Paperchase Products Limited

Report and Financial Statements

2 February 2008

Registered No 3185938

Directors
David Bateman
Timothy Melgund
George Mrkonic
Robert Warden
Sharon Horth

Secretary
David Bateman

Auditors
Ernst & Young LLP
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Bankers
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12 Alfred Place
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Directors' report

The dırectors present theır report and financıal statements for the penod to 2 February 2008

Results and dividends

The profit for the penod amounted to £9,000,000 (2007 £4,306,000) The dırectors do not recommend the payment of any dıvıdends

Principal activities and review of the business

Prıncıpal Actıvıty

The company's prıncıpal actıvıty durıng the penod was the retaıl sale of gıfts, statıonery, greetıng cards and art materıals

Key Performance Indıcators

The Company's key financıal performance ındıcators durıng the year were as follows

	2008 *£'000*	*2007* *£'000*	*% Change*
Company turnover	57,334	47,112	+22%
Internatıonal Income	3,453	2,671	+29%
EBITDA	10,057	7,871	+28%
Profit before tax	8,144	6,278	+30%
Gross profit margın	24%	24%	+0%

Developments ın the perıod

Paperchase contınued ıts UK expansıon by openıng 10 standalone shops and further concessıons ın House of Fraser Lıke for lıke sales ıncreases were achıeved across the portfolıo

Concessıons were also opened ın Borders Dubaı and Sıngapore stores

Other operatıng ıncome represents monıes earned from the sale of product to Borders Inc for onward sale ın ıts US stores In that geography over 300 stores now have Paperchase concessıons whıch have replaced the old gıfts and statıonery departments One standalone store was opened ın the US

Paperchase Products Lımıted does not rely on ıts Parent Company for fundıng Bank of Scotland provıde a Term Loan and workıng capıtal facılıty

Future developments

The dırectors aım to maıntaın the strategıc dırectıon whıch has resulted ın the company's recent growth ın profitabılıty They consıder that 2008 wıll show further growth both domestıcally and ın the Unıted States

Principal Risks and Uncertainties

The nsk exposure of the company ıs monıtored by the board The company has establıshed nsk and financıal management procedures to ıdentıfy and, where possıble, mıtıgate the nsks to the busıness

The prıncıpal nsks and uncertaıntıes are broadly grouped as follows

Commercıal Rısks

The company ıs exposed to general fluctuatıons ın the consumer retaıl envıronment The product offer ıncludes a range of demand elastıcıtıes wıth respect to these fluctuatıons Any nsk to a sales downturn would be managed to mınımıse profit loss

Directors' report

Currency Risks

The expansion of the Company's operations internationally increases foreign currency exposure The Company aims to manage its assets and liabilities denominated in foreign currency to minimize foreign exchange risk and to ensure sufficient availability of working capital

Creditor Payment Policy

It is the Company's policy to pay creditors when they fall due for payment Terms of payment are agreed with suppliers when negotiating each transaction and the policy is to abide by those terms, provided that the suppliers also comply with all relevant terms and conditions

Disabled employees

The company gives full consideration to applications for employment from disabled persons where the candidate's particular aptitudes and abilities are consistent with adequately meeting the requirements of the job Opportunities are available to disabled employees for training, career development and promotion

When existing employees become disabled, it is the companies policy to provide continuing employment wherever practible in the same or an alternative position and to provide alternative training to achieve this aim

Employee involvement

Paperchase seeks to provide employees systematically with information on matters of concern to them and consults on a regular basis so their views can be taken into account Head office and store management bonuses and incentive schemes are performance related and there is regular communication to encourage awareness of the financial and economic factors affecting the performance of the company

Directors

The directors serving during the period were as follows

David Bateman
Timothy Melgund
George Mrkonic (Chairman)
Robert Warden
Sharon Horth
Rick Vanzura (Resigned 5th September 2007)

Donations

During the period, the company made charitable contributions totalling £252,049 (2007 £203,469) in connection with sale of charity greetings cards

Directors' report

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Directors' report

Directors' statement as to disclosure of information to auditors

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware Having made enquiries of fellow directors and the company's auditor, each director has taken all the steps that he/she is obliged to take as a director in order to made himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information

Re-appointment of auditors

In accordance with s 385 of the Companies Act 1985, a resolution is to be proposed at the Annual General Meeting for reappointment of Ernst & Young LLP as auditor of the Company

By order of the board

Secretary

Date 1ST JULY 2008

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) The financial statements are required by law to 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 judgments and estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements,
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

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

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

Independent auditors' report

We have audited the company's financial statements for the period ended 2 February 2008 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet, the Statement of Cash Flows, and the related notes 1 to 24 These financial statements have been prepared under the accounting policies set out therein

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

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable United Kingdom law and Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities

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

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985 We also report to you whether in our opinion the information given in the directors' report is consistent with the financial statements

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

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatements within it

Basis of audit opinion

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

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

Independent auditors' report

Opinion

In our opinion

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 2 February 2008 and of its profit for the period then ended,

- the financial statements have been properly prepared in accordance with the Companies Act 1985, and

- the information given in the directors' report is consistent with the financial statements

Ernst & Young LLP

Ernst & Young LLP
Registered Auditor
London

23 July 2008

Date

Profit and loss account
for the Period to 2 February 2008

	Notes	*Period to 2 February 2008 £'000*	*Period to 3 February 2007 £'000*
Turnover	2	57,334	47,112
Cost of sales		(43,464)	(36,020)
Gross profit		13,870	11,092
Other operating income		3,453	2,671
Distribution costs		(2,177)	(1,653)
Administrative expenses		(7,136)	(5,657)
Operating profit	3	8,010	6,453
Bank interest receivable	6	271	67
Interest payable	7	(137)	(242)
		134	(175)
Profit on ordinary activities before taxation		8,144	6,278
Tax on profit on ordinary activities	8	856	(1,972)
Profit retained for the financial year attributable to members of the parent undertaking		9,000	4,306

Statement of total recognised gains and losses
There are no recognised gains or losses other than the profit of £9,000,000 attributable to the shareholders for the Period to 2 February 2008 (2007 - profit of £4,306,000)

Balance sheet
at 2 February 2008

	Notes	2 February 2008 £'000	3 February 2007 £'000
Fixed assets			
Tangible assets	9	9,337	7,467
Current assets			
Stocks	11	7,087	5,773
Debtors	12	5,023	4,871
Cash at bank		7,548	1,902
		19,658	12,546
Creditors amounts falling due within one year	13	9,396	9,065
Net current assets		10,262	3,481
Total assets less current liabilities		19,599	10,948
Creditors: amounts falling due after more than one year	14	200	767
Provisions for liabilities and charges	15	–	99
Net assets		19,399	10,082
Capital and reserves			
Called up share capital	19	100	100
Share premium account	20	2,095	2,095
Other reserves	20	3,342	3,342
Profit and loss account	20	13,862	4,545
Equity shareholders' funds	20	19,399	10,082

Director 1st July 2008

Statement of cash flows
for the Perıod to 2 February 2008

	Notes	*Perıod to 2 February 2008 £'000*	*Perıod to 3 February 2007 £'000*
Net cash inflow from operatıng actıvitıes	22(a)	10,276	5,005
Returns on ınvestments and servıcıng of finance	22(b)	134	(163)
Taxatıon	22(c)	(400)	(600)
Capıtal expendıture	22(d)	(3,666)	(3,406)
Fınancing	22(e)	(643)	(577)
Increase ın cash		5,701	259

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

		2 February 2008 £'000	*3 February 2007 £'000*
Increase ın cash		5,701	259
Cash outflow from movement ın finance leases		153	137
Cash outflow from movement ın bank loans		490	440
Change ın net funds/debt resultıng from cash flows	22(f)	6,344	836
Movement ın net funds/debt		6,344	836
Opening net funds/(debt)	22(f)	389	(447)
Closıng net funds/(debt)	22(f)	6,733	389

Notes to the financial statements
at 2 February 2008

1. Accounting policies

Basis of preparation
The financial statements are prepared under the historical cost convention, and in accordance with applicable accounting standards

The company is exempt from the requirement to prepare group financial statements under sections 229(2) and 229(5) of the Companies Act 1985

Fixed assets
All fixed assets are initially recorded at cost

Depreciation
Depreciation is provided on all tangible fixed assets, at rates calculated to write off the cost, less estimated residual value based on prices prevailing at the date of acquisition of each asset evenly over its expected useful life, as follows

Leasehold improvements	-	Over 20 years for the Manchester outlet and over 6 years for all others
Furniture, fixtures and fittings	-	Over 6 years
Computer hardware and software	-	Over 6 years and 3 years respectively

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable

Other operating income
Other income represents amounts receivable in relation to overseas franchising arrangements

Stocks
Stocks are stated at the lower of cost and net realisable value Cost includes all costs incurred in bringing each product to its present location and condition, as follows

Goods for resale	-	purchase cost on a weighted average basis

Net realisable value is based on estimated selling price less any further costs expected to be incurred to completion and disposal

Deferred taxation
Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or to receive more, tax, with the following exception

- deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted

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

Notes to the financial statements
at 2 February 2008

1. Accounting policies (continued)

Foreign currencies
Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction

Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date

All differences are taken to the profit and loss account

Leasing and hire purchase commitments
Assets held under finance leases, which are leases where substantially all the risks and rewards of ownership of the asset have passed to the company, and hire purchase contracts are capitalised in the balance sheet and are depreciated over their useful lives The capital elements of future obligations under the leases and hire purchase contracts are included as liabilities in the balance sheet

The interest elements of the rental obligations are charged in the profit and loss account over the periods of the leases and hire purchase contracts and represent a constant proportion of the balance of capital repayments outstanding

Rentals payable under operating leases are charged in the profit and loss account on a straight line basis over the lease term

Pension costs
The company operates a defined contribution pension scheme Contributions are charged in the profit and loss account as they become payable in accordance with the rules of the scheme

Share based payments
The group has applied the requirements of FRS20 Share Based Payments In accordance with the transitional provisions, FRS 20 has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 January 2005

The group issues equity-settled share based payments to certain employees They are measured at fair value at the date of grant The fair value determined at the grant date of the equity-settled share based payments is expensed on a straight line basis over the vesting period, based on the Company's estimate of shares that will eventually vest

Notes to the financial statements
at 2 February 2008

2. Turnover
Turnover, which is stated net of value added tax, represents amounts received and receivable from the company's continuing principal activity, the sale of stationery and art materials

An analysis of turnover by geographical market is given below

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
United Kingdom	57,334	47,112

3. Operating profit
This is stated after charging

		Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Auditors' remuneration	- audit services	35	30
	- turnover rent certification	2	2
	- taxation advice	10	5
Depreciation of owned fixed assets		1,919	1,279
Depreciation of assets held under finance leases		128	139
		2,047	1,418
Operating lease rentals	- land and buildings	6,371	5,082
	- plant and machinery	85	47
Loss on disposal of fixed assets		–	21

Notes to the financial statements
at 2 February 2008

4. Staff costs

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Wages and salaries	11,253	8,688
Social security costs	754	584
Staff pension contributions	247	190
Share Based Payments	317	223
	12,571	9,685

The monthly average number of employees during the period was as follows

	Period to 2 February 2008 No	*Period to 3 February 2007 No*
Purchasing and stock control	68	58
Administration and finance	53	41
Sales and display	1,152	815
	1,273	914

5. Directors' emoluments

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Emoluments	863	647
Value of company pension contributions to money purchase schemes	123	109

Notes to the financial statements
at 2 February 2008

5. Directors' emoluments (continued)

	Period to 2 February 2008 No	*Period to 3 February 2007 No*
Members of money purchase pension schemes	4	4

Three Directors exercised share options which became unrestricted during the year

The amounts in respect of the highest paid director are as follows

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Emoluments	308	221
Value of company pension contributions to money purchase schemes	38	29

6. Interest receivable

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Bank interest receivable	218	67
Interest receivable of tax overpayment	53	
	271	67

7. Interest payable

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Bank interest payable	127	220
Finance charges payable under finance leases	10	22
	137	242

Notes to the financial statements
at 2 February 2008

8. Tax

(a) Tax on profit on ordinary activities

The tax charge/(credit) is made up as follows

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Current tax		
UK corporation tax	2,392	1,867
Group relief received for nil payment in prior years	(2,799)	–
Total current tax (note 8(b))	(407)	1,867
Deferred tax		
Origination and reversal of timing differences	(449)	105
Tax on profit on ordinary activities	(856)	1,972

(b) Factors affecting current tax charge/(credit)

The differences are reconciled below

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Profit on ordinary activities before tax	8,144	6,278
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2007 - 30%)	2,443	1,883
Expenses not deductible for tax purposes	41	71
Depreciation for the period in arrears of capital allowances	(110)	(165)
Other short term timing differences	17	78
Utilisation of losses	(2,798)	–
Total current tax (note 8(a))	(407)	1,867

During the period the company made a claim for tax losses from other group companies by way of group relief in connection with the 2006 and 2007 period ends following the finalisation of the tax returns of these group companies These losses were received for nil payment and therefore give rise to a large credit to the tax charge relating to prior periods

Notes to the financial statements
at 2 February 2008

8. Tax (continued)
(c) Deferred tax

The deferred tax included in the Balance Sheet is as follows

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Included in debtors/(provision for liabilities) (note 12/15)	350	(99)

	2 February 2008 £'000	*3 February 2007 £'000*
Depreciation in excess/(arrears) of capital allowances	181	(225)
Other timing differences	169	156
Deferred tax asset/(liability)	350	(99)

	£'000
Deferred tax liability at 24 January 2007	(99)
Profit and loss account movement arising during the period	449
Deferred tax asset at 2 February 2008	350

Deferred tax is recognised in line with FRS 19 on the basis that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted

As a result of the reduction in the UK corporate tax rate in April 2008, deferred tax has been provided at a rate of 28%

Notes to the financial statements
at 2 February 2008

9. Tangible fixed assets

	Leasehold improvements £'000	*Furniture, fixtures and fittings £'000*	*Computer hardware and software £'000*	*Total £'000*
Cost				
At 3 February 2007	2,316	11,277	1,086	14,679
Additions	717	2,338	862	3,917
At 2 February 2008	3,033	13,615	1,948	18,596
Depreciation				
At 3 February 2007	867	5,871	474	7,212
Provided during the period	249	1,420	378	2,047
At 2 February 2008	1,116	7,291	852	9,259
Net book value				
At 3 February 2008	1,917	6,324	1,096	9,337
At 2 February 2007	1,449	5,406	612	7,467

The net book value of assets above includes an amount of £65,950 (2007 - £195,024) in respect of assets held under finance leases

10. Investments

At 3 February 2007 and 2 February 2008 the company held investments in the following principal dormant subsidiary undertakings

Company	*Class of shares*	*Percentage held*
Paperchase Limited	£1 ordinary	100%
Paperchase Designs Ltd	£1 ordinary	100%

11. Stocks

	2 February 2008 £'000	*3 February 2007 £'000*
Consumables	189	94
Finished goods	6,898	5,679
	7,087	5,773

Notes to the financial statements
at 2 February 2008

12. Debtors

	2 February 2008 £'000	3 February 2007 £'000
Trade debtors	1,256	1,902
Amounts owed by group undertakings	1,325	1,170
Other debtors	185	263
Prepayments and accrued income	1,502	1,159
Payments on account	405	377
Deferred taxation (note 8)	350	–
	5,023	4,871

13. Creditors: amounts falling due within one year

	2 February 2008 £'000	3 February 2007 £'000
Bank overdraft	52	107
Current instalment due on bank loan (note 16)	540	490
Obligations under finance leases (note 17)	23	149
Trade creditors	2,260	3,313
Corporation tax	1,008	1,869
Other taxation and social security	526	275
Other creditors	80	39
Accruals and deferred income	4,880	2,801
Pension Accrual	27	22
	9,396	9,065

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

	2 February 2008 £'000	3 February 2007 £'000
Loans (note 16)	200	740
Obligations under finance leases (note 17)	–	27
	200	767

15. Provisions for liabilities

	2 February 2008 £'000	3 February 2007 £'000
Deferred taxation (note 8)	–	99

Notes to the financial statements
at 2 February 2008

16. Loans

	2 February 2008 £'000	3 February 2007 £'000
Amounts repayable		
In one year or less or on demand	540	490
In more than one year but not more than two years	200	540
In more than two years but not more than five years	–	200
	740	1,230

	2 February 2008 £'000	3 February 2007 £'000
Wholly repayable within five years		
Bank loans and other loans	740	1,230
Less included in creditors amounts falling due within one year (note 13)	(540)	(490)
	200	740

The loans from HBOS are secured by an unscheduled mortgage debenture incorporating a fixed and floating charge over all current and future assets of the company

17. Obligations under finance leases

The maturity of these amounts is as follows

	2 February 2008 £'000	3 February 2007 £'000
Amounts payable		
Within one year	23	149
In two to five years	–	27
	23	176

18. Commitments under operating leases

At 2 February 2008 the company had annual commitments under non-cancellable operating leases as set out below

	2 February 2008		3 February 2007	
	Land and buildings £'000	Other £'000	Land and buildings £'000	Other £'000
Operating leases which expire				
Within one year		1	32	8
In two to five years	631	69	547	29
In over five years	5,476	–	4,272	–
	6,107	70	4,851	37

Notes to the financial statements
at 2 February 2008

19. Share capital

		Authorısed
	2 February 2008	*3 February 2007*
	£'000	*£'000*
Class A ordınary shares of £0 10 each	63	63
Class B ordınary shares of £0 10 each	143	143
Class C ordınary shares of £0 10 each	62	62
Preferred ordınary shares of £0 10 each	40	40
Class A preference shares of £1 each	550	550
Class B preference shares of £1 each	710	710
Class BB ordınary shares of £1 each	3,430	3,430
Class CC ordınary shares of £1 each	282	282
Class AA ordınary shares of £1 each	288	288
	5,568	5,568

			Allotted, called up and fully paıd	
	2 February 2008		*3 February 2007*	
	No	*£'000*	*No*	*£'000*
Class BB ordınary shares of £1 each	96,476	96	96,476	96
Class AA ordınary shares of £1 each	3,524	4	3,524	4
		100		100

The 'A' ordınary shares, the 'B' ordınary shares, the 'C' ordınary shares and the preferred ordınary shares shall rank parı passu

The 'AA' ordınary shares and the 'A' ordınary shares shall rank parı passu and the 'AA' ordınary shares shall have all the rıghts, prıvıleges and restrıctıons attachıng to the 'A' ordınary shares The 'BB' ordınary shares and the 'B' ordınary shares shall rank parı passu and the 'BB' ordınary shares shall have all the rıghts, prıvıleges and restrıctıons attachıng to the 'B' ordınary shares and the 'C' ordınary shares shall rank parı passu and the 'CC' ordınary shares shall have all the rıghts, prıvıleges and restrıctıons attachıng to the 'C' ordınary shares

Notes to the financial statements
at 2 February 2008

20. Reconciliation of shareholders' funds and movement on reserves

	Share capital £'000	*Share premium account £'000*	*Capital redemption reserve £'000*	*Capital reserve £'000*	*Profit and loss account £'000*	*Total shareholders' funds £'000*
At 28 January 2006	100	2,095	3,268	74	16	5,553
Profit for the period	–	–	–	–	4,306	4,306
Share based payments	–	–	–	–	223	223
At *3 February* 2007	100	2,095	3,268	74	4,545	10,082
Profit for the period	–	–	–	–	9,000	9,000
Share based payments	–	–	–	–	317	317
At 2 February 2008	100	2,095	3,268	74	13,862	19,399

21. Share based payments

Equity settled share option plan

Share based payments are made to Directors of Paperchase Products Limited under the Borders Group Inc 2004 Long Term Incentive Plan The payments relate to equity in Borders Inc There are two types of award made under this scheme

Restricted Shares

Restricted shares awarded to participants confer the right to vote and receive dividends on the shares The Restricted shares are granted without being subject to performance objectives

Restricted Share Units

Restricted share units do not confer the right to vote and receive dividends on the shares until the point of vesting Upon vesting the RSUs are converted to Borders Inc Common Stock The quantity of Common Stock received by member of the plan is determined in relation to the compound annual growth in Profit before tax for Paperchase Products Limited

The vesting period for both instruments is 3 years There are no cash settlement alternatives

The expense recognised relating to the share based payments is measured with reference to the fair value of the share based payments at grant date The fair value at this date is considered to be the prevailing midpoint share price at close on the day of grant The restrictions on the restricted shares and the restricted share units are not considered to have a material effect on the market value of the shares

The detail of the grants issued during the year were as follows –

	Number	*Weighted average fair value*
Restricted shares	30,000	$15 42
Restricted Share Units	28,805	$20 42

Notes to the financial statements
at 2 February 2008

The fair value determined at the grant date of the equity-settled share based payments is expensed on a straight line basis over the vesting period, based on the Company's estimate of shares that will eventually vest

The total expense recognised during the period for share based payments was £317,000

22 Notes to the statement of cash flows

(a) Reconciliation of operating profit to net cash inflow from operating activities

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Operating profit	8,010	6,453
Depreciation	2,047	1,418
Share based payments	318	223
Loss on disposal of fixed assets	(5)	(21)
Increase in stocks	(1,357)	(1,565)
Increase in debtors	198	(1,753)
Increase in creditors	1,065	250
Net cash inflow from operating activities	10,276	5,005

(b) Returns on investments and servicing of finance

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Interest received	271	67
Interest paid	(127)	(208)
Interest element of finance leases rentals payments	(10)	(22)
	134	(163)

(c) Taxation

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Corporation tax paid	(400)	(600)

Notes to the financial statements
at 2 February 2008

(d) Capital expenditure

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Payments to acquire tangible fixed assets	(3,666)	(3,406)

(e) Financing

	Period to 2 February 2008 £'000	*Period to 3 February 2007 £'000*
Movement in bank loans	(490)	(440)
Repayment of capital element of finance leases	(153)	(137)
	(643)	(577)

(f) Analysis of changes in net /funds

	At 3 February 2007 £'000	*Cash flows £'000*	*Exchange difference £'000*	*At 2 February 2008 £'000*
Cash at bank and in hand	1,902	5,722	(76)	7,548
Overdrafts	(107)	55		(52)
Debt due within one year	(490)	(50)		(540)
Debt due after one year	(740)	540		(200)
Finance leases	(176)	153		(23)
	389	6,420	(76)	6,733

Notes to the financial statements
at 2 February 2008

23. Related party transactions

During the year the company entered into transactions, in the ordinary course of business, with other related parties Transactions entered into, and trading balances outstanding at 2 February 2008, are as follows

	Sales to related party £'000	*Purchases from related party £'000*	*Amounts owed from related party £'000*	*Amounts owed to related party £'000*
Borders (UK) Ltd				
Period ended 2 February 2008	12,784		355	
Period ended 3 February 2007	11,318		219	
Borders Books Ireland Ltd				
Period ended 2 February 2008	153		108	
Period ended 3 February 2007	121		423	

Borders UK & Ireland

Borders Inc, the ultimate parent undertaking of the company, has a 20% interest in Borders (UK) Ltd and Borders Books Ireland Ltd

Exemption

The company has taken advantage of the exemption available under FRS8 not to disclose transactions with other members of the Borders Group Inc

24. Parent undertaking and controlling party

The company's immediate parent undertaking is BGP (UK) Ltd This is the parent undertaking of the smallest group for which group financial statements are prepared

The directors consider the ultimate parent undertaking and the controlling party to be Borders Group Inc , a company incorporated in the United States and whose shares are listed on the New York Stock Exchange This is the parent undertaking of the largest group for which group financial statements are prepared

Financial statements can be obtained from Borders Group Inc , 180 Phoenix Drive, Ann Arbor, Michigan, USA 48108