# Novartis Pharmaceuticals UK Limited

# Annual Report
# for the year ended 31 December 2013

Registered no: 119006

# Novartis Pharmaceuticals UK Limited
# Annual Report
# for the year ended 31 December 2013

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# Novartis Pharmaceuticals UK Limited
# Directors and Advisors



## Directors

G Guidi (Chairman)
E Arrocha
H Kirsch
L Prat
F Guerard

## Secretary

B Holgate

## Registered office

Frimley Business Park
Frimley
Camberley
Surrey
GU16 7SR

## Independent Auditors

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
The Portland Building
25 High Street
Crawley
West Sussex
RH10 1BG

The Directors present their Strategic Report of the Company for the year ended 31 December 2013.

## Review of business and future developments

The results for the Company show a loss for the financial year of £15,625,000 (2012 restated: £ 12,084,000) and turnover of £550,712,000 (2012: £544,297,000). The Company had net assets of £624,000 as at 31 December 2013 (2012: £59,507,000). During the year the Directors recommended a final dividend of £10,000,000 in relation to the year ended 31 December 2013 (2012: £20,000,000).

The Directors are pleased with the performance of the Company for 2013 given the continued competitive pressure from both branded and generic pharmaceuticals present in the market.

Third party turnover for Pharma increased by 1.2% driven by strong volume growth on Lucentis, Gilenya, Seebri, Afinitor and Tasigna, this was part offset by generic erosion of Zometa, Exelon and Exelon Patch.

Turnover from Services declined by 33.6% vs. 2012 due to the phased closure of the production facility.

## Principal risks and uncertainties

More recently the Company has seen other industries facing financial uncertainty with the economic downturn. The Directors do not anticipate this downturn will have a significant impact on the business due to the industry in which the Company operates.

An inherent risk to the pharmaceutical industry is the entry of generic competition and continued government pressure to control spending on NHS medicines.

## Key performance indicators ("KPIs")

The Company operates in a highly complex environment and management use and review many performance measures.

Four of the Company's KPIs in line with the long term strategies are as follows:

| | 2013 | 2012 | Comments |
|---|---|---|---|
| Increase in turnover (%) | 1.2 | -3.3 | Revenue increased by 1.2%, driven by strong volume growth on Lucentis, Gilenya, Seebri, Afinitor and Tasigna. This was part offset by generic erosion of Zometa, Exelon and Exelon Patch and a decline in turnover from services due to the phased closure of the production facility. |
| Gross margin (%) | 18.4 | 17.6 | Gross margins increased by 1.8 ppt vs. 2012 due to changes in the brand mix. |
| Market share (%) | 3.9 | 3.4 | Novartis growth was in line with the market growth of 3.6%. |
| Number of new launches | 0 | 5 | 2013: None<br>2012: Seebri Breezhaler, Jakavi, Afinitor, Votubia in AML and Signifor. |

On behalf of the Board

E Arrocha
Director
30 September 2014

# Novartis Pharmaceuticals UK Limited
# Directors' Report
# for the year ended 31 December 2013

The Directors present their report and the audited financial statements of the Company for the year ended 31 December 2013. These financial statements are prepared under United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 101 *Reduced Disclosure Framework* (FRS 101).

## Directors

The Directors who held office during the year and up to the date of signing these financial statements were as follows:

J Symonds (Resigned on 20 June 2013)
H Kirsch (Appointed on 20 June 2013)
L Prat
S Kapadia (Resigned on 26 August 2014)
E Arrocha (Appointed on 26 August 2014)
F Guerard
E Cornut (Chairman) (Resigned on 24 January 2013)
G Guidi (Chairman) (Appointed on 24 January 2013)

## Research and Development

The Company maintains laboratories and other facilities and devotes considerable resources to research and development aimed at developing new products and new processes. The amounts spent by the Company on research and development activities are shown in the Profit and Loss Account on page 10.

## Political and Charitable Donations

Charitable donations totalling £13,150 (2012: £11,000) were made to local charities during the year. £2,000 related to Marie Curie Cancer Care, £2,150 to Whizz-Kidz (Movement for non-mobile children), £3,000 to Phyliss Tuckwell Hospice and £6,000 was a donation to Horsham in Bloom. No political donations were made.

## Dividends

An interim dividend amounting to £10,000,000 (2012: £20,000,000) was proposed and paid.

## Employees

The Company gives full and fair consideration to applications for employment received from disabled persons, having regard to their particular aptitudes and abilities and wherever possible the Company continues the employment of, and arranges for the appropriate training of, employees who become disabled persons whilst employed by the Company. Disabled employees are treated no differently from other employees as regards training, career development and promotion opportunities. This policy was operated by the Company, where appropriate, throughout the year.

The Company recognises the importance of keeping employees informed of the progress of the business. During the year employees were regularly provided with information regarding the financial and economic factors affecting the performance of the Company and on other matters of concern to them as employees. Regular consultations take place with employee representatives. The employee share scheme introduced in 2002 continued to be available in 2013 to encourage employee involvement in the Company's performance. The share scheme relates to shares in Novartis AG, the ultimate parent company of Novartis Pharmaceuticals UK Limited.

## Post Balance Sheet Events

On 22 April 2014, Novartis announced a global restructure of its portfolio. As part of this Novartis will acquire GlaxoSmithKline (GSK) oncology products, Novartis will also become GSK's preferred commercialization partner for its current and future oncology R&D pipeline. The deal is expected to close during the first half of 2015.

## Directors Indemnity

The Company has entered into qualifying indemnity arrangements for the benefit of all its Directors in relation to certain losses and liabilities which they may incur to third parties in the course of acting as directors of the Company and in compliance with the requirements of the Companies Act 2006. It has been in place at any time during the financial year and at the date of approval of the Directors' report.

## Statement of Directors' responsibilities

The Directors are responsible for preparing the Strategic Report and Directors' Report and the financial statements in accordance with applicable law and regulations.

## Statement of Directors' responsibilities (continued)

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 101 *Reduced Disclosure Framework* (FRS 101).

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable United Kingdom Accounting Standards, including FRS 101, have been followed, subject to any material departures disclosed and explained in the financial statements;
- notify its shareholders in writing about the use of disclosure exemptions, if any, of FRS 101 used in the preparation of financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## Directors' statement on disclosure of information to auditors

Each of the Directors in office at the date the Directors' report is approved confirms that:

(a) so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and

(b) he has taken all the steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

## Independent Auditors

An elective resolution has been passed to maintain PricewaterhouseCoopers LLP as auditors until such time as the Board decides otherwise.

On behalf of the Board

E Arrocha
Director
30 September 2014

# Independent auditors' report to the members of Novartis Pharmaceuticals UK Limited

## Report on the financial statements

### Our opinion

In our opinion the financial statements, defined below:

- give a true and fair view of the state of the Company's affairs as at 31 December 2013 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

This opinion is to be read in the context of what we say in the remainder of this report.

### What we have audited

The financial statements, which are prepared by Novartis Pharmaceuticals UK Limited, comprise:

- the Balance Sheet as at 31 December 2013;
- the Profit and Loss Account and Statement of Total Recognised Gains and Losses for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 "Reduced Disclosure Framework".

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

### What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

# Independent auditors' report to the members of Novartis Pharmaceuticals UK Limited

## Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

## Other matters on which we are required to report by exception

### Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

### Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

## Responsibilities for the financial statements and the audit

### Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' responsibilities set out on pages 5 and 6, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

## Other matter

The Company has passed a resolution in accordance with section 506 of the Companies Act 2006 that the senior statutory auditor's name should not be stated.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Gatwick
30 September 2014

# Novartis Pharmaceuticals UK Limited
# Profit and Loss Account
# for the year ended 31 December 2013



| | Note | 2013 £'000 | Restated 2012 £'000 |
|---|---|---|---|
| **Turnover** | 3 | 550,712 | 544,297 |
| Cost of sales | | (443,772) | (448,486) |
| **Gross profit** | | 106,940 | 95,811 |
| Other operating income | | 109,728 | 105,046 |
| Selling and marketing costs | | (93,146) | (92,953) |
| Research and development costs | | (86,030) | (88,984) |
| Administrative expenses | | (6,762) | (10,803) |
| **Operating profit before exceptional items** | | 30,730 | 8,117 |
| Exceptional items | 4 | (46,761) | - |
| **Operating (loss) / profit** | 4 | (16,031) | 8,117 |
| Interest receivable and similar income | 5 | 30 | 145 |
| Interest payable and similar charges | 5 | (171) | (184) |
| (Loss) / profit on ordinary activities before taxation | | (16,172) | 8,078 |
| Tax credit on profit on ordinary activities | 6 | 547 | 4,006 |
| **(Loss) / profit for the financial year** | | (15,625) | 12,084 |

The notes on pages 14 to 42 are an integral part of these financial statements.

# Novartis Pharmaceuticals UK Limited 
# Statement of Total Recognised Gains and Losses for the year ended 31 December 2013

| | Note | 2013<br>£'000 | Restated<br>2012<br>£'000 |
|---|---|---|---|
| (Loss) / profit for the financial year | | (15,625) | 12,084 |
| Actuarial (loss) / gain on pension obligation | 18 | (40,223) | 5,349 |
| Deferred tax on actuarial (loss) / gain | 14 | 6,568 | (2,145) |
| (Loss) / gain on post retirement medical benefit | | (23) | 105 |
| **Net (loss) / profit not recognised in the Profit and Loss Account** | | (33,678) | 3,309 |
| **Total recognised losses and gains relating to the year** | | (49,303) | 15,393 |

Cumulative actuarial losses on the pension scheme amount to £107,765,000 (2012 restated: £67,542,000), recognised directly in the Statement of Total Recognised Gains and Losses.

The notes on pages 14 to 42 are an integral part of these financial statements.

# Novartis Pharmaceuticals UK Limited



# Balance Sheet as at 31 December 2013

| | Note | 2013 £'000 | 2012 £'000 |
|---|---|---|---|
| **Fixed assets** | | | |
| Tangible assets | 8 | 31,437 | 75,943 |
| Investments | 9 | 28,100 | 28,100 |
| | | 59,537 | 104,043 |
| **Current assets** | | | |
| Stocks | 10 | 62,099 | 71,139 |
| Debtors | 11 | 87,377 | 62,385 |
| Deferred tax asset | 14 | 15,700 | 2,496 |
| Cash at bank and in hand | | 675 | 4,854 |
| | | 165,851 | 140,874 |
| **Creditors – amounts falling due within one year** | | | |
| Financial liabilities: borrowings | 12 | 44,852 | - |
| Creditors | 13 | 83,611 | 115,984 |
| Provisions for liabilities | 15 | 32,592 | 9,514 |
| Current tax liability | | 3,289 | - |
| | | 164,344 | 125,498 |
| **Net current assets** | | 1,507 | 15,376 |
| **Creditors – amounts falling due after more than one year** | | | |
| Financial liabilities: borrowings | 12 | - | 19,000 |
| Retirement benefit liability | 18 | 60,154 | 23,896 |
| Provisions for liabilities | 15 | 266 | 17,016 |
| | | 60,420 | 59,912 |
| **Net assets** | | **624** | 59,507 |
| **Capital and reserves** | | | |
| Called up share capital | 16 | 5,400 | 5,400 |
| Share option recharge reserve | 17 | (2,174) | (2,594) |
| Profit and loss account | | (2,602) | 56,701 |
| **Total shareholders' funds** | | **624** | 59,507 |

The notes on pages 14 to 42 are an integral part of these financial statements.
The financial statements of Novartis Pharmaceuticals UK Limited (registered no: 119006) on pages 10 to 42 were approved by the Board of Directors and were signed on its behalf by:

E Arrocha
Director
30 September 2014

# Novartis Pharmaceuticals UK Limited

# Statement of Changes in Equity

| | Called up share capital £'000 | Share option recharge reserve £'000 | Profit and Loss Account £'000 | Total shareholders' fund £'000 |
|---|---|---|---|---|
| **At 1 January 2012** | 5,400 | (2,798) | 61,308 | 63,910 |
| Profit for the financial year (restated) | - | - | 12,084 | 12,084 |
| Actuarial gain on retirement benefit schemes (restated) | - | - | 5,349 | 5,349 |
| Deferred tax on actuarial gain on retirement benefit schemes (restated) | - | - | (2,145) | (2,145) |
| Gain on post retirement medical benefit | - | - | 105 | 105 |
| Dividends | - | - | (20,000) | (20,000) |
| Share options | - | 204 | - | 204 |
| **At 31 December 2012** | 5,400 | (2,594) | 56,701 | 59,507 |
| | | | | |
| **At 1 January 2013** | 5,400 | (2,594) | 56,701 | 59,507 |
| Loss for the financial year | - | - | (15,625) | (15,625) |
| Actuarial loss on retirement benefit schemes | - | - | (40,223) | (40,223) |
| Deferred tax on actuarial loss on retirement benefit schemes | - | - | 6,568 | 6,568 |
| Loss on post-retirement medical benefit | - | - | (23) | (23) |
| Dividends | - | - | (10,000) | (10,000) |
| Share options | - | 420 | - | 420 |
| **At 31 December 2013** | 5,400 | (2,174) | (2,602) | 624 |

The share option recharge reserve represents shares and options purchased on behalf of qualifying employees, from either the open market or the ultimate parent company, which are still to vest in future years. The share options and any recharges made by the parent company in respect of options granted are expensed over the vesting period of the options with the corresponding amount being taken to share option reserve.

The notes on pages 14 to 42 are an integral part of these financial statements.

## 1 Principal accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated. These financial statements were prepared on a going concern basis.

### General information

The Company is a limited company, domiciled and incorporated in the United Kingdom.

### Basis of preparation

These financial statements have been prepared in accordance with United Kingdom Accounting Standards, in particular, Financial Reporting Standard 101 *Reduced Disclosure Framework* (FRS 101) and the Companies Act 2006 (the Act) as applicable to companies using FRS101. FRS 101 sets out a reduced disclosure framework for a 'qualifying entity' as defined in the standard which addresses the financial reporting requirements and disclosure exemptions in the individual financial statements of qualifying entities that otherwise apply the recognition, measurement and disclosure requirements of EU - adopted IFRS.

The Company is a qualifying entity for the purposes of FRS 101. Note 22 gives details of the Company's ultimate parent and from where its consolidated financial statements prepared in accordance with IFRS may be obtained.

The Company has adopted the intermediate parent exemption under section 400 of the Companies Act 2006, whereby it is not required to prepare consolidated financial statements as the ultimate parent company prepares publicly available consolidated financial statements in accordance with IFRS.

The disclosure exemptions adopted by the Company in accordance with FRS 101 are as follows:
- Statement of cash flows
- Capital risk management
- Related party transactions
- Accounting standards issued but not yet effective
- Reduced disclosures in relation to share options

The financial statements have been prepared under the historical cost convention. A summary of the more important accounting policies is set out below.

## 1 Principal accounting policies (continued)

The preparation of financial statements in conformity with FRS 101 requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. The critical accounting policies of the Company pertain primarily to pensions and sales deduction provision which are described in further detail below.

### New and amended standards adopted by the Company:

IAS 19R *Employee Benefits* reporting has been adopted by the Company effective 1 January 2013, with 2012 results restated for the impact. See note 23 for the impact on the financial statements.

### Turnover

Turnover represents amounts received for packaged drugs sold primarily in the UK, net of trade discounts, rebate provisions, VAT and other related taxes. All turnover is recognised at the date of delivery when the risks and rewards transfer. Rebate provisions are calculated to represent management's best estimate of the likely rebate payments that will be required, taking into account historical rebate rates and expected drug efficacy. In addition, the Company also provides manufacturing services on a toll basis to fellow group undertakings, turnover from which is recognised at the point of shipment when the risks and rewards transfer.

### Other operating income

Other operating income represents the reimbursement of costs from other group companies, primarily relating to certain costs incurred in research and development activities. These amounts are recognised at a mark up when research and development costs are incurred.

### Research and development

Research and development expenditure incurred on behalf of the ultimate parent company in Switzerland is written off to the Profit and Loss Account in the year in which it is incurred unless the development project meets the recognition criteria specified in IAS 38 in which case these costs are capitalised. This expenditure is recovered from the ultimate parent company and recorded in other operating income.

## 1 Principal accounting policies (continued)

### Leases

Costs in respect of operating leases, that is where the risks and rewards of ownership remain with the lessor, are charged on a straight line basis over the term of the lease in arriving at the operating profit for the year.

### Tangible Assets

All property, plant and equipment are carried at cost less accumulated depreciation and impairment losses. Cost represents the original purchase price of the asset and any costs attributable to bringing the asset to its working condition for its intended use. No provision is made for depreciation on freehold land. Depreciation is calculated so as to write off the cost less estimated residual value of other assets on a straight line basis over the expected economic useful lives, commencing when the assets are first brought into use. The principal annual rates used for this purpose are:

| | |
|---|---|
| Buildings | 20 - 40 years |
| Plant, machinery and equipment | 3 - 15 years |
| Assets under construction | Not depreciated until brought into use |

The residual values and the remaining useful economic lives are reviewed on an annual basis.

Assets are tested for impairment wherever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the assets carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

### Stocks

Stocks and work in progress are valued at the lower of cost and net realisable value.

Cost includes expenditure which is incurred in the normal course of business in bringing the product or service to its present location and condition and a due proportion of overhead expenses. Net realisable value is the estimated selling price less all further costs to completion and estimated selling costs.

Provision is made for obsolescent, slow moving and defective stock.

## 1 Principal accounting policies (continued)

### Investments

Investments are stated at cost unless, in the opinion of the Directors, an impairment in the value of the investment has occurred. In these circumstances the investment is stated at its written down value and the related impairment is charged to the Profit and Loss Account. Directors perform an impairment review annually.

### Cash at bank and in hand

Cash at bank and in hand comprise deposits with banks. In the Balance Sheet, bank overdrafts are included in borrowings in current liabilities.

### Debtors

Debtors are recognised initially at fair value less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments (more than 180 days overdue) are considered indicators that the trade debtor is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the Profit and Loss Account within 'selling and marketing costs'.

When a debtor is uncollectible, it is written off against the allowance account for debtors. Subsequent recoveries of amounts previously written off are credited against 'selling and marketing costs' in the Profit and Loss Account.

### Employee benefit costs

The Company contributes to the group defined contribution and defined benefit pension schemes, which are operated by Novartis UK Limited.

The liability recognised in the Balance Sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the Balance Sheet date less the fair value of plan assets, together with adjustments for any actuarial gains or losses and unrecognised past service costs.

The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method.

## 1 Principal accounting policies (continued)

### Employee benefit costs (continued)

The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability.

The Company recognises, in accordance with IAS 19R, actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in full as they arise, outside of the Profit and Loss Account. They are presented in the Statement of Total Recognised Gains and Losses, with the exception of gains and losses arising from changes in the benefits regarding past services, which are recognised in the Profit and Loss Account.

Past service costs are recognised immediately in the Profit and Loss Account unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time. In this case, the past service costs are amortised on a straight line basis over the vesting period.

The interest and service costs associated with defined benefit schemes are recognised in the Profit and Loss Account.

The contributions to defined contribution plans are recognised as an expense as the costs are incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available. Amounts in respect of these plans are held in separately administered funds.

### Creditors

Creditors are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Creditors are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.

### Provisions for liabilities

Provisions are recognised when the Company has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably measured.

Post retirement medical benefits are paid to certain former employees and full provision is made in the financial statements.

## 1 Principal accounting policies (continued)

### Provisions for liabilities (continued)

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

### Current taxation

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

### Deferred taxation

Deferred tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, the deferred tax is not accounted for, if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred tax assets and liabilities relate to taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

### Share-based payments

In accordance with IFRS 2 the fair value of the equity-settled share-based payments to employees is determined at the date of grant and is expensed on a straight line basis over the vesting period based on the estimate of shares and options that will eventually vest. In the case of options granted, fair value is measured by use of the trinomial model. Further details are set out in note 17.

## 1 Principal accounting policies (continued)

### Share Capital

Ordinary shares are classified as equity.

### Dividends

Dividends are recorded in the financial statements once they have been authorised and the Company is committed to making the payment. Interim dividends are recorded when paid.

### Foreign currencies

Foreign currency transactions during the year are translated into sterling at the rates of exchange in force at the time they arise. Both the functional and presentational currency is sterling.

Monetary assets and liabilities denominated in foreign currencies are translated into sterling at rates of exchange ruling at the balance sheet date. Translation differences are taken to the Profit and Loss Account.

### Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred.

### Consolidation

These separate financial statements contain information about Novartis Pharmaceuticals UK Limited as an individual company and do not contain consolidated financial information as the parent of a group. The Company has taken advantage of the exemption under section 400, of the Companies Act 2006 from the requirement to prepare consolidated financial statements as it and its subsidiaries are included by full consolidation in the consolidated financial statements of its ultimate parent, Novartis AG.

### Exceptional item

When items of income or expense, either individually, or if similar, in aggregate are considered material due to their size or nature, they are separately disclosed and classified as exceptional items.

## 2 Critical accounting estimates and assumptions

The Company makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the actual related results. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying value of assets and liabilities are addressed below:

a) Pensions

The present value of the pension obligations depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost for pensions include the discount rate. Any changes in these assumptions will impact the carrying amount of pension obligations.

The Company determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of estimated future cash outflows expected to be required to settle the pension obligations. In determining the appropriate discount rate, the Company considers the interest rates of high quality (AA rated) bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating the terms of the related pension liability. Other key assumptions for pension obligations are based in part on current market conditions, additional information is disclosed in note 18.

b) Sales deduction provision

The company has entered into various pricing and rebate schemes which are accrued for on a consistent basis according to the terms of the agreements.

## 3 Turnover

The Directors consider that the operations of the Company fall into one business class, being the production and distribution of pharmaceutical products and turnover from Manufacturing for the Novartis Group.

The categories of turnover are as follows:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Sale of goods | 529,759 | 512,729 |
| Turnover from manufacturing services provided to Novartis Group | 20,953 | 31,568 |
| | 550,712 | 544,297 |

## 4 Operating Profit

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| The following items have been charged / (credited) in arriving at operating profit: | | |
| Employee benefit expenses (note 17) | 109,464 | 101,801 |
| Depreciation of property, plant and equipment (note 8) | 16,254 | 16,659 |
| Loss on disposal of property, plant and equipment | 969 | 562 |
| Other operating lease rentals payable | 2,375 | 2,244 |
| Repairs and maintenance expenditure on property, plant and equipment | 2,699 | 2,945 |
| Exchange differences | (13) | 75 |
| Exceptional items | | |
| - Impairment of property, plant and equipment (note 8) | 31,823 | - |
| - Restructuring costs (note 15) | 14,938 | - |
| Services provided by the Company's auditors | | |
| - fees payable for the audit | 111 | 103 |

## 5 Interest receivable and similar income and Interest payable and similar charges

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Interest payable and similar charges: | | |
| Interest payable on bank overdraft and loans | (28) | (151) |
| Interest payable on loans from group undertakings | (143) | (33) |
| | (171) | (184) |
| Interest receivable and similar income on cash on deposits: | 30 | 145 |
| | 30 | 145 |
| Net interest payable | (141) | (39) |

 

## 6 Tax on profit on ordinary activities

| Analysis of charge in the year | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Current tax - continuing operations | | |
| - UK corporation tax on (loss) / profit of the year | 6,089 | 701 |
| - Adjustment in respect of prior year | - | (62) |
| **Total Current Tax** | 6,089 | 639 |
| Deferred tax | | |
| Origination and reversal of timing differences (accelerated capital allowances and other) | (5,930) | (2,812) |
| Adjustment in respect of prior years | (706) | (1,833) |
| **Total Deferred Tax (note 14)** | (6,636) | (4,645) |
| **Total Tax Credit** | (547) | (4,006) |

| Tax on items credited /(charged) to equity | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Deferred tax on actuarial losses / (gains) (note 18) | 6,568 | (2,145) |

The (charge) for the year can be reconciled to the profit per the Profit and Loss Account as follows:

| | 2013 £'000 | Restated 2012 £'000 |
|---|---|---|
| (Loss) / profit on ordinary activities before taxation | (16,172) | 8,078 |
| Profit on ordinary activities multiplied by effective rate of corporation tax in the UK of 23.25% (2012: 24.5%) | (3,760) | 1,979 |
| Effects of: | | |
| Expenses not deductible for tax purposes | 7,625 | 236 |
| Effects of rate changes | (958) | (1,413) |
| Research and development tax credits | (2,748) | (3,490) |
| Adjustments in respect of prior years – deferred tax | (706) | (1,256) |
| Adjustments in respect of prior years – income tax | - | (62) |
| Tax credit/(charge) for the year | (547) | (4,006) |

## 6 Tax on profit on ordinary activities (continued)

**Factors that may affect future tax charge:**

Current tax assets for the current and prior years are measured at the amount expected to be paid to or recovered from the taxation authorities, using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. As such, current tax assets have been recognised at an effective rate of 23.25% (2012: 24.5%). The Finance Act 2013, which was substantively enacted in July 2013, included provisions to reduce the rate of corporation tax to 21% with effect from 1 April 2014 and to 20% with effect from 1 April 2015. Accordingly, deferred tax balances have been revalued to the lower rate of 20% in these financial statements.

## 7 Dividends

| | 2013<br>£'000 | 2012<br>£'000 |
|---|---|---|
| 185.2p per £1 share (2012: 370.4p) | 10,000 | 20,000 |
| Dividend paid | 10,000 | 20,000 |

## 8 Tangible Assets

| | Freehold land | Buildings | Plant, machinery and equipment | Assets under construction | Total |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Cost** | | | | | |
| At 1 January 2013 | 11,378 | 117,712 | 87,805 | 1,783 | 218,678 |
| Additions at cost | - | 11 | 2,074 | 3,302 | 5,387 |
| Transfers | - | - | 3,142 | (3,142) | - |
| Disposals | - | (4,396) | (26,129) | - | (30,525) |
| At 31 December 2013 | 11,378 | 113,327 | 66,892 | 1,943 | 193,540 |
| **Accumulated depreciation** | | | | | |
| At 1 January 2013 | - | (68,255) | (74,480) | - | (142,735) |
| Depreciation charge | - | (8,180) | (8,074) | - | (16,254) |
| Impairment charge | - | (24,192) | (7,631) | - | (31,823) |
| Disposals | - | 2,599 | 26,110 | - | 28,709 |
| At 31 December 2013 | - | (98,028) | (64,075) | - | (162,103) |
| **Net book value** | | | | | |
| 31 December 2013 | 11,378 | 15,299 | 2,817 | 1,943 | 31,437 |
| 31 December 2012 | 11,378 | 49,457 | 13,325 | 1,783 | 75,943 |

Included in tangible assets are the following:

(a) Capitalised interest at cost amounting to £523,000 (2012: £523,000).

(b) Assets with a cost of £55,988,000 (2012: £65,904,160) are fully depreciated but still in use.

## 9 Investments

The investment in subsidiary undertakings is made up as follows:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Investment at 1 January and 31 December | 28,100 | 28,100 |
| | 28,100 | 28,100 |

| | Percentage of Voting rights and Issued Share capital (ordinary shares) | Nature of Business |
|---|---|---|
| NeuTec Pharma Limited | 100% | Non-trading |

The Company acquired NeuTec Pharma Limited from Novartis Pharma AG on 18 November 2011 for £28,100,000. NeuTec Pharma Limited is a non-trading entity with total net assets of £28,411,000 (2012: £28,305,000) as at 31 December 2013.

The Directors believe that the carrying value of the investment is supported by its underlying assets.

## 10 Stocks

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Materials & consumables | 54 | 901 |
| Work in progress | - | 886 |
| Finished goods | 62,045 | 69,352 |
| | 62,099 | 71,139 |

The Company consumed £409,557,123 (2012: £408,302,434) of stocks during the year.

Included above are finished goods of £ Nil (2012: £ Nil) carried at net realisable value being lower than cost for which full provision has been made.
The Company has decreased the stock provision to £748,878 (2012: £2,096,550) to reflect changes in stock management, slow and obsolete stock.

## 11 Debtors

| Amounts falling due within one year: | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Trade debtors (financial assets) | 64,380 | 22,972 |
| Less: Provision for impairment of trade debtors | (95) | (129) |
| Net Trade Debtors | 64,285 | 22,843 |
| Amounts owed by fellow group undertakings (financial asset) | 18,841 | 33,461 |
| Other debtors (financial asset) | 1,668 | 1,829 |
| Prepayments and accrued income | 2,583 | 1,276 |
| Current Tax Asset | - | 2,976 |
| | 87,377 | 62,385 |

Concentrations of credit risk with respect to trade debtors are limited due to the Company's customer base being large and unrelated. Due to this, management believes there is no further credit risk provision required in excess of normal provision for doubtful debtors.

All debtors are stated at book value which approximate to fair value and are denominated in pounds.

 

## 12 Financial liabilities - borrowings

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| **Current** | | |
| Unsecured bank overdrafts due within one year or on demand | 44,852 | - |
| | 44,852 | - |
| **Non current** | | |
| Unsecured loans from group undertakings due after one year | - | 19,000 |
| **Total financial liabilities – borrowings** | 44,852 | 19,000 |

The Company is party to a composite cross guarantee arrangement in relation to the bank overdrafts, as referred to in note 20. Loans from group undertakings consist of non interest bearing loans with fellow subsidiaries of £19,000,000 (2012: £19,000,000) which are due on 31 December 2014, early repayments are possible on mutual agreement by both parties.

The carrying value of borrowings approximates to fair value as the impact of discounting is not significant.

The note above analyses the Company's financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

## 13 Creditors

| Amounts falling due within one year: | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Creditors (financial liability) | 21,299 | 19,053 |
| Amounts owed to fellow group undertakings (financial liability) | 27,821 | 59,283 |
| Other tax and social security payable | 10,717 | 11,009 |
| Other creditors (financial liability) | 1,054 | 8,298 |
| Accruals and other liabilities (financial liability) | 22,720 | 18,341 |
| | 83,611 | 115,984 |

Creditors are stated at book value which approximates to their fair value. No security has been given by the Company in respect of the payables detailed above. The Company has standard payment terms for trade suppliers of settlement of account by last day of the following month. These payment terms are on all purchase orders raised by the Company and there are no material creditors subject to different terms. The Company has no derivative financial liabilities.

The above creditors are due within one year based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

## 14 Deferred tax liabilities and assets

The following are the major deferred tax liabilities and assets recognised and movements thereon during the current and prior year. Deferred tax is calculated in full on temporary differences under the liability method using a tax rate of 20% (2012: 23%).

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. As such, deferred tax assets and liabilities have been recognised at the rate of 20% (2012: 23%).

| Movement on deferred taxation balance in the year | 2013<br>£'000 | 2012<br>£'000 |
|---|---|---|
| At 1 January | (2,496) | 4 |
| Profit and Loss Account | (6,636) | (4,645) |
| Retained earnings - retirement benefit obligations | (6,568) | 2,145 |
| At 31 December | (15,700) | (2,496) |

| | 2013<br>£'000 | 2012<br>£'000 |
|---|---|---|
| Capital allowance in excess of depreciation | 2,616 | 8,625 |
| Retirement benefit obligations | (12,031) | (5,509) |
| Share based payments | (6,285) | (5,572) |
| Other short term timing difference | - | (40) |
| Total deferred tax | (15,700) | (2,496) |

| | 2013<br>£'000 | 2012<br>£'000 |
|---|---|---|
| Deferred tax assets | (18,316) | (11,121) |
| Deferred tax liability | 2,616 | 8,625 |
| Net deferred tax asset | (15,700) | (2,496) |

All of the deferred tax assets were available for offset against deferred tax liabilities and hence the net deferred tax asset at 31 December 2013 was £15,700,000 (2012: £2,496,000 asset).

## 15 Provisions for liabilities

| | Post-Retirement Medical Benefit | Sales Deduction Provisions* | Restructuring Provisions** | Other | Total |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| At 1 January 2013 | 222 | 16,680 | 9,514 | 114 | 26,530 |
| Additional provisions | 97 | - | 14,938 | - | 15,035 |
| Utilised in the year | (8) | (1,316) | (3,836) | - | (5,160) |
| Released in the year | (58) | (1,600) | (1,788) | (101) | (3,547) |
| At 31 December 2013 | 253 | 13,764 | 18,828 | 13 | 32,858 |

**Analysis of total provisions for liabilities:**

| | 2013 | 2012 |
|---|---|---|
| Current | 32,592 | 9,514 |
| Non-current | 266 | 17,016 |
| | 32,858 | 26,530 |

*Sales Deduction Provisions
Further details are provided in Accounting Note 2b Critical accounting estimates and assumptions

**Restructuring Provisions
In 2013, the short-term provision of £18,828,000 (2012: £7,829,000) relates to a restructuring of our manufacturing site in Horsham and to the Primary Care marketing restructuring. The provision relates mainly to redundancies.

## 16 Called up share capital

| Authorised | 2013 £'000 | 2012 £'000 |
|---|---|---|
| 6,000,000 (2012: 6,000,000) ordinary shares of £1 each | 6,000 | 6,000 |
| | 6,000 | 6,000 |

| Issued and fully paid | Shares | 2013 £'000 | Shares | 2012 £'000 |
|---|---|---|---|---|
| Ordinary shares of £1 each | | | | |
| At 1 January | 5,400,000 | 5,400 | 5,400,000 | 5,400 |
| At 31 December | 5,400,000 | 5,400 | 5,400,000 | 5,400 |

## 17 Employees and Directors

| Employee benefit expenses during the year | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Wages and salaries, including restructuring costs | 90,993 | 81,283 |
| Share based payments | 1,655 | 2,594 |
| Social security costs | 8,890 | 9,416 |
| Other pension costs – defined contribution plans | 5,950 | 6,427 |
| Other pension costs – defined benefit plans | 1,976 | 2,081 |
| | 109,464 | 101,801 |

| Average monthly number of people (including executive directors) employed | 2013 no. | 2012 no. |
|---|---|---|
| Manufacturing | 115 | 189 |
| Research & development | 388 | 456 |
| Administration & marketing | 643 | 665 |
| | 1,146 | 1,310 |

| Directors | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Aggregate emoluments | 1,379 | 819 |
| Company contributions to money purchase pension schemes | - | 61 |
| | 1,379 | 880 |

## 17 Employees and directors (continued)

Mr H Kirsch, Mr G Guidi, Mr E Cornut, and Mr L Prat are remunerated by the ultimate parent company in Switzerland for their services in the Novartis Group and no recharge is made to the Company. Their remuneration is therefore not included in the above figures.

No Director (2012: none) who is remunerated in the UK exercised options and no Director (2012: none) received shares under a long term incentive scheme in 2013.

Aggregate emoluments for the highest paid Director were £981,000 (2012: £370,000; this Director started in the month of September in 2012 and therefore has had his emoluments pro-rated in this year). The accrued pension for the highest paid Director was £nil (2012: £30,000) per annum under the defined benefit scheme and £nil (2012: £ nil) accrued lump sum under the money purchase scheme at the end of the year. No share options (2012: none) were exercised by the highest paid Director. No shares were received by the highest paid Director in respect of qualifying services under a long-term incentive scheme during the year (2012: none).

No Director (2012: one) is accruing benefits under the ultimate parent company's defined benefit scheme, the costs of which are recharged to the Company. No Directors (2012: none) are accruing benefits under defined contribution schemes.

### Employee share participation plans

Employee and management share participation plans consist of both share option plans and share plans.

### Senior management share plans

Under the current plan, tradable share options and restricted stock are granted annually as part of remuneration of executives and other employees, as selected by senior management and reviewed and agreed by the Equity Schemes Board of Novartis International AG. Both the option and restricted stock grants have a three year vesting period. Options must be exercised within 10 years from grant date. Each option entitles the holder to acquire one Novartis AG share at the exercise price, being the market value of the shares on grant date.

The Novartis Share Incentive Plan ("SIP") is an HMRC approved plan open to all UK permanent employees. Eligible employees may contribute up to £125 each month and the trustee of the plan uses the money to buy shares on their behalf. For every two shares purchased the Company purchases another matching share at market price on grant date. The shares received under this plan have a three year vesting period. UK based Directors are eligible to participate in the SIP.

## 17 Employees and Directors (continued)

### General employee share plans

The Incentive Conversion Plan provides incentive for certain employees where 10% of the annual bonus can be converted to shares. Shares received under the plan have a three year vesting period and are matched with one share for every two shares purchased at market price on due date. In 2013 employees received 2,709 (2012: 4,538) shares under the scheme.

The market value of the shares held in trust at year end was £12,883,290 (2012: £10,112,290).

The following table shows the assumptions on which the valuation of share options granted under senior management share plans during the year was based on:

| | 2013 | 2012 |
|---|---|---|
| Valuation date | 17 January 2013 | 19 January 2012 |
| Expiration date | 17 January 2023 | 19 January 2022 |
| Closing share price on grant date | CHF 61.70 | CHF 54.20 |
| Exercise price | CHF 61.70 | CHF 54.20 |
| Volatility | 13.40% | 14.85% |
| Expected dividend yield | 4.64% | 4.82% |
| Interest rate | 0.94% | 0.94% |
| Market value of option at grant date | CHF 4.28 | CHF 4.30 |

 

## 17 Employees and directors (continued)

All options were granted at an exercise price which was equal to or greater than the market price of the Group's shares at the grant date.

The expenses recorded in the 2013 Profit and Loss Account related to the general employee share plans amounted to £1,655,000 (2012: £2,594,000).

The weighted average exercise price for options that were sold or exercised in the year was CHF 0.

The following table summarises information about the share options outstanding at 31 December 2013:

| | Options outstanding | | | Options exercisable | |
|---|---|---|---|---|---|
| Range of exercise prices CHF | Number outstanding | Weighted average remaining contractual life | Weighted average exercise price | Number exercisable | Weighted average exercise price |
| 50 – 59 | 540,588 | 5.78 | 55.03 | 254,642 | 38.36 |
| 60 – 69 | 180,125 | 6.28 | 62.98 | 98,087 | 64.05 |
| 70 – 79 | 172,207 | 3.73 | 72.31 | 172,207 | 72.31 |
| Total | 892,920 | 5.49 | 59.97 | 524,936 | 42.33 |

The weighted average exercise prices and the fair value of options granted are quoted in Swiss Francs (CHF), the currency of issue of such options in the ultimate parent company.

## 18 Retirement benefit obligations

The Company participates in the defined benefit and defined contribution pension schemes for the UK employees of the wider Novartis Group, with assets held in a separately administered fund. The defined benefit costs and contributions attributable to the Company are calculated on a pro-rata basis on employee numbers. Towers Watson are the advising actuaries for the Company scheme. All actuarial gains and losses are recognised through the Statement of Total Recognised Gains and Losses, with the exception of gains and losses arising from changes in the benefits regarding past services, which are recognised in the Profit and Loss Account.

The scheme is closed with no member contributions nor company service cost contributions in 2013 (2012: nil).

Pension costs for defined contribution schemes are as follows:

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Defined contribution schemes | 5,950 | 6,427 |

### Defined benefit plans

In calculating the liabilities of the defined benefit scheme, the following financial assumptions have been used:

| | 2013 % pa | 2012 % pa |
|---|---|---|
| Discount rate | 4.5% | 4.75 |
| Salary growth | n/a[2] | n/a[2] |
| RPI | 3.40 | 3.10 |
| Pension-in payment increases | 3.40 | 3.10 |
| Post retirement mortality assumption | S1NMA/ S1NFA[1] | S1NMA/ S1NFA[1] |
| Current life expectancy for a 65-year-old male/female | 22.8/25.1 | 23.2/25.4 |

[1] These are updated versions of the PA92 standard mortality tables to allow for more recent mortality experience. The standard table has been projected forward in line with the medium cohort projection from 2000 onwards based on each members' year of birth.

[2] Following the closure of the scheme, pension payments are linked to RPI rather than salary growth and hence this measure is no longer applicable.

 

## 18 Retirement benefit obligations (continued)

The expected return on plan assets is a blended average of projected long term returns for the various asset classes. Asset classes are based on the forward looking building block approach. Equity returns are developed based on the selection of an equity risk premium above the risk free rate which is measured in accordance with the yield on government bonds. Bond returns are selected by reference to the yields on government and corporate debt as appropriate to the plan's holdings of these instruments. Other assets comprise investments in property and expected returns reflect long-term real rates of return experienced in the respective markets.

Under the current pension scheme rules, retiring employees are allowed to take up to a maximum of 25% of the value of their pension fund as a lump sum. The scheme valuation has assumed a 19% (2012: 15%) conversion rate since it is not expected that all employees will take the maximum cash lump sum.

Changes in the actuarial assumptions can result in significant volatility in the accounting for the Company's pension obligations. This can result in substantial changes in the Company's other comprehensive income and long-term liabilities and pension costs.

The defined benefit obligation (DBO) is significantly impacted by assumptions regarding the rate that is used to discount projected benefit payments. This rate is based on yields of high quality corporate bonds. A decrease in corporate bond yields will lead to lower discount rates which in turn will result in a higher DBO and a lower funded status.

The impact of decreasing interest rates on scheme assets is more difficult to predict. A significant portion of scheme assets is invested in bonds. Bond values usually rise when interest rates decrease and may, therefore, partially compensate for the decrease in funded status. Furthermore, the scheme assets also include significant holdings of equity instruments. Share prices tend to rise when interest rates decrease and, therefore, often counteract the negative impact of the rising DBO on the funded status although correlation of interest rates with equities is not as strong as with bonds, especially in the short term.

The expected rate for pension increases, which in turn depends on the expected rate of future inflation, significantly affects the DBO. Higher expected pension increases decrease the funded status. A proportion of the scheme assets are hedged against changes in the expected rate of future inflation. For the remaining assets, in the short-term, there is no strong correlation between the value of the scheme assets and pension/inflation increases.

Assumptions regarding life expectancy significantly impact the DBO with an increase in expected longevity increasing the DBO. There is no offsetting impact from the plan assets as no longevity bonds or swaps are held by the pension scheme. The assumptions allow for anticipated future improvements in longevity.

## 18 Retirement benefit obligations (continued)

The following table shows the sensitivity of the Company's DBO to the main actuarial assumptions for its participation in the Novartis UK Pension Scheme (on an aggregated basis):

| | Change in 2013 year end defined benefit obligation £m |
|---|---|
| 25 basis point increase in discount rate | (22.7) |
| 25 basis point decrease in discount rate | 24 |
| 1 year increase in life expectancy | 13.4 |
| 25 basis point increase in rate of pension increase | 18.3 |
| 25 basis point decrease in rate of pension increase | (17.6) |
| 25 basis point increase of interest on savings account | - |
| 25 basis point decrease of interest on savings account | - |

**The major categories of assets as a percentage of total plan assets are as follows:**

| Asset category | | 2013 | | 2012 |
|---|---|---|---|---|
| | £'000 | | £'000 | |
| Equities and hedge funds | 130,576 | 33.6% | 136,880 | 47.2% |
| Bonds | 187,703 | 48.3% | 105,848 | 36.5% |
| Other | 70,340 | 18.1% | 47,270 | 16.3% |
| Total | 388,619 | 100.0% | 289,998 | 100.0% |

**The amounts recognised in the Balance Sheet are determined as follows:**

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Fair value of plan assets | 388,619 | 289,998 |
| Present value of defined benefit obligation | (448,773) | (313,894) |
| Deficit in the Balance Sheet | (60,154) | (23,896) |

The Directors have recognised the pension deficit as at the year end of £60,154,000 (2012: £23,896,000 deficit).

## 18 Retirement benefit obligations (continued)

**The amounts recognised in the Profit and Loss Account are as follows:**

| | 2013<br>£'000 | 2012<br>(restated)<br>£'000 |
|---|---|---|
| Administrative cost | 970 | 642 |
| Interest cost | 14,912 | 14,375 |
| Interest income on plan assets | (13,906) | (12,936) |
| Total included within employee benefit expenses (note 17) | 1,976 | 2,081 |

**Change in the defined benefit obligation:**

| | 2013<br>£'000 | 2012<br>(restated)<br>£'000 |
|---|---|---|
| Present value of defined benefit obligation at start of year | 313,894 | 287,466 |
| Administrative cost | 970 | 642 |
| Interest paid | 14,912 | 14,375 |
| Actuarial loss | 50,994 | 12,053 |
| Reallocation of the defined benefit and fair value plan assets | 80,292 | - |
| Benefit payments including administrative costs | (12,289) | (642) |
| Present value of defined benefit obligation at end of year | 448,773 | 313,894 |

**Change in plan assets:**

| | 2013<br>£'000 | 2012<br>(restated)<br>£'000 |
|---|---|---|
| Fair value of plan assets at start of year | 289,998 | 254,596 |
| Interest income on plan assets | 13,906 | 12,936 |
| Actuarial gain on plan assets | 6,066 | 17,402 |
| Reallocation of the defined benefit and fair value plan assets | 84,997 | - |
| Employer contributions | 5,941 | 5,706 |
| Benefit payments including administrative cost | (12,289) | (642) |
| Fair value of plan assets at end of year | 388,619 | 289,998 |

## 18 Retirement benefit obligations (continued)

**Amount recognised in the Statement of Total Recognised Gains and Losses:**

| | 2013 £'000 | 2012 (restated) £'000 |
|---|---|---|
| Actuarial (loss) on defined benefit obligation | (50,994) | (12,053) |
| Actuarial gain on plan assets | 6,066 | 17,402 |
| Actuarial gain on reallocation of the defined benefit and fair value plan assets | 4,705 | - |
| Actuarial (loss) / gain | (40,223) | 5,349 |
| Deferred tax on actuarial (loss) / gain | 6,568 | (2,145) |
| Net actuarial (loss) / gain recognised in the in the Statement of Total Recognised Gains and Losses | (33,655) | 3,204 |

**The history of experience losses / (gains):**

| | 2013 | 2012 (restated) | 2011 | 2010 | 2009 |
|---|---|---|---|---|---|
| Experience losses / (gains) on plan assets (£'000) | (6,066) | 17,402 | 19,498 | (14,351) | 26,578 |
| Percentage of plan assets | 1.56% | 6.00% | 7.66% | 5.88% | 9.89% |
| Experience losses / (gains) on plan liabilities (£'000) | 50,994 | 12,053 | 20,985 | (17,183) | 62,861 |
| Percentage of plan obligation | 11.36% | 3.84% | 7.3% | 6.97% | 20.82% |
| Fair value of plan assets (£'000) | 388,619 | 289,998 | 254,596 | 244,091 | 268,794 |
| Present value of plan obligation (£'000) | 448,773 | 313,894 | 287,466 | 246,463 | 301,912 |
| (Deficit) / Surplus (£'000) | (60,154) | (23,896) | (32,870) | (2,372) | (33,118) |

The liabilities of the scheme are gradually settled over time until all members have left. As per the wind-up rule, any remaining assets must be distributed to the companies in the scheme.

The company expects to contribute £6,937,000 to the Group pension scheme in 2013 (2012 actual: £ 5,941,000).

 

## 19 Operating lease commitments – minimum lease payments

| Commitments under non-cancellable operating leases expiring | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Vehicles and Other assets | | |
| - within one year | 1,800 | 2,289 |
| - two to five years | 1,895 | 3,429 |
| | 3,695 | 5,718 |
| Buildings & Land | | |
| - within one year | 582 | 880 |
| - two to five years | 1,164 | 3,520 |
| | 1,746 | 4,400 |

## 20 Contingent liabilities

The Company is party to a composite cross-undertaking to its principal banker (HSBC plc) to secure the liabilities to the bank of its fellow UK group companies. The contingent liability is limited to the net cash position of the Company's own bank account, to the extent that it is required to cover the total liabilities of the group companies who are party to the cross guarantee.

At 31 December 2013, the Company was in a net overdraft position having taken cleared funds into account and therefore no contingent liability existed (2012: £244,000 net cash position). The maximum potential liability for the total UK group is limited to the overdraft position of the UK companies bank accounts, calculated on cleared funds. As at 31 December 2013 the overdraft position of the UK companies was £1,187,000 (2012: £655,000).

The total facility for the total UK group is a £6m overdraft facility (2012: £6m).

## 21 Capital and other financial commitments

| | 2013 £'000 | 2012 £'000 |
|---|---|---|
| Contracts placed for future capital expenditure not provided in the financial statements) | 945 | 1,202 |

The contracts placed above are in relation to tangible assets.

## 22 Ultimate parent company and controlling party

Novartis AG, a company incorporated in Switzerland, is the Company's ultimate parent undertaking and controlling party. Copies of the group financial statements can be obtained from Novartis AG, Building S-210, CH-4002, Basel, Switzerland.

Novartis AG is the parent undertaking of the largest and smallest group of which Novartis Pharmaceuticals UK Limited is a member and for which group financial statements are drawn up.

Novartis UK Limited, incorporated in Great Britain, is the parent undertaking of the smallest group of which Novartis Pharmaceuticals UK Limited is a member.

## 23 Reconciliation of profit and retained earnings as a result of IAS19R restatement for 2012

Impact of restatement on the Profit and Loss Account:

| | 2012<br>£'000 |
|---|---|
| Profit under IAS 19 pension accounting per 2012 statutory reporting | 14,438 |
| Adjusted for: | |
| Administration costs | (642) |
| Interest income on pension assets calculated at discount rate | (1,712) |
| Restated profit | 12,084 |

Impact of restatement on Statement of Total Recognised Gains and Losses:

| | 2012<br>£'000 |
|---|---|
| Actuarial gain on retirement benefit scheme per 2012 statutory reporting | 2,995 |
| Adjusted for IAS 19R actuarial gain on plan assets | 2,354 |
| Restated actuarial gain on retirement benefit scheme before deferred tax | 5,349 |

There was no impact on the opening Balance Sheet at 1 January 2013.