

HEALTHCARE ENTERPRISE
GROUP PLC

ANNUAL REPORT
2004

Healthcare Enterprise Group PLC
Annual Report 2004



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**Healthcare Enterprise Group PLC
is an international healthcare
company focused on specialised,
high-value products and services
in the UK, Europe and the US.**

Highlights

- **Creation of the market leader in the UK occupational health and first aid sector**
- **Acquisition of a pipeline of exciting healthcare products for major market sectors**
- **Ebiox – rollout of decontamination products to combat MRSA and other infections**
- **Focus on UK, US and EU growth sectors in healthcare**
- **Acquisition of a US healthcare advisory business**

The Group's commercial goals are to:

- **Build a significant international healthcare group**
- **Identify and acquire synergistic high value products and services**
- **Leverage the Group's operating platform to provide effective international distribution to niche healthcare markets**



Stuart Bruck
Executive Chairman

The Group today operates as a single synergistic entity with three principal areas of activity: occupational healthcare and first aid, new products and strategic consultancy.

Overview

The past twelve months have been a period of transformation and opportunity for Healthcare Enterprise Group PLC ("HCEG" or the "Company"). In the course of an exciting year, the Group has conducted an in-depth assessment of its market, refined its focus and then set about acquiring and developing the best commercial vehicles to achieve sustainable growth.

In March 2003, a reverse takeover of Interactivity Group plc provided HCEG with a stock market listing on the Alternative Investment Market ("AIM") and an appropriate structure with which to advance its plans.

Strategy

The HCEG business model is extremely straightforward. It deploys the considerable experience and expertise of its directors and management team to create the financial and operational infrastructure required to build and develop a significant international healthcare business. Initial drivers include laying a solid foundation for cash generation, while exploiting underdeveloped synergies and opportunities for consolidation in the healthcare sector.

The Group today operates as a single synergistic entity with three principal areas of activity: occupational healthcare and first aid, new products and strategic consultancy.

Acquisitions

The Group considers that the best way to maximise growth is through strategic acquisitions. Following its initial reverse takeover, HCEG entered negotiations with two major operators in the UK occupational healthcare market. Collectively, The S.A.F.A. Group Ltd and Industrial Pharmaceutical Service Ltd comprise a market-leading enterprise with opportunities for increased profitability from economies of scale and an enhanced customer base. These acquisitions were completed in November 2003.

As part of this transaction, HCEG also acquired a controlling interest in SafaTec (UK) Ltd, a holding company with equity holdings in a pipeline of innovative and high-value healthcare products from an established healthcare incubator. A major new product from this source is already generating revenues for the Group and another is at an advanced stage of development.

This approach underlines HCEG's commitment to commercialising innovative healthcare technologies via proven distribution platforms.

These early acquisitions exemplify HCEG's determination to grow market share, maximise profitability and bring significant new products to market. The strategy has been initiated in the UK and the intention is to mirror this approach internationally in the year ahead, with an early focus on the German and US markets. Combined with the UK, these markets comprise approximately two-thirds of the world's healthcare economy.



The acquisition of Medical Development Specialists, Inc. in January 2004 provides HCEG with in-depth strategic and advisory support in the realisation of these objectives.

Management and employees

Without the commitment of the Board of Directors and staff, the transformation of the business would not have been possible. I would like to express my gratitude to the Board, management team and our employees.

Over the year there were a number of strategic additions to the management team with direct experience in healthcare product commercialisation, occupational healthcare and first aid businesses. The Board was also strengthened further and I am pleased to report the appointment of Nigel Wray as a non-executive Director on 15 June 2004.

Outlook

In June 2004, HCEG announced terms to acquire First Aid UK Ltd. This acquisition will represent our next step in consolidating the occupational health and first aid sector in the UK. We hope that this is the first of many positive announcements to be made in the 2005 financial year.

The financial year ahead will be about sustaining the momentum, drive and sense of purpose that characterised the previous year. The Group will continue to forge a successful business by exploiting exciting product development opportunities, underpinned by the profitability of a solid core enterprise.

HCEG is already building reputation and significant market share in the UK. We are now ready to take our winning formula to the global arena.

Stuart Bruck

Executive Chairman

HCEG is already building reputation and significant market share in the UK. We are now ready to take our winning formula to the global arena.



Gordon Wood
Group Chief Operating Officer

While SAFA-IPS provides a revenue-generating backbone for the business, SafaTec is a holding company with equity interests in companies with proprietary, high-value healthcare technologies that open the door to the future.

Prior to November 2003, HCEG acted as adviser and financier to healthcare companies in the US, UK and Germany. In the final quarter of the year, the board implemented key strategic initiatives that both enlarged the Group and established its commercial agenda within the healthcare sector.

HCEG's commercial imperatives are simple and unambiguous – to transform the Group into a significant international healthcare business with strong leadership, a solid financial backbone and a reputation for vision and innovation.

This year has been about starting to turn these ambitions into reality.

The market

HCEG estimates that annual global spend on disposable medical supplies was approximately US\$150 billion in 2002 and should grow to US\$200 billion by 2007. Growth in potentially valuable niches within this market is often constrained by small owner-operated businesses with limited product offerings and/or underdeveloped infrastructure.

This fragmentation represents a major opportunity for HCEG to consolidate portions of this market in order to meet escalating market demand more effectively and profitably. The Group's strategy is to evolve the financial, operational and logistical infrastructure that can bring economies of scale and improved market penetration to parts of the healthcare industry.

At present the sector's inefficient and fragmented distribution mechanisms can make it difficult to bring new products to market. HCEG believes strategic consolidation also implies the evolution of a commercial environment more conducive to delivering such innovation to newly accessible consumer segments.

The acquisitions

Early steps towards realising the Group's commercial goals included a series of strategic acquisitions:

The S.A.F.A. Group Ltd ("SAFA") and Industrial Pharmaceutical Service Ltd ("IPS")

These companies are suppliers of occupational healthcare and first aid products to corporate and professional clients. Both companies also provide a wide range of medical and pharmaceutical supplies to the larger medical, veterinary and retail markets.

Following acquisition, these companies were consolidated into a single entity. SAFA-IPS Healthcare Ltd ("SAFA-IPS") is now the UK's leading occupational healthcare supplier.

SafaTec (UK) Ltd ("SafaTec")

This company has interests in a number of early stage healthcare companies that develop technology and products HCEG believes can introduce innovation and new revenue opportunities to support Group business and build new markets.



Medical Development Specialists, Inc. ("MDS")

MDS is a US based provider of planning, policy and advisory services to health systems, hospitals, health plans, government agencies and businesses not competitive with HCEG. This acquisition offers the Group a vital healthcare market research capability to assist development of new Group businesses and products worldwide.

The potential

These acquisitions provide a solid foundation for HCEG to grow market share, revenues and profitability in key healthcare sectors. Once again, the emphasis is on exploiting cost-saving synergies, while expanding the Group's customer base.

The consolidation of SAFA and IPS has created a market leader with important distribution channels to Europe and the Americas and exclusive, specialised manufacturing sources in Thailand and China. HCEG is already in the process of identifying additional products that can augment SAFA-IPS's existing distribution portfolio and further extend market reach.

While SAFA-IPS provides a revenue-generating backbone for the business, SafaTec is a holding company with equity interests in companies with proprietary, high-value healthcare technologies that open the door to the future. One of these companies, Ebiox Ltd, already has products in the commercial domain, and a second, Optiscope Technologies Ltd, is at an advanced stage of product development.

Ebiox Ltd ("Ebiox")

Ebiox produces an innovative range of cleansing and decontamination products designed to penetrate and remove bacterial biofilm and embedded pathogens to create a clean and disinfected surface. Ebiox products can be used to clean skin, surgical instruments and a range of washable surfaces.

Ebiox wipes have already been purchased by 50 National Health Service ("NHS") hospitals and 10 NHS health centres. In addition, Ebiox products are currently being marketed in the US where distribution is subject to a number of regulatory approvals, the first of which has been received from the US Environmental Protection Agency.

There are also opportunities for significant revenues from Ebiox products outside the hospital and health centre markets. For example, EbioxVet has already been launched in the UK for the veterinary market. The company also envisages Ebiox applications for the industrial, personal care, household, institutional and water management markets.

Studies undertaken by Fredonia Industry Studies and Frost & Sullivan imply a combined market opportunity across all these sectors in excess of US\$34 billion on an annual basis for Ebiox decontamination technologies.

Optiscope Technologies Ltd ("Optiscope")

Optiscope is developing both advanced optical viewing tubes for rigid endoscopes and complete disposable endoscopes.

The market for disposable endoscopes is extremely attractive. Such products would compete with re-usable endoscopes that cost around US\$40 per use, taking into account purchase cost, repairs and cleaning protocols. It is estimated that Optiscope's disposable design can be manufactured for around US\$3.

Annual sales of today's rigid endoscopes indicate a market of around US\$165 million worldwide.

Other interests

Through SafaTec, HCEG has the right of first refusal on a wide range of new and innovative healthcare products.

Summary

HCEG's operating highlights of 2003/4 include:

- the creation of a newly quoted business in the healthcare sector;
- securing solid financing and revenue generation to fuel future development;
- an active acquisition programme;
- the refinement of an effective consolidation vehicle for the UK occupational health and first aid markets;
- the acquisition and launch of innovative new products.

Gordon Wood

Group Chief Operating Officer



Lyndon Gaborit
Finance Director

The months since the major acquisitions in November 2003 have been witness to remarkable activity leading to the formation of an extremely exciting quoted entity.

The Group's operations changed dramatically in November 2003 with a series of significant acquisitions. Following the reverse takeover in March 2003, the directors and management team assessed the healthcare market with a view to:

- building a significant international healthcare group;
- identifying and acquiring synergistic high value products and services; and
- developing and leveraging a robust distribution platform to provide effective international access to niche healthcare markets.

Acquisitions - SAFA, IPS and SafaTec

The initial consideration paid for these companies, including debts discharged, was £11.6 million. This was satisfied as follows:

- £2.5 million through the issue of ordinary shares to the vendors; and
- a balance of £9.1 million in cash (funded by a placing of shares and debt).

Under the terms of the acquisition of SafaTec, deferred consideration not exceeding £5.8 million may also become payable on the realisation of up to six objectively quantifiable milestones on or before 30 June 2005. Such deferred consideration will be satisfied through issuance of ordinary shares. Two of these milestones have been met and provision for these have been made in the financial statements.

In addition, further sums may be payable to SafaTec vendors if Optiscope enters into specific third-party licensing agreements with an aggregate value in excess of US\$5 million. Under such circumstances, any further amount will be satisfied by the issue of ordinary shares and/or loan notes to SafaTec vendors.

Under the terms of the acquisition of IPS, deferred consideration of £400,000 has become due. £200,000 has been paid in cash since the balance sheet date and a further £200,000 has been deposited in an escrow account to be released to the IPS vendors on 28 February 2005. Both amounts were accrued in full at the balance sheet date.

MDS acquisition

This acquisition was structured as a merger of MDS into a wholly owned HCEG subsidiary. The initial consideration comprised a share issue to MDS shareholders equating to a value of £346,000.

Under the terms of the acquisition, contingent consideration not exceeding the lesser of 100 million shares or shares with the value US\$6 million (at the relevant market price of HCEG shares) may also become payable on the realisation of specific quantifiable milestones over a three year period.

Financing

In August 2003, Prestbury Investment Holdings Ltd entered into an agreement to subscribe for ordinary shares (with warrants attached) with a value of £300,000. This was done to provide the Company with the ability to cover professional fees and other costs related to its acquisition program.



In November 2003, HCEG agreed a debt facility of up to £3.5 million with Barclays Bank plc to:

- finance acquisitions identified above;
- provide working capital for the enlarged group;
- exploit additional strategic opportunities.

Also in November 2003, the Company's brokers, Numis Securities, placed shares (with warrants attached) with institutional and other investors to generate gross proceeds of £10.5 million, resulting in £8.8 million of net proceeds after the deduction of expenses.

Application of proceeds

The subscription proceeds and the term loan facilities described above were used primarily to finance the Company's cash obligations created as part of its acquisition program. The balance of the subscription proceeds and term loan facilities, amounting to approximately £3.5 million, was used to fund working capital requirements.

Reported results

The total loss for the year was £3.0 million. This loss was after goodwill amortisation of £1.1 million, exceptional items of £1.0 million and tax and other items of £159,000. The reported operating results, before goodwill amortisation and exceptional items, for the financial year are as follows:

Year ended 29 February 2004	£'000
Turnover	2,999
Cost of sales	(1,635)
Gross profit	1,364
	45%
Net operating expenses	(2,077)
Group operating loss	
Acquisitions	(185)
Continuing activities	(528)
Group operating loss	(713)

Goodwill amortisation was primarily due to the reverse takeover accounting adopted in accordance with generally accepted accounting practice.

Exceptional items consisted mainly of an expense recognised for the economic value of options granted to executives and staff members, as well as estimated National Insurance premiums on those amounts in accordance with UK accounting standards, totalling £891,000. In addition to this, exceptional costs in relation to the reorganisation of the Group totalling £148,000 have also been incurred.

Because the acquisitions referred to above were completed late in the Company's financial year (SAFA and IPS in November 2003 and MDS in January 2004), they are only partly recognised in the consolidated profit and loss account. It should be noted that if the acquisitions had been owned for the whole financial year, they would have contributed to the Group's results as follows:

Pro Forma*	£'000
Turnover	10,053
Cost of sales	(5,407)
Gross profit	4,646
	46%
Net operating expenses	(3,225)
Operating profit	1,421

*Unaudited. Adjusted to eliminate abnormal and non recurring items.
Source: internal management accounts.

Cashflow and net debt

During the year, the Group raised £10.9 million in new share capital and increased debt by £2.8 million. At the year-end, the Group had cash at bank and in hand of £2.3 million and a further £435,000 available in un-drawn credit lines.

The major cashflow items included the consideration paid for acquisitions, including debts discharged, totalling £9.1 million and associated costs totalling £1.7 million.

Assets

The Group's major asset is the goodwill attributed to its businesses. Goodwill arising from the acquisitions amounted to £840,000 for the transaction in March 2003 (wholly written off in the year) and £14.9 million for all other acquisitions in the year (written down to £14.7 million at the year-end).

Tangible fixed assets amounted to £960,000, stocks amounted to £866,000 and debtors a further £2.2 million.

Total assets of the Group amounted to £21.5 million.

Lyndon Gaborit

Finance Director



01



02



03



04

Board of Directors

01 Stuart Bruck (54)

Executive Chairman

Stuart Bruck has more than 25 years experience in the healthcare industry at the executive level. He is a founder of HCEG having reversed his advisory company, Healthcare Enterprise Group, Inc. ("HEI") into the Group in March 2003. Previously he was Chief Executive Officer of AIM-listed Barbican Healthcare Plc, which was sold successfully to BUPA in 1999.

Bruck began his career with the United Hospital Fund of New York in 1974, joined National Medical Enterprises, Inc. (now Tenet Healthcare) in 1979 and in 1984, was appointed vice-president of marketing and development at Nu-Med, Inc., a publicly traded healthcare management company. In 1990 he became a principal of Medical Development and Technology, Inc. before selling it to and joining AHI Healthcare Systems, Inc. ("AHI"), a physician practice management company, as senior vice-president in 1992. AHI was listed on NASDAQ in 1995 and was sold successfully in 1997.

02 Gordon Wood (42)

Group Chief Operating Officer

Starting his career in healthcare in 1983 with Hoechst AG, Gordon Wood later moved to the newly-merged veterinary businesses of ICI and Wellcome in 1987. In 1989 Wood established his own company encompassing Dunnwood Ltd, DataVet Systems and the Vetfile locum agency servicing the UK veterinary sector. In 1993 he successfully divested of his interests in the business, joining Lloyds Chemists Plc as commercial director of its veterinary division. In October 1994 he joined The Intercare Group Plc as managing director of the medical products division before leading the management buy-out of SAFA from Intercare in 1996.

In 1999 Wood established SafaTec, a holding company with equity holdings in a pipeline of innovative and high-value healthcare products. In 2001 he established Safasia Co. Ltd ("Safasia"), which sources medical dressings from Asia, and whose products are marketed by SAFA-IPS in Europe and the Americas. (Safasia is not part of HCEG).

03 Michael Low (49)

CEO Advisory Services

Michael Low has more than 20 years experience in the healthcare industry, covering international business development, strategic planning and mergers and acquisitions. Prior to joining HEI, Low co-founded Medical Development and Technology, Inc. with Stuart Bruck, and was subsequently appointed vice-president for business development at AHI in 1993.

Previously, Low held similar positions with a variety of healthcare organisations. Low is responsible for the US based advisory services of HCEG, including MDS.



04 Lyndon Gaborit CA (56)

Finance Director and Company Secretary

Lyndon Gaborit, a Chartered Accountant, has been adviser to and Finance Director of HCEG since the acquisition of HEI. He was formerly the Chief Operating Officer (Europe) for Moore Clayton & Co, Inc. ("MCC"). Before that he was Deputy Chairman and CEO of Infoshare Europe Ltd, an adviser to ConAgra Foods, Inc. from 1991 to 1997, and from 1988 to 1990 he was General Manager, Group Strategy for Elders IXL Ltd in London and Melbourne. He also serves as Managing Director of Industrial Management & Equity Ltd, a corporate strategy adviser to HCEG, and as Deputy Chairman of Capital Accumulation Ltd, a holding company of financial services businesses.

05 Kenneth Denos (36)

General Counsel

Kenneth Denos, a practising lawyer, has served as general counsel to HCEG since the acquisition of HEI and as general counsel of HEI since its inception. He also serves as director and executive of MCC, a global strategic and financial advisory firm. Denos' expertise lies in public and private corporate finance, mergers and acquisitions, licensing and joint venture agreements, and technology commercialisation. His background includes executive-level experience in venture capital and emerging growth companies in the UK and the US. Denos is also a member of the Board of Directors of Morphogenesis, Inc., a US-based biotechnology firm.

06 Nicholas Brigstocke (62)

Non-executive Deputy Chairman

Nick Brigstocke is Deputy Chairman of HCEG. Between 1998 and 2001, he was Chairman of UK Equity Capital Markets at Credit Suisse First Boston ("CSFB") in London following CSFB's acquisition of Barclays de Zoete Wedd ("BZW"), where he was Chairman and Managing Director of UK Corporate Broking. He is also a non-executive director of Turbo Genset, Inc., Azure Dynamics, Inc., Bridgewell Group Ltd, DDD Group Plc and Capital Accumulation Ltd.

07 Mark Tompkins (63)

Non-executive Director

Mark Tompkins is a private investor with experience in assisting emerging companies in Europe and the US. His prior experience includes investment banking, management consulting and investment advice on an international level. He currently serves, inter alia, on the board of Sodexo Alliance SA, the Paris listed food services and facilities management company. In the past he has served on the boards of two NYSE listed healthcare companies, Abbey Healthcare Group, Inc. and Apria Healthcare Group, Inc. and on that of AIM-quoted Bioprojects International Plc.

08 Nigel Wray (56)

Non-executive Director

Nigel Wray has extensive experience as an investor in both quoted and unquoted companies. He was Chairman of Burford Holdings Plc from 1988 until February 2001. He is currently non-executive Chairman of WLink Plc, Electric Word plc, and a non-executive director of several other companies including Urbium plc, Domino's Pizza UK and IRL plc. He is also a director and major shareholder of Saracens Rugby Club.

Directors' Report

for the year ended 29 February 2004



The Directors present their report and audited consolidated financial statements for the year ended 29 February 2004.

During the period under review, the principal activities of the Group were the distribution of occupational health and first aid products and the provision of consulting and advisory services to the healthcare market. A full review of the business is given in the Chairman's Statement, the Review of Operations and the Financial Review on pages 2 to 7.

Results and dividends

The results of the Group for the period are set out in the Group Profit and Loss Account on page 19.

The Directors do not recommend the payment of a dividend for this accounting period.

Directors

The Directors who served during the period were as follows:

S Bruck	appointed 11 March 2003
G A Wood	appointed 2 December 2003
M K Low	appointed 11 March 2003
L J Gaborit	appointed 11 March 2003
K Denos	appointed 16 January 2004
N O Brigstocke	appointed 11 March 2003
H J M Tompkins	appointed 11 March 2003
A R Moore	appointed 11 March 2003
C R Akers	resigned 16 January 2004
G A Perske	resigned 11 March 2003
R D Sargent	resigned 11 March 2003

N W Wray was appointed as a Director on 15 June 2004.

A statement of Directors' remuneration and their interests in the shares and options of the Company are disclosed in the Report on Directors' Remuneration on pages 12 to 14.

Substantial shareholdings

The following interests in 3% or more of the issued share capital of the Company at 8 June 2004 have been disclosed to the Company:

Name	Number of ordinary shares of 0.1p each	Percentage of issued ordinary share capital
LPMCC, LLC	647,328,974	22.20%
S Bruck ¹	647,328,974	22.20%
M K Low ²	647,328,974	22.20%
N W Wray ³	335,698,820	11.51%
Prestbury Investment Holdings Ltd	262,448,820	9.00%
N Leslau ⁴	262,448,820	9.00%
G A Wood ⁵	250,715,631	8.60%

Note 1 S Bruck holds 80% of the membership of London and Pacific Healthcare Development, LLC ("LPHD"), which owns 96.5% of LPMCC, LLC ("LPMCC"). At 8 June 2004, LPMCC held 647,328,974 ordinary shares in the Company and therefore S Bruck was interested, indirectly, in 647,328,974 ordinary shares of the Company.

Note 2 M K Low holds 20% of the membership of LPHD and therefore, for the reasons given in note (1) above, M K Low was interested, indirectly, in 647,328,974 ordinary shares of the Company at 8 June 2004.

Note 3 At 8 June 2004, N W Wray directly held 48,000,000 ordinary shares of the Company. Prestbury Investment Holdings Limited, a company in which N W Wray is entitled to exercise more than one third of the voting power at general meetings, held 262,448,820 ordinary shares. In addition, N W Wray's child and certain trusts of which he is a trustee were interested in 25,250,000 ordinary shares. Therefore, in total, N W Wray was interested, directly and indirectly, in 335,698,820 ordinary shares of the Company at 8 June 2004.

Note 4 At 8 June 2004, Prestbury Investment Holdings Limited, a company in which N Leslau is entitled to exercise more than one third of the voting power at general meetings, held 262,448,820 ordinary shares. Therefore, N Leslau was interested, indirectly, in 262,448,820 ordinary shares of the Company at 8 June 2004.

Note 5 At 8 June 2004, G A Wood directly held 216,715,433 ordinary shares in the Company. In addition, 34,000,198 ordinary shares were held by G A Wood's family trust, of which he is a trustee. Therefore, at 8 June 2004, G A Wood was interested, directly and indirectly, in 250,715,631 ordinary shares of the Company.



Payment of creditors

The Group's current policy concerning the payment of its trade creditors is to:

- (a) settle the terms of payment with its suppliers when agreeing the terms of such a transaction;
- (b) ensure that these suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and
- (c) pay in accordance with its contractual and other legal obligations.

The payment policy applies to all payments to creditors for all supplies of goods and services.

At 29 February 2004, the Group's trade creditors represented 85 days (2003: 86 days) of purchases.

Donations

There were no charitable or political contributions made by the Group during the period.

Auditors

A resolution proposing that HLB AV Audit plc be re-appointed as auditors of the Company will be proposed at the forthcoming Annual General Meeting.

By Order of the Board

L J Gaborit

Company Secretary

22 June 2004

Report on Directors' remuneration

Remuneration Committee

The remuneration of the executive Directors is determined by the Remuneration Committee, which consists of the two non-executive Directors, under the chairmanship of N O Brigstocke.

The committee's principal function is to determine the remuneration, benefits and terms of employment of the executive Directors with due regard to the interests of shareholders. It is also responsible for making allocations from the Company's share option scheme and for setting objective conditions governing its exercise.

Remuneration policy

In determining the remuneration policy which applies to the executive Directors, the committee strives to ensure that Directors are rewarded competitively relative to comparable companies in order to retain and motivate them.

Remuneration of executive Directors

The committee's aim is to provide a balanced package to executive Directors with both fixed and variable elements to ensure that an appropriate proportion is performance related. No executive Director is involved in deciding his own remuneration.

Remuneration of executive Directors comprises elements of basic salary and benefits, bonus, pension arrangements and share options.

The benefits provided to executive Directors may include a car allowance, health insurance and life assurance.

Under the terms of their service contracts, executive Directors may earn bonuses that are discretionary and/or based on specific performance targets set by the committee.

Executive Directors are eligible for share options, granted at the discretion of the Board, under the Company's share option schemes.

Remuneration of non-executive Directors

The Board determines the remuneration of the non-executive Directors. No non-executive Director is involved in deciding his own remuneration.

Directors' service contracts

Executive Directors' contracts, save for G A Wood's, may be terminated by the Director or Company giving not less than six months' written notice at any time. G A Wood's appointment is for a fixed term of two years from 2 December 2003, but may be terminated early in certain specific circumstances including, by the Director, giving not less than 12 months' prior written notice.

There are no termination payments other than those determined by notice periods (pay in lieu), except in terminating the employment contracts of S Bruck and M K Low without cause, for which compensation equal to two years' base salary would be payable.

The agreements with non-executive Directors are not for fixed terms, but are each terminable on not less than three months' written notice at any time by the Director or Company. In the case of H J M Tompkins, such notice may not be given until the expiry of two years from appointment.

Directors' emoluments

The remuneration of the Directors of the Company from the date of their appointment to 29 February 2004 (or date of resignation, if earlier) was as follows:

	Year ended 29 February 2004			
	Salaries and fees £'000	Benefits £'000	Pension contributions £'000	Total £'000
Executive Directors				
S Bruck	114	3	–	117
G A Wood	29	1	2	32
M K Low	69	3	–	72
L J Gaborit	28	–	–	28
K Denos	–	–	–	–
	240	7	2	249

Directors' emoluments (continued)

	Year ended 29 February 2004			Total £'000
	Salaries and fees £'000	Benefits £'000	Pension contributions £'000	
Non-Executive Directors				
N O Brigstocke ¹	15	–	–	15
H J M Tompkins ¹	15	–	–	15
A R Moore ¹	12	–	–	12
	42	–	–	42
	282	7	2	291

Note 1 Fees to be settled through issuance of shares.

All of the current Directors were appointed after 1 March 2003 and, as a result, no prior year comparative information is disclosed.

C R Akers, G A Perske and R D Sargent, who resigned on 11 March 2003, received no remuneration for their duties as Directors during the period of their appointment in the current or prior years.

Directors' shareholdings

The interests of the Directors in the issued share capital of the Company at 29 February 2004 were as follows:

	Number of ordinary shares of 0.1p each
S Bruck ¹	724,795,181
G A Wood ²	169,386,326
M K Low ³	724,795,181
L J Gaborit	–
K Denos	–
N O Brigstocke	–
H J M Tompkins ⁴	11,438,974

Note 1 S Bruck holds 80% of the membership of LPHD, which owns 96.5% of LPMCC. At 29 February 2004, LPMCC held 724,795,181 ordinary shares in the Company and therefore S Bruck was interested, indirectly, in 724,795,181 ordinary shares of the Company.

Note 2 At 29 February 2004, G A Wood directly held 147,371,499 ordinary shares in the Company. In addition, 22,014,827 ordinary shares were held by G A Wood's family trust, of which he is a trustee. Therefore, at 29 February 2004, G A Wood was interested, directly and indirectly, in 169,386,326 ordinary shares of the Company.

Note 3 M K Low holds 20% of the membership of LPHD and therefore, for the reasons given in note (1) above, M K Low was interested, indirectly, in 724,795,181 ordinary shares of the Company at 29 February 2004.

Note 4 H J M Tompkins has a contingent beneficial interest in shares through Ballerat International Ltd, a company which is wholly owned by a trust associated with H J M Tompkins.

As at 8 June 2004, these shareholdings had changed as follows:

	Number of ordinary shares of 0.1p each
S Bruck ¹	647,328,974
G A Wood ²	250,715,631
M K Low ³	647,328,974
L J Gaborit	–
K Denos	–
N O Brigstocke	25,000,000
H J M Tompkins ⁴	11,438,974

Note 1 S Bruck holds 80% of the membership of LPHD, which owns 96.5% of LPMCC. At 8 June 2004, LPMCC held 647,328,974 ordinary shares in the Company and therefore S Bruck was interested, indirectly, in 647,328,974 ordinary shares of the Company.

Note 2 At 8 June 2004, G A Wood directly held 216,715,433 ordinary shares in the Company. In addition, 34,000,198 ordinary shares were held by G A Wood's family trust, of which he is a trustee. Therefore, at 8 June 2004, G A Wood was interested, directly and indirectly, in 250,715,631 ordinary shares of the Company.

Note 3 M K Low holds 20% of the membership of LPHD and therefore, for the reasons given in note (1) above, M K Low was interested, indirectly, in 647,328,974 ordinary shares of the Company at 8 June 2004.

Note 4 H J M Tompkins has a contingent beneficial interest in shares through Ballerat International Ltd, a company which is wholly owned by a trust associated with H J M Tompkins.

Report on Directors' remuneration

continued

Directors' share options

Details of options held under the Company's share option schemes are set out below:

Options granted in the year under the amended and restated 2001 L&P MCC, Inc. ("L&P MCC") stock option plan, which was adopted by the Company in connection with the acquisition of Healthcare Enterprise Group, Inc. ("HEI") in March 2003.

	At 1 March 2003	Granted in the year	Exercised in the year	At 29 February 2004	Exercise price	First exercise date	Expiry date
S Bruck	–	45,298,388	–	45,298,388	0.1p	1 August 2001	31 July 2006
M K Low	–	30,198,963	–	30,198,963	0.1p	1 August 2001	31 July 2006
L J Gaborit	–	12,740,172	–	12,740,172	0.1p	1 January 2003	31 December 2007
K Denos ¹	–	8,493,448	–	8,493,448	0.1p	1 January 2003	31 December 2007
N O Brigstocke	–	16,916,117	–	16,916,117	0.1p	1 August 2001	31 July 2006
N O Brigstocke	–	2,831,149	–	2,831,149	0.1p	1 January 2003	31 December 2007
H J M Tompkins ²	–	33,973,791	–	33,973,791	0.41p	19 December 2002	18 December 2007

Note 1 Options granted to K Denos prior to his appointment as Director.

Note 2 H J M Tompkins has a contingent beneficial interest in options through Ballerat International Ltd, a company which is wholly owned by a trust associated with H J M Tompkins.

Options issued under the Healthcare Enterprise Group PLC ("HCEG") 2003 Share Option Scheme.

	At 1 March 2003	Granted in the year	Exercised in the year	At 29 February 2004	Exercise price	First exercise date	Expiry date
Approved							
G A Wood ¹	–	1,875,000	–	1,875,000	1.6p	14 November 2003	13 November 2013
Unapproved							
S Bruck	–	4,529,839	–	4,529,839	1p	10 December 2004	9 December 2013
G A Wood ¹	–	31,000,000	–	31,000,000	0.98p	14 November 2003	13 November 2013
M K Low	–	3,019,896	–	3,019,896	1p	10 December 2004	9 December 2013
L J Gaborit	–	38,124,017	–	38,124,017	1p	10 December 2004	9 December 2013
K Denos ¹	–	22,849,345	–	22,849,345	1p	10 December 2004	9 December 2013
N O Brigstocke	–	12,974,727	–	12,974,727	1p	10 December 2004	9 December 2013
H J M Tompkins ²	–	14,397,379	–	14,397,379	1p	10 December 2004	9 December 2013

Note 1 Options granted prior to appointment as a Director.

Note 2 H J M Tompkins has a contingent beneficial interest in options through Ballerat International Ltd, a company which is wholly owned by a trust associated with H J M Tompkins.

Options issued under an unapproved stand alone share option scheme.

	At 1 March 2003	Granted in the year	Exercised in the year	At 29 February 2004	Exercise price	First exercise date	Expiry date
G A Wood ¹	–	17,125,000	–	17,125,000	0.98p	14 November 2003	13 November 2013

Note 1 Options granted prior to appointment as a Director.

In addition to the options held above, the Directors have been granted options over shares held by LPMCC. These options were granted prior to the appointment of the Directors and carry warrants in the ratio of one warrant for every ten ordinary shares. Details of share warrants are given in note 23 to the financial statements.

	Granted prior to appointment	Exercised in the year	At 29 February 2004	Exercise price	First exercise date	Expiry date
S Bruck	22,649,194	–	22,649,194	0.054p	15 January 2003	31 December 2007
M K Low	15,099,463	–	15,099,463	0.054p	15 January 2003	31 December 2007
L J Gaborit	4,246,724	–	4,246,724	0.054p	15 January 2003	31 December 2007
K Denos	8,493,448	–	8,493,448	0.054p	15 January 2003	31 December 2007
N O Brigstocke	5,733,077	–	5,733,077	0.054p	15 January 2003	31 December 2007

At 1 March 2003, C R Akers, who resigned on 11 March 2003, held options over 2,000,000 ordinary shares of 0.5 pence each in the Company. These options had an exercise price of 10 pence per ordinary share, were exercisable from 5 March 2001 and expired on 4 March 2003. These options lapsed during the year.

Warrants

At 29 February 2004, 1,143,897 share warrants were held by Ballerat International Ltd, a company which is wholly owned by a trust associated with H J M Tompkins and 14,737,149 were held by G A Wood. Details of these warrants are given in note 23 to the financial statements.

Statement of Directors' responsibilities

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

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

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

Corporate governance

Corporate Governance Committee

HCEG is listed on the Alternative Investment Market ("AIM") and is not subject to the requirements of the combined code on corporate governance, nor is it required to disclose its specific policies in relation to corporate governance. However, the Directors are committed to delivering high standards of corporate governance to the Company's shareholders and other stakeholders, including employees, suppliers and the wider community. A corporate governance committee, comprising N O Brigstocke and H J M Tompkins, has been established for this purpose and meetings of this committee are held at least twice a year. The Board of Directors operates within the framework described below.

The Board of Directors

The Board comprises the Executive Chairman, four other executive Directors, a non-executive Deputy Chairman and two other non-executive Directors. The Directors believe that the composition of the Board is appropriate for the current size of the Group and its stage of development. The Board demonstrates a range of experience and calibre sufficient to ensure appropriate independent judgement on issues of strategy, performance, resources and standards of conduct vital to the continued success of the Group.

The Board meets at least four times a year and has a schedule of matters reserved for its decision. The Board directs and controls the Group and is responsible for strategy, operating performance and stewardship of the Group's resources. Relevant papers are circulated to the Board on a timely basis and in advance of each meeting.

In furtherance of their duties, all Directors have access, as appropriate, to independent professional advice and to the services of the company secretary.

Any Director appointed during the year is required under the Company's articles of association to retire and seek re-appointment by the shareholders at the next annual general meeting.

The Board does not consider it necessary to have a Nomination Committee to make recommendations to the Board on new Board appointments. The Board itself considers all such appointments and decides whether persons nominated have the appropriate skills and experience.

In addition to the corporate governance committee, the Board has appointed two other standing committees, as follows:

The Audit Committee

The Audit Committee is chaired by N O Brigstocke and comprises two of the non-executive Directors and L J Gaborit, the Finance Director. It meets four times a year and its duties include a comprehensive review of the annual and interim financial statements before they are presented to the Board for approval. It also reviews the findings of the external auditors and key accounting policies and judgements. It has unrestricted access to the Group's auditors.

The Remuneration Committee

The Remuneration Committee meets four times a year and comprises two of the non-executive Directors. It is chaired by N O Brigstocke and is responsible for making recommendations to the Board on remuneration policy for executive Directors and for setting the salaries, incentive payments and granting share options relating to the executive Directors. The Board of Directors (excluding non-executive Directors) determines the remuneration of the non-executive Directors.

Relations with shareholders

The Board of Directors seeks to ensure that all shareholders are kept informed about the Group and its activities. A comprehensive annual report and accounts and an interim report are sent to shareholders and there is frequent dialogue with institutional investors, including presentations following the preliminary and interim announcements.

The annual general meeting provides shareholders with the opportunity to meet and question Directors, including the Chairman of the Board. Details of the resolutions to be proposed at the annual general meeting, to be held on 26 July 2004, are set out in the Notice of Annual General Meeting, to which this report is attached.

Internal control

The Directors recognise that they have overall responsibility for ensuring that the Group maintains a sound system of internal control. However it should be recognised that such a system can provide only reasonable and not absolute assurance against material misstatement or loss.

As an AIM listed company, the Board is not required to make a statement on the effectiveness of its internal controls, however the Directors believe it is useful to highlight the following elements of the Group's systems and controls:

- a clearly defined structure which delegates authority, responsibility and accountability;
- a comprehensive system for reporting financial results. Actual results are measured monthly against budget which, together with a commentary on variances and other unusual items, allows the Board to monitor the Group's performance on a regular basis;
- a comprehensive annual budgeting process;
- a revision of annual forecasts on a quarterly basis.

Going concern

Under company law, the Directors are required to consider whether it is appropriate to prepare the financial statements on the basis that the Company and Group are going concerns. As part of its normal business practice, budgets, cash flow forecasts and longer term financial projections are prepared, and in reviewing this information, the Directors are satisfied that the Company and the Group have adequate resources to enable them to continue in business for the foreseeable future. The Directors have therefore adopted the going concern basis in the preparation of the financial statements.

Independent auditor's report

to the members of Healthcare Enterprise Group PLC

We have audited the financial statements for the year ended 29 February 2004 which comprise the Group Profit and Loss Account, Group Statement of Total Recognised Gains and Losses, Group Balance Sheet, Company Balance Sheet, Group Cash Flow Statement and the related notes 1 to 33. These financial statements have been prepared on the basis of the accounting policies set out therein.

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

Respective responsibilities of directors and auditors

The Directors are responsible for preparing the Annual Report, including the financial statements which are required to be prepared in accordance with applicable United Kingdom law and Accounting Standards as set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the 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 transactions with the Company is not disclosed.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the Chairman's Statement, the Review of Operations, the Financial Review, the Directors' Report, the Report on Directors' Remuneration and the Corporate Governance Report.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 29 February 2004 and of its loss for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

HLB AV Audit plc

22 June 2004

Registered Auditor

66 Wigmore Street
London
W1U 2HQ

Group profit and loss account

for the year ended 29 February 2004

	Notes	Year ended 29 February 2004			Total £'000	Fourteen months to 28 February 2003 (restated) £'000
		Before exceptional items and goodwill amortisation £'000	Goodwill amortisation £'000	Exceptional items £'000		
Turnover	2					
Acquisitions		2,999	–	–	2,999	–
Continuing activities		–	–	–	–	109
Cost of sales		(1,635)	–	–	(1,635)	–
Gross profit		1,364	–	–	1,364	109
Net operating expenses		(2,077)	(1,085)	(891)	(4,053)	(392)
Group operating loss						
Acquisitions		(185)	(1,085)	(427)	(1,697)	–
Continuing activities		(528)	–	(464)	(992)	(283)
Group operating loss	3	(713)	(1,085)	(891)	(2,689)	(283)
Share of operating results of associates		(5)	–	–	(5)	–
Total operating loss		(718)	(1,085)	(891)	(2,694)	(283)
Exceptional costs	3	–	–	(148)	(148)	–
Loss on ordinary activities before interest		(718)	(1,085)	(1,039)	(2,842)	(283)
Net interest payable and similar charges	6	(74)	–	–	(74)	(2)
Loss on ordinary activities before taxation		(792)	(1,085)	(1,039)	(2,916)	(285)
Taxation on loss on ordinary activities	7	(92)	–	20	(72)	–
Loss on ordinary activities after taxation		(884)	(1,085)	(1,019)	(2,988)	(285)
Minority interests		12	–	–	12	–
Loss for the financial year		(872)	(1,085)	(1,019)	(2,976)	(285)
Basic and diluted loss per share	9				(0.17p)	(0.02p)

All amounts derive from continuing activities.

Group statement of total recognised gains and losses

for the year ended 29 February 2004

	2004 £'000	2003 (restated) £'000
Loss for the financial year	(2,976)	(285)
Exchange losses offset in reserves	(49)	–
Movement in provision for share options	33	–
Total recognised losses relating to the year	(2,992)	(285)

Balance sheets

as at 29 February 2004

	Notes	Group		Company	
		2004 £'000	2003 (restated) £'000	2004 £'000	2003 £'000
Fixed assets					
Goodwill	11	14,676	–	–	–
Tangible assets	12	960	11	427	–
Investments in subsidiary undertakings	13	–	–	24,281	–
Investments in associated undertakings	13	463	–	389	–
Other investments	13	52	32	18	–
		16,151	43	25,115	–
Current assets					
Stock	15	866	–	–	–
Debtors	16	2,194	103	1,066	267
Current asset investments		4	–	–	–
Cash at bank and in hand		2,339	207	2,277	671
		5,403	310	3,343	938
Creditors: amounts falling due within one year	17	4,294	28	2,235	308
Net current assets		1,109	282	1,108	630
Total assets less current liabilities		17,260	325	26,223	630
Creditors: amounts falling due after more than one year	18	1,516	–	1,475	–
Provisions for liabilities and charges	20	29	–	–	–
Net assets		15,715	325	24,748	630
Capital and reserves					
Called up share capital	21	3,558	6	3,558	932
Shares to be allotted	21	2,258	–	2,258	–
Warrants issued	23	364	–	364	–
Share premium account	24	14,219	618	20,418	1,919
Profit and loss account	24	(3,291)	(299)	(3,661)	(2,273)
Merger reserve	24	(2,293)	–	–	–
Other reserves	24	892	–	1,811	52
Shareholders' funds (including non-equity interests)	25	15,707	325	24,748	630
Minority interests		8	–	–	–
Capital employed		15,715	325	24,748	630

The financial statements were approved by the Board of Directors on 22 June 2004.

S Bruck
Executive Chairman

L J Gaborit
Finance Director

Group cash flow statement

for the year ended 29 February 2004

	Notes	Year ended 29 February 2004 £'000	Fourteen months to 28 February 2003 (restated) £'000
Net cash outflow from operating activities	27	(1,323)	(287)
Returns on investments and servicing of finance			
Interest received		17	1
Interest paid		(326)	(3)
Net cash outflow from returns on investments and servicing of finance		(309)	(2)
UK corporation tax paid		(1)	–
Capital expenditure and financial investment			
Purchase of tangible fixed assets		(47)	–
Loan to associated undertaking		(50)	–
Other loans		(16)	–
Purchase of fixed asset investments		(20)	(32)
Net cash outflow from capital expenditure and financial investment		(133)	(32)
Acquisitions			
Purchase of subsidiary undertakings		(7,375)	–
Acquisition expenses		(1,716)	–
Net cash acquired with subsidiaries		446	–
Purchase of interest in associated undertakings		(21)	–
Net cash outflow from acquisitions		(8,666)	–
Cash outflow before financing		(10,432)	(321)
Financing			
Issue of ordinary share capital		10,856	528
Share issue costs		(175)	–
Increase in long term borrowings		2,750	–
Repayment of short term loans		(865)	(11)
Repayment of principal under hire purchase contracts		(2)	–
Net cash inflow from financing		12,564	517
Increase in cash in the year	29	2,132	196

Notes to the financial statements

for the year ended 29 February 2004

1. Accounting policies

The financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards in the United Kingdom. A summary of the more important accounting policies of the Group is set out below.

Basis of consolidation and comparative figures

On 11 March 2003 HCEG, then named Interactivity Group plc, became the legal parent company of HEI (formerly L&P MCC) in a share for share transaction. Due to the relative values of the companies, the former HEI shareholders became the majority shareholders with over 50% of the enlarged share capital. Further, the Company's continuing operations and executive management were those of HEI. Accordingly, the substance of the combination was that HEI acquired Interactivity Group plc in a reverse acquisition. As part of the business combination Interactivity Group plc changed its name to Healthcare Enterprise Group PLC and changed its year end to 28 February.

Under the requirements of the Companies Act 1985 it would normally be necessary for HCEG's consolidated accounts to follow the legal form of the business combination. In that case the pre-combination results would be those of Interactivity Group plc and its subsidiary undertakings, which would exclude HEI. HEI would then be brought into the Group from 11 March 2003. However, this would portray the combination as an acquisition of HEI by Interactivity Group plc and would, in the opinion of the Directors, fail to give a true and fair view of the substance of the business combination. Accordingly, the Directors have adopted reverse acquisition accounting as the basis of consolidation in order to give a true and fair view.

In invoking the true and fair override the Directors note that reverse acquisition accounting is endorsed under International Accounting Standard 22 and that the Urgent Issues Task Force of the UK's Accounting Standards Board considered the subject and concluded that there are instances where it is right and proper to invoke the true and fair override in such a way.

All other subsidiary undertakings acquired during the period have been incorporated into the Group accounts using the acquisition method of accounting. Under the acquisition method of accounting the results of subsidiary undertakings acquired during the period are included in the Group profit and loss account from the date control passes.

As a consequence of applying reverse acquisition accounting to the HEI acquisition, the results for the year ended 29 February 2004 comprise the results of HEI for the year ended 29 February 2004, plus those of HCEG from 11 March 2003, the date of the reverse acquisition, to 29 February 2004. The results also include the results of all other subsidiary undertakings acquired from the date control passes. The comparative figures are those of HEI for the fourteen months ended 28 February 2003. The consolidated balance sheet comprises the combined balance sheets of HEI and HCEG as well as all other acquired subsidiary undertakings as at 29 February 2004. The comparative consolidated balance sheet is that of HEI at 28 February 2003.

The effects on the consolidated financial statements of adopting reverse acquisition accounting, rather than following the legal form, are widespread. However, the following table indicates the principal effect on the composition of the reserves.

	Reverse acquisition accounting (as disclosed) 2004 £'000	Normal acquisition accounting 2004 £'000	Impact of reverse acquisition accounting 2004 £'000
Called up share capital	3,558	3,558	–
Share premium account	14,219	20,418	(6,199)
Profit and loss account	(3,291)	(4,830)	1,539
Merger reserve	(2,293)	–	(2,293)
Other reserves	892	1,811	(919)
	13,085	20,957	(7,872)

Goodwill

Goodwill represents the difference between the fair value of the consideration paid on the acquisition of a business and the fair value of the identifiable net assets acquired.

Goodwill arising as a result of the March 2003 reverse acquisition is fully written off at acquisition as Interactivity Group plc has no continuing activity and therefore the goodwill has no intrinsic value.

Goodwill arising on other acquisitions is capitalised and amortised on a straight line basis over the Directors' estimate of its useful economic life, up to a maximum of 20 years.

Associates

Entities (other than subsidiaries) in which the Group has a participating interest and over whose operating and financial policies the Group exercises significant influence are treated as associates. In the Group financial statements associates are accounted for using the net equity method.

1. Accounting policies (continued)

Tangible fixed assets

Tangible fixed assets are stated at cost, net of depreciation and any provision for impairment. The cost of tangible fixed assets is their purchase cost, together with any incidental costs of acquisition.

Depreciation is calculated so as to write off the cost of tangible fixed assets, less their estimated residual values on a straight line basis over the expected useful economic lives of the assets concerned. The principal annual depreciation rates are:

Freehold property	2% per annum
Computer equipment	20% - 30% per annum
Plant, equipment, fixtures and fittings	10% - 33% per annum
Motor vehicles	20% - 50% per annum

Leasehold premises are amortised over the period of the lease. Freehold land is not depreciated.

Turnover

Turnover represents amounts receivable for goods and services net of VAT and intra-Group transactions.

Stock

Stocks are valued at the lower of cost and net realisable value. Provisions are made for obsolete, slow moving and defective stock where appropriate.

Operating leases

Costs in respect of operating leases are charged to the profit and loss account on a straight line basis over the term of the lease.

Investments

Investments held as fixed or current assets are stated at cost less any provision for impairment.

Deferred taxation

Deferred taxation is provided, without discounting, on all material timing differences which have originated but not reversed at the balance sheet date except for those which should not be recognised under FRS 19, calculated at the enacted rates at which it is estimated that tax will be payable. No deferred tax asset has been recognised for the future benefit of tax losses available to be carried forward.

Financial instruments

The Group's financing strategy, which is approved at Board level, is to use medium and long term debt together with equity to finance acquisition expenditure. This debt is currently at floating rates and the resulting interest rate exposure is kept under review by the Board.

The Group's activities are undertaken in a number of markets and as a result there is exposure to currency risk at a Group level although at an operating level exposure to currency risk is not significant.

Hire purchase contracts

Assets obtained under hire purchase contracts, which transfer to the Group substantially all the risks and rewards of ownership of the asset, are capitalised as tangible fixed assets and depreciated over their estimated useful life. Obligations under such contracts are included in creditors net of finance charges allocated to future periods. The finance element of the rental payment is charged to the profit and loss account so as to produce a constant periodic rate of charge on the net obligations outstanding in each period.

Foreign currencies

Transactions in foreign currencies are recorded at the rate of exchange ruling at the date of the transaction. Assets and liabilities expressed in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date.

The results of overseas subsidiaries are translated into sterling at the rates of exchange ruling at the balance sheet date. Any exchange differences arising on the retranslation of opening net assets are taken directly to reserves.

All other foreign exchange differences are taken to the profit and loss account in the year in which they arise.

Pensions

Certain subsidiaries of the Company operate defined contribution pension schemes for their employees and Directors. The assets of the schemes are held separately from those of the Group. The annual contributions payable are charged to the profit and loss account. The Company provides no other post-retirement benefits to its employees and Directors.

Notes to the financial statements

for the year ended 29 February 2004
continued

2. Segmental information

	2004 £'000	2003 £'000
Turnover by destination		
United Kingdom	2,556	–
North America	20	109
South America	32	–
Middle East	134	–
Continental Europe	257	–
	2,999	109

Turnover for the year is attributable to the distribution of occupational health and first aid products, originating in the United Kingdom. Turnover for the previous period is that of HEI for consulting and advisory services, originating in North America.

In the opinion of the Directors the disclosure of the results on ordinary activities before taxation and net assets by geographical segment and class of business would be seriously prejudicial to the interests of the Group and have therefore not been provided.

3. Group operating loss

	2004 £'000	2003 £'000
Operating loss is stated after charging:		
Amortisation of goodwill (note 11)	1,085	–
Exchange differences	66	–
Depreciation of owned tangible fixed assets	29	3
Depreciation of tangible fixed assets held under hire purchase contracts	3	–
Operating lease rentals – land and buildings	92	24
Operating lease rentals – other	9	–
Auditors' remuneration for audit services	36	1
Exceptional item	891	–

In accordance with Urgent Issues Task Force abstract number 17, an exceptional charge of £727,000 has been recognised on share options granted to executives and staff members during the year. This charge represents the economic benefit given to option holders, calculated as the difference between the exercise price and the share price on the date of grant. In accordance with Urgent Issues Task Force abstract number 25, an additional provision of £164,000 has been made in the year for potential employer's national insurance payable on the difference between the share price at the balance sheet date and the exercise price to be paid by the option holder.

In addition, a further exceptional charge in relation to the reorganisation of the Group, totalling £148,000, has been charged to the profit and loss account in the year.

4. Directors' emoluments

Details of Directors' emoluments are set out in the report on Directors' remuneration on pages 12 to 14.

5. Employees

The average number of employees, including executive Directors, employed by the Group during the year was:

	2004 No.	2003 No.
Sales	7	–
Distribution	8	–
Administration	15	1
	30	1

Staff costs, including Directors' remuneration, are as follows:

	2004 £'000	2003 £'000
Wages and salaries	1,584	29
Social security costs	232	2
Other pension costs	29	–
	1,845	31

The costs disclosed above include the exceptional charges relating to share options issued during the year as follows: wages and salaries – £727,000 (2003: £nil) and social security costs – £164,000 (2003: £nil).

One Director is a member of a defined contribution pension scheme operated by a subsidiary of the Company.

6. Net interest payable and similar charges

	2004 £'000	2003 £'000
Interest payable on bank loans and overdrafts	(104)	(3)
Interest payable on hire purchase contracts	(1)	–
	(105)	(3)
Other interest receivable	31	1
	(74)	(2)

7. Taxation on loss on ordinary activities

	2004 £'000
Tax charge comprises:	
United Kingdom corporation tax at 30%	72
The reconciliation of the current year tax charge is as follows:	
Group loss on ordinary activities before taxation	(2,916)
Amortisation of goodwill	1,085
Exceptional items	891
	(940)
Standard UK corporation tax at 30%	(282)
Effects of:	
Expenses not deductible for tax purposes	25
Amortisation of goodwill	15
Capital allowances for the year lower than depreciation	1
Overseas losses not used	161
UK losses not used	100
Other	52
Current tax charge	72

In the consolidated profit and loss account, the comparative figures relate to HEI prior to the reverse acquisition. HEI had no liability to corporate tax in 2003.

At 29 February 2004, the Group has accumulated UK tax losses of approximately £700,000 which are available for offset against future trading profits of certain Group operations.

8. Loss attributable to Healthcare Enterprise Group PLC

No separate profit and loss account is presented for the Company as permitted by Section 230 of the Companies Act 1985. The loss after tax of the Company is £1,421,000 (five months to 28 February 2003: £2,000).

9. Loss per share

(a) Basic loss per share

The basic loss per share is based on the loss for the financial year of £2,976,000 (2003: £285,000) and on the weighted average number of ordinary shares in issue during the year of 1,772,333,816 (2003: 1,180,723,605). The weighted average number of ordinary shares for the year ended 29 February 2004 assumes that the 1,180,723,605 ordinary shares in relation to the reverse acquisition existed for the entire year. The weighted average number of shares for the 14 months ended 28 February 2003 is assumed to be equal to the 1,180,723,605 ordinary shares issued in relation to the reverse acquisition.

(b) Diluted loss per share

Because the inclusion of potential ordinary shares would decrease the basic loss per ordinary share they are not deemed to be dilutive and accordingly the basic and diluted loss per ordinary share are identical.

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10. Related party transactions

A R Moore and K Denos are Directors and shareholders, N O Brigstocke was formerly a shareholder and S Bruck and M K Low were former indirect shareholders in the ultimate parent company of MCC Securities, Inc. ("MCCS"), Moore, Clayton & Co., Inc. ("MCC"). HEI paid a fund raising fee to MCCS totalling US\$40,000 in the year. There were no amounts outstanding at 29 February 2004.

HEI purchased various management services from MCC totalling US\$67,000 in the year. There were no amounts outstanding at 29 February 2004.

L J Gaborit is the Managing Director of Industrial Management & Equity Ltd ("IME"). HCEG purchased strategic consultancy services from IME totalling £160,000 and advanced a further £15,000 in the year. There were no amounts outstanding at 29 February 2004.

G A Wood is a Director and shareholder of Safasia Co. Ltd ("Safasia"). S.A.F.A. Ltd ("SAFA") purchased first aid disposables from Safasia totalling £35,000 in the year. As at 29 February 2004, SAFA owed £1,000 to Safasia.

K Denos is the Managing Director of Talwar Capital Group Ltd ("Talwar"). HEI purchased strategic consultancy services from Talwar totalling US\$90,000 in the year. There were no amounts outstanding at 29 February 2004.

K Denos is the principle of Kenneth I. Denos, P.C. ("KID"). HEI purchased legal services from KID totalling US\$124,000 in the year. As at 29 February 2004, HEI owed US\$12,000 to KID.

11. Goodwill

Group	Goodwill arising on reverse acquisition £'000	Goodwill arising on acquisitions in the year £'000	Total £'000
Cost			
At 1 March 2003	–	–	–
Additions	840	14,921	15,761
At 29 February 2004	840	14,921	15,761
Amortisation			
At 1 March 2003	–	–	–
Provided for the year	840	245	1,085
At 29 February 2004	840	245	1,085
Net book value			
At 29 February 2004	–	14,676	14,676
At 28 February 2003	–	–	–

12. Tangible fixed assets

Group	Freehold land & buildings £'000	Leasehold land & buildings £'000	Computer equipment £'000	Plant, equipment, fixtures & fittings £'000	Motor vehicles £'000	Total £'000
Cost						
At 1 March 2003 as previously reported	–	–	–	–	–	–
Adjustment for reverse acquisition	–	–	4	12	–	16
At 1 March 2003 as restated	–	–	4	12	–	16
Acquisition through new subsidiaries	876	10	612	431	101	2,030
Additions	–	–	44	3	–	47
Exchange differences	–	–	(1)	(2)	(1)	(4)
At 29 February 2004	876	10	659	444	100	2,089
Depreciation						
At 1 March 2003 as previously reported	–	–	–	–	–	–
Adjustment for reverse acquisition	–	–	1	4	–	5
At 1 March 2003 as restated	–	–	1	4	–	5
Acquisition through new subsidiaries	95	8	575	380	35	1,093
Charge for the year	5	–	10	9	8	32
Exchange differences	–	–	–	(1)	–	(1)
At 29 February 2004	100	8	586	392	43	1,129
Net book value						
At 29 February 2004	776	2	73	52	57	960
At 28 February 2003	–	–	3	8	–	11

The net book value of motor vehicles includes an amount of £24,000 (2003: £nil) in respect of assets held under hire purchase contracts and a related depreciation charge of £3,000 (2003: £nil).

Company	Freehold land & buildings £'000	Leasehold land & buildings £'000	Computer equipment £'000	Plant, equipment, fixtures & fittings £'000	Motor vehicles £'000	Total £'000
Cost						
At 1 March 2003	–	–	–	–	–	–
Additions	–	–	6	–	–	6
Acquired from subsidiary undertaking	422	–	–	–	–	422
At 29 February 2004	422	–	6	–	–	428
Depreciation						
At 1 March 2003	–	–	–	–	–	–
Charge for the year	–	–	1	–	–	1
At 29 February 2004	–	–	1	–	–	1
Net book value						
At 29 February 2004	422	–	5	–	–	427
At 28 February 2003	–	–	–	–	–	–

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13. Fixed asset investments

(a) Investments in subsidiary undertakings

Company	£'000
At 1 March 2003	–
Acquisitions	15,163
Loans to subsidiary undertakings	9,118
At 29 February 2004	24,281

(b) Investments in associated undertakings

Group	£'000
At 1 March 2003	–
Goodwill arising on acquisitions in the year	449
Group's share of post acquisition results of associated undertakings	(5)
Group's share of net assets of associated undertakings	19
At 29 February 2004	463

Company	£'000
At 1 March 2003	–
Acquisitions	389
At 29 February 2004	389

The Group's associated undertakings are as follows:

Name	Principal activity	Country of incorporation or registration	Proportion of issued shares held	Accounting reference date
Ebiox Ltd ¹	Developer and manufacturer of surface decontamination products	England and Wales	35%	31 March
Optiscope Technologies Ltd ²	Developer and manufacturer of disposable endoscopes	Israel	18%	31 December
Biosilk Ltd ³	Developer and manufacturer of wound dressings	Israel	12%	31 December

Note 1 An interest of 35% is held through SafaTec (UK) Limited ("SafaTec"), a subsidiary in which the Group has a 60.7% interest. A further 14.17% is held directly by HCEG.

Note 2 An interest of 29% is held by SafaTec.

Note 3 An interest of 20% is held by SafaTec.

In addition, at the year end, the Group had a 50% economic interest in Strategic Creative Solutions, LLC, a healthcare marketing and advertising firm based in the United States of America.

(c) Other investments

	Group £'000	Company £'000
At 1 March 2003 as previously reported	–	–
Adjustment for reverse acquisition	32	–
At 1 March 2003 as restated	32	–
Additions in the year	25	18
Exchange difference	(5)	–
At 29 February 2004	52	18

14. Principal subsidiaries

The principal subsidiary undertakings of the Group are as follows:

Name	Principal activity	Country of incorporation or registration	Proportion of issued shares held
Healthcare Enterprise Group, Inc.	Healthcare consulting and advisory services	United States of America	100%
Medical Development Specialists, Inc.*	Healthcare planning and marketing services	United States of America	100%
Healthcare Enterprise Ltd	Holding company	England and Wales	100%
SAFA-IPS Healthcare Ltd*	Distribution of occupational health and first aid products	England and Wales	100%
S.A.F.A. Ltd*	Dormant (post year end)	England and Wales	100%
Moore Health Care Ltd*	Dormant	England and Wales	100%
Chaincroft Ltd*	Dormant	England and Wales	100%
SafaTec (UK) Ltd	Holding company	England and Wales	60.7%

* A sub-subsidiary of HCEG.

All of the companies have accounting reference dates of 28 February except for Medical Development Specialists, Inc. ("MDS") whose accounting reference date is 31 December.

15. Stocks

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Finished goods and goods for resale	866	–	–	–

16. Debtors

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Trade debtors	1,838	22	–	–
Amounts due from subsidiary undertakings	–	–	954	–
Amounts due from associated undertakings	96	–	–	–
Prepayments and accrued income	145	–	20	–
Other debtors	115	81	92	267
	2,194	103	1,066	267

Included in amounts due from subsidiary undertakings, in the Company's balance sheet, is an amount of £50,000 (2003: £nil) which is due after one year.

Notes to the financial statements

for the year ended 29 February 2004
continued

17. Creditors: amounts falling due within one year

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Bank and other loans	1,280	15	1,275	–
Net obligations under hire purchase contracts	7	–	–	–
Trade creditors	1,443	13	125	206
Corporation tax	296	–	–	–
Other taxation and social security	69	–	–	–
Amounts due to subsidiary undertakings	–	–	265	–
Other creditors	11	–	1	7
Accruals and deferred income	1,188	–	569	95
	4,294	28	2,235	308

18. Creditors: amounts falling due after more than one year

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Bank and other loans	1,501	–	1,475	–
Net obligations under hire purchase contracts	15	–	–	–
	1,516	–	1,475	–

Bank and other loans are repayable as follows:

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
In one year or less	1,280	15	1,275	–
Between one and two years	465	–	450	–
Between two and five years	1,036	–	1,025	–
	2,781	15	2,750	–

Bank loans of £2,750,000 are secured by £1,150,000 held in the Company's collateral account. In addition, security has been granted to the bank as follows:

- (a) Cross-guarantees from the Company and certain of its subsidiaries;
- (b) Fixed and floating charges over the business and assets of the Company and certain of its subsidiaries;
- (c) A first legal charge over two freehold premises belonging to the Group;
- (d) Share pledges given by certain members of the Group.

Of the Group's £750,000 invoice discounting facility, £315,000 has been drawn down at 29 February 2004 and is secured over the trade debtors of certain members of the Group.

19. Obligations under hire purchase contracts

The maturity of amounts due under hire purchase contracts is as follows:

Group	2004 £'000	2003 £'000
Repayable within one year	8	–
Repayable between one and five years	18	–
	26	–
Finance charges and interest allocated to future accounting periods	(4)	–
	22	–
Included in creditors falling due within one year	7	–
Included in creditors falling due after more than one year	15	–
	22	–

20. Provisions for liabilities and charges

The amount of £29,000 (2003: £nil) shown in the consolidated balance sheet represents the Group's share of the net liabilities of Ebiox Ltd as at 29 February 2004.

21. Called up share capital

Group and Company	2004 £'000	2003 £'000
Authorised:		
20,000,000,000 ordinary shares of 0.1 pence each	20,000	–
186,502,731 deferred shares of 0.4 pence each	746	–
500,000,000 ordinary shares of 0.5 pence each	–	2,500
	20,746	2,500

Group and Company	2004 £'000	2003 £'000
Allotted, called up and fully paid:		
2,811,638,955 ordinary shares of 0.1 pence each	2,812	–
186,502,731 deferred shares of 0.4 pence each	746	–
186,502,731 ordinary shares of 0.5 pence each	–	932
	3,558	932

In the consolidated balance sheet, the share capital balance of £6,000 as at 28 February 2003 is that of HEI prior to the reverse acquisition. This represented 10,426,187 Common Stock Shares of \$0.001.

By an ordinary resolution on 10 March 2003:

- Each of the issued ordinary shares of 0.5 pence in the capital of the Company were sub-divided and converted into one ordinary share of 0.1 pence and one deferred share of 0.4 pence;
- Each of the unissued ordinary shares of 0.5 pence in the capital of the Company were sub-divided into five ordinary shares of 0.1 pence;
- The authorised share capital of the Company was increased from £2,500,000 to £4,000,000 by the creation of 1,500,000,000 ordinary shares of 0.1 pence each.

The resulting new ordinary shares have the same rights, including voting rights, dividend rights and rights on a return of capital, as the existing ordinary shares. The resulting deferred ordinary shares carry no voting rights and are not marketable.

By a special resolution on 13 November 2003, the authorised share capital of the Company was further increased from £4,000,000 to £20,746,010 by the creation of 16,746,010,924 ordinary shares of 0.1 pence each.

Notes to the financial statements

for the year ended 29 February 2004
continued

21. Called up share capital (continued)

During the year the Company issued 2,625,136,224 ordinary shares of 0.1 pence each as follows:

Number	Price	Reason
1,180,723,605	0.625p	Issued as consideration for the reverse acquisition of HEI
7,450,500	0.75p	Issued as a result of the exercise of share options
30,000,000	1.0p	Subscription by Prestbury Investment Holdings Ltd
16,906,750	1.0p	Issued as part settlement of professional advisers' fees
1,050,000,000	1.0p	Placing by Numis Securities Ltd on 14 November 2003
250,900,000	1.0p	Issued as consideration for the acquisition of The S.A.F.A. Group Ltd, Industrial Pharmaceutical Service Ltd and SafaTec
20,478,374	1.69p	Issued as consideration for the acquisition of MDS
700,000	1.74p	Issued in cancellation of a phantom share scheme previously operated by SAFA
2,645,503	1.89p	Issued as part settlement of professional advisers' fees
15,000,000	1.94p	Issued as consideration for the acquisition of a 14.17% share in Ebiox Ltd
50,331,492	0.1p	Issued as a result of the exercise of share options
2,625,136,224		

Deferred consideration payments, totalling £2,258,000 have been accrued at the balance sheet date. These payments will be satisfied by the issue of ordinary shares in the Company and are more fully explained in note 26 to the accounts.

22. Options

The Company operates both an Inland Revenue approved share option scheme and unapproved share option schemes, under which options have been granted to employees and Directors.

Options over ordinary shares outstanding at 29 February 2004 are as follows:

Date of grant	No. of shares	Exercise price	First exercise date	Expiry date
Approved				
14 November 2003	1,875,000	1.6p	14 November 2003	13 November 2013
Unapproved				
1 August 2001	105,153,640	0.1p	1 August 2001	31 July 2006
19 December 2002	33,973,791	0.41p	19 December 2002	18 December 2007
1 January 2003	38,928,303	0.1p	1 January 2003	31 December 2007
14 November 2003	48,125,000	0.98p	14 November 2003	13 November 2013
14 November 2003	21,070,153	1p	14 November 2003	13 November 2006
10 December 2003	124,275,521	1p	10 December 2004	9 December 2013
10 December 2003	1,245,706	0.883p	10 December 2003	23 June 2013
6 January 2004	40,000,000	1.38p	6 January 2004	5 January 2014
	414,647,114			

23. Warrants issued

On 14 November 2003, a total of 272,107,681 warrants were issued as follows:

- One warrant for every ten ordinary shares subscribed for under the placing by Numis Securities Ltd of 1,050,000,000 ordinary shares;
- One warrant for every ten existing ordinary shares held as at 12 November 2003;
- One warrant for every ten ordinary shares issued as consideration for the acquisition of The S.A.F.A. Group Limited ("SAFA Group"), Industrial Pharmaceutical Service Ltd ("IPS") and SafaTec.

The warrants are tradeable on AIM, separately from the ordinary shares of the Company, and each warrant entitles the holder to subscribe to one ordinary share of the Company at a price of 1.5 pence per share on any one of the following dates: 30 June 2004, 2005, 2006, 2007 and 2008 (or, if later, on the thirtieth day after the date on which copies of the audited accounts of the Company for the immediately preceding financial year are despatched to shareholders). These warrants were assigned a value of 0.13 pence each at the date of issue.

On 29 August 2003, along with 30,000,000 ordinary shares of 1 pence each, 30,000,000 warrants were issued to Prestbury Investment Holdings Ltd. Each warrant entitles the holder to subscribe to one ordinary share of the Company at a price of 1 pence per share. These warrants, which are not tradeable on AIM, are exercisable for a period of two years commencing on 14 November 2003 on giving 5 days' written notice. If not exercised during this period, the warrants will lapse.

24. Reserves

Group	Share premium account £'000	Profit and loss account £'000	Merger reserve £'000	Other reserves £'000
At 1 March 2003 as previously reported	1,919	(2,273)	–	52
Adjustment for reverse acquisition	(6,199)	1,974	(2,293)	(919)
At 1 March 2003 as restated	(4,280)	(299)	(2,293)	(867)
Exchange losses offset in reserves	–	(49)	–	–
Retained loss for the financial year	–	(2,976)	–	–
Movement in provision for share options	–	33	–	1,759
Issue of ordinary share capital (net of warrants issued)	18,674	–	–	–
Costs associated with issue of ordinary share capital	(175)	–	–	–
At 29 February 2004	14,219	(3,291)	(2,293)	892

Company	Share premium account £'000	Profit and loss account £'000	Other reserves £'000
At 1 March 2003	–	1,919	52
Retained loss for the financial year	–	–	(1,421)
Movement in provision for share options	–	–	33
Issue of ordinary share capital (net of warrants issued)	–	18,674	–
Costs associated with issue of ordinary share capital	–	(175)	–
At 29 February 2004	–	20,418	(3,661)

25. Reconciliation of movements in shareholders' funds

	Group		Company	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Loss for the financial year	(2,976)	(285)	(1,421)	(2)
Issue of new share capital net of expenses	21,489	528	21,489	–
Shares to be allotted	2,258	–	2,258	–
Movement in provision for share options	1,792	–	1,792	(51)
Exchange losses offset in reserves	(49)	–	–	–
Capital adjustment for reverse acquisition accounting	(7,132)	–	–	–
Opening shareholders' funds	325	82	630	683
Closing shareholders' funds	15,707	325	24,748	630
Shareholders' funds comprise:				
Equity interests	14,961	325	24,002	630
Non-equity interests	746	–	746	–
	15,707	325	24,748	630

26. Acquisitions and disposals

(a) Reverse acquisition by Healthcare Enterprise Group, Inc.

On 11 March 2003, HEI completed the reverse acquisition of Interactivity Group plc. To reflect the reverse acquisition, a notional cost of investment, based on the fair value of Interactivity Group plc shares at the date of acquisition, has been used. Goodwill has been calculated as the difference between this cost of investment and the fair value of Interactivity Group plc's net assets acquired, as set out below:

	Book value £'000	Fair value adjustment £'000	Fair value to the Group £'000
Debtors	41	–	41
Cash at bank and in hand	671	–	671
Creditors	(386)	–	(386)
Net assets	326	–	326
Goodwill	–	–	840
Consideration (186,502,731 shares at 0.625p)			1,166

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continued

26. Acquisitions and disposals (continued)

The goodwill of £840,000 has been written off in the year to 29 February 2004, as Interactivity Group plc has no continuing business and therefore the goodwill has no intrinsic value.

A merger reserve balance of £2,293,000 arises as a result of the reverse acquisition accounting method and relates to the difference between Interactivity Group plc and HEI share capital and share premium accounts prior to the reverse acquisition.

From 1 March 2003 to 11 March 2003, Interactivity Group plc had no turnover and incurred no costs. From 1 October 2002 to 28 February 2003, Interactivity Group plc had no turnover and an operating loss of £11,000. The loss before and after tax was £2,000 and there was no difference between the loss after tax and the recognised gains and losses for the period.

(b) Acquisition of The S.A.F.A. Group Ltd, Industrial Pharmaceutical Service Ltd and 60.7% of SafaTec (UK) Ltd

Effective November 2003, the Company acquired the whole of the issued share capital of SAFA Group and 60.7% of SafaTec.

On the same date SAFA, a wholly owned subsidiary of SAFA Group, acquired the whole of the issued share capital of IPS.

Total consideration, including costs of acquisition and deferred consideration payments which have been accrued at the balance sheet date, amounted to £14,101,000. The transactions have been accounted for under the acquisition method of accounting.

The total goodwill arising is being amortised through the consolidated profit and loss account over its useful economic life.

From 1 August 2003 to 31 October 2003, SAFA Group had sales of £828,000 and an operating loss of £154,000. The loss before and after tax was £185,000. The loss after tax for SAFA Group, for the year ended 31 July 2003, was £23,000. There was no difference between the loss after tax and the recognised gains and losses in either period.

From 1 January 2003 to 31 October 2003, IPS had sales of £5,730,000 and an operating profit of £876,000. Profit before tax was £851,000 and taxation amounted to £228,000. The profit after tax for IPS, for the year ended 31 December 2002, was £496,000. There was no difference between profit after tax and the recognised gains and losses in either period.

The following table sets out the book values of the identifiable assets and liabilities acquired and their provisional fair values to the Group:

	The S.A.F.A. Group £'000	Industrial Pharmaceutical Service Ltd £'000	Fair value adjustment £'000	Total fair value to the Group £'000
Fixed assets	511	402	–	913
Stock	313	578	–	891
Debtors	1,205	849	–	2,054
Cash at bank and in hand	–	413	–	413
Creditors and provisions	(2,813)	(1,775)	–	(4,588)
Net (liabilities)/assets	(784)	467	–	(317)
Goodwill				10,329
Purchase consideration and costs of acquisition				10,012
Satisfied by:				
Shares issued				600
Cash				8,781
Costs satisfied through the issue of shares				231
Deferred consideration				400
				10,012

Of the £10,329,000 goodwill arising on the acquisitions, £3,410,000 relates to the acquisition of SAFA Group and £6,919,000 to the acquisition of IPS.

The deferred consideration of £400,000 relates to the acquisition of IPS. £200,000 has been paid in cash after the balance sheet date. A further £200,000 has been deposited into an escrow account to be released to the IPS vendors on 28 February 2005. Both amounts were accrued in full at the balance sheet date.

SafaTec was incorporated on 2 April 2003. Other than acquiring interests in other entities, the Company did not trade in the period to 14 November 2003. At acquisition, it had net assets of £50,000 and no fair value adjustments were made. Initial consideration of £100,000 was paid in cash and shares to the value of £1,909,000 were issued. As a result of certain performance milestones being achieved after the transaction date, additional deferred consideration of £2,080,000 became payable. This consideration has since been satisfied by the issue of shares and was accrued in full at the balance sheet date. Goodwill of £4,059,000 has arisen on the acquisition of SafaTec.

26. Acquisitions and disposals (continued)

Further performance related amounts, up to a maximum of £3,695,000 (to be satisfied by the issue of shares), may become payable between the date of acquisition and 30 June 2005 depending upon the attainment of certain milestones.

In addition further sums could become payable dependent upon the success (up to 30 June 2005) of an Israeli company in which SafaTec holds an interest. At this point in time it is not considered necessary to accrue any additional deferred consideration.

Initial estimates of the deferred consideration will be revised as further and more certain information becomes available, with corresponding adjustments to goodwill.

(c) Acquisition of Medical Development Specialists, Inc.

On 7 January 2004, HEI acquired the whole of the issued share capital of MDS. The consideration for the transaction amounted to £553,000 and the transaction has been accounted for under the acquisition method of accounting. Goodwill arising on the transaction is being amortised through the consolidated profit and loss account over its useful economic life.

MDS had net assets of £20,000 and no fair value adjustments were made. Initial consideration of £346,000 in shares was given, while costs of the acquisition of £29,000 were satisfied in cash. Further additional consideration of £178,000 (to be satisfied by the issue of shares) has been accrued, which represents the best estimate at the present time of the amount reasonably expected to be payable. Goodwill of £533,000 has arisen on the acquisition of MDS. Further additional amounts could become payable dependent upon the attainment of certain performance targets in the years to 28 February 2006 and 2007.

Initial estimates of the deferred consideration will be revised as further and more certain information becomes available, with corresponding adjustments to goodwill.

(d) Disposal of portfolio holdings

On 6 January 2004, HEI sold its entire interests in five private healthcare/biotechnology companies. The consideration for the disposal comprises:

1. A loan note of \$2,650,000 payable on 5 January 2009. The loan note bears interest at 5% per annum, which is also payable on 5 January 2009. The loan note is secured on the interests being sold.
2. HEI is entitled to 20% of any realised increase in each of the portfolio interests above their base amounts (determined in accordance with the loan note).
3. HEI has a 20% limited partnership interest in the Delaware Limited Partnership which has purchased these portfolio interests.

The interests in these five companies were represented on the HEI balance sheet at \$1.

The Group has not, at the balance sheet date, recognised any income relating to the above disposal because of the uncertainty in quantifying the current value of the loan note. As further and more certain information becomes available concerning the development of the five companies, the Directors will reconsider what, if any, income can be recognised in the Group financial statements.

27. Reconciliation of operating loss to net cash outflow from operating activities

	2004 £'000	2003 £'000
Operating loss	(2,689)	(283)
Amortisation of intangible fixed assets	1,085	–
Depreciation of tangible fixed assets	32	3
Decrease in stocks	25	–
Decrease/(increase) in debtors	255	(15)
(Decrease)/increase in creditors	(756)	8
Movement in provision for share options	873	–
Reorganisation costs	(148)	–
Net cash outflow from operating activities	(1,323)	(287)

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28. Analysis of movement in net funds/(debt)

	At 1 March 2003 £'000	Cash flow £'000	Acquisitions (excluding cash and overdrafts) £'000	Other non cash changes £'000	Exchange difference £'000	At 29 February 2004 £'000
Cash at bank and in hand	207	2,132	–	–	–	2,339
Debt due after one year	–	(1,475)	(17)	(13)	4	(1,501)
Debt due within one year	(15)	(410)	(868)	13	–	(1,280)
Hire purchase contracts	–	2	(24)	–	–	(22)
Net funds/(debt)	192	249	(909)	–	4	(464)

29. Reconciliation of net cash flow to movement in net (debt)/funds

	2004 £'000	2003 £'000
Increase in cash in the year	2,132	196
Cash (inflow)/outflow from change in debt and lease financing	(1,883)	11
Change in net funds resulting from cash flows	249	207
Loans and hire purchase contracts acquired with subsidiaries	(909)	–
Exchange difference	4	–
Movement in net (debt)/funds	(656)	207
Net funds/(debt) at the beginning of the year	192	(15)
Net (debt)/funds at the end of the year	(464)	192

30. Financial instruments

The following analysis excludes short term debtors and creditors as permitted under Financial Reporting Standard 13. The Group's policy in respect of financial instruments is set out in note 1 to the financial statements.

(a) Financial assets

The interest rate and currency profiles of the Group's financial assets, excluding short term debtors, as at the end of the year were:

Currency	Floating rate 2004 £'000	Non-interest bearing 2004 £'000	Total 2004 £'000	Floating rate 2003 £'000	Non-interest bearing 2003 £'000	Total 2003 £'000
Sterling	1,124	1,195	2,319	–	–	–
US Dollar	–	40	40	–	229	229
Euro	–	36	36	–	10	10
	1,124	1,271	2,395	–	239	239

The financial assets consist of cash at bank and in hand, current asset investments and fixed asset investments (excluding interests in associated undertakings).

The floating rate assets earn interest at rates based on LIBOR. The non-interest bearing assets include equity investments for which there is no maturity date and cash at bank and in hand.

30. Financial instruments (continued)

(b) Financial liabilities

The interest rate and currency profiles of the Group's financial liabilities, excluding short term creditors, as at the end of the year were:

Currency	Fixed rate 2004 £'000	Floating rate 2004 £'000	Total 2004 £'000	Fixed rate 2003 £'000	Floating rate 2003 £'000	Total 2003 £'000
Sterling	22	2,750	2,772	–	–	–
US Dollar	31	–	31	15	–	15
	53	2,750	2,803	15	–	15

The floating rate liabilities incur interest at rates related to LIBOR.

The weighted average interest rate on fixed rate liabilities is 7% and is fixed for a period of 2 years.

(c) Currency exposure

Group companies principally operate in their functional currency and the impact of any currency exposures would not be material.

(d) Borrowing facilities

At the balance sheet date the Group had an undrawn invoice discounting facility of £435,000 which is subject to review in less than one year.

(e) Fair value of assets and liabilities

There is no material difference between the fair value of the Group's financial assets and liabilities and their book value as shown in the financial statements.

31. Financial commitments

At 29 February 2004, the Group had annual commitments under non-cancellable operating leases as set out below:

Group	Land & buildings 2004 £'000	Other 2004 £'000	Land & buildings 2003 £'000	Other 2003 £'000
Operating leases which expire:				
Within one year	36	24	–	–
In two to five years	17	35	–	–
In more than five years	8	–	–	–
	61	59	–	–

At 29 February 2004 the Company had annual commitments of £36,000 (2003: £nil) under non-cancellable operating leases relating to land and buildings, which expire within one year.

32. Contingent assets

The Group has not recognised any income in respect of the disposal of interests in five companies because of uncertainties over the current value of the consideration. Further details are set out in note 26(d).

33. Post balance sheet events

After the balance sheet date, the Company signed heads of agreement to acquire the whole of the issued share capital of First Aid UK Ltd. Total consideration for the acquisition, which is subject to agreement of definitive documentation, is expected to be £2,000,000 with approximately half payable on completion and the remainder paid as an earn-out over two years.

The transaction had not completed at the date on which these financial statements were approved but was expected to complete shortly thereafter.

Company information

Executive Chairman	S Bruck
Executive Directors	G A Wood M K Low L J Gaborit K Denos
Non-Executive Directors	N O Brigstocke H J M Tompkins N W Wray (appointed 15 June 2004)
Secretary	L J Gaborit
Company Number	3627383
Registered Office	Second Floor College House 272 King's Road London SW3 5AW
Auditors	HLB AV Audit plc 66 Wigmore Street London W1U 2HQ
Nominated Advisers and Stockbroker	Numis Securities Ltd Cheapside House 138 Cheapside London EC2V 6LH
Solicitors	Norton Rose Kempson House Camomile Street London EC3A 7AN
Bankers	Barclays Bank plc 54 Lombard Street London EC3P 3AH
Registrars	Capita IRG plc The Registry 34 Beckenham Road Beckenham Kent BR3 4TU

