Company Registration No. 2907641

Chancel House Limited

Report and Financial Statements

31 December 2009

Chancel House Limited

Report and Financial Statements 2009

Contents

Contents	Page
Directors' Report	1
Statement of Directors' Responsibilities	3
Independent Auditors' Report	4
Profit and Loss Account	6
Statement of Total Recognised Gains and Losses	7
Balance Sheet	8
Notes to the Accounts	9

Chancel House Limited

Directors' Report

The Directors present their annual report and the audited financial statements for the year ended 31 December 2009

This Directors Report has been prepared in accordance with the special provisions relating to small companies under section 415a of the Companies Act 2006

Principal activities

The principal activity of the Company is to invest in commercial property

Review of the business

The results for the year are shown on page 6 The Directors expect the principal activity of the Company to remain unchanged for the foreseeable future

The financial statements have been prepared on a going concern basis as described in note 1 2

Dividends

The Directors do not propose any dividends for the year ended 31 December 2009 (2008 - £nil)

Financial risk management

The Company's operations expose it to the risk of interest rate fluctuations The Company addresses such risks by purchasing interest rate hedging instruments Such instruments have a year end book value of £nil (2008 £nil) and a year end market value of £12,487,500 (2008 £1,818,173)

Principal risks and uncertainties

The Company considers there are a number of potential risks and uncertainties which could have a material impact on the Company's performance and could cause the actual results to differ materially from expected and historical results Management and mitigation of these risks is the responsibility of the Directors of the Company

Risk	**Mitigation**
Cyclical downturn in property market	Long-term investment strategy to mitigate short-term unrealised losses
Covenant breaches in downturn	Historically supported by ultimate parent company, ability to re-negotiate terms with lender
Changes in tenant demand	Strategy of securing long-leased tenants with strong covenants
Ability to access finance	Parent debt service cover guarantees given to secure funding
Credit risk – tenants	All potential tenants assessed for credit worthiness Rental depo required
Credit risk – lenders	Large institution with good credit rating used

Chancel House Limited

Directors' Report

Directors

The Directors, who served throughout the year except as noted, were as follows

Mr E H Klotz
Mr T J L Wills
Mr A G P Millet
Mr J H Whiteley (appointed 22 January 2010)

Qualifying third-party indemnity provisions (as defined in section 234 of the companies Act 2006) are in force for the benefit of the Directors and former Directors who held office in 2009

Auditors

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

- so far as he is aware, there is no relevant audit information of which the Company s auditors are unaware, and
- 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

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006

Pursuant to s386 Companies Act 1985, an Elective Resolution was passed on 9 October 2002 dispensing with the requirement to appoint auditors annually In accordance with that Elective Resolution and paragraph 45(2), Schedule 3 of the Companies Act 2006 (Commencement No 3 Consequential Amendments, Transitional Provisions and Savings) Order 2007, Deloitte LLP is deemed to continue as auditor of the Company

Approved by the Board of Directors
and signed by order of the Board

Mr D F Fuller
Company Secretary

6 May 2010

Registered office:
86 Bondway
London
SW8 1SF

Chancel House Limited

Statement of Directors' Responsibilities

The Directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations

Company law requires the Directors to prepare financial statements for each financial year Under that law the Directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law) 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 estimates that are reasonable and prudent, 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 with reasonable accuracy at any time the financial position of the Company, and to 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

Independent Auditors' Report to the Members of Chancel House Limited

We have audited the financial statements of Chancel House Limited for the year ended 31 December 2009 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet and the related notes 1 to 15 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)

This report is made solely to the Company s members, as a body, in accordance with chapter 3, part 16 of the Companies Act 2006 Our audit work has been undertaken so that we might state to the Company s members those matters we are required to state to them in an auditors report and for no other purpose To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company s members as a body, for our audit work, for this report, or for the opinions we have formed

Respective responsibilities of directors and auditors

As more fully explained in the Statement of Directors Responsibilities, 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 the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practice Board s (APB s) Ethical Standards for Auditors

Scope of the audit of financial statements

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

Opinion

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2009 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

Opinion on matters prescribed in the Companies Act 2006

- In our opinion the information in the Directors Report for the financial year for which the financial statements are prepared is consistent with the financial statements

Independent Auditors' Report to the Members of Chancel House Limited (continued)

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- 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, or
- certain disclosures of Directors remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit, or
- the Directors were not entitled to take advantage of the small companies exemption in preparing the Directors report

Mark Goodey

Mark Goodey (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom
6 May 2010

Chancel House Limited

Profit and Loss Account
Year ended 31 December 2009

	Notes	2009 £	2008 £
Turnover	2	1,599,420	1,298,941
Service charge expenditure		(691,129)	(535,744)
		908,291	763,197
Administrative expenses		(147,711)	(236,095)
Operating profit		760,580	527,102
Interest receivable and similar income		1,033	1,213
Interest payable and similar charges	3	(846,758)	(692,224)
Loss on ordinary activities before taxation	5	(85,145)	(163,909)
Tax charge on loss on ordinary activities	6	(33,592)	(123,894)
Loss for the financial year	14	(118,737)	(287,803)

There is no material difference between the loss on ordinary activities before taxation and the loss for the year stated above, and their historical cost equivalents

All items included in the Profit and Loss Account are part of continuing operations

Chancel House Limited

Statement of Total Recognised Gains and Losses
Year ended 31 December 2009

	Notes	2009 £	2008 £
Loss for the financial year		(118,737)	(287,803)
Unrealised surplus/(deficit) on revaluation of property	7	500,000	(2,000,000)
Total recognised gains/(losses) for the year		381,263	(2,287,803)

Chancel House Limited

Balance Sheet
31 December 2009

	Notes	2009 £	2008 £
Fixed assets			
Freehold investment properties	7	10,000,000	9,500,000
Current assets			
Debtors due within one year	8	400,721	500,289
Debtors due after one year	9	37,981	-
Total debtors		438,702	500,289
Cash at bank and in hand		16	37,079
		438,718	537,368
Creditors. amounts falling due within one year	10	(2,071,278)	(2,157,134)
Net current liabilities		(1,632,560)	(1,619,766)
Total assets less current liabilities		8,367,440	7,880,234
Creditors· amounts falling due after more than one year	11	(7,490,573)	(8,311,415)
Provisions for liabilities	12	(607,561)	(580,776)
Net assets/(liabilities)		269,306	(1,011,957)
Capital and reserves			
Called up share capital	13	300,900	300,000
Share premium	14	899,100	-
Revaluation reserve	14	195,793	(304,207)
Profit and loss account	14	(1,126,487)	(1,007,750)
Shareholder funds/(deficit)		269,306	(1,011,957)

The financial statements of Chancel House Limited (registered number 2907641) were approved by the Board of Directors on 6 May 2010

Signed on behalf of the Board of Directors

Mr J H Whiteley
Director

Notes to the Financial Statements
31 December 2009

1. Accounting policies

The financial statements are prepared in accordance with applicable United Kingdom accounting standards The particular accounting policies adopted are described below

1.1 Basis of preparation

The financial statements are prepared under the historical cost convention, modified to include the revaluation of land and buildings and in accordance with applicable United Kingdom accounting standards and on the going concern basis The Directors consider that the Company is a going concern The Company has taken advantage of the exemption in Financial Reporting Standard No 1 not to prepare a cash flow statement as a cash flow statement has been prepared for the Group The Company is a wholly-owned subsidiary of CLS Holdings plc and has taken advantage of the exemption in Financial Reporting Standard No 8 not to detail transactions with fellow Group undertakings The Company has taken advantage of the exemption in Financial Reporting Standard No 29 as equivalent disclosure is made in the Group accounts of CLS Holdings plc which are publicly available

1.2 Going concern

The Company s business activities and review of the business are set out in the Directors Report

The Company is funded by a combination of external and internal interest bearing debt The Directors have reviewed the current and projected financial position of the Company making reasonable assumptions about future rental income and property values The Company is subject to the current economic uncertainties and if property values were to deteriorate significantly further over the foreseeable future then there are scenarios in which the financial covenants within its external facilities could fail to be met The Directors have identified that in advance of covenant breaches they would discuss potential breaches with lenders which they believe would lead to renegotiation and possible waiving of the covenant, particularly in cases where all other covenants, including external debt service, are complied with Furthermore the immediate parent company has guaranteed to provide support should the Company need to rectify loan to value covenant breaches for the foreseeable future The guarantee is limited to a maximum amount of £231,000 In light of the equity deficit of the Company at 31 December 2008, the Directors sought equity funding to strengthen the Balance Sheet The Company was recapitalised by £900,000 on 14 July 2009 by its immediate parent company to restore the net assets position of the Company (note 13) This had the impact of greatly reducing the intercompany interest burden going forward and therefore increased the profitability of the Company For these reasons, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future Accordingly, the Directors continue to adopt the going concern basis in preparing the annual report and financial statements

Chancel House Limited

Notes to the Financial Statements
31 December 2009

1 Accounting policies (continued)

1.3 Investment properties

Investment properties are revalued annually Completed investment properties are stated at their open market value Investment properties in the course of development are stated at open market value in their existing state Surpluses or deficits arising on revaluation are reflected in the revaluation reserve Revaluation deficits in excess of the amount of prior revaluation surpluses are charged to the Profit and Loss Account, unless considered temporary

In accordance with Statement of Standard Accounting Practice 19 no depreciation is provided on completed freehold investment properties The requirement of the Companies Act 2006 is to depreciate all properties, but that requirement conflicts with the generally accepted accounting principle set out in SSAP 19 The Directors consider that, as these properties are not held for consumption but for investment, to depreciate them would not give a true and fair view and that it is necessary to adopt SSAP 19 in order to give a true and fair view Depreciation or amortisation is one of the many factors influencing a property valuation and if depreciation or amortisation might have been charged, it is not possible to identify or quantify this separately

1.4 Turnover

Turnover comprises the total value of investment income and rents receivable under operating leases, including reverse premiums paid by tenants on surrender of leases and property-related services provided during the year, excluding VAT and intra-group trading Where there is a material rent free period and the amount is considered to be recoverable, the income is spread evenly over the period to the date of the first break Rents received in advance are shown as deferred income in the Balance Sheet

1 5 Taxation

Corporation tax is provided on taxable profits at the current rate

Deferred tax is recognised in respect of all timing differences which have originated but not reversed at the balance sheet date where transactions or events which result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date Timing differences are differences between the Company s taxable profits and its results as stated in the financial statements

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the reversal of the underlying timing differences can be deducted

Deferred tax is measured, on an undiscounted basis, at the average tax rates which are expected to apply in the periods in which the timing differences are expected to reverse based on tax rates and laws which have been enacted or substantively enacted at the balance sheet date

Provision is not made in respect of property revaluation gains and losses

1.6 Issue costs of loans

Issue costs relating to new loans are capitalised and amortised to follow the profile of the loan principal Unamortised amounts at the balance sheet date are deferred against the loan liability

Notes to the Financial Statements
31 December 2009

2 Turnover

	2009	2008
	£	£
Rental income	947,635	713,414
Other income	7,635	33,436
Service charge expenditure recovered	644,150	552,091
	1,599,420	1,298,941

Turnover arose wholly within the United Kingdom

3. Interest payable and similar charges

	2009	2008
	£	£
On bank loan	423,100	628,916
Amortisation of arrangement fees	4,373	10,844
On loans from group undertaking	46,285	52,464
Swap break costs	373,000	-
	846,758	692,224

It was the Directors expectations that short-term interest rates would remain at a low level for longer than the interest rate curve was pricing Therefore on 8 July 2009, the Company unwound half of the £8,325,000 interest rate swap at a cost of £373,000 As a result, £4,162,500 of the loan is hedged at a fixed rate of 5 45% + 1 00% margin and the remaining amount of the loan bears interest at UK base rate + 1 00% margin

4. Directors' emoluments and employee information

None of the Directors received any remuneration during the year in respect of services as Directors to the Company (2008 £nil) The Company had one employee during the year (2008 one)

	2009	2008
	£	£
Wages and salaries	24,388	21,958
Pension costs	1,549	1,003
Social security costs	3,580	2,635
	29,517	25,596

Notes to the Financial Statements
31 December 2009

5. Loss on ordinary activities before taxation

	2009 £	2008 £
This is stated after charging		
Fees payable to the Company s auditors for the audit of the Company s financial statements	3,000	4,000

6 Tax charge on loss on ordinary activities

	2009 £	2008 £
Payments made for losses claimed as group relief in respect of previous periods	6,807	-
Total current tax charge	6,807	-
Deferred tax charge origination and reversal of timing differences	26,785	123,894
Total tax charge on loss on ordinary activities	33,592	123,894

Notes to the Financial Statements
31 December 2009

6. Tax charge on loss on ordinary activities (continued)

The differences between the total current tax shown above and the amount calculated by applying the standard rate of UK corporation tax to the loss on ordinary activities before tax is as follows

	2009 £	2008 £
Loss on ordinary activities before tax	(85,145)	(163,909)
Loss on ordinary activities before taxation multiplied by the standard rate of UK corporation of 28 0% (2008 28 5%)	(23,841)	(46,714)
Effect of		
Differences due to non-deductible expenses and items not included in loss for tax purposes	-	20,676
Losses surrendered by group/consortium relief for nil payment and differences between capital allowances and depreciation	23,841	26,038
Payment for group relief claimed in respect of previous periods	6,807	-
Current tax charge	6,807	-

7. Investment properties

	Freehold investment properties 2009 £
Valuation at 1 January 2009	9,500,000
Surplus on revaluation	500,000
Valuation at 31 December 2009	10,000,000

The investment properties were revalued at 31 December 2009 to their fair value The valuations were based on current prices in an active market The property valuations were carried out by Lambert Smith Hampton who are external, professionally qualified valuers (2008 Allsop & Co)

The Directors are satisfied that the external valuations supplied are appropriate to adopt for these financial statements without adjustment

The historical cost of investment properties included at valuation is £9,804,207 (2008 £9,804,207)

Chancel House Limited

Notes to the Financial Statements
31 December 2009

8. Debtors: due within one year

	2009 £	2008 £
Trade debtors	43,756	269,897
Other debtors	-	42,597
Amounts due from group undertakings	190,848	-
Prepayments and accrued income	166,117	187,795
	400,721	500,289

9 Debtors. due after one year

	2009 £	2008 £
Other debtors	37,981	-

10. Creditors: amounts falling due within one year

	2009 £	2008 £
Trade creditors	3,089	-
Unamortised arrangement fees	(3,331)	(3,547)
Amounts due to group undertakings	1,745,285	1,642,623
Other taxation and social security	39,205	58,930
Accruals and deferred income	287,030	459,128
	2,071,278	2,157,134

Notes to the Financial Statements
31 December 2009

11. Creditors: amounts falling after more than within one year

	2009 £	2008 £
Bank loan	7,500,000	8,325,000
Unamortised refinancing/arrangement fees	(9,427)	(13,585)
	7,490,573	8,311,415

The bank loan is repayable as follows

	2009 £	2008 £
In one year or less, or on demand	(3,331)	(3,547)
In more than one year but not more than two years	(3,331)	-
In more than two years but not more than five years	7,493,904	-
More than five years	-	8,325,000
	7,487,242	8,321,453

Interest on the loan is charged at LIBOR plus a margin of 1 00% and is secured by a legal charge over the property

The capitalised arrangement fees for the year were £nil (2008 £nil)

Following negotiation with the Company s external lender an amount of £825,000 was repaid on 15 July 2009

The ultimate parent company CLS Holdings Plc has given a guarantee to the loan provider which guarantees the shortfall between the interest payments due under the facility and the net rental income from the property The maximum total liability under the guarantee is £231,000

Chancel House Limited

Notes to the Financial Statements
31 December 2009

12. Provisions for liabilities

Deferred taxation is provided as follows

	Provision 2009 £	Amount unprovided 2009 £	Provision 2008 £	Amount unprovided 2008 £
Capital allowances in excess of depreciation	607,561	-	580,776	-
	607,561	-	580,776	-
At 1 January	580,776		456,882	-
Amount charged to profit and loss	26,785		123,894	
At 31 December	607,561		580,776	

No deferred tax liability arises on the revaluation gain due to the benefit of indexation

13 Called up share capital

	2009 £	2008 £
Authorised		
Ordinary shares of £1 each	300,900	300,000
Allotted, called up and fully paid		
Ordinary shares of £1 each	300,900	300,000

On 14 July 2009 the Company issued 900 ordinary shares of £1 each at a premium of £999 per share, which were fully subscribed for and paid up by the immediate parent undertaking

14 Combined statement of reserves and reconciliation of movement in shareholders' deficit

	Share capital £	Share premium £	Revaluation reserve £	Profit and loss account £	2009 Total £	2008 Total £
At 1 January	300,000	-	(304,207)	(1,007,750)	(1,011,957)	1,275,846
New shares issued	900	899,100	-	-	900,000	
Loss for the year	-	-	-	(118,737)	(118,737)	(287,803)
Surplus on revaluation	-	-	500,000	-	500,000	(2,000,000)
Balance at 31 December	300,900	899,100	195,793	(1,126,487)	269,306	(1,011,957)

Notes to the Financial Statements
31 December 2009

15. Parent undertaking

The Directors consider that the immediate and ultimate parent undertaking and controlling party is CLS Holdings plc which is incorporated in Great Britain Copies of the parent's group financial statements may be obtained from The Secretary, CLS Holdings plc, 86 Bondway, London SW8 1SF