



WORLD LEADERS IN BIO-DECONTAMINATION, ENVIRONMENTAL CONTROL AND TESTING.

The BIOQUELL Group comprises two divisions; Bio-decontamination and TRAC – Testing, Regulatory and Compliance – which includes Cape and new service businesses, TRL Compliance and KTL, acquired in October 2005.



THE BIO-DECONTAMINATION DIVISION

RBDS – the Room Bio-Decontamination Service (RBDS)

CLARUS – hydrogen peroxide vapour bio-decontamination equipment

LABORATORY – Microflow and Astec branded specialist laboratory filtration equipment

DEFENCE – chemical, biological, radiological and nuclear (CBRN) filtration equipment

SERVICE – after-sales service and support

THE TRAC DIVISION

CAPE – environmental testing and finite element analysis

TRL Compliance – electromagnetic compatibility (EMC) testing

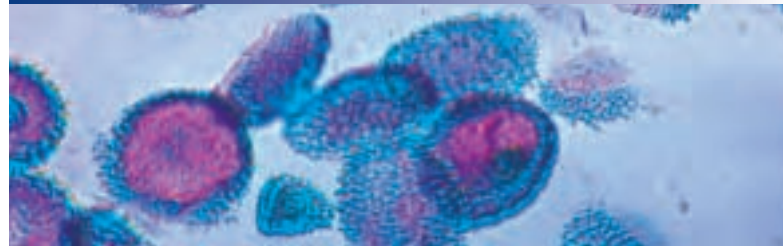
EMC Projects – EMC testing

KTL – specialist telecoms testing

KTL Inc – specialist telecoms testing (eg DSL, VoIP) located in Santa Clara, California

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BIOQUELL – an overview

- the Group moves firmly into profit
- turnover £25.2 million (2005: £17.2 million), a 47% increase (excluding acquisitions, organic revenue growth was 19%)
- increase in gross margin to 39% (2005: 37%), reflecting the increasing proportion of turnover from higher value equipment and services
- gross expenditure on product development £1.0 million (2005: £1.2 million)
- profit before tax: £1.2 million (2005: loss: (£0.5) million)
- net cash from operating activities £3.5 million (2005: £1.7 million)
- capital expenditure £1.5 million (2005: £1.2 million)
- net debt £0.6 million (2005: £1.6 million) – gearing 5% (2005: 16%)
- net assets £11.5 million (2005: £10.1 million)
- basic earnings per share 2.9p (2005: (0.8)p)



OPERATIONAL

Bio-decontamination division

- turnover £14.6 million (2005: £11.5 million), organic growth of 27%
- strong growth in hydrogen peroxide vapour ("HPV") bio-decontamination equipment and service revenues, particularly in North America
- launch of new product: BIOQUELL Z – for zone/room bio-decontamination – to generate increased international revenues
- licensing of RBDS to international partners to increase market share and international revenues
- increased "superbug" problems in healthcare facilities leading to higher bio-decontamination revenues
- substantial growth in specialist CBRN (chemical, biological, radiological and nuclear) filtration system revenues from defence sector
- pursuing further significant defence-related opportunities for BIOQUELL's HPV and CBRN filtration technologies
- good progress on the development of new wound healing technology – amalgamation of two clinical trials into one

TRAC (Testing, Regulatory and Compliance) division

- turnover £10.6 million (2005: £5.7 million), a 86% increase (adjusting for acquisitions, the organic increase in revenues was 4%)
- strong performance from TRL Compliance and KTL – the two businesses acquired in October 2005
- property consolidation progressing to plan: the new EMC centre of excellence for TRLC generating significant interest from the military/aerospace market
- military/aerospace orders robust throughout the TRAC division
- new management at Cape making good progress with significantly reduced cost base
- integration of businesses under TRAC Global branding proceeding well and beginning to generate significant incremental revenues and take market share

Chairman's statement



The increased turnover from the Bio-decontamination division was seen across a broad range of sectors and territories

Overview

The BIOQUELL Group comprises two divisions: Bio-decontamination and TRAC – Testing, Regulatory and Compliance – which includes Cape and the new service businesses, TRL Compliance and KTL, acquired in October 2005.

Results and finance

Turnover for the Group increased by 47% to £25.2 million (2005: £17.2 million). Excluding the two businesses acquired in October 2005, the Group's revenues showed organic growth of 19%. The Bio-decontamination division's revenues in 2006 were £14.6 million (2005: £11.5 million), representing organic growth of 27%. The TRAC division's revenues were £10.6 million (2005: £5.7 million), representing growth of 86%; growth excluding the effect of acquisitions was 4%. The Group's revenues outside the UK increased by 75% from £4 million to £7 million, largely reflecting increased US sales in the bio-decontamination sector.

The increased turnover from the Bio-decontamination division was seen across a broad range of sector and territories, although growth in Clarus equipment and RBDS (Room Bio-Decontamination Service) revenues was particularly strong in North America. Significant growth was also seen in the Group's defence business which supplies specialist CBRN (Chemical, Biological, Radiological and Nuclear) filtration and environmental control equipment. Turnover in the Group's original laboratory equipment and after-sales service businesses was basically unchanged. The consolidated gross margin showed a further increase of 2% to 39% reflecting the higher value equipment and service revenues.

Demand remained strong for the specialist testing, regulatory and compliance services provided by businesses within the TRAC division, particularly from clients in the defence, aerospace and telecoms sectors. The integration of the five separate testing businesses into one division is

proceeding well and we are already seeing tangible commercial benefits from increased levels of sales from across the enlarged division's client base. The TRAC division's gross margin increased by two percentage points to 38%, reflecting the higher margins generated by the businesses acquired late in 2005.

Gross expenditure on product development in the year was £1.0 million (2005: £1.2 million). This reflects the continuing high levels of expenditure on new products, such as the recently launched BIOQUELL Z, as well as new wound healing technology which the Group is developing. It also reflects the ongoing research we are undertaking in the eradication of "superbugs" from hospitals in the UK and internationally.

Sales and marketing costs were unchanged at approximately £3 million but these declined as a proportion of Group revenues from 18% (2005) to 12%, reflecting both cost cutting and the revenue effect of acquisitions.

Profit before tax was £1.2 million (2005: loss before tax of £0.5 million). The £1.7 million improvement in profitability reflects a number of factors including the higher revenues from both divisions, increased operational efficiencies and gross margins across the Group, lower costs at the Andover facility following the reduction in costs associated with the original laboratory equipment business and a full year's contribution from the acquired businesses in the TRAC division. The full profit effect of the substantial increase in BIOQUELL's revenues from the United States in 2006 was suppressed due to the significant decline in the US dollar against sterling in the second half.

The Group does not expect to incur a tax charge in the year, principally due to the use of tax allowances relating to capital expenditure and research and development costs. The Group had approximately £4 million of deferred UK tax assets at 31 December 2006.



Earnings for the year were £1.2 million (2005: (£0.3) million); basic earnings per share were 2.9p (2005: (0.8p)).

The Group's net debt at 31 December 2006 was £0.6 million, some £1 million lower than at 30 June 2006 and 31 December 2005 when it had been £1.6 million. This reduction in net debt shows the significant improvement in cash generated by the Group's businesses, notwithstanding substantial levels of ongoing research and development and capital expenditure.

Capital expenditure was £1.5 million (2005: £1.2 million) relating largely to investment in specialist testing and move-related equipment for the TRAC division.

Depreciation of property, plant and equipment was £1.0 million (2005: £1.0 million); amortisation of intangibles was £0.6 million (2005: £0.4 million).

Net cash from operating activities was £3.5 million (2005: £1.7 million.) Cash inflow after expenditure on product development and before capital investment was £2.5 million (2005: £0.5 million).

Net assets at 31 December 2006 were £11.5 million (2005: £10.1 million); gearing was 5% (2005: 16%).

Bio-decontamination division

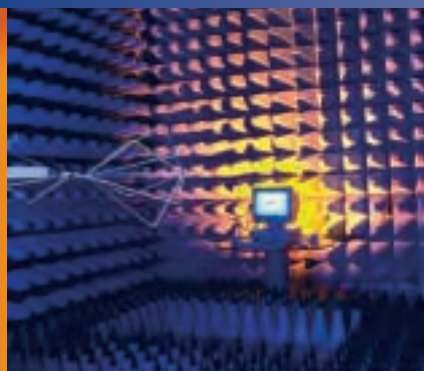
The Bio-decontamination division had a good year in 2006 and has entered 2007 with order momentum and new products. The new technology products – particularly the Group's hydrogen peroxide vapour bio-decontamination technology – performed well showing, as noted above, strong revenue growth in the UK and overseas. We continue to see further opportunities and applications for BIOQUELL's bio-decontamination technology in a range of sectors. Although we are firmly of the view that a substantial opportunity for this technology relates to healthcare applications – particularly the eradication of "superbugs" – we are also pleased by the increasing revenues being generated from other sectors such as pharmaceutical, bio-technology, research, food and universities.

BIOQUELL's technology is highly effective at eradicating "superbugs" from the hospital environment and can significantly reduce the patient infection rate of "superbug" *Clostridium difficile*



Chairman's statement

Continued



The TRAC division also performed well in 2006 with strong increases in turnover and profitability from the businesses acquired in late 2005

The "superbug" opportunity remains both a large opportunity and a source of frustration. We continue to find, as a general rule, that most hospitals move slowly in terms of adopting new technology and the scale of the "superbug" problem is, in some senses, overwhelming as it affects so many different aspects of a hospital's operations. Moreover, hospitals are generally extremely reluctant to admit to having a "superbug" problem due to, among other things, the associated liability and public relations issues. However, we typically find that once hospitals have experienced BIOQUELL's technology in a stressful outbreak situation we tend to secure repeat business and client referrals. We are seeing increasing levels of interest in BIOQUELL's technology from healthcare providers in a number of countries and are in discussions with several hospitals relating to the deployment of a BIOQUELL "implant" team (which comprises BIOQUELL technicians and equipment permanently located at the hospital). Our first implant team has now been continuously in place at a US hospital for nearly two years. We are expecting the publication shortly of further research involving BIOQUELL's technology successfully reducing "superbug" related infection rates in a hospital. In addition, the launch of the BIOQUELL Z will extend the Group's product offering further into the healthcare sector.

In 2006 the Group saw increased levels of demand from defence customers in the UK and overseas for its CBRN filtration and environmental control equipment, including substantial sales to US vehicle manufacturers supplying vehicles deployed in Iraq and Afghanistan. Demand for this equipment has increased further in the first-quarter of this year and we expect defence-related contracts to contribute significantly to turnover in the Bio-decontamination division in 2007.

TRAC division

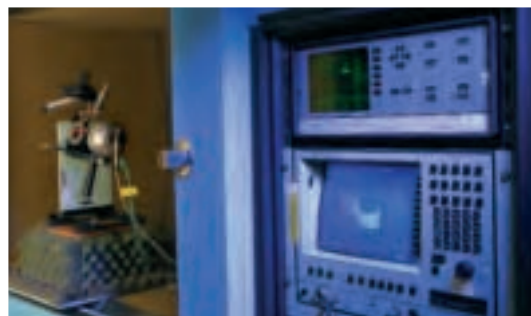
The TRAC division also performed well in 2006 with strong increases in turnover and profitability from the businesses

acquired in late 2005. The property moves are proceeding well and the division has three well equipped 'centres of excellence' as well as some highly competent and successful regional offices providing effective levels of customer service. The senior management of Cape was changed during 2006 and we are expecting Cape's performance to improve significantly in 2007, in part due to a substantially reduced cost base. Activity from companies operating in the defence sector increased, particularly given the increased levels of governmental investment in electronic-based warfare and counter-terrorism technologies. In addition, activity from aerospace clients remains at high levels. We are seeing the success of 2006 continuing into 2007 – in part assisted by the increasing market recognition of the 'TRAC Global' brand.

Prospects

Your Board anticipates that the improvements and developments seen in 2006 will continue into 2007. The benefits of a more extensive international sales network on the back of new products should be seen this year – as well as increased interest in BIOQUELL's technology from the healthcare and defence sectors. In particular, demand for the Group's CBRN technology has been strong so far this year. We also expect the performance from the TRAC division to improve during the year. The prospects for the Group, across both divisions, continue to improve both in the UK and internationally.

John Salkeld
Chairman
26 March 2007



During 2006 the TRAC businesses were melded into a coherent and effective division, able to win large contracts from substantial multi-nationals.

Review of activities



We continue to carry out "superbug" eradication work for hospitals in Europe and North America

Bio-decontamination solutions RBDS and bio-decontamination equipment

During 2006 the Group saw strong growth in turnover from its specialist bio-decontamination equipment and services. Significant activity was seen from the pharmaceutical and bio-technology sectors with, for example, substantial interest seen from manufacturers of avian flu vaccine. We anticipate that this growth will continue due to a number of factors including the increasing international market position which BIOQUELL enjoys (including increasing levels of client referrals), the banning of formaldehyde (a confirmed human carcinogen which until recently was used to decontaminate production and research facilities) and the extension of BIOQUELL's product range, particularly taking into account the launch of the BIOQUELL Z.

The BIOQUELL Z has just been launched and represents an easy-to-use but sophisticated product which enables zones, rooms or buildings to be bio-decontaminated rapidly, reliably and safely using BIOQUELL's hydrogen peroxide vapour technology. The design and engineering of this new product draws heavily upon BIOQUELL's experience gained from providing a room bio-decontamination service ("RBDS") internationally for the last three years as well as the latest technical innovations incorporated in BIOQUELL's Clarus range of bio-decontamination equipment. This new product has been designed to be sold by BIOQUELL's distributors in volume around the world, due, in large part, to its ease of use. In particular, it uses a patent-protected algorithm to control the critical bio-decontamination process to help give reliable, repeatable cycles. We believe that the new BIOQUELL Z will help promote sales of the RBDS service internationally, particularly in emerging markets in Asia, as we have already seen that bio-decontamination service promotes bio-decontamination equipment sales and vice versa; and a number of clients now take both.

Demand continues to increase for the RBDS service and, in addition to the US and Europe, BIOQUELL has deployed teams in recent months as far away as Taiwan and Australia. We anticipate that during 2007 demand for RBDS will increase, in part due to the overseas RBDS licensees we are in the process of signing up; these

licensees are beginning to promote RBDS and the BIOQUELL Z in their territories.

Healthcare and "superbugs"

We continue to carry out work for hospitals in Europe and North America, and continue to add to our expertise in deploying BIOQUELL's technology in the demanding and complex hospital environment. We have recently developed new, high speed catalytic conversion equipment which enables us to sterilise a hospital room in approximately two hours (reduced from some four hours). We believe that the shortened cycle times for hospital side rooms will assist significantly the adoption of the Group's technology in the healthcare sector.

We are also continuing research into the use of BIOQUELL's technology to reduce the level of "superbug" environmental contamination and the associated rate of Hospital Acquired Infection ("HAI"). We remain convinced that the presentation and publication of ongoing high quality research is the best way of educating and influencing healthcare professionals working in the field of "superbugs" on the merits of BIOQUELL's technology. The level of work we undertake for hospitals to counter "superbugs" or HAI continues to increase; however, the healthcare market is conservative and relatively slow to adopt new technologies.

The "superbug" problem continues to increase. Hospitals in North America and Europe are continuing to see increasing levels of the new hyper-virulent strain of *Clostridium difficile* ("*C. diff*"), PVL toxin producing MRSA and multi-drug resistant *Acinetobacter*. In the US substantial litigation-related settlements are being seen – with individual settlements in one State of \$10 million, \$22 million and \$32 million. In addition, 'Pay for Performance' in the US is being extended during 2008 which, in essence, is likely to result in the US government funded Medicare and Medicaid not paying the full costs associated with patients contracting certain "superbugs" in healthcare facilities. This would cost many US hospitals substantial sums. In addition, based on previous analogous developments it is likely that the private sector health insurers will adopt a similar no-payment, or reduced payment, regime for costs associated with hospital acquired infection.



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 be caused by 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. New threats continue to emerge, such as the potential for a global pandemic of Avian Influenza. 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 threatening to return us to the pre-antibiotic era.

Clostridium difficile ("C. diff")

C. diff was first recognised as a cause of antibiotic-associated diarrhoea in the 1970s.¹ Since that time, rates of *C. diff*-associated disease ("CDAD") have increased steadily, until the early 2000s when a new strain emerged in North America known as "NAP1" (in the USA) and "O27" (in the UK) and has since spread to Europe.² The epidemic NAP1 / O27 strain is more often associated with severe disease and death compared with "old" strains. *C. diff* is a spore forming bacterium, which causes widespread environmental contamination and can survive for many months on surfaces. For this reason, effective environmental decontamination is essential for the control of *C. diff*.³

MRSA

Methicillin-resistant *Staphylococcus aureus* ("MRSA") is the best known "superbug" and rates of antibiotic resistance are high worldwide.⁴ Some 30% of the population have *Staphylococcus aureus* residing in their nose. However, only a very small proportion of the population, typically less than 1%, who have not been to hospital, or other healthcare facilities, will have a strain which is resistant to methicillin. There are signs that distinct types of MRSA are emerging in people who have had no healthcare contact, particularly in the USA and Australia.⁵ 'Community-associated MRSA' ("CA-MRSA") usually causes skin infections that can be treated easily, but occasionally causes life-threatening infections. There is evidence that CA-MRSA is beginning to cause HAI, which is significant because CA-MRSA is readily spread between patients.⁶ Currently patients who contract MRSA in hospital can normally be cured by the use of other antibiotic including vancomycin, 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 micro-organisms

Unfortunately for healthcare providers *C. diff* and MRSA are not their sole problems and there are a number of other highly problematic micro-organisms infecting patients who stay in hospital. For example, *Acinetobacter* is becoming resistant to antibiotics significantly more quickly than MRSA. Recent reports in the scientific literature have described multiple-drug-resistant strains of *Acinetobacter* causing infections in patients all over the world.⁷ *Acinetobacter* infections usually affect critically ill patients on Intensive Care Units so due to the nature of the patients affected combined with high levels of drug resistance, mortality associated with *Acinetobacter* infection is high. **Norovirus** is responsible for outbreaks of diarrhoea and vomiting in hospitals and also in

Review of activities

Continued



There is increasing evidence that the hospital environment can become heavily contaminated and does contribute to the spread of infection

other semi-closed environments such as cruise ships and schools. Norovirus infections usually peak in the winter, so it is sometimes called the “winter vomiting disease”.

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, and *Candida albicans* can cause HAI. As a general rule anti-fungal drugs are expensive and toxic.

International problem

HAI and antibiotic resistance is an international problem. Taking the example of MRSA,⁴ Japan has reported MRSA rates (the proportion of *Staphylococcus aureus* blood isolates which are resistant to methicillin) of nearly 70%, and in China in excess of 80%. The US MRSA rates are estimated to range from 50% – 63%. In Europe, 2004 MRSA rates in Romania (73%) 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%.

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 significant source of infection.⁸ 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 via 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.⁹ 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.¹⁰ 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*.^{3, 11} The latest reports in the scientific literature have provided compelling evidence that MRSA is transmitted from the environmental to patients.^{12, 13}

BIOQUELL has been carrying out intensive research in this area. A pilot study published in 2004 showed that BIOQUELL’s technology is successful for the eradication of MRSA from hospital wards whereas MRSA persists despite terminal cleaning.¹⁴ Several recent reports published in the scientific literature have demonstrated the effectiveness of BIOQUELL’s technology for bringing nosocomial outbreaks under control. Preliminary results from an “implant” trial in the USA have demonstrated that routine bio-decontamination can reduce the rates of *C. diff*.¹⁵

Costs of HAI

A number of studies have been undertaken looking at 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 in a range of £4,000 to £11,500.¹⁶ 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' Centers 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.

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We believe that the new BIOQUELL Z will achieve significant levels of sales into the healthcare sector, in particular in markets such as France where there is currently little appetite for outsourcing or service provision. We also expect that the sale of the BIOQUELL Z will help develop BIOQUELL's relationships with hospitals which, in turn, will also help promote the sale of BIOQUELL's RBDS service for outbreaks or the bio-decontamination of large, complex facilities such as Intensive Care Units. In short, we are positioning the Group so that hospitals contact BIOQUELL in the case of a "superbug" outbreak or endemic problem; and we are starting to roll this strategy out internationally.

The Group's overseas sales and service offices in France and the US achieved strong growth in 2006 and made important contributions to Group profitability. They also help us gain direct visibility as to market developments. We anticipate that the BIOQUELL Z will enable these international subsidiaries to increase further their revenues.

Defence

We are seeing increasing interest from the defence sector in the Group's hydrogen peroxide vapour bio-decontamination technology – particularly in respect of remediation of sensitive electronic equipment following biological or chemical agent attack. We intend to pursue these defence-related opportunities during 2007 and anticipate responding, with a US partner, to the forthcoming Request For Proposals from the US Government's Department of Defense for a Joint Materials Decontamination System.

MDH Defence, the Bio-decontamination division's defence business, has a current product range based around specialist CBRN (Chemical, Biological, Radiological and Nuclear) filtration and environmental control for military vehicles (and other military assets). Increasing concern over biological, chemical or dirty bombs has caused an

Review of activities

Continued



Extensive development work continues with BIOQUELL's wound healing technology

increased level of interest in CBRN technologies. At the same time many of the vehicles deployed in Iraq or Afghanistan have either proven to be poorly equipped to stand up to explosive devices and/or have no crew cooling. Over the last five years MDH Defence has redesigned its range of products and services and is now selling sophisticated, specialist equipment directly to a range of international customers including US vehicle manufacturers. We have also secured a contract to provide crew cooling on a retrofit basis to certain vehicles belonging to the UK's Ministry of Defence. We anticipate further growth, particularly from the US, in 2007.

Laboratory equipment

Until 2003 the laboratory division, with the Astec Microflow range of equipment, had the highest business segment turnover in the Group – but had the lowest margins. Over the last four years we have deliberately reduced the size of this business, focusing on retaining profitable business with strategically important customers as opposed to competing for market share irrespective of margin. We have also been aggressively taking costs out of products and associated product support. In 2006, notwithstanding the strength of sterling we saw the export sales from this business segment increase, largely due to the superior technology and service associated with the Group's laboratory equipment. We also saw an improved net contribution from this division in 2006 and we anticipate that this improved trading will continue, although we are not expecting significant levels of growth.

Service and EBDS

The Group's after sales service and Equipment Bio-Decontamination Service (EBDS) improved its profitability in the year although revenues remained broadly flat. We continue to focus on more profitable accounts and are avoiding marginally profitable business. On certain pharmaceutical sites the Group's unique EBDS service helps to secure large, higher margin contracts.

Although historically the Group's Service business provided after sales service and support to the Group's lower margin laboratory equipment clients, we are also

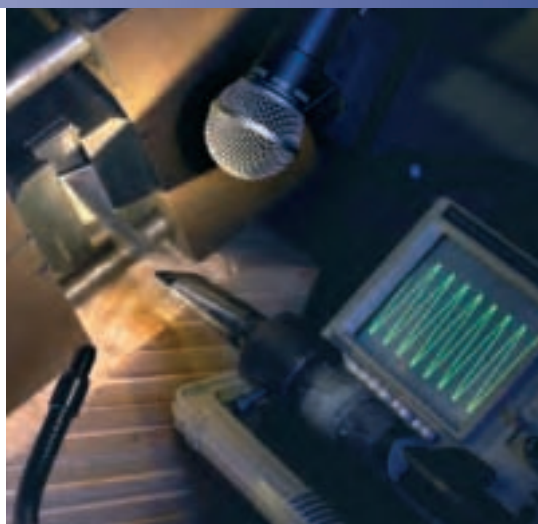
beginning to see improved returns due to the increased proportion of revenues associated with the Group's higher margin bio-decontamination equipment. We anticipate that these higher margin revenues will continue to grow, in part due to the increased volume of Clarus equipment in the field and also due to increased demands for training as the BIOQUELL Z starts to take market share. In addition, we are beginning to bio-decontaminate equipment for third parties at our Andover facility.

Wound Healing

Extensive development work continues with BIOQUELL's wound healing technology. The pre-production model is substantially complete and the production engineering and optimisation of the consumables, accessories and principal unit is underway.

Following discussions with the relevant UK regulators, we are modifying the approach we are taking to obtain regulatory approval for the Group's wound healing technology. In summary, we have decided to consolidate two clinical trials into one and have started preparing the necessary documentation. This has the advantage of reducing the costs of the clinical trials and should also shorten the timetable for regulatory approval, although we have already lost several months as a result of our protracted discussions with the UK regulatory authorities. The UK regulatory environment for clinical trials appears to have become significantly more demanding over the last year and this has had a consequential effect on BIOQUELL's overall clinical trial and regulatory approval timetable.

The chronic wound market which BIOQUELL is planning to target with its technology is substantial, international and growing, due in large part to the ageing population. BIOQUELL is clear on the optimal route to market for the UK but has yet to determine the best route for other markets including the critical US market. However, before routes to market are planned and, as appropriate, partners selected, it is important for BIOQUELL to complete a successful Randomised Controlled Trial (with the appropriate regulatory approvals) to demonstrate irrefutably the efficacy of BIOQUELL's wound healing



technology. We anticipate that this research, and the development of BIOQUELL's wound healing equipment, should be completed in 2007.

Regulatory

The Group is spending more time interacting with international regulatory bodies around the world which in large part reflects the growing complexity of its products and the increasingly global nature of its sales and marketing. It is clear that regulatory issues will continue to represent an important issue for the Bio-decontamination division and the Group is looking to increase the size of its team dealing with such regulatory affairs.

TRAC DIVISION

Overview

The Group's testing service businesses have been positioned under the TRAC – Testing, Regulatory and Compliance – divisional brand. The division was formed in October 2005 to include Cape, EMC Projects, the two acquired businesses (TRL Compliance and KTL) and the recently formed KTL Inc. During 2006 significant work was undertaken in melding the five separate businesses into a coherent and effective division, with a particular focus on winning large contracts from substantial multi-national groups. This integration work is ongoing but already significant progress has been made with some large contracts. In addition, the property consolidation started following the acquisitions in late 2005 is well advanced. Critically, most of TRAC's businesses are primarily involved in the testing of new products or devices in the product development stage – and little work is related to clients' actual manufacturing processes (which for many products is often carried out in the Far East). TRAC effectively has three centres of excellence in Malvern (EMC), Hull (telecoms) and Warwick (environmental).

EMC

Electromagnetic compatibility ("EMC") remains a major cause of concern for regulators as well as large aerospace and military companies. Simplistically electronic devices can give out or be susceptible to electromagnetic radiation which can cause devices to interact and/or malfunction. As a result specialist EMC testing is needed and such testing is particularly onerous for military and aerospace equipment. Over recent years the scale of this testing has increased with new activities such as lightning testing or testing at higher frequencies increasing the turnover of the Group's businesses. The costs of purchasing such specialist testing equipment is high and as a result there are significant barriers to entry as such costs make it difficult for the smaller EMC laboratories to fund the investment in such new technology or find the necessary trained and skilled testing engineers.

TRL Compliance Limited is the TRAC division's principal EMC testing business which is moving its headquarters to Malvern. The Malvern facilities comprise an EMC centre of excellence with state-of-the-art equipment including seven high capacity EMC chambers including one which can accommodate larger vehicles such as main battlefield tanks. The Malvern site is equipped for the new European Military EMC standard which is expected to be published in 2007. TRL Compliance addresses the EMC market in the North of England via its facilities in Lancashire which, in addition to EMC testing, also provide specialist ATEX and DSEAR testing for explosive atmospheres. EMC Projects Limited, located close to Ringwood, Hampshire covers the important South of England market which includes a number of aerospace groups. Over recent months there has been increasing levels of collaborative work between TRL Compliance and EMC Projects relating to the optimal way of addressing the EMC market in the UK.

TRAC's EMC business experienced strong growth in revenues from the military aerospace sector with TRL Compliance's new facilities in Malvern already

Review of activities

Continued



TRL Compliance, EMC Projects and Cape are working extremely closely to maximise the revenue potential of their respective client bases

achieving high utilisation rates. With an increasing proportion of modern military and aerospace equipment linked to electronic devices, we anticipate continued strong growth in EMC-related revenues in 2007.

Telecoms

KTL Limited ("KTL") is headquartered in Hull. (The business was originally the Kingston Telecommunications test laboratory.) KTL has worldwide expertise in a broad range of analogue and digital telecoms testing to ensure interoperability - essentially the ability of the telecoms device to communicate successfully with the telecoms network without causing interference. In addition, KTL has internationally recognised expertise in DSL technology – digital subscriber line – which enables high speed, high capacity broadband internet access to be transmitted down conventional copper wire telephone lines which are installed in most houses in Europe and North America. Given the significant increase in broadband internet access globally, KTL continues to carry out a high volume of DSL testing. This work is being extended by new DSL standards – including ADSL, ADSL2+ and VDSL – which will increase data transmission speeds and capacity resulting in, for example, the download of films or TV programmes over the internet or to mobile phones. KTL is also looking at other new technologies where it can exploit its specialist telecoms-related testing skills including WiMAX (broadband wireless internet), ZigBee (the use of wireless technology to control industrial and domestic appliances including electronics and lighting) and VoIP (voice over internet protocol, used to facilitate telephone calls over the internet).

In 2005 KTL Inc was established with its unique digital testing facilities in Silicon Valley, California. KTL Inc draws upon KTL's telecoms expertise, with a particular focus on DSL, and sells specialist testing services to hardware manufacturers based in Silicon Valley. Although we experienced growth from KTL Inc in 2006, this was somewhat behind our own estimates and we have recently adjusted the management team, equipment range and strategic direction of KTL Inc in order to help ensure that the business is well positioned for growth in 2007.

Environmental

Cape Engineering is the Group's original testing business, headquartered in Warwick and less than one hour's drive from TRL Compliance's headquarters in Malvern. Environmental testing comprises vibrating, heating and otherwise exerting environmental stress on components or products. Environmental testing tends to require larger facilities than EMC or telecoms testing and is in many respects a more mature business. However, the high replacement costs of these assets and the requisite expertise to "drive" them represents a substantial barrier to entry. Cape's facilities at Warwick comprise an environmental centre of excellence able to provide substantially all of the specialist environmental tests required by clients. In addition, Cape has a specialist environmental testing facility at Wimborne (some 10 miles from EMC Projects) in the South of England which is co-located on the facilities of a large aerospace group. Cape also provides 'Cape-on-Call' where clients are able to call upon Cape's specialist testing experts to assist at the clients' facilities.

Although environmental testing does not benefit from the same regulatory drivers which tend to increase the underlying demand for EMC and telecoms testing, it is clear that most clients who require EMC testing will require environmental testing – and vice versa. Accordingly TRL Compliance, EMC Projects and Cape are working extremely closely to maximise the revenue potential of their respective client bases – particularly the large, multinational military aerospace groups – assisted by TRAC division marketing campaigns.

During the year Cape has increased the volume of captive, outsourced work as large engineering groups have continued to close down their test facilities and place their testing requirements with Cape. Given the high fixed costs of Cape, we anticipate that the higher baseline load of work should increase the profitability of Cape during 2007.

Nick Adams
Chief Executive

Operations and finance review



Finance and control

The Group continues to grow in size and complexity, including an increasing proportion of turnover generated overseas. Mindful of this we have a rolling programme of investment in new systems and hardware to ensure the management teams and Head Office are provided in a timely manner with the key indicators used to monitor the trading performance of each business.

We have also strengthened our accounting capabilities in the US as BIOQUELL Inc continues to grow and represents an increasingly large proportion of the Group's business. We expect BIOQUELL Inc to grow further in 2007.

As a result of the increasing level of US dollar receipts generated by the Group, from both BIOQUELL Inc, KTL Inc and the direct sale of equipment and services into the US market by other businesses within the Group, we have looked carefully at our foreign exchange hedging strategy. Accordingly, we monitor the forward dollar/sterling rates prevailing in the market at any time. As a general policy we seek to hedge all our contracted dollar revenues and a significant proportion of our anticipated net US dollar receipts, taking into account the prevailing rates in the market. However, the timing of the non-contracted receipts is not always easy to predict. Further, the significant reduction in the value of the US dollar over the last twelve months has forced us to consider a number of ways to ameliorate the effect of the relatively weak US dollar on Group's profitability. For example, we are considering ways of sourcing more components from suppliers located in the US.

Notwithstanding the significant increase in Clarus bio-decontamination revenues over the year, we expect that the Group will also continue to achieve strong increases in service-related revenues and accordingly we are looking at the next stage of our controls/systems investment programme to be linked to certain of our service businesses. Moreover, the new service systems available in "shrink wrap" format on the market have greatly improved in functionality and significantly reduced in cost over recent years.

Cash and working capital

We are particularly pleased with the cash collection and working capital profile that the Group achieved in 2006, resulting in net debt of £0.6 million and gearing of 5% at the year end. We believe that this is as a direct result of improving financial control across the Group as well as being testimony to the quality of the Group's products and services: in short, clients tend to pay on time if they are happy with the product or service. Focus on cash collection remains high and already in 2007 the Group has been in a net cash positive position on a number of occasions. We are mindful that we have some large investment programmes including the move of the Andover facilities, the completion of the research and development programme for the new wound healing technology and the completion of the moves within TRAC. However, we expect to be able to complete such investments comfortably within our overdraft limits.

Operations and finance review

Continued



We have also strengthened our accounting capabilities in the US as BIOQUELL Inc continues to grow and represents an increasingly large proportion of the Group's business

Facilities for the Bio-decontamination division

The headquarters of the Bio-decontamination division and the PLC offices are located in Andover on a site which is over 40 years old – and where we only use approximately half of the space. We have started negotiations with our landlord to, in summary, move approximately half a mile to a smaller and more modern site which would be renovated to fulfil BIOQUELL's specialist requirements. There should be minimal net increase in rent due to the reduced size of the new building offsetting the increased price per square foot. Following this move the Bio-decontamination division will be located in a facility which is appropriately equipped and significantly more efficient, both in terms of management and the environment.

Given the increasing level of US defence orders we are winning – and the increased number of US defence-related quotations and proposals we are submitting – there are a number of strong commercial reasons for BIOQUELL to open a manufacturing facility in the United States. A detailed feasibility study is being prepared.

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 NEWSCOM PLC 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, Xena Systems Ltd, and Capstone Foster Care 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 and a consultant with Davenport Lyons.

* Member of the Audit, Remuneration and Nominations Committees.

Secretary

Georgina Pope, ACMA

Registered Office

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Andover
Hampshire
SP10 5PY

Auditors

Deloitte & Touche LLP
Chartered Accountants
Reading

Stockbrokers

Investec Limited

Bankers

Barclays Bank PLC

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 2006.

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 activities of the Group include the design, manufacture and supply of bio-decontamination and containment equipment, related products and services to the pharmaceutical, healthcare, food and defence industries, and testing, regulatory and compliance services to the aerospace, telecoms, defence and other industries.

Review of developments

The results for the year are set out in the income statement on page 28. 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.

Directors and directors' interests

The directors of the Company are shown on page 15. 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 20 to 23.

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

Mr J G Salkeld 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 Salkeld 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 66 days (2005: 56 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. The amount charged to the income statement in the year on research and development under IFRS amounted to £464,000 (2005: £407,000) – the total expenditure was £1,038,000 (2005: £1,213,000).

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 as at 19 March 2007.

Ordinary shareholders	Number	Percentage of issued Ordinary Share Capital
M&G Investment Management Limited *	6,039,522	14.8%
Caledonia Investments PLC *	5,462,500	13.4%
Hermes Investment Management Limited *	4,395,113	10.8%
A.H.J. Muir	1,850,000	4.5%
C.B.T. Adams	1,440,380	3.5%
Thompson Clive Investments Growth Industries Fund *	1,394,192	3.4%

*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.

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.

Credit risk

The Group's financial risk management objectives are covered in note 17 to the accounts.

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

Each of the persons who is a director at the date of approval of this report confirms that:

- (1) so far as the director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- (2) the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with provisions of s234ZA of the Companies Act 1985.

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

Georgina Pope
Secretary

26 March 2007

Corporate governance statement

The Company is committed to the principles of corporate governance contained in the Combined Code on Corporate Governance which is appended to the Listing Rules of the Financial Services Authority ('the code') for which the Board is accountable to shareholders.

The Directors consider that throughout the year ended 31 December 2006 the Company has been in compliance with the Code provisions set out in Section 1 of the Code, except for code provision A.1.2 as the Board has not nominated a senior independent director other than the Chairman. This is because the Board is small.

During 2006 the Company had no Nominations Committee and therefore did not comply with code provision A.4.6. Since the end of the year a Nominations Committee has been established, and the Directors consider that the Company will be in compliance with code provision A.4.6 during 2007 and subsequently. The Nominations Committee consists of the three non-executive directors and is chaired by Mr R E Towner.

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. Before re-election the Chairman will confirm to the shareholders that the individual's performance continues to be effective and the individual continues to demonstrate their commitment to the role. 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, Mr Adams and Mr Salkeld were unable to attend 1 of the 11 meetings each, Mr Towner was unable to attend 3 of the 11 meetings. 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 considers that because of its small size it is impracticable to carry out formal performance evaluations (as required by code provision A.6.1).

The Board has established audit and remuneration committees. There was no formal Nominations

Committee during the year. In future the Nominations Committee will meet to consider appointments to the Board.

The Audit Committee, which met three times, consists of the three non-executive directors and was 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 Report 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 auditors' 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 was 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 20 to 23.

The Board attaches a high priority to communications with shareholders. The Group's annual and half-yearly Report 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 2006 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 2006 and the period up to 26 March 2007. In carrying out this review the Board takes account of material developments through reports by the Group Finance Director and the Audit Committee.

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 Schedule 7A of the Companies Act 1985. 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 relating to directors' remuneration. As required by the Act, a resolution to approve the report will be proposed at the Annual General Meeting at which the financial statements will be approved.

The Act requires 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. 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 R E Towner (Chairman), Mr J G Salkeld and Mr S J Constantine. Terms of reference are available for inspection. No director plays a part in any discussion about his own remuneration.

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 2005 and to various senior managers in 2006, which are conditional upon market based 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.

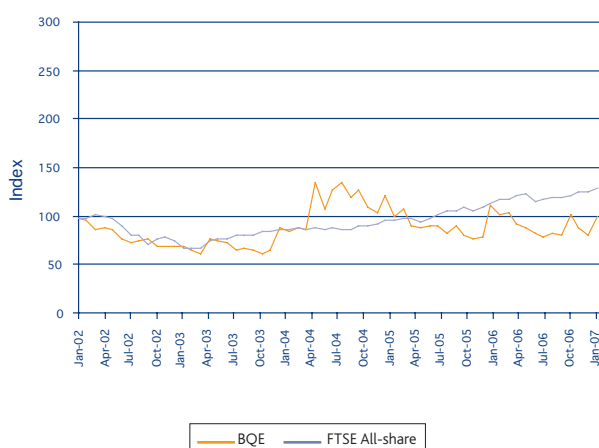
Pension arrangements

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

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 N M T Adams and Mr B M 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 terminatable on three months notice and their remuneration is determined by the Board within the limits set by the Articles of Association. The non-executive directors receive no further fees for additional work performed for the Company both in respect of membership of both the Remuneration Committee and Audit Committee. Non-executive directors have historically participated in the Company's share option schemes, with the last grant of such options on 4 October 2001, but are not eligible to join the Company's pension scheme. The terms of engagement of the non-executive directors are available for inspection.

Audited Information

Aggregate directors' remuneration

The total amount for directors' remuneration was as follows:

	2006 £'000	2005 £'000
Emoluments	459	393
Gains on exercise of share options	129	–
Money purchase pension contributions	16	13
	604	406

Directors' emoluments

	Fees/basic salary £'000	Benefits in kind £'000	Annual bonuses £'000	2006 £'000	2005 £'000
Executive					
Nicholas Adams	151	11	40	202	167
Mark Bodeker	141	8	40	189	153
	292	19	80	391	320
Non-executive					
John Salkeld	28	–	–	28	27
Richard Towner	20	–	–	20	19
Simon Constantine	20	–	–	20	19
Aggregate emoluments	360	19	80	459	385

Directors' remuneration report

Continued

Directors' interest in ordinary shares

The directors who held office at 31 December 2006 had the following interests in the ordinary shares of the Company:

Beneficial holdings*	31 December 2006	Percentage of share capital	1 January 2006
J G Salkeld	2,001,477	4.9%	2,001,477
N M T Adams	674,113	1.7%	674,113
S J Constantine	360,000	0.9%	360,000
R E Towner	309,369	0.8%	309,369
B M Bodeker	14,367	–	14,367
	3,359,326	8.3%	3,359,326

*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.

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

Name of director	Granted/ (exercised)		Exercise price (p)	Date from which exercisable	Expiry date	
	1 Jan 2006	31 Dec 2006				
Nicholas Adams	150,000	(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	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	04.10.08
Richard Towner	25,000	–	25,000	44.0	19.04.03	18.04.07
	20,000	–	20,000	93.5	04.10.04	04.10.08
Simon Constantine	25,000	–	25,000	44.0	19.04.03	18.04.07
	20,000	–	20,000	93.5	04.10.04	04.10.08
	1,815,000	(150,000)	1,665,000			

Further information on the Share Option Schemes can be found in the unaudited section of this report, on pages 20 to 21. There have been no variations to the terms and conditions or performance criteria for share options during the last year. None of the directors' share options lapsed during the year.

The market price of the ordinary shares at 31 December 2006 was 125p (2005: 139p) and the range during the year was 96p to 140p.

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 35 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	2006 £'000	2005 £'000
Nicholas Adams	9	7
Mark Bodeker	7	6
	16	13

This report was approved by the Board of Directors,
and signed on behalf of the Board

Richard Towner
Chairman of the Remuneration Committee

26 March 2007

Statement of directors' responsibilities

The directors are responsible for preparing the Annual Report and the financial statements. The directors are required to prepare financial statements for the Group in accordance with International Financial Reporting Standards (IFRS). Company law requires the directors to prepare such financial statements in accordance with IFRS, the Companies Act 1985 and Article 4 of the IAS Regulation.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the Preparation and Presentation of Financial Statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable International Financial Reporting Standards. Directors are also required to:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information; and
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a directors' report and directors' remuneration report which comply with the requirements of the Companies Act 1985.

The directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

Independent auditors' report

To the members of BIOQUELL PLC

We have audited the Group financial statements of BIOQUELL PLC for the year ended 31 December 2006 which comprise the consolidated income statement, the consolidated statement of recognised income and expenses, the consolidated balance sheet, the consolidated cash flow statement and the related notes 1 to 36. These Group financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Parent Company financial statements of BIOQUELL PLC for the year ended 31 December 2006.

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

The directors' responsibilities for preparing the annual report, the directors' remuneration report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union are set out in the statement of directors' responsibilities.

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

We report to you our opinion as to whether the Group financial statements give a true and fair view, whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation and whether the part of the directors' remuneration report described as having been audited has been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Group financial statements.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding director's remuneration and other transactions is not disclosed.

We review whether the corporate governance statement reflects the Company's compliance with the nine provisions of the 2003 Combined Code specified 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 other information contained in the annual report as described in the contents section and consider whether it is consistent with the audited Group financial statements. The other information comprises only the directors' report, the chairman's statement, the unaudited part of the directors' remuneration report, the operating and financial review and the corporate governance statement. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any further information outside the Annual Report.

Basis of audit opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements and the part of the directors' remuneration report to be 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 Group financial statements and the part of the directors' remuneration report to be audited.

Independent auditors' report

Continued

Opinion

In our opinion:

the Group financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the Group's affairs as at 31 December 2006 and of its profit for the year then ended;

- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation;
- the part of the directors' remuneration report described as having been audited has been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the Group financial statements.

Separate opinion in relation to IFRS

As explained in Note 2 to the Group financial statements, the Group in addition to complying with its legal obligation to comply with IFRS as adopted by the European Union, has also complied with the IFRS as issued by the International Accounting Standards Board.

In our opinion the Group financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's affairs as at 31 December 2006 and of its profit for the year then ended.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
Reading, United Kingdom

26 March 2007

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Consolidated income statement

for the year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Revenue	4	25,238	17,220
Cost of sales		(15,521)	(10,925)
Gross profit		9,717	6,295
		39%	37%
Operating expenses:			
Sales & marketing cost		(2,952)	(3,118)
Administration costs before share based payments and non-recurring inventory write off		(3,922)	(2,507)
Share based payments		(160)	(196)
Non-recurring inventory write off on business disposal	10	–	(101)
Administration costs		(4,082)	(2,804)
R&D and Engineering costs		(1,362)	(767)
Profit/(loss) from operations	6	1,321	(394)
Finance costs	8	(164)	(100)
Pension scheme net interest		–	(7)
Profit/(loss) before tax		1,157	(501)
Tax	9	4	177
Profit/(loss) for the year		1,161	(324)
Profit/(loss) per share – basic	11	2.9p	(0.8)p
– diluted		2.6p	(0.8)p

Movements in reserves are set out in notes 27, 28, 29 & 30

All amounts are derived from continuing operations

Consolidated statement of recognised income and expense

for the year ended 31 December 2006

	2006 £'000	2005 £'000
Net profit/(loss) for the year	1,161	(324)
Actuarial gain/(loss) on defined benefit pension scheme	56	(57)
Exchange differences on translation of foreign operations	(225)	105
Total recognised income/(expense) since last annual report	992	(276)

Consolidated balance sheet

as at 31 December 2006

	Notes	2006 £'000	2005 £'000
Non-current assets:			
Goodwill	12	730	665
Other intangible assets	13	6,108	5,666
Property, plant & equipment	14	3,596	3,263
		10,434	9,594
Current assets:			
Inventories	16	1,415	2,147
Trade and other receivables	17	5,570	5,573
Deferred tax	20	100	55
Cash and cash equivalents		306	113
		7,391	7,888
Total assets		17,825	17,482
Current liabilities:			
Trade and other payables	22	(4,072)	(4,451)
Obligations under finance leases	21	(205)	(30)
Bank overdraft	18	–	(1,189)
Provisions	23	(1,136)	(820)
Net current assets		1,978	1,398
Non-current liabilities:			
Total non-current liabilities	24	(955)	(847)
Total liabilities		(6,368)	(7,337)
Net assets		11,457	10,145
Equity			
Share capital	25	4,069	4,032
Share premium account	26	10,506	10,393
Equity reserve	27	525	365
Capital reserve	28	255	255
Translation reserve	29	(274)	(31)
Retained earnings	30	(3,624)	(4,869)
Equity attributable to equity holders of the parent		11,457	10,145

The Financial Statements were approved by the Board of Directors and authorised for issue on 26 March 2007.

They were signed on its behalf by:

Nicholas Adams }
Mark Bodeker } Directors

26 March 2007

Consolidated cash flow statement

for the year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Net cash from operating activities	32	3,505	1,691
Investing activities			
Proceeds on disposal of property, plant & equipment		20	46
Purchases of property, plant & equipment		(933)	(1,192)
Expenditure on product development		(1,031)	(1,182)
Acquisition of trade and assets	31	–	(364)
Net cash used in investing activities		(1,944)	(2,692)
Financing activities			
Proceeds on issue of ordinary shares		150	124
Repayment of borrowings		(20)	(25)
Repayment of obligations under finance leases		(132)	(35)
Net cash (used in)/from financing activities		(2)	64
Net increase/(decrease) in cash & cash equivalents		1,559	(937)
Bank overdraft at beginning of year		(1,076)	(139)
Effect of foreign exchange rate changes		(177)	–
Bank cash/(overdraft) at end of year		306	(1,076)

Notes to the consolidated financial statements

for the year ended 31 December 2006

1. General

BIOQUELL PLC ("the Company") is a Public Limited Company incorporated in the United Kingdom. The address of the registered office is given on page 15. The nature of the Group's operations and its principal activities are set out on page 16. The financial statements are presented in pounds sterling (£) since that is the currency in which the majority of the Group's transactions are denominated.

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not effective:

IFRS 7	Financial instruments: Disclosures; and the related amendments to IAS 1 on capital disclosures
IFRIC 4	Determining whether an Arrangement contains a Lease
IFRIC 5	Right to Interests Arising from Decommissioning, Restoration and Environmental Re-Economics
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies
IFRIC 8	Scope of IFRS 2
IFRIC 9	Reassessment of embedded derivatives
IFRIC 10	Interim reporting and impairments
IFRIC 11	IFRS 2 – Group and Treasury Share Transactions

The directors anticipate that the adoptions of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Group except for additional disclosures on capital and financial instruments when the relevant standards come into effect for periods commencing on or after 1 January 2007.

2. Significant accounting policies

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board. The financial statements have been prepared on the historical cost basis. The principal accounting policies adopted are set out below. They have been applied consistently throughout the year and in the preceding year.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year.

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 are recognised at their fair value at the acquisition date.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

Revenue recognition

Sales of goods are recognised when goods are delivered and title has passed. Revenue from services is recognised throughout the contract as services are provided or upon completion dependent upon contractual terms.

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other sales related taxes.

Notes to the consolidated financial statements

Continued

2. Significant accounting policies continued

Property, plant and equipment

Fixtures and equipment are stated at cost less accumulated depreciation and any recognised impairment loss. Depreciation is charged so as to write off the cost or valuation of assets, over their estimated useful lives, using the straight-line method, on the following bases:

Short-term leasehold improvements	10 years
Fixtures and equipment	3 to 8 years

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets, or, where shorter, over the term of the relevant lease.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour cost and those overheads that have been incurred in bringing the inventories to their present location and condition. Net realisable value represents the estimated selling price less all estimated costs of completion.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

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

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and Group intends to settle its current tax assets and liabilities on a net basis.

Bank borrowings

Interest-bearing bank loans and overdrafts are recorded as the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accrual basis to the profit and loss account using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill is tested for impairment annually and whenever there is an indication that it may be impaired. Any impairment is recognised immediately in profit or loss and is not subsequently reversed.

2. Significant accounting policies continued

Goodwill arising on acquisitions prior to the date of transition to IFRS has been retained at the previous UK GAAP amounts subject to being tested for impairment at that date. Goodwill written off to reserves under UK GAAP prior to 1988 has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

Internally-generated intangible assets – research and development expenditure

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

An internally-generated intangible asset arising from the Group's development activity is recognised only if all of the following conditions are met:

- an asset is created that can be identified (such as products and new processes related to decontamination solutions);
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Internally-generated intangible assets are amortised on a straight-line basis over their useful lives which is deemed to be 15 years. Where no internally-generated intangible asset can be recognised, development expenditure is expensed in the period in which it is incurred.

Intangible assets – customer relationships

Customer relationship intangible assets, acquired in a business combination are initially measured at cost, based on discounted cash flows, and amortised over their estimated useful lives of 5 years on a straight line basis.

Patents and trademarks

Patents and trademarks are measured initially at purchase cost. They are amortised over their estimated useful lives, which is on average 15 years, although patent protections extends to 20 years.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that these assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Provision is made for any impairment and immediately expensed in the period.

Foreign currencies

Transactions in currencies other than sterling are initially recorded at the rate of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are retranslated at the rate prevailing on the balance sheet date. Non-monetary items are not re-translated. Gains and losses arising on exchange are included in net profit or loss for the period.

In order to hedge its exposure to certain foreign exchange risks, the Group enters into forward contracts and options (see below for details of the Group's accounting policies in respect of such derivative financial instruments).

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Groups' foreign operations are translated at the average exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

Leasing

Leases are classified as finance leases wherever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Notes to the consolidated financial statements

Continued

2. Significant accounting policies continued

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below).

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight line basis over the lease term.

Retirement benefit costs

Payments to defined contribution retirement benefit plans are charged as an expense as they fall due. The defined benefit scheme has been closed to new members since May 1990 and related solely to former employees of the Group. The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised actuarial gains and losses and unrecognised past service cost, and as reduced by the fair value of the plan assets. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside profit or loss and presented in the statement of recognised income and expense.

Past service costs are recognised immediately to the extent that the benefits are already vested, and otherwise are amortised on a straight-line basis over the average period until the benefits become vested.

Trade receivables

Trade receivables do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Trade payables

Trade payables are not interest bearing and are stated at their nominal value.

Financial instruments

The Group's activities expose it primarily to the financial risks of changes in foreign currency exchange rates. The group uses foreign exchange forward contracts to hedge these exposures. The Group does not use derivative financial instruments for speculative purposes.

The use of financial derivatives is governed by the Group's policies approved by the board of directors which provides written principles on the use of financial derivatives. Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting are recognised in the income statements as they arise.

Provisions

Provisions for warranty costs are recognised at the date of sales of the relevant products, at management's best estimate of the expenditure required to settle the Group's liability.

Provisions for restructuring costs are recognised when the Group has a detailed formal plan for the restructuring that has been communicated to affected parties. Other provisions represent property maintenance required under lease obligations.

Share-based payments

The Group has applied the requirements of IFRS 2 Share-based Payments. In accordance with the transitional provisions, IFRS 2 has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 January 2005. The Group is able to issue equity-settled and cash-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share based payments is expensed on a straight line basis over the vesting period, based on the Group's estimate of shares that will eventually vest. Fair value is measured by use of the Black Scholes model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

3. Critical accounting judgements and key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Internally generated intangible assets

Internally generated intangible assets arising from the Group development activity are recognised when certain conditions are met. Management applies certain assumptions in measuring development activity cost and in assessing future economic benefits. Development assets are subject to annual impairment review.

Valuation of share based payments

In order to determine the value of share based payments, management are required to make an estimation of the effects of non-transferability, exercise restrictions and behavioural considerations. Fair value is measured by use of the Black Scholes Model and the inputs used are set out in note 34.

Impairment of goodwill and other intangible assets

Management applies certain assumptions in assessing impairment of goodwill and intangible assets. These assumptions are subject to annual impairment review.

4. Revenue

An analysis of the Group's revenue is as follows:

	2006 £'000	2005 £'000
Sales of goods	9,871	7,413
Revenue from the rendering of services	15,367	9,807
	25,238	17,220

Notes to the consolidated financial statements

Continued

5. Business and geographical segments

For management purposes, the Group is currently organised into two divisions – Bio-decontamination Solutions and Testing, Regulatory and Compliance. These divisions are the basis on which the Group reports its primary segment information.

Segment information about these businesses is presented below

Year ended 31 December 2006

	Bio- decontamination £'000	Testing, regulatory & compliance £'000	Consolidated £'000
Revenue			
Total revenue	14,607	10,631	25,238
Result			
Segment result	749	913	1,662
Unallocated head office costs			(341)
Profit from operations			1,321
Finance costs and pension net interest			(164)
Profit before tax			1,157
Tax			4
Profit for the year			1,161
Other information			
Capital additions	1,250	1,278	2,528
Depreciation and amortisation	969	662	1,631

Balance sheet as at 31 December 2006

	Bio- decontamination £'000	Testing, regulatory & compliance £'000	Consolidated £'000
Assets			
Segment assets	11,558	6,196	17,754
Unallocated corporate assets			71
Consolidated total assets			17,825
Liabilities			
Segment liabilities	(2,409)	(2,814)	(5,223)
Unallocated corporate liabilities			(1,145)
Consolidated total liabilities			(6,368)

5. Business and geographical segments continued

Year ended 31 December 2005

	Bio- decontamination £'000	Testing, regulatory & compliance £'000	Consolidated £'000
Revenue			
Total revenue	11,483	5,737	17,220
Result			
Segment result	(309)	795	486
Unallocated head office costs			(880)
Loss from operations			(394)
Finance costs			(107)
Loss before tax			(501)
Tax			177
Loss after tax			(324)
Other information			
Capital additions	1,642	1,909	3,551
Depreciation and amortisation	1,021	371	1,392

Balance sheet as at 31 December 2005

	Bio- decontamination £'000	Testing, regulatory & compliance £'000	Consolidated £'000
Assets			
Segment assets	12,018	5,362	17,380
Unallocated corporate assets			102
Consolidated total assets			17,482
Liabilities			
Segment liabilities	(4,083)	(2,273)	(6,356)
Unallocated corporate liabilities			(981)
Consolidated total liabilities			(7,337)

Notes to the consolidated financial statements

Continued

5. Business and geographical segments continued

Geographical segments

The Group's Bio-decontamination equipment is manufactured within the UK and sold into the UK, Europe and Rest of World markets. The Testing, Regulatory and Compliance segment offers services from bases within the UK and the USA.

The following table provides an analysis of the Group's sales by geographical market, irrespective of the origin of the goods or services:

Sales revenue by geographical market

	Year ended 31 December 2006 £'000	Year ended 31 December 2005 £'000
UK	14,822	10,727
Rest of Europe	3,368	2,520
Rest of World	7,048	3,973
	25,238	17,220

The following is an analysis of the carrying amount of segments assets, and additions to property, plant and equipment and intangible assets, analysed by the geographical area in which the assets are located:

	Carrying amount of segment assets		Additions to property, plant & equipment and intangible assets	
	Year ended 31 December 2006 £'000	Year ended 31 December 2005 £'000	Year ended 31 December 2006 £'000	Year ended 31 December 2005 £'000
UK	15,521	15,480	2,342	3,085
Rest of Europe	932	869	9	3
Rest of World	1,372	1,133	177	463
	17,825	17,482	2,528	3,551

6. Profit/(loss) from operations

Profit/(loss) from operations has been arrived at after charging/(crediting):

	2006 £'000	2005 £'000
Research and development costs	8	31
Depreciation of property, plant and equipment	1,042	950
Amortisation of internally generated intangible assets	458	376
Amortisation of customer relationships	131	66
Staff costs (see note 7)	9,873	7,752
Loss on disposal of property, plant & equipment	(11)	(16)
Auditors remuneration for audit services (see below)	99	80
Auditors remuneration for tax services	20	17
Net foreign exchange losses/(gains)	124	(17)

Amounts payable to Deloitte & Touche LLP by the Company and its UK subsidiary undertakings in respect of non-audit services were £20,000 (2005: £17,000).

6. Profit/(loss) from operations continued

A more detailed analysis of auditors' remuneration is provided below:

	2006		2005	
	£'000	%	£'000	%
Audit services				
– statutory audit	78	79%	65	76%
– audit-related regulatory reporting	21	21%	15	24%
	99	100%	80	100%
Tax services				
– compliance services	13	65%	17	100%
– advisory services	7	35%	–	–
	20	100%	17	100%

A description of the work of the audit committee is set out in the corporate governance statement on page 18 and includes an explanation of how auditor objectivity and independence is safeguarded when non-audit services are provided by the auditors.

7. Staff costs

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

	2006 Number	2005 Number
Production shop-floor	57	68
Engineering directs	123	59
	180	127
Sales & marketing	37	44
Administration	34	24
Other	12	14
	83	82
	263	209

Their aggregate remuneration comprised:

	2006 £'000	2005 £'000
Wages and salaries	8,505	6,689
Social security costs	953	756
Other pension costs	415	307
	9,873	7,752

Details of directors' remuneration, share options and pension contributions are included in the element of the Directors' Remuneration Report, marked as audited, on pages 21 to 23.

Notes to the consolidated financial statements

Continued

8. Finance costs

	2006 £'000	2005 £'000
Interest on bank loans and overdrafts	147	83
Interest on obligations under finance leases	24	6
Dividend payable on 7.5% preference shares	11	11
Fair value gains on hedging	(18)	–
	164	100

9. Tax

	2006 £'000	2005 £'000
Current tax credit	(41)	177
Deferred tax charge	45	–
	4	177

Corporation tax is calculated at 30% (2005: 30%) of the estimated assessable profit for the year. Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

The charge for the year can be reconciled to the profit per the income statement as follows

	2006 £'000	2005 £'000
Profit/(loss) before tax	1,157	(501)
Tax at the UK corporation rate of 30% (2005: 30%)	(347)	150
Adjusted for:		
Tax effect of expenses not deductible in determining taxable profit	(44)	(92)
Effect of accelerated capital allowances not previously recognised	265	–
Tax effect of utilisation of tax losses not previously recognised	109	76
Utilisation of tax losses brought forward	19	70
R&D tax credit	95	(44)
Tax effect of different tax rate of subsidiaries operating in other jurisdictions	2	17
Deferred tax not recognised on other timing differences	(54)	–
Prior year adjustment	(41)	–
	4	177

10. Business disposal

In October 2005 the Group entered into an agreement to dispose of the steriliser servicing business. This business had not made a material contribution to the Group in the preceding years. The disposal resulted in an inventory write down of £101,000.

11. Earnings per share

The calculation of the basic and diluted earnings per share is based on the following data:

Earnings	Year ended 31 December 2006 £'000	Year ended 31 December 2005 £'000
Earnings/(loss) for the purposes of basic earnings per share being net profit/(loss) attributable to equity holders of the parent	1,161	(324)
Number of shares	Year ended 31 December 2006	Year ended 31 December 2005
Weighted average number of ordinary shares for the purposes of basic earnings per share	40,495,439	40,225,216
Effect of dilutive potential ordinary shares: – share options	3,707,000	–
Weighted average number of ordinary shares for the purposes of diluted earnings per share	44,202,439	40,225,216

For a profit making company with outstanding share options, net profit per share is decreased by the exercise of share options. Therefore diluted earnings per share are calculated by including 'live' share options in the denominator.

12. Goodwill

	£'000
Cost	
As at 1 January 2005	347
Recognised on acquisition of a subsidiary (note 31)	572
Adjustment to deferred consideration on prior period acquisition	(240)
As at 1 January 2006	679
Increase in carrying amount of goodwill in year (note 31)	65
As at 31 December 2006	744
Accumulated impairment	
As at 1 January 2005	14
Impairment losses for the year	–
As at 1 January 2006	14
Impairment losses for the year	–
As at 31 December 2006	14
Carrying amount	
As at 31 December 2006	730
As at 31 December 2005	665

Notes to the consolidated financial statements

Continued

12. Goodwill continued

Goodwill acquired in a business combination is allocated, at acquisition, to the cash generating units (CGUs) that are expected to benefit from that business combination. Before recognition of impairments losses, the carrying amount of goodwill had been allocated as follows:

	2006 £'000	2005 £'000
Bio-decontamination segment	–	–
Testing, Regulatory & Compliance segment	730	665
	730	665

The Group tests goodwill annually for impairment, based on estimated future cash flows and discounted at a rate reflecting current market assessments of the time value of money and the risks specific to the business segments, or more frequently if there are indications that goodwill might be impaired. The Group prepares discounted cash flows using the most recent financial budgets approved by the management and assumes an estimated blended growth rate of 5% per year over five years. The cash flows are discounted at a rate of 12%.

13. Other intangible assets

	Customer relationships £'000	Development costs £'000	Total Intangible assets £'000
Cost			
As at 1 January 2005	263	5,169	5,432
Additions	–	1,182	1,182
Acquired on acquisition of a subsidiary	403	–	403
Adjustment to fair value	(47)	–	(47)
As at 1 January 2006	619	6,351	6,970
Additions	–	1,031	1,031
As at 31 December 2006	619	7,382	8,001
Amortisation			
As at 1 January 2005	26	836	862
Charge for the year	66	376	442
As at 1 January 2006	92	1,212	1,304
Charge for the year	131	458	589
As at 31 December 2006	223	1,670	1,893
Carrying amount			
As at 31 December 2006	396	5,712	6,108
As at 31 December 2005	527	5,139	5,666

The amortisation period for development costs incurred on the Group's product development is 15 years. Patents and trademarks are amortised over their estimated useful lives, which is on average 15 years, although patent protection extends to 20 years. Customer relationships are amortised over 5 years.

14. Property, plant and equipment

	Short-term leasehold improvements £'000	Fixtures and equipment £'000	Total £'000
Cost			
As at 1 January 2005	873	7,359	8,232
Additions	74	1,118	1,192
Acquisition of subsidiary	–	202	202
Disposals	–	(371)	(371)
As at 1 January 2006	947	8,308	9,255
Additions	–	1,432	1,432
Disposals	(15)	(1,042)	(1,057)
Effect of foreign exchange	–	(64)	(64)
As at 31 December 2006	932	8,634	9,566
Accumulated depreciation			
As at 1 January 2005	262	5,121	5,383
Charge for the year	65	885	950
Disposals	–	(341)	(341)
As at 1 January 2006	327	5,665	5,992
Charge for the year	70	972	1,042
Disposals	(15)	(1,033)	(1,048)
Effect of foreign exchange	–	(16)	(16)
As at 31 December 2006	382	5,588	5,970
Carrying amount			
As at 31 December 2006	550	3,046	3,596
As at 31 December 2005	620	2,643	3,263

The carrying amount of the Group's fixtures and equipment includes an amount of £598,000 (2005: £137,000) in respect of assets held under finance leases.

The Group had no capital expenditure contracted but not provided for at the year end (2005: £nil).

15. Subsidiaries

A list of the significant investments in subsidiaries, including name and country of incorporation, is given in note 5 to the Company's separate financial statements.

16. Inventories

	2006 £'000	2005 £'000
Raw materials, spare parts and consumables	1,180	1,688
Work in progress	106	259
Finished goods and goods for resale	129	200
	1,415	2,147

Notes to the consolidated financial statements

Continued

17. Trade and other receivables

	2006 £'000	2005 £'000
Trade debtors	4,695	4,698
Other debtors	336	198
Corporation and other tax	198	326
Prepayments and accrued income	341	351
	5,570	5,573

All trade and other receivables are short-term and non-interest bearing. The directors consider that the carrying amount of trade and other receivables approximates their fair value.

The average credit period taken on sales of goods is 58 days. An allowance has been made for estimated irrecoverable amounts from the sales of goods of £12,000 (2005: £5,000). This allowance has been made with reference to past default experience.

Credit risk

The Group's principal financial assets are trade and other receivables and investments.

The Group's credit risk is primarily attributable to its trade receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables. An allowance for impairment is made where there is an identified loss event which, based on previous experience, is evidence of a reduction in the recoverability of the cash flows. The Group has no significant concentration of credit risk.

18. Bank overdrafts and loans

	2006 £'000	2005 £'000
Bank overdraft	–	1,189
Bank loans	410	430
	410	1,619

The borrowings are repayable as follows:

	2006 £'000	2005 £'000
On demand or within one year	8	1,189
In the second year	–	28
After five years	402	402
	410	1,619

Analysis of borrowings by currency:

31 December 2006

	Total £'000	Sterling £'000	Euros £'000
Bank overdrafts	–	–	–
Bank loans	410	8	402
	410	8	402

Analysis of borrowings by currency:

31 December 2005

	Total £'000	Sterling £'000	Euros £'000
Bank overdrafts	1,189	1,189	–
Bank loans	430	28	402
	1,619	1,217	402

18. Bank overdrafts and loans continued

The weighted average interest rates paid were as follows:

	Year ended 2006 %	Year ended 2005 %
Bank overdrafts	–	5.6%
Bank loans	4.8%	4.7%

The Group had committed overdraft facilities available at 31 December 2006 of £2,200,000 (2005: £2,200,000). The facility is reviewed each year.

The Company has a currency denominated loan in Euros bearing interest at a fixed rate of 4.54%. In addition EMC Projects Ltd, a wholly owned subsidiary of Cape Engineering UK Ltd, has a sterling denominated loan bearing interest at a floating rate that is repayable in the next 12 months.

19. Derivative financial instruments – currency derivatives

The Group utilises currency derivatives to hedge significant future transactions and cash flows as the customers' orders are received. It is the Group's policy to cover the full value of all orders received. The Group is a party to a variety of foreign currency forward contracts in the management of its exchange rate exposures. The instruments purchased are primarily denominated in the currencies of the Group's principal markets.

At the balance sheet date, total notional amount of outstanding forward foreign exchange contracts that the Group has committed are as below.

	2006 £'000	2005 £'000
Forward foreign exchange contracts	402	–

These arrangements are designed to address significant exchange exposures for the first half of 2007, and are renewed on a revolving basis as required. At 31 December 2006 the fair value of the Group's currency derivatives is estimated to be approximately £382,000 (2005: £nil). The fair value has been calculated as the present value of future expected cash flows at market related rates, which are current at the balance sheet date.

20. Deferred tax

The following are the major deferred tax liabilities and assets recognised by the Group and movements thereon during the current and prior reporting period.

	Deferred development costs £'000	Retirement benefit obligations £'000	Tax losses £'000	Decelerated capital allowances £'000	Other timing differences £'000	Total £'000
At 1 January 2005	2	(14)	67	–	–	55
Charge to income	–	–	–	–	–	–
Charge to equity	–	–	–	–	–	–
Exchange differences	–	–	–	–	–	–
At 1 January 2006	2	(14)	67	–	–	55
Charge/(credit) to income	(1,716)	14	1,138	503	106	45
Charge to equity	–	–	–	–	–	–
Exchange differences	–	–	–	–	–	–
At 31 December 2006	(1,714)	–	1,205	503	106	100

At the balance sheet date, the Group had an unrecognised deferred tax asset of £557,000 (2005: £520,000) relating primarily to trade losses available for offset against future profits. A deferred tax asset of £100,000 (2005: £55,000) has been recognised in respect of such losses. No deferred tax asset has been recognised in respect of the remaining £457,000 (2005: £465,000) due to the unpredictability of future profit streams.

This year, in the above note, the deferred tax assets and liabilities have been disclosed on a gross basis.

Notes to the consolidated financial statements

Continued

21. Obligations under finance leases

	Minimum lease payments		Present value of minimum lease payments	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Amounts payable under finance leases:				
Within one year	205	30	205	30
In the second to fifth years inclusive	260	68	237	62
After five years	–	–	–	–
	465	98	442	92
Less: future finance charges	23	6		
Present value of lease obligations	442	92		
Less: amount due for settlement within 12 months (shown under current liabilities)			205	30
Amount due for settlement after 12 months			237	62

It is the Group's policy to lease certain of its fixtures and equipment under finance leases. The average lease term is 5 years. For the year ended 31 December 2006, the average effective borrowing rate was 6.8% (2005: 6.4%). All lease obligations are denominated in sterling. The fair value of the Group's lease obligations approximates their carrying amount. The Group's obligations under finance leases are secured by the lessors' rights over the leased assets.

22. Trade and other payables

	2006 £'000	2005 £'000
Trade creditors	1,787	2,135
Accruals and deferred income	2,285	2,316
	4,072	4,451

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchases is 66 days. The directors consider that the carrying amount of trade payables approximates to their fair value.

23. Provisions

	Warranty provision £'000	Restructuring provision £'000	Other £'000	Total £'000
At 1 January 2006	47	684	89	820
Additional provision in the year	75	55	454	584
Utilisation of provision	(59)	(195)	(14)	(268)
At 31 December 2006	63	544	529	1,136
Included in current liabilities	63	544	529	1,136
Included in non-current liabilities	–	–	–	–
	63	544	529	1,136

The warranty provision represents management's best estimate of the Group's liability under 12 month warranties granted on products and services, based on past experience. The restructuring provision represents the estimated cost of moving the newly acquired businesses as required in the purchase agreement. Other provisions represent property maintenance required under lease obligations within the subsidiaries.

24. Non-current liabilities

	2006 £'000	2005 £'000
Bank loans	402	430
Retirement benefit obligations	143	199
Non equity preference shares	150	150
Obligations under finance leases	260	68
	955	847

The fair value of the financial liabilities is approximately equal to book value due to the short maturity of the liabilities or because they bear interest at rates approximate to the market.

25. Share capital

	2006		2005	
	Number	£'000	Number	£'000
Authorised				
Ordinary shares of 10p each	55,947,780	5,595	55,947,780	5,595
Redeemable deferred ordinary shares of £1 each	255,222	255	255,222	255
		5,850		5,850
Called up, allotted and fully paid				
Ordinary shares of 10p each	40,694,545	4,069	40,320,220	4,032
		4,069		4,032

During the year the Company issued a total of 374,325 ordinary shares of 10p each for £150,000 on the conversion of options under the executive share option schemes, which is being used to provide additional working capital.

26. Share premium account

	£'000
Balance at 1 January 2005	10,285
Premium arising on issue of equity shares	108
Balances at 31 December 2005	10,393
Premium arising on issue of equity shares	113
Balance at 31 December 2006	10,506

Notes to the consolidated financial statements

Continued

27. Equity reserve

	£'000
Balance at 1 January 2005	169
Credit to equity for share-based payments	196
Balance at 31 December 2005	365
Credit to equity for share-based payments	188
Debit to equity on exercise of share options	(28)
Balance at 31 December 2006	525

28. Capital reserve

	£'000
Balance at 1 January 2005 & 1 January 2006	255
Additions	–
Balance at 31 December 2006	255

29. Translation reserve

	£'000
Balance at 1 January 2005	(136)
Effects of foreign exchange in the period	105
Balance at 31 December 2005	(31)
Effects of foreign exchange in the period	(225)
Fair value gain on hedging	(18)
Balance at 31 December 2006	(274)

30. Retained earnings

	£'000
Balance at 1 January 2005	(4,488)
Net loss for the year	(324)
Actuarial loss on defined benefit pension scheme	(57)
Balance at 1 January 2006	(4,869)
Net profit for the year	1,161
Actuarial gain on defined benefit pension scheme	56
Exercised share options	28
Balance at 31 December 2006	(3,624)

31. Acquisition of trade and assets

On 27 October 2005 Cape Engineering UK Ltd acquired certain assets and goodwill of two businesses formerly known as Laboratory Accreditation Services Ltd (KTL) and TRL Compliance Solutions Ltd (TRL) for a total consideration of £413,000. The companies are involved in Telecoms, Digital and EMC testing services. These transactions were accounted for using the purchase method of accounting. The purchase agreement allowed the businesses to remain in the current premises for a period of six months under a licence to occupy. As a result there was an additional restructuring cost to the Group which will be incurred upon relocation. This was recognised as a provision.

	TRL Book & fair value £'000	KTL Book & fair value £'000	Combined Book & fair value £'000
Net assets acquired			
Property, plant & equipment	152	50	202
Total assets acquired	152	50	202
Restructuring liability	(684)	(80)	(764)
Goodwill	535	37	572
Fair value of customer relationships	309	94	403
Total consideration	312	101	413
Satisfied by:			
Cash	241	80	321
Directly attributable cost of acquisition	22	21	43
Pre-acquisition debt	49	–	49
	312	101	413

The fair value of the assets and liabilities of the acquired businesses shown above were provisional.

TRL and KTL generated revenues of £1,132,000 and net income (based on assessed tax rate of 30%) of £259,000 in the post acquisition period from 27 October 2005 to 31 December 2005. The results were recorded in the Testing, Regulatory and Compliance segment. As the accounting records prior to acquisition of the trade and assets were not available it has not been possible to determine what Group revenues and results would have been had the acquisition taken place on the first day of the financial year.

The fair value of the above assets and liabilities was reviewed during the year. This review highlighted an increase in goodwill of £65,000 and an increase in the restructuring provision (note 23).

Notes to the consolidated financial statements

Continued

32. Notes to the cash flow statement

	2006 £'000	2005 £'000
Profit/(loss) from operations	1,321	(394)
Adjustments for:		
Depreciation of property, plant and equipment	1,042	950
Amortisation and impairment losses of intangible assets	589	442
Share based payments	188	196
Profit on disposal of property, plant and equipment	(11)	(16)
Decrease in provisions	251	(124)
Operating cash flows before movements in working capital	3,380	1,054
Decrease in inventories	732	201
Increase in receivables	(42)	(854)
Increase in payables	(383)	1,390
Cash generated by operations	3,687	1,791
Non equity preference share dividends paid	(11)	(11)
Interest paid	(171)	(89)
Net cash from operating activities	3,505	1,691

Of the new additions to fixtures and equipment during the year assets to the value of £499,000 (2005: £nil) were financed by new finance leases. Cash and cash equivalents (which are presented as a single class of assets on the face of the balance sheet) comprise cash at bank and other short term highly liquid investments with a maturity of three months or less.

33. Operating lease arrangements

	2006 £'000	2005 £'000
Minimum lease payments under operating leases recognised in income for the year	875	887
At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:		
	2006 £'000	2005 £'000
Within one year	620	502
In the second to fifth years inclusive	1,376	776
After five years	1,723	151
	3,719	1,429

Operating lease payments represent rentals payable by the Group for certain of its office properties. Leases are negotiated for an average term of 4 years and rentals are generally fixed for the period of the lease.

34. Share-based payments

Equity-settled share option schemes

The Company has a share option scheme for all employees of the Group. Options are exercisable at a price equal to the average quoted market price of the Company's shares on the date of grant. The vesting period is 3 years. If the options remain unexercised after a period of 10 years from the date of grant, the options expire. Options are forfeited if the employee leaves the Group before the options vest except in certain circumstances in accordance with the Scheme Rules.

Special options with market-based conditions, have also been granted to certain directors (as disclosed in the Directors' Remuneration Report) and senior members of staff.

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price (pence)	Number of share options	Weighted average exercise price (pence)
Outstanding at beginning of period	3,615,000	97.6p	3,470,900	96.5p
Adjustment to opening balance	16,000	110.5p	–	–
Granted during the period	760,500	109.0p	332,000	113.9p
Lapsed during the period	(315,000)	112.3p	(149,900)	112.8p
Exercised during the period	(364,500)	39.0p	(38,000)	49.0p
Outstanding at the end of the period	3,712,000	104.6p	3,615,000	97.6p
Exercisable at the end of the period	1,439,000	86.7p	1,421,000	75.9p

The weighted average share price at the date of exercise for share options exercised during the period was 114.8p. The options outstanding at 31 December 2006 had a weighted average exercise price of 104.6p, and a weighted average remaining contractual life of 5.0 years. In 2006, 215,000 options were granted on 3 May and a further 540,000 were granted on 12 September. The aggregate of the estimated fair values of the options granted on those dates was £823,495. In 2005, options were granted on 11 April. The aggregate of the estimated fair values of the options granted on that date is £152,082.

The Black-Scholes model has been adopted as the directors believe it provides a reasonable approximation to the fair values of the options concerned.

The inputs into the Black-Scholes model are as follows:

	2006	2005
Weighted average share price	109.0p	110.5p
Expected volatility	45%	45%
Expected life	4.5 yrs	4.5 yrs
Risk free rate	4.43%	4.43%
Expected dividends	–	–

Each tranche of share options was valued separately using the actual exercise price.

Expected volatility was determined by calculating the historical volatility of the Group's share price over the previous 5 years. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Outstanding at the beginning and end of the period were 800,000 directors' special options issued in April 2004 at an exercise price of 120.5p, conditional upon the market-based performance condition. A further tranche of 540,000 special options were issued to certain senior members of staff in October 2006 at an exercise price of 109.0p, again conditional upon the market-based condition. The inputs into the Black-Scholes model are as set out in the table above, adjusted by a factor based on the probability of meeting the market-based conditions.

The Group recognised total expenses of £188,000 and £196,000 related to equity-settled share-based payment transactions in 2006 and 2005 respectively.

Notes to the consolidated financial statements

Continued

35. Pension arrangements

The Group 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 £415,000 (2005: £307,000). Amounts owing to schemes at 31 December 2006 amounted to £27,000 (2005: £58,000).

The Group also 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 2006 and updated to 31 December 2006 by a qualified actuary.

The overall expected rate of return of the plan assets has been based on the average expected return for each asset class, weighted by the amount of assets in each class. Actuarial gains and losses which arose during the year have been deferred. The following disclosures have been produced in line with the December 2004 Amendments to IAS 19.

The major assumptions used for the actuarial valuation were:

	2006	2005
Rate of increase in salaries	N/a	N/a
Rate of increase in pension payment	3.0%	3.0%
Discount rate	5.0%	4.75%
Inflation assumption	3.0%	3.0%

In the year to 31 December 2006, the Company made contributions of £15,500 (2005: £3,600). There was no pension cost charge for this scheme in the year, other than a finance cost of £8,000 (2005: £7,000). The Company expects to make contributions of £17,000 during 2007.

Amounts recognised in income in respect of the Group's defined benefit scheme are as follows:

	2006 £'000	2005 £'000
Employers current service cost	–	–
Interest on obligation	30	31
Expected return on pension plan assets	(22)	(24)
Total included in employee benefits expense	8	7

Amounts included in the balance sheet in respect of the defined benefit scheme are as follows:

	2006 £'000	2005 £'000
Present value of defined benefit obligation	560	655
Fair value of plan assets	(417)	(456)
Liability recognised in the balance sheet	143	199

Movements in the present value of defined benefit obligations were as follows:

	2006 £'000	2005 £'000
Opening defined benefit obligation	655	570
Employer's current service cost	–	–
Interest on obligation	30	31
Actuarial (gains)/losses on obligations	(59)	79
Benefits paid	(66)	(25)
	560	655

35. Pension arrangements continued

Movements in the fair value of the scheme assets were as follows:

	2006 £'000	2005 £'000
As at 1 January	456	432
Expected return on scheme assets	22	24
Actuarial losses and gains	(10)	22
Contributions	15	3
Benefits	(66)	(25)
As at 31 December	417	456

The analysis of the scheme assets and the expected rate of return at the balance sheet date is as follows:

	Expected return		Fair value of assets	
	31 December	31 December	31 December	31 December
	2006 %	2005 %	2006 £'000	2005 £'000
Equities	7.75%	7.75%	46	62
Bonds	4.50%	4.75%	341	342
Other	4.50%	4.50%	30	52
			417	456

The five-year history of experience adjustments is as follows:

	2006	2005	2004	UK GAAP	
	£'000	£'000	£'000	2003 £'000	2002 £'000
Present value of defined benefit obligation	(560)	(655)	(570)	(565)	(540)
Fair value of scheme assets	417	456	432	427	422
Surplus/(deficit) in the scheme	(143)	(199)	(138)	(138)	(118)
Experience adjustments on scheme liabilities					
Amount (£'000)	41	3	–	–	31
Percentage of scheme liabilities (%)	7%	–	–	–	6%
Experience adjustments on scheme assets					
Amount (£'000)	(10)	23	5	–	(35)
Percentage of scheme assets (%)	(2%)	5%	1%	–	(8%)

36. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are therefore not disclosed.

Five year summary

	IFRS 2006 £'000	IFRS 2005 £'000	IFRS 2004 £'000	UK GAAP 2003 £'000	UK GAAP 2002 £'000
Revenue	25,238	17,220	15,494	12,575	12,243
Operating profit/(loss)	1,321	(397)	201	(2,050)	(2,529)
Profit/(loss) for the year before tax	1,157	(504)	129	(2,061)	(2,535)
Equity	11,457	10,145	10,101	6,345	8,190
Earnings/(loss) per share	2.9p	(0.8p)	0.8p	(4.7p)	(5.9p)

The amounts disclosed for 2003 and earlier periods are stated on the basis of UK GAAP because it is not practicable to restate amounts for periods prior to the date of transition to IFRS.

Company Accounts

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Statement of directors' responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the Company for that period. In preparing these financial statements, the directors are required to:

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

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

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

Independent auditor's report

To the members of BIOQUELL PLC

We have audited the Parent Company financial statements of BIOQUELL PLC for the year ended 31 December 2006 which comprise the balance sheet and the related notes 1 to 15. These Parent Company financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the Group financial statements of BIOQUELL PLC for the year ended 31 December 2006 and on the information in 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

The directors' responsibilities for preparing the annual report, the directors' remuneration report and the Parent Company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the Parent Company financial statements and the part of the directors' remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the Parent Company financial statements give a true and fair view and whether the Parent Company financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the directors' report is consistent with the Parent Company financial statements.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the other information contained in the annual report as described in the contents section and consider whether it is consistent with the audited Parent Company financial statements. The other information comprises only the directors' report, the chairman's statement and the operating and financial review. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Parent Company financial statements. Our responsibilities do not extend to any further information outside the annual report.

Basis of audit opinion

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

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

Opinion

In our opinion:

- the Parent Company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 December 2006;
- the Parent Company financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the directors' report is consistent with the Parent Company financial statements.

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
Reading, United Kingdom

26 March 2007

Company balance sheet

At 31 December 2006

Results for the Company are presented under UK GAAP

	Notes	2006 £'000	2005 £'000
Fixed assets:			
Investments	5	7,441	7,446
Property, plant & equipment	4	10	11
		7,451	7,457
Current assets:			
Debtors			
– due within one year	6	904	1,301
– due after one year	6	767	756
Cash at bank and in hand		9,689	9,018
		11,360	11,075
Creditors: Amounts falling due within one year			
Other creditors	7	(1,237)	(1,392)
Net current assets		10,123	9,683
Total assets less current liabilities		17,574	17,140
Creditors: Amounts falling due after more than one year	7	(1,005)	(790)
Net assets		16,569	16,350
Capital and reserves			
Called up share capital	8	4,069	4,032
Share premium account	9	10,506	10,393
Equity reserve	10	267	178
Capital reserve	11	255	255
Profit and loss account	12	1,472	1,492
Shareholders' funds		16,569	16,350

The financial statements were approved by the board of directors and signed on its behalf by:

N M T Adams	}	Directors
B M Bodeker		

26 March 2007

Notes to the company financial statements

for the year ending 31 December 2006

1. Significant accounting policies

Basis of accounting

The separate financial statements of the Company are presented as required by the Companies Act 1985. They have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards and law.

The principal accounting policy is summarised below. It has been applied consistently throughout the year and the preceding year.

Investments

Fixed asset investments in subsidiaries and associates are shown at cost less provision for any impairment.

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:

Plant, vehicles and machinery	3 to 8 years
-------------------------------	--------------

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

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.

Share based payments

Refer to the policy statement in Note 2 to the Group accounts.

2. (Loss)/profit for the year

As permitted by section 230 of the Companies Act 1985 the Company has elected not to present its own profit and loss account for the year. BIOQUELL PLC has reported a loss, after the cost of share-based payments (£89,000) for the financial year ended 31 December 2006 of (£38,000) (2005 profit: £177,000).

The auditors' remuneration for the audit services to the Company was £1,250 (2005: £1,250).

Notes to the company financial statements

Continued

3. Staff costs

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

	2006	2005
Administration	3	3
Total	3	3

Their aggregate remuneration comprised:

	2006 £'000	2005 £'000
Wages and salaries	339	349
Social security costs	55	47
Other pension costs	33	18
	427	414

4. Fixed assets

	Property, plant & equipment £'000
Cost	
As at 1 January 2006	49
Additions	–
As at 31 December 2006	49
Accumulated amortisation	
As at 1 January 2006	38
Charge for the year	1
As at 31 December 2006	39
Net book value	
As at 31 December 2006	10
As at 31 December 2005	11

5. Fixed asset investments

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

	Location
BIOQUELL UK Limited	Andover, UK and Paris, France
Cape Engineering UK Limited	Warwick, UK
EMC Projects Ltd	Ringwood, UK
Laboratory Accreditation Solutions Ltd	Kingston Upon Hull, UK & Santa Clara, USA
TRL Compliance Ltd	Tewkesbury, UK
BIOQUELL Inc	Philadelphia, USA

The principal activities of the above companies include the design, manufacture and supply of bio-decontamination and containment equipment, related products and services to the pharmaceutical, healthcare, food and defence industries, and testing services to the aerospace, telecoms, defence and other industries.

	Investment in Subsidiaries		
	Shares £'000	Loans £'000	Total £'000
Cost			
As at 1 January 2006	111	7,994	8,105
Foreign exchange differences	–	(5)	(5)
As at 31 December 2006	111	7,989	8,100
Provision for impairment			
As at 1 January 2006	(103)	(556)	(659)
As at 31 December 2006	(103)	(556)	(659)
Net book value			
As at 31 December 2006	8	7,433	7,441
As at 31 December 2005	8	7,438	7,446

6. Debtors

	2006 £'000	2005 £'000
Amounts due from subsidiary undertakings		
– due within one year	785	1,144
– due after one year	767	756
Other debtors	11	19
Corporation and other tax	8	27
Deferred tax	50	64
Prepayments and accrued income	50	47
	1,671	2,057

Notes to the company financial statements

Continued

7. Creditors

	2006 £'000	2005 £'000
Amounts falling due within one year:		
Amounts due to subsidiary undertakings	1,090	1,185
Accruals and deferred income	141	201
Proposed preference dividend	6	6
	1,237	1,392
Amounts falling due after one year:		
Bank loan	402	401
Provision	310	40
Retirement benefit obligations	143	199
First preference shares of £1 each	150	150
	1,005	790

8. Called up share capital

	2006 Number	2006 £'000	2005 Number	2005 £'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 up				
Ordinary shares of 10p each	40,694,680	4,069	40,320,220	4,032
First preference shares of £1 each		–	–	–
		4,069		4,032

During the year the Company issued a total of 374,325 ordinary shares of 10p each for £150,000 on the conversion of options under the executive share options schemes, which is being used to provide additional working capital. Under FRS 25 'Financial instruments: disclosure and presentation' the first preference shares are reclassified from called up share capital to Creditors: amounts falling due after more than one year with effect from 1 January 2005.

9. Share premium account

	£'000
Balance at 1 January 2005	10,285
Premium arising on issue of equity shares	108
Balance at 1 January 2006	10,393
Premium arising on issue of equity shares	113
Balance at 31 December 2006	10,506

10. Equity reserves

	£'000
Balance at 1 January 2005	79
Credit to equity for share-based payments	99
Balance at 1 January 2006	178
Credit to equity for share-based payments	89
Balance at 31 December 2006	267

11. Capital reserves

	£'000
Balance at 1 January 2005 & 1 January 2006	255
Additions	–
Balance at 31 December 2006	255

12. Profit and loss account

	£'000
Balance at 1 January 2005	1,372
Profit for the financial year	177
Actuarial loss on defined benefit pension scheme	(57)
Balance at 1 January 2006	1,492
Loss for the financial year	(38)
Actuarial gain on defined benefit pension scheme	56
Exchange loss	(38)
Balance at 31 December 2006	1,472

Under FRS 20 'Share based payments', equity settled share based payments to employees are part of employee benefit expense in the profit and loss account. A corresponding increase in equity reserves has been made.

Under IAS 19 'Employee benefits' the defined benefit pension liability has been recognised. See note 35 of the consolidated financial statements.

Notes to the company financial statements

Continued

13. Reconciliation of movements in shareholders' funds

	£'000
Balance at 1 January 2005	16,157
Issue of equity shares	124
Equity reserve – share based payments	99
Reclassification of preference shares as creditors: due after one year	(150)
Profit for the financial year	177
Actuarial loss on defined benefit pension scheme	(57)
Balance at 1 January 2006	16,350
Issue of equity shares	150
Equity reserve – share based payments	89
Loss for the financial year	(38)
Actuarial gain on defined benefit pension scheme	56
Exchange loss in the year	(38)
Balance at 31 December 2006	16,569

FRS 24 'Financial instruments: disclosure and presentation' has been implemented with effect from 1 January 2005. Accordingly preference share capital has been reclassified as a long-term liability.

14. Share-based payments

Equity settled share option schemes

The Company's employees are able to participate in the Group's share options scheme. Details of this scheme as given in note 34 of the Group's accounts.

Details of the share options outstanding with employees of the Company during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price (pence)	Number of share options	Weighted average exercise price (pence)
Outstanding at beginning of period	1,707,000	99.8p	1,702,000	99.7p
Granted during the period	2,000	109.0p	5,000	110.5p
Lapsed during the period	–	–	–	–
Exercised during the period	(150,000)	23.0p	–	–
Outstanding at the end of the period	1,559,000	106.0p	1,707,000	99.8p
Exercisable at the end of the period	742,000	90.0p	737,000	77.8p

Note 34 of the Group accounts describes the valuation of share options.

15. Pension arrangements

The Company pension arrangements are discussed in note 35 of the Group accounts.

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 29 May 2007 at 12.00pm for the following purposes:

1. To receive and consider the report of the Directors and the audited accounts for the year ended 31 December 2006.
2. To approve the Directors' Remuneration Report for the year ended 31 December 2006.
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 Salkeld as a director of the Company.
5. To authorise & declare 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 for the purpose of section 80 of the Companies Act 1985 to allot and to grant rights to subscribe for securities or to convert securities into unissued shares of the Company up to a maximum aggregate nominal amount of £1,356,489 at any time on or before the conclusion of the Annual General Meeting of the Company to be held in 2008 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 before the expiry of such period 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 before the expiry of such period; and
- (3) This authority be in substitution for all existing authorities given by the Company for the purpose of section 80 of the Companies Act 1985 to the extent such authorities are unused.

Special Resolution

7. That the Directors of the Company be and they are 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 2008 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 £203,473.

Registered office
34A Walworth Road
Andover
Hampshire
SP10 5PY

By order of the Board
G N Pope
Secretary

26 March 2007

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, Proxy Processing Centre, Telford Road, Bicester, OX26 4LD, not less than 48 hours before the time fixed for the Annual General Meeting (i.e. no later than 12.00pm on 27 May 2007) 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 27 May 2007 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 27 May 2007 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 J G Salkeld 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 J G Salkeld 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 authorised and 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 £1,356,489. The authority will terminate no later than 15 months after the Annual General Meeting, or if sooner the holding of the Annual General Meeting in 2008.
6. **Resolution 7: Renewal of directors' authority to allot shares for cash and under rights issues**
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 £203,473, representing approximately 5% of the Company's issued ordinary share capital as at 26 March 2007. The authority will terminate no later than 15 months after the Annual General Meeting, or if sooner the holding of the Annual General Meeting in 2008.

Form of proxy

BIOQUELL PLC

FOR USE BY HOLDERS OF ORDINARY SHARES OF 10P EACH AT
THE ANNUAL GENERAL MEETING OF BIOQUELL PLC ON 29 MAY 2007

*I/We
(PLEASE USE BLOCK CAPITALS)

Address:
being (a) member(s) of BIOQUELL PLC ('the Company') by virtue of my/our holding of ordinary shares of 10p each hereby appoint the
Chairman of the Meeting or (see note (2) below)

of
as my/our proxy to vote for me/us on my/our behalf at the Annual General Meeting of the Company to be held at 12.00 p.m., and at any
adjournment of the Annual General Meeting. I/We direct my/our proxy to vote on the under-mentioned resolutions as follows:

Please insert an X in the appropriate boxes alongside the resolutions.

ORDINARY RESOLUTIONS	FOR	AGAINST
1 To receive the Accounts for the year ended 31 December 2006		
2 To approve the Directors' Remuneration Report for the year ended 31 December 2006.		
3 To re-appoint Deloitte & Touche LLP as auditors and to authorise the Directors to fix their remuneration		
4 To re-appoint Mr Salkeld as a director		
5 To authorise and declare a dividend on the First Preference Shares		
6 To renew the Directors' authority to allot shares		
SPECIAL RESOLUTION		
7 To renew the Directors' authority to allot shares for cash		

If this form is signed and returned without any indication as to how the proxy shall vote, the proxy will exercise discretion both as to how the proxy votes and whether or not the proxy abstains from voting. The proxy will also exercise discretion as to voting (and whether or not the proxy abstains from voting) on any other business transacted at the Annual General Meeting.

Signed this day of2007

Signature

NOTES

- To be effective this form of proxy (together with the power of attorney (if any) under which it is signed (or a notarily certified copy of that power of attorney)) must be lodged with the Company's Registrars, Capita IRG plc, Proxy Processing Centre, Telford Road, Bicester, OX26 4LD not less than 48 hours before the time appointed for the holding of the Annual General Meeting or any adjournment of that Meeting.
- If you wish to appoint someone other than the Chairman of the Meeting as your proxy, you should complete in block capitals his or her full name and address in the space provided and delete the words "the Chairman of the Meeting or". Such proxy need not be a member of the Company. Any alteration to this form should be initialled by the person signing the form.
- In the case of joint holders, the signature of any holder will be sufficient but the names of the joint holders should be stated. In the event of more than one joint holder voting in person or by proxy, the vote of the senior holder who tenders a vote whether by proxy or in person shall be accepted to the exclusion of the votes of the other joint holders, seniority being determined by the order in which their names stand in the register of members.
- In the case of a corporation, the proxy must be under the common seal or signed on its behalf by or a duly authorised officer of the corporation.
- You are requested to complete and return this form of proxy even if you intend to attend and vote at the Annual General Meeting. Completion of a form of proxy will not preclude a member from attending and voting in person at the Meeting.
- Every holder of ordinary shares present in person and entitled to vote shall have one vote on a show of hands and every holder of ordinary shares present in person or by proxy shall on a poll be entitled to one vote for every ordinary share held. Holders of First Preference Shares are not entitled to attend or vote at the Annual General Meeting.
- A member entitled to attend and vote at the Annual General Meeting may appoint one or more proxies to attend and vote on his behalf and a proxy need not be a member of the Company. If a member appoints more than one proxy, the form of proxy must specify the number of ordinary shares in respect of which the proxy is entitled to vote and no member is permitted to appoint more than one proxy (save in the alternate) to vote in respect of any one ordinary share held by that member.

SECOND FOLD

BUSINESS REPLY SERVICE
Licence No. MB 122



Capita IRG
Proxy Processing Centre
Telford Road
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OX26 4LD

FIRST FOLD

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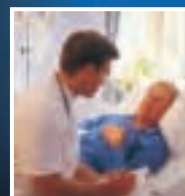
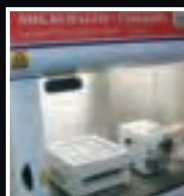
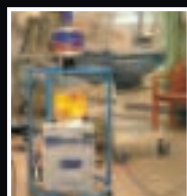
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