Biocompatibles

2004 Annual Report

Corporate Synopsis

Biocompatibles is the medical device company focused on the treatment of cancer, cardiovascular disease, and benign tumours.

The Company's proprietary biomedical polymer systems provide medical devices with enhanced biocompatibility and offer a platform for drug delivery.

2004

- **Positive ruling in Isostent trial – jury finds in favour of the defendants**
- **First patient enrolled in Abbott's Drug Eluting Stent Clinical Trial**
- **Positive preliminary data from PRECISION clinical trials**

Contents

Financial Summary

- 2004 operating loss of £7.6m (2003: £7.8m).
- Net funds at 31 December 2004 of £45.2m (2003: £55.1m).
- £17.6m in escrow account, on which interest is accruing.
- £4.9m release of disposal provisions (2003: £21.6m).
- Turnover of £2.6m (2003: £2.1m).
- Loss before tax of £0.6m (2003: profit £16.0m).
- Net cash outflow before acquisitions and financing £6.5m (2003: £8.9m).

2005

- **Acquisition of CellMed AG, announced on 4 March 2005, expands product pipeline**
- **Further data shows positive tumour response in PRECISION trial**
- **Basis for a global, multi-centre randomised controlled trial – PRECISION IV**

OUR VISION

"We intend to establish our Drug Eluting Bead technology as the Gold Standard treatment for Intermediate HCC and plan that our polymer systems will be recognised as the best in the field of Interventional Medicine"

Biocompatibles made good progress in 2004.

The Principal Investigators of the Company's PRECISION clinical trial presented positive data at the CIRSE[1] conference on 26 September 2004; and Abbott announced the start of a clinical trial for the evaluation of its ZoMaxx™ Drug Eluting Stent on 14 September 2004.

The Company is delivering its plan.

The Business

Biocompatibles is a world leader in technology for "Combination Products" – medical products that combine the functionality of a medical device, like an orthopaedic hip or a coronary pacemaker, with the systemic therapeutic action of a drug, like a cytotoxic cancer drug or an anti-inflammatory steroid. The growth in the market for Drug Eluting coronary stents, from $1.3bn[2] in 2003 to $3.9bn[2] in 2004 was a significant factor in the growth of the wider market for Combination Products whose sales are expected to reach $10bn in 2009[3].

We are focused on two markets within Combination Products – Drug Eluting Beads and Drug Eluting Stents. Both products are delivered by means of the same keyhole surgery imaging system, fluoroscopy, used by interventional radiologists and interventional cardiologists respectively.

Our lead programme is the Drug Eluting Bead which we are developing without a partner at this stage. The Board believes that the value of this programme will grow with more clinical evidence of efficacy and that the Company has sufficient cash and management resources to continue to develop this programme in the near term. The Company's first generation Bead product, Bead Block, is distributed in a marketing alliance with Terumo, a leading supplier of products for interventional medicine, head-quartered in Japan.

We also have a programme in partnership with Abbott Laboratories in the market for Drug Eluting Stents, which is managed and financed by Abbott.

The Technology

Biocompatibles has a portfolio of granted patents around the two proprietary polymer systems – the PC Technology that formed the origin of the company and which is used by Abbott and Dideco, amongst other leading medical device companies; and the N-fil™ technology licensed from the Biocure affiliate of Novartis' Ciba Vision subsidiary and which is used in the Drug Eluting Bead programme. The patents provide a strong position over the use of these polymer systems in the target interventional products markets.

> "Current evidence on uterine artery embolisation (UAE) suggests that it is safe enough for routine use and that there is symptomatic benefit in the majority of patients in the short term."
>
> *The National Institute for Clinical Excellence (NICE).*

1 Cardiovascular and Interventional Radiological Society of Europe
2 Merrill Lynch: 18 January 2005: Boston Scientific Corp.: Updated Stent Model
3 Reference: Navigant Consulting (2003) Combination Products: An Impact Analysis on the Convergence of Medical Devices and Therapeutic

A considerable part of Biocompatibles' intellectual property also resides in the expertise of its product development staff. For nearly a decade, Biocompatibles' team of scientists, engineers, clinical, quality and regulatory as well as other support staff, have been developing drug eluting polymer systems. This experience is vital, given the complex interaction of sophisticated Combination Products with the many facets of human biology and disease. We also have a team which has considerable experience in dealing with the requirements of the agencies that regulate the marketing of our products.

Strategic Milestones

The Board is measuring the implementation of the Company's plan with strategic milestones, adapted from previous years. These are as follows:

2005	PRECISION establishes our Drug Eluting Bead as a safe and effective treatment for intermediate HCC. We establish the PRECISION IV Randomised Control Trial.
2006	We intend to become the market leader in spherical embolic devices.
2007	Abbott launch the Drug Eluting Stent in the United States.
2008	PRECISION IV shows a survival benefit and our Drug Eluting Bead becomes the global gold standard treatment for Intermediate HCC.

We intend to establish a similar strategic roadmap for CellMed which was acquired in March 2005 as their programmes develop.

The strategic milestones form the basis of the annual goals which are described in the Operational Review.

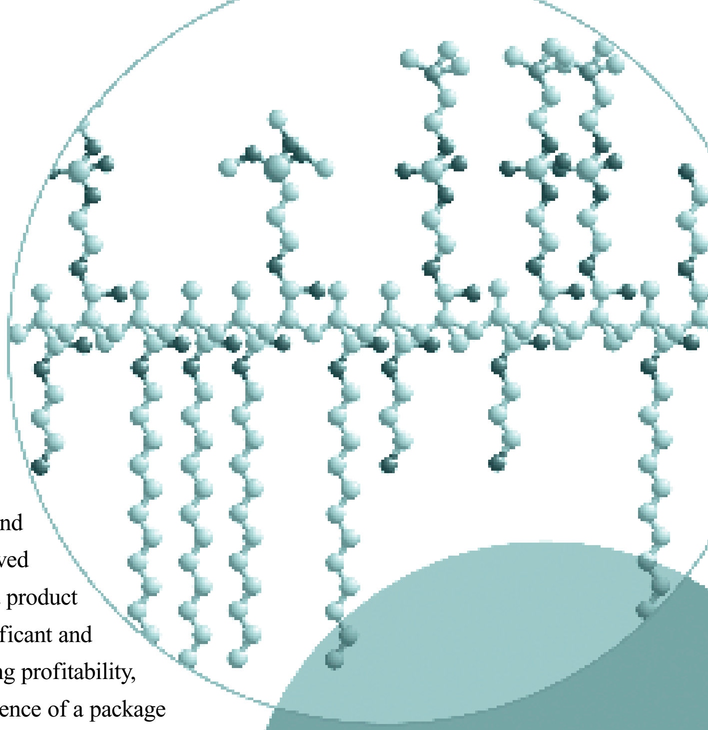
Crystallising Value

The Company's principal objective is to maximise shareholder value and this might be achieved either by growing a product line to deliver significant and sustainable operating profitability, or by the sale or licence of a package of products and technologies. The latter approach was taken in 2002 with the sale of the cardiovascular stent and contact lens businesses, and the subsequent return to shareholders of £111m of capital, with a further £12m to come.

Business Development

In the 2004 Annual Report, the Chief Executive Officer commented that, with the Drug Eluting Bead in clinical trials, the Board had concluded that it was appropriate to narrow the focus of business development on the two key areas identified – medical device and pharmaceutical technologies to support the Company's strategic focus on drug-device combinations; and small investments in sensibly valued medical device programmes that offered the prospect of high value growth without consuming excessive financial or managerial resource.

We were pleased to identify a German medical technology company that met these criteria and we completed the acquisition of CellMed after the year-end. CellMed is described in more detail in the Operational Review.



MOLECULAR STRUCTURE for Phosphorylcholine (PC) Technology central to the drug-eluting stent and licensing programmes

Corporate Governance

The Directors place a high priority on maintaining high standards of corporate governance and rigorous management systems, and the Company is now in compliance with the revised Combined Code on Corporate Governance. Biocompatibles' quality management system incorporates a number of the important provisions, including those relating to risk management and internal control. A fresh approach was adopted during 2004 to the internal control risk review ensuring that, as the Company and its technology evolves, its approach to risk keeps pace at all times.

> "The Drug Eluting Bead is a promising option. Our patients have tolerated the treatment well."
>
> *Dr Ronnie Poon, Associate Professor at the Centre for the Study of Liver Disease, University of Hong Kong.*

The Company's continued accreditation to the ISO 9001 quality standard represents independent verification of the Company's compliance with some of the key elements of corporate governance.

Since 2001, the Company has also held both the FTSE4Good and Investor in People accreditations. The FTSE4Good status symbolises a commitment to high standards of corporate and social responsibility, and Investors in People recognises the Company's dedication to employee development.

INVESTOR IN PEOPLE

FTSE4Good

Board Changes

Ian Ardill's appointment as Finance Director was reported in the 2004 Interim Report.

Outlook

The Company recognises that, in the absence of the traditional business metrics of profitability and cash generation, regular updates on the progress being made with new product programmes are important. The Company made seven such announcements in 2004. Expected newsflow in 2005 includes tumour response data from the PRECISION trials, following the good safety data in 2004; data from Abbott's clinical trial outside the United States as well as the progress of Abbott's planned clinical programme within the United States; and progress towards the release of the escrow account, described in the Finance Director's report.

The Company's programmes are focused on areas of unmet or poorly met clinical needs and the Board remains optimistic about the potential of the programmes to create shareholder value.

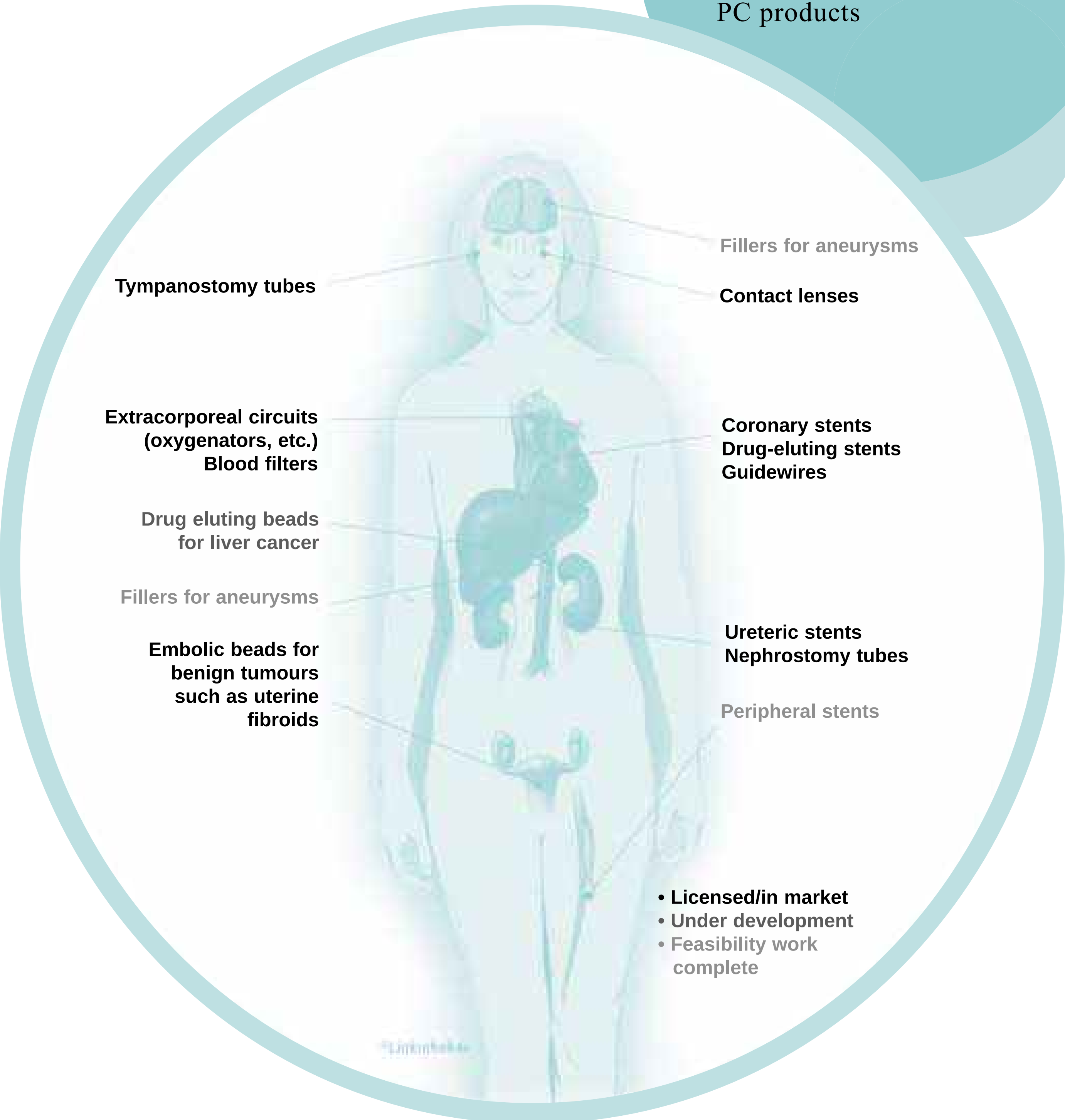
As always, my fellow Directors and I would like to recognise the splendid contribution made by Biocompatibles' employees. It is because of their talent and enthusiasm that the Company remains strong and positioned at the cutting edge of medical technology.

Richard Needham

Sir Richard Needham
Chairman

The Potential of Biocompatibles' Technology

Together, Biocompatibles' proprietary PC Technology and the N-fil technology cover a broad range of medical applications. Leading companies such as Abbott Laboratories and The Cooper Companies market PC products



Biocompatibles had a good year in 2004. In the 2003 Annual Report, the Company established ten items that were planned for announcement during the course of the year. These were largely accomplished.

Commercial Product Lines: Bead Block and PC Licensing

Sales of our Bead Block product, for the embolisation of tumours such as uterine fibroids and liver cancer, continued to grow through our global distribution partner, Terumo Corporation. Sales in the second half fell short of budget with sales in the United States growing at a slower rate than planned. Sales in Europe continued to grow steadily. Bead Block is now used by more than 100 hospitals globally. In 2005 we expect sales growth to increase in the United States as a result of planned growth in the Terumo sales force and the anticipated publication of positive clinical data on Bead Block.

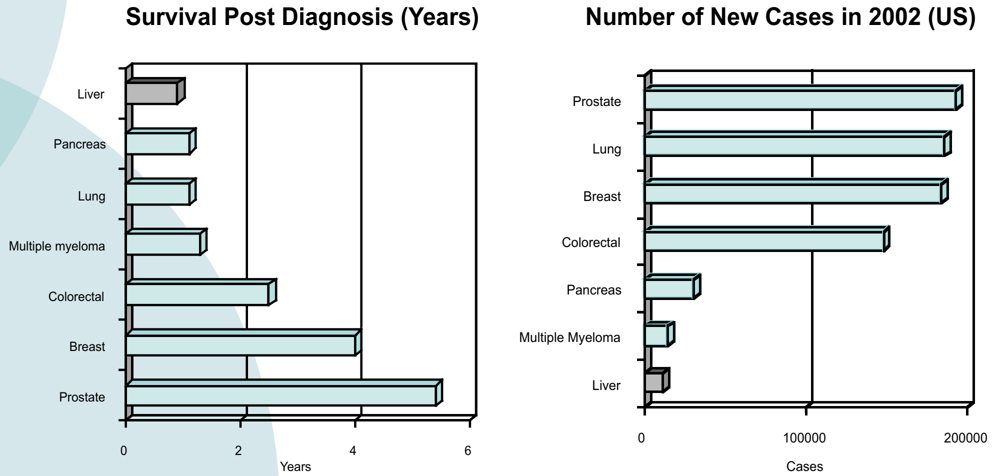
Based on independent market research, we estimate the world market for spherical embolisation products to be worth approximately $22m: $17m in the US where Bead Block has an estimated market share of less than 5% and $5m in Europe where Bead Block has an estimated market share of 20%. We expect continued market share growth for Bead Block in 2005 and expect additional growth following the approval of Drug Eluting Bead product which is expected in 2006.

We estimate the Bead Block market to be growing at 5-10% per annum – largely as a result of growth in the uterine fibroid embolisation procedure. There is not yet widespread adoption of the procedure as an alternative to hysterectomy, but the publicity about the procedure continues to be positive. A new set of guidelines was published by the UK's National Institute for Clinical Excellence in 2004 and news reports on US Secretary of State Dr Condoleeza Rice's fibroid embolisation treatment in the United States further raised the profile of the procedure.

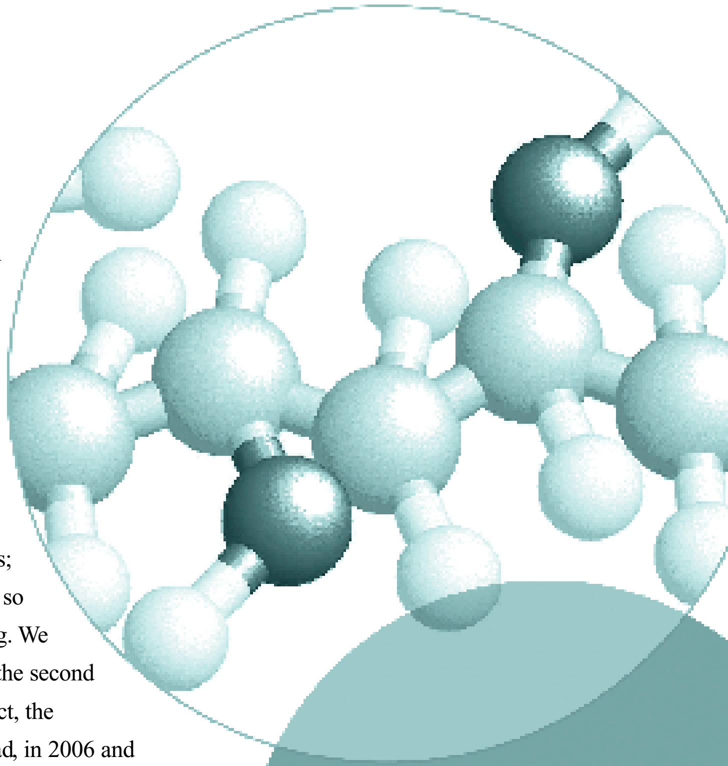
Bead Block manufacturing processes have been validated at Biocompatibles' Farnham facility and product from Farnham is now available for both the European and United States markets. The focus for the Farnham process development team is manufacturing systems for the Drug Eluting Bead products.

Our PC Licensing activities had a satisfactory year – featuring increased demand from Dideco SpA for a PC Technology™ coating for cardio-pulmonary by-pass systems and income from feasibility studies exploring the use of PC coatings on a range of medical devices. The Company signed a letter of intent for a new PC Technology out-licence and studies required for the Licence agreement have continued into 2005.

Cancer: Significant Unmet Needs



Source : Globocan 2002, Biocompatibles' analysis.



PVA MOLECULAR STRUCTURE
for N-fil, the basis of Bead Block and the Drug Eluting Bead

The Pipeline

Implementation of the Drug Eluting Bead programme, which is initially focused on the treatment of primary liver cancer with the Doxorubicin Eluting Bead, continues to make good progress.

On 26 September 2004, the Principal co-investigator of the PRECISION trial, Dr Ronnie Poon, Associate Professor at the Centre for the Study of Liver Disease at the University of Hong Kong, presented positive safety data – showing a statistically significant reduction in the level of circulating doxorubicin in the first 15 patients, low complication rates in the first 30 patients and a positive initial trend in tumour response.

The benchmark for assessing the data from the PRECISION trial is another study conducted in Barcelona with a similar protocol, published in the Lancet in 2002, where a tumour response rate of 35% and a complication rate of 27.5% rate were recorded.

During the course of 2004 the United States Food and Drug Administration (FDA) confirmed that the Drug Eluting Bead is a “Combination Product”, the same designation given to drug eluting stents. We are now in a dialogue with the FDA on their specific requirements for the design of the required clinical trial. We expect to initiate the PRECISION IV clinical trial before the end of 2005. It will be a multi-centre, randomised, controlled trial with endpoints that will include tumour response, survival and quality of life.

The first generation of the Drug Eluting Bead, the DC Bead, has CE Mark approval and, after the year end, we initiated a limited European pre-marketing evaluation with our Bead Block marketing partner, Terumo, and a selection of key doctors. We intend to record results from 100 cases in the pre-marketing evaluation and review them for insight into a number of key factors including physician technique, product utilisation, dosing, clinical indication and pricing. We have already recorded initial product evaluations in a variety of clinical indications including primary liver cancer and liver metastases from neuro-endocrine and colorectal cancers; and the feedback so far is encouraging. We intend to launch the second generation product, the PRECISION Bead, in 2006 and expect to have selected our distribution strategy at that time.

Based on independent market research, we estimate that for the doxorubicin beads only and for the intermediate primary hepatocellular carcinoma (HCC) indication, the initial market opportunity in Europe and the target markets in Asia (China, Korea and Taiwan) to be worth approximately $70m, of which only 20% is conservatively estimated to be in Asia. With positive PRECISION IV data and a US approval, we estimate the market opportunity to be worth up to $400m. There is therefore scope for the market opportunity to be increased to the extent the Doxorubicin Eluting Bead can be used to treat other indications.

Two further Drug Eluting Bead programmes are now in pre-clinical evaluation. A Bead eluting irinotecan will focus on the treatment of colorectal cancer and a Bead eluting ibuprofen will be targeted at pain relief. The most significant application for pain relief is likely to be in fibroid embolisation.

Since the year end, Biocompatibles has acquired CellMed AG, a medical technology company developing medical device and drug delivery products. CellMed’s core biodegradable bead technology complements Biocompatibles’ existing permanent bead

2004 Goals

In early 2004 we set ourselves goals for the year, most of which were achieved.

Review of 2004 Goals

- Completion of recruitment in the PRECISION Drug Eluting Bead trial and first data by year-end
  This goal was partly met – 46 out of the 60 patient target were recruited by year end. The goal of presentation of the first data was met by the presentations at the CIRSE conference.

- Strengthening of the pipeline with two new programmes
  This goal was met - see Operational Review

- Additional clinical trial for the Doxorubicin Eluting Bead
  This goal was met – see Operational Review

- Pre-clinical development for a second Drug Eluting Bead product *This goal was exceeded - see Operational Review*

- Bead Block used in its 100th hospital *This goal was met- see Operational Review*

- Launch of Bead Block in Asia (excluding Japan)
  This goal was not met - product for Asia was shipped but there was limited field activity

- Signing of a new PC Technology licence agreement
  This goal was not met –though a letter of intent for a potentially valuable licence was signed

- Announcement of Drug Eluting Stent trial data from Medtronic *This goal was met – see Operational Review*

- Announcement from Abbott on Drug Eluting Stent trials
  This goal was met – see Operational Review

- Further developments in Isostent litigation
  This goal was met - see Operational Review

products, which are focused on cancer and benign tumours. The acquisition strengthens Biocompatibles' product pipeline and extends the patent portfolio.

Biocompatibles will prioritise three programmes:

- The development of CellMed's biodegradable drug-eluting embolisation bead technology to add to Biocompatibles' drug-eluting bead programme.
- The development of CellMed's tissue transplant bead that is in a Phase 2a trial for the treatment of hypoparathyroidism.
- The commercialisation of CellMed's cosmetic implant bead.

Biocompatibles continues to support the development of Abbott's ZoMaxx Drug Eluting Stent programme, which uses our PC Technology coating in combination with Abbott's proprietary drug, ABT578. In September 2004, Abbott announced the start of ZoMaxx I, a 400-patient prospective randomized clinical trial that will be conducted in more than 30 centres in Europe, Australia and New Zealand. The study compares Abbott's ZoMaxx drug eluting coronary stent to Boston Scientific's market leading Taxus Express drug eluting stent. Analysts estimate the world market for drug eluting stents to have reached \$3.9bn in 2004.

Abbott is reportedly expecting to register the ZoMaxx stent in Europe in 2006 and in 2007 in the US. Biocompatibles will receive a royalty on Abbott's sales of drug eluting stents.

Medtronic announced in May 2004 that its drug eluting stent, ENDEAVOR, was found to be safe and effective 12 months after implantation in a 100-patient Phase I trial (ENDEAVOR I). Medtronic is now recruiting patients in three other trials with more than 2,500 patients and further results are expected during 2005. The Medtronic drug eluting stent also uses PC Technology and ABT578 and Biocompatibles will receive a small royalty on sales of the ENDEAVOR stent.

Intellectual Property

Biocompatibles' patent portfolio continued to grow in 2004 with the filing of four new patent applications, in relation to some of our drug eluting embolic materials. The company obtained five US and four European patent grants during 2004, and two US patents were granted early in 2005. These patents are in relation to new stent coating technology.

Biocompatibles is a world technology leader in the development of Combination Products - medical devices combined with an active pharmaceutical agent. In 2004 we made significant progress with the implementation of our business plan and we are optimistic about the progress we can make in 2005. Our Drug Eluting Bead programme, Abbott's Drug Eluting Stent programme, with which we are partnered, and the development of CellMed under Biocompatibles' ownership, all offer potential for improved products for patients and the doctors that treat them and improvement in the value of our shareholders' investment in Biocompatibles.

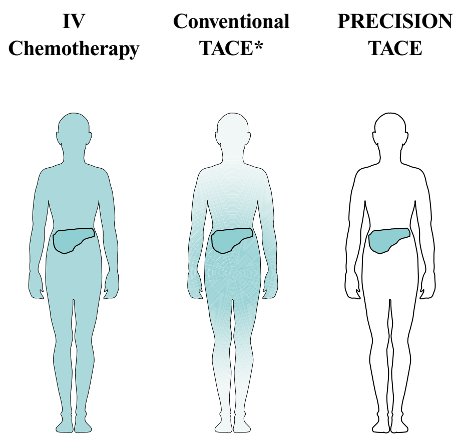
Crispin Simon
Chief Executive

2005 Goals

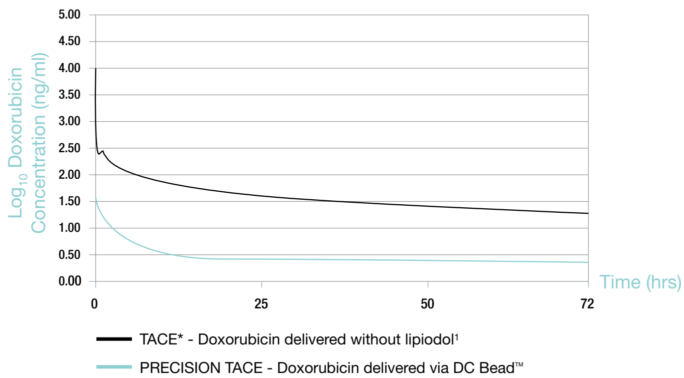
We have set ourselves the following goals for 2005 and will report on their progress through the course of the year.

- Farnham: *Final report from PRECISION I (Asia) (H2).*
- Farnham: *First patient PRECISION IV (H2).*
- Farnham: *100 cases in the DC Bead pre-marketing programme (H2).*
- Farnham: *Filing the CE Mark application for the PRECISION Bead (H2).*
- Farnham: *Abbott's start of US Drug Eluting stent clinical trial.*
- Farnham: *Data from the ZoMaxx I clinical trial.*
- CellMed: *Initiating a pre-clinical trial for a biodegradable drug eluting bead (H2).*
- CellMed: *Completing recruitment in the hypoparathyroidism Phase 2a trial (H2).*
- CellMed: *Securing CE Mark approval for the cosmetic implant bead (H2).*
- Group: *Achieving the sales guidance of £3-4m.*
- Group: *Delivering the year-end cash balance guidance of £35m.*
- Group: *Delivering the Escrow release (H1) and the third return of capital (H2).*

Less Drug in the Bloodstream (1)



Less Drug in the Bloodstream (2)



* Transarterial Chemoembolisation
[1]Johnson et al.

Financial Review

Profit and Loss Account

The loss before tax for the year ended 31 December 2004 was £0.6m, including £4.9m of exceptional profit resulting from the release of provisions related to the 2002 disposals of the Cardiovascular, Eyecare and Urology divisions (2003: profit of £16.0m, which included £21.6m of profit on disposals). As a result of the provision release, the total profit on sale of these divisions is now £76.0m.

Turnover increased by 23% to £2.6m in 2004 (2003: £2.1m) and primarily comprised revenues from Bead Block and PC licensing. Sales growth in 2005 is expected to continue as a result of the increase in the size of the US sales force of Terumo, Biocompatibles' partner for Bead Block, which occurred in the second half of 2004.

Operating expenses, before intangible amortization and exceptional items, increased by 5%, from £8.0m in 2003 to £8.4m in 2004. Selling, marketing and distribution costs increased by 9% to £1.2m (2003: £1.1m) as a result of the continuing support for the Bead Block product and PC Technology out-licensing programme. Research and development costs increased by 15% to £5.3m (2003: £4.6m) due to the investment made in the Bead programmes, including pre-clinical and clinical trials and the set up of the Bead Block manufacturing site in Farnham. These increases were partly funded by reducing general and administrative costs by 17% to £1.9m (2003: £2.3m), as a result of the continuing focus on cost reduction.

Overall, the operating loss decreased from £7.8m in 2003 to £7.6m.

Following the review of the provisions at the year end, the Directors decided that a further provision release of £4.9m was appropriate. The Board believes that the remaining disposal provision balance of £4.1m represents a prudent view of the liabilities associated with the remaining warranties and indemnities given as part of the 2002 disposals of the Cardiovascular, Eyecare and Urology divisions.

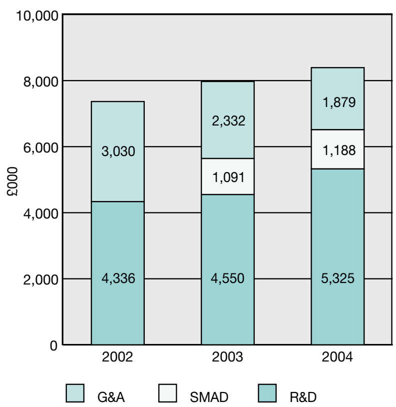
The Group has recognised Research and Development tax credits of £0.5m which are receivable from the Inland Revenue. This is as a result of the Group being classed as a small or medium enterprise (SME) in 2004.

At the year-end, the Group had 74 employees (2003: 69) and the net increase reflects the investment in the Bead programmes being partly offset by a rationalisation of roles in the general and administrative functions.

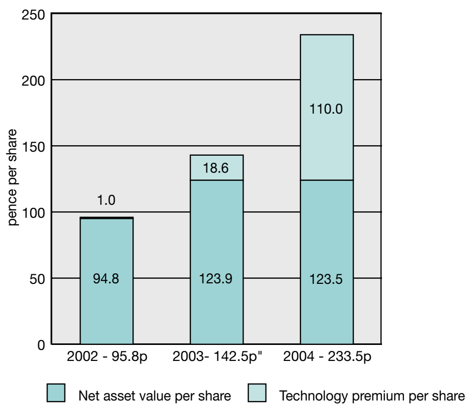
Isostent Lawsuit and Return of Capital

In the civil trial in the Santa Clara County Superior Court for the state of California in relation to the claim by Isostent LLC ("Isostent") against the defendants, LPL Systems and Divysio Solutions ULC Inc., the jury found in favour of the defendants. Isostent has filed several

Continuing operating expenses



Analysis of year end share price



post trial motions, including a request for a new trial and equitable relief for unjust enrichment, but all motions have been denied. Isostent has since exercised its automatic right of appeal to the intermediate appellate court based in San Jose. The appeal process is expected to take six months to a year. If successful, it is likely to result in a new trial. If not, Isostent may appeal to the California Supreme Court.

If the Isostent litigation has not been concluded by 8 May 2005, the Company will seek the release of the £17.6m held in an escrow account, in relation to a number of matters including the Isostent indemnity, under the terms of the agreement between the Company and Abbott for the sale of the Company's Cardiovascular Stent Business to Abbott, subject to the retention of an amount to cover any bona fide claims by Abbott under the Isostent indemnity.

The release of the monies held in the escrow account is a condition for the third of three capital repayments to be made to Biocompatibles' shareholders. The first payment of £100m was made in June 2002. The second payment of £11.3m was made in October 2003. The size of the third payment is expected to be in the region of £12m or approximately 29p/share. Once the escrow is released, the Company will seek High Court approval for the return of capital and expects to make the payment in the third quarter of 2005.

Cash Flow

The net cash outflow from operating activities was £8.5m (2003: £10.3m). Cash outflow relating to acquisitions and disposals (Abbott R&D services agreement and the settlement of warranties and indemnities) was £4.8m (2003: £4.1m). Capital expenditure, net of disposals, was £0.1m (2003: £1.2m). This was offset by net interest received of £2.1m (2003: £2.6m) and proceeds from the issue of share capital for the exercise of employee share options of £1.2m (2003: £0.5m). No return of capital was made in 2004 (2003: £11.3m).

Balance Sheet

Net assets at 31 December 2004 were £48.5m (2003: £47.5m as restated for the adoption of UITF 38). These included net funds of £45.2m (2003: £55.1m) and debtors including funds of £17.6m held in escrow. The total amount remaining due to Abbott in relation to the R&D services agreement was £2.6m (2003: £7.1m). The creditor relating to the royalty prepaid by Abbott decreased from £5.6m to £5.3m in the year due to the recognition of income arising from Abbott's sales of its Dexamet stent.

At the year end, net assets represented 123.5 pence per share. The growth in the share price over the year led to a technology premium of 110.0 pence per share.

CellMed AG Acquisition

On 4 March 2005 the Company announced that it had conditionally agreed to acquire CellMed AG and confirmed that it had completed the acquisition on 7 March. The Company has acquired 97 per cent of the CellMed shares and has the right to acquire the remaining 3 per cent. CellMed is a medical technology company developing medical device and drug delivery products and is both located and incorporated in Germany. CellMed employs 15 people and in the year ended 31 December 2004 recorded a net loss before taxation of £0.8m. Its net liabilities as at 31 December 2004 were £0.1m. The acquisition of CellMed brings new product programmes to the Group and will contribute modest revenues to the Group in 2005.

The consideration is payable in three stages: initial consideration payable on closing, deferred consideration payable in 2006 and profit-sharing payments payable on the receipt of net cash income from CellMed's cell technology up to and including 2010. The initial consideration paid was £3.4m (£2.0m in cash and £1.4m by issue of 573,276 new ordinary shares). The deferred consideration is £3.4m and is payable in two instalments: £0.8m by the issue of 358,295 new ordinary shares on 30 June 2006 and £2.6m

> We are pleased to be joining Biocompatibles. The company has complementary technology and relevant skills to ours – and an excellent track record of generating shareholder value from its product portfolio.
>
> *Dr Peter Geigle, Chief Executive of CellMed*

by the issue of 1,074,890 new ordinary shares on 31 December 2006. The profit-sharing payments are to be made annually at the rate of 10 per cent of the net cash income received by the group from the sales and licensing of products based on CellMed's cell technology, up to a maximum of £8.4m, payable as to 30 per cent in cash and 70 per cent by the issue of up to 2,418,823 new ordinary shares. The maximum consideration payable for CellMed is £15.2m, of which approximately 30 per cent will be satisfied in cash and 70 per cent by the issue of shares.

The Company has the option to sell CellMed back to the vendors for nominal value on 30 June 2006 or on 31 December 2006 in which case the obligations to make future payments of deferred consideration or profit sharing payments would cease.

2005 Cash Expectation

The Group's expectation for 2005 cash outflow is summarised in the following table:

	BII £m	CellMed £m	Acquisition Costs £m	Total £m
Operating cash expenditure	(8)	(2)	–	(10)
Non operating cash flow	(2)	–	(3)	(5)
Abott R&D expenditure	(3)	–	–	(3)
	(13)	(2)	(3)	(18)
Escrow release including accrued interest	20	–	–	20
Return of capital	(12)	–	–	(12)
	(5)	(2)	(3)	(10)

The closing net funds position is expected to be around £27m prior to the anticipated escrow release and subsequent return of capital, or £35m following these events.

Foreign Currency

The Group has a policy of monitoring exchange rate movements in the main currencies in which it trades. Anticipated future foreign currency cash flows are hedged using forward contracts where there is risk of significant adverse exchange rate movements. No speculative transactions are undertaken.

International Financial Reporting Standards

The Company will be required to report its 2005 interim results under International Financial Reporting Standards (IFRS) and has completed a review of its accounting policies to identify changes required under IFRS. The Company has produced a plan to ensure reporting compliance and is currently implementing the steps to ensure such compliance. The Company sees the key areas of change as: segmental reporting (increasing the visibility of operating results), financial instruments (current asset investment revaluations made through reserves until sale or redemption) and share-based awards (charging fair value of share option awards to the profit and loss account).

Ian Ardill

Finance Director

Principal Advisors

Professor William Bonfield
Professor of Medical Materials,
University of Cambridge.

Dr Jordi Bruix
Head of the Barcelona Clinic Liver Cancer Group within the Liver Unit at the Hospital Clinic in Barcelona.

Dr Jeff Geschwind
Associate Professor of Radiology, Surgery and Oncology;
Director of Cardiovascular and Interventional Radiology;
Section Chief, Interventional Radiology;
Director, Interventional Radiology Research at The Johns Hopkins Hospital in Baltimore.

Professor Allan S. Hoffman
Professor of Bioengineering at the University of Washington, Seattle, WA, USA

Professor Philip Johnson
Professor of Oncology & Translational Research; Director of the Clinical Trials Unit; Clinical Head, Cancer Research UK Institute for Cancer Studies; The University of Birmingham.

Professor James Kirkpatrick
Professor and Chairman of Pathology at the Johannes Gutenberg University of Mainz, Germany.

Dr Josep M. Llovet
Associate Professor of Medicine,
Division of Liver Diseases,
Mount Sinai Medical Center, New York.
Senior Researcher, BCLC Group,
Hospital Clinic, Barcelona.

Professor Andrew Lloyd
Professor of Biomedical Materials and Dean of the Faculty of Science and Engineering, University of Brighton.

Professor Paolo Netti
Professor of Biomaterials,
Director of Interdisciplinary Research,
Center on Biomedical Materials,
University 'FEDERICO II' of Naples.

Professor Ronnie Poon
Associate Professor and Assistant Dean in Research Affairs of the Faculty of Medicine Department of Surgery, Queen Mary Hospital, The University of Hong Kong.

Management

The following senior managers, along with the three executive directors on Biocompatibles' Board, make up the Company's Executive Committee. The members combine a broad array of disciplines and experience to provide the vision and leadership of the Company.

Paul Baxter
Director, Intellectual Property
Since joining Biocompatibles in September 1997, Paul Baxter has been responsible for the management of the Company's intellectual property and has supported licensing activities. Paul previously worked with Warwick International Limited for sixteen years managing that company's chemical process development and then as the Information Manager. Prior to that, he spent six years with Glaxo working on the isolation of biological materials such as heparin. Paul has an MBA and is a Fellow of the Royal Society of Chemistry.

Mike Driver
Director of Licensing
Mike Driver joined Biocompatibles in 1990, working initially in the Sight Correction Group and then taking responsibility for the New Technologies Division. More recently, Mike has focused increasingly on business development activities and has been responsible for delivering numerous commercial agreements. Mike is also responsible for all PC licensing programmes, including the collaboration with Abbott. Previously, Mike spent 12 years with Beecham Pharmaceuticals working as a chemist on anti-infectives. He obtained a BSc in chemistry and PhD on the Synthesis of Anti-Tumour Alkaloids from the University of Bath, England.

Andy Lewis
Research & Technology Director
Andy Lewis has been with Biocompatibles since 1996. Following roles in the Cardiovascular Division as Projects Manager and as Head of Chemistry in the Biomaterials Development Group, Andy now directs projects within the Drug Delivery Division and coordinates the external research programmes with academic collaborators. Previously Andy had spent four years with ICI in the area of membrane technology and two years with Johnson & Johnson leading projects in absorbent technologies. He has a BSc in Biochemistry and Chemistry and a PhD in Chemistry.

Tim Maloney
Sales & Marketing Director
Tim Maloney joined Biocompatibles in 1998 as the product manager for the PC-coated BiodivYsio coronary stent range. Tim now works on the embolisation product range focused on the sales and marketing of Bead Block. Prior to joining Biocompatibles, Tim spent three years with BARD in sales and marketing roles. Tim has a BA in History and a BA in Philosophy from Holy Cross in the United States.

Alistair Taylor
Director of Clinical and Regulatory Affairs
Alistair Taylor joined Biocompatibles in 1992, working initially in the Coatings Group and joining the management team of the Cardiovascular Division at its creation in 1993. He currently works on regulatory affairs activities for all programmes within the Group. Previously, Alistair spent 11 years with British Petroleum working as a chemist on enhanced oil recovery. He obtained a BSc in Applied Chemistry, an MSc in Colloid and Interface Science and a PhD on the Behaviour of Artificial Tears on the Human Cornea from the University of Strathclyde, Scotland.

Geoff Tompsett
Director of IT and HR
Geoff Tompsett joined the Company in January 2001 as IT Director, responsible for Information Technology globally within Biocompatibles. In February 2003, he additionally took on the role of HR Director. Geoff is an experienced strategic and operational manager, predominantly in the pharmaceutical and healthcare industry. His current project portfolio includes supply chain responsibility. He joined Biocompatibles from the French pharmaceutical company, Sanofi-Synthelabo.

Board of Directors

The Rt. Hon. Sir Richard Needham
Chairman and Non-Executive Director
Richard Needham joined the Board as Chairman on 6 July 2000. He was a Member of Parliament (United Kingdom) between 1979 and 1997, serving as a Minister in Northern Ireland (1985-1992) and at the Department of Trade (1992-1995). He is currently a non-executive director of Dyson Appliances Limited and Vice Chairman of NEC (Europe) Limited. Age 63.

Crispin Simon
Chief Executive
Crispin Simon joined the Company in June 1998. After working at NM Rothschild and McKinsey & Company, he gained general management experience at senior executive level with Rexam plc (then Bowater) and then as President of the Endoscopy Division of Smith & Nephew plc, based in Boston, USA. Age 47.

Jeremy Curnock Cook
Independent Non-Executive Director
Jeremy Curnock Cook joined the Board in 1990. He is Executive Chairman of Bioscience Managers Limited, an investment advisory company to the biotechnology industry. He served as Managing Director of the Rothschild Bioscience Unit from 1987 until his retirement in 2000. Other directorships include: Chairman of Targeted Genetics Inc. (USA) and Atugen AG (Germany), and director of Bioscience Managers Limited, Q Chip Limited, Inflazyme Pharmaceuticals (Canada), Sirna Therapeutics (USA), Intersuisse Bioscience Managers Pty. (Aus.) and Bioscience Managers Limited (Canada). Age 55.

David Hankinson
Senior Independent Non-Executive Director
David Hankinson joined the Board as a Non-Executive Director in September 1997. He is Chairman of Premier High Income Trust plc and a non-executive director of Choice Hotels Europe plc. He was previously Finance Director of a number of listed companies including Rover Group plc, Lucas Industries plc and Fisons plc. Age 65.

Ian Ardill
Finance Director & Company Secretary
Ian Ardill, appointed to the Board in October 2004, joined Biocompatibles in January 2003 having spent the previous five years working for Novartis Pharmaceuticals in a variety of financial positions covering Financial Accounting, Systems Implementation, and Treasury. Prior to that, he worked for Letheby & Christopher, a subsidiary of Compass Group PLC; NHA International, a sales and management consultancy; and qualified as an accountant with Grant Thornton. He has a BSc in Accounting and Financial Analysis from Warwick University, England. Age 38.

Peter Stratford
Managing Director, Drug Delivery
Peter Stratford was appointed to the Board in September 2002. Peter joined Biocompatibles in January 1990. After completion of development work in contact lens application, he joined the management team of the Cardiovascular Division at its creation in 1993. He took the role of Group Director Research and Development in 1998 and has since transitioned the group to the current drug delivery focus. Peter has a BSc in Chemistry, a MSc in Polymer Synthesis and a PhD in Pharmaceutical Synthesis. Age 41.

Directors' Report

for the year ended 31 December 2004

The Directors present their annual report on the affairs of the Group to the shareholders, together with the audited financial statements for the year ended 31 December 2004.

PRINCIPAL ACTIVITIES AND REVIEW OF BUSINESS

The Chairman's Statement, the Operational Review and the Financial Review together contain details of the principal activities and development of the business of the Company during the year and likely future developments.

EARNINGS AND DIVIDENDS

The loss for the financial year of £139,000 (2003: profit £16,022,000) has been taken to reserves. The Directors do not recommend the payment of a dividend.

DIRECTORS

Names and biographies of the current directors are detailed on page 14. Swag Mukerji resigned on 15 October 2004 and Ian Ardill was appointed as a director on the same date.

DIRECTORS' INTERESTS

The interests of the directors in the 19 $\frac{4}{99}$p ordinary shares of the Company at 31 December 2004 and 31 December 2003 or upon appointment were as follows:

	Shares 25 April 2005	Shares 31 December 2004	Shares 31 December 2003	Options 31 December 2004	Options 31 December 2003
I Ardill	–	–	–	125,000	50,000
(appointed 15.10.04)					
J Curnock Cook	11,452	11,452	11,452	–	–
D Hankinson	4,542	4,542	4,542	–	–
S Mukerji		9,391	9,391	–	350,000
(resigned 15.10.04)					
R Needham	19,586	19,586	15,786	–	–
C Simon	110,077	110,077	94,077	1,033,220	973,220
P Stratford	26,853	26,853	2,803	172,588	258,944

None of the directors at any time during the year ended 31 December 2004 had any material interests in any contracts with the Company or any of its subsidiaries. None of the directors at any time during the year ended 31 December 2004 or subsequent to 31 December 2004 held any debentures of the Company or shares or debentures of the Company's subsidiaries. Details of options granted and exercised by the directors in the financial year are set out on page 30.

The executive directors, together with all employees of the Group, are potential beneficiaries of the Company's Employee Share Ownership Plan and are therefore interested in 127,753 ordinary shares held in Trust at 31 December 2004.

SUBSTANTIAL SHAREHOLDINGS

As at 25 April 2005 the Company has been notified, in accordance with sections 198 to 208 of the Companies Act 1985 (or are otherwise aware) of the following interests in 3% or more of the ordinary share capital of the Company.

	Shareholding	%
Hunter Hall Investment Management Limited	4,302,448	10.77
Aberforth Smaller Companies Trust plc	2,457,754	6.15
Legal & General Investment Management	2,000,374	5.00
The Contra Fund Limited	1,640,795	4.10
Invesco English and International Trust plc	1,400,000	3.50

RESEARCH AND DEVELOPMENT

The Group is committed to research and development activities in order to develop its business. Costs of £5,325,000 (2003: £4,550,000) have been charged to the profit and loss account in the year. Details of the Group's research and development activities are contained on pages 6 to 9.

DONATIONS

The Group's charitable donation policy is to match the fundraising activities of its employees. The Group's Charity Team identified local children's and science-based charities to support in 2004 and organised events in which all employees participated. In 2004 total charitable donations were £7,430 (2003: £2,454). No donations were made to political parties.

EMPLOYEES

Biocompatibles' people are fundamental to the success of the business. Their skills and intellect are vital components in the successful implementation of the Group's business strategy. An effective human resource policy drives the Group's ability to attract and retain high calibre people.

The Group is committed to a working environment of mutual trust and respect where each individual is responsible for the performance and reputation of the Group. A system of open and transparent communication is considered of paramount importance and the Group consults its employees on matters likely to affect their interests. Information and progress updates are provided in a number of ways including regular monthly all-employee briefings, notice boards and other communication channels, promoting a common awareness of the Group's business performance.

The Board places considerable emphasis on the development and motivation of its employees to enable them to fulfil their potential for the benefit of both themselves and the Group. Accreditation as an "Investor in People", the National Standard which sets a level of good practice for improving organisations' performance through its people, demonstrates such commitment. All employees undergo an induction programme, have a bi-annual review that has a clear focus on their development and a system of internal promotion is encouraged.

Biocompatibles is committed to human resource policies free from discrimination against potential or existing staff on the grounds of age, gender, race, nationality, faith, sexual orientation or disability. The Group promotes a policy of recruiting talented and committed people with a positive attitude and sense of urgency.

HEALTH, SAFETY AND ENVIRONMENT POLICY

Summary

Human health, safety and impact upon the environment are considered when the Group conducts its business. It is the Group's aim to provide a safe working environment for employees at all times. We operate in a socially and environmentally responsible manner, proactively seeking ways of reducing any adverse impact upon our surroundings through recycling schemes, making more efficient use of utilities and seeking ways to reduce waste.

Organisation and Responsibility

The Environmental Committee is responsible for implementing the Group's policy on environmental issues and for monitoring environmental performance. The Committee includes at least one member of the Executive Committee, who reports to the Chief Executive on environmental matters. The Chief Executive is the Board member with responsibility for environmental matters. The Environmental Committee reports formally to the Board at least once each year.

Communication

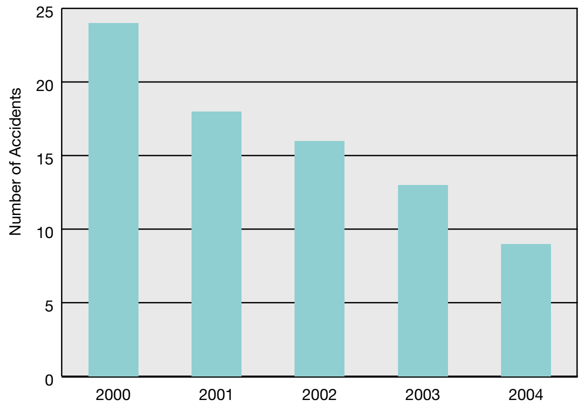
Environmental performance is reported to shareholders in the annual report and to staff through internal communication channels, such as induction, Biocom (internal communications forum), and through notice boards. The Group reports environmental policy and performance through agencies such as EIRIS and will strive to maintain membership of the FTSE4Good index.

HEALTH, SAFETY AND ENVIRONMENT PERFORMANCE

Health and Safety Performance

The Group monitors its health and safety performance to aid the provision of a safe place of work for staff and visitors. The total number of accidents continues to decline. The Group's Safety Committee meets monthly and publishes the minutes of meetings for staff information. The Safety Committee conducts safety audits and reviews Health and Safety practices. The Group benefits from advice from a retained Occupational Health Consultancy service and membership of the British Safety Council.

The chart below shows the number of accidents per year over the last five years. During 2004 there were 0.6 accidents (2003: 1 accident) per 10,000 hours worked and the accidents were very minor in nature. There were no notifications under the Reporting of Injuries, Disease and Dangerous Occurrences Regulations.



Environmental Performance

The Group monitors its usage of gas and electricity and evaluates opportunities to reduce the amount of energy used. The target for energy usage is that used in the baseline year, 2000. Waste generation is also monitored and consideration is given to the use of recycling schemes to lessen the impact of this waste upon the environment. Biocompatibles recycles waste paper and card, plastic cups, toner cartridges, mobile telephones and aluminium cans and makes use of recycled materials. We consider methods of increasing the amount of waste that is recycled. Risk assessments are completed for all controlled procedures and the possible impact upon the environment is considered as part of this assessment. We audit our major suppliers regarding their environmental policy. The Company is committed to continual improvement and undertakes environmental and energy audits as tools to aid environmental performance.

Key data for 2004, compared with previous years, is shown below. There was a 4% increase in electricity usage in 2004 compared with 2003, largely due to the installation of a new Cleanroom during the year, but gas consumption was reduced by 9%. In 2004, the Group's focus on improvement in environmental performance has been on the recycling of paper and this focus will continue over the coming years. Over the year, 47% of paper was recycled and a target of 70% has been set to be achieved by 2006.

	2001	2002	2003	2004
Electricity (kWh)	761,000	680,000	762,000	792,000
Gas (kWh)	393,000	383,000	350,000	317,000
Total (kGJ)	4.15	3.83	4.00	3.99
C02 equivalent (tonnes)	402	365	394	401

All figures relate to continuing activities.

Waste disposal data for the past three years are reported below:

	2002	2003	2004
Liquid hazardous waste (l)	4,761	3,300	2,600
Solid chemical waste (kg)	21	30	57
Recycled paper (kg)	3,260	4,170	4,600
Percentage paper recycled (%)	n/a	n/a	47

CREDITOR PAYMENT POLICY

The Group's payment policy is to negotiate terms with its suppliers at the time they are engaged and to abide by the terms agreed. The Group's average creditor payment period at 31 December 2004 was 30 days (2003: 30 days).

POST BALANCE SHEET EVENT

On 7 March 2005, the Company completed the purchase of CellMed AG, for a total maximum consideration of £15.2m. CellMed is a medical technology company developing medical device and drug delivery products and is located and incorporated in Germany. For further details on the CellMed acquisition, refer to the Operational and Financial reviews on pages 6 to 12.

AUDITORS

A resolution to reappoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the Annual General Meeting.

ANNUAL GENERAL MEETING

Notice of the 2005 Annual General Meeting and the Chairman's letter setting out explanations for the Resolutions to be proposed are given in a separate notice to shareholders.

By order of the Board

Ian Ardill
Company Secretary
25 April 2005

Statement of Directors' Responsibilities

for the year ended 31 December 2004

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that year.

In preparing those financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently.
- make judgments and estimates that are reasonable and prudent.
- state whether applicable 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 Group will continue in business.

The Directors confirm that they have complied with the above requirements in preparing the financial statements.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and the Group 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 the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The maintenance and integrity of the Biocompatibles' website is the responsibility of the Directors. The work carried out by the Auditors does not involve consideration of these matters and, accordingly, the Auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the UK governing the preparation and dissemination of the financial statements may differ from legislation in other jurisdictions.

By order of the Board

Ian Ardill

Company Secretary

25 April 2005

Independent Auditors' Report to the Members of Biocompatibles International Plc

We have audited the financial statements which comprise the consolidated profit and loss account, the balance sheets, the consolidated cash flow statement, the statement of total recognised gains and losses, the reconciliation of movements in Group shareholders' funds, and the related notes. We have also audited the disclosures required by Part 3 of Schedule 7A to the Companies Act 1985 contained in the directors' report on remuneration ("the auditable part").

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 are set out in the statement of directors' responsibilities. The directors are also responsible for preparing the directors' report on remuneration

Our responsibility is to audit the financial statements and the auditable part of the directors' report on remuneration in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the auditable part of the directors report on remuneration have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report, the unaudited part of the directors' report on remuneration, the chairman's statement, the operational review, the financial review and the corporate governance statement.
We review whether the corporate governance statement reflects the company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

Basis of audit opinion
We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the auditable part of the directors' remuneration report. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

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

Opinion
In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and Group at 31 December 2004 and of its loss and cash flows of the group for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- those parts of the directors' report on remuneration required by Part 3 of Schedule 7A to the Companies Act 1985 have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
West London
25 April 2005

Biocompatibles is committed to upholding the principles of corporate governance as part of its policy to achieve best practice in standards of business integrity. This section of the annual report and the Report on Directors' Remuneration on pages 26 to 31 describe how the Company has applied the principles set out in the Combined Code on Corporate Governance published in July 2003 (the "revised Code") and the related guidelines produced by Derek Higgs and Sir Robert Smith. The Company undertook to implement in full the provisions of the revised Code during the year and was pleased to report full compliance at the time of the publication of the 2004 interim report.

Compliance with the Combined Code

The Board confirms that, since September 2004, the Company has been in compliance with the requirements of Section 1 of the revised Code.

BOARD AND BOARD COMMITTEES

Board

The Company is controlled through its Board of Directors. The Board is responsible to shareholders for providing entrepreneurial leadership within a framework of controls for managing risk. It approves the Company's strategic objectives and ensures that the necessary financial and other resources are made available to meet those objectives.

The Board, which met on ten occasions during the year, has a schedule of matters reserved for its approval (available on the Company's website: www.biocompatibles.com) including: the Company's strategy and the annual budget, the full year and half-year accounts, acquisitions and disposals and other major capital or operational expenditure. The Board reviews the Company's system of financial control and risk management, ensures health, safety and environmental performance, approves appointments to the Board and to the position of Company Secretary, and ensures that a dialogue takes place with shareholders. A comprehensive set of papers is provided to each director in advance of each Board meeting.

The Board currently comprises three executive directors and three non-executive directors. The non-executive directors of the Company bring a wide range of experience and expertise to the Company's affairs and they carry significant weight in the Board's decisions. The directors' names and biographies are set out on page 14.

The Board delegates defined responsibilities in relation to specific projects to Board Committees. In addition, there is frequent contact between directors outside the formal meetings. The annual schedule of meetings includes meetings of the non-executive directors without the executive directors being present as well as a meeting between the Senior Independent Director and the other non-executive director without the Chairman being present.

The attendance of individual directors at scheduled meetings of the Board and at meetings of the Audit, Nomination and Remuneration Committees during the year is set out in the table below. In June 2004 Sir Richard Needham resigned from the Audit and Remuneration Committees to comply with the revised Code's requirement that the Committees consist solely of independent directors. On 15 October 2004, Swag Mukerji resigned as Finance Director and the Board appointed Ian Ardill to the position from his previous role as Financial Controller and Company Secretary.

	Board		Audit Committee		Nomination Committee		Remuneration Committee	
R Needham	10	**10**	2	**2**	3	**3**	3	**3**
D Hankinson	10	**10**	4	**4**	3	**3**	6	**6**
J Curnock Cook	10	**10**	4	**4**	3	**3**	6	**6**
C Simon	10	**10**		–		–		–
S Mukerji	6	**8**		–		–		–
P Stratford	10	**10**		–		–		–
I Ardill	2	**2**		–		–		–

Figures in bold indicate the maximum number of meetings in the period in which the individual was a Board or Committee member.

The directors have access to the advice and services of the Company Secretary, who is responsible to the Board for ensuring that Board procedures, corporate governance and compliance, and applicable regulations under the Company's Articles of Association or otherwise are complied with. In addition, the Board has a procedure for directors, in furtherance of their duties, to take independent professional advice at the Company's expense, when the directors deem it is necessary.

The Company provides comprehensive induction training for all new directors on appointment at which they receive information on the Company, the role of the Board and the matters reserved for its decision, the terms of reference and membership of the Board and Executive Committees and corporate governance practices and procedures. Throughout their period in office the directors receive briefings from senior management executives on developments within the Company and its markets through regular presentations at Board meetings. In addition, the directors receive the Monthly Management Report which includes a full set of financial reports and updates on all key areas of the business. All directors are invited to attend the annual management conference at which they receive a detailed overview of business activities and strategy implementation. During the 2004 financial year the Board adopted new practices which brought the Company into full compliance with the revised Code by September 2004.

The Board has established a formal process, led by the Chairman, for the annual performance evaluation of the Board, its Committees and individual Board members. A series of questionnaires was used to provide a framework for the evaluation process. There were five questionnaires in total, one for each of the Board, the individual directors, the Remuneration, Audit and Nomination Committees. The responses to these questionnaires were analysed, discussed and required actions were captured for later implementation.

The Chairman conducts the annual performance evaluation process using the questionnaires as the basis of the assessment of each of the non-executive directors, taking into account the views of the other directors. The non-executive directors, led by the Senior Independent Director, conduct the annual performance evaluation of the Chairman, taking into account the views of the executive directors. The Chairman assessed the performance of the Chief Executive by means of the Company's formal Performance and Development Review process. The Chief Executive reviewed the performance and effectiveness of the executive directors and members of the Executive Committee who report directly to him. The results of the reviews performed by the Chief Executive were also discussed with the non-executive directors. The results of these reviews drive training and development plans for the individuals concerned.

The Role of the Chairman and Chief Executive

Sir Richard Needham is Chairman of the Company and Crispin Simon is the Chief Executive, each with clearly defined responsibilities.

The Chairman

The Chairman leads the Board in the determination of its strategy and in the achievement of its objectives. The Chairman is responsible for organising the business of the Board, ensuring its effectiveness and setting its agenda. The Chairman has no involvement in the day-to-day management of the Company. The Chairman facilitates the effective contribution of non-executive directors and constructive relations between executive and non-executive directors, ensures directors receive accurate, timely and clear information and that effective communication occurs with institutional shareholders. The Chairman's professional commitments are included in his biography on page 14. The Chairman serves on a number of Boards but the Board is satisfied that these do not interfere with the effective performance of his duties as Chairman of the Company.

Senior Independent Director

David Hankinson is the Senior Independent Director. He is available to meet shareholders on request and to ensure that the Board is aware of shareholder concerns not resolved through the normal channels of communication of the Chairman, Chief Executive and Finance Director.

Independence

The Board considers that Sir Richard Needham, David Hankinson, and Jeremy Curnock Cook are independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgment although it recognises that under the revised Code, the Chairman is not considered to be independent.

Jeremy Curnock Cook has served three terms as a non-executive director and under the terms of the revised Code is required to seek re-election annually. The Board is pleased that he has indicated his willingness to stand for re-election at the 2005 Annual General Meeting. The Board considers Jeremy Curnock Cook to be independent because, during his tenure as a non-executive director, the composition of the Board and executive management has changed significantly. Jeremy Curnock Cook brings to the Board a wealth of knowledge and experience and his deep understanding of the industry enables him to make significant constructive and critical contributions to the Board and its Committees. The Board is of the opinion that Jeremy Curnock Cook continues to act in an independent capacity and therefore recommends his re-appointment.

Any director appointed during the year is required, under the provisions of the Company's Articles of Association, to seek election by shareholders at the next Annual General Meeting (AGM). The Articles also require that each director retires once every three years.

Board Committees

The Board Committees, which are comprised solely of non-executive directors, operate within clearly defined terms of reference and report regularly to the Board. The Committees are as follows:

Nomination Committee

The members of the Nomination Committee are Sir Richard Needham (Chairman), Jeremy Curnock Cook and David Hankinson.

The Committee is responsible for the process of the nomination, selection, training and evaluation of directors and of executive succession planning. Its aim is to appoint directors who have the experience and track record to make a significant contribution. When considering an appointment, the Committee will work with the Board and the Director of Human Resources, as necessary, to prepare a formal job specification and an assessment of the anticipated time commitment. The Committee, in recommending appointments to the Board, considers the balance of membership of non-executive and executive directors and the blend of skills and experience of existing directors and prospective candidates. The Chairman would not chair the Committee when it is dealing with the appointment of a successor to the chairmanship. The Committee typically uses external search consultants to identify prospective candidates and seeks the opinions of all directors on new appointments. The recommendations of the Committee are ultimately made to the Board for consideration prior to any appointment being made. The Committee met three times during the year and all members attended each meeting. The terms of reference for the Committee can be found on the Company's website.

Remuneration Committee

The members of the Remuneration Committee are Jeremy Curnock Cook (Chairman) and David Hankinson. Sir Richard Needham resigned from the Committee in June in compliance with the independence criterion of the revised Code. Details of the activities undertaken by this Committee are provided in the Directors' Report on Remuneration on pages 26 to 31.

The Committee has written terms of reference setting out its authority and duties which can be found on the Company's website. The Committee met on six occasions during the year and the attendance at each meeting is set out in the table on page 20.

No executive director serves as a director on any board of directors outside the Group.

Audit Committee

The members of the Audit Committee are David Hankinson (Chairman) and Jeremy Curnock Cook. Sir Richard Needham resigned from the Committee in June in compliance with the independence criterion of the revised Code. David Hankinson, who is considered by the Board to have recent and relevant financial experience, chairs the Committee. The Committee met four times during the year and has written terms of reference dealing with its authority and duties, which are available on the Company's website. The external auditors, Finance Director and Financial Controller attend the meetings by invitation. The Committee met with the external auditors on one occasion without finance management present. Attendance at each meeting of the Committee was as shown in the table on page 20.

The remit of the Committee is to review the effectiveness of the Company's system of internal controls, including financial, operational and compliance controls and of risk management; to agree the appointment or removal of auditors and the scope of their duties; and to review the half-year and full-year results prior to their approval by the Board. The Committee undertakes an annual review of the performance of the external auditors, monitoring the nature and extent of non-audit work which they undertake, thereby ensuring that their objectivity and independence are not compromised. The split between audit and non-audit fees for the year under review appears on page 40. Any significant non-audit work is put out to tender and awarded on the basis of cost, efficiency and quality.

The Committee has a procedure whereby employees may, in confidence, notify management or the non-executive directors of any concerns regarding suspected financial impropriety, fraud or other wrongdoing. Upon being made aware of such circumstances, the Committee would promptly undertake a thorough investigation and ensure that any concerns are properly resolved.

MANAGEMENT SYSTEM

Executive Committee

This Committee is made up of the three executive directors and six senior executives whose biographies appear on page 13. The Committee is chaired by the Chief Executive, meets monthly and has formal terms of reference laid down by the Board which are available on the Company's website. The Committee has responsibility for the day-to-day management of the Group's activities, the implementation of the Company's strategy approved by the Board, monitoring the performance of the business, the instigation of any necessary corrective actions and the development of the Group's strategy and preparation of the budget for Board approval.

Management Structure

The organisational structure of the Group ensures that there are clear lines of responsibility and that authority is delegated to managers, who are accountable to the Chief Executive and the other members of the Executive Committee and the Board.

Quality System

The Company is committed to the highest standards of business conduct. Each employee, upon joining, undergoes a thorough induction programme and receives a staff handbook and a copy of "The Guide", a manual that covers the Company's management system, the key business processes and the Company's quality improvement tools. The Company also has a comprehensive quality system in place, and complies with ISO9001 and the updated standard ISO13485:2003. ISO9001 is an internationally recognised standard that is independently audited. ISO13485 sets out the requirements for the application of ISO9001 to medical device companies. There is comprehensive training on compliance with the quality system for each employee.

The quality control system consists of a policy manual and control procedures covering business planning processes, technical methods and equipment operating procedures.

Performance Review

The Board receives reports from senior management at regular intervals assessing the performance of the operations against key performance indicators. Reports are also made on the status of each programme, market trends, competitor activity and intellectual property. This information helps to identify control issues and other business risks. This information is collated into the Monthly Management Report.

Information and Communication

The Company undertakes an annual strategic review and the Board also reviews presentations made by senior management for each key area of the business including updates on human resources, intellectual property, health and safety, environment, tax and insurance matters. Treasury matters are reported to the Board at every meeting.

Monitoring and Corrective Action

The Board monitors the system of internal control through the processes outlined above, and in addition:

Finance:

The Audit Committee meets with the external auditor to review any control issues highlighted through the annual audit process. A statutory external audit is performed at the year-end with a review at the half year.

Quality:

The Company conducts internal audits to monitor the compliance of its quality system with ISO9001 and ISO13485. Management undertakes an annual review of the quality system.

RISK AND CONTROL

The directors confirm that the Company has implemented the guidelines on the management and control of risk issued by the Turnbull Committee. The Board undertakes an annual review of internal controls which extends to all financial and operational controls as well as compliance controls and risk management. The Board has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. The system is designed to identify and manage the risks of failure to achieve business objectives rather than eliminate them, and can only provide reasonable and not absolute assurance against material misstatement or loss.

Review and Management of Risk

The Company's risk assessment of management, financial, strategic, legal, intellectual property, business programme and general risks, is the subject of annual Board review and approval, based on the input of the Audit Committee.

During 2004 the Board instigated a full and detailed internal review of risk across the whole business. Senior managers in the finance and research & development departments, below the Executive Committee level, led the project with input from operational and functional areas of the Group. The review covered sales and marketing; manufacturing; research and development; clinical, quality and regulatory affairs; intellectual property; IT systems; corporate and financial functions; health, safety and environmental matters. As part of the review, risks were identified, categorised by reference to level of importance and probability and steps to mitigate such risks were discussed and remedial measures put in place. The risk management paper was reviewed by the Executive Committee and presented to the Audit Committee before the paper was considered and approved by the Board. The Executive Committee is responsible for reviewing risk management procedures throughout the year and for managing the risks faced by the Group. The Audit Committee is responsible for reviewing the effectiveness of the Group's internal control policies and procedures for identifying, assessing and reporting risks. The Board is responsible for ensuring the Group maintains a sound system of internal control and risk management. The risk review is incorporated within the Company's Quality system and is therefore subject to independent audit.

Internal Controls
The Group has financial control procedures that are designed to ensure complete and accurate recording of financial transactions which limits the potential exposure to loss of assets or fraud and ensures adherence to good business practices. Particular attention is paid to the control of research and development expenditure and the performance of the treasury function. Measures taken include comprehensive authorisation approvals, physical controls to safeguard assets, segregation of duties, management and Board review and external audits. The approvals required for any level of capital and revenue expenditure are documented and made known to employees.

The Board does not consider it to be necessary for the Company to have a separate internal audit function due to the Company's current size and relatively straightforward organisational and operational structure.

Social, Environmental and Ethical
The Group has adopted a formal statement with regard to its approach to social, environmental and ethical issues whereby the Group and its employees embrace the responsibility inherent in supplying healthcare products. The Group and its employees undertake to comply with all legal and regulatory requirements and show personal integrity in dealings with each other and the outside world. The Group works to reduce any adverse impact of its business on the environment and provide a safe working environment for its employees. Further, the Group seeks to minimise the use of pre-clinical trials and to present clinical data with due regard for statistical significance.

A separate report on Environmental Policy and Performance is included on pages 16 and 17.

Treasury Management
The Group uses professional fund managers to invest the Group's liquid assets in the short-term money and bond markets. All investment transactions are governed by the Group's investment policy, which is periodically reviewed by the Board.

Management performed a review of the treasury function in 2003 and improved controls and procedures, including: the establishment of a detailed treasury policy covering financial risks and approved financial instruments, the formalisation of the dealing process and the creation of formal job descriptions for staff involved in the treasury function. Further enhancements to treasury controls have been made in 2004; in particular, the reporting of treasury performance, the implementation of a short-term cash flow forecast and the development of a foreign currency hedging policy.

SHAREHOLDERS

Relations with Shareholders
The Directors place great importance on maintaining clear, accurate and timely communications with both institutional and private investors. The Chief Executive has responsibility for day-to-day investor relations. The Chief Executive and the Finance Director meet regularly with the Company's institutional shareholders and report their views back to the full Board. During 2004, the Company initiated a project to increase communication with non-institutional investors through private-client brokers. The Company has adopted a policy of consulting with its major shareholders in advance on matters which would be referred to an Extraordinary General Meeting. In March 2005 the Chairman of the Remuneration Committee wrote to all major shareholders to inform them of the Company's proposals for new share incentive plans outlined within the Directors' Report on Remuneration on page 27 and in the letter from the Chairman incorporated in the Notice of Annual General Meeting.

Annual General Meeting

The Company welcomes the opportunity, presented by the AGM, to meet with individual private shareholders. The Chief Executive makes a presentation on the Company's business and strategy and there is an opportunity to ask questions on these topics. Shareholders also have an opportunity to talk informally with the directors both before and after the AGM. The proxy votes for and against each resolution, as well as those withheld, are counted before the AGM and the results are made available at the meeting.

Annual and Interim Reports

Each shareholder receives a copy of the interim report and annual report, which includes an operational and a financial review.

Company Website

The Company's website is an important channel for communication with shareholders. The annual and interim reports and press releases are made available on the website. There is also information on the Group and its products which is updated regularly. The Company's website is www.biocompatibles.com and shareholders can register to receive the Company's press announcements by email when they are released.

CORPORATE AND SOCIAL RESPONSIBILITY

The Company Statement describes the way in which the Company seeks to make a positive impact on its stakeholders. All employees receive training on the Company Statement and performance against Corporate and Social Responsibility (CSR) goals is monitored through the management system. Examples of measures that relate to CSR goals include customer satisfaction measures such as delivery and product quality performance; the results of quality audits designed to improve the capability of key suppliers; information sharing, and reward and recognition systems for employees; delivery of growth in the value of shareholders' investments; a policy for the environment with a commitment to a reduction in the use of non-renewable energy and an increase in the use of recycling; and targeted levels of charitable fundraising by employees matched or exceeded by the Company.

In 2004 the Biocompatibles' Charities Team raised over £12,000, including Company donations, for charitable projects within the local community. The recipients included a local hospice for children with life-threatening illnesses, a special school for children with severe learning needs, and financial support to a science based learning tool operated in local junior schools. In addition, the Company supported individual employees in their more specific fund raising efforts. The charitable projects for 2005 continue this support for the local community adopting a science and children's focus.

In evidence of its focus on such issues, the Company has retained its membership of the FTSE4Good index which is comprised of companies that meet globally recognised standards of corporate and social responsibility.

GOING CONCERN

The financial statements have been prepared on a going concern basis. This assumes that the Company will have sufficient financial resources to allow it to continue in operational existence for at least twelve months following the date of this report. The directors believe it is appropriate to prepare the accounts on a going concern basis.

This report on Corporate Governance has been approved by the Board and signed on its behalf by

Ian Ardill

Company Secretary

25 April 2005

Directors' Report on Remuneration

This report has been prepared by the Remuneration Committee (the "Committee") on behalf of the Board and in accordance with the provisions of Schedule 7A of the Companies Act 1985. The Committee operates according to the principles outlined in the Listing Rules of the Financial Services Authority and this report describes how the Board has applied these Principles of Good Governance relating to Directors' remuneration.

A resolution to approve the Committee's report will be proposed at the forthcoming Annual General Meeting of the Company.

REMUNERATION COMMITTEE

The members of the Committee are Jeremy Curnock Cook (Chairman) and David Hankinson, both of whom are independent non-executive Directors of the Company. Sir Richard Needham retired from the Committee in compliance with the independence criterion of the Combined Code on Corporate Governance published in July 2003. No Committee member has a personal financial interest (other than as a shareholder) in the matters to be decided. In 2004 the Committee met on six occasions. Attendance at meetings is set out on page 20 and the Terms of Reference for the Committee are available on the Company's website: www.biocompatibles.com.

Dr. Michael Driver, an Executive Committee member, is Secretary to the Committee and attends the meetings. Crispin Simon, Chief Executive, attends the meetings at the invitation of the Committee, but is not present when his own remuneration is being discussed. Geoff Tompsett, Director of Human Resources and an Executive Committee member, also attends meetings upon the invitation of the Chairman to facilitate discussions on remuneration and incentive schemes. The Committee, in setting executive directors' remuneration, referred to a survey undertaken by New Bridge Street Consultants LLP on remuneration levels amongst comparator companies. New Bridge Street Consultants LLP also provided advice on the policy for the award of share options and the proposed introduction of new Share Incentive Plans. Aon Consulting Limited provided advice to the Committee in relation to executive Directors' pensions and a bonus sacrifice scheme for pensions. Aon provided actuarial, pension and employee benefit administration services to the Company. Pitmans provide legal services to the Company including advice on employment law.

POLICY ON DIRECTORS' REMUNERATION

The Committee's policy on executive directors' remuneration mirrors the Company's policies on pay and benefits and is subject to regular review. This is to reward on the basis of median salaries within the healthcare/biotech sector with the potential to reward up to the upper quartile of the sector through bonuses and share incentive schemes. The packages are designed to attract, motivate and retain talented executives. The four main elements of the remuneration package for executive Directors and senior managers are basic annual salary and associated benefits, performance related annual bonus, the long term incentive programme and pension arrangements. This mix of performance related and non-performance related remuneration is designed to incentivise Directors and senior executives.

Salary and Benefits

The Committee sets salaries after consideration of the Company's performance, market conditions, comparable salaries in peer companies and the need to reward individual performance. The Committee reviews executive Directors' basic salaries annually in December with changes becoming applicable from the start of the following year. In addition, salaries are reviewed at the time of the appointment of new directors to the Board. The average increase effective from 1 January 2005 was 7%, which was driven by above inflation increases for Dr. Peter Stratford and, particularly, Ian Ardill. These increases were required to reflect median levels for the roles in comparable companies. Details of each executive Directors' remuneration are set out on page 29.

Executive Directors' service contracts, which include details of remuneration, will be available for inspection at the Annual General Meeting. In addition to basic salary, the executive Directors receive the following benefits in kind: car allowance, life assurance, private medical insurance and pension.

Annual Bonus Payments

The Company's policy is that a substantial proportion of the remuneration of the executive Directors and senior executives should be performance related. As described below, executive Directors may earn annual bonus payments (which are non-pensionable) of up to 50% of their basic salary.

The Committee establishes the targets annually. The achievement of the 2004 annual goals is described in the Operational Review on page 8. For 2005 the bonus payments are based on the achievement of predefined goals and the individual weightings of those goals. 2005 performance targets were determined at the beginning of the financial year based on the following criteria:

- Achievement of budgeted sales revenue targets.
- Achievement of budgeted cash balance for the year end.
- Achievement of regulatory filing goals.
- Commencement of a new clinical programme and a new indication.
- Commencement of and first patient recruitment in a randomised controlled trial for the Doxorubicin Eluting Bead

Each of these "business" goals is allocated a specific bonus percentage. Achievement of all of the goals will earn the executive Directors a 35% bonus while non-achievement of the goals will reduce the bonus paid. There are additional criteria which will pay a bonus of up to 15% based on pre-determined personal goals for the executive Directors, proportionate to the achievement of the Company's Bonus Goals.

LONG TERM INCENTIVE PLANS

New Performance Share Plan

The Remuneration Committee is mindful of the need to reward performance and align the interests of management and shareholders whilst being constrained by the dilution effect of the returns of capital and subsequent share consolidations. Given the imminent expiry of the 2003 Employee Share Option Scheme, the Committee has considered the adoption of new share based incentive schemes in the form of a Performance Share Plan in which the most senior executives may participate and a Share Incentive Plan in which all employees may participate. The proposals will be put to shareholders at the Annual General Meeting and are set out in full in the Notice thereof. The Committee considers that the proposals reflect current best practice and enable the Committee to reward performance without at the same time exacerbating the dilution issue which has been adversely affected by the reduction in the number of shares in issue following the returns of capital in 2002, 2003 and a further return of approximately 29p per share expected in 2005. The Remuneration Committee is mindful of dilution to shareholders through issuing new shares to employees under various employee share schemes. The move away from a policy based on share options to one based on awarding shares will result in a significantly lower level of share usage and the Remuneration Committee anticipates that, over time, the Company will be able to operate within a dilution framework of 10% of issued share capital over any ten-year period. The issue of dilution is explored more fully in the Shareholder Circular accompanying the Notice of Meeting for this year's AGM.

It is proposed that the shares awarded under the Performance Share Plan will be limited to one times salary except in exceptional circumstances such as recruitment to senior positions where the maximum value of shares awarded will be limited to two times salary. The awards will vest after three years, subject to a performance condition based on the Company's Total Shareholder Return ("TSR") against a comparator group comprising the constituents of the FTSE techMARK All-Share Index of which the Company is a member. Where the TSR ranks between median and upper quartile after three years the Performance Award will vest pro-rata between 25% and 100%. Where the TSR ranks below median after three years the performance target will not have been met and the Performance Award will lapse. The relevant TSR figures will be averaged over the three-month periods preceding the beginning and end of the performance period. There is no opportunity for retesting the performance condition.

Measuring the Company's TSR performance against this benchmark will reward stock market outperformance and will preserve good alignment between the interests of executives and shareholders. The TSR performance condition will be calculated by independent advisers and verified by the Remuneration Committee.

Upon the launch of this scheme, no further share options will be awarded under the existing schemes.

Shareholding

In order to ensure that executive Directors' interests are aligned with those of shareholders, it is proposed to adopt shareholding guidelines linked to the out-turn from the proposed share based incentive schemes whereby executive directors will be expected to retain no fewer that 50% of shares net of taxes until a shareholding equivalent to 100% of base salary has been achieved. Executive Committee members will also be expected to build and maintain a shareholding within the Company based on a percentage of salary yet to be set by the Remuneration Committee.

PENSION ARRANGEMENTS

Each of the executive Directors is a member of the Biocompatibles Retirement Plan, which is a money purchase scheme. The Plan also provides for dependants' pensions and a lump sum on death-in-service. Contributions by the Director and the Company are based on a percentage of pensionable salary (not including bonus payments) and vary according to the age of the Director. No other payments to Directors are pensionable. The normal retirement age under the Pension Plan for Directors is 60 years and for other employees is 65 years; early retirement is permissible with Company consent from age 55. The Committee has introduced a scheme whereby employees and executive Directors can elect to sacrifice all or a proportion of a potential annual bonus payment in return for Company contributions into the pension scheme. An additional voluntary contribution ("AVC") matching arrangement was introduced in 2004 whereby the Company matches AVCs made by employees and Directors up to a maximum of 3 per cent of basic salary.

LETTERS OF APPOINTMENT AND SERVICE CONTRACTS

Director	Non-executive director			Executive director	
	Effective date of letter of appointment	Term of letter of appointment	Unexpired Term	Date of service contract	Notice period
Jeremy Curnock Cook	6 July 2004	1 year	6 months	–	–
David Hankinson	9 September 2003	3 years	1 years 8 months	–	–
Richard Needham	6 July 2003	3 years	1 years 6 months	–	–
Crispin Simon	–	–	–	15 June 1999	1 year
Peter Stratford	–	–	–	25 September 2002	1 year
Ian Ardill				23 November 2004	1 year
Swag Mukerji*	–	–	–	9 May 2001	1 year

* Swag Mukerji resigned as a Director on 15 October 2004.

It is the Company's policy that service contracts for executive Directors are for an indefinite period terminable by either party with twelve months' notice, and that payments in lieu of notice should not exceed the Director's salary for the unexpired term of their notice period. The Company has adopted a policy on mitigation to reduce the payment in lieu of notice.

The interests of the Directors in the Company's share capital are shown on page 15.

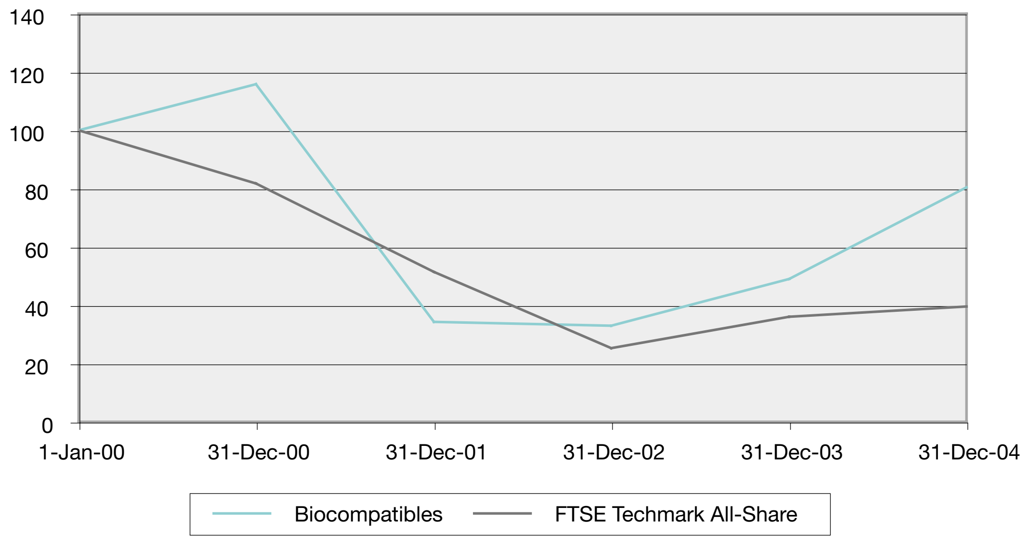
NON-EXECUTIVE DIRECTORS

The remuneration of the non-executive Directors is determined by the Board within limits set out in the Articles of Association, based on duties performed, time required and independent surveys of fees paid by comparable companies. Non-executive Directors have letters of appointment. The Company's policy is to appoint non-executive Directors for an initial three-year term subject to the requirements for re-election under the Articles of Association. Non-executive Directors are not entitled to compensation for loss of office beyond the three month notice period in their letter of appointment. The non-executive Directors do not participate in any bonus or share schemes of the Company and are not eligible to join the Company's pension scheme.

PERFORMANCE GRAPH

The following graph shows the Company's performance, measured by total shareholder return, compared with the performance of the FTSE techMARK All-Share index. The Directors believe this to be the most appropriate index for comparison. It is the benchmark against which performance is measured for the Company's 1995 share option scheme and is an index of which the Company has been a constituent member throughout the period.

Total shareholder return of Biocompatibles versus the FTSE Techmark All-Share Index



The following information has been audited by the Company's auditors, PricewaterhouseCoopers LLP, as required by Schedule 7A of the Companies Act 1985.

DIRECTORS' EMOLUMENTS

The aggregate remuneration of the individual directors for the year ended 31 December 2004 was as follows:

Name of Director	Fees £'000	Salary £'000	Bonus £'000	Benefits £'000	Compensation for loss of office £'000	2004 Total £'000	2003 Total £'000
Ian Ardill (appointed 15.10.04)	–	23	6	3	–	32	–
Swag Mukerji (resigned 15.10.04)	–	125	46	14	117	302	242
Crispin Simon	–	256	96	17	–	369	400
Peter Stratford*		146	55	16	–	217	217
Jeremy Curnock Cook	28	–	–	–	–	28	37
David Hankinson	28	–	–	–	–	28	36
Richard Needham	55	–	–	–	–	55	53
Total:	111	550	203	50	117	1,031	985

The Committee applied its policy for termination payments in relation to the compromise agreement reached with Swag Mukerji on his resignation. A compensation for loss payment was calculated on the basis of his salary and benefits for one year. This amount was reduced under the mitigation provisions of the agreement as Mr. Mukerji found alternative employment. The Committee exercised its discretion under the share option schemes to allow him to exercise his options during a period of six months following his departure.

Directors' Pension Entitlements

All the executive Directors are members of the Biocompatibles Retirement Plan. Contributions by the employee and the Company are based on a percentage of pensionable salary. The Directors' contributions during the year were:

Ian Ardill (appointed 15 October 2004) contributed £1,752 and the Company contributed £3,154.
Crispin Simon contributed £15,055 and the Company contributed £34,060.
Peter Stratford contributed £6,919 and the Company contributed £15,537.
Swag Mukerji (resigned 15 October 2004) contributed £6,713 and the Company contribution £24,398.

Directors may, at their discretion, make AVCs up to the limits defined by the Inland Revenue. Any such payments and the Company's matching cost are included above.

Directors' Share Options as at 31 December 2004

	Scheme	Date of Grant	1 January 2004 Number of shares under option	Granted during the year	Exercise Price £	Number of options Exercised during the year	Market price on date of exercise	31 December 2004 Number of shares under option	Exercise period
Ian Ardill	Exec 1995	Apr 2003	20,000		1.23	–	–		Apr 2006 - Apr 2013
(appointed	Exec 2003	July 2003	30,000		1.47	–	–		July 2006 - July 2013
15.10.04)	Exec 2003	Apr 2004		45,000	1.96	–	–		Apr 2007 - Apr 2014
	Exec 2003	Oct 2004		30,000	2.19	–	–	125,000	Oct 2007 - Oct 2014
Swag	Exec 1995	Aug 2001	160,000		1.89	160,000	2.22[2]		Aug 2004 - Apr 2005
Mukerji[2]	Exec 1995	Apr 2002	140,000		1.04	140,000	2.22[2]		Apr 2005 - Apr 2005
(resigned	Exec 2203	July 2003	50,000		1.47	50,000	2.22[2]		July 2006 - Apr 2005
15.10.04)	Exec 2003	Apr 2004		45,000	1.96	45,000	2.22[2]	0[2]	Apr 2007 - Apr 2005
Crispin	Exec 1995	June 1998	316,874		1.262	–	–		June 2001 - June 2008
Simon	Exec 1995[1]	June 1998	316,875		1.262	–	–		June 2003 - June 2008
	SAYE 1995	July 1998	19,971		0.976		–		Sept 2005 - Feb 2006
	Exec 1995	June 2000	75,000		2.910	–	–		June 2003 - June 2010
	Exec 1995[1]	June 2000	75,000		2.910	–	–		June 2005 - June 2010
	Exec 1995	Sept 2000	28,500		3.84				Sept 2003 - Sept 2010
	Exec 1995[1]	Sept 2000	28,500		3.84				Sept 2005 - Sept 2010
	Exec 1995	Aug 2001	31,250		1.89	–	–		Aug 2004 - Aug 2011
	Exec 1995[1]	Aug 2001	31,250		1.89	–	–		Aug 2006 - Aug 2011
	Exec 2003	July 2003	50,000		1.47	–	–		July 2006 - July 2013
	Exec 2003	Apr 2004		60,000	1.96	–	–	1,033,220	Apr 2007 - Apr 1014
Peter	Exec 1995	Apr 1995	22,306		1.53	22,306[3]	2.45		Apr 1998 - Apr 2005
Stratford	Exec 1995	Apr 1999	76,050		1.074	76,050[3]	2.45		Apr 2002 - Apr 2009
	Exec 1995	Aug 1999	48,000		1.18	48,000[3]	2.45		Aug 2002 - Aug 2009
	Exec 1995	Aug 1999	12,588		1.26	–	–		Aug 2002 - Aug 2009
	Exec 1995	Sept 2000	20,000		3.84	–	–		Sept 2003 - Sept 2010
	Exec 1995	Sept 2001	30,000		0.59	–	–		Sept 2004 - Sept 2011
	Exec 2003	July 2003	50,000		1.47	–	–		July 2006 - July 2013
	Exec 2003	Apr 2004		60,000	1.96	–	–	172,588	Apr 2007 - Apr 2014
Total			1,642,164	240,000		541,356		1,330,808	

[1] Super options.

[2] On the date of resignation Mr. Mukerji held 395,000 shares under option which were exercised immediately, in compliance with the terms of his Compromise Agreement, with an aggregate gain of £267,000 before tax.

[3] The aggregate gain from the exercise of options by Peter Stratford was £186,000 before tax.

The market price of the Company's shares at the end of the financial year was 233.5p and the range of market prices during the year was between 144p and 247.5p.

Employee Share Option Scheme 2003

For those share options granted after June 2003, the performance condition is that the Total Shareholder Return of the Company's shares must outperform the FTSE techMARK mediscience index.

Executive Share Option Scheme 1995

For those share options granted during and after August 1999, the performance condition is that the total shareholder return of the Company's shares must outperform that of the FTSE techMARK All Share index.

For options granted prior to August 1999, the increase in Total Shareholder Return since the date of grant must be at least 10 per cent greater than the increase in the Retail Prices index over a period of 3 years from the date of grant.

Executive Share Option Scheme 1995 – Super Options

For super options granted during and after June 2000, participants will be able to exercise their options if the increase in the Total Shareholder Return since the date of grant falls within the top quartile of Total Shareholder Return performance by the constituents of the FTSE Mid-250 index of companies over the same period. Super options were created in 1998 to link higher potential reward for exceptional performance for the most senior executives.

For super options granted before June 2000, participants will be able to exercise their options if, over a period of any three months (such period to begin no earlier than three months before the fifth anniversary of the date of grant) the average market value of an ordinary share of the Company is at least 350p.

Super options can be exercised after the fifth anniversary of the date of grant but only if the performance criteria have been met.

Approval

This report was approved by the Board of Directors on 25 April 2005 and is signed on its behalf by:

Jeremy Curnock Cook
Chairman
Remuneration Committee

Consolidated Profit and Loss Account

for the year ended 31 December 2004

	Notes	2004 £000	2003 £000
Turnover	*2*	**2,599**	2,107
Cost of sales		**(1,115)**	(965)
Gross profit		**1,484**	1,142
Operating expenses before intangible amortisation and exceptional items	*3*	**(8,392)**	(7,973)
Operating exceptional items	*4*	**37**	(209)
Intangible amortisation	*3*	**(754)**	(754)
Operating expenses	*3*	**(9,109)**	(8,936)
Operating loss before intangible amortisation and exceptional items		**(6,908)**	(6,831)
Operating loss	*2*	**(7,625)**	(7,794)
Non operating exceptional items:			
profit on disposal of operations			
– discontinued activities	*4*	**4,928**	21,570
Net interest income	*7*	**2,108**	2,246
(Loss)/profit on ordinary activities before taxation	*2*	**(589)**	16,022
Tax credit on (loss)/profit on ordinary activities	*8*	**450**	–
(Loss)/profit on ordinary activities after taxation	*23*	**(139)**	16,022
(Loss)/earnings per ordinary share (basic and diluted)	*9*	**(0.4)p**	42.2p
Loss per ordinary share (before exceptional items)	*9*	**(13.3)p**	(14.1)p

Consolidated Balance Sheet

at 31 December 2004

	Notes	2004 £000	2003 £000 As restated
Fixed assets			
Intangible assets	*10*	**754**	1,508
Tangible assets	*11*	**759**	875
Investments	*12*	**–**	–
		1,513	2,383
Current assets			
Stock	*13*	**370**	230
Debtors	*14*	**20,241**	19,043
Investments	*15*	**15,140**	19,929
Cash at bank and short term deposits		**31,277**	35,584
		67,028	74,786
Creditors: amounts falling due within one year	*16*	**(10,600)**	(13,906)
Net current assets		**56,428**	60,880
Total assets less current liabilities		**57,941**	63,263
Creditors: amounts falling due after more than one year	*17*	**(5,319)**	(6,590)
Provision for liabilities and charges	*20*	**(4,102)**	(9,221)
Net assets		**48,520**	47,452
Capital and reserves			
Called up share capital	*21,23*	**7,480**	7,292
Share premium account	*23*	**61,173**	60,168
Merger reserve	*23*	**17,748**	17,748
Other reserves	*23*	**47,800**	47,800
Profit and loss account	*23*	**(85,681)**	(85,556)
Equity shareholders' funds	*23*	**48,520**	47,452

Signed on behalf of the Board.

Ian Ardill

Finance Director

25 April 2005

Consolidated Cash Flow Statement

for the year ended 31 December 2004

	Notes	2004 £000	2003 £000
Net cash outflow from operating activities	*24*	**(8,502)**	(10,317)
Returns on investments and servicing of finance			
Interest received		**2,146**	2,627
Interest paid		**(11)**	(13)
Interest paid on finance leases		**–**	(3)
Net cash inflow from returns on investments and servicing of financing		**2,135**	2,611
Capital expenditure and financial investment			
Purchase of intangible fixed assets		**–**	(993)
Purchase of tangible fixed assets		**(153)**	(254)
Sale of tangible fixed assets		**9**	–
Net cash outflow for capital expenditure and financial investment		**(144)**	(1,247)
Net cash outflow before acquisitions and financing		**(6,511)**	(8,953)
Acquisitions and disposals			
Disposal of subsidiary undertakings*		**(4,775)**	(4,063)
Net cash outflow for acquisitions and disposals		**(4,775)**	(4,063)
Net cash outflow before management of liquid resources and financing		**(11,286)**	(13,016)
Management of liquid resources			
(Increase)/reduction in short term deposits	*25*	**(3,304)**	42,854
Reduction/(increase) in current asset investments	*25*	**4,915**	(20,480)
		1,611	22,374
Financing			
Issue of share capital		**1,193**	503
Return of capital		**–**	(11,265)
Repayment of principal advanced under bank loans and promissory notes	*25*	**(383)**	(41)
Repayment of principal advanced under finance leases	*25*	**(7)**	(16)
Net cash inflow/(outflow) from financing		**803**	(10,819)
Decrease in cash in the year	*25*	**(8,872)**	(1,461)

* The disposal of subsidiary undertakings cash flow mainly relates to cash outflow under the Abbott R&D agreement following the disposals made in 2002.

Statement of Group Total Recognised Gains and Losses

for the year ended 31 December 2004

	Notes	2004 £000	2003 £000
(Loss)/profit for the year		**(139)**	16,022
Exchange differences	*23*	**14**	31
Total recognised (losses)/gains relating to the year		**(125)**	16,053
Prior year adjustment	*1,23*	**381**	
Total gains recognised since the last annual report		**256**	

There is no difference between the profit on ordinary activities before taxation and the profit for the years stated above and their historical cost equivalents.

Reconciliation of Movements in Group Shareholders' Funds

for the year ended 31 December 2004

	Notes	2004 £000	2003 £000
(Loss)/profit for the year		**(139)**	16,022
Exchange differences	*23*	**14**	31
New share capital issued, including premium	*23*	**1,193**	503
Return of capital		**–**	(11,303)
Net increase in shareholders' funds		**1,068**	5,253
Opening shareholders' funds (as previously reported)		**47,689**	42,436
Prior year adjustment	*1,23*	**(237)**	(237)
Opening shareholders' funds (as restated)		**47,452**	42,199
Closing shareholders' funds		**48,520**	47,452

Company Balance Sheet

at 31 December 2004

	Notes	2004 £000	2003 £000 As restated
Fixed assets			
Intangible assets	*10*	**754**	1,508
Investments	*12*	**–**	108
		754	1,616
Current assets			
Debtors	*14*	**50,962**	43,105
Investments	*15*	**15,140**	19,929
Cash at bank and short-term deposits		**31,077**	35,374
		97,179	98,408
Creditors: amounts falling due within one year	*16*	**(8,251)**	(11,092)
Net current assets		**88,928**	87,316
Total assets less current liabilities		**89,682**	88,932
Creditors: amounts falling due after more than one year	*17*	**(5,319)**	(6,590)
Provision for liabilities and charges	*20*	**(4,102)**	(9,221)
Net assets		**80,261**	73,121
Capital and reserves			
Called up share capital	*21,23*	**7,480**	7,292
Share premium account	*23*	**61,173**	60,168
Merger reserve	*23*	**8,809**	8,809
Other reserves	*23*	**57,114**	57,114
Profit and loss account	*23*	**(54,315)**	(60,262)
Equity shareholders' funds	*23*	**80,261**	73,121

As permitted by section 230 of the Companies Act 1985, a separate profit and loss account for the Company is not presented.

Signed on behalf of the Board.

Ian Ardill

Finance Director

25 April 2005

1. Accounting policies

The accounting reference date for the current period is 31 December 2004.

Basis of accounting

The financial statements have been prepared under the historical cost convention and in accordance with applicable UK Accounting Standards and the Companies Act 1985. A summary of the more important Group accounting policies is set out below together with an explanation of where changes have been made to previous policies on the adoption of new accounting standards in the year.

Basis of consolidation

The consolidated profit and loss account and balance sheet include the financial statements of the Company and its subsidiary undertakings. Intra-Group sales and profits are eliminated on consolidation.

Research and development

Expenditure on research and development is charged to the profit and loss account as incurred.

Finance and operating leases

Costs in respect of operating leases are charged on a straight line basis over the lease term. Leasing agreements, which transfer to the Group substantially all the benefits and risks of ownership of an asset, are treated as if the asset had been purchased outright. The assets are included in fixed assets and the capital element of the leasing commitments is shown as obligations under finance leases. The lease rentals are treated as consisting of capital and interest elements. The capital element is applied to reduce the outstanding obligations and the interest element is charged against profit so as to give a constant periodic rate of charge on the remaining balance outstanding in each accounting period. Assets held under finance leases are depreciated over the shorter of the lease term and the useful lives of equivalent owned assets.

Pensions

The Group operates defined contribution pension schemes for certain of its employees in the UK, and charges the amount of employer's contribution payable during the year to the profit and loss account.

Accounting for Employee Share Ownership Plan – prior year adjustment

In accordance with UITF 38 – Accounting for ESOP Trusts, shares purchased through Employee Share Option Trusts (ESOPs) are held at cost and treated as Treasury Shares and are taken as a deduction from Shareholders' Equity. Previously these were held within Fixed Asset Investments at the lower of cost less provision for impairments with any impairments being taken to the Profit and Loss Account. The 2003 financial statements have been restated in accordance with UITF 38 and an impairment charge taken against the value of shares held within Employee Share Option Trusts has been reversed.

Tangible fixed assets

The cost of tangible fixed assets is their purchase cost, together with any incidental expenses of acquisition.

Depreciation is calculated so as to write off the cost of tangible fixed assets on a straight line basis over the expected useful economic lives of the assets concerned. The principal economic lives used for this purpose are:

Machinery and equipment	5 – 10 years
Office equipment and furniture	4 – 10 years
Leasehold improvements	3 – 10 years
Leasehold premium	lease term

Intangible assets

These represent payments made to third parties, including associated acquisition costs, to acquire licences to utilise their intellectual property. They are valued at cost on acquisition and written off over a period not exceeding the remaining patent life after taking into account the risk factors associated with pharmaceutical and medical device development.

The principal economic lives used for this purpose are:

License agreements and patents	1 – 5 years

1. Accounting policies *continued*

Stocks and work in progress

Stocks and work in progress are stated at the lower of cost and net realisable value. In general, cost is determined on a first-in-first-out basis and includes transport and handling costs. In the case of manufactured products, cost includes all direct expenditure including production overheads. Where necessary, provision is made for obsolete, slow moving or defective stocks.

Current asset investments

Current asset investments are stated at the lower of cost and net realisable value. In the case of the corporate bond investments, net realisable value is taken as market value.

Foreign currencies

Assets and liabilities of subsidiaries in foreign currencies are translated into sterling at rates of exchange ruling at the end of the financial year and the profit and loss accounts of foreign subsidiaries are translated at the average rates of exchange for the year. Differences on exchange arising from the retranslation of the opening net investment in subsidiary companies, and from the translation of the results of those companies at average rate, are taken to reserves and are reported in the statement of total recognised gains and losses. Exchange differences arising on long-term foreign currency borrowings used to finance the Group's foreign currency investments are also taken to reserves. All other foreign exchange differences are taken to the profit and loss account in the year in which they arise.

Turnover

Turnover, which excludes value added tax, represents the value of goods and services supplied and royalty income.

Royalty income is credited to the profit and loss account at the rate applicable to sales, of those products attracting a royalty, arising during each accounting period as reported by the licencee.

Non refundable one time licence fees are taken to the profit and loss account when the fee is due, unless the substance of the license fee contract is such that recognition on a contract basis is appropriate.

Deferred taxation

Provision is made for deferred taxation using the full provision method on timing differences in accordance with FRS 19 "Deferred Tax". Timing differences arise from the inclusion of items of income and expenditure in tax computations in periods different from those in which they are recognised in the financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

Financial instruments

The Group uses financial instruments primarily to manage its exposure to fluctuations in currency exchange rates. Except as described in foreign currencies above, any gain or loss on currency revaluation is recognised in the profit and loss account.

Transactions may be hedged using appropriate treasury instruments. Exposure arising from foreign currency deposits and translation of the results, assets and liabilities of subsidiary undertakings may be hedged by way of local currency borrowings by the Group and appropriate treasury instruments.

2. Segment information

2004	**Turnover £000**	**Operating loss before exceptionals and intangible amortisation £000**	**(Loss)/profit before taxation £000**	**Net assets £000**
Continuing activities				
Commercial research and development	**2,599**	**(6,908)**	**(7,625)**	**48,520**
	2,599	**(6,908)**	**(7,625)**	**48,520**
Discontinued activities				
Cardiovascular	**–**	**–**	**1,000**	**–**
Eye Care	**–**	**–**	**3,800**	**–**
Urotech	**–**	**–**	**128**	**–**
	–	**–**	**4,928**	**–**
Net interest receivable	**–**	**–**	**2,108**	**–**
Total	**2,599**	**(6,908)**	**(589)**	**48,520**

2003	Turnover £000	Operating loss before exceptionals and intangible amortisation £000	(Loss)/profit before taxation £000	Net assets £000 As restated
Continuing activities				
Commercial research and development	2,107	(6,831)	(7,794)	47,452
	2,107	(6,831)	(7,794)	47,452
Discontinued activities				
Cardiovascular	–	–	20,128	–
Eye Care	–	–	1,374	–
Other	–	–	68	–
	–	–	21,570	–
Net interest receivable	–	–	2,246	–
Total	2,107	(6,831)	16,022	47,452

The analysis by geographical area of the Group’s turnover, (loss)/profit before taxation and net assets is set out below:

	2004 £000	2003 £000
Turnover by source		
United Kingdom	**2,599**	2,107
Turnover by destination		
United Kingdom	**41**	1
Rest of Europe	**1,910**	1,300
United States of America	**648**	806
	2,599	2,107

Turnover by destination represents sales of products to third parties.

2. Segment information *continued*

	2004 £000	2003 £000
(Loss)/profit before taxation		
United Kingdom	**(581)**	16,235
United States of America	**(8)**	(213)
	(589)	16,022
Net assets		
United Kingdom	**48,518**	47,682
United States of America	**2**	7
	48,520	47,689

3. Operating expenses

2004	**Before exceptional items and intangible amortisation £000**	**Intangible amortisation £000**	**Exceptional items £000**	**Total £000**
Selling, marketing and distribution	**(1,188)**	**(754)**	**–**	**(1,942)**
Research and development	**(5,325)**	**–**	**–**	**(5,325)**
General and administrative	**(1,879)**	**–**	**37**	**(1,842)**
	(8,392)	**(754)**	**37**	**(9,109)**

2003	Before exceptional items and intangible amortisation £000	Intangible amortisation £000	Exceptional items £000	Total £000
Selling, marketing and distribution	(1,091)	(754)	–	(1,845)
Research and development	(4,550)	–	–	(4,550)
General and administrative	(2,332)	–	(209)	(2,541)
	(7,973)	(754)	(209)	(8,936)

	2004 £000	2003 £000
(Loss)/profit before tax is stated after charging:		
Depreciation	**279**	296
Amortisation of intangible assets	**754**	754
Operating lease rentals:		
Plant and equipment	**–**	–
Other assets	**360**	360
(Profit)/loss on disposal of tangible fixed assets	**(5)**	57
Auditors’ remuneration, including Company £54,000 (2003: £49,000)	**60**	55

Amounts paid to the Company’s auditors in respect of non-audit fees for work provided to the Company and its UK subsidiaries were £52,000 (2003: £284,000) in respect of the following:

Disposals and associated costs	**–**	50
Tax services:		
Compliance	**47**	122
Advisory	**5**	112
	52	284

4. Exceptional items

The exceptional operating credit of £37,000 (2003: charge of £209,000) relates to the release of strategic review costs accrued following the disposal of the Eye Care division and the cardiovascular businesses.

The non-operating exceptional items relate to the release of provisions for warranties and indemnities created on the disposal of the Eye Care division and the Cardiovascular and the Urology businesses.

5. Employee information

The average number of persons (including executive Directors) employed by the Group during the year was:

	2004 Number	2003 Number
Manufacturing and production	**6**	2
Selling, marketing and distribution	**3**	2
Research and development	**44**	44
General and administrative	**19**	19
	72	67

Staff costs (for the above persons) were:	**£000**	£000
Wages and salaries	**3,813**	3,630
Social security costs	**332**	387
Other pension costs (see note 19)	**287**	171
	4,432	4,188

6. Directors' emoluments

Directors' emoluments and options are given in the tables in the Directors' Report on Remuneration on pages 26 to 31.

7. Net interest income

	2004 £000	2003 £000
Interest receivable on bank deposits and current asset investments	**2,117**	2,261
Interest payable:		
Bank loans and overdrafts	**(1)**	(6)
Other loans	**(8)**	(6)
Finance leases	**–**	(3)
Total interest payable	**(9)**	(15)
Net interest receivable	**2,108**	2,246

8. Taxation

	2004 £000	2003 £000
UK Corporation tax:		
Current	**(450)**	–
Deferred	**–**	–
Total	**(450)**	–

	2004 £000	2003 £000
(Loss)/profit on ordinary activities before taxation	**(589)**	16,022
(Loss)/profit on ordinary activities multiplied by the standard rate of tax in the UK of 30% (2003: 30%)	**(177)**	4,807
Expenses not deductible for tax purposes	**18**	8
Adjustment in respect of sale of assets	**(1,478)**	(3,705)
Accelerated capital allowances	**(133)**	8
Losses carried forward and other timing differences	**927**	(1,118)
Loss surrendered for R&D tax credits	**843**	–
R&D tax credit claims	**(450)**	–
Total	**(450)**	–

Factors that may affect future tax charge

Carried forward tax losses and the availability of R&D incentives may affect the future tax rate of the Group.

The Group has a potential deferred tax asset, which is not recognised as follows:

	Amount provided		Amount unprovided	
Group	**2004 £000**	2003 £000	**2004 £000**	2003 £000
Accelerated capital allowances	**–**	–	**(606)**	(40)
Short-term timing differences	**–**	–	**(1,308)**	(2,891)
Losses	**–**	–	**(20,673)**	(19,636)
Total	**–**	–	**(22,587)**	(22,567)

The Company has no actual or potential liability to deferred taxation.

The deferred tax asset has not been recognised as the Directors consider it more likely than not that the asset will not crystallise in the foreseeable future.

9. (Loss)/earnings per share

The calculation of basic earnings per share has been based on the loss on ordinary activities after taxation of £139,000 (2003: profit of £16,022,000) and on 38,421,309 (2003: 37,934,959) issued shares, being the weighted average number of shares in issue.

Potential ordinary shares are not treated as dilutive as their conversion to ordinary shares does not increase the net loss per share from continuing operations.

The calculation of adjusted loss per share has been based on loss before exceptional items.

	2004		2003	
	Pence per share	**£000**	Pence per share	£000
(Loss)/earnings per ordinary share	**(0.4)**	**(139)**	42.2	16,022
Non operating exceptional items	**(12.8)**	**(4,928)**	(56.9)	(21,570)
Operating exceptional items	**(0.1)**	**(37)**	0.6	209
Loss per share before exceptional items	**(13.3)**	**(5,104)**	(14.1)	(5,339)

10. Intangible fixed assets

Group & Company **Cost**	**License agreements and patents** **£000**
At 1 January 2004	2,262
Acquisition	–
Disposal	–
At 31 December 2004	**2,262**
Amortisation	
At 1 January 2004	754
Charge in year	754
Disposal	–
At 31 December 2004	**1,508**
Net book value	
At 31 December 2003	1,508
At 31 December 2004	**754**

11. Tangible fixed assets

The Company has no tangible fixed assets. Details of those relating to the Group are as follows:

Cost	Machinery & equipment £000	Office equipment & furniture £000	Leasehold improvements £000	Leasehold premium £000	Assets in course of construction £000	Total £000
At 1 January 2004	1,391	541	1,699	150	249	4,030
Additions	151	8	9	–	–	168
Disposals	(209)	–	–	–	–	(209)
Transfers	239	–	–	–	(239)	–
At 31 December 2004	**1,572**	**549**	**1,708**	**150**	**10**	**3,989**
Depreciation						
At 1 January 2004	1,325	460	1,291	79	–	3,155
Charge for year	60	45	164	10	–	279
Disposals	(204)	–	–	–	–	(204)
At 31 December 2004	**1,181**	**505**	**1,455**	**89**	**–**	**3,230**
Net book value						
At 31 December 2003	66	81	408	71	249	875
At 31 December 2004	**391**	**44**	**253**	**61**	**10**	**759**

The net book value includes £nil (2003: £5,000) in respect of assets held under finance leases and hire-purchase contracts. Depreciation charged on these assets during the year was £5,000 (2003: £25,000).

12. Fixed assets investments

Group **Cost**	Notes	ESOP shares £000
At 1 January 2004 (as previously reported)		618
Prior year adjustment	1,23	(618)
At 1 January 2004 (as restated) and 31 December 2004		**–**
Provision		
At 1 January 2004 (as previously reported)		381
Prior year adjustment	1,23	(381)
At 1 January 2004 (as restated) and 31 December 2004		**–**
Net book value		
At 31 December 2003 (as restated)		–
At 31 December 2004		**–**

12. Fixed assets investments *continued*

Company Cost	Notes	Investments in subsidiaries £000	ESOP shares £000	Total £000
At 1 January 2004 (as previously reported)		8,746	726	9,472
Prior year adjustment	1,23	–	(618)	(618)
At 1 January (as restated)		8,746	108	8,854
Write off during the period		–	(108)	(108)
At 31 December 2004		**8,746**	**–**	**8,746**
Provision				
At 1 January 2004 (as previously reported)		8,746	381	9,127
Prior year adjustment	1,23	–	(381)	(381)
At 1 January (as restated) and 31 December 2004		**8,746**	**–**	**8,746**
Net book value				
At 31 December 2003 (as restated)		–	108	108
At 31 December 2004		**–**	**–**	**–**

Interests in Group undertakings

The following principal subsidiary undertakings have been included in the Group consolidation. All interests are held in the form of equity shares.

Name of undertaking	Principal area of activity	Country of incorporation
Biocompatibles (UK) Limited	Research and development	Great Britain
Biopolymerix Inc.	Research and development	United States of America

All subsidiary undertakings are 100% owned and operate principally in their country of incorporation.

13. Stocks

	Group 2004 £000	Group 2003 £000	**Company 2004 £000**	Company 2003 £000
Raw materials and consumables	**17**	41	**–**	–
Finished goods and goods for resale	**353**	189	**–**	–
	370	230	**–**	–

14. Debtors

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Amounts falling due within one year				
Trade debtors	**473**	483	**–**	–
Corporation Tax	**450**	–		–
Other debtors	**18,354**	17,719	**17,560**	17,560
Prepayments and accrued income	**761**	645	**200**	344
	20,038	18,847	**17,760**	17,904
Amounts falling due after more than one year				
Other debtors	**203**	196	**–**	–
Amounts owed from group undertakings	**–**	–	**33,202**	25,201
	20,241	19,043	**50,962**	43,105

Other debtors include £17,600,000 in respect of proceeds from disposal of the Cardiovascular business activities that are held in an Escrow account. The release of this amount is expected in 2005, upon which interest will be received and recognised in the profit and loss account.

15. Current asset investments

The Group and the Company

The current asset investments of £15,140,000 (2003: £19,929,000) comprise corporate bonds with a high credit rating (AA or above as rated by Moody's or Standard and Poors credit rating agencies).

16. Creditors: amounts falling due within one year

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Bank loans and overdrafts	**1,262**	1	**1,262**	–
Other borrowings	**–**	383	**–**	383
Obligations under finance leases	**1**	8	**–**	–
Trade creditors	**412**	726	**53**	104
Other taxation and social security	**209**	115	**–**	–
Other creditors	**2,662**	6,237	**2,557**	6,101
Accruals and deferred income	**2,071**	2,453	**396**	521
Taxation	**3,983**	3,983	**3,983**	3,983
	10,600	13,906	**8,251**	11,092

Other borrowings in 2003 included £383,000 of loan notes which bore interest at 2% below bank base rate and were all redeemed in 2004.

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

	Group 2004 £000	Group 2003 £000	Company 2004 £000	Company 2003 £000
Accruals and deferred income	**5,319**	6,590	**5,319**	6,590

These relate to royalties prepaid by Abbott following the disposal of the cardiovascular division in 2002.

18. Financial instruments

The Group's strategy is to use financial instruments, where appropriate, to secure finance for its operations and to manage the risks arising from those operations. Transactions using financial instruments are undertaken only to manage interest and currency risks associated with the Group's underlying business activities and the financing of those activities. The Group does not undertake any trading or speculative activity in derivatives and financial instruments.

The Board reviews and agrees policies for managing each of these risks and they are summarised below:

Liquidity risk

The Group's policy is to ensure continued availability of funds for its operations. In the case of the current asset investments, the Group's policy is that the weighted average life of the bond portfolio should not exceed 2 years, the maximum life of an individual bond is 4 years.

Interest rate risk

The Board regularly reviews the profile of deposits to ensure that rates are maximised, taking into consideration liquidity requirements, risk and current market conditions.

Foreign currency risk

The Group has a policy of monitoring exchange rate movements in the main currencies in which it trades. These are the US Dollar and the Euro.

Financial instruments are used to reduce exposure to exchange rate movements where there is a specific asset, liability or cash flow and the risk of an adverse exchange rate movement is high. There were no financial instruments in place at year end.

Short term debtors and creditors have been excluded from the following disclosures, other than currency risk disclosures.

Interest rate and currency profile of financial assets, other than cash, short term deposits and current asset investments:

	Total £000	Floating rate financial assets £000
Sterling	203	203
At 31 December 2004	**203**	**203**
Sterling	196	196
At 31 December 2003	196	196

Interest rate and currency profile of cash, short term deposits and current assets investments:

	Total £000	Cash at bank and in hand £000	Short term deposits £000	Current asset investments £000
Sterling	46,395	25,451	5,804	15,140
US dollars	6	6	–	–
Euros	16	16	–	–
At 31 December 2004	**46,417**	**25,473**	**5,804**	**15,140**
Floating rate	31,275	25,471	5,804	–
Fixed rate	15,140	–	–	15,140
No rate	2	2	–	–
At 31 December 2004	**46,417**	**25,473**	**5,804**	**15,140**

18. Financial instruments *continued*

	Total £000	Cash at bank and in hand £000	Short term deposits £000	Current asset investments £000
Sterling	55,428	32,999	2,500	19,929
US dollars	38	38	–	–
Euros	47	47	–	–
At 31 December 2003	55,513	33,084	2,500	19,929
Floating rate	35,499	32,999	2,500	–
Fixed rate	19,929	–	–	19,929
No rate	85	85	–	–
At 31 December 2003	55,513	33,084	2,500	19,929

The floating rate cash and short term deposits are placed with banks on a rolling basis for various periods and earn interest at approximately base rate. The fixed rate current asset investments are placed in investment grade corporate bonds and earn a variety of coupon rates.

Interest rate and currency profile of financial liabilities:

2004 Currency	Total £000	Fixed rate financial liabilities £000	Floating rate financial liabilities £000	Financial liabilities on which no interest is paid £000
Sterling	10,684	–	–	10,684
At 31 December 2004	**10,684**	**–**	**–**	**10,684**
2003 Currency				
Sterling	16,203	8	384	15,811
At 31 December 2003	16,203	8	384	15,811

Fixed and floating rate financial liability maturity profile:

2004 Currency	Weighted average interest rate %	Weighted average period for which rate is fixed Years	Weighted average period until maturity Years
Sterling	–	–	–
Weighted average total at 31 December 2004	**–**	**–**	**–**
2003 Currency			
Sterling	1.8	0.3	1.2
Weighted average total at 31 December 2003	1.8	0.3	1.2

Floating rate financial liabilities bear interest at rates based on relevant national LIBOR equivalents.

18. Financial instruments *continued*

Maturity of financial liabilities:

The maturity profile of the Group's financial liabilities, other than short term trade creditors and accruals, was:

	2004			2003		
	Debt	**Other financial liabilities**	**Total**	Debt	Other financial liabilities	Total
	£000	**£000**	**£000**	£000	£000	£000
Within 1 year	**–**	**1,263**	**1,263**	384	8	392
More than 1 year	**–**	**9,421**	**9,421**	–	15,811	15,811
Total	**–**	**10,684**	**10,684**	384	15,819	16,203

Debt due within one year includes £nil (2003: £1,000) in respect of overdrafts and £nil (2003: £383,000) of other loans.

Fair values:

The following table provides a comparison by category of the carrying values and fair values of the Group's financial assets and financial liabilities at 31 December 2004 and 2003. The fair value of short term investments and borrowings approximated to their carrying value due to the short maturity of the instruments held. The fair value of current assets investments was based on quoted market prices for these investments. The fair value of the convertible loan stock was estimated by reference to the movement in market interest rates between their issue date and the year end.

	Carrying value		Fair value	
	2004	2003	**2004**	2003
	£000	£000	**£000**	£000
Assets				
Cash at bank and in hand	**25,473**	33,084	**25,473**	33,084
Short term investments	**5,804**	2,500	**5,804**	2,500
Current assets investments	**15,140**	19,929	**15,296**	19,931
Debts due after more than one year	**203**	196	**203**	196
Liabilities				
Short term financial instruments	**(1,263)**	(392)	**(1,263)**	(392)
Total	**45,357**	55,317	**45,513**	55,319

Net foreign currency exposure of the Group's monetary assets and liabilities:

	Sterling		Total	
	2004	2003	**2004**	2003
Functional currency of Group operation	**£000**	£000	**£000**	£000
Sterling	**–**	–	**–**	–
Euro	**16**	47	**16**	47
Other	**5**	33	**5**	33
Total	**21**	80	**21**	80

19. Pension obligations

Defined contribution scheme

The Group operates defined contribution pension schemes for certain of its employees in the UK, and charges the amount of employer's contributions payable during the year to the profit and loss account. The charge for the year was £287,000 (2003: £171,000).

20. Provisions for liabilities and charges

Group & Company	2004 £000	2003 £000
At 1 January 2004	**9,221**	32,110
Utilised during the year	**(191)**	(1,436)
Released to profit and loss account	**(4,928)**	(21,453)
At 31 December 2004	**4,102**	9,221

The provisions above relate to indemnities and warranties relating to the disposals made in 2002. It is expected that the provisions will be utilised within the next five years.

21. Share capital

	2004 £000	2003 £000
Authorised		
53,832,891 ordinary shares of $19\frac{4}{99}$p each (2003: 53,832,891 ordinary shares of $19\frac{4}{99}$p each)	**10,250**	10,250
Allotted, called up and fully paid		
39,278,346 ordinary shares of $19\frac{4}{99}$p each (2003: 38,295,421 ordinary shares of $19\frac{4}{99}$p each)	**7,480**	7,292

New share capital issued during the year was as follows:

	Number of Shares	Nominal Value £000
Exercise of options (see note 22)	**982,925**	**188**

22. Share options

During the year there were the following movements in executive and savings-related options.

	Executive Options	SAYE Options	Total
At 1 January 2004	3,961,354	57,975	4,019,329
Options granted	795,000	–	795,000
Options lapsed	(928,918)	(636)	(929,554)
Options exercised	(972,327)	(10,598)	(982,925)
Options cancelled	–	(19,229)	(19,229)
At 31 December 2004	**2,855,109**	**27,512**	**2,882,621**

The market price of the Company's shares at the end of the financial year was 233.5p and the range of market prices during the year was 144p to 247.5p.

At 31 December 2004 executive and savings-related options were outstanding as follows (listed by period of exercise):

Date Options Granted	Exercise Price Per Share Pence	Exercisable From	Exercisable To	No of Shares
13/04/1995	153	13/04/1998	13/04/2005	44,610
26/06/1998	126	26/06/2001	26/06/2008	347,294
26/06/1998	126	26/06/2003	26/06/2008	316,875
24/07/1998	98	01/09/2005	01/03/2006	22,367
04/11/1998	77	04/11/2001	04/11/2008	17,930
11/08/1999	118	11/08/2002	11/08/2009	108,529
16/08/1999	126	16/08/2002	16/08/2009	81,603
14/06/2000	291	14/06/2003	14/06/2010	105,000
14/06/2000	291	14/06/2005	14/06/2010	75,000
22/09/2000	384	22/09/2003	22/09/2010	190,750
22/09/2000	384	22/09/2005	22/09/2010	28,500
17/11/2000	274	01/01/2006	01/07/2006	2,463
17/11/2000	274	01/01/2008	01/07/2008	2,682
05/01/2001	365	05/01/2004	05/01/2011	20,000
22/08/2001	189	22/08/2004	22/08/2011	31,250
22/08/2001	189	22/08/2006	22/08/2011	31,250
24/09/2001	59	24/09/2004	24/09/2011	162,018
24/04/2002	104	24/04/2005	24/04/2012	1,000
23/04/2003	123	22/04/2006	22/04/2013	35,000
08/07/2003	147	08/07/2006	08/07/2013	497,000
02/12/2003	168	02/12/2006	02/12/2013	13,000
23/04/2004	196	24/04/2007	24/04/2014	712,500
07/10/2004	219	07/10/2007	07/10/2014	36,000
				2,882,621

Since the year end 108,904 options have been exercised by employees at prices of 59p, 104p, 118p, 126p, 126.2p and 153.3p under the normal rules of the share option schemes.

23. Capital and reserves

Group	Called up share capital £000	Share premium account £000	Merger reserve £000	Other reserves £000	Profit and loss account £000	Total equity shareholders' funds £000
At 1 January 2004 (as previously reported)	7,292	60,168	17,748	47,800	(85,319)	47,689
Prior year adjustment						
Deduction of ESOP investment cost from shareholders' funds	–	–	–	–	(618)	(618)
Reversal of permanent diminution of ESOP investment	–	–	–	–	381	381
At 1 January 2004 (as restated)	7,292	60,168	17,748	47,800	(85,556)	47,452
Retained loss for the year	–	–	–	–	(139)	(139)
Exchange differences	–	–	–	–	14	14
New share capital issued	188	1,005	–	–	–	1,193
At 31 December 2004	**7,480**	**61,173**	**17,748**	**47,800**	**(85,681)**	**48,520**

As explained in the accounting policies, the investment cost of £618,000 representing the purchase price of the shares held by the Biocompatibles Trust ("the ESOP Trust") has been deducted from shareholders' funds. A movement of £381,000 has been reported in the Statement of Total Recognised Gains and Losses, which represents the reversal of the permanent diminution of the investment through reserves under UITF 38.

No shares were acquired by the ESOP Trust in the year (2003: nil). At 31 December 2004, the ESOP Trust held 127,753 ordinary $19\frac{4}{99}$p shares (2003: 127,753 ordinary $19\frac{4}{99}$p shares) in the Company with a cost of £618,000 (2003: £618,000). The market value of the shares held at 31 December 2004 was £298,000 (2003: £182,000).

Company	Called up share capital £000	Share premium account £000	Merger reserve £000	Other reserves £000	Profit and loss account £000	Total equity shareholders' funds £000
At 1 January 2004 (as previously reported)	7,292	60,168	8,809	57,114	(60,025)	73,358
Prior year adjustment						
Deduction of ESOP investment cost from shareholders' funds	–	–	–	–	(618)	(618)
Reversal of permanent diminution of ESOP investment	–	–	–	–	381	381
At 1 January 2004 (as restated)	7,292	60,168	8,809	57,114	(60,262)	73,121
Retained profit for the year	–	–	–	–	5,947	5,947
New share capital issued	188	1,005	–	–	–	1,193
At 31 December 2004	**7,480**	**61,173**	**8,809**	**57,114**	**(54,315)**	**80,261**

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

	2004 £000	2003 £000
Operating loss	**(7,625)**	(7,794)
Strategic review costs incurred	**–**	(421)
Depreciation on tangible fixed assets	**279**	296
Amortisation of intangible fixed assets	**754**	754
(Profit)/loss on disposal of tangible fixed assets	**(5)**	57
Increase in stock	**(160)**	(95)
(Increase)/decrease in debtors	**(887)**	724
Decrease in creditors	**(858)**	(3,838)
Net cash outflow from operating activities	**(8,502)**	(10,317)

25. Analysis of net funds

	At 1 January 2004 £000	Cash flow £000	Non-Cash Movement £000	At 31 December 2004 £000
Cash at bank	33,084	(7,611)	–	**25,473**
Bank overdraft	(1)	(1,261)	–	**(1,262)**
	33,083	(8,872)	–	**24,211**
Debt due within 1 year	(383)	383	–	**–**
Finance leases	(8)	7	–	**(1)**
	(391)	390	–	**(1)**
Short term deposits	2,500	3,304	–	**5,804**
Current Asset Investments	19,929	(4,915)	126	**15,140**
	22,429	(1,611)	126	**20,944**
	55,121	(10,093)	126	**45,154**

26. Reconciliation of net cash flow to movement in net funds

	2004 £000	2003 £000
Decrease in cash for the year	**(8,872)**	(1,461)
Cash flow from decrease in liquid resources	**(1,611)**	(22,374)
Cash flow from decrease in debt	**390**	57
Change in net funds resulting from cash flows	**(10,093)**	(23,778)
Non cash movement	**126**	(551)
Movement in net funds in the year	**(9,967)**	(24,329)
Net funds at 1 January 2004	**55,121**	79,450
Net funds at 31 December 2004	**45,154**	55,121

27. Financial commitments

At 31 December 2004 the Group was committed to make the following payments during 2005 in respect of operating leases:

	2004 Land and buildings £000	2003 Land and buildings £000
Expiring in more than five years	**360**	360

At 31 December 2004 the Group had commitments to pay £685,000 to one of its suppliers for the manufacturing of finished goods in 2005 (2003: £281,000).

28. Post balance sheet events

On 7 March 2005, the Company completed the purchase of CellMed AG, for a total maximum consideration of £15.2m. CellMed is a medical technology company developing medical device and drug delivery products and is located and incorporated in Germany. For further details on the CellMed acquisition refer to the Operational and Financial reviews.

Five Year Record

Consolidated profit and loss account	**2004 £000**	2003 £000 As restated	2002 £000	2001 £000	2000 £000
Turnover	**2,599**	2,107	21,987	69,023	55,059
Operating loss (before exceptional charges)	**(6,908)**	(6,831)	(5,694)	(13,381)	(11,559)
Intangibles amortisation	**(754)**	(754)	(956)	(4,214)	(3,748)
Exceptional income (charges)	**4,965**	21,361	48,677	–	(4,288)
Net interest receivable/(payable)	**2,108**	2,246	2,287	(1,727)	(1)
Taxation	**450**	–	(4,129)	(396)	(410)
Retained profit/(loss)	**(139)**	16,022	40,185	(19,718)	(20,006)
(Loss)/earnings per share	**(0.4)p**	42.2p	91.0p	(14.0)p	(14.4)p
Weighted average number of shares in issue after adjusting for rights issue	**38.4m**	37.9m	44.2m	140.8m	139.1m
Consolidated balance sheet					
Fixed assets	**1,513**	2,383	3,498	46,022	51,691
Cash and other net current assets	**56,428**	60,880	81,230	23,727	18,098
Creditors: amounts falling due after one year	**(5,319)**	(6,590)	(10,182)	(28,860)	(10,296)
Provision for liabilities and charges	**(4,102)**	(9,221)	(32,110)	–	–
Net assets	**48,520**	47,452	42,436	40,889	59,493
Capital and reserves					
Called up share capital	**7,480**	7,292	7,215	7,070	7,056
Share premium account	**61,173**	60,168	71,045	170,202	169,525
Merger reserve	**17,748**	17,748	17,748	–	–
Other reserves	**47,800**	47,800	47,800	28,466	29,263
Profit and loss account	**(85,681)**	(85,556)	(101,372)	(164,849)	(146,351)
Equity shareholders' funds	**48,520**	47,452	42,436	40,889	59,493

Advisors

Board Committees

Audit Committee*
Members of the Audit Committee are:
David Hankinson (Chairman),
Jeremy Curnock Cook

Remuneration Committee*
Members of the Remuneration Committee are:
Jeremy Curnock Cook (Chairman),
David Hankinson

Nomination Committee*
Members of the Nomination Committee are:
Sir Richard Needham (Chairman),
Jeremy Curnock Cook, David Hankinson

*Terms of reference for the Board
Committees are available on the Company's Website:
www.biocompatibles.com

Company Secretary
Ian Ardill

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Investment information

Trading Symbol: LSE:BII
Shares Outstanding: 39.9m
Employees as at 25 April 2005:
UK: 78 (52 in R&D)
Germany: 18 (16 in R&D)

2005 calendar
Preliminary Results: 17th March
Annual General Meeting: 23rd June
Interim Results: September

Corporate website
Information about the Company is available at
www.biocompatibles.com

Major holders
25 April 2005
Aberforth Smaller Companies Trust plc
Contra Fund Limited
Hunter Hall Investment Management Limited
Invesco English & International Trust plc
Legal & General Investment Management

Analyst coverage
Code Securities Limited
Evolution Beeson Gregory
Nomura International
Numis Securities Limited

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