

Reg no SC 182368

Pelamis Wave Power Limited

Directors' Report and Financial Statements

For the Year Ended

31 December 2010

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Pelamis Wave Power Limited

Directors' report and financial statements for the year ended 31 December 2010

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Pelamis Wave Power Limited

Company information

Directors

Gina Domanig	Non-Executive Chairman
Per Pedersen	Chief Executive Officer
Richard Yemm	Commercial Director
Stuart Deed	Non-Executive Director
Charles Vaslet	Non-Executive Director

Registered office

31 Bath Road, Leith, Edinburgh, EH6 7AH

Company number

SC 182368

Independent Auditors

PricewaterhouseCoopers LLP, Chartered Accountants and Registered Auditors, 141 Bothwell Street, Glasgow, G2 7EQ.

Legal Advisers

McClure Naismith LLP, 292 St Vincent Street, Glasgow, G2 5TQ

Bankers

The Royal Bank of Scotland plc, 36 St Andrew Square, Edinburgh, EH2 2YB

Pelamis Wave Power Limited

Report of the directors for the year ended 31 December 2010

The directors present their report together with the audited financial statements for the year ended 31 December 2010.

Registered number

The registered number of the company is SC182368.

Principal activities, business review and future developments

The principal activities of the Company are the development and construction of wave energy converter systems and associated engineering projects. During the year the Company completed the build of its first P2 wave energy converter which was supplied to E.ON. The machine is currently undergoing testing at the European Marine Energy Centre (EMEC) at Orkney. The company also made substantial progress on the design and construction of an enhanced P2 wave energy converter for ScottishPower Renewables.

In March 2010 the Company also announced that it had acquired an offshore licence to develop a wave farm at Farr Point off the North coast of Scotland and that it had been cited on offshore site licences in Orkney and Pentland Firth by both E.ON and ScottishPower Renewables. It also announced that it had entered into a joint venture with Vattenfall, Aegir Limited, for the development of a wave farm in the Shetland Islands. All of these initiatives lay the foundations for the future sale of Pelamis machines.

The directors expect that the Company will have the same principal activities for the foreseeable future.

Going Concern

The company's business activities, together with the factors likely to affect its future development, performance and financial position are set out in the business review above and key risk section on page 3. The financial position of the company and its cash flows for the year ended 31 December 2010 are set out in the Balance Sheet and Cashflow Statement on pages 10 and 12 of the accounts.

Since 31 December 2010, the company has received additional funding from shareholders of £2.3m, grant awards of £0.6m and a loan of £1m and at the date of approval of these accounts, the company had a cash balance of £1.0m and unaudited net liabilities of £2.6m.

At this date, however, the company has insufficient secured funding to continue as a going concern for the next twelve months, although the Directors consider the outlook for the company to be positive as:

- The P2 machine has undergone over 1,100 hours of testing and the work-up programme is progressing well. No significant issues have been identified during this process and the results from the testing to date are positive;
- There are existing contracts in place with two key customers being E.ON and ScottishPower Renewables;
- There are well-progressed discussions in place with prospective customers for substantial future orders;
- There is significant confidence in the company and its technology, as evidenced by the additional funding received from shareholders and grants awarded post year end; and
- Advisors have been appointed and a process is currently underway to secure additional funding to take the technology through to commercialisation.

Despite this, the directors have concluded that the current lack of secured funding may mean that the company is unable to continue to realise its assets and discharge its liabilities in the normal course of business,

Pelamis Wave Power Limited

Report of the directors for the year ended 31 December 2010 (continued)

Going Concern (continued)

and accordingly this fact represents a material uncertainty that casts significant doubt upon the company's ability to continue as a going concern.

Nevertheless, after making enquiries and, in particular, considering the matters described above, the directors have a reasonable expectation that the company will have adequate resources to continue in operational existence for the foreseeable future, and for this reason, they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

If the accounts were produced on a break-up basis the most significant adjustment would be the write-off of capitalised development expenditure of £6.8m and release of £4.2m of grants held in deferred income.

Key performance indicators

The Company has identified a number of key performance indicators which are relevant to development of its business during the year.

In 2010 the Group had turnover of £5.1m (2009: £3.3m) which was substantially derived from its contracts to build, install and operate two P2 machines at EMEC in Orkney. The Company has capitalised development expenditure on the P2 machine projects up to the point of hand over of the machines to customers. As these are development projects partially funded by customers, the costs associated with the projects which are over and above those funded have been capitalised as development costs. The operating loss was slightly lower than last year at £1.46m (2009: £1.53m).

There was an operating cash inflow of £3.5m (2009: £3.5m outflow) and an investment in development expenditure of £3.7m (2009: £3.2m). The operating cash inflow benefitted from grants receivable of £5.2m for the year (2009: £0.4m). R&D tax credit receipts in 2010 relating to the year 2009 totalled £0.5m (2009: £2.3m relating to 2005 to 2008). The Group had a net inflow of cash for the year of £0.1m (2009: £4.7m outflow). At the end of the year the Group had net borrowings (including £51.6m in respect of 'A' shares) of £49.8m (2009 £48.7m). The 'A' shares are treated as debt although a cash redemption was not technically permissible under the Companies Act 2006. On 24 May 2011 the Company Articles of Association were amended following a financing round and the 'A' shares now have no right of redemption and therefore cannot be considered as debt. If the 'A' shares were treated as shareholder funds the adjusted net liabilities would amount to net assets of £2.9m (2009: £4.1m).

Key risks / uncertainties

The directors have identified a number of key risks / uncertainties for the Company's business:

- Technology risk that the Company's technology may not work as envisaged or that the Company will fail to develop equipment at an acceptable cost.
- Political risk that the governments in the jurisdictions where the Company aims to sell its machinery will fail to establish adequate revenue support mechanisms or planning regimes to enable the Company to increase its sales volumes as planned by management.
- Financial risk that the Company will not be able to secure adequate finance to fund its successful future commercial development.
- Personnel risk that the Company will lose key personnel to competitors or other industries which would slow down progress with the research and development programme.

Pelamis Wave Power Limited

Report of the directors for the year ended 31 December 2010 (continued)

Directors

The directors who held office during the year except as noted are set out below:

Lord Colin Moynihan	(Chairman)	(resigned 16 May 2011)
Per Pedersen	(Chief Executive Officer)	(appointed 15 October 2011)
Cornelius Kriek	(Chief Executive Officer)	(resigned 27 September 2010)
Richard Yemm	(Commercial Director)	
Gina Domanig	(Non-executive)	
Marco Fabbri	(Non-executive)	(resigned 7 June 2011)
Hans Middelthon	(Non-executive)	(resigned 7 June 2011)
Charles Vaslet	(Non-executive)	(appointed 7 June 2011)
Stuart Deed	(Non-executive)	(appointed 24 June 2011)

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 prepared the group and parent company 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 group and the company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to:

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

The directors are responsible for keeping 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 the group 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 the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities

In accordance with Section 418 of the Companies Act 2006 all current directors confirm that;

- so far as each director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Pelamis Wave Power Limited

Report of the directors for the year ended 31 December 2010 (continued)

Auditors and disclosure of information to auditors

As far as each of the directors, at the time the report is approved, are aware

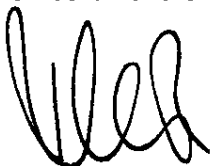
- there is no relevant information of which the company's auditors are unaware
- the directors have taken all reasonable steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

Auditors

The auditors, PricewaterhouseCoopers LLP, were appointed on 16 April 2008 in accordance with Section 385 of the Companies Act 1985.

In accordance with section 366A(1) of the Companies Act 2006, an elective resolution has been passed by shareholders in order to dispense with the need to hold Annual General Meetings and to appoint auditors annually.

On behalf of the Board



P. Pedersen
Chief Executive Officer

31 October 2011

Pelamis Wave Power Limited

Report of the independent auditors

Independent auditors' report to the members of Pelamis Wave Power Limited

We have audited the group and parent company financial statements (the "financial statements") of Pelamis Wave Power Limited for the year ended 31 December 2010 which comprise the consolidated profit and loss account, the consolidated statement of total recognised gains and losses, the consolidated balance sheet, the company balance sheet, the consolidated cash flow statement and the related notes. 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).

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 4 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 International Standards on Auditing (UK and 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 expressed by our consent in writing.

Scope of the audit of the 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 group's and parent 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 on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the group's and the parent company's affairs as at 31 December 2010 and of the group's loss and cash flows 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.

Emphasis of Matter – Going Concern

In forming our opinion on the financial statements, which is not qualified, we have considered the adequacy of the disclosure made in the Directors' Report and note 1 to the financial statements concerning the company's ability to continue as a going concern. The company incurred a net loss of £2,167,000 during the year ended 31 December 2010 and, at that date, the company's total assets exceeded its current liabilities by £3,077,000. Total assets include £6,812,000 of capitalised development expenditure which is to be amortised against future sales. These conditions, along with the other matters explained in note 1 to the financial statements, indicate the existence of a material uncertainty which may cast significant doubt about the company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the company were unable to continue as a going concern.

Pelamis Wave Power Limited

Report of the independent auditors (continued)

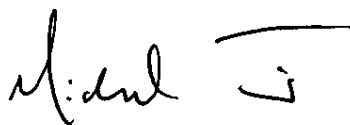
Opinion on other matter prescribed by the Companies Act 2006

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

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 by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company 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.



Michael Timar (Senior Statutory Auditor)
For and behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Glasgow

31 October 2011

Pelamis Wave Power Limited

Consolidated profit and loss account for the year ended 31 December 2010

	Note	2010 £000	2009 £000
Group Turnover	2	5,086	3,309
Cost of sales		(5,568)	(2,805)
Gross profit / (loss)		(482)	504
Administrative expenses		(1,244)	(2,484)
Other operating income	3	270	445
Group operating loss	6	(1,456)	(1,535)
Share of operating (loss) / profit in associate		(41)	(38)
Loss on ordinary activities before finance charges and taxation		(1,497)	(1,573)
Other interest receivable and similar income	7	24	68
Interest payable and similar charges			
Group	7	(1,178)	(1,303)
Associate	7	(31)	(27)
Loss on ordinary activities before taxation		(2,682)	(2,835)
Taxation on loss from ordinary activities	8	515	910
Loss for the year	17	(2,167)	(1,925)

All amounts relate to continuing activities.

Pelamis Wave Power Limited

Consolidated statement of total recognised gains and losses for the year ended 31 December 2010

	2010	2009
	£000	£000
Loss for the financial year	(2,167)	(1,925)
Exchange differences on consolidation	(11)	(34)
Total recognised gains and losses for the year	(2,178)	(1,959)

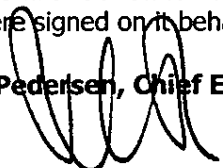
Pelamis Wave Power Limited

Consolidated balance sheet as at 31 December 2010

	Note	2010 £000	2009 £000
Fixed assets			
Intangible assets	10	7,101	3,412
Tangible assets	11	502	330
Investments	12	293	378
		7,896	4,120
Current assets			
Stocks	13	31	87
Debtors	14	1,135	616
Cash at bank and in hand		1,875	1,817
		3,041	2,520
Creditors: amounts falling due within one year	15	(7,860)	(2,587)
Net current assets		(4,819)	(67)
Total assets less current liabilities		3,077	4,053
Creditors: amounts falling due after more than one year	15	(51,647)	(50,470)
Net liabilities		(48,570)	(46,417)
Capital and reserves			
Called up share capital	16	123	123
Share premium account	17	78	78
Profit and loss account	17	(49,470)	(47,328)
Foreign exchange reserve	17	699	710
Total shareholders' deficit	19	(48,570)	(46,417)

The financial statements on pages 8 to 30 were approved by the Board of Directors on 31 October 2011 and were signed on its behalf by:

P. Pedersen, Chief Executive Officer

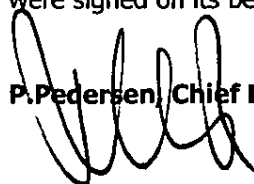


Pelamis Wave Power Limited

Company balance sheet as at 31 December 2010

	Note	2010 £000	2009 £000
Fixed assets			
Intangible assets	10	7,101	3,412
Tangible assets	11	502	329
Investments	12	120	378
		7,723	4,119
Current assets			
Stocks	13	31	87
Debtors	14	1,119	711
Cash at bank and in hand		1,855	1,691
		3,005	2,489
Creditors: amounts falling due within one year	15	(7,824)	(2,555)
Net current assets		(4,819)	(66)
Total assets less current liabilities		2,904	4,053
Creditors: amounts falling due after more than one year	15	(51,647)	(50,470)
Net liabilities		(48,743)	(46,417)
Capital and reserves			
Called up share capital	16	123	123
Share premium account	17	78	78
Profit and loss account	17	(48,944)	(46,618)
Total shareholders' deficit	19	(48,743)	(46,417)

The financial statements on pages 8 to 30 were approved by the Board of Directors on 31 October 2011 and were signed on its behalf by:



P. Pedersen, Chief Executive Officer

Pelamis Wave Power Limited

Consolidated cash flow statement for the year ended 31 December 2010

		2010	2010	2009	2009
		£000	£000	£000	£000
Net cash inflow / (outflow) from operating activities	22		3,544		(3,457)
Returns on investments and servicing of finance					
Interest received		24		120	
Net cash inflow from returns on investments and servicing of finance			24		120
Taxation			522		2,272
Capital expenditure and financial investment					
Purchase of tangible fixed assets		(332)		(291)	
Investment in intangible fixed assets		(3,707)		(3,211)	
Disposal of tangible fixed assets		-		1	
Investment in associates		-		(109)	
Net cash outflow from capital expenditure and financial investment			(4,039)		(3,610)
Cash inflow / (outflow) before financing			51		(4,675)
Cash inflow from financing			-		-
Increase / (Decrease) in cash	23		51		(4,675)

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010

1 Accounting policies

Basis of accounting

The financial statements have been prepared under the historical cost convention and are in accordance with the Companies Act 2006 and applicable accounting standards. The following principal accounting policies have been applied consistently:

Basis of consolidation

The consolidated financial statements include those of the Company and its subsidiary undertakings for the year ended 31 December 2010. No profit and loss account is presented for Pelamis Wave Power Limited as permitted by section 408 of the Companies Act 2006.

Entities, other than subsidiary undertakings, in which the group has a participating interest and over whose operating financial policies the group exercises a significant influence are treated as associates. In the group financial statements, associates are accounted for using the equity method.

All inter-company balances and transactions are eliminated and sales and profits or losses relate to external transactions only.

Going concern

The accounts are prepared on a going concern basis.

At this point in time, the company has insufficient secured funding to continue as a going concern for the next twelve months. The Directors consider it appropriate, however, to prepare the accounts on a going concern basis as discussed within the Directors' Report. Refer to page 2 of the Directors' Report for further information.

Turnover

Turnover comprises the value of goods and services supplied by the Company, exclusive of Value Added Tax and other sales taxes. It also includes income earned under long term contracts.

Foreign currency translation

Transactions denominated in foreign currencies are translated at the exchange rate at the date of the transaction. Monetary assets and liabilities held at the balance sheet date are retranslated at the exchange rates ruling at that date. Any resulting exchange profit or loss is dealt with in the profit and loss account.

The results of overseas operations are translated at the average rates of exchange during the year and their balance sheets translated into sterling at the rates of exchange ruling on the balance sheet date. Exchange differences which arise on the retranslation of the opening net assets are taken directly to reserves.

Intangible fixed assets and depreciation

Patents and licences are stated at cost and are amortised on a straight line basis over their expected useful economic life of 20 years.

1 Accounting policies (continued)

Research and development

Expenditure on pure and applied research is charged to the profit and loss account in the year in which it is incurred.

Development costs are capitalised within intangible assets only where they can be identified as relating to a specific project anticipated with reasonable certainty to be completed and produce measurable future benefits, and are amortised over the anticipated life of the benefits arising from the completed product or project.

Deferred development costs are reviewed annually, and where future benefits are deemed to have ceased or to be in doubt, the balance of any related costs are written off to the profit and loss account in that year.

Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost net of depreciation and any provision for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation is provided at rates calculated to write off the cost less the residual value of each asset on a straight line basis over its expected useful life as follows:

Plant and machinery	- 4 years
Fixtures, fittings and office equipment	- 3-4 years
Motor vehicles	- 4 years

Investments

Fixed asset investments are stated at cost plus direct acquisition costs less provisions for any impairment. The carrying value of investments are regularly assessed for permanent impairment and provisions made if appropriate. Fixed asset investments include loans made to associate undertakings with no fixed repayment date which form part of the long term capital of the associate undertaking.

Leases

Rentals payable under operating leases are charged to the profit & loss account on a straight line basis over the lease term.

Long term contract work in progress

Profit on long term contracts is taken as the work is carried out only if the final outcome can be assessed with reasonable certainty. The profit included is calculated on a prudent basis to reflect the milestones achieved and milestones in progress. Turnover is recognised as significant milestones are achieved and accepted by the customer. Revenues derived from variations on contracts are recognised only when they have been accepted by the customer. Full provision is made for losses in the year in which they are first foreseen.

Deferred taxation

Deferred tax is provided in full in respect of timing differences that have originated but not reversed by the balance sheet date. The recognition of deferred tax assets is limited to the extent that the Group anticipates making sufficient taxable profits in the future to absorb the reversal of the underlying timing differences.

Pension costs

Contributions to the Company's stakeholder pension scheme and group pension plan, both defined contribution pension schemes, are charged to the profit and loss account in the year in which they become payable.

1 Accounting policies (continued)

Government grants

Government grants relating to tangible fixed assets are treated as deferred income and released to the profit and loss account over the expected useful lives of the assets concerned. Government grants relating to capitalised development expenditure are credited to the profit and loss account against the release of the associated expenditure. Grants of a revenue nature are credited to the profit and loss account in the period to which they relate.

Share based payments

The Company grants share options to certain employees. The fair value of the options at the date of grant is charged to the profit and loss account over the vesting period. Non-market vesting conditions are taken into account by adjusting the number of equity instruments expected to vest at each balance sheet date so that, ultimately, the cumulative amount recognised over the vesting period is based on the number of options that eventually vest. No adjustment is made for changes in market related vesting conditions. Fair value is measured by use of the Black-Scholes pricing model.

2 Turnover

Group	2010 £000	2009 £000
Class of business:		
Sale of Pelamis wave energy converters	3,609	2,565
Sale and installation of offshore moorings infrastructure	630	538
Operation and maintenance of wave energy converters	442	-
Feasibility study income	405	206
	5,086	3,309
Geographical analysis:		
United Kingdom	4,760	2,822
Rest of Europe	299	442
Other	27	45
	5,086	3,309

3 Other operating income

Group	2010 £000	2009 £000
Grant income	270	367
Income from lease of equipment	-	78
	270	445

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

4 Employees

Group	2010 £000	2009 £000
Staff costs (including directors) consist of:		
Wages and salaries	3,140	3,191
Social security costs	328	347
Pension costs	75	71
	3,543	3,609

The average number of employees, including executive directors, employed during the year was:

Group	2010 number	2009 number
Engineering and operations	56	59
Selling and administration	11	15
	67	74

5 Directors' emoluments

Directors' remuneration consists of:	2010 £000	2009 £000
Aggregate emoluments	354	588
Compensation for loss of office	137	113
Pension	3	14
	494	715

Emoluments of the highest paid director were £177,000 (2009: £161,145).

One (2009: four) director participated in either the stakeholder pension scheme or the group personal pension plan.

No directors received shares during the year in respect of qualifying services (2009: nil) and no directors exercised share options during the year (2009: nil).

Pelamis Wave Power Limited**Notes forming part of the financial statements for the year ended 31 December 2010 (continued)****6 Operating loss**

Group	2010	2009
	£000	£000
Operating loss is stated after charging:		
Depreciation of tangible fixed assets	152	144
Amortisation of intangible fixed assets	18	15
Operating leases - land & buildings	516	378
Auditors' remuneration	27	24
Loss/(gain) on disposal of fixed assets	2	(1)

7 Finance and similar charges (net)

Group	2010	2009
	£000	£000
Interest receivable	(24)	(68)
Provision for 'A' share redemption	1,178	1,303
Finance and similar charges - Group	1,154	1,235
Share of associate's interest charge	31	27
	1,185	1,262

8 Taxation on loss from ordinary activities

Group	2010	2009
	£000	£000
Current Tax Credit		
UK corporation tax at 28% (2009: 28%)	-	-
Tax credit in respect of prior years	(523)	(915)
	(523)	(915)
Foreign tax	8	5
Share of associate's current tax	-	-
Total current tax	(515)	(910)

The tax assessed for the year differs from the standard rate of corporation tax in the UK applied to profit before tax. The differences are explained below:

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

8 Taxation on loss from ordinary activities (continued)

Group	2010 £000	2009 £000
Factors affecting current tax charge for the period		
Loss on ordinary activities before taxation	(2,682)	(2,835)
Loss on ordinary activities at the standard rate of corporation tax in the UK of 28% (2009 : 28%)	(751)	(794)
Effects of:		
Non deductible expenditure	90	39
Difference between depreciation and capital allowances	(5)	(5)
Tax losses available for carry forward	673	759
Difference in overseas tax rate	1	1
Prior year losses surrendered for research & development tax credit	(523)	(910)
Current tax charge for year	(515)	(910)

Factors that may affect future tax charges

The Group has estimated tax losses, subject to the agreement of HMRC, arising in the UK of £38,222,000 (2009: £37,652,000) that are available indefinitely for offset against future taxable profits of Pelamis Wave Power Limited. In addition, the Group has estimated tax losses arising in Portugal of £97,000 (2009: £89,000) that are available for a period of between 1 and 6 years, for offset against future taxable profits in Pelamis Portugal SA.

Deferred tax assets have not been recognised in respect of any of these losses which will become recoverable when the Group makes sufficient future taxable profits. All timing differences at the balance sheet date have been measured at 27% (2009: 28%). The unrecognised deferred tax asset is estimated as £10,264,000 (2009: £10,508,000).

Group	2010 £000	2009 £000
Provision for deferred tax comprises:		
Tax losses available for carry forward	10,344	10,564
Capital allowances	(79)	(55)
Other timing differences	(1)	(1)
Total deferred tax asset not recognised	10,264	10,508

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

9 Loss for the financial year

As permitted by Section 408 of the Companies Act 2006, the profit and loss account of the parent company is not presented as part of these financial statements.

The consolidated retained loss for the financial year of £2,167,000 (2009: £1,925,000) includes a £2,351,000 loss (2009: £1,993,000 loss) in respect of the parent company.

10 Intangible fixed assets

Group and Company	Development expenses £000	Patents and licences £000	Total £000
Cost			
At 1 January 2010	3,151	328	3,479
Additions	3,661	46	3,707
At 31 December 2010	6,812	374	7,186
Amortisation			
At 1 January 2010	-	67	67
Charge for year	-	18	18
At 31 December 2010	-	85	85
Net book value			
At 31 December 2010	6,812	289	7,101
At 31 December 2009	3,151	261	3,412

Development costs relate to the design and build of the first two P2 machines including related tooling and infrastructure. The P2 machines build on the experience gained by the Company in the deployment of previous prototypes. The amount stated is net of costs which have been funded by customers. The Company anticipates that the current development phase will continue for the next two years. It is anticipated that the first large scale projects will be undertaken in 2013.

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

11 Tangible fixed assets

Group	Plant and machinery £000	Fixtures, fittings and office equipment £000	Motor vehicles £000	Total £000
Cost				
At 1 January 2010	886	290	14	1,190
Additions	312	4	11	327
Disposals	-	(86)	(5)	(91)
At 31 December 2010	1,198	208	20	1,426
Accumulated depreciation				
At 1 January 2010	606	244	10	860
Charge for year	127	18	7	152
Disposals	-	(83)	(5)	(88)
At 31 December 2010	733	179	12	924
Net book value				
At 31 December 2010	465	29	8	502
At 31 December 2009	280	46	4	330

No fixed assets were held under finance leases.

Pelamis Wave Power Limited**Notes forming part of the financial statements for the year ended 31 December 2010 (continued)****11 Tangible fixed assets (continued)**

Company	Plant and machinery £000	Fixtures, fittings and office equipment £000	Motor vehicles £000	Total £000
Cost				
At 1 January 2010	886	288	14	1,188
Additions	312	4	11	327
Disposals	-	(85)	(5)	(90)
At 31 December 2010	1,198	207	20	1,425
Accumulated depreciation				
At 1 January 2010	606	243	10	859
Charge for year	127	18	7	152
Disposals	-	(83)	(5)	(88)
At 31 December 2010	733	178	12	923
Net book value				
At 31 December 2010	465	29	8	502
At 31 December 2009	280	45	4	329

Pelamis Wave Power Limited**Notes forming part of the financial statements for the year ended 31 December 2010 (continued)****12 Fixed asset investments**

Share of net tangible assets of associates	£000
At 1 January 2010	378
Additions	210
Share of loss retained by associates	(282)
Translation adjustments	(13)
At 31 December 2010	293

Company	Loans to Associates £000
At 1 January 2010	378
Provisions for impairment	(258)
At 31 December 2010	120

At the end of the year the Company carried out a further review of the value of its investment in Companhia da Energia Oceânica SA. Due to uncertainty over the form of future operations and therefore future cash flows, the investment has been written down to the net book value of its assets.

The loans form part of a revolving loan facility and were granted for an indefinite period of time. The loans are unsecured and attract interest corresponding to an aggregate of six month EURIBOR plus a spread of 1.5%.

During the year the company acquired 9,800 B shares of £0.01 in Aegir Wave Power Limited being 49% of the issued share capital. The majority shareholder contributed a loan of £420,000 to Aegir during the year. Aegir is developing a wave farm site in Shetland.

The following were directly owned as at the balance sheet date:

Subsidiary undertakings	Description and proportion of share capital owned	Country of Incorporation	Nature of business
Pelamis Portugal SA	Ordinary 100%	Portugal	Wave power
Associate undertakings			
Companhia da Energia Oceânica SA	Ordinary 22.9%	Portugal	Wave power
Aegir Wave Power Limited	B shares 49%	Scotland	Project Development

For all undertakings listed, the country of operation is the same as the country of incorporation.

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

13 Stocks

	Group 2010 £000	Group 2009 £000	Company 2010 £000	Company 2009 £000
Raw materials and consumables	31	87	31	87
	31	87	31	87

There is no material difference between the balance sheet value of stocks and their replacement value.

14 Debtors

	Group 2010 £000	Group 2009 £000	Company 2010 £000	Company 2009 £000
Due within one year:				
Trade debtors	945	219	943	219
Amounts owed by group undertakings	-	-	1	260
Other debtors	59	200	44	42
Prepayments and accrued income	131	190	131	190
Corporation tax	-	7	-	-
	1,135	616	1,119	711

Amounts owed by Group undertakings are unsecured, interest free, have no fixed date of repayment and are repayable on demand.

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

15 Creditors

	Group 2010 £000	Group 2009 £000	Company 2010 £000	Company 2009 £000
Amounts falling due within one year:				
Trade creditors	759	802	726	794
Payments received on account on long-term contracts	1,561	478	1,561	478
Other taxation and social security payable	73	77	72	77
Other creditors	823	10	823	10
Accruals and deferred income	4,644	1,220	4,642	1,196
	7,860	2,587	7,824	2,555

Included within Other creditors is an amount of £807,000 relating to a customer's share of a government grant. Subsequent to the year end, this balance was converted into a loan on 24 May 2011 within a total facility of £1,017,000. This loan was subsequently refinanced through a loan of £1,017,000 on 27 October 2011. This loan is repayable on the earlier of an exit by shareholders, substantial investment in the Company or three years. The loan attracts interest at 6% over the Bank of England base rate and carries a floating charge over the assets of the Company. The loan may be converted into 'B' shares of the company in event of an exit at £6 per share and carries a 30% redemption premium.

	Group 2010 £000	Group 2009 £000	Company 2010 £000	Company 2009 £000
Amounts falling due after more than one year:				
'A' shares	51,647	50,470	51,647	50,470
	51,647	50,470	51,647	50,470

The 'A' shares are included as a liability at the balance sheet date as they may have been redeemed, subject to the Companies Act 2006, at the option of a majority of 66% of the holders by 3 months notice. During April 2010 the holders of the 'A' shares waived their right to give notice to redeem their shares before 1 January 2011. A premium of 20% was payable upon redemption. On 24 May 2011 the 'A' shares further waived their right to any redemption. Accordingly 'A' shares are included in creditors due after more than one year but will be reclassified as Share Capital in the 2011 financial statements.

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

16 Share capital

Group and Company

Allotted, called up and fully paid

Included in share capital

493,000 ordinary shares of 25p each

(2009 – 493,000 ordinary shares of 25p each)

123

123

Included in creditors due after more than one year

4,324,729 'A' shares of 25p each

(2009 – 4,324,729 'A' shares of 25p each)

1,081

1,081

1,204

1,204

The Company's 'A' shares are included in the balance sheet as a liability owing to the holders' rights to require their redemption at the balance sheet date. A redemption was not technically permissible under the Companies Act 2006 other than through a fresh issue of shares. The 'A' shareholders waived their right to redemption on 24 May 2011. The 'A' shareholders have the right to convert their shares to ordinary shares and thereafter rank pari passu with the ordinary shares in terms of voting rights and rights to dividends.

Pelamis Wave Power Limited**Notes forming part of the financial statements for the year ended 31 December 2010 (continued)****17 Reserves**

Group	Share premium account £000	Profit and loss account £000	Foreign exchange reserve £000
At 1 January 2010	78	(47,328)	710
Loss for the year (note 19)	-	(2,167)	-
Translation differences on consolidation	-	-	(11)
Share based payments	-	25	-
At 31 December 2010	78	(49,470)	699
Company			
At 1 January 2010	78	(46,618)	-
Loss for the year (note 19)	-	(2,351)	-
Share based payments	-	25	-
At 31 December 2010	78	(48,944)	-

18 Share-based payments

The Company has operated different share based payment schemes for directors, employees and advisors.

Unapproved Share Options

Certain directors, employees and advisors to the Company have been granted unapproved share options. Option deeds are drafted on a case by case basis and in some cases include performance conditions. Lenders to the Company have also been granted options as one of the conditions of the loans provided.

Enterprise Management Incentive (EMI)

Directors and employees have been granted options under the EMI scheme where they satisfied the eligibility conditions of the scheme. Subject to the rules, options may normally be exercised after the first anniversary of the date of grant and before the tenth anniversary of the date of grant. Performance conditions may be required to be met at the discretion of the Board.

In accordance with FRS20 'Share-based payments', a charge to the profit and loss account in respect of any options granted under the above schemes is recognised and spread over the vesting period of the options based on the fair value of the options at the date of grant. This charge has no cash impact.

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

18 Share-based payments (continued)

Group and Company	2010 £000	2009 £000
Total share-based remuneration	25	(77)

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the year.

	No.	WAEP
Outstanding at 1 January 2010	201,158	£9.66
Forfeited during the year	(4,625)	£10.00
Outstanding at 31 December 2010	196,533	£9.65
Exercisable at 31 December 2010	158,395	£9.56

Included in the opening and closing balances are options over 76,200 shares that have not been recognised in accordance with FRS 20 as the options were granted on or before 7th November 2002.

There were no options granted during the year. No options were exercised during the year. There are no cash settlement alternatives for any share options.

The options outstanding at 31 December 2010 had an expected weighted average remaining life of 1 year. The exercise prices for options outstanding at the year end ranged between £9.00 and £23.58. The number of options exercisable were in the following ranges:

Range of exercise prices	No.
Between £9 and £10	190,031
Greater than £10	6,502

The fair value of the equity-settled options granted is estimated at the date of grant using a Black-Scholes option pricing model. The following table lists the inputs to the model for years ended 31 December 2010 and 31 December 2009.

Valuation Information	2010	2009
Weighted average share price at grant date	n/a	n/a
Weighted average exercise price	n/a	n/a
Expected life of option (years)	n/a	n/a
Expected volatility	n/a	n/a
Expected dividend growth	n/a	n/a
Risk-free interest rate	n/a	n/a

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

19 Reconciliation of movements in shareholders' funds

Group	2010 £000	2009 £000
Shareholders' funds at 1 January 2010	(46,417)	(44,381)
Loss for the year	(2,167)	(1,925)
Translation differences on consolidation	(11)	(34)
Share based payments	25	(77)
Shareholders' funds at 31 December 2010	(48,570)	(46,417)
Company		
Shareholders' funds at 1 January 2010	(46,417)	(44,347)
Loss for the year	(2,351)	(1,993)
Share based payments	25	(77)
Shareholders' funds at 31 December 2010	(48,743)	(46,417)

20 Commitments under operating leases

The Group and Company had annual commitments under non-cancellable operating leases as set out below:

	Land and Buildings 2010 £000	Land and Buildings 2009 £000
Operating leases which expire:		
Within one year	3	12
	3	12

Pelamis Wave Power Limited**Notes forming part of the financial statements for the year ended 31 December 2010 (continued)****21 Related party transactions**

The Group has taken advantage of the exemption in FRS8 whereby related party transactions do not need disclosed where they are in relation to subsidiaries, specifically Pelamis Portugal SA, which is consolidated into these accounts.

During the year the Group transacted with related parties in the normal course of business and on an arm's length basis. Details of these transactions are shown below:

Related Party	Group Share holding	Sales to related party £000
Aegir Wave Power Limited	49%	79

22 Reconciliation of operating loss to net cash outflow from operating activities

	2010 £000	2009 £000
Operating loss	(1,456)	(1,535)
Depreciation of tangible fixed assets	152	144
Amortisation of intangible assets	18	15
Share based payments	25	(77)
Loss on disposal of tangible fixed assets	2	(1)
Decrease/(increase) in stocks	56	(87)
(Increase)/decrease in debtors	(532)	491
Increase/(decrease) in creditors	5,279	(2,407)
Net cash inflow/(outflow)	3,544	(3,457)

23 Reconciliation of net cash flow to movement in net debt

	2010 £000	2009 £000
Increase / (decrease) in cash	51	(4,675)
Change in net debt resulting from cash flows	51	(4,675)
Premium charged on 'A' share redemption	(1,177)	(1,303)
Translation differences	7	45
Net debt at beginning of period	(48,653)	(42,720)
Net debt at end of period	(49,772)	(48,653)

Pelamis Wave Power Limited

Notes forming part of the financial statements for the year ended 31 December 2010 (continued)

24 Analysis of net debt

	31 December 2009 £000	Cash Flow £000	Non-Cash Changes £000	Translation Adjustments £000	31 December 2010 £000
Cash and deposits	1,817	51	-	7	1,875
'A' Shares	(50,470)	-	(1,177)	-	(51,647)
Net debt	(48,653)	51	(1,177)	7	(49,772)

Non-cash changes relate to the accrual of the premium on redemption of 'A' shares.

25 Capital commitments

Amounts contracted for but not provided in the financial statements amounted to £7,000 for the group and the Company (2009: £2,000 group and Company).

26 Post balance sheet events

Between 24 May 2011 and 27 October 2011 the Company raised a further £2.3m through the creation of 'B' series convertible redeemable preference shares of £0.25 each at a price of £1.98 per share and 'A1' series convertible preference shares of £0.01 each at a price of £0.01 per share.

On 24 May 2011 the Company Articles of Association were amended and the 'A' shares now have no right of redemption and therefore cannot be considered as debt. If the 'A' shares were treated as shareholder funds the adjusted net liabilities at 31 December 2010 would amount to net assets of £2.9m (2009:£4.1m).

Included within Other creditors is an amount of £807,000 relating to a customer's share of a government grant. Subsequent to the year end, this balance was converted into a loan on 24 May 2011 within a total facility of £1,017,000. This loan was subsequently refinanced through a loan of £1,017,000 on 27 October 2011. This loan is repayable on the earlier of an exit by shareholders, substantial investment in the Company or three years. The loan attracts interest at 6% over the Bank of England base rate and carries a floating charge over the assets of the Company. The loan may be converted into 'B' shares of the company in event of an exit at £6 per share and carries a 30% redemption premium.