instruments. The credit risk of these instruments is limited to the positive fair values of such contracts. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet.

Market risk is the sensitivity of the value of financial instruments to changes in related currency and interest rates. The group is not exposed to material market risk because gains and losses on the derivative financial instruments are largely offset by gains and losses on the underlying assets, liabilities and transactions subject to hedge.

Notes *(continued)*

19 Borrowings, financial instruments and risk management *(continued)*

Fair values of financial assets and financial liabilities

Set out below is a comparison by category of book values and fair values of all the group's financial assets and financial liabilities as at 31 December 2005:

	2005	2005	2004	2004
	Carrying	Fair value	Carrying	Fair value
	amount		Amount	
	£m	£m	£m	£m
Short term borrowings and current portion of long term borrowings	-	-	(72.9)	(72.9)
High yield bonds	(70.3)	(74.5)	(272.9)	(294.7)
Payment in kind preference shares	(42.5)	(47.2)	(37.6)	(61.2)
Finance lease	-	-	(4.4)	(4.4)
Other financial assets	0.2	0.2	(6.4)	(6.4)
Cash and cash equivalents	49.1	49.1	22.7	22.7
Forward foreign currency contracts – assets	0.2	0.2	0.2	0.2
Forward foreign currency contracts – liabilities	-	-	(0.3)	(0.3)
	<hr/> (63.3) <hr/>	<hr/> (72.2) <hr/>	<hr/> (371.6) <hr/>	<hr/> (417.0) <hr/>

Market values have been used to determine the fair value of forward foreign currency contracts and all listed debt issued. The fair values of all other items have been calculated by discounting expected future cash flows at 31 December 2005 LIBOR interest rates.

Fair value judgements and changes in market conditions and assumptions could significantly affect these estimates. The disclosed values of those which are representative of fair values at the dates indicated. No financial instruments were held for the purpose of dealing or other financial instrument trading activities.

Notes *(continued)*

20 Provisions for liabilities and charges

	Pensions and similar obligations £m	Reorganisation and other provisions £m	Total £m
1 January 2005	0.3	9.6	9.9
Charge for the year	-	11.3	11.3
Utilised during year	-	(8.9)	(8.9)
Disposals	-	(3.2)	(3.2)
Liabilities included in disposal groups	(0.2)	-	(0.2)
Exchange	(0.1)	-	(0.1)
	<hr/>	<hr/>	<hr/>
At 31 December 2005	-	8.8	8.8
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
Non-current	-	0.3	0.3
Current	-	8.5	8.5
	<hr/>	<hr/>	<hr/>
	-	8.8	8.8
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

The reorganisation and other provisions primarily relate to severance costs these are expected to be fully paid out by the end of January 2007.

Notes (continued)

21 Deferred taxation

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2005 £m	2004 £m	2005 £m	2004 £m	2005 £m	2004 £m
Property, plant and equipment	-	-	-	1.1	-	1.1
Intangible assets	-	-	0.3	0.6	0.3	0.6
Inventories	-	-	-	0.2	-	0.2
Interest-bearing loans and borrowings	-	-	-	-	-	-
Employee benefits	(0.1)	-	-	2.2	(0.1)	2.2
Impairment of investments	-	-	-	1.0	-	1.0
Other items	(0.1)	(0.1)	-	0.6	(0.1)	0.5
Tax value of loss carry-forwards recognised	-	-	-	-	-	-
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Tax(assets)/liabilities	(0.2)	(0.1)	0.3	5.7	0.1	5.6
Set off of tax	0.2	0.1	(0.2)	(0.1)	-	-
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Net tax liabilities	-	-	0.1	5.6	0.1	5.6
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>

The 2004 liabilities include £3.6m included in "assets held for sale".

Unrecognised deferred tax assets

Deferred tax assets have not been recognised in respect of the following items:

	2005 £m	2004 £m
Accelerated capital allowances	7.8	1.2
Short term timing differences	2.7	3.4
Long term timing differences	10.6	10.3
Tax losses	44.9	30.9
	<hr/>	<hr/>
	66.0	45.8
	<hr/>	<hr/>

Movement in temporary differences during the year

	Balance 1 Jan 05 £m	Recognised in income £m	Recognised in equity £m	Balance 31 Dec 05 £m
Property, plant and equipment	1.1	1.1	-	-
Intangible assets	0.6	0.4	-	0.2
Inventories	0.2	0.2	-	-
Employee benefits	2.2	2.3	-	(0.1)
Impairment of investments	1.0	1.0	-	-
Other items	0.5	0.5	-	-
	<hr/>	<hr/>	<hr/>	<hr/>
	5.6	5.5	-	0.1
	<hr/>	<hr/>	<hr/>	<hr/>

Notes (continued)

21 Deferred taxation (continued)

	Balance 1 Jan 04	Recognised in income	Recognised in equity	Balance 31 Dec 04
	£m	£m	£m	£m
Property, plant and equipment	1.3	(0.2)	-	1.1
Intangible assets	1.0	(0.4)	-	0.6
Inventories	-	0.2	-	0.2
Employee benefits	2.7	(0.5)	-	2.2
Impairment of investments	0.2	0.8	-	1.0
Other items	-	0.5	-	0.5
	5.2	0.4	-	5.6
	5.2	0.4	-	5.6

22 Called up share capital

	2005 Number of shares	2005 Nominal value of shares £'000	2004 Number of shares	2004 Nominal value of shares £'000
Authorised				
Equity: ordinary shares of £1 each	400,000,000	400,000	400,000,000	400,000
Non equity – Pay-in-Kind (PIK) 16% cumulative redeemable preference shares of \$1 each	3,500,000	2,222	3,500,000	2,222
	403,500,000	402,222	403,500,000	402,222
	403,500,000	402,222	403,500,000	402,222
Allotted, called up and fully paid				
Equity: ordinary shares of £1 each	329,100,001	329,100	329,100,001	329,100
	329,100,001	329,100	329,100,001	329,100
Non equity – Pay-in-Kind (PIK) 16% cumulative redeemable preference shares of \$1 each	3,022,489	1,751	3,022,489	1,561
	3,022,489	1,751	3,022,489	1,561
	3,022,489	1,751	3,022,489	1,561

Redeemable preference shares

The redemption of preference shares is mandatory on 1 July 2010 but they may be redeemed at the option of the company on or after 1 January 2005 or earlier on certain public equity offerings at a redemption value equal to the issue price of \$25 per share plus all accumulated and unpaid dividends to the date of redemption. In addition, on redemption prior to 1 January 2008, a redemption premium is payable in accordance with the Company's articles of association. On winding up the preference shares rank in priority to ordinary shares.

Up to 1 July 2004 the company was able to issue further preference shares instead of a cash dividend (based on the issue price of \$25 per share). After 1 July 2004 this option was no longer available and subsequent dividends became payable in cash. All dividends on the preference shares payable during the year ended 31 December 2005 were paid in full in cash when due. Since 31 December 2005 however, the company was unable to pay in cash the dividend due in January 2006 because it did not have adequate distributable reserves for this purpose.

Subject to certain exceptions contained in the articles of association, the preference shares have no voting rights at meetings of the ordinary shareholders. They attract a dividend rate of 16% but, during any period where dividends due are unpaid, a further 2% default rate is also payable. The carrying value of the preferred shares is being increased from the date of issue to the mandatory redemption date, by the interest method, such that the carrying value at the mandatory redemption date will equal the redemption value of \$25 per share. The accretion for 2005 was £0.1 million (2004: £0.1 million).

Notes (continued)

23 Share capital and reserves

Group

	Share capital £m	Translation reserve £m	Hedging Reserve £m	Reserve for own shares £m	Retained earnings £m	Total £m
At 1 January 2004	329.1	(6.7)	(9.1)	-	(331.0)	(17.7)
Total recognised income and expense	-	6.6	(10.4)	-	21.1	17.3
Own shares acquired	-	-	-	(0.3)	-	(0.3)
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
At 31 December 2004	329.1	(0.1)	(19.5)	(0.3)	(309.9)	(0.7)
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
At 1 January 2005	329.1	(0.1)	(19.5)	(0.3)	(309.9)	(0.7)
Total recognised income and expense	-	(1.2)	6.1	-	31.9	36.8
Capital contribution from parent	-	-	-	-	27.0	27.0
Own shares acquired	-	-	-	(0.4)	-	(0.4)
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
At 31 December 2005	329.1	(1.3)	(13.4)	(0.7)	(251.0)	62.7
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations that are not integral to the operations of the company.

Hedging reserve

The hedging reserve comprises the effective portion of the net investment hedge between borrowings and foreign currency net assets.

Reserve for own shares

The reserve for the company's own shares comprises the cost of the company's shares held by the group.

24 Contingent liabilities and contingent assets

Environmental

On the acquisition by the group of the speciality chemicals business of the AstraZeneca group in 1999, the group acquired all the sites of that business which were then in operation or use. Sites which were formerly part of the speciality chemicals business but which were not in operation at the date of its acquisition by the group were not transferred to the group. Since the acquisition of the speciality chemicals business in 1999, the group has disposed of its interest in most of its major operational sites, including the group's former sites at St. Clair du Rhone (France), Mount Pleasant (Tennessee), Grangemouth (UK), Huddersfield (UK), Waalwijk (The Netherlands) and Parets (Spain). Since 31 December 2005, the group has also disposed of its interest at the New Castle (Delaware) site and now retains only operational sites at Billingham (UK), Blackley (UK) and Milford (Massachusetts). The group has actual or potential environmental liabilities in respect of its current or former sites and is subject to contingencies pursuant to laws and regulations which in the future may require it to take action to correct the effects on the environment of the prior disposal, release or escape of chemical substances

An Environmental Deed of Covenant entered into by companies in the AstraZeneca group, notably Zeneca Limited (as a principal seller of the business to the group) and AstraZeneca plc (as guarantor), on the group's acquisition of AstraZeneca's speciality chemicals business, provides certain indemnities to and by group companies for

Notes (continued)

24 Contingent liabilities and contingent assets (continued)

environmental liabilities and costs arising from events or circumstances existing prior to the acquisition. These include liabilities relating to or arising out of pre-acquisition contamination at sites which were transferred to group companies in 1999 but which have subsequently been disposed of. These also include historic liabilities arising on any sites previously owned by companies acquired by the group in the course of the acquisition transaction but where the sites in question were not themselves part of the acquisition transaction. The liability of the AstraZeneca group to indemnify group companies in respect of these matters is, subject to certain exceptions, subject to maximum caps of liability, de minimis levels of liability, time limits for claims to be made and/or contributions by group companies. Where time limits or caps on liability apply, on the expiry of the relevant time limit or if the environmental liabilities and costs exceed the relevant cap, the environmental liabilities and costs, or excess thereof, would be the responsibility of group companies. On the disposal of relevant businesses out of the group, where purchasers have assumed liabilities which may be subject to indemnity from the AstraZeneca group under the Environmental Deed or which may otherwise be the responsibility of group companies under the deed, the benefits and obligations under the Environmental Deed have, insofar as they relate to the sold businesses or sites, been assigned to the purchasers subject to appropriate limitations on the maximum amounts which the purchasers may claim under the Environmental Deed.

While the outcome of some of these matters cannot be readily foreseen, the directors believe that they will be disposed of without material effect on the financial position as shown in these consolidated financial statements.

The ultimate requirement for remediation work and its cost are difficult to estimate. However, where such costs are not within the scope of the indemnities provided by the deed of covenant referred to above, and where such costs are deemed probable and identifiable, provision has been made in the financial statements.

Litigation and other claims

Various companies in the group are parties to legal actions and claims by third parties, regulatory and fiscal authorities. While the outcome of some of these matters cannot be readily foreseen, the directors believe that they will be disposed of without material effect on the financial position as shown in these consolidated financial statements.

Excise Duties Inspection, Spain

During 2003, the Spanish tax authority carried out a tax inspection of the quantity of alcohol used by Avecia Spain SL (Avecia Spain) exempt from excise duties, compared with its authorization. The period covered was 1999 to 2002. The tax inspector came to the view that Avecia Spain had exceeded its authority limit for each year and issued an assessment for the excise duty arising from that excess. The final amount of the assessment was €4.2 million. Avecia Spain appealed against the assessment to the Administrative Tribunal. In November 2004, Avecia Spain heard that the Tribunal had not accepted the appeal. Avecia Spain therefore submitted a further appeal to the Court of Justice. A decision on this further appeal is not expected for many months.

On 2 February 2005, Avecia Spain was purchased by Koninklijke DSM NV ("DSM") as part of the NeoResins business disposal by the Avecia group. Under Paragraph 3.1.2 of the Tax Deed to the disposal, DSM accepted responsibility for any liability arising from the assessment. The liability of the Avecia group ceased at that point.

Corporate Tax Audit, Avecia Spain

During 2003 and 2004, the Spanish tax authority carried out a corporate tax audit at Avecia Spain. As a result the tax inspector decided that the merger transaction undertaken by the company in 1999 did not have sufficient economic reasons to qualify for the beneficial tax regime for restructuring processes. In October 2004 the tax inspector therefore raised an assessment on the company for tax on the capital gain arising from the goodwill and tangible assets revaluation. The amount of the assessment including delay interest, was €18.7m. During January 2005, the company appealed against that assessment.

Notes *(continued)*

24 Contingent liabilities and contingent assets *(continued)*

On 2 February 2005, the company was purchased by Koninklijke DSM NV ("DSM") as part of the NeoResins business disposal by the Avecia group. Under Paragraph 3.1.1 of the Tax Deed to the disposal, DSM accepted responsibility for any liability arising from the assessment. The liability of the Avecia group ceased at that point.

Corporate Tax Audit, Stahl Iberica, Spain

Stahl Iberica SL was owned by the group in 1999 at the time it undertook a similar merger transaction as that for Avecia Spain referred to above. The Spanish tax authority carried out a parallel tax audit at Stahl Iberica, but the tax inspector delayed his conclusions until a decision was made in the case of Avecia Spain.

On 4 July 2005, the tax inspector issued a final tax assessment arising from the tax audit in an amount €2,474,047 plus delay interest of €648,912.

On 7 July 2005, the current owners of Stahl Iberica made a claim to the group in respect of that assessment.

At the group's request, an appeal against the assessment was submitted in July 2005. As a condition to submitting the appeal, it has been necessary for the group to pay the disputed tax and delay interest totalling €3,122,959: this was paid on 17 August 2005. This means that group will have no further liability arising from the audit.

The appeal is being pursued with a final appeal document submitted in March 2006.

Notes (continued)

25 Commitments

(a) Capital commitments of the group at the end of the financial period, for which no provision has been made are as follows:

	2005 £m	2004 £m
Contracted capital commitments	0.4	5.3
	<u> </u>	<u> </u>

Capital commitments are expected to be settled within one year.

(b) Total commitments under non cancellable operating leases are as follows:

	2005 Land and buildings £m	2004 Land and buildings £m
Operating leases which expire:		
In the second to fifth years inclusive	0.3	0.5
After five years	2.7	2.2
	<u> </u>	<u> </u>
	3.0	2.7
	<u> </u>	<u> </u>

The future minimal lease payments under operating and finance leases, including finance charges, were as follows:

	2005 Operating leases £m	2005 Finance leases £m	2004 Operating leases £m	2004 Finance leases £m
Due in one year or less	0.5	-	0.7	0.8
Due between one and two years	0.5	-	0.4	0.8
Due between two and three years	0.5	-	0.4	0.5
Due between three and four years	0.5	-	0.4	0.5
Due between four and five years	0.5	-	0.4	0.5
Due in five years or more	0.5	-	0.4	1.1
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	3.0	-	2.7	4.2
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

There were no commitments (2004: £nil) under finance leases at the balance sheet date that were due to commence thereafter.

Notes (continued)

26 Employee benefits

The Avecia group participates in retirement plans, which cover the majority of its employees. These plans are either defined contribution, where the level of company contribution is fixed at a set level or percentage of employees pay, or defined benefit, where benefits are based on employees' years of service and average final remunerations. In general all plans are funded through separate trustee-administered funds. The pension cost for the main defined benefit plans is established in accordance with the advice of independent qualified actuaries based on valuations undertaken on varying dates. There are material plans in the UK and the US but the group no longer has employees or pension plans in The Netherlands.

UK

An actuarial valuation was carried out as at 31 March 2003 using a market-led approach. The assets are taken at market value with the liabilities valued using financial assumptions derived from market yields on Government Fixed Interest and Index Linked gilts at the valuation date. The significant assumptions used in this valuation were UK price inflation of 2.5 per cent pa, investment returns of 6.5 per cent pa (pre-retirement) and 5.0 per cent pa (post-retirement), salary increases of 3.5 per cent pa and pension increases of 2.5 per cent pa. The market value of the fund's assets was £109.6 million and represented 64 per cent of the accrued liabilities at that date allowing for projected future salary increases. The next valuation will be as at March 2006.

The contribution rate currently payable by the employer is 14.5% of pensionable salaries. Employees pay varying levels of contribution in accordance with the rules and the current average is 3.6% of pensionable salaries.

Avecia's investment policy for the UK pension scheme is to consider a full range of asset classes, the risks and rewards of alternative asset allocation strategies, the suitability of each asset class in the planned asset allocation strategy, and the need for appropriate diversification. It is the trustee's policy to delegate all day-to-day decisions about the investments that fall within each investment option to the fund manager.

US

In the US an actuarial valuation was carried out as at 1 January 2003. The significant assumptions used in this valuation were that the rate of return on investment would be 8.0% per annum, the rate of salary increases would be 5.0% and pension increases 0% per annum. The market value of the plans' assets at that date was \$31.0 million. The primary reason for the decrease in market value of plans' assets from \$41.5 million as at 1 January 2002 was the transfer out of \$8.4 million of trust assets in 2002 coincidental with the sale of Stahl. The 1 January 2003 market value of the plans' assets represented 64% of the accrued liabilities as at that date, based on salaries projected to the date of retirement or assumed earlier death or leaving services. There is a deficiency of \$11.4 million on this funding level basis and the basis of the actuarial value of assets that is used in the US to determine employer contributions.

During the year \$3.5 million was funded in the plan's trust. It is anticipated that amounts will also be funded in 2006. Employer contributions are based on the minimum funding requirements of ERISA.

Netherlands

Following the disposal of the NeoResins business in February 2005 the group no longer has employees or pension plans in the Netherlands.

In the Netherlands an actuarial valuation was carried out as at 31 December 2003. The value of assets was €42.265 million, which represents 107.4% of the plan liabilities at that date. Total contributions in 2003 were payable at a rate of 23.2% of pensionable salaries less the state pension offset of €15,973. In 2003 this was approximately equivalent to 14.5% of members' pensionable salaries. Contributions are currently payable by the employee at the rate of 2% between earnings limits of €23,960 and €43,065 and 7.5% of earnings above the €43,065 limit. In 2003 this was equivalent to approximately 1.8% of gross pensionable salaries. Employer's contribution is approximately 12.7%.

Further additional payments have been made by Avecia in 2003 for a total amount of €1.48 million to close the gap between liabilities and assets because of a negative return on assets in 2001 and 2002. At the end of 2002 Stahl left the Avecia Pension fund and transferring liabilities for an amount of €23.5 million to the Stahl Pension fund. Per 1 January 2004 we changed, after reaching agreement with the stakeholders, the pension plan from a final pay into an average weighted system and furthermore increased the contribution from the employees to a higher level.

Notes *(continued)*

26 Employee benefits *(continued)*

Major assumptions

	2005 UK %	2005 US %	2005 Netherlands %	2004 UK %	2004 US %	2004 Netherlands %
Rate of general increase in salaries	3.90	4.25	-	3.90	4.25	3.00
Rate of increase to pensions in payment	2.80	-	-	2.70	-	1.75
Discount rate at 31 December	4.70	5.50	-	5.30	6.25	4.50
Medical cost trend rate	-	5.00	-	-	5.00	-
Inflation	2.90	3.25	-	2.90	3.25	2.00

	2005 UK £m	2005 USA £m	2005 Netherlands £m	2005 Other £m	2004 UK £m	2004 USA £m	2004 Netherlands £m	2004 Other £m
Present value of unfunded obligations	(45.2)	(4.3)	-	(4.5)	(72.9)	(9.2)	(14.7)	(8.9)
Present value of funded obligations	(124.0)	(12.7)	-	-	(175.3)	(12.9)	(32.7)	-
Fair value of plan assets	124.0	12.7	-	-	175.3	12.9	32.7	-
Present value of net obligations	(45.2)	(4.3)	-	(4.5)	(72.9)	(9.2)	(14.7)	(8.9)
Recognised liability for defined benefit obligations	(45.2)	(4.3)	-	(4.5)	(72.9)	(9.2)	(14.7)	(8.9)
Total employee benefits	(45.2)	(4.3)	-	(4.5)	(72.9)	(9.2)	(14.7)	(8.9)

Notes (continued)

26 Employee benefits (continued)

Movements in net liability for defined benefit obligations recognised in the balance sheet

	2005 UK £m	2005 USA £m	2005 Netherlands £m	2005 Other £m	2004 UK £m	2004 USA £m	2004 Netherlands £m	2004 Other £m
Net liability for defined benefit obligations at 1 January	(72.9)	(6.1)	-	(5.8)	(79.3)	(11.7)	(12.0)	(10.2)
Contributions received	16.5	2.6	-	0.2	17.7	2.0	1.7	0.4
Actuarial (loss)/ gain	(7.9)	0.5	-	(0.7)	(5.1)	(2.4)	(2.9)	(0.1)
(Loss)/gain due to exchange	-	(0.8)	-	2.1	-	1.0	0.2	0.7
Expense recognised in the income statement	19.1	(0.5)	-	(0.4)	(6.2)	1.9	(1.7)	0.3
Transfer to liabilities classified as held for sale	-	3.0	-	2.7	-	3.1	14.7	3.1
	<u>(45.2)</u>	<u>(1.3)</u>	<u>-</u>	<u>(1.9)</u>	<u>(72.9)</u>	<u>(6.1)</u>	<u>-</u>	<u>(5.8)</u>
Net liability for defined benefit obligations at 31 December	<u>(45.2)</u>	<u>(1.3)</u>	<u>-</u>	<u>(1.9)</u>	<u>(72.9)</u>	<u>(6.1)</u>	<u>-</u>	<u>(5.8)</u>

Expense recognised in the income statement

	Year ended 31 December 2005				Year ended 31 December 2004			
	UK £m	USA £m	Netherlands £m	Other PRB's £m	UK £m	USA £m	Netherlands £m	Other PRB's £m
Current service cost	(7.1)	(0.3)	-	(0.2)	(8.3)	(0.8)	(1.4)	(0.4)
Past service cost	(2.8)	-	-	-	(0.4)	-	-	-
Interest cost	(11.4)	(1.4)	-	(0.2)	(12.2)	(1.3)	(2.0)	(0.6)
Expected return on assets	10.8	1.2	-	-	11.1	1.2	1.7	-
Gain/(loss) due to curtailments/settlements	29.6	3.1	14.7	5.8	3.6	2.8	-	1.3
	<u>19.1</u>	<u>2.6</u>	<u>14.7</u>	<u>5.4</u>	<u>(6.2)</u>	<u>1.9</u>	<u>(1.7)</u>	<u>0.3</u>

The expense is recognised in the following lines in the income statement:

	2005 £m	2004 £m
Operating costs	(10.4)	(11.3)
Interest costs	(1.0)	(2.1)
Gain on disposal of discontinued business operations	53.2	7.7
	<u>41.8</u>	<u>(5.7)</u>

Notes (continued)

27 Post balance sheet events

On 26 December 2005 the group announced that Fuji Photo Film Co. Ltd ("Fujifilm") was to acquire Avecia's Inkjet and Electrophotography businesses for £143 million (approximately Yen 30 billion). The transaction was completed on 17 February 2006. The sale included all the group's Inkjet and Electrophotography development and manufacturing assets in Manchester, England, Grangemouth, Scotland and New Castle, Delaware, USA. 340 employees transferred with the business on completion.

Following the disposal the group utilised £76m of the proceeds to redeem all of the outstanding high yield bonds, including accrued interest and the premium due on redemption.

The group also made a one-off contribution of £25m to the UK pension scheme on 3 April 2006, reducing the pension deficit by the same amount.

On 31 March 2005 Avecia sold its interest in the Image Polymer business, a jointly controlled entity to Mitsui, for \$8.7m.

Avecia Group plc was unable to make the dividend payment due on 2 January 2006 on the Redeemable preference shares due to insufficient distributable reserves in the Company. The delay in paying the dividend increased the rate at which the dividend accrues from 16% to 18%. On 25 May 2006, Avecia Group plc received permission to reduce its ordinary share capital by £150m following application to the court. This resulted in a credit to the company's retained earnings which enabled it to pay the outstanding dividend and accrued interest thereon on the redeemable preference shares on 26 May 2006, and the rate at which dividends accrue on these shares reverted to 16%. On 5 July 2006 the company redeemed 1,822,489 of the Redeemable preference shares at a total cost of US\$ 48,056,048, leaving 1,200,000 of the Redeemable preference shares in issue.

28 Related party disclosures

In June 1999, Cinven and Investcorp S.A. jointly directed the formation of Avecia, and its acquisition of the Zeneca Specialties business. Cinven and Investcorp S.A. continue to provide consulting services to the group, for which they may receive payments of up to £400,000 per annum. In January 2002 Avecia completed the sale of its Stahl business to Luxembourg 101 S.A. and its affiliates. The purchase of Stahl from Avecia was managed by Investcorp S.A. on behalf of Luxembourg 101 SA and its affiliates, which under the terms of the Bond Indenture means that Luxembourg 101 SA is considered a related party. The sale of the Stahl business was therefore conducted under the terms of the bond indenture relating to related party transactions.

At December 31, 2005 debtors include £42.1 million (2004: £15.0 million) owed to companies within the group by the parent companies of Avecia Group plc, Avecia Holdings plc and Avecia Finance plc of which £15.0 million relates to acquisition fees (this amount is interest free) and £27.0million relates to a capital contribution.

The principal undertakings of Avecia Group plc as at 31 December 2005 were as follows:

Subsidiary undertakings	Country of incorporation	Principal activity	Percentage of equity owned %
Avecia Corporation Limited	UK	Holding company	100*
Avecia Investments Limited	UK	Holding company	100*
Avecia UK Holdings Limited	UK	Holding company	100*
Avecia Limited	UK	Chemical manufacture	100*
Avecia Inkjet Limited*	UK	Chemical manufacture	100*
Avecia Inc.**	USA	Chemical manufacture	100*
Avecia Holdings Inc.	USA	Holding company	100*
Avecia Biotechnology Inc.	USA	Chemical manufacture	100*

* This company ceased to be part of the group on 17 February 2006.

** This company became a holding company in the group on 1 January 2006.

Jointly controlled entities

The group makes recharges of certain expenses to the jointly controlled entity.

Notes *(continued)*

29 Explanation of transition to IFRS

As stated in note 1(a), these are the group's first consolidated financial statements prepared in accordance with IFRSs.

The accounting policies set out in note 1 have been applied in preparing the financial statements for the year ended 31 December 2005, the comparative information presented in these financial statements for the year ended 31 December 2004 and in the preparation of an opening IFRS balance sheet at 1 January 2004 (the group's date of transition).

In preparing its opening IFRS balance sheet, the group has adjusted amounts reported previously in financial statements prepared in accordance with its old basis of accounting (previous GAAP). An explanation of how the transition from previous GAAP to IFRSs has affected the group's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables.

Notes (continued)

29 Explanation of transition to IFRSs (continued)

Reconciliation of equity

In millions of £	Note	Previous GAAP	Effect of transition to IFRSs 1 January 2004	IFRSs	Previous GAAP	Effect of transition to IFRSs 31 December 2004	IFRSs
ASSETS							
Non-current assets							
Property, plant and equipment	a	263.2	(30.8)	232.4	198.6	(52.5)	146.1
Goodwill	a, e	277.7	(49.5)	228.2	199.6	(159.4)	40.2
Intangible assets		10.1		10.1	8.5	(8.0)	0.5
Investment in joint controlled entities		18.8		18.8	7.9	-	7.9
Amounts due from parent undertakings		17.2		17.2	15.0	-	15.0
		<u>587.0</u>	<u>(80.3)</u>	<u>506.7</u>	<u>429.6</u>	<u>(219.9)</u>	<u>209.7</u>
Current assets							
Inventories	a	74.9	(17.8)	57.1	50.2	(16.9)	33.3
Trade and other receivables	a, c	75.1	(11.2)	63.9	69.7	(33.8)	35.9
Cash and cash equivalents		8.0		8.0	22.7	-	22.7
Assets classified as held for sale	a	-	112.4	112.4	-	291.9	291.9
		<u>158.0</u>	<u>83.4</u>	<u>241.4</u>	<u>142.6</u>	<u>241.2</u>	<u>383.8</u>
		<u>745.0</u>	<u>3.1</u>	<u>748.1</u>	<u>572.2</u>	<u>21.3</u>	<u>593.5</u>
LIABILITIES							
Current liabilities							
Trade and other payables	a, c	91.2	(9.1)	82.1	82.3	(25.0)	57.3
Financial liabilities		70.0		70.0	76.0	0.8	76.8
Current tax liabilities		4.3		4.3	0.6	-	0.6
Provisions	a, d	2.3	(0.5)	1.8	11.2	(1.3)	9.9
Liabilities classified as held for sale	a	-	11.6	11.6	-	53.1	53.1
		<u>167.8</u>	<u>2.0</u>	<u>169.8</u>	<u>170.1</u>	<u>27.6</u>	<u>197.7</u>
Non-current liabilities							
Financial liabilities		431.0		431.0	273.1	37.6	310.7
Other payables	a, b	7.4	37.0	44.4	2.1	(0.5)	1.6
Amount due to parent undertakings		2.2		2.2	-	-	-
Deferred tax liabilities		5.2		5.2	5.7	(3.6)	2.1
Pension liabilities		113.2		113.2	105.7	(23.6)	82.1
		<u>559.0</u>	<u>37.0</u>	<u>596.0</u>	<u>386.6</u>	<u>9.9</u>	<u>396.5</u>
Total liabilities		<u>726.8</u>	<u>39.0</u>	<u>765.8</u>	<u>556.7</u>	<u>37.5</u>	<u>594.2</u>
Net assets		<u>18.2</u>	<u>(35.9)</u>	<u>(17.7)</u>	<u>15.5</u>	<u>(16.2)</u>	<u>(0.7)</u>
Capital and reserves							
Called up share capital	b	330.6	(1.5)	329.1	330.7	(1.5)	329.2
Share premium account	b	13.4	(13.4)	-	14.9	(14.9)	-
Shares to be issued	b	3.0	(3.0)	-	-	-	-
Retained earnings	b	(328.8)	(18.0)	(346.8)	(330.1)	0.2	(329.9)
Total capital and reserves		<u>18.2</u>	<u>(35.9)</u>	<u>(17.7)</u>	<u>15.5</u>	<u>(16.2)</u>	<u>(0.7)</u>

Notes (continued)

29 Explanation of transition to IFRSs (continued)

(a) The group has elected to apply IFRS 5 to all disposals from 1 January 2004. Accordingly, at 1 January 2004 the group has reclassified the assets and liabilities of the Additives and Biocides businesses to assets and liabilities held for sale. As a result of this adjustment goodwill of £45.0m, property, plant and equipment of £30.8m, inventories of £17.8m and trade and other debtors of £14.3m have been reclassified to assets held for sale and trade and other creditors of £11.1m and provisions of £0.5m have been reclassified as liabilities included in disposal groups.

At 31 December 2004 the group has reclassified the assets and liabilities of the NeoResins and the Displays and Organic Semiconductor businesses to assets and liabilities held for sale. As a result of this adjustment goodwill of £159.4m, intangible assets of £8.0m, property, plant and equipment of £52.5m, inventories of £16.9m and trade and other debtors of £34.1m have been reclassified to assets held for sale and trade and other creditors of £25.0m, deferred taxation of £3.6m, provisions of £0.8m and pension liabilities of £23.6m have been reclassified as liabilities classified as held for sale.

(b) Consistent with IFRSs the Redeemable preference shares have been reclassified from equity to non-current liabilities. At 1 January 2004 as a result of this adjustment, equity was reduced by and non-current liabilities were increased by £37.7m. At 31 December 2004 the corresponding adjustment was £37.6m. Under IFRS dividends on these shares are reclassified to finance costs and for the year ending 31 December 2004 this increased finance costs by £6.6m.

(c) In accordance with IFRSs all derivative financial instruments have been recognised as assets or liabilities at fair value. At 1 January 2004 the measurement of all derivatives at fair value has resulted in a fair value derivatives and hedging reserve of £1.8m, comprising assets of £3.1m and liabilities of £1.3m. At 31 December 2004 the fair value derivatives and hedging reserve was £(0.1)m, comprising assets of £0.3m and liabilities of £0.4m.

(d) Under IFRSs a provision for restructuring at 31 December 2004 has been fair valued and this has resulted in a reduction in provisions in the balance sheet of £0.5m, an increase in operating profit of £1.3m and an increase in finance costs of £0.8m profit and loss account.

(e) The group has applied IFRS 3 to all business combinations that have occurred since 1 January 2004, from this date the goodwill is no longer amortised under IFRSs, but is tested annually for impairment. As a result the carrying value of goodwill was increased by £4.4m at 31 December 2004, the profit and loss account increased by £3.6m for the year in respect of continuing operations and £18.6m in respect of discontinued operations. The foreign exchange translation reserve was adjusted by £0.2m.

(f) In accordance with IFRS exchange gains or losses on the translation of overseas assets are recycled through the income statement upon the disposal of assets this results in a reduction of £0.3m in the gain on disposal of discontinued operations for the year ended 31 December 2004.

Notes (continued)

29 Explanation of transition to IFRSs (continued)

Reconciliation of profit for 2004

	<i>Note</i>	Previous GAAP	Effect of Transition to IFRS's	IFRSs
In millions of £				
Continuing Operations				
Group revenue:		60.8		60.8
Operating costs	<i>e</i>	(84.3)	3.6	(80.7)
Restructuring costs	<i>d</i>	(15.9)	1.3	(14.6)
Other operating income		5.2		5.2
		<hr/>	<hr/>	<hr/>
Loss before interest		(34.2)	4.9	(29.3)
Finance income		47.1		47.1
Finance costs	<i>b, d</i>	(67.6)	(9.3)	(76.9)
		<hr/>	<hr/>	<hr/>
Loss before tax		(54.7)	(4.4)	(59.1)
Tax		(1.9)		(1.9)
		<hr/>	<hr/>	<hr/>
Loss after tax from continuing operations		(56.6)	(4.4)	(61.0)
Profit from discontinued operations and gain on disposal of discontinued operations	<i>f</i>	95.5	17.1	92.6
		<hr/>	<hr/>	<hr/>
Loss for the year		18.9	12.7	31.6
PIK preference Dividend		(6.6)	6.6	-
		<hr/>	<hr/>	<hr/>
Retained profit for the year		12.3	19.3	31.6
		<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
Discontinued operations is broken down as follows:				
Group turnover		346.4	-	346.4
Operating costs	<i>e</i>	(342.6)	18.6	(324.0)
Other operating income		3.9		3.9
Onerous contracts		(1.7)		(1.7)
Impairment of non-current assets		(22.2)		(22.2)
		<hr/>	<hr/>	<hr/>
Profit from discontinued operations		(16.2)	18.6	2.4
Gain on disposal of discontinued operations		98.6	(1.5)	97.1
Share of operating profit of joint ventures		(6.9)	-	(6.9)
		<hr/>	<hr/>	<hr/>
Profit from discontinued operations & gain on disposal of discontinued operations		75.5	17.1	92.6
		<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

Notes (continued)

30 Difference between IFRS and US accounting principles

These consolidated financial statements are prepared in accordance with IFRSs. Significant differences between IFRSs and US GAAP which affect the net income and net assets of Avecia Group plc are set out below.

Reclassification of parent company debtors

Since the acquisition of the Specialty Chemicals business of AstraZeneca in 1999, certain amounts have been due from Avecia Holdings plc and Avecia Finance plc, the parent companies of Avecia Group plc on a long term basis (see note 28). Under US GAAP, such amounts are reflected as a reduction of shareholders' funds. Net assets in accordance with US GAAP have been reduced by £15.0 million to reflect this reclassification at December 31, 2005 (*December 31, 2004: £15.0 million*).

Capitalization of interest

There is no mandatory IFRS accounting standard regarding the capitalization of interest and, accordingly, the business does not capitalize interest as part of the cost of fixed assets in financial statements prepared under IFRS. US GAAP requires interest incurred and associated with the cost of constructing fixed assets to be capitalized and amortized over the life of the asset.

Revenue recognition

Under US GAAP specific guidance is given regarding allocating revenue to separate elements of multiple element arrangements. Under this guidance a fair value cannot be readily ascertained for the separate elements of certain contracts and consequently revenue is recognised on a straight line basis over the term of the contract. Under IFRS there is no equivalent guidance and revenue has been recognised on separate elements of certain arrangements based upon the rendering of the associated service.

In 2001, £4.8m of contract revenue which was recognized under UK GAAP was deferred as contingent revenue under US GAAP as a liability was deemed to exist under the terms of the contract. Under IFRS transition rules the liability derecognition criteria under IAS 39 are not applied retrospectively therefore this revenue is not deferred under Adopted IFRS.

Deferred taxation

This represents the deferred taxation in respect of the US GAAP adjustments.

Pension Expense

There are various differences between IFRS and US GAAP in accounting for pension costs.

Under IFRS, actuarial gains and losses are permitted to be recognised immediately in the statement of recognised income and expense. Under US GAAP, such actuarial gains and losses are permitted to be amortised on a straight-line basis over the average remaining service period of the employees.

Under US GAAP, a minimum pension liability is recognized through other comprehensive income in certain circumstances when there is a deficit of plan assets relative to the accumulated benefits obligation. Under IFRS, there is no such requirement.

Under IFRS, prior service costs are recognised immediately in the income statement. Under US GAAP prior service costs are deferred and amortised over the average remaining life of the employees.

Software Costs

US GAAP mandates the capitalisation of software costs when under certain circumstances these costs would be expensed under IFRS.

Notes *(continued)*

30 Difference between IFRS and US accounting principles *(continued)*

Goodwill Amortisation

Under US GAAP, goodwill is not amortised but is tested annually for impairment in accordance with SFAS 142. Similar principles apply under IFRS, however this applies only from the effective date of transition (1st January 2004). Prior to this goodwill was amortised according to UK GAAP. This leads to different carrying values of goodwill.

Onerous Contracts

Under IFRS, when a contract is recognised as onerous a provision must be made for unavoidable future losses. This is generally not permitted under US GAAP.

Purchase accounting adjustments (goodwill and intangibles)

In respect of acquisitions prior to 1 January 2004, goodwill is included at 1 January 2004 on the basis of its deemed cost, which represents the amount recorded under UK GAAP. On transition amortisation of goodwill has ceased as required by IFRS 1.

In the consolidated financial statements, goodwill arising on acquisitions made prior to January 1998 accounted for under the purchase method has been eliminated against shareholders' equity, in accordance with UK GAAP. Under the requirements of UK Financial Reporting Standard 10 'Goodwill and intangible assets', goodwill on acquisitions made after January 1, 1998 is capitalized and amortized over its estimated useful life, which is generally presumed not to exceed 20 years. UK GAAP requires that on subsequent disposal or termination of a previously acquired business, any goodwill previously taken directly to shareholders' equity is charged in the income statement against the profit or loss on disposal or termination.

Under IFRSs goodwill created outside the Avecia Group plc group of companies is not reported in the financial statements of Avecia Group plc. Under US GAAP an element of this goodwill is pushed down into the net assets of the group as it is deemed to be attached to assets held by the Avecia Group plc group of companies.

Impairment of Assets and Goodwill

Under US GAAP impairments are calculated in accordance with SFAS 142 (for goodwill and intangible assets) and SFAS144 (for other long-lived assets).

Groups of long-lived assets (including finite-lived intangible assets) are tested for impairment by comparing the recoverable amount of the asset group (determined using undiscounted cash flows) to its carrying amount to determine whether an impairment exists. If the asset group is impaired, an impairment charge is determined by comparing the carrying amount of the asset group with its fair value. Goodwill is tested for impairment by comparing the fair value of each reporting unit with its carrying amount to determine whether the related goodwill is potentially impaired. Any impairment of goodwill is measured by comparing the fair value of goodwill to its carrying amount. The fair value of goodwill is determined by deducting the fair value of identifiable assets and liabilities within a reporting unit from the total fair value of that reporting unit. Indefinite-lived intangibles are tested for impairment under US GAAP by comparing the fair value of the asset with its carrying amount.

Under IFRS, the carrying value of cash generating units is compared with its recoverable amount and any deficit is written off initially to goodwill, then intangible assets, then other long-lived assets on a pro-rata basis.

Notes *(continued)*

30 Difference between IFRS and US accounting principles

The following is a summary of the material adjustments to retained profit and net assets/(liabilities) which would have been required if US GAAP had been applied instead of IFRS.

	Avecia Group plc Consolidated	
	For the year ended December 31, 2005	For the year ended December 31, 2004
	£ million	£ million
Retained profit for the financial period under IFRS	40.0	31.6
	—	—
Adjustments to conform to US GAAP		
Capitalization of interest, less disposals and amortization	(2.9)	0.6
Software costs capitalized under US GAAP	-	0.3
Income recognition deferral	(0.9)	(1.8)
Pension expense	(4.8)	(16.6)
Post-retirement benefits	(0.1)	0.9
Differences on profit on disposal of business	(35.0)	(42.8)
Goodwill additional impairment under US GAAP	-	(4.2)
Fixed asset additional impairment under US GAAP	-	4.9
Onerous contract provision not recognized under US GAAP	0.5	1.7
Deferred taxation on adjustments to conform to US GAAP	0.3	(0.1)
	—	—
Net loss in accordance with US GAAP	(2.9)	(25.5)
	—	—
Net loss available to common shareholders in accordance with US GAAP	(2.9)	(25.5)
	—	—
(Loss)/profit before taxation in accordance with US GAAP from:		
continuing operations	(94.6)	(71.1)
discontinued operations	93.0	47.6
Taxation in accordance with US GAAP on:		
continuing operations	(1.3)	(2.0)
discontinued operations	-	-
Net (loss)/profit in accordance with US GAAP from:		
continuing operations	(95.9)	(73.1)
discontinued operations	93.0	47.6

Notes *(continued)*

30 Difference between IFRS and US accounting principles *(continued)*

	Avecia Group plc	
	Consolidated	
	As at December 31,2005	As at December 31,2004
	£ million	£ million
IFRS		
Total shareholders funds as previously stated	62.7	(0.7)
	<hr/>	<hr/>
Adjustments to conform to US GAAP		
Reclassification of parent company debtors	(15.0)	(15.0)
Capitalization, less disposals and amortization of interest	8.3	11.2
Software costs capitalized under US GAAP	-	0.5
Income recognition deferral	(7.5)	(6.6)
Pension liability	17.8	84.4
Post-retirement benefits/plan amendment	1.7	1.9
Additional minimum liability	(4.4)	(54.0)
Pensions intangible assets	0.1	2.6
Purchase accounting adjustments	22.0	43.7
Additional goodwill impairment under US GAAP	(4.2)	(15.9)
Difference in historical basis of goodwill	9.6	46.5
Additional fixed asset impairment	-	(14.1)
Onerous contract provision not recognized under US GAAP	0.5	1.7
Tax on adjustments to conform to US GAAP	-	(0.3)
	<hr/>	<hr/>
Shareholders equity in accordance with US GAAP	91.6	85.9
	<hr/> <hr/>	<hr/> <hr/>

31 Ultimate parent company

The company is a subsidiary undertaking of Avecia Finance plc which is incorporated in Great Britain. The ultimate parent company is Avecia (Jersey) Limited, a company registered and incorporated in Jersey. The registered number is 74318. The external address of the ultimate parent company is:

Avecia (Jersey) Limited
 Mourant du Feu & Jeune
 22 Grenville Street
 St. Helier
 Jersey
 JE4 8PX

Notes (*continued*)

32 Company balance sheet under UK GAAP at 31 December 2005

	<i>Note</i>	2005 £m	2005 £m	2004 £m	2004 £m
Fixed assets				Restated	Restated
Investments	35		294.5		328.6
Current assets					
Debtors: amounts due within one year	36	41.7		30.7	
Debtors: amounts due after one year	36	78.4		284.9	
		<hr/>		<hr/>	
			120.1	315.6	
Creditors: amounts falling due within one year	37	(7.4)		(18.4)	
		<hr/>		<hr/>	
Net current assets			112.7		297.2
			<hr/>		<hr/>
Total assets less current liabilities			407.2		625.8
Creditors: amounts falling due after more than one year	38		(115.2)		(313.0)
			<hr/>		<hr/>
Net assets			292.0		312.8
			<hr/>		<hr/>
Capital and reserves					
Called up share capital	39		329.1		329.1
Profit and loss account	39		(37.1)		(16.3)
			<hr/>		<hr/>
Equity Shareholders' funds			292.0		312.8
			<hr/> <hr/>		<hr/> <hr/>

These financial statements were approved by the board of directors on 10 July 2006 and were signed on its behalf by:

[D MCLELLAN]

D Mclellan
Director

Notes *(continued)*

33 Company reconciliation of movements in shareholders' funds

for the period ended 31 December 2005

	2005	2004
	£000	£000
Loss for the period	(47.8)	(3.2)
Other recognised gains and losses relating to the period (net)	-	0.1
Capital contribution	27.0	-
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>
Net reduction to shareholders' funds	(20.8)	(3.1)
Opening shareholders' funds (as previously stated)	350.4	353.6
On adoption of FRS25	(37.6)	(37.7)
Opening shareholders' funds (as restated)	312.8	315.9
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>
Closing shareholders' funds	292.0	312.8
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>

Notes (continued)

34 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements, except as noted below.

In these financial statements the following new standards have been adopted for the first time:

- FRS 21 'Events after the balance sheet date';
- the presentation requirements of FRS 25 'Financial instruments: presentation and disclosure'
- FRS26 'Financial Instruments: measurement'; and
- FRS 28 'Corresponding amounts'.

The accounting policies under these new standards are set out below together with an indication of the effects of their adoption. FRS 28 'Corresponding amounts' has had no material effect as it imposes the same requirements for comparatives as hitherto required by the Companies Act 1985.

The corresponding amounts in these financial statements are restated where relevant in accordance with the new policies.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards, and under the historical cost accounting rules.

Under Financial Reporting Standard 1(Revised 1996) the company is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the company in its own published consolidated financial statements,

As the Company is a wholly owned subsidiary of Avecia Finance Limited, the company has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the group (or investees of the group qualifying as related parties). The consolidated financial statements of Avecia Group plc, within which this company is included, can be obtained from Avecia Group plc, PO Box 42, Hexagon Tower, Blackley, Manchester M9 8ZS.

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the contracted rate or the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

Fixed asset investments

Fixed asset investments are stated at cost less provision for any permanent impairment.

Notes (continued)

34 Accounting policies (continued)

Taxation

The charge for taxation is based on the loss for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Classification of financial instruments issued by the company

Following the adoption of FRS 25, financial instruments issued by the company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

- a) they include no contractual obligations upon the company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the company; and
- b) where the instrument will or may be settled in the company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the company's own equity instruments or is a derivative that will be settled by the company's exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability. Where the instrument so classified takes the legal form of the company's own shares, the amounts presented in these financial statements for called up share capital and share premium account exclude amounts in relation to those shares.

Finance payments associated with financial liabilities are dealt with as part of interest payable and similar charges. Finance payments associated with financial instruments that are classified as part of shareholders' funds, are dealt with as appropriations in the reconciliation of movements in shareholders' funds.

Notes (*continued*)

35 Fixed asset investments

Company

	Shares in group undertakings £m
<i>Cost</i>	
At beginning and end of year	328.6
<i>Amortisation</i>	
At beginning of year	-
Impairment	34.1
At end of year	34.1
<i>Net book value</i>	
At 31 December 2005	294.5
At 31 December 2004	328.6

The directly held company in which the company's interest at the year end is more than 20% is as follows:

	Country of incorporation	Principal activity	Class and Percentage of shares held
<i>Subsidiary undertaking</i> Avecia Corporation Limited	UK	Intermediate holding	Ordinary – 100

The principal indirectly owned subsidiary undertakings at the year end are:

	Country of incorporation	Principal activity	Class and percentage of shares held
<i>Subsidiary undertakings</i> Avecia UK Holdings Limited	UK	Intermediate holding	Ordinary - 100
Avecia Limited	UK	Chemical manufacture	Ordinary - 100
Avecia Holdings Inc.	USA	Intermediate holding	Ordinary - 100
Avecia Inc.	USA	Chemical manufacture	Ordinary - 100

Notes *(continued)*

36 Debtors

	Company 2005 £m	Company 2004 £m
Debtors due within one year		
Amounts owed by group undertakings	41.7	30.7
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>
	41.7	30.7
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>
	£m	£m
Debtors due after one year		
Amounts owed by parent undertakings	78.4	284.9
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>
	120.1	315.6
	<hr style="width: 100%;"/>	<hr style="width: 100%;"/>

The £41.7m due within one year is owed by Avecia Limited and is interest free.

£78.4m (2004: £284.9m) of amounts owed by group undertakings are due after more than one year. £76.1m (2004: £282.6m) of the amounts owed by group undertakings is denominated in US dollars with a weighted average fixed rate of interest of 12.1% and a weighted average period for which the rate is fixed of 4.5 years. The balance is sterling denominated of which £2.3m (2004: £2.3m) bears interest at 16% and is due for repayment in July 2010.

Notes *(continued)*

37 Creditors: amounts falling due within one year

	Company 2005 £m	Company 2004 £m
Accruals and deferred income	7.4	18.4
	<u>7.4</u>	<u>18.4</u>

38 Creditors: amounts falling due after more than one year

	Company 2005 £m	Company 2004 £m Restated
Other loans	112.1	313.0
Amounts owed to group undertakings	3.1	-
	<u>115.2</u>	<u>313.0</u>

Company

Analysis of debt:

	2005 £m	2004 £m Restated
Debt can be analysed as falling due:		
Between one and two years	3.1	-
Between four and five years	42.4	310.2
In five years or more	69.7	2.8
	<u>115.2</u>	<u>313.0</u>

The US Dollar denominated high yield bond is repayable in 2009 and interest is fixed at 11%. It is guaranteed by Avecia Corporation Limited.

Notes (continued)

39 Called up share capital

	2005 Number of shares	2005 Nominal value of shares £'000	2004 Number of shares	2004 Nominal value of shares £'000
Authorised				
Equity: ordinary shares of £1 each	400,000,000	400,000	400,000,000	400,000
Non equity – Pay-in-Kind (PIK) 16% cumulative redeemable preference shares of \$1 each	3,500,000	2,222	3,500,000	2,222
	<u>403,500,000</u>	<u>402,222</u>	<u>403,500,000</u>	<u>402,222</u>
Allotted, called up and fully paid				
Equity: ordinary shares of £1 each	329,100,001	329,100	329,100,001	329,100
Non equity – Pay-in-Kind (PIK) 16% cumulative redeemable preference shares of \$1 each	3,022,489	1,751	3,022,489	1,561
	<u>332,122,490</u>	<u>330,851</u>	<u>332,122,490</u>	<u>330,661</u>

Redeemable preference shares

The redemption of preference shares is mandatory on 1 July 2010 but may be redeemed at the option of the company on or after 1 January 2006 or earlier on certain public equity offerings at a redemption value equal to the liquidation preference value plus all accumulated and unpaid dividends to the date of redemption. On a winding up they would rank in priority to ordinary shares. Up to 1 July 2004 the company was able to issue further PIK preference shares instead of a cash dividend (based on the liquidated preference amount of \$25 per share). Subsequent to 1 July 2004 this option was no longer available and subsequent dividends became payable in cash. The PIK preference shares have no voting rights at meetings of the ordinary shareholders and attract a dividend of 16%. The carrying value of the preferred shares is being increased from the date of issue to the mandatory redemption date, by the interest method, such that the carrying value at the mandatory redemption date will equal the redemption value of \$25 per share. The accretion for 2005 was £0.1 million (2004: £0.1 million).

Company

	Equity share capital	Non equity share capital	Share premium account	Profit and loss account	Total
	£m	£m	£m	£m	£m
At 1 January 2005	329.1	1.6	14.9	4.8	350.4
On adoption of FRS 25	-	(1.6)	(14.9)	(21.1)	(37.6)
	<u>329.1</u>	<u>-</u>	<u>-</u>	<u>(16.3)</u>	<u>312.8</u>
At beginning of year (as restated)	329.1	-	-	(16.3)	312.8
Loss for year	-	-	-	(47.8)	(47.8)
Capital contribution	-	-	-	27.0	27.0
	<u>329.1</u>	<u>-</u>	<u>-</u>	<u>(37.1)</u>	<u>292.0</u>
At 31 December 2005	<u>329.1</u>	<u>-</u>	<u>-</u>	<u>(37.1)</u>	<u>292.0</u>