

BIOQUELL – an overview

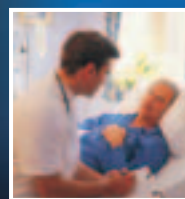
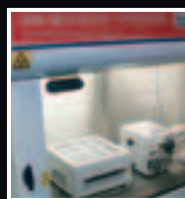
BIOQUELL has developed a unique, market leading and patent-protected range of bio-decontamination technologies which use hydrogen and oxygen peroxides to bio-deactivate micro-organisms such as bacteria (including “superbugs”), viruses and fungi in the pharmaceutical, biotechnology, laboratory and healthcare sectors.

BIOQUELL is fast developing the service side to its business via the provision of a Room Bio-Decontamination Service (RBDS) and an Equipment Bio-Decontamination Service (EBDS). BIOQUELL also manufactures and sells the Clarus range of bio-decontamination equipment.

The eradication of antibiotic resistant “superbugs” from the hospital environment is a key area of focus for the Group.

BIOQUELL also designs and manufactures specialist HEPA and activated carbon filtration equipment used in its range of laboratory and defence products.

Cape provides specialist testing services to a broad range of companies in the aerospace, automotive, defence, rail and telecoms sectors.



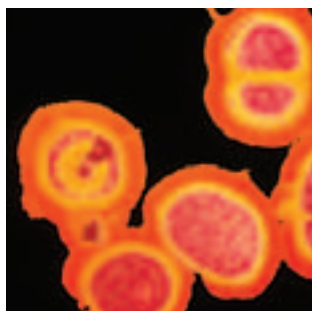
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Year in brief

- Significant improvement in turnover and bottom line performance
- BIOQUELL's unique RBDS service is seeing growth in revenues from emergency "superbug" outbreaks in hospitals in the UK and continental Europe
- Significant growth in RBDS was also seen in the pharmaceutical/biotechnology sector
- Strong growth in the year for the Group's bio-decontamination equipment sales, particularly in North America
- A novel treatment for chronic wounds is undergoing clinical trials and preliminary results look encouraging
- Cape, the Group's specialist testing service business, showed continued top line growth with further blue-chip clients signing up for long term outsourcing contracts



Chairman's statement



Good progress was made on the selling of RBDS into the pharmaceutical and bio-technology sectors

Overview

BIOQUELL made significant progress in 2004 in the commercialisation of its new bio-decontamination products and services. This progress can be seen in the financial results which demonstrate a substantial year-on-year improvement.

Results and finance

Turnover increased by 23% to £15.5 million (2003: £12.6 million). This increase was largely attributable to sales of Clarus bio-decontamination equipment, with a particularly strong performance in the North American market. In addition, RBDS, the Group's flagship room bio-decontamination service, and Cape, the Group's specialist testing service business, also showed strong revenue growth in the year with Cape benefiting from the acquisition of EMC Projects Limited.

The gross margin increased two points to 37% (2003: 35%). This improvement reflects the increasing proportion of sales of sophisticated bio-decontamination equipment and revenues from the Group's specialist service businesses.

Research and development costs were £0.9 million (2003: £1.4 million). The Group continues to invest in technological innovation and the upgrading of its existing product range.

Loss before tax was £0.3 million (2003: £2.1 million).

Cash inflow before capital expenditure and acquisitions was £0.5 million (2003: outflow of £1.3 million). Capital expenditure was £0.7 million (2003: £1.0 million), principally relating to investment in bio-decontamination

equipment for the Group's service businesses and Cape. During the year £0.2 million (2003: £nil) was paid as the initial tranche of consideration for the acquisition of EMC Projects Limited.

The Group is in a good financial state. The specialist service businesses are cash generative and the balance sheet is sound. Net debt at the year end was £0.7 million (2003: £0.3 million) and net assets were £6.2 million (2003: £6.3 million). The Group has overdraft facilities and other debt funding of £2.7 million.

Activities

Good progress was made on the selling of RBDS into the pharmaceutical and bio-technology sectors. The publication in the well respected Journal of Hospital Infection of the successful bio-decontamination of MRSA in St. Thomas' Hospital, London has been helpful in generating interest in the RBDS technology which is currently focused on emergency "superbug" outbreak eradication.

In order to generate substantial revenues from this technology it will be important to sell permanent on-site RBDS "implant" teams to hospitals who will provide an ongoing bio-decontamination service to help ensure that "superbugs" such as MRSA, *Acinetobacter*, VRE and *Clostridium difficile*, are eradicated from the hospital environment. We are pleased that a leading US hospital is planning to start shortly an RBDS "implant" trial in order to assess the level of "superbug" reduction that is achieved in the hospital. In contrast, we are disappointed by the slow take up of this technology in the NHS.

The preliminary results of the clinical trials relating to the Group's novel wound healing technology are encouraging. Wound healing



The size of the opportunities for the Group in relation to "superbug" eradication in hospitals and wound healing are both very large and international. The Group's existing bio-decontamination and specialist service businesses provide a sound platform from which to develop the Group into these substantially larger markets.



is a large global market. One estimate of the annual current treatment costs in the United States exceeds US\$ 9.5 billion. Chronic wounds can become infected with antibiotic resistant bacteria, including MRSA, and this new technology fits well with BIOQUELL's RBDS "superbug" eradication services for hospitals.

Sales of the Clarus range of bio-decontamination equipment showed strong year-on-year growth and BIOQUELL's market share continues to increase in a number of territories. We are continuing to develop this product range and anticipate good ongoing demand for these products, particularly in North America.

In the second half we began to see renewed demand for the Group's laboratory equipment products which previously had been experiencing decline in the face of cheaper overseas imports. In spite of this improvement this market remains extremely competitive and commoditised.

Cape continues to expand with increasing levels of outsourced testing contracts including with Rolls-Royce and Flight Refuelling (part of the Cobham Group). EMC Projects, acquired in June 2004, has been fully integrated into Cape and there have been notable successes in terms of cross sales of both environmental testing and EMC testing to the enlarged client base.

Dividends

The Board is proposing the payment of the dividend for the year on the preference shares of 7.5p per preference share, representing a total payment of £11,250. The Board is not recommending the payment of an ordinary dividend.

Prospects

The size of the opportunities for the Group in relation to "superbug" eradication in hospitals and wound healing are both very large and international. The Group's existing bio-decontamination and specialist service businesses provide a sound platform from which to develop the Group into these substantially larger markets. The Group also has the management teams needed to execute this strategy. Since the beginning of the year there have been some signs of weakness in the supply of equipment to the pharmaceutical sector and it is clear that we will need to invest further to achieve widespread adoption of the Group's RBDS technology in hospitals. However, the Board is confident of the prospects for BIOQUELL in 2005 which we anticipate will be an exciting year.

A handwritten signature in black ink, which appears to read 'MSalkeld'.

John Salkeld
Chairman

11 April 2005

Review of activities



BIOQUELL's unique RBDS technology continues to grow

RBDS

RBDS – the Group's Room Bio-Decontamination Service – continues to grow.

RBDS has now been deployed in nine countries in Western Europe, as well as Singapore and North America.

Over the last twelve months significant progress has been made in demonstrating the effectiveness of the technology to eradicate problematic micro-organisms – bacteria, viruses and fungi – from the hospital environment. At the same time the scale of the problem facing hospitals from these micro-organisms, including increased levels of antibiotic resistance, continues to increase. Although the UK public is well aware of the issues in hospitals relating to MRSA, hospitals are also facing significant problems from other organisms such as *Acinetobacter* and *Clostridium difficile*. BIOQUELL has demonstrated on a number of occasions in hospitals in the UK and in Europe that its technology can be used to stop a "superbug" outbreak and we are seeing increasing levels of interest in the RBDS technology from hospitals trying to combat such outbreaks. We are seeking to migrate the hospitals from a reactive to preventative approach to "superbug" eradication and are in discussions with a number of UK hospitals about deploying the technology via a permanent on-site RBDS team, a so-called "implant" model. Unfortunately, notwithstanding the positive report from the Department of Health's Rapid Review Panel in December 2004, take up by NHS hospitals has been slower than we could have reasonably anticipated and we are having to invest further to secure adoption of the technology. We have also started to promote this technology overseas and are pleased that a leading US hospital is planning to start shortly a trial of the RBDS implant model. The application of the RBDS technology against "superbugs" represents a

substantial global market which, once established, BIOQUELL intends to license, as appropriate, internationally to ensure that the technology takes market share rapidly.

Hospital Acquired Infection

Hospital Acquired Infection ("HAI") – technically known as nosocomial infection – is the term given to infection contracted by patients whilst in hospital. HAI can comprise bacteria, viruses or fungi. HAI is not a new problem – a significant part of Florence Nightingale's work was designed to reduce HAI by, for example, increasing the distance between beds in hospitals. HAI is a global problem and in addition to the UK causes substantial difficulties in Japan, North America and other parts of Europe.

HAI is becoming a large and more difficult problem for healthcare providers due to a number of factors. A major issue is the increasing resistance being displayed by bacteria against antibiotics. Increasing levels of international travel enable organisms to be spread rapidly across the globe, as was illustrated vividly by SARS. Due to advances in modern medicine people are living longer, able to have more challenging operations (such as transplant surgery) and are often sicker – and hence more susceptible to infection – when admitted to hospital. The continued mutation of "superbugs" with increasing antibiotic resistance is considered by many experts to be one of the greatest threats of our times.

MRSA

Increasing levels of antibiotic resistance is widely recognised to be a substantial problem. The best known organism is MRSA – Methicillin resistant *Staphylococcus aureus*. Some 30% of the population are thought to have *Staphylococcus aureus* residing on the body, often in the nose. However, only a very small proportion of the population who have not been to hospital, or other healthcare facilities, will have a strain which



Hospital Acquired Infection is a global problem and, in addition to the UK, causes substantial difficulties in Japan, North America and other parts of Europe. A major issue is the increasing resistance being displayed by bacteria against antibiotics.



is resistant to methicillin (or other antibiotics). In March 2005 the UK's Health Protection Agency reported that they were only aware of 100 cases of community acquired MRSA over the last three years. Currently patients who contract MRSA in hospital can normally be cured by the use of vancomycin, a different class of antibiotic, which is often considered to be the antibiotic of "last resort". However, there are increasing signs – particularly in Japan and the United States – of *Staphylococcus aureus* becoming increasingly resistant to vancomycin.

Other Bacteria

Unfortunately for healthcare providers MRSA is not their sole problem and there are a number of other highly problematic bacteria infecting patients who stay in hospital, including, for example, *Acinetobacter* and *Clostridium difficile*. *Acinetobacter* is becoming resistant to antibiotics significantly more quickly than *Staphylococcus*. A recent report in the scientific literature stated that a strain affecting the South East of England was fast becoming resistant to all antibiotics. Similar strains have been seen in North and South America. The literature also suggests that a new strain of *Clostridium difficile* is currently spreading in the United States and Canada. It is more virulent and difficult to detect in patients, and is causing significant concern and costs to healthcare providers in North America. In the United Kingdom cases of *Clostridium difficile* increased from 28,819 in 2002 to 35,537 in 2003, an increase of 23%.

Viruses and Fungi

HAI can also be caused by viruses and fungi. Parainfluenza is a virus which has been known to cause significant trouble in transplant units and Norovirus – which is also found on cruise ships – regularly causes outbreaks in hospitals. Fungal infections can also cause major problems in transplant units or other hospital departments

where immuno-suppressed patients are being treated. *Aspergillus* spores, which are often released into the environment after building works, can cause *aspergillosis*. *Candida albicans* is another fungus which causes HAI. As a general rule anti-fungal drugs are expensive and toxic.

Role of the Environment

The role of the hospital environment in contributing towards HAI is a controversial area. From the 1960s to the mid 1990s many of the top experts in this field were advising that the hospital environment was not a source of infection. In other words, it was thought that infection could only be caught directly from other patients – or via healthcare workers – and it was thought highly unlikely that infection could be transmitted by inanimate objects in the environment. One of the consequences of this approach was that the emphasis on hospital cleanliness – which had effectively started with Florence Nightingale – was reduced, expenditure on cleaning reduced and it is widely accepted that the UK hospitals were allowed to become dirty. At the same time it was thought that most of the bacteria causing HAI died rapidly when outside of the body. For example, it was thought that MRSA would die within hours when dried in the hospital environment – and as such did not represent a risk within the hospital.

Over the last few years the role of the hospital environment in terms of infection transmission has been reconsidered. There is increasing evidence that the hospital environment can become heavily contaminated. It is now known that many of the organisms causing HAI can survive for long periods in the hospital environment – for example MRSA has been shown to survive for at least 300 days. And there is increasing evidence that the hospital environment does contribute to the spread of infection, although the evidence is currently stronger with certain organisms such as *Acinetobacter* and *Clostridium difficile*.



Review of activities

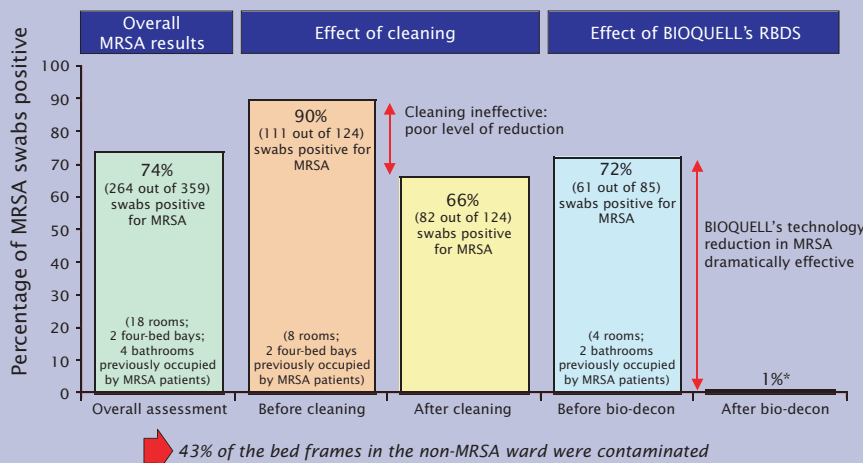
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The costs of Hospital Acquired Infection are substantial

BIOQUELL has been carrying out research in this area with a team led by Professor French at St Thomas' Hospital. In May 2004 a joint research paper was published which showed, in summary, that (i) the hospital environment can become heavily contaminated with MRSA; (ii) conventional cleaning does not eradicate MRSA from the hospital environment; and (iii) BIOQUELL's RBDS technology was dramatically effective. A graph summarising the research is shown below.

Graphical summary of St Thomas'/BIOQUELL's research



Costs of HAI

A number of studies have been undertaken examining the costs of HAI. A study undertaken for the National Audit Office in 1999 estimated that the cost to the NHS of HAI was approximately £1 billion. The same study estimated that the average cost per HAI was £3,154, covering, among other things, an additional 14 days in hospital. (BIOQUELL believes that this average cost is too low because the implied fully loaded cost of £225 per NHS bed day appears unrealistically low.) Other studies of HAI costs show, in broad terms, estimates for the incremental cost of a single HAI in a range of £4,000 to £11,500. These studies focus on the typical costs associated with extended hospital bed days and increased drug expenditure. They typically do not include an estimate of litigation costs which are increasing fast in the UK. Further, in the private sector hospitals are

sensitive to the effect of reputation damage.

The United States' Centres for Disease Prevention and Control has estimated that HAI is costing US healthcare providers approximately \$US 6 billion, with some two million Americans being affected by HAI and an estimated 88,000 dying annually.

International Problem

HAI and antibiotic resistance is an international problem. Japan is reported to have MRSA rates (the proportion of *Staphylococcus aureus* blood isolates which are resistant to Methicillin) of some 64%. The US MRSA rates are estimated to range from 50% - 63%. In Europe, 2003 MRSA rates in Greece (52%) and the UK (44%) are cause for concern. In contrast the success of the Scandinavian and Dutch "search and destroy" policies can be seen with MRSA rates of circa 2%.

BIOQUELL's Clarus range of bio-decontamination equipment had an excellent year with strong revenue growth and continued market share capture. The pharmaceutical market is becoming much more aware of the technology and its benefits.



The importance of contamination control has long been accepted by the pharmaceutical sector and its regulators. During the year we saw good levels of demand for RBDS in the pharmaceutical sector and allied sectors such as medical devices, biomedical and biotechnology. We have made some progress migrating clients from an occasional to a scheduled service. We believe that there is considerable scope to extend the number of contract RBDS clients in the pharmaceutical sector.

We have also invested significant resources in developing the military and civilian defence market for RBDS. The United States Environmental Protection Agency published data generated from research undertaken with BIOQUELL's technology which demonstrated rapid bio-deactivation of anthrax on a range of substrates. Data also exist which suggest that BIOQUELL's technology will be effective against certain chemical weapons and we anticipate running chemical weapon and toxin deactivation trials later this year. This market is potentially large and BIOQUELL is talking to a number of government agencies; however, the decision making process tends to be slow and, in the absence of an unforeseen crisis involving biological, chemical or toxin agents, it will take time to generate substantial revenues in this market.

Clarus bio-decontamination equipment

Although the Clarus range of bio-decontamination equipment is not as high profile as the RBDS service, it had an excellent year with strong revenue growth and continues to take market share. Moreover, the pharmaceutical market is becoming much more aware of the technology and its benefits. BIOQUELL has an increasing international reputation for its expertise in this market segment.

BIOQUELL has a team of specialist consultants who advise clients on the optimal way to fulfil their bio-decontamination and regulatory requirements. There is a developing trend for these experts to be contacted by clients at the beginning of large investment programmes and accordingly BIOQUELL is able to ensure that the client gets an optimised solution using the Group's technology.

The launch in the UK market of the Clarus PORT generated revenues in the hospital pharmacy market which we anticipate will continue in 2005. The PORT is a rapid hydrogen peroxide vapour bio-decontamination device used by clients with a requirement for fast bio-decontamination of product or equipment.



EBDS and Service

During the year we launched EBDS – an Equipment Bio-Decontamination Service – principally for the laboratory equipment and research markets. There is increasing demand for this service from users of specialist equipment such as research robots as well as ubiquitous laboratory equipment including biological safety cabinets and incubators. One of the principal benefits of EBDS is that formaldehyde, a confirmed human carcinogen with persistent residues, is no longer needed to decontaminate laboratory equipment.

We invested significant time during the year working with our service clients to establish how best to integrate EBDS with the conventional preventative maintenance service required on laboratory equipment. We are seeing increasing success at selling this combined service to a range of users in the laboratory market.

We are also working with a number of service partners internationally who typically buy the

Review of activities

Continued



EBDS gives BIOQUELL an unique service offering

EBDS equipment, initially on an exclusive basis, and work with us to generate leads for RBDS.

The conventional laboratory equipment preventative maintenance service business remains highly commoditised and price sensitive; however, EBDS gives BIOQUELL an unique service offering which we expect will support and expand the conventional service business over the coming years.

Laboratory equipment

We are beginning to see an improvement in the sales of the Group's HEPA and activated carbon filtered products sold into the laboratory sector. Although the laboratory equipment market remains highly commoditised and price sensitive, with large volumes of equipment manufactured in the Far East, there are signs that many clients are prepared to pay a premium for expertise and associated service in the UK market. We have also been successful in winning large build contracts, which combine the requirement for BIOQUELL's laboratory equipment, Clarus technology and service provision. Further, the other large British manufacturers of biological safety cabinets have changed ownership or ceased to exist during the year creating further opportunities for us to take market share.

We do not anticipate substantial growth in this market but it appears that the decline in revenues has been arrested and its day to day operations are requiring less senior management time. Further, it gives BIOQUELL another conduit into its core markets and customers.

Defence

The Group's NBC (nuclear, biological and chemical) filtration defence business declined during the year. In the UK the Ministry of Defence is not currently buying any appreciable number of

new military vehicles hence demand for NBC is low. Demand from the overseas market is also subdued. However, during the year a small contract was won in the US market and we are proactively seeking to expand our market share in the United States. We also anticipate an increase in the spares market as vehicles are used in Iraq and other locations, and repairs as well as spare parts will inevitably be needed.



United States

BIOQUELL Inc had its first full year of trading in 2004 and showed strong growth. The business is winning market share and the US market for pharmaceutical research and production appears to be appreciably better funded than in Europe. We now have a high quality team of professionals in place and anticipate expanding this team further in 2005.

France

The French market remains challenging. During the year the business increased its turnover significantly although costs also increased. It is noteworthy that the first "superbug" RBDS bio-decontamination happened in a large French hospital. Notwithstanding the challenges of operating in France, we believe that it is worth persevering with this market as ultimately the potential size of the market is substantial and we have recruited a good team.

Sales and marketing

In addition to the investment in sales and marketing in the United Kingdom, the United States and France, the Group is considering means of expanding its routes to market principally in Europe and Asia. In Europe we are intending to put in place a network of agents to

The Group continues to invest in research and development as it believes that innovation is critical to its future success and there are a number of significant commercial applications for its low temperature, residue-free bio-decontamination technology.



ensure that BIOQUELL's technology becomes widely available and takes market share. In Asia we intend to emulate the success of BIOQUELL Inc and are examining the feasibility and financial viability of setting up an operation in the Far East.

We are also starting to invest further in marketing and business development to ensure that BIOQUELL exploits the "first mover" advantage, which it has in many sectors.

Research and development

The Group continues to invest in research and development as it believes that innovation is critical to its future success and there are a number of significant commercial applications for its low temperature, residue-free, bio-decontamination technology. In addition to research and development relating to the Group's hydrogen peroxide vapour technology, work continues on aqueous oxygen peroxide based equipment. Careful analysis of any market, particularly market size, is undertaken prior to any R&D taking place. Significant time and resources are spent in filing appropriate patent protection for the Group's technology and innovations.

Wound healing

The Group has been carrying out innovative research and development into novel wound healing technology for over three years exploiting its expertise in peroxide-based bio-decontamination. Patent protection has been filed on the technology. Regulatory approval for clinical trials in the UK was received at the end of last year. Clinical trials started earlier this year on venous leg ulcers at the Wound Healing Research Unit, at University of Wales College of Medicine. The initial results are encouraging. BIOQUELL is now undertaking the necessary product development engineering to bring a product to market.

Wound Healing

The market relating to wound care is substantial. According to the US National Institute of Nursing Research, chronic wounds such as leg ulcers, foot ulcers, pressure sores and surgical wounds affect up to 4.5 million Americans at a cost of more than \$9.5 billion annually. Leg ulcers are the most common of the chronic wounds with an estimated occurrence in approximately 1% of the world's population, representing some 2.5 million people in the United States. Burns victims also represent wounds which are hard to heal. The nature of chronic wounds is not well understood and treatments are currently not always successful.

The healing time for wounds can range from a few weeks to many months or even years depending on the size and type of the wound. Many leg ulcers remain unhealed for more than 10 years. Wound treatment currently comprises many direct and indirect costs, including wound dressings and the cost of medical staff needed to dress the wound.

Leg ulcers are thought to occur in approximately 0.5 to 1.0% of the US population, rising to 5% in the elderly. In the UK, it has been estimated that between 80,000 and 100,000 people suffer with a leg ulcer at any one time. Chronic leg wounds represent significant medical and financial challenges to healthcare systems. In the United States, it has been calculated that the average cost of treating a leg ulcer was approximately \$30,000 per year. Venous leg ulcers alone account for the loss of 2 million US work days per year. In the UK, the financial cost of venous disease (venous leg ulcers) has been estimated at between £294 and £650 million per year. Such wounds can significantly limit the mobility of patients and thus adversely affect their social, psychological, physical and economic quality of life. Moreover, many such wounds can become malodorous and cause substantial embarrassment to patients.



Review of activities

Continued



The acquisition of EMC Projects has been well received by Cape's clients

The current treatment for venous ulcers typically comprises the use of compressive wraps, bandages, semi rigid dressings and pumps to facilitate movement of excess fluid from the legs to promote wound healing.

The total cost of treatment of a diabetic foot ulcer has been reported to be in the range of \$10,000 to nearly \$60,000. Even when properly managed these wounds may not heal in a timely manner.

Cape

Cape enjoyed strong revenue and order intake growth during the year. It also undertook a number of key steps, including acquisition, equipment purchase and the provision of outsourced testing services, in order to position itself for growth in 2005 and beyond.

Cape's senior management team is taking a number of actions to strengthen and make more predictable the revenues from the core environmental testing business where profitability was below the level we were expecting. These have included focusing on securing long-term preferred supplier agreements or outsource partnerships. Examples include Rolls-Royce for whom Cape has established a dedicated testing facility at its Warwick site which is now undertaking a range of specialist tests on Rolls-Royce components. In addition Cape has established a testing facility in Wimborne for Flight Refuelling (and other South coast-based aerospace companies) and has signed a five year testing contract which is expected to generate revenues in excess of £1.25 million over the period. Cape has also taken over the specialist testing requirements for Areva, the French nuclear engineering group, in the UK. Cape intends to expand its provision of specialist outsource testing services in 2005.

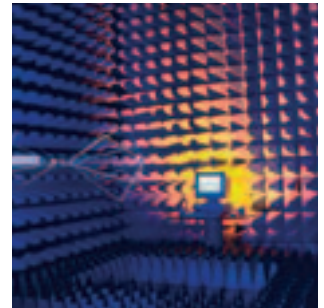
Cape has also expanded Cape-on-call, whereby specialist testing engineers undertake work at clients' facilities. Clients typically comprise blue-chip companies including, for example, Hewlett Packard.

Mindful of the trend of consolidation of suppliers and the opportunities available to Cape in other specialist testing fields, Cape acquired EMC Projects Limited at the beginning of June 2004. Cape has worked closely with EMC Projects for some 15 years and had previously subcontracted high levels of electromagnetic compatibility testing to this company. The acquisition has been well received by Cape's clients and a significant level of incremental work has been placed with EMC Projects from Cape's client base.

Cape believes that there are further opportunities to consolidate the provision of specialist testing services to large blue chip UK corporates and has signed marketing agreements and made strategic investments in specialist assets in order to optimise its position in any further consolidation in this sector.

Cape's software-based consultancy has started to show strong growth, particularly in the petrochemical field. Further investment is planned in 2005 in expanding this consultancy business, which undertakes finite element analysis and other structural stress related software modelling for clients. We believe that Cape has the opportunity and management team to develop a significant and profitable specialist testing business. We intend to continue to invest in the business and are expecting higher returns from Cape in the future.

Nick Adams
Chief Executive



Operations and finance review



Operations

The increase in turnover at the Group's Andover and Warwick sites required high quality execution by the operations teams during the year. This was made more challenging by the increasing levels of service activities, including the provision at short notice of emergency RBDS contracts. At the same time BIOQUELL continues to focus on initiatives to reduce its input, assembly and distribution costs. It is a credit to the operations personnel throughout the Group that they were able to cope with the fluctuating demands placed upon them, often at very short notice. It is notable that the core operations team based at Andover is high quality and multi-skilled and can assemble the full range of products, as well as provide service support for RBDS contracts.

During the year BIOQUELL Inc, based just north of Philadelphia, continued to expand. This has required investment in the development of a service team to, among other things, service Clarus equipment sold into the North American market. Recruitment of high quality individuals has been challenging and time consuming; however, the core team now in place at BIOQUELL Inc is competent and the business continues to grow.

Finance and controls

The Group is becoming increasingly complex notwithstanding its relatively small size. It is also expanding technologically and internationally. Accordingly BIOQUELL takes considerable care putting in place appropriate means to manage and monitor all its activities, in order to be able to manage the growth of the Group.

During the year a number of changes were made to the structure of the finance team at Andover. There has been a notable improvement in working capital levels notwithstanding the increase in turnover. The Group anticipates extracting further efficiencies and achieving improvements in customer service levels by investing in systems during 2005.

The increased margins and cash generative nature of the specialist service businesses started to affect the financial results of the Group positively in 2004. The balance sheet is sound and appropriate levels of overdraft facilities are in place.

BIOQUELL's detailed management information helps to ensure that there is a rigorous control of costs and detailed financial data across all parts of the business. This helps the management teams make informed and appropriate investments in capital equipment and

acquisitions, which totalled £0.9 million during 2004. The Group generated positive cashflow during the year before acquisitions and capital expenditure of £0.5 million (2003: cash outflow of £1.3 million).

At the end of 2004 the significant fall of the dollar against sterling caused a notable reduction in our sterling denominated results. As BIOQUELL Inc continues to grow – and with many Asian currencies currently pegged to the dollar – the Group has started to hedge a significant proportion of our anticipated dollar receipts on an annual basis.

International Financial Reporting Standards

BIOQUELL will be adopting International Financial Reporting Standards (IFRS) from 1 January 2005. This will affect the reporting of its future financial results in a number of ways.

For example, IFRS 2 "Share based payment" requires companies to expense via the Profit and Loss account the option value intrinsic in share options awarded to employees under the Group's Share Option Schemes. Currently no charges for the award of options arise under UK GAAP.

Goodwill arising on acquisition will also be frozen and a test for impairment undertaken annually. As a result goodwill amortisation charges previously made to the Profit and Loss Account will no longer occur. All development expenditure, previously written off in the year in which it was incurred, now has to be capitalised and amortised over an anticipated 10-year period under IAS 38 providing that the costs meet certain criteria.

IAS 39 introduces more stringent criteria for the accounting of hedging in respect of forward foreign exchange cover and the "marking to market" of such hedges and taking any gains or losses to the Profit and Loss Account.

The above is not intended to reflect the full impact of IFRS and the interpretation of IFRS, both in industry and the accounting profession, continues to develop in a number of areas.

BIOQUELL's 2005 interim and preliminary results will include information on the impact of IFRS on the Group's financial statements and a reconciliation of the necessary adjustments arising from the adoption of IFRS.

Mark Bodeker
Chief Operating Officer and Finance Director

Directors, officers and professional advisers

Directors

John Salkeld, FCA*

Non-Executive Chairman, joined the Board in March 1991. Previously he was a partner in Binder Hamlyn, Chartered Accountants, Director of Finance at GEC and Deputy Chief Executive of Myson Group. He was also Chairman of NEWSOM PLC and LICA Development Capital Limited and holds a number of other non-executive positions.

Nicholas Adams

Chief Executive, joined the Board in May 1997 and was appointed Chief Executive in May 1998. Previously he was a Director of Corporate Finance at Barings, having spent nine years in Barings' Corporate Finance Department both in the UK and continental Europe. He read chemistry at Durham University.

Mark Bodeker, CA

Chief Operating Officer and Finance Director, joined the Board in April 2000. He qualified with and subsequently worked for Deloitte Haskins and Sells for five years before moving to TI Group, holding a number of financial positions. Latterly he was divisional finance director of Meggitt Aerospace Components.

Simon Constantine, ACA*

Non-Executive Director, joined the Board in November 1999. Previously he held a number of financial and operational positions at Board level within Life Sciences International PLC. He is also a non-executive director of Sterigenics Holdings, Inc and Xena Systems Ltd.

Richard Towner*

Non-Executive Director, joined the Board in 1992. Previously he was a Corporate Finance partner of Richards Butler, a leading firm of City solicitors. He is a non-executive director of a number of private and quoted companies.

* Member of the Audit and Remuneration Committees.

Secretary

Mark Bodeker

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Stockbrokers

Investec Limited

Bankers

Barclays Bank PLC

Solicitors

Richards Butler

Financial PR

Redleaf Communications

Registrars

Capita IRG Plc

Directors' report

The directors present their annual report and the audited financial statements for the year ended 31 December 2004.

Principal activity

The Company is a holding Company with operating subsidiaries located in the United Kingdom and sales offices in France and the US.

The principal activity of the Group is the research and development, design, manufacture and supply of bio-decontamination and containment equipment, related products and services to the pharmaceutical, healthcare, food and other industries.

The Chairman's Statement and Review of Activities provide further details of the year under review and future developments.

Review of developments

The results for the year are set out in the profit and loss account on page 24. A review of the Group's business and future prospects is dealt with in the Chairman's Statement and the Chief Executive's Review of Activities.

Substantial shareholdings

The following interests in three per cent or more of the issued ordinary share capital, excluding Board members whose interests are disclosed in the Directors' Remuneration Report, had been notified to the Company:

Ordinary shareholders	Number	Percentage of issued Ordinary Share Capital
M&G Investment Management Limited	5,864,522	14.6%
Caledonia Investments PLC	5,162,499	12.9%
Hermes Investment Management Limited*	4,095,113	10.2%
A.H.J. Muir	1,454,453	3.6%
C.B.T. Adams	1,440,380	3.6%
Thompson Clive Investments Growth Industries Fund*	1,394,192	3.5%

*The registered owners of shares in which these holders have an interest may be subsidiaries and associated companies and/or pension funds, unit trusts or investment trusts under that holder's management.

Directors

The directors of the Company are shown on page 12. All of them served throughout the year. The interests of the directors in ordinary shares and options to acquire ordinary shares in the Company are shown in the Directors' Remuneration Report on pages 17 to 20.

None of the directors had any interest in the preference shares at any time during the year or subsequently.

Mr R E Towner will retire in accordance with the Articles of Association and being eligible will offer himself for re-election.

In common with all the non-executive directors, the services of Mr Towner are made available to the Company under a letter of appointment terminable at three months' notice.

Supplier payment policy

It is the policy of the Group, in the absence of dispute, to settle amounts due to trade and other creditors as expeditiously as possible within their terms of payment which are normally between thirty and sixty days. At the year-end the Group had 58 days (2003: 50 days) of purchase invoices outstanding.

Research and development expenditure

The Group's policy is to develop new and improve existing products and services to meet the needs of its customers. Expenditure in the year on research and development amounted to £936,000 (2003: £1,421,000).

Directors' report

Continued

Disabled employees

The Group continues its policy of giving disabled people full and fair consideration for all job vacancies for which they offer themselves as suitable applicants, having regard to their particular aptitudes and abilities. Training and career development opportunities are available to all employees and the Group endeavours to retain any member of staff who develops a disability during their employment.

Employee consultation

The Group continues to provide employees with information on matters of concern to them and regularly consults them and their representatives about the affairs of the Group.

Every reasonable effort is made to maintain and develop existing arrangements, which include life assurance and pension schemes and to promote awareness amongst the employees of the financial and economic factors affecting the performance of the Group.

Auditors

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

Approved by the Board of Directors,
and signed on behalf of the Board

Mark Bodeker
Secretary

11 April 2005

Corporate governance statement

This section of the annual report describes how the Company has applied the principles set out in the Combined Code on Corporate Governance issued by the Financial Reporting Council in July 2003 (the Combined 'Code'), which is appended to the Listing Rules of the Financial Services Authority, and for which the Board is accountable to shareholders. The Directors consider that throughout the year ended 31 December 2004 the Company has been in compliance with the provisions set out in Section 1 of the Combined Code, except for code provisions, A.1.3 and A.3.3 as the Board has not nominated a senior independent director other than the Chairman and code provision A.4.6 as there is no nominations committee. In both instances these exceptions arise because the Board is small. The Board also believes that the Company is in compliance with the recommendations set out in the Review of the Role and Effectiveness of Non-executive Directors (the Higgs Review) published in January 2004.

The Board comprises two executive and three non-executive directors. The non-executive directors are considered by the Board to be independent in character and judgement; the Board does not consider the fact that the non-executive directors hold shares in the company to impair their independence. The non-executive directors are required to submit themselves for re-election at regular intervals. This composition satisfies the Code's Principles and Provisions that the Board should have a balance of executive and non-executive directors in terms of number and relevant experience to enable it to have effective leadership and control of the Company and its subsidiaries. The directors have access to all information and, if required, independent professional advice at the expense of the Company. The Board normally convenes monthly with attendance by all directors, with the exception of Mr Adams who was unable to attend one of the 11 meetings, due to pre-arranged business commitments in the US. The Board has formally adopted a schedule of matters which are specifically reserved for its decision and retains full control over key strategic, financial and organisational issues within the Group.

The Board has established audit and remuneration committees. Although there is no formal nominations committee appointments to the Board are made following an interview process carried out by the Chairman and one other Non-Executive Director, again because the Board is small.

The Audit Committee, which met three times, consists of the three non-executive directors and is chaired by Mr J G Salkeld. This committee deals with issues such as the proper observation of

accounting standards, the application of the Group's accounting policies, its systems of internal controls and all issues relating to the preparation and approval of the Group's annual and half-yearly Reports and Accounts. The Group also considers the objectivity and independence of its Auditors by a process of assessment and keeping the scope of non-audit service and the level of non-audit fees under review. The Board is also involved in the approval of the audit fees and the Auditor's terms of engagement.

The Board has considered the need to introduce a Group internal audit function but has decided that the current control mechanisms are appropriate in the context of the size and complexity of the Group. The Board continues to review this position.

The Remuneration Committee consists of the three non-executive directors and is chaired by Mr R E Towner. This committee, which met three times, is responsible for recommending to the Board the terms of service and remuneration of the executive directors, including the allocation of share options. The report of the Remuneration Committee is included on pages 17 to 20.

The Board attaches a high priority to communications with shareholders. The Group's annual and half-yearly Reports and Accounts are sent to all shareholders. The Group meets regularly with its institutional shareholders and there is an opportunity for individual shareholders to question the Chairman and executive directors at the AGM.

An ongoing process for identifying, evaluating and managing significant risks faced by the Group has been in place since 1 January 2004 to the date of approval of the Annual Report and Accounts. That process is regularly reviewed by the Board and accords with "Internal Control: Guidance for Directors on the Combined Code" produced by the Turnbull working party.

The directors have overall responsibility for the system of internal control throughout the Group and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, as it can only provide reasonable, but not absolute, assurance against material misstatement or loss.

The Board has conducted a review of the effectiveness of the system of internal controls for the year ended 31 December 2004 and the period up to 11 April 2005. In carrying out this review the Board takes account of material developments through reports by the Group Finance Director and the Audit Committee.

Corporate governance statement

Continued

A risk management policy has been adopted by the Board setting out the Board's role and responsibilities and its overall approach to management and acceptance of risk. The directors and senior managers of each Group business are required to undertake their own risk identification and assessment according to their own individual circumstances, and this is then reviewed and evaluated by the Group Finance Director and submitted to the Board for their consideration.

The Board has established an organisation structure with clear lines of accountability. Formalised processes are in place for the preparation, review and approval of business plans, budgets and investment proposals for the Group as a whole and for the individual divisions. Financial results and other key business monitors are reported regularly and variances from approved budgets identified and used to initiate action. The Board has published, internally, management rules which include financial and operating control procedures with which the management of each subsidiary or division is required to comply.

Going concern

In accordance with the Corporate Governance requirements, the directors confirm that after making enquiries they have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Directors' remuneration report

Introduction

This report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002, which introduced new statutory requirements for the disclosure of directors' remuneration in respect of periods ending on or after 31 December 2002. The report also meets the relevant requirements of the Listing Rules of the Financial Services Authority and describes how the Board has applied the Principles of Good Governance relating to directors' remuneration. As required by the Regulations, a resolution to approve the report will be proposed at the Annual General Meeting at which the financial statements will be approved.

The regulations require the auditors to report to the Company's members on the 'auditable part' of the Directors' Remuneration Report and to state whether in their opinion that part of the report has been properly prepared in accordance with the Companies Act 1985 (as amended by the Regulations). The report has therefore been divided into separate sections for unaudited and audited information.

Unaudited Information Remuneration Committee

The Company has established a Remuneration Committee, which is constituted in accordance with the recommendations of the Combined Code. It consists of three independent non-executive directors: Mr J G Salkeld, Mr S J Constantine and Mr R E Towner (Chairman). Terms of reference are available for inspection.

Remuneration policy

The Committee follows certain fundamental principles in deciding levels and forms of remuneration. This includes providing a base salary, which reflects the current stage of development of the Group and aligning the interests of those executives with those of the shareholders through the use of share options and bonuses linked to, amongst other things, the development of the Group. The remuneration of the non-executive directors is determined by the Board within limits set out in the Articles of Association.

Basic salary

The basic salary of executive directors is determined by the Committee generally during March each year and when an individual changes position or responsibility. In addition to basic salary, the executive directors receive certain benefits-in-kind, principally private medical insurance.

Incentive Schemes/Share Option Schemes

Executive directors are eligible for an annual performance bonus based on attaining agreed profit levels and specific non-profit financial criteria, the amount of which is determined following an assessment by the Remuneration Committee, based on a number of quantitative and qualitative factors including the financial results and prospects of the Company at the relevant time and the implementation of the strategic plan. The Committee views the performance element as important and accordingly the bonus is determined following strict review.

There are no long-term incentive schemes other than the Share Option Schemes. As the Company is at an early stage in its development, share options are considered part of overall remuneration and are issued without pre-conditions, with the exception of Special Options granted to Mr N M T Adams and Mr B M Bodeker in 2004, which are conditional upon cumulative share price growth over a three year period.

The Committee is responsible for supervising the Company's Share Option Schemes in accordance with the rules approved by shareholders.

Pension arrangements

The Group operates a defined contribution pension scheme for employees and executive directors.

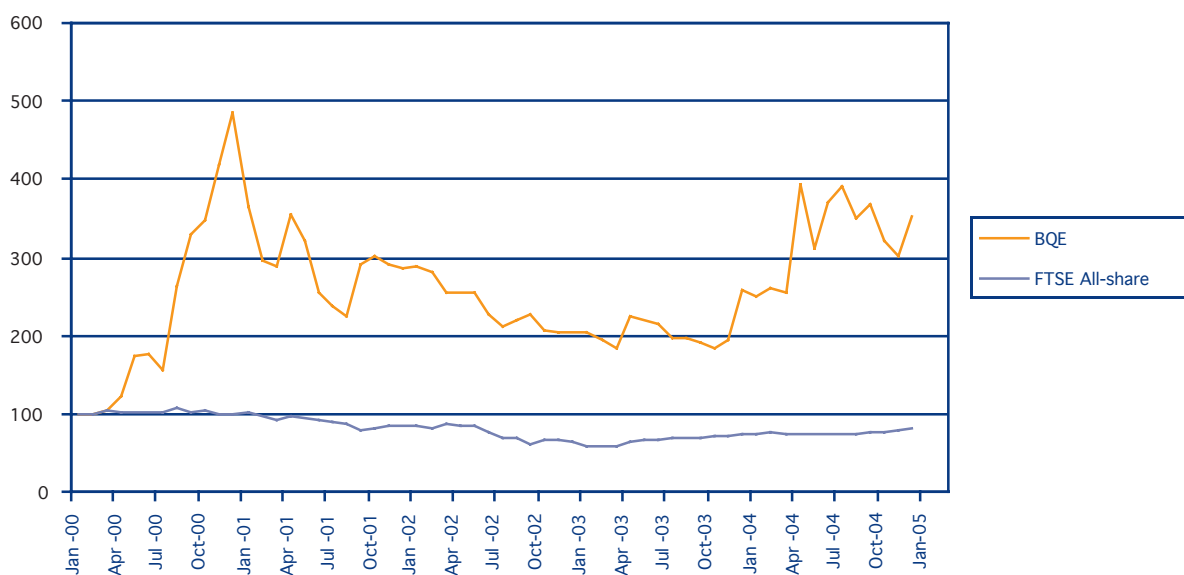
Directors' remuneration report

Continued

Performance graph

The following graph shows the Company's performance, measured by total shareholder return, compared with the performance of the FTSE All Share Index also measured by total shareholder return. The FTSE All Share Index is considered the most appropriate benchmark against which to measure Group performance. The graph is prepared on the basis of constituent companies in the Index at a point in time.

5 Year Index of BIOQUELL share price relative to FTSE All-share Index.



Directors' contracts

The executive directors have service contracts with an indefinite term with notice periods of 12 months in respect of Mr N M T Adams and 6 months in respect of Mr B M Bodeker. The contract date for Mr Adams and Mr Bodeker is 16 April 2000. In the event of a change of control of the Company, the notice periods of Mr Adams and Mr Bodeker are extended to two years, and this may be treated by the individual as a terminating event. In the event of early termination, the directors' contracts provide for basic compensation up to a maximum of basic salary for the notice period.

The Remuneration Committee considers these notice periods to be reasonable and proper and in the interests of both the Company and the directors, having regard to market conditions and current practice.

Non-executive directors

All non-executive directors have specific terms of engagement terminated on three months notice and their remuneration is determined by the Board within the limits set by the Articles of Association. The non-executives receive no further fees for additional work performed for the Company both in respect of membership of the Remuneration Committee and Audit Committee. Non-executive directors have historically participated in the Company's share option schemes but are not eligible to join the Company's pension scheme. The terms of employment of the non-executive directors are available for inspection.

Audited information

Aggregate directors' remuneration

The total amount for directors' remuneration was as follows:

	2004 £'000	2003 £'000
Emoluments	329	293
Gains on exercise of share options	256	–
Money purchase pension contributions	13	11
	598	304

Directors' emoluments

	Fees/basic salary £'000s	Benefits in kind £'000s	Annual bonuses £'000s	2004 £'000	2003 £'000
Executive					
Nicholas Adams	122	11	12	145	127
Mark Bodeker	112	7	12	131	113
Non-executive					
John Salkeld	23	–	–	23	23
Richard Towner	15	–	–	15	15
Simon Constantine	15	–	–	15	15
Aggregate emoluments	287	18	24	329	293

Directors' interest in ordinary shares

The directors who held office at 31 December 2004 had the following interests in the ordinary shares of the Company:

	31 December 2004	Percentage of share capital	1 January 2004
Beneficial holdings*			
J G Salkeld	2,001,477	5.0%	2,001,477
N M T Adams	667,562	1.7%	637,562
R E Towner	309,369	0.8%	309,369
S J Constantine	300,058	0.8%	300,058
B M Bodeker	10,000	–%	10,000
	3,288,466	8.3%	3,258,466

*Beneficial holdings include holdings of spouses and infant children

Directors' share options

Aggregate emoluments disclosed above do not include any amounts for the value of options to acquire ordinary shares in the Company granted to or held by the directors. Mr N M T Adams exercised 150,000 and sold 120,000 and Mr B M Bodeker exercised and sold 120,000 share options during the year. The market price at the date of exercise, in each case was £1.39 per share.

Directors' remuneration report

Continued

Details of options for directors who served during the year are as follows:

Name of director	1 Jan 2004	Granted/ (exercised)	31 Dec 2004	Exercise price (p)	Date	
					from which exercisable	Expiry date
Nicholas Adams	30,000	(30,000)	–	24.0	10.04.00	09.04.07
	70,000	(70,000)	–	18.5	06.05.01	05.05.05
	200,000	(50,000)	150,000	23.0	17.06.02	16.06.06
	200,000	–	200,000	44.0	19.04.03	18.04.07
	120,000	–	120,000	123.0	30.04.04	29.04.08
	80,000	–	80,000	107.5	30.04.05	29.04.09
	50,000	–	50,000	84.0	17.04.06	16.04.10
	–	400,000	400,000	120.5	07.04.07	06.04.11
Mark Bodeker	120,000	(120,000)	–	44.0	19.04.03	18.04.07
	100,000	–	100,000	123.0	30.04.04	29.04.08
	80,000	–	80,000	107.5	30.04.05	29.04.09
	100,000	–	100,000	84.0	17.04.06	16.04.10
	–	400,000	400,000	120.5	07.04.07	06.04.11
John Salkeld	25,000	–	25,000	44.0	19.04.03	18.04.07
	20,000	–	20,000	93.5	04.10.04	03.10.11
Richard Towner	25,000	–	25,000	44.0	19.04.03	18.04.07
	20,000	–	20,000	93.5	04.10.04	03.10.11
Simon Constantine	25,000	–	25,000	44.0	19.04.03	18.04.07
	20,000	–	20,000	93.5	04.10.04	03.10.11
	1,285,000	530,000	1,815,000			

Further information on the Share Option Schemes can be found in the unaudited section of this report, on pages 17 to 18.

The market price of the ordinary shares at 31 December 2004 was £1.50 (2003: £1.10) and the range during the year was £1.10 to £1.92.

Directors' pension entitlements

No directors are members of, or have any accrued benefits from, the Company's defined benefit scheme, which relates solely to former employees of the Group, details of which can be found in Note 23 to the Financial Statements. This scheme was closed to new members in May 1990.

Two directors are members of money purchase schemes, and the contributions paid by the Company in respect of such directors were as follows:

Name of director	2004 £'000	2003 £'000
Nicholas Adams	7	6
Mark Bodeker	6	5
	13	11

Approved by the Board of Directors,
and signed on behalf of the Board

Richard Towner
Chairman of the Remuneration Committee

11 April 2005

Statement of directors' responsibilities

United Kingdom company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the Group as at the end of the financial year and of the profit or loss of the Group for that year. In preparing these financial statements, the directors consider they have:

- selected suitable accounting policies and applied them consistently;
- made judgements and estimates that are reasonable and prudent; and
- followed applicable United Kingdom accounting standards.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for the Group's system of internal financial controls, for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent auditors' report

To the members of BIOQUELL PLC

We have audited the financial statements of BIOQUELL PLC for the year ended 31 December 2004, which comprise the consolidated profit and loss account, the balance sheets, the consolidated cash flow statement, the consolidated statement of total recognised gains and losses, the reconciliation of movements in consolidated shareholders' funds, the statement of accounting policies and the related notes 1 to 23. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the part of the Directors' Remuneration Report that is described as having been audited.

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 Auditors' 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

As described in the Statement of Directors' Responsibilities, the Company's directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. They are also responsible for the preparation of the other information contained in the annual report including the Directors' Remuneration Report. Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report that is described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report that is described as having been audited are properly prepared in accordance with the Companies Act 1985. We also report 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 or the Listing Rules regarding directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the July 2003 FRC Combined Code specific for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or

form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the Directors' Report and other information contained in the annual report for the above year as described in the contents section including the unaudited part of the Directors' Remuneration Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom auditing standards 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 and the part of the Directors' Remuneration Report that is described as having been audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, 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 and the part of the Directors' Remuneration Report that is described as having been audited 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 and the part of the Directors' Remuneration Report that is described as having been audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2004, and of the loss of the Group for the year then ended; and
- the financial statements and the part of the Directors' Remuneration Report that is described as having been audited have been properly prepared in accordance with the Companies Act 1985.

DELOITTE & TOUCHE LLP
Chartered Accountants and Registered Auditors
Reading

11 April 2005

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Consolidated profit and loss account

for the year ended 31 December 2004

	Notes	2004 £'000	2003 £'000
Turnover			
Existing operations		14,939	12,575
Acquisitions		555	–
Continuing operations	1	15,494	12,575
Cost of sales		(9,782)	(8,235)
Gross profit		5,712 37%	4,340 35%
Operating profit/(loss) before R&D and exceptional items		660	(269)
R&D	2	(936)	(1,421)
Exceptional items	2	–	(360)
Net operating expenses	2	(5,988)	(6,390)
Operating (loss)/profit			
Existing operations		(388)	(2,050)
Acquisitions		112	–
Continuing operations		(276)	(2,050)
Net interest payable and similar charges	4	(61)	(11)
Loss on ordinary activities before tax		(337)	(2,061)
Tax on loss on ordinary activities	5	173	222
Loss on ordinary activities after tax		(164)	(1,839)
Dividends on non equity shares	6	(11)	(11)
Retained loss for the year	20	(175)	(1,850)
Loss per share – basic and diluted	7	(0.4p)	(4.7p)

Movements in reserves are set out in note 20.

Group and company balance sheets

at 31 December 2004

	Notes	Group		Company	
		2004 £'000	2003 £'000	2004 £'000	2003 £'000
Fixed assets:					
Intangible assets	8	550	265	–	–
Tangible assets	9	2,849	2,721	12	13
Investments	11	–	–	7,454	7,453
		3,399	2,986	7,466	7,466
Current assets:					
Stocks	12	2,534	2,599	–	–
Debtors	13	4,646	3,504	1,263	1,149
Cash at bank and in hand	17	430	269	9,974	9,703
		7,610	6,372	11,237	10,852
Creditors:					
Amounts falling due within one year	14	(4,038)	(2,393)	(1,995)	(2,335)
Net current assets		3,572	3,979	9,242	8,517
Total assets less current liabilities		6,971	6,965	16,708	15,983
Creditors:					
Amounts falling due after more than one year	15	(570)	(543)	(413)	(411)
Provisions for liabilities and charges	18	(179)	(77)	–	–
Net assets		6,222	6,345	16,295	15,572
Capital and reserves:					
Called up share capital	19	4,166	4,124	4,166	4,124
Share premium	20	10,285	10,139	10,285	10,139
Capital reserve	20	255	255	255	255
Profit and loss account	20	(8,484)	(8,173)	1,589	1,054
Shareholders' funds		6,222	6,345	16,295	15,572
Shareholders' funds may be analysed as:					
Equity interests		6,072	6,195	16,145	15,422
Non equity interests		150	150	150	150
		6,222	6,345	16,295	15,572

The Financial Statements were approved by the Board of Directors and signed on its behalf by

Nicholas Adams }
Mark Bodeker } Directors

11 April 2005

Consolidated cash flow statement

for the year ended 31 December 2004

	Notes	2004 £'000	2003 £'000
Net cash in/(out) flow from operating activities	21(a)	412	(1,323)
Returns on investments and servicing of finance	21(b)	(72)	(22)
Capital expenditure and financial investment	21(c)	(649)	(989)
Acquisitions: EMC Projects Ltd	21(d)	(222)	–
Financing	21(e)	123	9
Decrease in cash in the year		(408)	(2,325)
Reconciliation of net cash flow to movement in net debt	21(f)		
Decrease in cash in the year		(408)	(2,325)
Cash outflow from decrease in debt financing		65	32
Change in net debt resulting from cash flows		(343)	(2,293)
New finance leases		–	(174)
Acquisitions: EMC Projects Ltd		(88)	–
Exchange difference		(3)	(34)
Movement in net debt in the year		(434)	(2,501)
Net (debt)/cash at 1 January		(305)	2,196
Net debt at 31 December		(739)	(305)

Consolidated statement of total recognised gains and losses

for the year ended 31 December 2004

	2004 £'000	2003 £'000
Loss for the financial year	(164)	(1,839)
Currency translation difference on foreign currency net investments	(136)	(36)
Total recognised loss relating to the year	(300)	(1,875)

Reconciliation of movements in consolidated shareholders' funds

for the year ended 31 December 2004

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
(Loss)/profit on ordinary activities after tax	(164)	(1,839)	546	58
Dividends on non equity shares	(11)	(11)	(11)	(11)
	(175)	(1,850)	535	47
Currency translation difference on foreign currency net investments	(136)	(36)	–	–
Shares issued and associated share premium	188	41	188	41
Net (decrease)/increase	(123)	(1,845)	723	88
Opening shareholders' funds	6,345	8,190	15,572	15,484
Closing shareholders' funds	6,222	6,345	16,295	15,572

The total amount of non equity interests in shareholders' funds is as follows:

	2004 £'000	2003 £'000
7.5% redeemable cumulative preference shares of £1 each (First Preference Shares)	150	150

Statement of accounting policies

The principal accounting policies are summarised below. They have all been applied consistently throughout the year and the preceding year.

Basis of accounting

The financial statements have been prepared under the historical cost convention and in accordance with applicable United Kingdom accounting standards.

Basis of consolidation

The Group financial statements consolidate the statements of the company and its subsidiary undertakings drawn up to 31 December each year. The results of subsidiaries acquired or sold are consolidated for the periods from or to the date on which control passes. Acquisitions are accounted for under the acquisition method.

Intangible fixed assets

Goodwill arising on the acquisition of subsidiary undertakings and businesses, representing the excess of the fair value of the consideration given over the fair value of the identifiable assets and liabilities acquired, is capitalised and written off on a straight line basis over its economic life, which is considered by the directors to be 10 years. Provision is made for any impairment.

Research and development

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

Tangible fixed assets

Tangible fixed assets are stated at cost, net of depreciation and provision for any impairment. Depreciation is provided on all tangible fixed assets at rates calculated to write off the cost or valuation, less estimated residual value, of each asset on a straight-line basis over its expected useful life, as follows:

Leasehold land and buildings	10 years
Plant, vehicles and machinery	3 to 8 years

Residual value is calculated on prices prevailing at the date of acquisition or revaluation.

Stocks

Stocks and work in progress are valued at the lower of cost, including factory overheads, and estimated net realisable value. Provision is made for obsolete, slow-moving or defective items where appropriate.

Taxation

Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided in full on material timing differences at the rate of tax anticipated to apply when these differences crystallise. Timing differences arise from the inclusion of items of income and expenditure in tax computations in periods different from those in which they are included in the financial statements. A deferred tax asset is only recognised where it is more likely than not that it will be recoverable in the future. Deferred tax assets and liabilities are not discounted.

Turnover

Turnover represents amounts receivable for goods and services provided in the normal course of business, net of trade discounts, VAT and other sales related taxes. Turnover is recognised on equipment sales upon delivery to or receipt by the customer and on services throughout the contract as services are provided or upon completion dependent upon contractual terms.

Pension costs

The defined benefit scheme, which has been closed to new members since May 1990 and relates solely to former employees of the Group, is managed in separate trustee-administered funds, with the assets of the scheme held separately from those of the Group. Pension scheme assets are measured at fair value and liabilities are measured independently on an actuarial basis. These valuations are obtained at least triennially and are updated at each balance sheet date.

For the defined contribution scheme the amounts charged to the profit and loss account in respect of pension costs and other post-retirement benefits is the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

Foreign currency transactions

Amounts receivable and payable in foreign currencies are generally translated into sterling at the rates of exchange ruling at the end of the period, or at the date of settlement. In cases where amounts receivable are covered by the forward sale of foreign currency, the rate at which the forward sale has been negotiated is used. Resulting exchange gains and losses are dealt with in the profit and loss account. For consolidation purposes, the assets and liabilities and profit and loss account of overseas operations are translated at the closing exchange rates. Exchange differences on this translation are taken to reserves.

Leases

Assets held under finance leases and other similar contracts are capitalised as tangible fixed assets and are depreciated over the shorter of the lease terms and their useful lives. The capital elements of future lease obligations are recorded as liabilities, while the interest elements are charged to the profit and loss account over the period of the leases to produce a constant rate of charge on the balance of capital repayments outstanding.

All other leases are treated as operating leases and their costs are charged to the profit and loss account as incurred.

Notes to the financial statements

for the year ended 31 December 2004

1. Turnover

Turnover represents amounts derived from the provision of goods and services which fall within the company's ordinary activities after deduction of trade discounts and Value Added Tax. The turnover, pre-tax loss and net assets, the majority of which arise in the United Kingdom (by origin), are attributable to a single class of business being the sale of bio-decontamination and filtration equipment and services.

The table below summarises turnover by destination.

	2004 £'000	2003 £'000
United Kingdom	9,657	8,392
Rest of Europe	2,435	1,963
Other	3,402	2,220
	15,494	12,575

2. Net operating expenses

	Existing operations 2004 £'000	Acquisitions 2004 £'000	Continuing operations 2004 £'000	Continuing operations 2003 £'000
Cost of Sales	9,427	355	9,782	8,235
Gross Profit	5,512	200	5,712	4,340
Net operating expenses				
Distribution costs	514	–	514	477
Administrative expenses	5,386	88	5,474	5,913
	5,900	88	5,988	6,390
Operating loss has been stated after charging:				
R&D expenditure			936	1,421
Legal costs including patent attorneys			36	–
Exceptional items: litigation and redundancy costs			–	360
Amortisation of intangible fixed assets			46	14
Amortisation of tangible fixed assets: – owned			807	764
– leased			17	21
Auditors' remuneration audit (Company: £4,475 (2003: £7,650))			58	57
tax compliance and advisory			17	17
Operating lease rentals in respect of:				
Plant and machinery			25	14
Other operating leases			679	575
Loss on disposal of fixed assets			5	–
Operating loss has been stated after crediting:				
Rents receivable			39	5

3. Staff costs

The average monthly number of employees (including executive directors) was:

	2004 Number	2003 Number
Production shop-floor	68	61
Engineering directs	46	50
	114	111
Sales & marketing	37	33
Administration	25	26
Other	13	16
	75	75
	189	186

Their aggregate remuneration comprised:

	2004 £'000	2003 £'000
Wages and salaries	5,772	5,112
Social security costs	652	562
Other pension costs	262	223
	6,686	5,897

Details of directors' remuneration, share options and pension contributions are included in the element of the Directors' Remuneration Report, marked as audited, on page 17 to 20.

4. Net interest payable and similar charges

	2004 £'000	2003 £'000
Payable		
Bank loans and overdrafts	53	24
Finance charges in respect of finance leases	10	7
	63	31
Receivable		
Bank interest	(2)	(20)
	61	11

Notes to the financial statements

for the year ended 31 December 2004

Continued

5. Tax on loss on ordinary activities

Analysis of tax credit on ordinary activities

	2004 £'000	2003 £'000
UK corporation tax on profits of the period at 30%	–	–
R&D tax credit	143	222
Adjustment in respect of prior periods	(27)	–
	116	222
Deferred tax: origination and reversal of timing differences	57	–
	173	222

Factors affecting tax credit for period

The tax assessed for the period is higher (2003: lower) than that resulting from applying the standard rate of corporation tax in the UK (30%). The differences are explained below:

	2004 £'000	2003 £'000
Loss on ordinary activities before taxation	(337)	(2,061)
Tax at 30% thereon	101	618
Effects of:		
Expenses not deductible for tax purposes	(55)	(18)
Capital allowances in excess of depreciation	209	(201)
Unutilised tax losses	(50)	(126)
Movement in short term timing differences	(40)	4
R&D tax credit	(26)	(55)
Overseas tax rate	4	–
Adjustment in respect of prior periods	(27)	–
	116	222

The Group is estimated to have an overall recognised deferred tax asset of £55,000 (2003: £nil), made up as follows:

	2004 £'000	2003 £'000
Capital allowances in excess of depreciation	(14)	–
Short term timing differences	2	–
Excess management expenses carried forward	67	–
	55	–

The Group also has an unrecognised deferred tax asset of £1,991,000 (2003: £2,117,000) relating mainly to trade losses. The asset has not been recognised as there is insufficient evidence that it will be recovered. The asset will be recovered if suitable profits are generated against which these losses can be offset.

The Group has estimated tax losses of £4,732,334 available for carry forward and offset against future taxable profits.

6. Dividends on non equity shares

	2004 £'000	2003 £'000
Paid and proposed dividends on non equity shares		
First Preference Shares		
7.5% redeemable cumulative preference shares of £1 each	11	11

7. Loss per share

The loss per ordinary share is based on a loss of £175,000 (2003: £1,850,000) being the loss after taxation less preference dividends. The weighted average number of shares during the year was 39,967,560 (2003: 39,677,730).

FRS 14 requires presentation of diluted EPS when a company could be called upon to issue shares that would decrease net profit or increase net loss per share. For a loss making company with outstanding share options, net loss per share would only be increased by the exercise of out-of-the-money options. Since option holders would normally only exercise for gain, and there are no other diluting future share issues, diluted EPS equals basic EPS.

8. Intangible fixed assets: goodwill

	Group Goodwill £'000
Cost	
As at 1 January 2004	279
Additions (note 11)	331
As at 31 December 2004	610
Accumulated amortisation	
As at 1 January 2004	14
Charge for the year	46
As at 31 December 2004	60
Net book value	
As at 31 December 2004	550
As at 31 December 2003	265

On 1 June 2004, Cape Engineering acquired EMC Projects Limited. Refer to note 11 for further details.

Notes to the financial statements

for the year ended 31 December 2004

Continued

9. Tangible fixed assets

	Short-term leasehold improvements £'000	Group Plant, vehicles and machinery £'000	Total £'000	Company Plant, vehicles and machinery £'000
Cost				
As at 1 January 2004	862	6,095	6,957	49
Additions	3	752	755	–
Acquisition of subsidiary undertaking	–	311	311	–
Disposals	–	(341)	(341)	–
As at 31 December 2004	865	6,817	7,682	49
Accumulated amortisation				
As at 1 January 2004	198	4,038	4,236	36
Charge for the year	56	768	824	1
Disposals	–	(227)	(227)	–
As at 31 December 2004	254	4,579	4,833	37
Net book value				
As at 31 December 2004	611	2,238	2,849	12
As at 31 December 2003	664	2,057	2,721	13

The figures stated above include assets held under finance leases as follows:

	Group	
	2004 £'000	2003 £'000
Net book value of plant and machinery	154	184

10. Capital commitments

The Group had capital expenditure contracted but not provided for at the year end of £19,125 (2003: £25,658).

11. Fixed asset investments

The companies listed below are all wholly owned trading subsidiaries of the Company, incorporated and operating in Great Britain, unless otherwise stated.

	Location
BIOQUELL UK Limited	Andover and Paris, France
Cape Engineering UK Limited	Warwick and Ringwood
BIOQUELL Inc	Philadelphia, USA

The activities of the above companies are the research and development, design, manufacturing and supply of bio-decontamination and containment equipment, related products and engineering services to the pharmaceutical, healthcare, defence and other industries.

	Company Investment in Group undertakings		
	Shares £'000	Loans £'000	Total £'000
Cost			
As at 1 January 2004	111	8,001	8,112
Additions	–	1	1
As at 31 December 2004	111	8,002	8,113
Impairment provision			
As at 1 January 2004	103	556	659
Charge for the year	–	–	–
As at 31 December 2004	103	556	659
Net book value			
As at 31 December 2004	8	7,446	7,454
As at 31 December 2003	8	7,445	7,453

On 1 June 2004 the Company's subsidiary, Cape Engineering Limited, acquired the entire share capital of EMC Projects Limited. The fair value of the total consideration was £601,000. The goodwill is being amortised over a period of ten years. The following table sets out the book value of the net assets and their fair value to the group:

	Book value £'000	Fair value adjustment £'000	Fair value to Group £'000
Net assets acquired:			
Tangible fixed assets	311	–	311
Stocks	16	–	16
Debtors	167	43	210
Creditors and provisions	(267)	–	(267)
	227	43	270
Goodwill	374	(43)	331
	601	–	601
Satisfied by:			
Cash consideration			222
Deferred consideration			379
			601

Notes to the financial statements

for the year ended 31 December 2004

Continued

11. Fixed asset investments continued

Deferred consideration estimated at £379,000 is contingent upon the profitability of the Company over a three year period ended 30 May 2007. The fair value adjustment has been made to properly account for the recoverable amount of trade debtors.

The profits/(losses) after taxation of EMC Projects Limited were as follows:

	Profit/(loss) after tax £'000
Results prior to acquisition	
Financial year ended 31 May 2004	(126)
Results subsequent to acquisition	
Date of acquisition to 31 December 2004	112

12. Stocks

	Group	
	2004 £'000	2003 £'000
Raw materials, spare parts and consumables	2,127	2,113
Work in progress	223	116
Finished goods and goods for resale	184	370
	2,534	2,599

13. Debtors

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Trade debtors	3,644	2,731	–	–
Amounts due from subsidiary undertakings	–	–	1,132	1,077
Other debtors	217	119	11	10
Corporation and other tax	364	350	12	31
Deferred tax	55	–	64	–
Prepayments and accrued income	366	304	44	31
	4,646	3,504	1,263	1,149

Included in Other debtors is an amount of £nil (2003: £29,000) due after more than one year. All other amounts are due within one year.

14. Creditors – amounts falling due within one year

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Bank overdraft	569	–	–	–
Finance leases (see note 16)	30	31	–	–
Payment received on account	15	–	–	–
Trade creditors	1,613	998	–	–
Amounts due to subsidiary undertakings	–	–	1,792	2,183
Taxation and social security	513	374	–	–
Accruals	1,292	981	197	143
Proposed preference dividend	6	9	6	9
	4,038	2,393	1,995	2,335

The Company has entered into a cross guarantee with subsidiary undertakings to guarantee the overdrafts of certain subsidiaries. The amount outstanding under this guarantee was £11,000,000 (2003: £11,000,000).

15. Creditors – amounts falling due after more than one year

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Bank loan	467	411	413	411
Finance leases (see note 16)	103	132	–	–
	570	543	413	411

A bank loan totalling £413,000 (2003: £411,000) is secured by a debenture creating a fixed and floating charge over all the assets of the Group, and has no fixed maturity date.

16. Finance leases

Net obligations under finance leases are secured on the assets to which they relate and are payable as follows:

	Group	
	2004 £'000	2003 £'000
Within one year	30	31
Between one and two years	30	30
Between two and five years	73	102
	133	163

Notes to the financial statements

for the year ended 31 December 2004

Continued

17. Financial instruments

The Group's financial instruments comprise cash balances, bank loans and overdrafts and various items such as trade debtors and creditors that arise directly from its operations. It is, and has been the Group's policy throughout the year, not to trade in financial instruments. The Group has taken advantage of the exemption available in FRS 13 Derivatives and Other Financial Instruments to exclude short term debtors and creditors from the disclosures of financial assets and liabilities.

Interest rate risk profile

Financial assets

The Group had financial assets as at 31 December 2004 of:

	Floating rate	
	2004 £'000	2003 £'000
Sterling	–	243
Euros	46	26
US Dollars	384	–
	430	269

Cash deposits are placed on short term deposit generating interest at a floating rate based on LIBOR.

The interest rate profile of the Group's financial liabilities as at 31 December 2004 was:

	Fixed rate		Floating rate	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Sterling				
Finance leases	103	132	–	–
Non equity shares	150	150	–	–
Euro				
Borrowings	413	411	54	–
	666	693	54	–

Further analysis of the interest rate profile at 31 December 2004 is as follows:

	2004		2003	
	Weighted average interest rate %	Weighted average period for which rate is fixed (years)	Weighted average interest rate %	Weighted average period for which rate is fixed (years)
Sterling				
Finance leases	8.3%	4	8.3%	5
Euro				
Borrowings – PLC	4.5%	1	4.5%	1
– EMC	7.25%	3	–	–
		2		2

The Group's policy for future borrowing will be to take floating rates unless fixed rate financing is available at more attractive rates.

The fair value of the above financial instruments is approximately equal to book value.

17. Financial instruments continued

Maturity of financial liabilities

The Company has a currency loan denominated in EUROS bearing interest at a fixed rate of 4.54%, and it is anticipated this will be converted into a term facility over a 3-year period from December 2004. In addition Cape, through the acquisition of EMC Projects Ltd, has a sterling denominated loan bearing interest at a floating rate that is repayable over three years.

For other financial liabilities, the maturity profile is shown in notes 16 and 19.

Currency profile

The main functional currencies of the Group are Sterling, the EURO and the US Dollar. The monetary assets and liabilities of the Group are held in the same functional currencies of the operations involved.

Borrowing facility

The Group had committed overdraft facilities available at 31 December 2004 of £2,200,000 (2003: £2,200,000). The facility is reviewable each year.

Liquidity risk

The Group's policy is to ensure that it has available sufficient facilities to enable it to satisfy its peak borrowing requirements with an appropriate level of headroom.

18. Provisions for liabilities and charges

Group	£'000
As at 1 January 2004	77
Charge for the year	102
Utilised during the year	–
As at 31 December 2004	179

The amounts above relate to warranty to be utilised over a 12 month period.

19. Called up share capital

	2004		2003	
	Number	£'000	Number	£'000
Authorised				
Ordinary shares of 10p each	55,947,780	5,595	55,947,780	5,595
First preference shares of £1 each	150,000	150	150,000	150
Redeemable deferred ordinary shares of £1 each	255,222	255	255,222	255
		6,000		6,000
Called up, allotted and fully paid				
Ordinary shares of 10p each	40,160,596	4,016	39,738,602	3,974
First preference shares of £1 each	150,000	150	150,000	150
		4,166		4,124

During the year the Company issued a total of 421,994 ordinary shares of 10p each for £188,000 on the conversion of options under the executive share option schemes, which is being used to provide additional working capital.

Notes to the financial statements

for the year ended 31 December 2004

Continued

19. Called up share capital continued

The First Preference Shares are redeemable at the option of the Company at a premium of 12.5p per share. Holders of the First Preference Shares have no voting rights unless the dividend has remained unpaid for six months after any half yearly payment date or a resolution is proposed for winding up the Company or reducing the capital of the Company or adversely varying the holders' rights and privileges.

When either of these criteria applies then holders of Preference Shares are entitled, on a show of hands, to one vote and, on a poll, holders present in person or by proxy are entitled to four votes for every one First Preference Share held. On the winding up of the company, the holders of the First Preference Shares receive a return of their capital together with a further amount by way of a premium of 12.5p per share together with all arrears of dividend, in priority to any repayment to any of the holders of ordinary shares.

The following options to subscribe for ordinary shares have been granted pursuant to the terms of the Share Option Schemes to employees:

Number of ordinary shares	Date from which exercisable	Expiry date	Exercise price
8,000	19.10.98	18.10.05	20.0p
25,000	15.04.99	14.04.06	22.0p
25,000	24.09.99	23.09.06	28.5p
10,000	06.05.01	05.05.05	18.5p
15,000	17.06.02	16.06.06	23.0p
102,000	17.06.02	16.06.09	23.0p
24,000	19.04.03	18.04.07	44.0p
79,000	19.04.03	18.04.10	44.0p
15,000	13.09.03	12.09.10	74.5p
42,000	30.04.04	29.04.08	123.0p
76,000	30.04.04	29.04.11	123.0p
35,000	04.10.04	03.10.11	93.5p
71,750	30.04.05	29.04.09	107.5p
151,150	30.04.05	29.04.12	107.5p
116,000	17.04.06	16.04.10	84.0p
179,000	17.04.06	16.04.13	84.0p
280,000	07.04.07	06.04.11	120.5p
392,000	07.04.07	06.04.14	120.5p
10,000	16.09.07	15.09.14	137.5p
1,655,900			

During the year the following options were granted or lapsed:

	Directors Number	Employees Number	Total Number
As at 1 January 2004	1,285,000	1,175,400	2,460,400
Lapsed	–	(73,000)	(73,000)
Converted	(270,000)	(128,500)	(398,500)
Granted	800,000	682,000	1,482,000
As at 31 December 2004	1,815,000	1,655,900	3,470,900

Further details of Directors' options are given in the Directors' Remuneration Report on pages 17 to 20.

20. Reserves

	Share premium £'000	Capital reserve £'000	Profit and loss account £'000
Group			
As at 1 January 2004	10,139	255	(8,173)
Arising on share issue	146	–	–
Retained loss for equity shareholders	–	–	(175)
Currency translation difference on the foreign currency net investments	–	–	(136)
As at 31 December 2004	10,285	255	(8,484)
Company			
As at 1 January 2004	10,139	255	1,054
Arising on share issue	146	–	–
Retained profit for equity shareholders	–	–	535
As at 31 December 2004	10,285	255	1,589

At 31 December 2004 the amount of purchased goodwill written off directly to reserves was £3,434,000 (2003: £3,434,000).

In accordance with Section 230 of the Companies Act 1985 BIOQUELL PLC is exempt from the requirement to present its own profit and loss account. The profit after taxation, dealt with in the financial statements of the company, is £535,000 (2003: £47,000).

In accordance with the transitional provisions of FRS 17, Retirement Benefits, the following additional reconciliation is provided showing Group profit and loss account reserves if FRS 17 were to be adopted in full:

	2004 £'000	2003 £'000
Profit and loss deficit excluding pension liability	(8,484)	(8,173)
Pension liability net of deferred tax	(97)	(97)
Profit and loss after deducting pension liability	(8,581)	(8,270)

Notes to the financial statements

for the year ended 31 December 2004

Continued

21. Notes to the cashflow

	2004 £'000	2003 £'000
(a) Reconciliation of operating loss to operating cash flows:		
Operating loss	(276)	(2,050)
Amortisation of intangible assets	46	14
Amortisation of tangible assets	824	785
Loss on disposal of fixed assets	5	–
Decrease in stocks	82	154
Increase in debtors	(759)	(19)
Increase/(decrease) in creditors	388	(161)
Increase/(decrease) in provisions	102	(46)
Net cash inflow (outflow) from operating activities	412	(1,323)
(b) Returns on investments and servicing of finance:		
Interest received	2	19
Interest paid	(53)	(24)
Interest element of finance lease rental payments	(10)	(6)
Preference dividend paid	(11)	(11)
Net cash outflow from returns on investments and servicing of finance	(72)	(22)
(c) Capital expenditure and financial investment		
Purchase of intangible fixed assets	–	(51)
Purchase of tangible fixed assets	(754)	(970)
Sale of tangible fixed assets	105	32
Net cash outflow from capital expenditure	(649)	(989)
(d) Acquisitions		
Purchase of subsidiary undertaking	(222)	–
Net cash outflow from acquisitions	(222)	–
(e) Financing		
Proceeds from share issue	188	41
Repayment of loans	(35)	–
Capital element of finance lease rental payments	(30)	(32)
Net cash inflow from financing	123	9

21. Notes to the cashflow continued

	At 1 January 2004 £'000	Cash flow £'000	Acquisitions £'000	Exchange movements £'000	At 31 December 2004 £'000
(f) Analysis of net debt					
Cash at bank and in hand	269	161	–	–	430
Overdrafts	–	(347)	(222)	–	(569)
	269	(186)	(222)	–	(139)
Debt after 1 year	(411)	35	(88)	(3)	(467)
Finance leases	(163)	30	–	–	(133)
	(574)	65	(88)	(3)	(600)
	(305)	(121)	(310)	(3)	(739)

The acquisition of EMC Projects Limited in the year contributed £111,000 to the Group's net operating cashflows, paid £35,000 in respect of net return on investments and services of finance, paid £nil in respect of taxation and utilised £3,000 for capital expenditure.

22. Financial commitments

Annual commitments under non-cancellable operating leases are as follows:

	Group			
	Land & buildings		Other	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Expiry date:				
Within one year	68	–	3	3
Between two and five years	294	338	279	151
After five years	177	156	–	–
	539	494	282	154

23. Pension arrangements

The Company operates a defined benefit scheme which has been closed to new members since May 1990 and whose assets are held separately from those of the Company. A full actuarial valuation was carried out at 5 April 2003 and updated to 31 December 2004 by a qualified actuary. As at 5 April 2003, the scheme was 84% funded. The major assumptions used for the actuarial valuation were:

	2004	2003	2002
Rate of increase in salaries	N/a	N/a	N/a
Rate of increase in pension payment	3.0%	3.0%	3.0%
Discount rate	5.5%	5.5%	5.5%
Inflation assumption	3.0%	3.0%	2.5%

In the year to 31 December 2004, the Company made contributions of £1,000 (2003: £8,400) and contributions will continue at this level for the foreseeable future. The pension cost charge equals the contributions made.

Notes to the financial statements

for the year ended 31 December 2004

Continued

23. Pension arrangements continued

The Group also operates a number of defined contribution pension schemes. The pension cost charge for the year represents contributions payable by the Group to the funds and amounted to £271,000 (2003: £279,000). Amounts owing to schemes at 31 December 2004 amounted to £21,000 (2003: £25,000).

The fair value of assets in the defined benefit scheme, the present value of the liabilities and the expected rate of return at each balance sheet date were:

	31 December 2004		31 December 2003		31 December 2002	
	Long term rate of return	Fair value £'000	Long term rate of return	Fair value £'000	Long term rate of return	Fair value £'000
Equities	7.5%	76	7.5%	95	7.0%	104
Bonds	5.5%	309	5.5%	287	5.5%	284
Other	3.5%	47	3.5%	45	4.0%	34
Total fair value of assets		432		427		422
Present value of scheme liabilities		570		565		540
Liability in the scheme		(138)		(138)		(118)
Related deferred tax credit		41		41		35
Net pension liability		(97)		(97)		(83)

Additional FRS 17 disclosures

Analysis of the amount charged to operating profit if FRS 17 were to be adopted:

	2004 £'000	2003 £'000
Current service cost	–	–
Past service cost	–	–
Gains and losses on any settlements or curtailments	–	–
	–	–

Analysis of the amount credited to other finance income:

	2004 £'000	2003 £'000
Expected return on pension scheme assets	24	21
Interest on pension scheme liabilities	(30)	(29)
Net return	(6)	(8)

Analysis of the actuarial loss in the statement of total recognised gains and losses:

	2004 £'000	2003 £'000
Actual return less expected return on pension scheme assets	5	–
Experience gains and losses arising on the scheme liabilities	–	–
Changes in assumptions underlying the present value of the scheme liabilities	–	(20)
	5	(20)

23. Pension arrangements continued

Movement in the scheme deficit during the year:

	2004 £'000	2003 £'000
At 1 January 2004	(138)	(118)
Employer's contributions	1	8
Net interest charges	(6)	(8)
Actuarial gain/(loss)	5	(20)
At 31 December 2004	(138)	(138)

History of experience gains and losses:

	2004 £'000	%	2003 £'000	%	2002 £'000	%
Differences between the expected and actual return on scheme assets	5	1%	–	–	(35)	8%
Experience gains on scheme liabilities	–	–	–	–	31	6%
Total actuarial gain/(loss)	5	1%	(20)	4%	(39)	7%

The information set out above is for memorandum purposes only as the net pension liability in respect of the defined benefit scheme of £97,000 (2003: £97,000) has not been reflected in the financial statements.

Five year summary

	2004 £'000	2003 £'000	2002 £'000	2001 £'000	2000 £'000
Turnover	15,494	12,575	12,243	15,869	14,579
Research & development	(936)	(1,421)	(1,656)	(1,168)	(1,671)
Exceptional costs	–	(360)	(763)	–	–
Operating (loss)/profit	(276)	(2,050)	(2,529)	(1,202)	(2,389)
Loss on ordinary activities after tax	(164)	(1,839)	(2,235)	(1,344)	(2,608)
Shareholders' funds	6,222	6,345	8,190	4,146	4,185
Loss per share	(0.4p)	(4.7p)	(5.9p)	(4.2p)	(9.5p)

BIOQUELL PLC

Notice of Annual General Meeting

Notice is hereby given that the Annual General Meeting of BIOQUELL PLC will be held at the offices of the Company, 34A Walworth Road, Andover, Hampshire SP10 5PY on 23 May 2005 at 12.00pm for the following purposes:

1. To receive and consider the audited accounts and report of the Directors and Auditors for the year ended 31 December 2004.
2. To approve the Directors' Remuneration Report for the year ended 31 December 2004.
3. To reappoint Deloitte & Touche LLP as auditors of the Company and to authorise the Directors to determine the remuneration of the Auditors.
4. To re-elect Mr R E Towner as a director of the Company.
5. To authorise the payment of the dividend for the year on the 7.5 per cent redeemable cumulative preference shares (First Preference Shares) as specified in the accompanying Chairman's Statement.

As special business to consider and if thought fit, pass the following resolutions, of which resolution number 6 will be proposed as an ordinary resolution and resolution number 7 as a special resolution.

Ordinary resolution

6. (1) The Directors be and they are hereby generally and unconditionally authorised pursuant to and for the purpose of section 80 of the Companies Act 1985 to exercise all the powers of the Company to allot relevant securities (within the meaning of that section) up to a maximum aggregate nominal amount of £1,338,687 at any time on or before the conclusion of the Annual General Meeting of the Company to be held in 2006 or the date falling 15 months after the passing of this resolution (whichever is the earlier);
(2) The Company be allowed to make any offer or agreement which will or might require any such relevant securities to be allotted or any such rights to be granted after the expiry of this authority and the Directors may, notwithstanding such expiry, allot shares and grant such rights pursuant to any such offer or agreement made by the Company as if the authority conferred hereby has not expired; and
(3) This authority be in substitution for all existing authorities given by the Company pursuant to and for the purpose of section 80 of the Companies Act 1985 to the extent that such authorities are not exercised.

Special resolution

7. That the Directors of the Company be and they are hereby generally and unconditionally authorised at any time during the period commencing on the date of the passing of this resolution and expiring at the conclusion of the Annual General Meeting of the Company to be held in 2006 or on the date falling 15 months after the passing of this resolution (whichever is the earlier) and at any time thereafter, notwithstanding that this authority has expired, pursuant to any offer or agreement made by the Company before the expiry of such period, to allot any equity securities of the Company under any authority conferred on them from time to time pursuant to section 80 of the Companies Act 1985 or any re-enactment thereof ("the Act") as if section 89(1) of the Act did not apply thereto, provided that such authority and power shall be limited to the allotment of equity securities (as defined for the purpose of section 95 of the Act), as follows:
 - (a) in connection with any rights issue or issues of equity securities to the holders of relevant shares of the Company in proportion (as nearly as may be) to their respective holdings of such shares or (where applicable) in accordance with the rights for the time being attached to such shares (but subject to statutory exclusion, or other arrangements as the Directors may deem necessary or expedient to deal with problems under the laws of any territory or the requirements of any regulatory body or any stock exchange in any territory or in connection with fractional entitlements or otherwise howsoever); and
 - (b) any other allotment for cash of equity securities up to a maximum aggregate nominal value of £200,803.

Registered office
34A Walworth Road
Andover
Hampshire
SP10 5PY

11 April 2005

By order of the Board
Mark Bodeker
Secretary

Notice of Annual General Meeting

Continued

Notes:

1. A member entitled to attend and vote at the Annual General Meeting is entitled to appoint one or more proxies to attend and, on a poll, vote on his or her behalf. A proxy need not be a member of the Company. Holders of First Preference Shares are not entitled, as such, to attend and vote at the Annual General Meeting.
2. A form of proxy is provided with this notice and instructions for use are shown on the form. To be valid, forms of proxy must be completed in accordance with the instructions set out in the form and returned so as to be received at the offices of the Company's Registrars, Capita IRG plc, Bourne House, 34 Beckenham Road, Beckenham, Kent BR3 4TU, not less than 48 hours before the time fixed for the Annual General Meeting (i.e. no later than 12.00pm on 23 May 2005) or any adjournment thereof. Completion of the form of proxy will not preclude a member from attending and voting in person at the meeting if the member so wishes.
3. Copies of the Directors' letters of appointment and service contracts are available for inspection at the registered office of the Company, 34A Walworth Road, Andover, Hampshire SP10 5PY during usual business hours on each business day and will also be available at the place of the Annual General Meeting for at least 15 minutes prior to and during the Annual General Meeting. The register of Directors' interests will be available for inspection at the commencement of, and during, the Annual General Meeting.
4. As permitted by regulation 41 of the Uncertificated Securities Regulations 2002, only those shareholders who are registered on the Company's register of members at 12.00pm on 23 May 2005 or, in the event that the Annual General Meeting is adjourned, on the register of members 48 hours before the time of any adjourned meeting, shall be entitled to attend the Annual General Meeting and to vote in respect of the number of ordinary shares registered in their names at that time. Changes to entries on the register of members after 12.00pm on 23 May 2005 or, in the event that the Annual General Meeting is adjourned, on the register of members 48 hours before the time of any adjourned meeting, shall be disregarded in determining the right of any person to attend and/or vote at the Annual General Meeting.

Explanatory notes

1. **Resolutions 1 & 2: Report of Directors and Accounts**
The Directors must lay the Company's Accounts, the Directors' Report, the Directors' Remuneration Report and the Auditors' Report before the members in general meeting. This is a legal requirement once the Directors have approved the Accounts and the Directors and the Auditors have prepared their respective reports.
2. **Resolution 3: Appointment of Auditors**
At each Annual General Meeting, the Company is required to appoint auditors to serve until the next such meeting. Resolution 3 proposes the re-appointment of the Company's present auditors, Deloitte & Touche LLP. In accordance with normal practice, the Directors should be authorised to fix their remuneration.
3. **Resolution 4: Re-election of Directors retiring by rotation**
Article 69 of the Company's Articles of Association states that one third of the directors, subject to retirement by rotation, shall retire from office at each Annual General Meeting. Mr R E Towner has agreed, in accordance with the Company's Articles of Association, that he shall retire and, being eligible, offers himself for re-appointment. Biographical details of Mr R E Towner are set out in the Report and Accounts.
4. **Resolution 5: Payment of dividend**
Article 119 of the Company's Articles of Association requires dividends to be declared by ordinary resolution of the Company. No dividend may exceed the amount recommended by the directors. The directors recommend a payment of £11,250 on the First Preference Shares representing 7.5p per First Preference Share.
5. **Resolution 6: Renewal of Section 80 authority**
This Resolution provides for the grant of authority to the Directors pursuant to Section 80 of the Companies Act 1985 to allot shares to a nominal value of £1,338,687. The authority will terminate no later than 15 months after the Annual General Meeting.
6. **Resolution 7: Renewal of directors' authority to allot shares for cash**
Section 89 of the Companies Act 1985 requires ordinary shares allotted for cash (other than pursuant to employee share schemes) to be offered to existing shareholders on a pro rata basis. Resolution 7 allows the directors to allot shares other than in accordance to Section 89 in connection with rights issues and other offers, and otherwise up to a maximum nominal amount of £200,803, representing approximately 5% of the Company's issued ordinary share capital as at 11 April 2005. The authority will terminate no later than 15 months after the Annual General Meeting.

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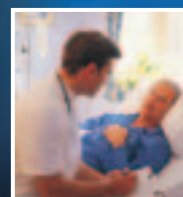
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